Chapter 9

Islamic Financial Inclusion: An Alternative Approach to Reach the Unbanked of Bangladesh

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ABSTRACT

Financial Inclusion (FI), a global concern of this decade, has been accepted by development agencies, governments, and policymakers as one of the pre-eminent ways to eradicate worldwide poverty and income inequality. Consequently, authorities are looking for possible ways to include the unbanked in formal financial chain. Islamic finance, specifically Islamic banking, with its welfare-oriented principles and unique products, has been able to capture the attention of policy makers. Moreover, a major portion of the Muslim population still exclude themselves from the formal financial chain due to religious prohibition of interest-based transactions for whom Islamic finance is the only way to inclusion. Bangladesh, one of the major Muslim countries in the world, is still to bring one-fourth of its total population under formal financial chain. At this backdrop, this chapter examines the empirical contribution of Islamic banking sector in financial inclusion condition as well as development scenario of Bangladesh.

INTRODUCTION

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Moreover, a major portion of Muslim population still excludes themselves from the formal financial chain due to religious prohibition of interest-based transactions for whom Islamic finance is the only way to inclusion. Bangladesh, one of the major Muslim inhabited country in the world, is still to bring one-fourth of its total population under formal financial chain. Despite a significant number of studies are conducted focusing on alternative FI mechanism, very few of them addressing Shari’ah mechanism from individual country perspective.

Starting from the early eighties, Islamic banking in Bangladesh has been able to capture one-fourth of the banking share of the country within a few decades and offers every potential to grow beyond that. At these circumstances, this chapter endeavors to examine the empirical contribution of Islamic banking sector in FI condition as well as development scenario of Bangladesh.

The current study employs four dependent variables and seven independent features to examine the extent of Islamic FI on development as well as inclusion. The dependent variables are the GDP Growth Rate (GDP_grt), Financial Development Index (FDI), Savings (% of GDP) and Consumption Growth (Cons_Grt). Then, seven independent features are Consumer Price Index (CPI), amount of deposits, amount of investment, number of branches, number of (Automated Teller Machines) ATMs, amount of Waqf (Charitable endowment) deposits and amount of Qard (Welfare loan) investment. The datasets span over 2009 to 2017 covering six full-fledged Islamic banks in Bangladesh. Nevertheless, employing fixed effects panel regression, the datasets are regressed applying both fixed and variable independent set to capture the contribution of Islamic FI on various development indicators as well as on inclusion condition.

Unlike the existing studies on FI, this chapter establishes Islamic FI as potential channel for inclusion in developing economies with majority of Muslim habitats. The study has practical implications to policymakers, development agencies and Islamic banking authorities in both Muslim and non-Muslim countries in introducing a viable FI mechanism directed to sustainable development of the targeted unbanked populace. Moreover, the study particularly addresses the case of Islamic FI situation of Bangladesh which can be of great use in reducing the access gap and obstacles in Islamic FI.

BACKGROUND

FI can be defined as the process of extending minimum financial services (deposit, low cost credit, fund transfer and insurance) to the unbanked at an affordable cost and within formal financial system. As a high policy priority concern of the current century and enabler of seven of sustainable development goals, academicians, practitioners, and policymakers are showing growing interest in FI in recent decades. After recognition as a political issue in the UK in 1997, FI has come into discussion in different meetings like G20 Summit 2010 where FI action plan was endorsed followed by formation of Global Partnership for FI (Kabakova & Plaksenkov, 2018). Moreover, the United Nations Development Program (UNDP) has launched several projects with different banks to design suitable plans for FI of the underserved from 2009. However, in most of the cases, initiatives for FI are not self-initiated rather undertaken to fulfill regulatory compliance imposed by public entities or lead by development agencies and civil activist agency through the establishment of non-government organizations (NGOs), microfinance institutions (MFIs), and co-operatives. In spite of the growing concern and collective efforts, the worldwide formal
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