



USAGE OF *AR-RAHNU* TOWARDS ACHIEVING
FINANCIAL SELF-SUFFICIENCY FOR WOMEN
MICRO-ENTREPRENEURS IN MALAYSIA

BY

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ABSTRACT

Issues of financial shortage among micro-enterprises have always being given attention by Malaysian government. Although there are incentives and grants offered by Malaysian government, these incentives and grants are still very limited. Micro-enterprises need to explore other potential financing channels in order to access for capital. One of the financing channels is by approaching *Ar-Rahnu*. *Ar-Rahnu* industry has shown growing acceptance and become a viable and competitive mode of financial instrument in the Islamic finance industry. *Ar-Rahnu* is one of the alternatives used especially by women micro-entrepreneurs. In order to cater these issues, this study aims to investigate the usage factors namely *shari'ah* compliancy, customer satisfaction, service charges, locality and collateral for *Ar-Rahnu* among women micro-entrepreneurs in Malaysia. Subsequently, it attempts to determine the role of *Ar-Rahnu* in contributing to financial self-sufficiency for the women micro-entrepreneurs. Besides, demographic factors are added as a moderator to better reflect the impact of the usage toward financial self-sufficiency. The samples of this study are 600 women micro-entrepreneurs from three states, namely, Kedah, Kelantan, and Terengganu. The structural equations modeling (SEM), in particular the analysis of moment structure (Amos) was used to investigate the relationship among the variables. The results revealed that the usage factors have positive and significant relationship towards the *Ar-Rahnu* usage. The results also provide strong evidence of the relationship between the *Ar-Rahnu* usage and financial self-sufficiency. Since the findings of the previous studies have been inconclusive, therefore to better understand the relationship between *Ar-Rahnu* usage and financial self-sufficiency, moderating variables were introduced. Demographic factors such as education level, age, marital status and location were used as moderating variables in between the relationship of *Ar-Rahnu* usage and financial self-sufficiency. The results showed the demographic factors have moderating effects in between *Ar-Rahnu* usage and financial self-sufficiency. This thesis contributes to the theoretical, practical and policies by providing evidence about the relationship between *Ar-Rahnu* usage and financial self-sufficiency and further, added moderating variables to fully understand this relationship. In general, the findings have provided empirical support that *Ar-Rahnu* is gaining acceptance among the community, particularly among women micro-entrepreneurs. *Ar-Rahnu* assists women micro-entrepreneurs to diversify and enhance their businesses. Therefore, it is important to ensure the growth of the *Ar-Rahnu* in order to cater the need for women micro-entrepreneurs. This can be ensure by offering the *shari'ah* compliancy product, the lowest service charges, near to potential customers, lenient on collateral and treat customer fairly regardless their races or religious.

ملخص

تبدي الحكومة اهتماما دائما للقضايا المتعلقة بالنقص المالي فيما بين المشاريع التعاونية الصغرى. وعلى الرغم من وجود حوافز ومنح تقدمها حكومة ماليزيا، إلا أن هذه الحوافز والمنح تقتصر على عدد محدود فقط. وتحتاج المؤسسات الصغرى إلى استكشاف قناة محتملة أخرى للتمويل من أجل الحصول على رأس المال. إحدى قنوات التمويل المتوفرة تكون عن طريق توظيف الرهن. وقد أظهر نظام الرهن قبولا متزايدا وأصبح وسيلة قابلة للحياة وهو من الأدوات المالية المتنافسة في قطاع التمويل الإسلامي. يشكل الرهن واحدا من البدائل المستخدمة خاصة من قبل النساء صاحبات المشاريع الصغيرة. ومن أجل تلبية هذه القضايا، تهدف هذه الدراسة إلى التعرف على عوامل الاستخدام، وهي الالتزام بالمادئ الشرعية، وإرضاء الزبائن، ورسوم الخدمات، والمحلية، والضمانات للرهن بين النساء، صاحبات المشاريع الصغيرة في ماليزيا. وفي الوقت نفسه، فإنها تحاول تحديد دور الرهن في الإسهام في الاكتفاء الذاتي المالي بالنسبة لصاحبات المشاريع الصغرى. وبالإضافة إلى ذلك، تضاف العوامل الديموغرافية كمحرر لتعكس بشكل أفضل أثر الاستخدام نحو الاكتفاء الذاتي المالي. تتكون عينات هذه الدراسة من 600 صاحبة الأعمال الصغيرة من ثلاث ولايات، هي قدح، وكلنتان، وترنجانو. وتم استخدام معادلات المعادلات الهيكلية (س.ي.م)، وعلى وجه الخصوص تحليل بنية اللحظة (أموس) لدراسة العلاقة بين المتغيرات. وأظهرت النتائج أن معاملات الاستخدام لها علاقة إيجابية وهامة نحو استخدام الرهن. كما توفر النتائج دليلا قويا على العلاقة بين استخدام الرهن والاكتفاء الذاتي المالي. وبما أن النتائج التي توصلت إليها الدراسات السابقة لم تكن حاسمة، فقد استحدثت متغيرات معتدلة من أجل فهم علاقة أفضل بين استخدام الرهن والاكتفاء الذاتي المالي. واستخدمت العوامل الديموغرافية مثل مستوى التعليم والعمر والحالة الاجتماعية والموقع كمتغيرات متداخلة بين علاقة استخدام الرهن والاكتفاء الذاتي المالي. وأظهرت النتائج أن للعوامل الديموغرافية أثارا معتدلة بين استخدام الرهن والاكتفاء الذاتي المالي. وتساهم هذه الأطروحة في النظرية والعملية والسياسات من خلال تقديم أدلة حول العلاقة بين استخدام الرهن والاكتفاء الذاتي المالي، وإضافة متغيرات متداخلة لفهم هذه العلاقة تماما. وبصفة عامة، فقد وفرت النتائج دعما تجريبيا من أن الرهن تكتسب قبولا لدى المجتمع المحلي، ولا سيما بين النساء صاحبات المشاريع الصغيرة. وتساعد "الرهن" النساء من أصحاب المشاريع الصغيرة على تنويع أعمالهن التجارية وتعزيزها. ولذلك، من المهم ضمان نمو منطقة الرهن من أجل تلبية احتياجات النساء من أصحاب المشاريع الصغيرة. ويمكن ضمان ذلك من خلال تقديم منتجات متوافقة مع أحكام الشريعة الإسلامية، وتخفيض رسوم الخدمة، واقترايين الزبائن المحتملين، وتسهيل الضمانات، ومعاملة الزبائن بصورة عادلة بغض النظر عن أجناسهم أو دينهم.

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DECLARATION

I hereby declare that this thesis is the result of my own investigations, except where otherwise stated. I also declare that it has not been previously or concurrently submitted as a whole for any other degrees at IIUM or other institutions.

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LIST OF ABBREVIATIONS

AIM	Amanah Ikhtiar Malaysia
AMOS	Analysis of Moment Structures
ARSAM	<i>Ar-Rahnu</i> Shop Acceptance Model
BIs	Banking Institutions
BIMB	Bank Islam Malaysia Berhad
BSN	Bank Simpanan Nasional
CFA	Confirmatory Factor Analysis
CFI	Comparative Fit Index
CMIN	Chi-Square Minimum Discrepancy
CR	Critical Ratio
DFIs	Development Financial Institutions
EFA	Exploratory Factor Analysis
FA	Factor Analysis
FIs	Financial Institutions
MAIDAM	Terengganu Islamic Religious and Malay Customs Council
MARA	Majlis Amanah Rakyat
MATRADE	Malaysia External Trade Development Corporation
MEs	Micro-enterprises
MFI	Microfinance Institutions
MGIT	Muassasah Gadaian Islam Terengganu
NFI	Normed Fix Index
PB	Public Bank
PKB	Pemodalan Kelantan Berhad
RMSEA	Root Mean Square Error of Approximation
SMEs	Small and Medium Enterprises
TEKUN	Tabung Ekonomi Kumpulan Usaha Niaga
UNDP	United Nations Development Programme
YAPEIM	Yayasan Pembangunan Ekonomi Islam Malaysia
WEDP	Women Exporters Development Programme

CHAPTER ONE

INTRODUCTION

1.0 OVERVIEW

In Malaysia, the definition of micro-enterprises (MEs) is based on two criteria, namely full-time employees and annual sales turnover (the National SME Development Council, 2017). MEs in Malaysia are defined as the establishment with less than five employees or less than RM 300,000 of the sales turnover for manufacturing sectors and RM300, 000 for other sectors namely agriculture, mining, quarrying, construction and services. However, if one of the criteria of MEs either number of employee or annual sales turnover is exceeded the requirement, then the lowest will be given priority.

Micro-entrepreneurs play a vital role in the Malaysian economy and could be considered as the backbone of the industrial development in Malaysia (Khalique, 2011). As documented by Fuad and Bohari (2011) and Darmansyah (2013), the contribution of micro-enterprises (MEs) is important to spur and sustain Malaysia's economic growth. MEs are now providing around 65 percent of total employment and it is expected that the value-added production of MEs to be around RM 120 billion or 50 percent of total production by 2020 (SME Corporation Malaysia, 2016).

The latest statistics from the Economic Census (2011) by the Department of Statistics Malaysia indicated that out of the 645,136 Small and Medium Enterprises (SMEs) establishments in Malaysia, 496,458 or 74.9 percent were contributed by the MEs. As shown in Table 1.1, MEs have a huge potential to be developed, as the number of establishments is larger compared to SMEs. The Table 1.1 also shows that

the number of entrepreneurs in micro-scale business increased to 496,458 in 2011 from 434,939 in 2005, recording an increase of 6.6 percent over the six-year period.

Table 1.1 Census of Establishments and Enterprises 2005 and 2011
Source: (Department of Statistics Malaysia, 2016)

Type/ Census	Census of Establishments and Enterprises 2005	Census of Establishments and Enterprises 2011	Growth (%)
Micro	434,939	496,458	6.60
Small	100,608	128,787	12.28
Medium	12,720	19,891	21.99
Total	548,267	645,136	8.12

Despite their increasing numbers, MEs have always faced the issue of obtaining funding. Without stable funding sources in place, most of the MEs will not likely to survive and possibly not be able to expand their businesses (Anane et al., 2013). This might be due to a variety of factors such as the non-existence of a business track record, weak credit rating, lack of collateral as well as documentation required by most banking and financial institutions (Department of Statistics Malaysia, 2016).

Thus, in order to provide greater accessibility to funding for the MEs, the Malaysian government offers various funding schemes or facilities through the Financial Institutions (FIs). In general, the FIs are comprised of Banking Institutions (BIs) and Development Financial Institutions (DFIs). Banking institutions (BIs) assisting MEs through offering few programs such as AmMikro plus implemented by Ambank (M) Berhad, Maybank Micro executed by Malayan Banking Berhad, Skim Micro operated under Bank Muamalat Berhad and PB Micro performed by Public Bank Berhad.

Apart from the financial facilities offered by the BIs, the access of financing is also channelled particularly through the DFIs. DFIs are established by the government that act as specialised financial institutions focusing on developing and promoting the key sectors that are considered as important to the overall socio-economic development of the country. Among the DFIs accessed by micro-entrepreneurs are Bank Simpanan Nasional (BSN) executed the BSN TemaNiaga, BSN TemanMesra, BSN TemaNiaga-i, Agrobank providing the Modal Usahawan 1 Malaysia-i, Bank Rakyat carries out the Skim Pembiayaan Mikro and SME Bank offers the for Enrichment and Enhancement Programme (E²).

Besides the access of financing channelled by the FIs, there are also agencies providing micro-financing such as Tabung Ekonomi Kumpulan Usaha Niaga (TEKUN) Nasional and Amanah ikhtiar Malaysia (AIM). TEKUN provides fund (known as Tekun Financing) and a wide range of business support to micro-entrepreneurs in Malaysia, while AIM assists micro-entrepreneurs through its financial programs such as i-Mesra, i-Srikandi and i-Wibawa. All in all, these financing facilities allow MEs to upgrade and enhance their capability, thus enabling them to improve their products and management system. The summary of financing facilities available for the micro-entrepreneurs is illustrated in Table 1.2.

Despite the various sources of financing for the MEs, most of the MEs still depend mainly on internally generated funds. Micro-entrepreneurs depend less on the grants or financing from government agencies, co-operatives and leasing companies as reflected by the fact that only 28.8 percent of MEs' funding sources come from these agencies (Department of Statistics, 2016). As shown by Table 1.3, the highest source of financing used by the MEs is from internally generated fund (58.1 percent). Apart from that, 16.2 percent financing access from micro-credits, banks and financial

institutions and 15 percent from friends and relatives. Based on the data presented, there is a need to identify what are the reasons financial institutions particularly the government agencies and banking institutions could not provide more financial assistance for the MEs.

Table 1.2 Sources of Financing for Micro-Entrepreneurs
Source: (SME Annual Report, 2014/2015, SME Corporation Malaysia, 2016)

Banking Institutions (BIs)	Development Financial Institutions (DFIs)	Microfinancing
Ambank (M) Berhad (AmMikro Plus)	Bank Simpanan Nasional (BSN TemaNiaga, BSN TemanMesra, BSN TemaNiaga-i)	TEKUN Nasional (Tekun Financing)
Malayan Banking Berhad (Maybank Micro)	Agro Bank (Modal Usahawan 1 Malaysia-i)	Amanah Ikhtiar Malaysia, AIM (ikhtiar financing scheme such as i-Mesra, i-Srikandi and i-Wibawa)
Bank Muamalat Berhad. (Skim Mikro)	Bank Rakyat (Skim Pembiayaan Mikro)	
Public Bank Berhad (PBMicro)	Small and Medium Enterprises Bank, SME Bank (Enrichment and Enhancement Programme)	

According to the Department of Statistics Malaysia (2016), the major obstacles faced by the MEs in obtaining financing from government agencies and financial institutions are due to the lack of collateral, insufficient loan documentation, long loan processing time and high cost of borrowing. Therefore, in order for the MEs to sustain businesses, there is an urgent need for alternative sources of financing since lack of fund and insufficient capital are often cited as a stumbling block for MEs development, particularly in their early stages of growth (Carpenter, 2001; Meijerink & Roza, 2007; SME Development Council, 2016).

Table 1.3 Access of Financing for Micro-Entrepreneurs
Source: (Department of Statistics, Malaysia, 2016)

Sources of financing	Percentage [%]
Internally generated funds/shareholders' own contribution/personal saving of business owner	58.1
Others (such as grants or financing from government agency, co-operative and leasing companies)	28.8
Micro-credits, banks and other financial institutions	16.2
Family and friends	15.0

Note. Each factor has total of 100%

Recently, one of the financing alternatives for MEs proposed by Bank Negara Malaysia (2016) is by approaching microfinance institutions (MFIs). Theoretically, MFIs have the potential to enable investment in income-generating activities, consumption smoothing, and financial planning (Stewart et al., 2013). Indeed, MFIs are established to supply financial services to individuals or groups that would otherwise lack access to traditional banking services (González, 2014). The emerging microfinance revolution, in recent decades, with appropriately designed financial products and services could enable MEs to expand and diversify their economic activities, increase their incomes and improve their social wellbeing (Bennett & Cuevas, 1996; Ledgerwood, 1999; Mordurch, 2000; Alam et al., 2011; Akhter et al., 2009; Manzur et al., 2013).

The focus of microfinance is to increase the financing share in micro-scale businesses through micro-financing instrument. There are several microfinance products and services offered such as micro-credit, micro-saving, micro-insurance and financial service training (González, 2014). However, among others, one of the prominent microfinance products used by MEs in Malaysia is micro-credit, which is

offered by *Ar-Rahnu* institutions (Mohd Sam et al., 2010). The introduction of *Ar-Rahnu* as a micro-credit instrument in Malaysia is seen as an alternative as it provides a financial product for the lower income group such as MEs who usually have limited capital or have been excluded from the mainstream financial system.

Ar-Rahnu scheme was initiated based on the decision made by the ministers on 30th January 1985. Terengganu was the first state to introduce this scheme through the Muassasah Gadaian Islam Terengganu (MGIT) on January 23rd, 1992. The MGIT is a fully financed agency by the Terengganu State Government established under the Islamic Religious Office and Terengganu Malay Custom. This establishment and operations are written under the allotment of Sections 12 and 14 Enactment of the Administration of the Terengganu Islamic Religion Affairs (no.2) 1986 (Hisham Sabri, Ummi Salwa & Yusof, 2013).

The good response by the customers of the MGIT has attracted the state government of Kelantan to establish *Ar-Rahnu* in Kelantan through the Pemodalan Kelantan Berhad (PKB) in March 1992. Both of these Islamic pawn centres are among the earliest exponents to the Islamic pawn scheme in Malaysia. When the scheme started to be well accepted by the community, Yayasan Pembangunan Ekonomi Islam Malaysia (Yapeim) started to offer the scheme at end 1992 by co-operating with Bank Islam Malaysia Berhad (BIMB), Bank Rakyat and AgroBank in Malaysia.

Ar-Rahnu institutions received good response from the public particularly to obtain liquidity services. As the banks mostly refuse to give financial loans especially to micro-entrepreneurs due to collateral issue and no stable income, micro-entrepreneurs tend to choose *Ar-Rahnu* as a source of capital for business (Rugayah, 1986; Yusri, 1995; González, 2014). According to Ismail and Ahmad (1997), *Ar-Rahnu* can be one of the potential financing channels for MEs. It shows that *Ar-Rahnu*

is clearly recognised as a source of capital for the MEs. In addition, *Ar-Rahnu* also being a source of capital for companies that are just starting as well as a source of capital injection for companies that have already been set up. Furthermore, as stated by the Department of Statistic (2016), it also highlights *Ar-Rahnu* as one of the sources of financing for MEs.

Apart from that, *Ar-Rahnu* also works as a tool for investment. *Ar-Rahnu* encourages people to save and trade at the same time (Hisham et al., 2013). This is seen as a form of investment as jewellery, especially those made from gold, always have a strong stable market value (Mydin Meera, 2009). As stated by Awang Kechil et al. (2005) and Othman et al. (2013), having gold as the underlying transaction will assist a person who needs the money to start a business or inject more capital to their business. In short, micro-entrepreneurs can pledge the gold and take cash immediately.

Although *Ar-Rahnu* is one of the viable services of financing for micro-entrepreneurs, there are issues in terms of its acceptance among customers. For example, the usage of *Ar-Rahnu* among male entrepreneurs is insignificant in value, whereas female micro-entrepreneurs view *Ar-Rahnu* as one of the important tools in order to get access for cash instantly. According to Aziz (2006), Chan and Owyong (2007), Muhamat et al. (2011), Amin (2011), Mokthar and Zambahari (2012) and Murisa and Chikweche (2013), women who are active in micro businesses often resort to pawn brokers as a means to get short term capital to enhance their business. They often pledge their jewellery early in the morning for cash to be used in their business activities during the early part of the day and redeem back at the later part of the day after receiving profit from the day's business.

According to Muhamat et al. (2011), such use of pawn broking facilities has been successful in helping women micro-entrepreneurs and invigorating the economy without putting much burden on the pawn broking services. In addition, Nik Azman, Kassim and Adeyemi (2016) suggested *Ar-Rahnu* can be the effective tools for women micro-entrepreneurs to be self-sufficient financially. According to the finding, it indicates women micro-entrepreneurs are able to diversify and expand their business by using *Ar-Rahnu*. *Ar-Rahnu* assists women micro-entrepreneurs to transform business from traditional to more profitable businesses.

On the contrary, documented by Muhamat et al. (2011), most men feel humiliated and embarrassed if they were to resort to pawning their spouse's jewellery to obtain cash. This finding suggests that men would rather borrow from relatives in times of need. Therefore, as women are most favourable group in using *Ar-Rahnu*, this study focuses only on women micro-entrepreneurs, specifically on how they diversify and expand their businesses by having capital from *Ar-Rahnu*.

1.1 PROBLEM STATEMENT

In the past few years, there has been a rapid growth in micro-enterprises in Malaysia. This is well-reflected by the increasing number of micro-enterprises registered from 434,939 in 2005 to 496,458 in 2011 (Department of Statistics, Malaysia, 2016). Today, micro-enterprises are playing an increasing role in the economy and have started to make positive contributions to the development of the Malaysian economy. MEs also provide similar economic functions as small and medium enterprises, particularly in terms of promoting employment, technological innovation and training of entrepreneurs, developing international economic relationships, accelerating market competition and maintaining economic vitality (Zhou, 2004).

An interesting development in the MEs in Malaysia is the increase in women's involvement in the MEs (Babajide, 2012; Department of Statistics, 2016). Ironically, despite the important role of women micro-entrepreneurs towards supporting the industrial development in Malaysia, there have been limited financial resources available for them (Department of Statistics, 2016). It is important to highlight the peculiarities in the financing needs of the women micro-entrepreneurs which are "urgent, small and frequent" in nature, often categorised as short-term loans (Ismail & Ahmad, 1997). Since most of them cannot successfully obtain financing from financial institutions or banks, this has greatly hindered the development of women micro-entrepreneurs over the years (Ismail & Ahmad, 1997).

Despite the various types of funding being allocated to women micro-entrepreneurs through several government agencies, these women micro-entrepreneurs are still facing difficulties to access funds. The difficulties can be attributed to various issues of which bureaucracy of the funding agencies has been identified as one of the main hindrances for women micro-entrepreneurs to access the funds. As stated by several studies such as Saleh and Ndubisi (2006), Westover (2008), Hassan et al. (2011), Mohamed Zabri (2012), Darmansyah (2013), and Abbas, Abdul Razak and Saad (2014), financial institutions take a long time to disburse the loans, usually around three to six months with various documents requested by the bank, in addition to high cost of borrowings, high legal documentation fees and other charges as imposed by the financial institutions. All these dampen the spirit of women micro-entrepreneurs from sourcing funding either from government-related agencies or financial institutions.

In view of the obstacles faced in accessing government funds, the major financing channels for women micro-entrepreneurs have remained private loans and