Chapter 4
Financing SMEs Through the Islamic Qard al-Hasan:
A Proposal of Islamic FinTech Interest-Free Lending for Government Initiatives

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ABSTRACT

Financing small and medium enterprises (SMEs) is one of the most important mechanisms to boost economic growth in both developed and developing nations. The contributions of SMEs in many countries' gross domestic product (GDP) have been overwhelming. SMEs improve job creation in all sectors of the economy and contribute to the people's economic wellbeing. However, many SMEs are not getting financing from their respective counties due to strict regulations and interest rate hike. With this kind of regulations and high interest, many brains are wasted, and many ideas are vanishing with the job opportunities attached them. Government agencies are therefore in need to innovate different ways to facilitate SME financing and support new businesses for achieving and maintaining sustainable economic growth. This chapter proposes an Islamic FinTech and its mechanisms to achieving this vital initiative using the Islamic benevolent loan "Alqard al-hasan."

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INTRODUCTION

Small and Medium Enterprises (SMEs) financing is growing rapidly and are becoming one of the most important mechanisms to help create jobs in the private sector economy. Financial technology is one of the most important mechanisms for enhancing people's well-being and can also lead to the achievements of financial prosperity in almost all economies, big or small and developed or developing. Islamic economic system is more than ever in need of modern technology enhancement to develop its unique techniques of doing business and digitalize its financing contracts for better application in modern societies. *Qard al-Hasan* (benevolent debt) is one of the most important mechanisms initiated to help those in need or with the good business ideas to engage their businesses by offering them interest-free loans for societal development and public enrichment purposes. MSE's can find this a way to go in every society as it is meant for their personal business development and economic well-being of the society.

SMEs Financing Initiatives

Small and Medium enterprise financing has gradually improved throughout the years, according to the investigations initiated by the Organization for Economic Cooperation and Development OECD's the findings on the development of SMEs financing shows a very encouraging development. Lending to SMEs generally improved in 2015, with a significant upward trend in new SME loans. While in 2013, only 6 out of 20 countries reported an increase in new SME lending, this number increased to 9 in 2014 and to 11 in 2015. For example, the volume of new SME loans in Finland rose by more than 23% in 2015 after seven consecutive years of decline. The median value of the annual growth rate of participating countries rose from -2.6% in 2013 to -0.1% in 2014, and then to 6.4% in 2015, illustrating a significant recovery in new lending to SMEs over this period.[1]

In 2015, the average interest rate charged to SMEs reduced for many countries, it may be, however, due to lose monetary policies in place. SME interest rates in 2015 were less than half of their level in 2008 in Belgium, France and Luxembourg peculiarly as low as one third.[2] Demand-side surveys also suggest a continued easing of credit conditions in a majority of participating countries, including a decline in loan rejection rates. At the same time, large cross-country differences persist, with credit standards remaining comparatively tight and interest rates relatively high in the economies most affected by the financial and ensuing sovereign debt crisis, such as Greece, Hungary, Ireland, Portugal, and Slovenia. Moreover, in emerging economies with relatively high inflation rates, including Brazil, Chile, Colombia, Georgia, Malaysia, Mexico, the Russian Federation, Serbia and Thailand, 2015 interest rates remained on average more than twice as high as the median value of participating countries.[3]

In our world today, SMEs in the industrialized countries managed over ninety percent of the existing firms employing almost two third of the labor force, such firms have very important role to play in growing the economy with further creation of new segment of employment. (Ronel Harel, 2016)

Identifying SMEs Financing Pain Points

SMEs always experience several pains in their fight to secure funding and execute their businesses amicably. SMEs are constantly hassling to physically rushing to their multiple funding banks accounts; manual paper work, check issues and many troubling payments procedures. Fintech is determined to be solving all these worrying pain points. And one of the most daring revelations was that of RSA group

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