

## ISLAMIC MICROFINANCE AND POVERTY ALLEVIATION PROGRAM: PRELIMINARY RESEARCH FINDINGS FROM INDONESIA

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**ABSTRACT** - Poverty should be defined, measured, and scrutinized its root causes from a multi-dimension perspectives. Therefore, in designing and implementation of poverty alleviation program, it should consider economic factors, social and political contexts surrounding the poor. Sen (1982; 1999) views poverty as a multifaceted world and ethical dimension essentially should be placed underpinning it as a vital economic problem. The paper takes the stance that the poor themselves have potential capacity to alleviate their condition in resolving poverty trap. Community development program is one of the strategies to deal with the poverty problem. Islamic microfinance can play an important role in combating poverty dilemma especially in Muslim majority population communities. Through the approach proposed by Bigg and Satterthwaite (2005) with strengthening local organizations and community development programs, Islamic microfinance should engage a strategic partnership with the Masjid and Islamic charity institutions (zakat and waqf organization). This strategic alliance will result more integrated programs and also capacity building of the institutions involved. This paper aims to contribute a grass root model in the purpose of combating poverty in the framework of Islamic economic system.

**Keywords:** Islamic microfinance, poverty alleviation, community development, local organization

**ABSTRAK** - Kemiskinan harus didefinisikan, diukur, dan diteliti akar penyebabnya dari berbagai perspektif. Oleh karena itu, dalam merancang dan mengimplementasikan program pengentasan kemiskinan, faktor-faktor ekonomi, konteks sosial dan politik yang mengelilingi kemiskinan juga harus dipertimbangkan. Sen (1982; 1999) memandang kemiskinan sebagai sebuah dunia yang kompleks, dan dimensi dasar etika harus ditempatkan sebagai sebuah masalah ekonomi yang vital. Peneliti sendiri dalam hal ini berpandangan bahwa orang-orang miskin pada dasarnya punya kapasitas yang memadai untuk keluar dari garis kemiskinan. Salah satunya adalah dengan program pengembangan masyarakat yang merupakan satu strategi dalam pengentasan kemiskinan. Keuangan mikro syariah dapat memainkan peran penting dalam memerangi dilema kemiskinan, khususnya di daerah-daerah yang mayoritas penduduknya Muslim. Pendekatan yang diusulkan oleh Bigg dan Satterthwaite (2005) adalah dengan cara penguatan organisasi lokal dan program pengembangan masyarakat dimana keuangan mikro syariah harus terlibat dalam kemitraan-kemitraan strategis dengan masjid-masjid dan lembaga-lembaga sosial lainnya (seperti lembaga zakat dan wakaf). Aliansi strategis ini akan menghasilkan program-program yang lebih terintegrasi dan juga ada penguatan capacity building dari lembaga-lembaga yang terlibat. Makalah ini bertujuan untuk berkontribusi dalam memberikan model akar rumput dalam hal pengentasan kemiskinan dalam kerangka sistem ekonomi Islam.

**Kata kunci:** Islamic microfinance, poverty alleviation, community development, local organization



## INTRODUCTION

Further and careful observations should be conducted to evaluate the achievement of the Millennium Development Goals (MDGs) in poverty alleviation programs. For instance, Mody and Pattilo (2004) point out that even though poverty reduction programs result in real impact but the number of people falling into poverty is quite considerable. Therefore, claims that there has been a significant turn down in the global incidence of extreme poverty (in percentage of the world population with income less than \$ 1 per day) is a controversial discourse.

Poverty should be defined, measured, and scrutinized its root causes from a multi-dimension perspectives. Thus, in designing and implementation of poverty alleviation programs, it should consider economic factors, social and political contexts surrounding the poor.

Sen (1981) views poverty as a multifaceted world and ethical dimension primarily should be placed underpinning it as a vital economic problem. Furthermore, he perceives that rather than taking into consideration income measurement as in categorizing poor people, he endorsed to deal with the poverty as the deprivation condition of basic capabilities from the poor.

In this regard, financial institution plays a vital role to provide intermediary function from surplus unit to the deficit unit in the economy system. This particular function will accelerate realization of economic growth. Especially, financial institutions provide financing instruments for the potential entrepreneurs and productive projects as engine of growth in economy.

Despite the vital function of financial institution, in fact most of the developing countries have been facing inadequate level of accessibility of finance. As reported by CGAP and World Bank (2000), in developing countries 72% (around 2.7 billion people) of adults do not have bank accounts. Mainly the banking sector has weaknesses in reaching SMEs and the poor people as the potential customers.

Consequently, optimizing the role of financial institution in reducing income inequality and poverty problem should emphasize the issue as financial inclusion (improve access to finance) in financial sector (World Bank, 2000; Iqbal & Mirakhor, 2013).

In the circumstance where financial inclusion has not reached the poor, then poverty alleviation programs should consider that microfinance institutions to play its important role in empowering the poor. Many studies have shown that



microfinance institution has positive impact in combating poverty problem, especially in increasing income and reduction vulnerability of the poor (Masyita & Ahmed, 2013).

Meanwhile, alongside current tremendous development of Islamic bank worldwide, the Islamic microfinance institutions assumed to have a vital role in financing the poor and SMEs (Small medium Enterprises) in the Muslim world. Hence, Mukatadir (2012) affirms for bringing initiatives in realizing the potential of Islamic microfinance institution in providing accessible financial services, promoting empowerment through entrepreneurship activities and creating an equitable distribution of wealth for the poor.

This paper aims to discuss the possibility of ending world poverty in the lens of local organizational initiatives rooted in the society (Bigg & Satterthwaite, 2005). Specifically, this paper presents a preliminary research findings and case studies of the strategic alliance experience of Islamic microfinance, the Masjid (the Mosque) and Islamic charity institutions (zakat and waqf organizations) in Indonesia.

#### **MICRO FINANCE DEBUT: BANKING FOR THE POOR**

Financial institution has a fundamental role to provide intermediary function from surplus unit to the deficit unit in the economy system. If this feature runs well, regardless the size of the economic scale, it will generate value added in economic activities (Hamada, 2010; Wijono, 2005).

However, the depth of the financial sector and financial inclusion in developing countries is still relatively low. According to CGAP and World Bank (2000) in developing countries about 72% of adults do not have bank accounts. It means the banking sector has weaknesses in reaching all segments of bank customers. Particularly SMEs and the poor people, these segments substantially have no adequate access to the banking sector.

Therefore, in the circumstance where financial inclusion has not reached the poor, then poverty alleviation programs should consider that microfinance institutions to play its potential role in empowering the poor.

World Development Report 2000/2001: *Attacking Poverty* (World Bank, 2000) raises a call for urged solution to address chronic poverty problem in around the world. World Bank exposes the need to find a breakthrough for a new strategy in fighting poverty. In this new policy, World Bank (2000) promotes actively to



a wide-ranging approach including "promoting opportunity, facilitating empowerment, and enhancing security".

Hamada (2010) asserts that the microfinance institution is a feasible financial institution for this purpose as it provides a viable access to the poor to financial resources and to facilitate community empowerment. Microfinance can serve a bridge the obstacles of poor in accessing formal financial institutions with more simple procedures and requirement compare to commercial banks.

Microfinance has been acknowledged as a success story in poverty alleviation efforts over past decades. Though, the origins of microfinance program in emerging markets can be referred in the mid of 1970s initiated by Muhammad Yunus, the Nobel Prize for Peace in 2006; for establishing Grameen Bank. Concurringly, ACCION in Brazil and Bank Rakyat Indonesia (BRI) in Indonesia, Banco Sol in Bolivia, ASA and SafeSave in Bangladesh developed similar microcredit business models to serve more broadly customers to the public.

The successful story of Grameen Bank with outstanding performance to achieve in providing loans to 7.9 million borrowers, of which 97% are women and with the repayment rate is 98% become magnitudes in many studies of economics and poverty reduction agenda (Becker, 2011; Hamada, 2010; Zeller & Meyer, 2002).

Furthermore, Robinson (2002) argues that micro credit is a powerful mechanism in overcoming poverty. This opinion is based on the understanding that the poor people should be categorized into several groups. Firstly, the extreme poor, people who have no income and are unable to perform economically productive activities. Secondly, the economically active working poor are people as poor but have a productive economic activity. Thirdly, lower income means community groups with insufficient income.

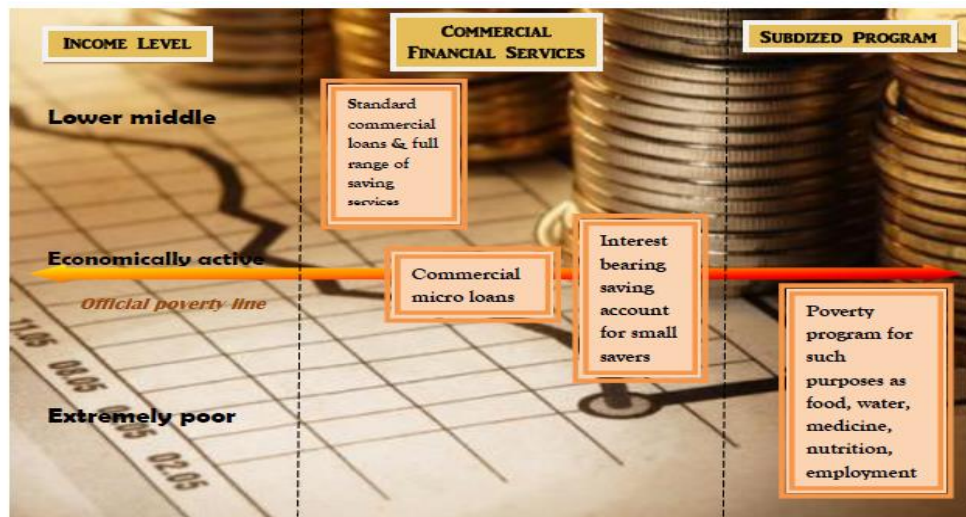
Therefore, Wijono (2005) argues that poverty reduction approaches dealing with the poor should be set to each category of the poor differentially as shown in Figure 1. The first group, for example, it is appropriate through the emergency program in order to ensure the basic needs of the poor, e.g. direct subsidy for food or cash for works. As for the second and the third groups indirect approach is more effective, for example in the form of the provision of financing facilities and business incubators for SMEs , provision of infrastructure for the poor, equitable business climate for businesses large and small will be a massive impact for poverty reduction.



Behind the success of microfinance in achieving resource providing financial access for the poor, a number of concerns and academic research has been carried out for assessing the performance and sustainability of microfinance in addressing poverty problem (Hamada, 2010; Zeller & Meyer, 2002). In this context, Hamada (2010) argues that the optimum contribution of microfinance can only be realized if microfinance strongly has appropriate institutional design and well management.

However, she underlines a number of paradigm shifts has occurred in the micro finance development (Hamada, 2010). Firstly, a change paradigm in looking at the microfinance movement as microfinance operation raises the issues of high transaction costs and risks and also information asymmetry problems. It can be drawn from the changing conditions when in the 1960s era micro finance has focused to serve farmers with subsidy and microloan, then turned into 1980s era when microfinance more active in empowerment financing for the poor massively. Secondly, a new paradigm emerged then as an attempt to acquire microfinance movement into initiatives in creating an inclusive financial sector (United Nations, 2006). As in 2004, the Consultative Group to Assist the Poor (CGAP) endorsed the "key principles of microfinance" framework in which the issue of financial inclusion becomes a new genre in global financial industry.

Figure 1. Financial Services in the Poverty Alleviation Toolkits



Source: Adopted from Wijono (2005)

Although microfinance achievement indicates outstanding expansion, but aggregate view around the world will find that the poor who fall in poverty trap remains large in numbers. Push factors to increase the outreach of microfinance



may bring the tendency to get funding from third-party financial sources such as donor fund, government support or even commercial banks. Here the first dilemma will take place; the expansion will lead to increase commercialization of microfinance at the expense of the occurrence risk in deviation microfinance's main objective in helping the poor.

Providing suitable measurement of direct impact contributed by microfinance in combating poverty will be second dilemma. Examine the performance of microfinance only with the lens of the number of borrowers or total amount of loans have given will result a misleading understanding on the impact of microfinance in poverty alleviation. Measuring microfinance's impact in poverty is needed in proving that the microfinance recipients have improved their economic capabilities and evaded from debt trap.

The next dilemma is associated with the financial sustainability of microfinance to fund its business operations. The commercialization of MFIs is one of solution in facing financial sustainability.

### **A CALL FOR ISLAMIC MICROFINANCE**

Iqbal and Mirakhor (2013) assert that the financial inclusion realized in Islamic finance core objectives with encouraging risk sharing modes of financial instruments contract and redistributive wealth concept in the economy.

In line with this notion, Muktadir (2012) recalls for a confluence of Islamic finance and microfinance as these particular institutions have the parallel objectives of providing accessible financial services, promoting empowerment through entrepreneurship activities and creating equitable distribution of wealth for the poor.

Therefore, Obaidullah (2008) asserts that at the core of Islamic spirit in solving the poverty dilemma is the inclusive nature should be attached to Islamic financial development. It means that Islamic finance has to concerning with poverty alleviation issues as fundamental social responsibility in achieving Shari'ah objective (*al maqashid shariah*) and avoiding poor people fall into debt trap as adverse effect of compound interest rate.

The fundamental difference between conventional and Islamic microfinance is the obligatory of Islamic microfinance in using financial contracts that comply with the shariah principles (e.g. it must free from interest rate/*riba*, speculative/*gharar* and gambling/*maysir* transactions) and adhere of Islamic business ethics. Some studies have distinguished in details the *modus operandi*



of conventional microfinance and Islamic microfinance as shown in Table 1 (Ahmed, 2002; Obaidullah, 2008; Riwijanti, 2013).

Ahmed (2004) asserts that Islamic finance modes are suitable in designing financial contracts and products of Islamic microfinance. Usually, Islamic microfinance provides sales based contracts (*murabahah*, *ijarah*) or project/equity partnership contract (*musyarakah* and *mudharabah*). In particular, Islamic microfinance has advantage to channel financing the poor with Zakat and Islamic charity fund. This specific financing are delivered in the format of non-interest loan/grant contract (*qardhul hasan*) and micro insurance for the SMEs in mitigate their business risk.

Table 1. Differences between Conventional and Islamic Microfinance

Category	Conventional Microfinance	Islamic Microfinance
CATEGORY OF POOR	One Category	Two level : 1. Deeply poor who do not need loan but social safety net and charitable fund ( <i>zakah</i> ). 2. Moderately poor who will be better of if they obtain credit for running microenterprises
BASED OF FINANCING	Debt based and interest based approach	Profit and Low Sharing (PLS) approach, free of interest ( <i>riba</i> ), and uncertainty ( <i>gharar</i> )
APPROACH / TARGET OF EMPOWERMENT	The poor and woman	The poorest and family
SOURCES OF FUND	External fund, saving of clients	External funds, saving of clients and Islamic charity fund
DEALING WITH DEFAULT	Group/Central Pressure and Threats	Group / centre / spouse guarantee, and Islamic ethics
SOCIAL DEVELOPMENT PROGRAM	Secular	Religious (behavior, ethics, and social)

Source: Adapted from Riwijanti (2013)

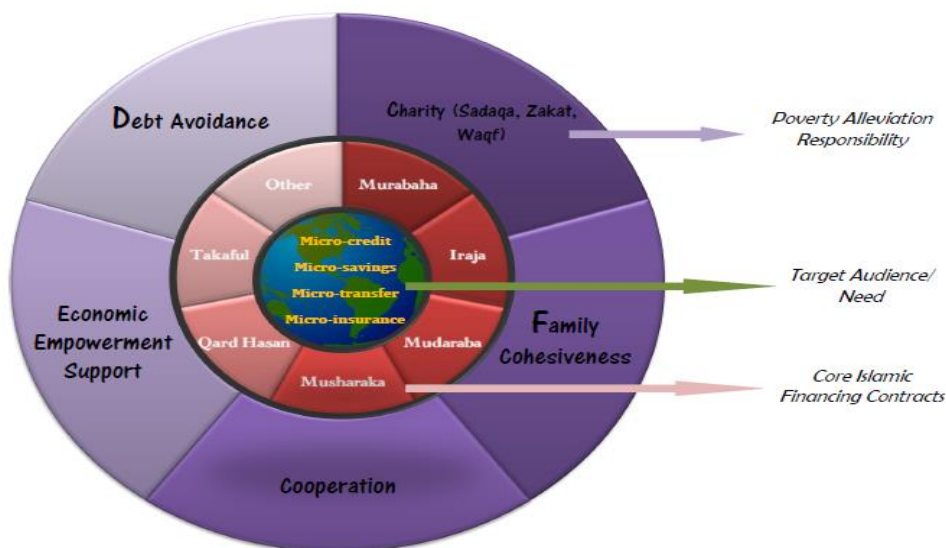
Based on the discussion above, we can offer a framework of Islamic microfinance business process based on three layers, namely responsibility in poverty alleviation mission, providing Shariah compliant financial services and focusing target of the poor. With this comprehensive framework, we can depict all aspect of concerning should be attached in Islamic microfinance programs (Shikoh, n.d).

Idealist spirit of Islamic microfinance in combating poverty will involve such considerations: avoiding debt trap, promoting economic empowerment program, giving society as foundation for cooperation among people, protecting family



institution as cohesiveness and put Islamic charity programs (*Zakat* and *Shadaqah*) as means for support the poorest. Meanwhile, Shariah financial contract become a basis for product development in Islamic microfinance in which profit and loss sharing (PLS) approach will be delivered to generate equality in the doing business. After all, as the target of Islamic micro finance, this institution will categorize two types of the poor as deeply poor who actually do not need loan but social safety net and charitable fund and moderately poor who need support in financial access for running microenterprises (See Figure 2).

Figure 2. Framework of Islamic Microfinance Business Process



Source: Adopted from Shikoh, n.d.

While the Islamic microfinance has a promising advantage in resolving poverty problems, according to CGAP (2008) currently Islamic microfinance outreach is remain concentrated in limited Muslim countries, contributing only 0.5 percent penetration of global microfinance and serving only about 380,000 customers.

However, Obaidullah (2008) argues that RDS (Rural Development Scheme) of IBBL's (Islamic Bank Bangladesh Limited) achievement which was better compared to three conventional leaders in microfinance; Grameen Bank, ASA (Association for Social Advancement), BRAC (Bangladesh Rural Advancement Committee); in terms of growth (12.5%), dropout rate (5%), and operational efficiency.

Riwajanti (2013) asserts that the impacts of Islamic microfinance program can be scrutinized in two aspects: economic and social impacts. In social impact, it



includes how the Islamic microfinance contributes in improving social harmony, higher Islamic knowledge and educated people, quality of life and health level of the society. Some studies have proven the economic impact delivered by Islamic microfinance programs. Among others, Rahman and Ahmad (2010) expose an example of economic impacts of Islamic Bank Bangladesh Limited (IBBL)'s microfinance financing on rural poverty. This study shows that productive financing has contributed to household earnings, output of harvest and cattle, disbursement and employment. Other study by Shirazi (2012) comprehensively exposes the successful of Islamic microfinance program to increase significantly economic benefit and wellbeing of the financing recipients.

In addition Masyita and Ahmed (2013) reports that in Indonesia Islamic microfinance also still in a niche market in the public as total number of Islamic micro finance (in the form of Cooperative or NGO under name Baitul Maal Wat Tamwil/BMT) only around 3,000 compare to total amount microfinance institution which reach 40,000. Important note should be underlined also in their survey that even though most of Islamic microfinance clients are Muslim and their preference to choose Islamic microfinance cause of fit in Shariah compliance but in choosing financial provider this microfinance customer has rational behavior in considering economic factors such as low interest rate, quality service and low collateral.

On the other hand, Masyita and Ahmed (2013) underlines two crucial issues related to Islamic microfinance modus operandi. Firstly, it should be considered that the poor not only need to increase their income but also to mitigate vulnerable risk for their future. This brings notion to have a shifting paradigm of microfinance to 'inclusive finance'. Recognizing this condition, Islamic microfinance program should equip their operation with saving instruments, microinsurance, and charity programs.

Secondly, Islamic microfinance has challenge to undertake trade-off obstacle between outreach and sustainability of their programs. In this sense, issues of institutional and organizational features should properly put in place in order to build a strong institutional capability to resolve the trade-off problems in running their business. In this sense, Masyita and Ahmed (2013) concludes that Islamic microfinance has two approaches to providing financial services for the poor: 'poverty approach' and self-sufficiency approach'. Under poverty approach, it is preferable that the Islamic microfinance operate as non-profit institution as mainly the financing program will be focused on the poor and core-poor recipients. Whereas in self-sufficiency approach, it is appropriate for the



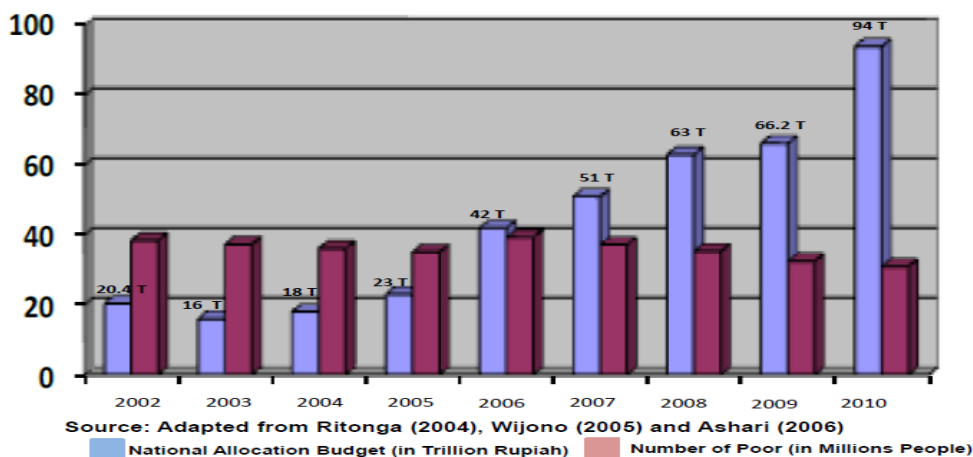
Islamic microfinance to have a commercial and profit oriented legal entity as the most recipient will be less poor or SMEs.

### **POVERTY ALLEVIATION PROGRAM IN INDONESIA: STRENGTHENING THE ROLE OF COMMUNITY DEVELOPMENT AND LOCAL ORGANIZATION**

Economic development and poverty alleviation programs in Indonesia have started since the proclaimed of Indonesia independence post Dutch colonialism in 1945. This very initial effort is continuing during the Old Order under the leadership of President Sukarno up to 1965. Following, the national development and poverty alleviation programs have been conducted intensively during the New Order period under the leadership of President Suharto since 1966-1998.

However, some studies show a series of poverty alleviation programs do not yet effectively reduce the number of poor people in Indonesia (Ritonga, 2004; Wijono, 2005). In statistic figure, even though Indonesia has experienced with significant economic growth in the New Order period since 1970-1996 with an average economic growth of 7.5 % per year, unfortunately the poor in 1996 is still relatively high at 34.5 million people (17.5 %).

Figure 3. Comparison National Allocation Budget on Poverty Reduction and Number of Poor in Indonesia (2002-2010)



Yet, when we look at the post-reform period since 1998 (after President Suharto's era), the government budget policy to allocate in poverty alleviation programs has been experiencing a considerable increasing significantly as shown in Figure 3. For instance, in the period 2002-2010, various government programs in combating poverty have received budget allocations amounted 20.4



trillion Rupiah in 2002 and increased amount to 94 Trillion Rupiah in the year 2010. Regrettably, in this period, these particular programs have not been significantly effected in reducing the number of poor people as at the end of 2010 the number poor of people was still quite high at 31 million people (13.3%).

Further scrutinizing on the Indonesia's poverty problem shows that the poor people is majority in rural areas with main job is farmer, work in the Small Medium Enterprises (SMEs) sector and other informal business (Ashari, 2006). He exposes that the number of poor people is at 36.1 million people in whom there are 21.3 million people living in the rural region and work in the agricultural sector for the period 2004. In fact, in this case the main problems faced by the poor among others are constraining to raising capital and lack of access to formal financial institutions.

Some studies have been conducted to evaluate these ineffective programs in alleviating poverty problems in Indonesia (Bahri, 2012; Ritonga, 2004; Wijono, 2005). The notions in this point of view conclude that basically there are two important factors causing the failure of poverty alleviation programs in Indonesia. First, poverty alleviation programs have been more focus on the distribution of social assistance for the poor and being in the charity means. These programs, usually are performed in the form of rice distribution, subsidy for the poor and the social safety net (Jaring Pengaman Sosial/JPS) to the poor. As a result, this kind of programs would be difficult to resolve the problem of poverty because these only lead to 'dependent behavioral' and do not bring community empowerment themselves. Supposedly, this poverty alleviation are more focus in productive economic activities in order to improve capabilities of people in their community (Sen, 1999; Wijono, 2005). The second factor that led to the failure of poverty alleviation programs is the lack of comprehensive understanding in the causes of poverty and performing the most effective strategy to reduce poverty in the root of the problems.

In general, poverty alleviation programs in Indonesia comprise these following approaches (Bahri, 2012). First, top-down model. In this model, the government runs centralized of policy and program. The poor is treated as target and object. They are not getting involved in the formulation and search for a strategy in addressing poverty problem. Secondly, bottom-up model. This model treats the poor not only as the object of the program, they are also involving in each stage of activities planning, executing and monitoring of poverty alleviation programs. Another model, it can be a hybrid of the two models explained before. In hybrid-model, some stages and or some programs will be performed using top-down



whereas the remains will be conducted under bottom-up model, which one is most effective.

Essentially, poverty reduction programs should be based on the idea that the poor themselves have potential capacity to alleviate their condition in resolving poverty trap. In this sense, government and community should hand in hand in facilitating the poor to empower their capacity and prevent any externalities which can cause ‘structuralized poverty’ in the society.

Hence, one of the strategies to deal with the poverty problem is community development program. This program actually intend to encourage community as a subject to engage poverty reduction program collectively by using various resources that attached by the community. So, the key success factors for the community development program are participation and empowerment exercise by the member of the community. Community development programs includes initiatives in training workers for capacity building in applied skills, simple education infrastructure for the farmer in the rural area, social entrepreneurship, financing through microfinance to the Small Medium Enterprise (SMEs), opening traditional market for the poor, etc.

In addition, Bigg and Satterthwaite (2005) highlight the importance of local organization contribution in achieving MDGs’ targets. Their arguments on this are based on some judgments. Firstly, outcomes of MGDs’ will be laid on the locality context of the poor, so it will require intensely local dimension involvement. Secondly, local organization in the construct of active citizenship (Green, 2012) can influence government and political view to support poverty reduction programs in public policy recommendation. Thirdly, the local organization involvement will reduce the negative impact of centralized model of government and international agency in poverty reduction engagements.

In this context, community development program based on capabilities of the local organization will become the key factor to achieve community empowerment circumstance. Conditions in which community-based effort can engage planning, decision-making and management of local resources through collective action and networking (Subejo and Supriyanto, 2004).

Notion of optimizing the role of Islamic microfinance in this sense can have this inspiration with this strengthening local organization contribution. Recognizing that Islamic microfinance mostly operate and target their program for the poor in Muslim community, this effort should further involving local organization (such as Masjid, Zakat and Waqf organization (Islamic charitable organization),



Islamic cooperative/community based microfinance) inclusively in empowering the poor.

### **OPTIMIZING THE ROLE OF LOCAL ORGANIZATION AND ISLAMIC MICROFINANCE AS CENTRE OF COMMUNITY DEVELOPMENT**

The idea of optimizing the role of Islamic microfinance in tackling poverty should obtain this inspiration from strengthening the local organization (Bigg & Satterthwaite, 2005). Considering, Islamic microfinance operates and targets their operation to the poor who are mostly located in Muslim communities, optimization model further involving the mosque and the Islamic charity organization inclusively.

As research finding results shown by SEBI Research Centre (2011), most programs of Islamic charity institution in are almsgiving oriented. They only put aside a small proportion of funds to support economic productive business activities to empower the poor and agriculture financing. There are only a few regional branches of Lembaga Amil Zakat Nasional (LAZNAS/national level of zakat organization) which offer agriculture financing schemes, like the economic empowerment programs for breeders-farmers. These programs, however, usually end unsuccessfully due to the beneficiaries' low commitment and weak program designs.

This paper briefly expose a preliminary research finding of two initiatives in community development activities through Islamic microfinance programs in the context of local organization strengthening. The first case study is Koperasi Ikhtiar Swadaya Mandiri (Ikhtiar Swadaya Mandiri Cooperative) in Kabupaten Bogor, West Java, Indonesia. Secondly, Best CD-Baitul Maal Muamalat projects of economic empowering in Bandung City, West Java, Indonesia.

Koperasi Ikhtiar Swadaya Mandiri is a community-based cooperative established by housewives in the Buanajaya village, Bogor which conduct household economic empowerment program with saving program-financing scheme for the members as peer group. Buanajaya village is categorized as poor rural villagers and low level of education. Mitra Mandiri NGO (Non-Governmental Organization) of Zakat Organization Dompot Dhuafa then became the village's counterpart for public education and mentoring programs in poverty alleviation programs.

Best CD is a NGO that focuses in contributing to community development project in Bandung and surrounding areas of West Java. This NGO collaborate



with Baitul Maal Muamalat Zakat Organization to undertake such program of economic empowerment through microfinance Islamic financing for farmers and SMEs (Small and Medium Enterprises). A number of findings features and modus operandi of both local organizations activities can be summarized in Table 2.

Table 2. Features and Modus Operandi of Local Organizations for Community Development

	<b>Koperasi Ikhtiar Swadaya Mandiri</b>	<b>Best CD NGO</b>
<b>Type of Institution</b>	Community based cooperative	NGO
<b>Core programs in poverty alleviation</b>	Profit sharing saving-financing activities as peer group	Entrepreneurship training and business coaching for farmers and SMEs
<b>Collaboration and source of funding for projects</b>	From Dompot Dhuafa Zakat Organization, saving from cooperative members, grant from governmental agency	Mainly from Baitul Maal Muamalat Zakat Organization
<b>Process of local organization strengthening</b>	From the beginning of cooperative establishment.	Establishment of NGO at the beginning and strengthening local organization through collaboration programs

Some interesting findings from the interview with the key persons of both local organizations could be presented below:

- The most important finding from the community developments programs of both local organizations is the establishing strategic alliance with the zakat organization as financing resource of the programs and capacity building of organization. In this context, the both local organization also recognized the Masjid as a vital public institution to become a center for public education and center of community development for the society.
- Noticeable, the Islamic microfinance schemes are recognized by both institutions in poverty combating programs. Especially in Koperasi Ikhtiar Swadaya Mandiri, peer group financing is an advantage for its sustainability programs.



- Efforts for strengthening local organization, in Koperasi Ikhtiar Mandiri, it is started from the beginning of the cooperative establishment in which Mitra Mandiri NGO (Non-Governmental Organization) of Zakat Organization Dompot Dhuafa became the village's counterpart and performed community poverty mapping, public education and empowerment motivation training for the society. However, in Best CD NGO, these strengthening efforts were conducted after economic empowerment program began in collaboration with Baitul Maal Muamalat Zakat Organization. In this regard, Koperasi Ikhtiar Mandiri has performed a comprehensive approach in community development consist of planning, community assessment problem using *Participatory Rural Appraisal (PRA)*, action program plan and programs execution.

This strategic partnership between the local organizations and the Islamic microfinance programs will result more integrated programs and also capacity building of the institutions involved. Through this breakthrough initiative two advantages will be attained; firstly, getting broadly involvement of Muslim community based religious activities in mosques as human resource in community development and empowerment programs; and secondly, performing effective accumulation and distribution of Islamic charity funds to finance poverty alleviation programs as research finding showed that most programs of Islamic charity institution in are merely almsgiving oriented. They only put aside a small proportion of funds to support economic productive business activities to empower the poor.

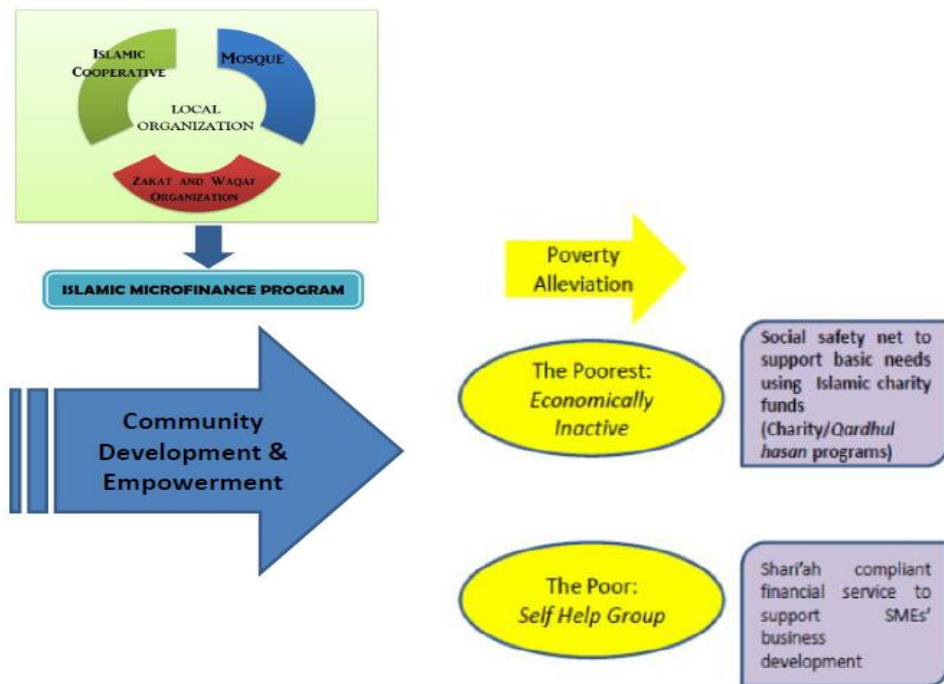
With the emphasis of using Islamic microfinance as an important instrument in poverty alleviation programs, this particular strategic alliance could be presented as a framework model to capture obstacles facing by local organization in the sense of program sustainability, lack of financial resource, lack of human resource and program evaluation and feedback (see in Figure 4 below).

In this strategic framework model, Islamic microfinance instruments which is inherently attached with local organizations (in this sense the Masjid, Zakat and Waqf Organization, Islamic cooperative) in order to conduct community development activities. From community development perspective, poverty alleviation programs should categorize poor people into two categorized namely *the Poorest* (economically inactive) and *the Poor* (self-help group). In these two types of target program, Islamic microfinance should design and develop programs which have optimum collaboration impact together with local organization. For instance, for the Poorest, community development should provide social safety net to support basic needs using Islamic charity funds.



Meanwhile, for the Poor, a slightly difference approach should be implemented in which business development for SMEs and entrepreneurship capacity building is the best choice.

Figure 4. Framework of Islamic Microfinance Instruments and Local Organization Strategic Alliance



In this regard, it is recognized that evaluation and feedback mechanism is imperative in engaging community development. Therefore, the possibility of ending poverty from the lens of local organizational strengthening initiatives will equip community development with adequate assessment process in two ways (Bigg & Satterthwaite, 2005). Firstly, poverty alleviation outcomes improved should be translated into particular locality measures, such as level of income, food security, and sustainability of income. Secondly, strengthening local organization will avoid a distortion of centralized planning result of economic empowerment for the society.

## CONCLUDING REMARKS

Poverty problem should be defined, measured, and scrutinized from multi-dimension perspectives. Moreover, in tackling poverty as a vital economic problem, a policy making process that has an ethical dimension must be put forward. From this comprehensive point view, the root causes of poverty will be



captured accurately as a basis for designing and implementation of poverty alleviation programs.

However, a note should be taken as Sen (1981) underscores to perceive poverty problem not merely as a matter of income measurement but should recognize poverty as the deprivation condition of basic capabilities from the poor. In the other hand, it is important to encourage decision making process in public policy to having a participated society approach as a basis for poverty reduction programs.

Microfinance has a high potential to perform as a financial intermediary that is viable for the poor and SMEs. However, despite the vital function of the financial institution, in fact, most of the developing countries have been facing inadequate level of accessibility of finance. As reported by CGAP and World Bank (2000), in developing countries 72% (around 2.7 billion people) of adults do not have bank accounts. Mainly the banking sector has weaknesses in reaching SMEs and the poor as the potential customers.

Meanwhile, alongside current tremendous development of Islamic bank worldwide, the Islamic microfinance institutions assumed to have a vital role in financing the poor and SMEs (Small medium Enterprises) in the Muslim world. Hence, Muktadir (2012) affirms for bringing initiatives in realizing the potential of Islamic microfinance institution in providing accessible financial services, promoting empowerment through entrepreneurship activities and creating an equitable distribution of wealth for the poor.

Islamic microfinance has the opportunity to actively contribute in poverty alleviation especially in areas with the largest Muslim community. Through the approach proposed by Bigg and Satterthwaite (2005) in strengthening the role of local organizations, Islamic microfinance should engage a strategic partnership with the local organizations (in this sense the Masjid, Islamic cooperative and Zakat and Waqf Organization) in order to conduct community development activities.

This strategic alliance will result more integrated programs and also capacity building of the institutions involved. This breakthrough effort also will get two advantages; firstly, getting broadly involvement of Muslim community based religious activities in mosques as human resource in community development and empowerment programs; and secondly, performing effective accumulation and distribution of Islamic charity funds to finance poverty alleviation programs.



As a preliminary research findings and case studies of the strategic alliance experience of Islamic microfinance, the Masjid (the Mosque) and Islamic charity institutions (zakat and waqf organizations) in Indonesia, this paper intends to propose a strategic framework model of Islamic microfinance and local organization strategic alliance to capture obstacles facing by local organization in the sense of program sustainability, lack of financial resource, lack of human resource and program evaluation and feedback process.

In conclusion, the possibility of ending poverty from the lens of strengthening local organizational initiatives will equip community development with adequate assessment process in two ways (Bigg & Satterthwaite, 2005). Firstly, poverty alleviation outcomes improved should be translated into particular locality measures, such as level of income, food security, and sustainability of income. Secondly, strengthening local organization will avoid a distortion of centralized planning of economic empowerment for the society.

In addition, it is an essential works to elaborate a grass root model of poverty reduction program using Islamic microfinance instrument in congruence with Islamic economic objective (*maqashid syariah*). In this sense, community development will be dealing with the poor to alleviate their condition in resolving socio-economic obstacles in the framework of Islamic worldview in perceiving poverty trap as universal human problem.

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