Journal of Islamic Finance, Vol. 8 No. 2 (2019) 10 – 20
IIUM Institute of Islamic Banking and Finance
ISSN 2289-2117 (O) / 2289-2109 (P)

Encouraging Islamic Financing to Achieve SDGs through Poverty Alleviation

Putri Ayu,[a] Achmad Rifa'i,[b] and Listiono[c]

[a]*Faculty of Economics, Andalas University, Indonesia;*
[b]*Directorate of Macro Planning and Statistical Analysis, Ministry of National Development Planning, Indonesia;*
[c]*Faculty of Islamic Studies, Muhammadiyah University of Yogyakarta, Indonesia;*

Abstract

Poverty is a challenge that must be encountered by every country in the world. Therefore, it is not surprising that poverty issues occupy the first goal out of the seventeen (17) goals in the Sustainable Development Goals or SDGs framework. Although, in general, the trend of poverty in Indonesia continues to decline, it turns out that the indication of a more acute poverty level is still difficult to be alleviated. The poverty index is reflected by the poverty severity index and poverty gap index. In this case, Islamic financing provides a more inclusive concept of poverty alleviation. The results of estimation by using panel data from 32 provinces from 2014 to 2018 in Indonesia reveal empirically that Islamic financing contributes to poverty alleviation programs through the financing of productive working capital. Hence, the financing made by Islamic banks are greatly supporting in achieving the SDGs' Goal 1 i.e. towards having no poverty. However, the achievement of Islamic banks needs to be expanded to reach the lowest point of people that are experiencing poverty through financing and productive economic activities.

Keywords: Financing, Islamic Banking, SDGs, Poverty, Panel Data

1. Introduction

The issue of poverty has always been a topic of discussion in both developed and developing countries. This is because poverty is taken as the beginning of all the vicious circles that make economy becomes not inclusive due to uneven growth excess. The poverty that afflicts society is very likely to continue to decline in the next generation. In addition, poverty also makes it difficult for society to access various basic facilities such as food, education, health, and social security. Such situation requires a multi-dimensional approach in term of policy in alleviating poverty. If it persists, the community will continue to be a poor community endlessly.

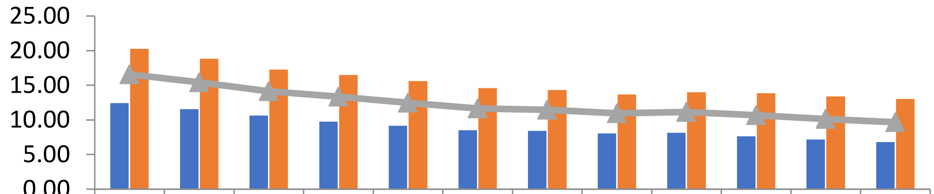
Thus, it is not surprisingly, that the issue of poverty becomes the first goal both in the era of the Millennium Development Goals (MDGs) and the Sustainable Development Goals (SDGs). This goal is reinforced from the MDGs' era, however, poverty is still the main enemy of every country. Thus, the struggle against poverty continues in the SDGs' era and stands as the main target.

Furthermore, Sirageldin (2000) explained that poverty is a complex phenomenon and this has survived at various levels in society and communities throughout the world since the recorded history. Regardless of available resources, developmental stages, and technological levels, and social or cultural structures, it continues to persist. This situation continues that even in the most advanced era, the issue of poverty surely emerges. However, each country has different characteristics of poverty. In developing countries, like Indonesia, poverty is placed as a top priority for every government's program. It can be inferred that the success of a government is assessed by looking at the indicator of poverty alleviation.

Poverty is identical to those low-income people who are unable to reach basic needs and result to low productivity because they do not have capital either financial or skillful capital. Judging from its location, poverty is divided into two levels: namely at (i) the urban, and (ii) rural levels.

Figure 1.0 shows Indonesia's efforts to reduce poverty significantly. In 2007, the national poverty rate was at the rate of 16.58 percent from the total population (Central Bureau of Statistics, 2019). With various poverty alleviation programs such as Direct Cash Assistance (BLT), Poor Rice (Raskin), Expectation Health Program (PKH) and so on, the poverty rate was successfully suppressed into a single digit in 2018 at 9.66 percent (Central Bureau of Statistics, 2019). Nonetheless, it is clear that the single digit decline in poverty at the national level is not followed by a significant decrease in the rural level. Even in the last 5 years, the magnitude of the decline in poverty levels in the rural level was quite low and stagnant at around 13 percent. It is very different from the decline in the poverty rate in the urban level which decreased significantly from 12.52 percent in 2007 to 6.89 percent in 2018. However, the poverty level in the urban level is always below the national poverty level, contrast to the poverty level on the rural level which is always above the national poverty level. Thus, the proportion of national poverty figures is more contributed by the population at the rural level compared to the urban level. Furthermore, the characteristics of poverty in urban and rural levels are different. Thus, the government should take distinguished policy.

Figure 1.0: Percentage of Poverty in Indonesia 2007-2018



	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Urban	12.52	11.65	10.72	9.87	9.23	8.60	8.52	8.16	8.22	7.73	7.26	6.89
Rural	20.37	18.93	17.35	16.56	15.72	14.70	14.42	13.76	14.09	13.96	13.47	13.1
Urban and Rural	16.58	15.42	14.15	13.33	12.49	11.66	11.47	10.96	11.13	10.70	10.12	9.66

Urban Rural Urban and Rural

Source: Central Bureau of Statistics (2019).

The issue of poverty is not only measured by the amount of income. Instead, poverty is also a condition where poor people are deprived of their basic abilities (Suzuki, Pramono, and Rufidah, 2016). Furthermore, by looking at the poverty level which is dominated by rural communities, poverty is a challenge for the government to find a proper solution. One of the basic capabilities of rural communities is the availability of natural resources for their daily needs. In relation to education, many rural communities are not highly educated. Moreover, many of them also find it difficult to access health facilities and very rarely among them are covered by social security. Poverty in rural areas is more about the ability to manage natural resources without any added value so that products sold have low value. In contrast, the low level of education makes them stand without the capacity to wrap their products to be more attractive due to their low marketing ability.

One of fundamental problems relating to poverty in rural areas is capital constraint. Capital constraint is a major problem for rural communities to develop their products. The products are basically part of the concept of micro, small, and medium enterprises or MSMEs. They exist in rural areas in informal forms. MSMEs are the backbone of the community's economy, especially at the lower level. Nevertheless, the contribution of MSMEs in absorbing workers is better than that of large industries (Irjayanti and Azis, 2012).

In addition, Irjayanti and Mulyono (2012) also explained that MSMEs are stronger against the impact of the global crisis because its main capital comes from the owner itself and that makes the capital scale of MSMEs limited. Poverty is also related to a condition of deprivation the poor from basic abilities. This can be seen especially from the aspects of education, health, and social security that start from the low economy. In overcoming such situation, capital injection from banking institutions is one of the main strategies that the government can do to alleviate poverty through working capital for MSMEs.

A financing bank is an institution that has the ability to provide working capital injection for MSMEs. Conventional banks seem to prefer to inject loans to large companies due to greater interest margins that they can gain if the given loans are also large. This is where the *Rahmatan Lil 'Alamin* role of Islamic banks through Islamic microfinance comes to apply. Here, *Rahmatan Lil 'Alamin* means the mercy for the universe. In reaching financial inclusion, poverty alleviation programs should consider Islamic microfinance through Islamic banks as institutions that can play an important role in empowering them. This is essential, especially when conventional financial institutions have not reached the poor.

Many studies revealed that microfinance institutions have a positive impact in combating poverty, especially in increasing income and reducing the vulnerability of the poor (Masyita and Ahmed, 2013). The profit-sharing scheme in Islamic banks is considered more appropriate, especially due to the limited capacity of MSMEs working capital. In addition, Islamic banks are more sensitive with a sense of belonging from MSMEs. This is by looking at the running of MSMEs business activities and the profit/loss of MSMEs that will also affect the profit-sharing received by Islamic banks.

The working capital injection through MSMEs is expected to provide good results on the issue of poverty alleviation. The multiplier effect that may result from alleviating the rural poor will also contribute to the opening of employment, increasing economic growth, and the application of the concept no one-left behind in the economic development. Thus, it is expected that SDGs' indicators, especially SDG1 i.e. no poverty is possible to be achieved more deeply to the community urban poor and also touches the acute poverty itself, especially among rural communities.

2. Literature Review

Microfinance institutions are projected as institutions that provide financial services for the poor, especially in efforts to alleviate poverty. Therefore, a study of the role of microfinance in alleviating poverty becomes an interesting topic. Such research is mostly carried out by experts by using both micro and macro data. Khandker (2005) examined the role of microfinance in poverty in Bangladesh, a country that becomes the pioneer of the development of microfinance by using the micro-level data. The results of the study show that the access to microfinance has a significant impact on household welfare in terms of increases in consumption levels. It is interesting that the impact of access to microfinance is not only enjoyed by borrowers but also has a spill-over effect on the surrounding environment. Besides that, microfinance is also able to reduce the rural poverty average.

Furthermore, Imai, Arun and Annim (2010) analyzed the impact of microfinance access towards households on poverty reduction. They used the data of Indian household level in 2001. The results show that the access to microfinance had a significant effect on reducing household poverty. Interestingly, the access to microfinance for productive purposes has more impacts on reducing poverty in rural areas compared to loans accessed by urban communities. In addition to the research based on micro data as given above, several studies are also done by using macro data. Imai, Gaiha and Thapa (2012) analyzed the impact of access to microfinance on poverty by using macro data i.e. by using the cross-sectional data of 48 developing countries. The results show that micro-per capita financial loans affect poverty negatively, and countries with high microfinance loan portfolios tend to have low poverty rates. The results of this study also emphasize that microfinance is able to reduce the depth and severity of poverty. This is indicated by the estimated results that are consistent with each poverty indicator used, headcount ratio, poverty gap, and squared poverty gap.

However, the share of credit to Gross Domestic Product (GDP) also has a significant effect on reducing poverty. Miled and Rejeb (2015) analyzed the effect of microfinance on poverty at the macro level by using data from 57 developing countries. The results show that countries with high gross loan portfolio per capita tend to have low poverty headcount ratio. Furthermore, Donou-Adonsou and Sylwester (2016) analyzed the effect of credit on poverty, with a sample of 71 developing countries during the period of 2002 to 2011. The results of the study show that the credit provided by banks has a negative and significant effect on poverty. Increasing bank loans by 10 percent can reduce poverty by 6.5 to 6.9 percent on the headcount ratio, and 5.5 to 5.9 percent when using the poverty gap measure.

In another research, there is no significant effect when the measurement for poverty used is based on the squared poverty gap. Rewilak (2017) analyzed the role of banks in reducing poverty by adding physical indicators such as number of banks and Automatic Teller Machines (ATMs) in certain regions. The results show that financial (credit) was deepening and physical financial access has an impact on reducing poverty. A quite interesting finding was that the financial deepening has a greater impact on reducing poverty. This indicates that access to loans made by the poor is surely far more impactful than the availability of physical access. Although, the existence and completeness of physical facilities also cannot be ignored.

Researches that are related to Islamic microfinance in Indonesia were carried out in versatile manner. Adnan and Ajiji (2015) focused on the role of the *Baitul Maal wat Tamwil* (BMT) in reducing poverty in one BMT in East Java. The results of the study indicate that the financing carried out by BMTs is effective in reducing poverty. Most respondents who have access to financing for productive business activities tend to experience an increase in income. In another research, Rijawanti and Asutay (2015) investigated the role of BMTs and BPRS in East Java involving 348 respondents. The results of their research show that the financing carried out by BPRS helps to reduce poverty, by reducing the percentage of poor customers from 35.5 percent to 23.1 percent after accessing financing. In addition, a more detailed research was conducted by Fianto, Gan and Roudaki (2018) where they analyzed the effects of Islamic microfinance on the welfare of rural households with the Double Difference in Difference method. This study was a survey-based research involving 548 respondents during November 2014 to February 2015 in East Java. The results show that the households that accessed the equity financing contracts experienced higher income increases compared to respondents who accessed debt-based financing. This study also confirms some of the previous findings that Islamic microfinance has a significant effect in reducing poverty, and in this case, it is indicated by the increase of income.

These studies show that micro-financial institutions play an important role in reducing poverty levels, at both micro and macro levels. Although, findings at the international level in the case of Indonesia tend to look from a conventional financial institution's perspective, there is strong evidence that Islamic microfinance has a significant effect on poverty alleviation. On the contrary, the development of Islamic banks such as Sharia People's Financing Banking (BPRS) in Indonesia is quite rapid. Thus, if it can be more optimized throughout Indonesia, it has a great potential in helping to reduce poverty.

BPRS is one form of Islamic Rural Banks that has more ability to reach small communities, especially in rural areas. Furthermore, the issue of poverty which is predominantly dominated by rural communities is an important capital for BPRS in implementing Islamic "Rural" Banks. By having so, all community groups can be reached by formal financial institutions while emphasizing on the concept of no one-left behind in implementing SDGs. This can also significantly contribute to SDG1 i.e. no poverty.

Some studies that focus on Islamic microfinance show and support for the importance of alleviating poverty fairly, especially financing through productive activities. Arguably, conventional microcredit programs do not reduce poverty effectively because borrowers remain in the cycle of interest-based debt that can exacerbate their financial burdens. Meanwhile, Islamic microfinance financing has an equity-based financing structure that considered a fair loan-lender agreement. This promotes an effective wealth redistribution mechanism to reach the poor, and to encourage their participation in the real economic productive sector. This not only reduces poverty, but also increases living standards (Abdul Manap, Siththi, Long, & Muneeza, 2017).

Furthermore, Riwajanti (2013) explained that Islamic microfinance has unique features compared to conventional ones. The underlying principle of Islamic microfinance depends on the application of Islamic values to promote social justice for all and to achieve economic development by building human capacity as the centre of attention. Therefore, the contents of the moral and value aspects, emphasizing on the human side and community responsibility tend to be more effective and comprehensive in alleviating poverty.

However, the poverty alleviation does not come by itself when Islamic bank provides assistance through Islamic microfinance financing. Productive cooperation is needed, especially between Islamic banks as providers of Islamic microfinance financing to productive partners such as MSMEs. Interestingly, based on the findings of Rokhman (2016), Islamic microfinance has an important role in increasing income levels, customers' children' education, and business progress.

Nonetheless, this study did not find a significant role for microfinance in access to healthcare. Another interesting finding is that Islamic microfinance plays an important role in improving living standards, per capita income, awareness level (education level), ethical values, profitability, sustainability, infrastructure position, level of employment in society, helping to control inflation, and distribution of uneven wealth (Aslam, 2014). This is allegedly happened because people are more interested in their religious perspectives such as on the prohibition of usury in Islam and Christian. Thus, there must be a regulation from an appropriate authority to control it in order to obtain useful results through a model that can be applied.

Both conventional and Islamic financing make a real contribution towards poverty alleviation. Nevertheless, there are fundamental differences between these two types of financing. Islamic microfinance provides financing that is more humane to their customers and not solely seeking for profits because Islamic microfinance is based on the principles that derived from Al-Qur'an and Sunnah in carrying out its activities.

3. Research Methodology

In this study, the researchers use (i) the provincial level poverty data in Indonesia as obtained from the Central Bureau of Statistics (BPS) and (ii) financing data as carried out by the Sharia People's Financing Bank (BPRS) from the Financial Services Authority (OJK) from the period of 2014 to 2018. Earlier researches as done in Indonesia have analyzed the impact of Islamic microfinance at the micro level, meanwhile researches that used macro data are still scarce. Adding to those researches, this study attempts to analyze the influence of Islamic microfinance on poverty level in Indonesia by using macro data.

The purpose of this study is to analyze the effect of financing carried out by BPRS as part of Islamic microfinance institutions against poverty level in Indonesia. In doing so, this study uses financing variables based on the purpose of allocation of use such as working capital, investment, and consumption. Additionally, for sake of viewing the consistency of results, this study uses two poverty indicators, namely (i) poverty severity index, and (ii) poverty gap index. Fixed-Effects and Random Effects are used as the estimation model to further analyze the consistency of the model built. Thus, the estimation is carried out using two poverty indicators in each Fixed-Random model. The Random-effects model assumes that the unobserved effect μ_i is not correlated with each explanatory variable. Meanwhile, the Fixed-effects model assumes that μ_i correlates with explanatory variables (Wooldridge, 2009). Therefore, the estimation results obtained from the random-effects model tend to be efficient, but the fixed-effects results are more consistent. The basic equations are as follows:

$$\text{LnDepth\_poor}_{it} = \alpha_0 + \beta_1 \text{LnWork\_capt}_{it} + \beta_2 \text{LnInvestment}_{it} + \beta_3 \text{LnConsumption}_{it} + \mu_i + \varepsilon_{it} \quad (1)$$

$$\text{LnCond\_Poor}_{it} = \alpha_0 + \beta_1 \text{LnWork\_capt}_{it} + \beta_2 \text{LnInvestment}_{it} + \beta_3 \text{LnConsumption}_{it} + \mu_i + \varepsilon_{it} \quad (2)$$

Table 1.0: Descriptive Statistics

Variable	Obs	Mean	Std. Dev	Min	Max
Pov_Gap	160	58.65625	34.55067	1	122
Pov_Severity	160	33.26875	21.36232	1	80
Work_Capt	113	56.17699	31.89078	1	111
Investment	97	47.36082	26.27387	1	92
Consumption	112	56.35714	32.06802	2	112

Source: Authors' own calculation

Figure 2.0 provides a descriptive explanation of the variables used. This study uses three independent variables, namely (i) Work_Capt which is the usage allocation purpose of BPRS in the working capital sector; (ii) Investment which is the usage allocation purpose of BPRS in the investment sector; and (iii) Consumption which is the usage allocation purpose of BPRS in the consumption sector, while Pov_Gap is the poverty gap index explaining a measure of the average expenditure gap of each poor person to the poverty line, and Pov_Severity is the poverty severity index revealing a measurement of the distribution of expenditure among the poor.

The usage allocation purpose of BPRS is allocated to be used by productive partners in the micro sector, namely the community and MSMEs. According to UNDP (2014), financial and banking allocations that are part of Islamic investment will strongly support the strategic goals of one of them to improve poverty. Therefore, the authors use three pre-existing independent variables which are Islamic BPRS financing based on usage.

4. Limitation of Research

This research is limited by several constraints particularly the variables. Poverty alleviation is influenced by many factors. Yet, this research focuses on *Shari'ah*-based financing variables, especially from *Shari'ah*-based instruments. Thus, the researchers consider that it is suitable to use capital working, investment, and consumption as proxies for Islamic microfinance that stands as one of Islamic financing products.

5. Results and Discussion

This section elaborates the results and provides the discussion of the results as found by the researchers in this study.

5.1 Results

Table 2.0: Estimation Results using Random and Fixed Effects

Variable	(1) **model 1 (fe)**	(2) **model 2 (re)**	(3) **model 3 (fe)**	(4) **model 4 (re)**
Dependent variable	**Pov_Gap**	**Pov_Gap**	**Pov_Severity**	**Pov_Severity**
Work_Capt	-5.397***	-5.328***	-6.313***	-6.191***
	(1.692)	(1.631)	(2.146)	(2.093)
Investment	0.740	0.649	0.711	0.666
	(1.870)	(1.802)	(2.372)	(2.312)
Consumption	-1.023	-0.713	-2.211	-1.904
	(1.703)	(1.632)	(2.160)	(2.100)
Constant	51.94***	49.87***	84.53***	80.87***
	(11.38)	(11.58)	(14.44)	(15.75)
Observations	79	79	79	79
R-squared	0.156		0.144	
Number of id	20	20	20	20

Note: Standard errors in parentheses, *** p<0.01, ** p<0.05, * p<0.1
Source: Authors' own calculation

Table 2.0 reveals the results of the four models described earlier in the research methodology section. Models 1 and 2 analyze the effect of capital working, investment, and consumption on the poverty severity index; while models 3 and 4 are based on the poverty gap index. The model in the panel estimation depends on the researchers' assumptions whether it is fixed effect or random effect (Wooldridge, 2012). Meanwhile according to Hausman, it is necessary to test the differences in the coefficient that is systematic in the research.

Based on Wooldridge (2012), the research can use the assumption whether fixed effect or random effect. The researchers used the fixed effect assumption because this model is assumed as being consistent over time even though there is a correlation between explanatory variables and unobserved heterogeneity. The results of fixed effects in both model 1 and 3 show that there is only one variable that has a significant negative effect on the poverty rate (Pov_Gap and Pov_Severity), namely the BPRS working capital. By increasing the BPRS working capital, it will reduce the poverty gap index -5.382 percent (model 2) and -6.191 percent poverty severity index (model 3).

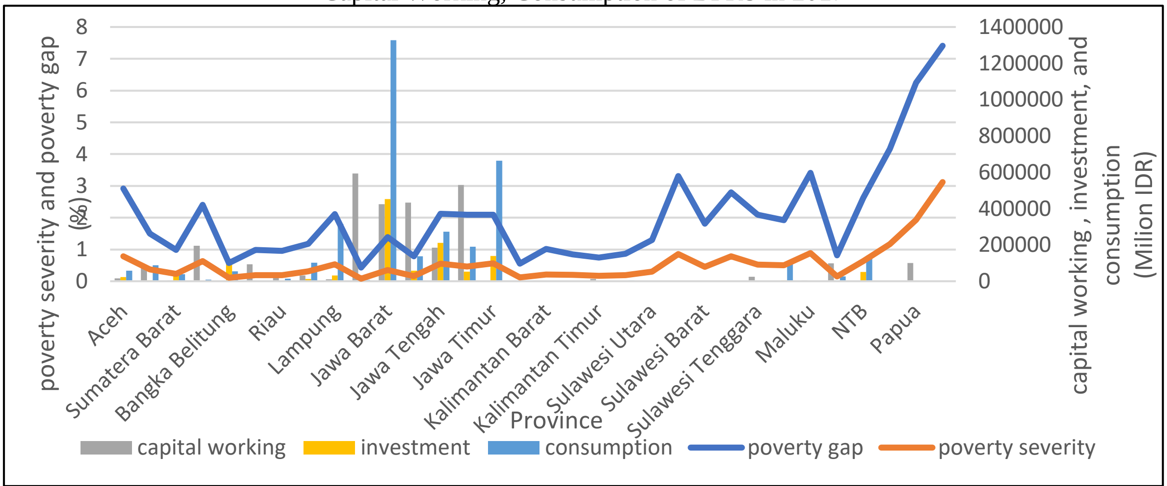
According to Gujarati (2004), by analyzing without assumptions, a good model can use a Hausman test. Based on the Hausman test, the feasible model is a random effect because the prob-Chi value is greater than the Alpha which is equal to 0.9279 (models 1 and 2) and 0.9377 (models 3 and 4). The random model shows the efficiency of a model but it is not consistent. The results are in line with the researchers' assumption by using the fixed effect. It shows that only the BPRS working capital has a significant negative effect on poverty (Pov_Gap and Pov_Severity). The increase in BPRS working capital will reduce the poverty severity index by -5.397 percent (model 1) and -6.313 percent of poverty depth index (model 4). However, the value of R-squared showed a small variation in the overall effect of financing. This is not under the researchers' attention. However, it is not surprising since the researchers analyzed only from around 6 percent from the market share of Islamic banking in Indonesia. In addition, the value of financing carried out by BPRS is much smaller when compared to other banks in general.

The allocation of BPRS funding is directed to reach people who are in need of funding within a micro value. In this case, BPRS is often referred to as rural Islamic banks in the international literature. However, if Islamic banking is able to grow consistently, it is possible that the size of the market share will have a better impact on poverty alleviation. On the other hand, the low variation in the overall effect of financing on poverty variation shows that it is also suspected that there are variations in very important macro variables that can influence poverty. However, they are not included in the model.

5.2 Discussion

This sub-section explains the results of the research on how the impact of Islamic banking in the implementation of Islamic microfinance affects poverty alleviation. Figure 2.0 shows the financing of BPRS based on Type of Usage (capital working, investment, and consumption) and poverty rates based on the poverty severity index and poverty gap index in Indonesia in 2017.

Figure 2.0: Poverty Gap Index, Poverty Severity Index and Investment, Capital Working, Consumption of BPRS in 2017



Source: Central Bureau of Statistics (2019).

In Figure 2.0, it can be seen that the poverty rate on the islands of Sulawesi and Papua is higher than other regions in Indonesia. Sumatra and Java Islands have a relatively low poverty rate in comparison to Sulawesi, while Kalimantan has the lowest poverty rate. When compared to the level of financing from *Shari'ah*-based financing on types of usage (capital working, investment, and consumption) and poverty levels; at a glance, provinces in Sumatra have more total funding than provinces in Maluku and Irian Islands. Sumatra has lower poverty rate compared to Maluku and Irian Islands. So, this area is in accordance with Riwajanti (2013) finding that Islamic microfinance is able to reduce poverty.

In contrast, Lampung and the Java Island show a high level of financing along with the high level of poverty. Thus, this is an interesting situation to consider, especially on how the relationship between *Shari'ah*-based financing and Islamic microfinance is actually related to poverty reduction.

The results of the study show that the financing used for the working capital has the ability to reduce the unemployment rate. This is in line with the finding made by Imai, Arun and Annim (2010) where they analyze the impact of microfinance access by households on reducing poverty. The results show that the access to microfinance has a significant effect on reducing household poverty.

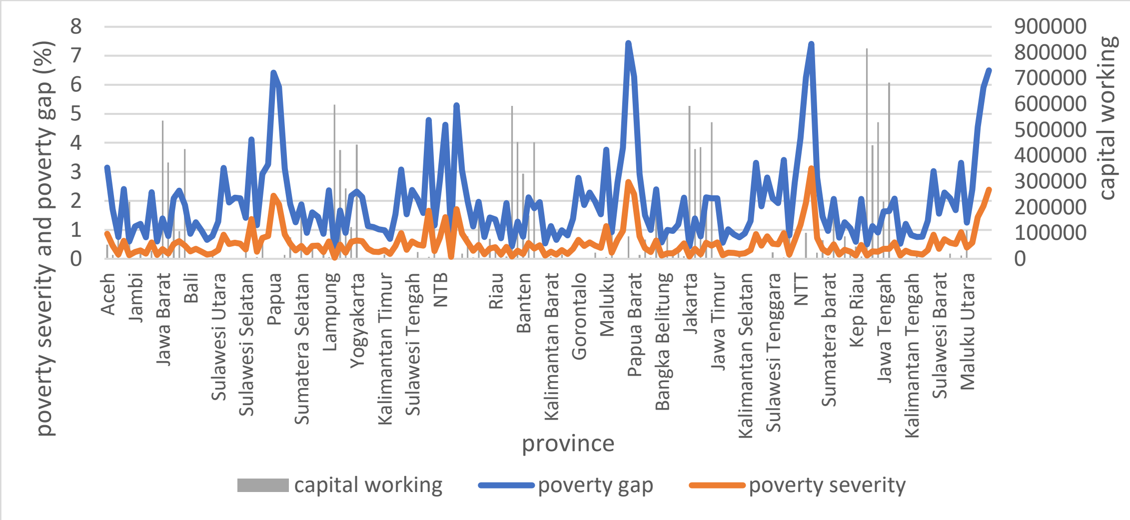
In addition, Imai, Gaiha and Thapa (2012) proved the same situation that micro-per capita financial loans significantly influence poverty. Moreover, countries with high microfinance loan portfolios tend to have low poverty rates and this is based on samples from forty-eight (48) developing countries. The results of this study also emphasize that microfinance is able to reduce the depth and severity of poverty. This is indicated by the estimated results that are consistent in each indicators of poverty.

Furthermore, Sabiti and Effendi (2017) found that investment can reduce poverty. The indicator used by Sabiti and Effendi (2017) is Islamic microfinance in Bogor Regency which was done through 90 respondents. The results of the study show a negative and significant effect on poverty. This result is also in line with the research done by Dhaoui (2018) in Bangladesh, where Islamic microfinance has a positive impact on poverty reduction as shown by empirical studies, especially in rural areas. Various loan programs have an important role in reducing poverty, except those in the environment with sufficient materials and social capital to achieve the program's objectives. Islamic microfinance carried out by BPRS has gained a recognition as an important strategy to fight poverty. This indicates that BPRS is ready to serve a larger targeted population of poor individuals.

Onakoya and Babatunde (2014) also proved through their research that the ideology of Islamic microfinance institutions has the potential to have a comparative advantage because Muslims want to carry out economic activities according to their religion which can reduce poverty and sustain economic development. This is based on 80 percent of the population of Nigerian Muslims. Onakoya and Babatunde (2014) revealed that religion is not an inhibiting factor for the application of Islamic microfinance.

Additionally, Wajdi Dusuki (2008) revealed that one of the efforts to reduce poverty was BPRS by providing financing to the rural poor with a Special Purpose Vehicle (SPV) model. The program offered a variety of different financing according to the needs of partners. It also protected Islamic banks without damaging the institutional feasibility, competitiveness and sustainability of the company.

Figure 3.0: Poverty Gap Index, Poverty Severity Index and Capital Working of BPRS in Indonesia during 2014-2018



Source: Central Bureau of Statistics (2019).

The capital working from BPRS in all provinces of Indonesia becomes a matter that needs to be considered more seriously since it can reduce poverty. Figure 3 shows how high financing in the working capital can reduce poverty. It supports *Shari'ah*-based economy by the government which is a very meaningful achievement in the economy. Moreover, Indonesia is a population with the largest Muslim population in the world that this country is very likely to become an Islamic economic leader in the world.

According to Litriani (2017), the financing in the capital working affects positively the customer's business income. This means that the higher the working capital provided by the BPRS, the higher the business income of the customer. Per capita income will increase and it will be able to reduce the level of poverty. Such simulative injections will have a long-term, sustainable benefits, and impacts as compare to financial assistance in cash to poor households that stand without any encouragement to make good financial turn-around efforts.

Islamic microfinance, which is one of the core activities of BPRS, has a mission to contribute to sustainable developments. Poverty alleviation becomes their priority concern and consistent with SDG1 i.e. no poverty. By encouraging an increase in the working capital to their productive partners also means to encourage government's programs in poverty alleviation. Simultaneously, it is in line with the global target of eliminating poverty in the world. However, all this can only be achieved through good cooperation by many players, especially stakeholders.

6. Conclusion

Basically, the financing allocation from Islamic banks for *Shari'ah*-based financing is not as big as conventional banks in general. Moreover, their financing services are relatively smaller in value than other conventional banks. Therefore, *Shari'ah*-based financing is considered closer to the lower and middle classes of the society. It is referred by locals as the rural bank. Nevertheless, Islamic microfinance carried out by Islamic banks is able to contribute to great efforts to reduce poverty. In this study, strong evidence was found that the funding allocation carried out specifically by BPRS for capital working activities had a negative and significant effect on the poverty level.

In other words, the higher the BPRS allocates funding for the business capital, the lower the poverty rate will decline. This study certainly confirms several previous findings, especially in Indonesia. However, Islamic banking's share is still lower than conventional banking. Nevertheless, it still has a contribution in implementing the concept of inclusiveness for sake of achieving SDGs through poverty alleviation. It is hoped that Islamic financing will play an extremely important role in the future. Even though *Shari'ah*-based financing is relatively lower, it still contributes to reduce poverty. It can be said that when the share of *Shari'ah*-based financing is greater, poverty can be alleviated deeper across society by using instruments from *Shari'ah*-based financing. The researchers also encourage future researches to use more variables in analyzing factors that influence poverty alleviation, particularly those that are related to *Shari'ah*-based financing perspective.

References

Adnan, M. A., & Ajiji, S. R. (2015). The Effectiveness of Baitul Maal wat Tamwil in Reducing Poverty: The Case of Indonesian Islamic Microfinance Institution. *Humanomics*, 31(2), 160-182.

Aslam, M. N. (2014). Role of Islamic Microfinance in Poverty Alleviation in Pakistan: An Empirical Approach. *International Journal on Academic Research in Accounting, Finance, and Management Sciences*, *4*(4), 143–152.

Babatunde, A., & Olasunkanm, A. (2014). Alternative Financial Inclusion Strategy: Islamic Expectations From Ogun Sub National Government, Nigeria. *Singaporean Journal of Business Economics and Management Studies*, *2*(11), 169 180.

Dhaoui, I. (2018). The Role of Islamic Microfinance in Poverty Alleviation: Lessons from Bangladesh Experience. *Munich Personal RePEc Archive*, (87358).

Dusuki, A. W. (2008). Banking for the Poor: The Role of Islamic Banking in Microfinance Initiatives. *Humanomics*, *24*(1),

Donou-Adonsou, F., Sylwester, K. (2016). Financial Development and Poverty Reduction in Developing Countries: New Evidence from Banks and Microfinance Institutions. *Review of Development Finance*, 6, 82-90.

Fianto, B. A., Gan, C., Roudaki, J. (2018). Equity Financing and Debt-Based Financing: Evidence from Islamic Microfinance Institutions in Indonesia. *Pacific-Basin Finance Journal*, 52, 163-172.

Gujarati, D., & Porter Dawn, C. (2008). *Basic Econometrics.* Fifth edition. New York: McGraw-Hill International Edition.

Hanna, S., Manap, A., Siththi, F., & Long, S. (2017). Poverty Alleviation via Microfinance using the Concept of Mudharabah. *International Journal of Management and Applied Research*, *4*(3).

Imai, K. S., Arun, T., Annim, S. K. (2010). Microfinance and Household Poverty Reduction: New Evidence from India. *World Development*, 38(12), 1760-1774.

Imai, K. S., Gaiha, R., Thapa, G., & Annim, S. K. (2012) Microfinance and Poverty - A Macro Perspective. *World Development*. 40(8), 1675-1689.

Irjayanti, M., & Mulyono, A. (2012). Barrier Factors and Potential Solutions for Indonesian SMEs. *Procedia Economics and Finance*, *4*(Icsmed), 3–12.

Khandker, S. R. (2005). Microfinance and Poverty: Evidence Using Panel Data from Bangladesh. *The World Bank Economic Review*, 19(2), 263-286.

Litriani, E., & Leviana, L. (2017). Pengaruh Pembiayaan Modal Kerja Terhadap Pendapatan Usaha Nasabah Pada PT. Bank Syariah Mandiri Kantor Cabang Simpang Patal Palembang. *I-Finance*, *3*(2), 123–140.

Masyita, D., & Ahmed, H. (2013). Why is Growth of Islamic Microfinance Lower than its Conventional Counterparts in Indonesia? *Islamic Economic Studies*, *21*(1), 35–62.

Miled, K. B. H., Rejeb, J. E. B. (2015). Microfinance and Poverty Reduction: A Review and Synthesis of Empirical Evidence. *Proceedia-Social and Behavioral Sciences*, 195, 705-712.

Onakoya & Babatunde, A. (2014). Alternative Financial Inclusion Strategy : Islamic Expectations from OGun Sub-National Government, *2*(11), 169–180.

Rewilak, J. (2017). The Role of Financial Development in Poverty Reduction. *Review of Development Finance*, 7,169-176.

Rijawanti, N. I., Asutay, M. (2015). The Role of Islamic Microfinance Institutions in Economic Development in Indonesia: A Comparative Analytical Empirical Study on Pre- and Post-Financing States.

In H A El-Karanshawy et al. (Eds), Access to Finance and Human Development. Essays on *Zakah*, *Awqaf*, and Microfinance. Doha, Qatar: Bloomsbury Qatar Foundation.

Riwajanti, N. I. (2013). Islamic Microfinance as an Alternative for Poverty Alleviation: A Survey. *Afro Eurasian Studies*, *2*, 254–271.

Rokhman, W. (2016). The Effect of Islamic Microfinance on Poverty Alleviation: Study in Indonesia. *Economic Review*, *XI*(2).

Sabiti, M. B., & Effendi, J. (2017). Islamic Micro Finance and Its Impact on Poverty Reduction of Two Village Models in Bogor, Indonesia. *Signifikan: Jurnal Ilmu Ekonomi*, *6*(1), 87–102.

Sirageldin, I. (2000). Elimination of Poverty: Challenges and Islamic Strategies. *Islamic Economic Studies*, *8*(1), 1–16.

Suzuki, Y., Pramono, S., & Rufidah. (2016). Islamic Microfinance and Poverty Alleviation Program: Preliminary Research from Indonesia. *SHARE*, *5*.

Wajdi Dusuki, A. (2008). Banking for the poor: The Role of Islamic Banking in Microfinance Initiatives. *Humanomics*, *24*(1), 49–66.

Wooldridge, J. M. (2009). *Introductory Econometrics*: A Modern Approach. USA: South–Western Cengage Learning.

Wooldridge, Jefry M. 2013. Introductory Econometics: A Modern Approach. 5th Edition. Amerika Serikat: South-Western Cencage Learning.

Central Bureau of Statistics. (2019). Persentase Penduduk Miskin Menurut Provinsi 2007-2019. Retrieved from https://www.bps.go.id/dynamictable/2016/08/18/1219/ persentase-penduduk-miskin-menurut-provinsi-2007---2019.html

Otoritas Jasa Keuangan. (2019). Official Website. Retrieved from https://ojk.go.id/id/ Default.aspx