Islamic Banking: A Panacea for Financial Inclusion in Northern Nigeria

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Abstract

The issue of financial exclusion which renders lot of the underprivileged and sometimes religious minded populace to be financially excluded, especially by the convention financial institutions, has been a stumbling block to development and realization of the contribution these groups of people are capable of providing to the economic growth and development of developing countries like Nigeria. This is because most formal financial mediators considered low-income households as too poor and incapable of satisfying the criteria laid by the commercial banks in terms of financial dealings. These reasons, consequently exposes these groups' limitation to financial inclusion. On the other hand, quiet a number of them shun relationship with the commercial banks for its inability to provide to them the required needs based on religious consideration and sometimes lack of easy accessibility, distances these group from being financially inclusive. Using a questionnaire survey and descriptive analysis with the help of SPSS the research was able to identify the major causes of financial exclusion and highlighted how Islamic banking could be a better alternative to those desiring to get not only access to finance but also a suitable and Shari'ah compliant one as well as providing a favorable ground thereby enhancing the financial inclusion among these vulnerable groups.

KEYWORDS: Islamic banking, Alternative, Financial inclusion, Northern Nigeria.

1. Introduction

Searching for the way to reduce the menace of poverty and ease the burden afflicting the vulnerable populace is increasingly becoming an area of interest and concern in the past and present decades. This make financial inclusion a fertile ground that ease the tension poise by lack of easily reach access to finance. Financial inclusion may be defined as the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost (Ene & Inemesit, 2015). No one is expected to have any concern on financial inclusion in the absence of financial exclusion. Financial exclusion relates to the condition where a considerable number of those in need of financial service failed to get the required financial services (Devlin, 2005).

Significant number of populace is financially excluded for variety reasons despite the fact that several efforts were made to ensure Nigerians embrace full utilization of the banking system. Yet, there was still resistance by many among the populace to patronize banks in the country (Balogun, 2011). This was evident in the reluctance of the predominantly Muslims in the northern part of Nigeria to participate in banking activities even with the conventional micro finance (Dogarawa, 2011). Therefore, it was observed that the essential capabilities of large number of the populace in northern Nigeria were yet to be tapped either due to insufficient access to finance or resistance from them for various reasons (Adewale & Daud, 2010). Islamic banking stands a chance to provide alternative to the unbanked, thereby accommodating an average man to participate in varieties of venture since the system provides alternative finance compatible to the lot of financially excluded populace and in turn would lead to wealth creation which would impact positively on the economy. Undoubtedly Islamic finance in general is capable of aiding financial inclusion which will promote inclusive growth and development in the economy by tackling the issues of poverty through its all-inclusive offer.

1.1 Objectives of the Study

The main objective of this study is to determine the major causes of financial exclusion and identify ways in which Islamic banking could help in enhancing financial inclusion. Hence, it set to:

1. Identify the major causes of financial exclusion
2. To Determined how Islamic banking could effectively provide financial needs of the poor and less- privileged
3. To identify how Islamic banking could enhance financial inclusion

1.2 Research Question

1. What are the major causes of financial exclusion?
2. How can Islamic banking effectively provide financial needs of the poor and less-privileged?
3. How can Islamic banking enhance financial inclusion?

2. Literature Review

This section of the study provides the literature related to the causes and barriers to financial inclusion. It further provide an insight on how Islamic banking can effectively provide financing need of the poor and those excluded for some other reasons in life. This was shown in the array of various products and services provided to cater for these group of people. The chapter also identify ways in which Islamic banking can enhances financial inclusion which include Qard-alhassan and participatory financing. All these was conducted hand in hand with review of related studies.

2.1 Causes and Barriers to Financial Inclusion

To identify the major causes of financial exclusion, literature were consulted and the following reasons were identify as the causes of financial exclusion in accordance with assertion by various researchers Ene & Inemesit. (2015), Abdulmumin, et al. (2019), Akilu, Sani & Tijjani (2019).

i. Low and irregular income
ii. religious value
iii. simple preference
iv. poverty
v. informality
vi. financial illiteracy
vii. high cost
viii. poor service
ix. lack of trust

2.2 Islamic Banking Products and Services

To Determined how Islamic banking could effectively provide financial needs of the poor and less- privileged. This could be through the provision of alternative and shariah compliant products.

i- Provision of Alternative and Shariah Compliant Products

The principles of Islamic finance which accommodates banking and finance are summarized as: i- prohibition of riba which is regarded as interest or usury in all form. Islamic banks neither pay nor received interest; ii- Avoidance of Gharah (excessive uncertainty) and encouragement of transparency and disclosure; iii- Prohibition and non-financing of gambling, game of chance and other socially undesirable and or sinful act like dealing with alcohol, Pork, pornography and the like; iv- Provision of alternative financing principle with emphasis on risk-sharing and benefiting from the favorable return of the business and trading in form of profit sharing; v- Avoidance of exploitation and maintenance of justice to all parties involved in the transactions and vi- Emphasis on the real economic activities where finances are directed to economically and socially productive ventures (Ayub, 2007; Gait & Worthington, 2008; Iqbal & Molyneux, 2005; ISRA, 2012; Obaidullah, 2005)

These principles depicted the compliance of the Islamic banking products to shariah provision which is compatible to many people that are financially excluded due to incompatibility issues related to faith and justice. Some of these products that could be grouped in to equity-based and debt based are explain below.

1. Equity-Based Products

Equity based products of Islamic bank are mostly in form of *Musharakah* and *Mudarabah*. These two products or Instrument are considered as the twin pillar of Islamic finance (Lewis, 2001). They formed the popularly known profit and loss sharing and or loss bearing products or instrument. They are the most preferred modes of financings to Islamic financial investors (Chowdhury, 2013; Gambo, 2013) and considered as the purest mode of finance (Chowdhury, 2013)

a) Musharakah (Equity/Partnership Financing)

Musharakah is a product of Islamic banking which is based on profit and loss sharing. It is formed between the participants where all the parties provide capital towards financing of the investment. All the parties are entitle to participate in managing the investment if they so wish, but not all of the capital providers are normally engaged with or required to do so (Chowdhury, 2013). This is done in pursuant of a legitimate profit in a halal (*shariah* permissible) business venture. The profit proceeds of the investment are shared among the parties in a mutually agreed ratio while the losses are apportioned to the parties strictly in accordance with their capital contributions (Obaidullah, 2005).

In Islamic banking context, the bank and the customer or client enter in to agreement and contribute to the capital and entrepreneurship. The combined resources are then invested and managed according to the term and condition of the agreement. Distribution of profit would be in consonance with the free-agreed ratio and the loss if any is shared in proportion to the capital contributed by each party (Obaidullah, 2005).

b) Mudarabah (Trust financing)

Mudarabah is a form of partnership which involves two parties with one of them providing capital requirement for funding or financing the project/investment called Rabb-al-maal (capital provider) and the other party called Mudarib (the enterpriser) who manages the investment using his expertise to nurture the business, he has the required skill but lack capital. Profits resulting from the investment are shared among the parties in a pre-determined agreed upon ratio and not a fixed return on the capital. In case of loss, the capital provider absorbed the entire loss on the capital and the enterpriser loses his effort and time value contributed in running the business. This is when there is no willful act from the side of the mudarib, however if there established fact of any negligence or willful act from the mudarib leading to the loss, he then becomes liable for the capital provider's claim (Ayub, 2007; Chowdhury, 2013; Gafoor, 2001; Obaidullah, 2005)

Islamic banks normally mobilize deposit through *Mudarabah* arrangement and then invest the money in to business (Ayub, 2007). According to Hussin and Hussin (2011), Islamic bank applied *Mudarabah* principle in the various type of account they operate which includes: Saving account-i, current account-i, general investment account-i and specific investment account-i. Islamic bank can play the role of a *rabb-al-mal* by providing capital to its customer who acts as the *mudarib*. On the other way Islamic bank served as the *mudarib* where it mobilize deposit from customer and engage it in investment opportunities. In either case, profit is shared according to the ratio mutually agreed between the parties.

2. Debt-based Products

a) Ijarah (Leasing)

One of the major products of Islamic banks is *Irajah* (Amin et al., 2013; Ayub, 2007). According to Al-Salem (2009) *Ijarah* is similar to conventional lease, it is a contract under which the financial institution buys and lease out an assets or equipment required by its client for a rental fee. It is a contract of sale which gives right to a party other than the actual owner to enjoy the usufruct of a property base on a rent payment (Haron & Azmi, 2009). *Ijarah* also connotes hiring of a physical asset in which Islamic bank served as the lessor by allowing the use of a particular assets it possess by its client- the lessee against payment of a pre-determined rentals within a specific time called *Ijarah* period (Obaidullah, 2005). The customer normally gives specification of the asset he requires for lease and, the bank accordingly provides the said asset on rental to the customer.

b) Bai Bithaman Ajil (BBA)

Bai Bithaman Ajil (BBA) simply refers to deferred payment sale. It is a sale contract in which the buyer pays the price at a later time period in installment or in lump sum. This practice is widely used in Malaysia (Haron & Azmi, 2009; Shanmugam & Zahri, 2009; Dusuki, 2012) and Brunei (Dusuki, 2012). Though the selling price is paid at a later period, it has to be known and fixed and agreed at the time of the contract.

BBA entails sale of particular goods to a client on deferred payment basis. Both the bank and the customer agreed on a specific time period of repayment at a price that includes a profit margin. Islamic banks used this type of product mostly in financing the purchase of tangible assets and particularly housing financing and vehicle.

c) Murabahah

Murabahah is a financing product which is often refers to as "cost plus financing" or "profit Margin". Essentially, *Murabahah* is the sale of asset at a price which covers the purchase price plus a mark up or profit margin agreed to by the parties concerned. (Haron & Azmi, 2009). In *Murabahah* financing a customer approaches a bank and requested it to purchase a particular asset which he promises to buy from the bank at a mark up or profit margin. The actual price of the asset must be disclosed to the customer. The bank then sells the asset to the customer at a cost price plus the profit margin and the customer pays in installment or lump sum. The *shariah* required that the bank must be in possession of the asset physically or constructively at the time of sale, the price must be disclose and the asset must be *shariah* compliant (Ayub, 2007; Shanmugam & Zahari, 2009).

d) Wadiah

Islamic banks used the principle of *wadiah* which is refers to the deposit accepted by the bank for safe-custody. Islamic bank as a trustee is obliged to keep the amount safely and repay back to the depositor when requested. The deposited amount under this type of agreement are basically similar to savings and current accounts in conventional banking with a major difference mainly in savings account where no interest is either paid or charged. Islamic banks use the concept of *wadiah* as *amanah* to accept deposits from customers. In some jurisdictions, the principle of *qard* is applied in the treatment of *wadiah* deposit and this gives the bank right to use the deposit for its business and guarantee the repayment of same to the depositor on demand.

e) Salam

Among the Islamic banking products is Salam financing. The term Salam refers to an advance payment against future delivery. It is mostly used in agricultural contexts, providing farmers an avenue to finance production in exchange for a future delivery of the crop. The amount and quality of the future goods and the actual delivery date is normally specified in the transaction.

2.3 Islamic Banking and Enhancement of Financial Inclusion

Islamic banking could enhance financial inclusion through the following efforts:

a) Awareness

According to (Rogers, 2003) in his book Diffusion of Innovation adoption is the acceptance or continued use of the product, services or idea. Customers' go through a process called knowledge, persuasion, decision and confirmation before they are ready to adopt a product or service. Therefore knowledge appears when an individual or decision making unit is exposed to an innovations existence and have access understanding of how it functions (Rogers, 2003). He quoted this as the pre- contemplation stage. Customers' awareness has been tested as one of the key variable that led to subscription of a particular product or service.

b) Provision of community banking and micro finance program

The emergence of micro finance is a step forward to economic development through the provision of financial needs of those who in the society are considered as less privileged or deprived group. This entails the provision of financial service to low-income clients including self -employed, low-income entrepreneurs in both urban and rural areas (ledgerwood, 1999)

This could be achieved through group based financial service, where the group members served as guarantors for one another.

It was reported that Islamic micro financial product providers of over 255 around the world are mostly located in east Asia and Pacific, Middle East and Noth Africa providing 164 providers (64 percent) and 72 providers representing 28 percent respectively Mayada, E-Z & Michael,T (2013). They successfully provided the needful finance to the religious observant around the communities they operate.

2.4 Some Studies Related to Financial Inclusion

Literature documents that formal financial service penetration rates are higher in the relatively more affluent countries with the exception of Nigeria who has a tiny penetration rate of financial services of 18.75 percent (Gabriel, 2013) despite being the largest economy of the African continent (theguardian.com, 2014). This figure is considered low compared to other African countries such as South Africa, 53.9 percent; Namibia, 47.4 percent and Botswana, 43.4 percent (King, 2012)

Numerous sort of literature relates the subject of financial inclusion to Islamic finance and banking. Among such literature of the modern scholars that display connection of financial inclusion with the subject of Islamic finance include the studies of Ali (2015); Demirguc-Kunt et al. (2014); Demirgüç-Kunt, Klapper, and Randall (2013); El-Zoghbi and Tarazi (2013); Iqbal and Mirakhor (2013); Ben Naceur et al. (2015) and Warsame (2009). .

It was argued that on the average, the accessibility to financial service is less on the population of Muslims countries as compared to the rest of the world. Equally the usage of such financial services is minimal in the former as against the later. Related to this and in order to curtail the menace of low penetrations in financial services and financial exclusion, Dogarawa (2011) has earlier echoed the capability of Islamic banking in enhancing financial inclusion of the financially excluded citizen as one of the advantages of Islamic banking in the country- Nigeria. Furthermore Mayada, & Michael, (2013) posit that accessibility of finance to millions of Muslims poor whose detested finances from non-shariah compliant institutions could be attained through sustainable Islamic banks model of finance.

Recently, Akilu , Yahaya and Tijjani (2019) conducted a research on financial inclusion, the paper provided a theoretical road-map through which financial inclusion could be achieved. In the study, the researchers were able to identify some important drivers necessary for the achievement of financial inclusion among less privileged group that includes low income earners, women and rural poor. Among those factors were extensive public awareness of the product available under Islamic financial services, micro credit and micro finance and a sound legal regulatory crietaria.

Even though the study was theoretical in nature, it has provided a remarkable insight on how financial inclusion could be achieved.

In another study, financial inclusion was describe as important element in redistribution of economic resource within the varied stratas of a given society which in turn aids economic growth and development. Abdulmumin, B. A., et al. (2019). The study opined that there is high propensity to gain a high level of financial inclusion with the establishment of more financial institution. This is workable in the northern region of nigeria especially with the Islamic banking alternative that was introduced in the last decade.

Ealier on, Abiola, A. B., et al. (2014) investigates the impact of financial inclusion on economic growth in Nigeria. The paper highlight the determinants of financial inclusion and its impact of economic growth. But in most of these studies secondary data were used in the analysis which make it different from the current study that seek to use the primary data to the analysis of the Islamic banking capability in enhancing financial inclusion in the northern part of Nigeria.

3. Methodology

This study is a mixture of qualitative and quantitative designed to investigate the major hindrance of financial inclusion and propose the way forward toward enhancing the financial inclusion of the financially excluded populace in the north. Therefore the study employed the use of questionnaire at the second stage after engaging some part of the targeted respondents in an interview at the first stage of the study. Content analysis was be used in analyzing the qualitative aspect while the use of both descriptive and inferential statistics with the help of SPSS.

The research cover five states, selected randomly as representation from the North Western zone of the country-Nigeria. The states are: Kaduna, Kano, Katsina, Sokoto and Zamfara.

3.1 Sampling procedure

According to Hair et al, (2007) a minimum sample size is 30 but they recommended using the sample larger than 30 as more appropriate. This tallied with the proposed rule of thumb by Roscoe (1975) and (Sekaran, 2000) of determining sample size in which they indicated the appropriateness of a sample of larger than 30 and less than 500 for most researches. Base on the rule of thumb above, this study sampled 450 respondents.

3.2 Sampling technic

In determining the number of respondents from each state and to ensure adequate representation of the subject from the five states, stratify sampling was applied in this study. Base on density of the states the percentage was assigned to each state for good representation as shown below.

Table 3.1 Sample Percentage based on State

SN	State	Percentage	Sample
1	Kaduna	20%	90
2	Kano	30%	134
3	Katsina	20%	90
4	Sokoto	15%	68
5	Zamfara	15%	68
Total		100%	450

4. Data Analysis

The core elements of this section is the presentation of the result of the study which led to the testing of the hypothesis where, Prior to presentation of the main results and the core findings of the study, data screening and preliminary analysis was conducted using Statistical Packages for Social Sciences (SPSS) software version 20.

4. 1 Response Rate

This study employed the used of questionnaire, where a total of four hundred and fifty (450) were administered. Two hundred and eighty two (282) questionnaires were returned, out of which two hundred and sixty three (263) were found duly completed and useable for the analysis. The remaining nineteen (19) copies of the returned questionnaire were not duly completed and were therefore exempted from the analysis.

The duly completed questionnaire ready for analysis accounted for 58% of the total number of administered questionnaires. While some studies reported 100% response rate, many others reported varied percentage level of response rate (Linder & Wingenbach, 2002). The response rate achieved in this study was considered sufficient in accordance with the suggestion by Sekaran (2003), who maintained that response rate of 30 percent is adequate for surveys.

Table 4.1 Correlation Analysis

Correlations				
		Perception	Enhancement	Barriers
Perception	Pearson Correlation	1	.507**	.366**
	Sig. (2-tailed)		.000	.000
	N	263	263	256
Enhancement	Pearson Correlation	.507**	1	.578**
	Sig. (2-tailed)	.000		.000
	N	263	263	256
Barriers	Pearson Correlation	.366**	.578**	1
	Sig. (2-tailed)	.000	.000	
	N	256	256	256

**. Correlation is significant at the 0.01 level (2-tailed).

Base on the above result, the variables under study were found to be correlated with one another as indicated in the result therein.

4.2 Descriptive analysis

The table 4.2 below present the result on the perception/preferences of the respondent base on five-point likert scale measurement from 1=strongly disagree, 2=disagree, 3=either agree nor disagree, 4=agree, and 5=strongly agree

Table 4.2: Perception/Preference on the Potentials Islamic Banks in Increasing Financial Inclusion

S/N	Statement/Items	N	Min.	Max.	Mean	Std. Deviatn
1	The presence of Islamic banking activities enhance financial inclusion	251	1	5	4.36	1.092
2	I am willing to operate account with Islamic Bank	251	1	5	3.81	1.228
3	I prefer Islamic banking to conventional banking	251	1	5	3.76	1.306
4	I will be contented by operating with Islamic banks	251	1	5	4.05	.926
5	I prefer shari'ah compliant banking	251	1	5	3.54	1.318

Table 4.2 above displayed the view of the respondents regarding their perceptions on the potentials of Islamic banking in increasing financial inclusion. There are five items in this section. 1. The presence of Islamic banking activities enhances financial inclusion, this item has mean and standard deviation (M = 4.36 and SD = 1.09) which indicate that the respondents are

in strong agreement with the statement. Others - I am willing to operate account with Islamic banks (M = 3.81 and SD = 1.22), I prefer Islamic banking to conventional banking (M = 3.76 and SD = 1.30), I will be contented by operating with Islamic banks (M = 4.05 and SD = 0.92) and I prefer shari'ah compliant banking (M = 3.54 and SD = 1.31) indicates the respondents have strong preference on Islamic banking and have a good perception on its ability to aid financial inclusion.

Table 4.3 Financial Inclusion could be Enhance by Islamic Banks

S/N	Statement/Items	N	Min.	Max.	Mean	Std. Deviation
1	Islamic banking can enhance financial inclusion through community banking	251	1	5	3.49	1.211
2	Islamic banks can enhance financial inclusion through micro finance	251	1	5	3.67	1.105
3	Salam financing (finance on agriculture) will help increase financial inclusion	251	1	5	4.16	.930
4	Minimal cost of financing by the Islamic banks enhance financial inclusion	251	2	5	3.83	.892
5	Extension of Islamic banking to rural areas could help enhance financial inclusion	251	1	5	4.09	1.002
6	Affordable and favorable repayment period	251	2	6	3.83	.983

The above table exhibit the response of the participant on how they believe Islamic banking could enhance financial inclusion. According to the respondents, Islamic banking can enhance inclusion through community banking (M = and SD 1.21), Micro finance (M = 3.67 and SD = 1.10), Salam financing (M = 4.16 and SD = 0.93), Minimal cost of financing (M = 3.83 and SD = 0.89) and extension of Islamic banking to rural areas (M = 4.09 and SD = 1.00). The respondents are also with the view that affordable and favorable repayment period (M = 3. 83 and 0.98) are all part of the ways in which financial inclusion could be achieved.

Table 4.4: Barriers to Financial Inclusion

S/N	Statement/Items	N	Min.	Max.	Mean	Std. Deviation
1	High cost of finance is a barrier to financial inclusion	251	1	5	3.58	1.199
2	Lack of trust hinders financial inclusion	251	1	5	4.30	.960
3	Low and irregular income is a barrier to financial inclusion	251	2	5	4.07	.876

4	Proximity (distance) of the financial institution cause hinders financial inclusion	251	1	5	3.64	1.043
5	Illiteracy and lack of awareness hinders financial inclusion	245	1	5	4.07	1.241

This table shows the respondents' views on what constitute the barriers to financial inclusion. High cost of finance is a barrier to financial inclusion (M 3.58 and SD = 1.19), Lack of trust hinders financial inclusion (M = 4.30 and SD = 0.96), Low and irregular income is a barrier to financial inclusion (M = 4. 07 and SD = 0.87), Proximity (distance) of the financial institution cause hinders financial inclusion (M = 3.64 and SD = 1.04) and Illiteracy and lack of awareness hinders financial inclusion (M = 4.07 and SD = 1.24) indicate that the respondents concord on the capacity of the above statement (items) in distancing people from being inclusive in the financial activities and provisions.

4.4 Regression Result

The multiple regression analysis was to determine the influence of perception and barriers on the enhancement of financial inclusion by the Islamic banking. The result is shown below.

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.675[a]	.455	.451	2.808

a. Predictors: (Constant), Barriers, Perception

According to the result above, the combine effect of the independent variables on the explained variable is indicated by the value of R^2 which was 0.455. This mean that the model is capable of explaining 45 percent variance of the dependent variable by the independents variables collectively.

ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	1668.493	2	834.246	105.783	.000[b]
	Residual	1995.257	253	7.886		
	Total	3663.750	255			

a. Dependent Variable: Enhancement

b. Predictors: (Constant), Barriers, Perception

The result in the table above indicate that the model is statistically significance with the sig. value of .000.

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
	(Constant)	8.161	1.058		7.713	.000
1	Perception	.299	.040	.375	7.516	.000
	Barriers	.467	.053	.441	8.840	.000

a. Dependent Variable: Enhancement

The coefficients indicates the individual contribution of independent variables on the explained variable. This is clearly explained by the beta results indicating the significance influence of the respective variables. Perception to toward Islamic banking appeared to have a significant influence on enhancing financial inclusion with beta score of .375 and P-value of .000 indicating significance level at 95 percent confidence. Barriers to inclusion on the other hand appeared to be negatively related to the financial inclusion with a significant beta result of .441 and a P-value of .000.

4. Conclusion

In conclusion, it's important to highlight that this survey was able to identify the causes of the financial exclusion as well as hindrance or barriers to financial inclusion. These were observed in the literature and also confirm via interview with some selected persons from the respondents in the survey. On the barrier to financial inclusion in particular, the descriptive statistics was able to point out the extent to which high cost of finance, lack of trust, irregular income, proximity and also lack of awareness and illiteracy have collectively served as a great challenge that set a barrier to financial inclusion. This was identify through the analysis of the agreement or otherwise of the respondents.

The result presented under descriptive analysis also buttress the power of Islamic banking products of enhancing financial inclusion. It was find out that the majority of the respondent were optimistic of the capability of the Islamic banking products and activities in improving the financial inclusion of the high number of the populace that are financially excluded due to one reason or the other as indicates both in the literature and in the findings from the descriptive analysis.

Based on the findings above, it is apparent that Islamic banking is capable of providing alternative finance that could accommodate lots of unbanked populace in Nigeria at large and in the Northern part in particular. Therefore effort should be made by the Islamic bank providers to improve on the awareness of their products and accessibility.

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