



## The Moderating Effects of Financial Inclusion on Qardhul Hassan Financing Acceptance in Nigeria: A Proposed Framework

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### ABSTRACT

This paper, which is conceptual in nature, discusses the moderating effects of the relationship between several factors that may affect the acceptance of Qardhul Hassan financing (QHF) in Nigeria. The proposed variables under examination are attitude towards QHF, knowledge of QHF, perceived benefits, perceived government support and religious obligations while financial inclusion serves as a moderator variable. If validated, the work would be used as a proposed financing model to the government, policy makers, regulators, practitioners and other stakeholder's *vis-à-vis* curbing the adverse effects of financial exclusion in various jurisdictions of the emerging markets.

**Keywords:** Qardhul Hassan, Financial Inclusion, Islamic Finance

**JEL Classifications:** D14, G21

### 1. INTRODUCTION

Islamic finance offers alternative solutions to conventional finance that comply with the principles of Islamic jurisprudence (Shari'ah). Shari'ah strives to promote moral and ethical values in establishing an economic system that prohibits the payments and receipts of interest (*ribah*), excessive uncertainty (*gharrar*) in business transactions and investment in prohibited industries (Aliyu, 2012). Although introduction of Islamic finance has significantly played an essential role in enhancing financial inclusion, available literature showed that about 2.7 billion people (70% of the adult population) in emerging markets such as Nigeria still have no access to basic financial services, and a significant part of the them come from countries with predominantly Muslim population (Iqbal, 2014; Mohseni-Cheraghloou et al., 2012). According to Iqbal (2014), only 24% of the world Muslims are financially included against their non-Muslims counterpart with 44%. The former had only 14% in Sub-Saharan Africa against the latter with 28%. Despite several reforms aimed at enhancing financial inclusion including the introduction of Islamic banking in Nigeria in 2011, the exclusion level was still high, and there was still no significant improvement between 2013 and 2014 in

which the exclusion rate was 39.7% and 39.5% respectively. Central Bank of Nigeria (CBN) planned to reduce this exclusion rate to 20% by the year 2020 as contained in its National Financial Inclusion Strategy - NFIS (CBN, 2012; EFINA, 2014; Sanusi, 2012). Even though the users of Islamic financial products in Nigeria were 74.7% very satisfied with the services, the level of awareness was very low as only 8.5% were familiar with the Islamic banking products such as Qardhul Hassan and only 0.3% uses (EFInA, 2014).

Prior researchers provided evidences on the studies conducted on the acceptance of Islamic financial products such as Qardhul Hassan in the emerging markets such as Malaysia (Amin et al., 2010; Mansori et al., 2015), Iran (Mojtahed and Hassanzadeh, 2009), Libya (Bardai, 2013), Bangladesh (Haneef et al., 2015; IFSB, 2014; Khan et al., 2007) and Indonesia (Febianto and Ashany, 2012; Yumna and Clarke, 2013). Moreover, in the developed countries, similar studies were conducted such as in Australia (Sain et al., 2013) and UK (Warsame, 2009).

These countries have different business, cultural and economic environment from Nigeria (Marcellus, 2009; National Commission

Planning, 2010). Therefore, it is imperative to conduct a similar study in a different context and country like Nigeria that is an emerging market with a newly introduced Islamic banking and its products in 2011. The previous study conducted showed a positive relationship between attitude towards Qardhul Hassan financing (QHF) (Abd Rahman et al., 2015; Amin et al., 2010; Amin et al., 2011; Jaffar and Musa, 2014), knowledge of QHF (Amin et al., 2014; Shahwan et al., 2007), perceived benefit (Amin, 2013), perceived government support (Amin et al., 2011) and religious obligation (Amin et al., 2014; Amin et al., 2011) on the intention to use Islamic financial services in various jurisdictions such as Malaysia, Indonesia, Iran, Bangladesh etc. It is equally noted that the researches on QHF were very scanty in the Sub-Saharan Africa particularly in Nigeria. Among the few related studies conducted in Nigeria was done by Ringim (2012) and was on the perception level of Nigerian Muslim account holders towards Islamic banking products. It is against this background that this paper adopted attitude towards QHF, knowledge of QHF, perceived benefit, perceived government support and religious obligation in the present study as independent variables to determine their relationship with the QHF acceptance in the Nigerian context. This is also in line with the recommendations by Amin et al. (2010) and Ringim (2012) on the need to improve the existing literature on the perception studies on the acceptance of Islamic financial services. To this end, this paper is divided into five sections with this introduction serving as the first section. Section two presents the literature review, and section three discusses the proposed variables. The fourth section presents the proposed theoretical framework and research methodology of the study and chapter five provides the conclusion and discussions of the paper.

## 2. LITERATURE REVIEW

### 2.1. Historical Evolution of Islamic Finance

The evolution of Islamic finance could be linked to the idea of reviving Islamic economic system and Islamic finance that was muted towards the end of colonial era among several Muslims countries. Some scholars were of the opinion that the modern Islamic finance may be traced to the Indian Muslims in the 1940s such as Abul Ala Mawdudi, Quraishi, and Sayyid Qutb in their books *Al-riba, Islam and the Theory of Interest*, and *Social Justice in Islam* respectively (Haniffa and Hudaib, 2010; Warde, 2000). Their work focus attention on developing economic activities that are acceptable and more compatible to Islamic Shari'ah in replacement of the interest based western-style of economic and banking system (Aliyu, 2012; Haniffa and Hudaib, 2010). Consequently, organizations such as Mit Ghamr savings and investment house and the Pilgrims Fund Corporation emerged in Egypt and Malaysia respectively. The establishment of Islamic Development Bank in 1973, equally rekindled the moment for Islamic banking in the world with the aim of fostering economic development and social progress of Muslim countries in accordance with the Islamic principles (Hussain et al., 2015; Ringim, 2012; Saeed, 2001). Islamic finance has recorded remarkable success in terms of size and the number of players in the past five decades. Starting with a handful of institutions and negligible amount of asset in 1970's, the Islamic financial asset grew up to US\$2 trillion in value and about 350 institutions globally by the end of 2014, at an average growth

rate of 16% annually since 2006 (Hussain et al., 2015). Despite this positive trend the market was still at infancy stage as it accounts for <1% of the world's financial assets (Askari et al., 2012; Gelbard et al., 2014; Kammer et al., 2015). Subsequently, other regulatory bodies such as Accounting and Auditing Organization for Islamic Financial Institutions, International Islamic Financial Market and International Islamic Liquidity Management Corporation Islamic Financial Services Board were set up for the smooth running of a global Islamic Finance (Mohammed et al., 2012; Obaidullah and Khan, 2010). Concentrated in Malaysia and Gulf Cooperation Council countries, Islamic finance has expanded throughout the Middle East, Indonesia, the United Kingdom, North Africa, and more recently, in some Sub-Saharan African countries such as Nigeria.

### 2.2. An Overview of Islamic Banking in Nigeria

The contentious implementation of Islamic Banking System and the growth of Islamic finance asset globally has attracted the attention of attracted the attention of Nigerian government policy makers and other stakeholders to implement the Islamic banking in Nigeria in 2011 (Ibrahim and Mustafa, 2011). This equally has to do with the Nigeria's overwhelming Muslim population that was more than 50% of the 177 million people (Aliyu, 2012) of the total population. The efforts to establish Islamic banking in Nigeria dates back to the 1990s when the idea was first mooted and subsequently, two licenses were granted in 1992. Unfortunately, none could commence operation until 1999 when the former Habib Nigeria Bank Limited (now Bank PHB) started an Islamic banking window (Daud, 2011; Dauda, 2013; Ibrahim and Mustafa, 2011). However, it is imperative to note that the promulgation of the Banks and Other Financial Institutions (OFI) Decrees 24 and 25 of 1991, beckoned a new dawn for banking operation in Nigeria (Aliyu, 2012; Dauda, 2013; Sanusi, 2011). This decree made new provisions for the establishment of non-interest banking in the country thereby leading CBN in 2010 to issue a guideline for the regulation and supervision of non-interest (Islamic) financial institutions (NIFI) that pave way for proper establishment of Islamic banking in Nigeria. This new banking model categorized non-interest banks as specialized banks which could be national non-interest bank with the capital base of N10 billion and shall operate in every state of the federation including the Federal Capital Territory. The second category is regional non-interest bank with capital base of N5 billion and shall operate in a minimum of 6 states and maximum of 12 contiguous states of the federation (Aliyu, 2012; Ibrahim and Mustafa, 2011). According to this guideline, a NIFI is defined as: "A bank or OFI under the purview of the CBN, which transacts banking business, engages in trading, investment and commercial activities, as well as the provision of financial products and services, are in accordance with Shari'ah principles and rules of Islamic commercial jurisprudence" (CBN, 2011). There were many permissible products under the Islamic banking system such as Murabahah, Salam, Istisna, Ijarah, Musharakah, Mudarabah, Sukuk, Qardhul Hassan, etc introduced in the Nigerian banking system.

### 2.3. Empirical Evidences on QHF

Qardhul Hassan refers to the loans that are free from any benefit or return to the lender and is more commonly known as interest-free

loan (Bhuiyan et al., 2012). Obaidullah and Khan (2010) refers Qardhul as zero-return loans that the Qur'an encourages Muslims to make available to the needy. Banks are allowed to charge borrowers a service fee to cover the administrative expenses of handling the loan. The fee should not be related to the loan amount or maturity. Furthermore, Qardhul Hassan to poverty approach means a beautiful loan. It is a loan granted by the lender without expectation of any return on the principal. The following verses from the holy Qur'an reveal the importance of this instrument:

- *Who is he that will loan to Allah a beautiful loan, which Allah will double unto his credit and multiply many times? It is Allah that giveth (you) Want or plenty, and to Him shall be you (Al-Quran Suratul Baqarah: 245).*
- *Verily, those who give sadaqa, men and women and lend to Allah a qardhul hassan, it shall be increased manifold (to their credit), and theirs shall be an honorable good reward (Al-Quran Suratul Hud, Verse No. 57).*
- *If you lend Allah a qardhul hassan, He will multiply it for you. Allah is the most appreciating, the most forbearing (Al-Quran Suratul Israel, Verse No. 64).*

Anas bn Malik reported that Allah's Messenger (PBUH) said:

*At night during which I was made to perform journey, I saw at the door of the Paradise written, "A sadaqa is equivalent to ten like that (in reward) while lending has eighteen times reward." I said, "O Gabriel, what is the reason that lending is more excellent than Sadaqa?" He said, "The beggar asks while he possesses it (money) while the one who demands loan does not demand it but because of his need." [Trans. Muhammad Tufail Ansari, Kitab Bhaban, India, 2000, Vol. #3, p. 438, #2431.]*

Qardhul Hassan is an important tool of providing loan for low-income groups of the society in the framework of Islamic banking system of the country. Organizing and making this micro-credit instrument aimed at income redistribution among the community can create the necessary structure and background for the development of poverty alleviation programs and enhancing financial inclusion through proper planning and implementation of micro-credit projects in the country (Mojtahed and Hassanzadeh, 2009). This paper emphasizes on the Qardhul Hassan because of its emphasis on the income redistribution aimed at reducing the gap between rich and poor populace in the society. It is also believed that Qardhul Hassan will play a significant role in enhancing financial inclusion (Saqib et al., 2015) and assist Nigeria in achieving its 80% inclusion rate by the year 2020 (CBN, 2012).

#### 2.4. An Overview of Financial Inclusion in Nigeria

Financial inclusion has been defined as: "The delivery of financial services at affordable costs to sections of disadvantaged and low-income segments of society" (Mohseni-Cheraghloou et al., 2012). These services include access to: Account at a Formal Financial Institution, Access to Formal Accounts, Use of Formal Accounts, Mobile Payments, Savings, Credit and Insurance and pensions (Allen et al., 2014; CBN, 2012; Demirguc-kunt and Kiapper, 2012; World Bank, 2014; Mohseni-Cheraghloou et al., 2012). The United Nations (UN) defines the goals of financial

inclusion as: (1) Access at a reasonable cost for all households to a full range of financial services, including savings or deposit services, payment and transfer services, credit and insurance; (2) sound and safe institutions governed by precise regulation and industry performance standards; (3) financial and institutional sustainability, to ensure continuity and certainty of investment; and (4) Competition to ensure choice and affordability for clients (World Bank, 2014).

A survey conducted in Nigeria in 2008 by Enhancing Financial Innovation and Access (EFInA) revealed that about 53.0% of adults were excluded from financial services. As at 2014, the exclusion rate remained 39.5% despite several effort by the CBN to improve the situation (EFInA, 2014). Nigeria has 28.6 million bank accounts with a population of over 168 million people, and 89.7 million adults (Abiola et al., 2014; CBN, 2012; EFInA, 2012; Sanusi, 2012). CBN in collaboration with other stakeholders launched the National Financial Inclusion Strategy (NFIS) on 23<sup>rd</sup> October 2012 aimed at reducing the exclusion rate to 20% by 2020. Specifically, adult Nigerians with access to payment services is to increase from 21.6% in 2010 to 70% in 2020, while those with access to savings should increase from 24.0% to 60%; and Credit from 2% to 40%, Insurance from 1% to 40% and Pensions from 5% to 40%, within the same period (Abiola et al., 2014; CBN, 2012; Kama and Adigun, 2013; Sanusi, 2012).

To achieve these targets, Nigeria joined other 20 developing countries and made financial inclusion commitment referred to as the "Maya Declaration," in Mexico. The number of countries increased to 35 in September 2012, which culminated into the Alliance for Financial Inclusion, Global Policy Forum in Cape Town, South Africa. Nigeria through CBN, targeted to increase Deposit Money Banks branches from 6.8 units per 100,000 adults in 2010 to 7.6 units per 100,000 adults in 2020, microfinance bank branches to increase from 2.9 units to 5.5 units; ATMs from 11.8 units to 203.6 units, point of sales from 13.3 units to 850 units, mobile agents from 0 to 62 units, all per 100,000 adults between 2010 and 2020 (CBN, 2012). Among the efforts to reach out to the financially excluded adults in Nigeria, was the introduction of Islamic Banking referred to as non-interest financial services (Sanusi, 2011). Therefore, this paper proposes the adoption of financial inclusion as a moderator on the relationship between the dependent (QHF acceptance) and independent variables (attitudes towards QHF, knowledge of QHF, government support, perceived benefits and religious obligations). These variables shall be discoursed in the following section.

#### 2.5. Attitude towards QHF

Attitude towards the behavior refers to the individual's favorable or unfavorable evaluations of the behavior (Vallerand et al., 1992). Previous studies by Amin et al. (2011) found that attitude influences the intention to use Islamic personal financing. Amin et al. (2010) had discovered the positive relationship between attitude and QHF acceptance. In fact, their study considered attitude as the key determinant of QHF acceptance in Malaysian context. Jaffar and Musa (2014) measured attitude towards Islamic financing among Halal-certified micro and SMEs in terms of equity, fairness, flexibility, beneficial and rewarding and found

positive relationship. Consequently, this paper comes up with the following proposition:

P1: Attitude towards QHF will influence QHF acceptance.

### 2.6. Knowledge of QHF

The study by Jaffar and Musa (2014) measured the relationship between awareness and knowledge of consumers towards Halal-certified micro and SMEs in Malaysia. This paper adopts this variable as one of determinants of QHF acceptance in Nigeria. This will enable the researchers to determine the influence of knowledge of QHF on the QHF acceptance. Hence, the following proposition is developed.

P2: Knowledge of QHF will influence QHF acceptance.

### 2.7. Perceived Benefits

Perceived benefits as being measured by cost of products and rate-of-return, availability of credit with favourable terms, lower service charge, lower interest charge on loan, high-interest payment on deposits and lower monthly payment (Jaffar and Musa, 2014). The cost benefits may be positively related to attitude towards Islamic financing which will in turn influence intention to adopt Islamic financing in business. Similarly, Ismail (2014) found a positive relationship between the perceived usefulness and acceptance of mobile marketing services. Therefore, this paper intends to determine the influence of perceived benefits on QHF acceptance in Nigeria. Hence, the following proposition is developed.

P3: Perceived benefits will influence QHF acceptance.

### 2.8. Perceived Government Support

Previous study by (Amin et al., 2011) found insignificant relationship between government support and customers intention to use Islamic personal financing in Malaysia while Ringim (2012) found significant influence of government support on the perception of Muslims account holders in conventional banks towards Islamic bank. Consequently, this paper intends to determine how government support will influence QHF acceptance in Nigeria. Hence, the following proposition is developed.

P4: Perceived government support will influence QHF acceptance.

### 2.9. Religious Obligations

Previous study by Essoo and Dibb (2004) have found Muslim consumers to be more practical and innovative compared to Catholics and Hindus (Sun et al., 2012). The study by Wiebe and Fleck (1980) argued that religious commitment is the greatest determinant of religious behaviour as it shapes motivations and behavioural intentions. Similarly, available evidence have shown that consumers with little religious commitment are less consistent in their religious behaviour and easily influenced by externalities (Sun et al., 2012). Previous studies by (Amin et al., 2011; Jaffar and Musa, 2014; Sun et al., 2012) have found positive relationship between religious obligations and Muslims intention to use or accept Islamic financing products. The measures of religion obligation involve perception to comply with the

underlying principles of Islamic jurisprudence (Shari'ah). This include perceptions fulfil the social aspect of religious obligation by investing in Qardhul Hassan fund and expecting reward in the hereafter. This will ensure income redistribution among the Muslims communities and in compliance with the dictates of Allah as contained in Quran suratul Baqarah, chapter 2:245 as cited above. Hence, the following proposition is developed.

P5: Religious obligations will influence QHF acceptance.

### 2.10. Financial Inclusion as a Potential Moderator

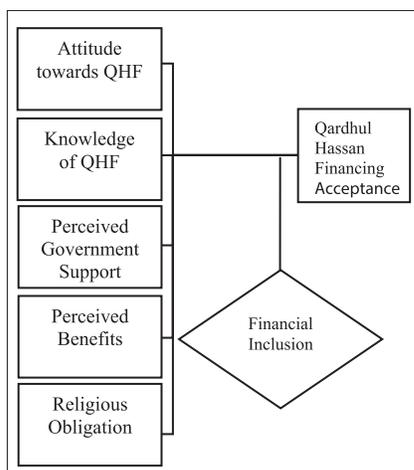
Ramasubbian (2012) measured the relative importance of different features of financial services and products related to: Access to financial services, flexible terms on savings and deposits, flexible terms on credits, information about various financial services, creditability and confidentiality about vulnerable accounts and found mixed results in terms of the relationship among variables. Similarly, Chakravarty et al. (2010) in their study, uses an axiomatic approach to measure financial inclusion across India and arrived at mixed findings as some variables were found positively related while others were found negative. Due to the inconsistencies in the results of previous studies of the relationship between variables, this paper intends to measure the moderating effects of financial inclusion on the relationship between attitudes towards QHF, knowledge of QHF, government support, perceived benefits, religious obligations and QHF acceptance in Nigeria. The paper believed that the customers that are financially included will behave differently from those that are financially excluded vis-à-vis the acceptance of QHF in Nigeria. The same applies to the other determinants but at the end of this study, the outcome will be used to justify this inference. Hence, the following proposition is developed.

P6: Financial inclusion moderates the relationship between attitudes towards QHF, knowledge of QHF, government support, perceived benefits, religious obligations and QHF acceptance.

## 3. PROPOSED THEORETICAL FRAMEWORK AND RESEARCH METHODOLOGY

Based on the literature review discussed above, this paper proposed a theoretical framework (Figure 1) which depicts the relationship between attitudes towards QHF, knowledge of QHF, government support, perceived benefits and religious obligations (independent variables) and the QHF acceptance (independent variables) in Nigeria. Similarly, the diagram also depicts the moderating effects of financial inclusion on the relationship between independent variables and dependent variable.

This paper employed theory of reasoned action (TRA) and theory of planned behaviour (TPB) as the underlying theories to understand the people's acceptance of QHF in Nigeria. This is in line with the recommendation of Ajzen et al. (1991) that TRA and TPB are made open for inclusion of any predictor variable that can explain human behaviour (Vallerand et al., 1992). This paper will adopt a quantitative approach to studying the relationship, and the

**Figure 1:** Research framework diagram

survey method of data collection will be adopted using a structured questionnaire since the nature of this study is cross-sectional.

#### 4. CONCLUSION

This paper has proposed the relationship between attitudes towards QHF, knowledge of QHF, perceived government support, perceived benefits and QHF acceptance in Nigeria. Similarly, the moderating effects of financial inclusion on the relationship mentioned above will be examined. If the proposed hypotheses are validated, the finding may assist the government, policy makers, regulators and practitioners in Nigeria for one of the remedies to the untold hardship suffered by the teeming Muslims population due to the high level of financial exclusion.

The findings will offer empirical evidence and justify the previously conducted studies on the relationship between attitude towards QHF, knowledge of QHF, perceived benefits, perceived government support, religious obligation and QHF acceptance in Nigeria. The study will also provide a new dimension to the existing literature on the moderating effect of financial inclusion on the relationship among variables. This is in line with the recommendation of Ajzen et al. (1991) that TRA and TPB are made open for inclusion of any predictor variable that can explain human behaviour (Vallerand et al., 1992). Similarly, the framework when validated may add to the existing literature on the practical application of the TRA and TPB as they serve as the underlying theories for this paper.

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