UNIVERSITY OF KWAZULU-NATAL

INVESTIGATING THE DEMAND FOR SHORT-TERM ISLAMIC FINANCE PRODUCTS FOR SMALL AND MEDIUM ENTERPRISES WITH AN ANNUAL TURNOVER UNDER R5 MILLION IN THE GREATER DURBAN AREA, KWAZULU-NATAL, SOUTH AFRICA.

By

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DECLARATION

I, Aarif Saib declare the dissertation entitled: 'Investigating the demand for short-term Islamic finance products for small and medium enterprises with an annual turnover under R5 million in the greater Durban area, KwaZulu-Natal, South Africa’, is as a result of my own research and that it has not been submitted in part for any other degree or to any other university.

16th December 2015

Aarif Saib | Date

DEDICATION

This dissertation is dedicated to my wife, Caelisha.

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I wish to thank Allah for granting me the wisdom, strength and guidance, without which this study would not have been possible.

My sincere gratitude, thanks and appreciation goes out to my wife, Caelisha, for her encouragement, tireless dedication and patience throughout this project.

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I would also like to thank Dr. Abdullah Kader, my supervisor. Your guidance has been very comforting throughout my thesis.

ABSTRACT

This study investigated the demand for short-term islamic finance products for small and medium enterprises with an annual turnover under R5 million in the greater Durban area, KwaZulu-Natal, South Africa. Data was collected by using the quantitative survey method. A sample of 500 businesses was targeted for the study with 94 businesses responding. Electronic mail surveys were utilized in this study. The data was analysed to (i) to establish whether SMEs would prefer an alternative source of funding rather than the conventional interest-based model; (ii) to establish the perceptions of SMEs for Islamic finance; and (iii) to establish whether SMEs would prefer Islamic finance's profit loss sharing financial instrument rather than the conventional interest-based model. The need for finance by SMEs is driven by a desire either for expansion or survival. This can be achieved through two types of financial services, namely conventional and Islamic financial services. Conventional banking is the standard banking approach whilst Islamic banking is a system of financial activities that is consistent with the Islamic law (Shariah). The latter financial system prohibits interest, uncertainty and risk, speculation and gambling and investing in unlawful activities. SMEs face multiple barriers when trying to secure conventional financing. If they are able to secure the financing needed, SMEs shoulder the risk irrespective whether the venture is successful or not. The demand and supply for credit for SMEs were examined. Further, the credit gap and support was discussed. The role that ethics plays in Islamic finance was examined and the Islamic finance instruments and concepts were further analysed. Islamic finance and their implications on South Africa was also discussed. The literature review and survey of the study reflected Islamic finance's profit loss sharing financial instrument is an alternative to the conventional interest-based model. Recommendations for the financial sector in South Africa were proposed including recommendations for future research.

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CHAPTER ONE
INTRODUCTION

1.1 Introduction

The Islamic finance market has been estimated to be worth $2.1 trillion in terms of assets at the end of 2014 (Malaysia International Islamic Financial Centre, 2014). This presents a huge opportunity to companies and individuals seeking to invest and benefit in Islamic finance.

Islamic finance adheres to the principles of the Sharia Law. The sharia law is the moral code and religious law of the Islamic religion. A key concept of Islamic finance is the prohibition of the charging and acceptance of interest which is known in Arabic as “riba” on loans (Jamaldeen, 2012). Due to interest being forbidden, Islamic finance has developed a financial instrument referred to as 'profit loss sharing' that circumvents interest.

According to Dar and Presley (2001), profit loss sharing (PLS) is the contractual arrangement between two or more transacting parties, which allows them to pool their resources to invest in a project to share in the profits and losses. PLS is in direct contrast to conventional banking, where the financial institution is guaranteed a predetermined rate of interest (Dar, et al., 2001). In other words, whether the business venture succeeds or not, the financial institution will receive their predetermined return. All the risk is shouldered by the entrepreneur. By contrast, in Islamic finance, the financial institution and the entrepreneur have an equal stake in the outcome of the business. In terms of losses, the financial loss is shouldered by the financial institution and the entrepreneur loses his labour whilst in profit both parties share in pre-agreed proportions (Farooq, 2006).

Small and Medium Enterprises (SMEs) have traditionally faced an uphill battle securing financing. According to Herrington, Kew, J and Kew, P (2010), the lack of financing of SMEs is not just a South African problem but is a global phenomenon. Furthermore, financial institutions require surety and holds the entrepreneur liable for the loan, something that SMEs do not readily have available (Mahembe, 2011). In this context, SMEs with an annual turnover under R5 million will find it extremely difficult to secure finance. With the stringent criteria of conventional financing unattractive and unattainable for majority of SMEs with an annual turnover under R5 million, the unique risk factor of the Islamic finance's profit loss sharing system makes it a very attractive financing option.

1.2 Motivation for the Study

Small and Medium Enterprises (SMEs) face a number of challenges securing financing. SMEs have a natural desire to grow, expand and become financially sustainable but many do not have the necessary capital to do so. Many SMEs turn to conventional financial institutions for their capital needs to ensure growth or survival but due to the stringent criteria, many do not qualify for financing. In this context, an alternative source of financing is needed.

The purpose of this study is to establish if Islamic finance products can be an alternative source of financing for SMEs. SMEs will immediately benefit as the study will open up a new frontier in SME funding and financing. As more SMEs benefit from this alternative source of funding, the survival rate of SMEs will increase which will have a direct positive impact on the unemployment rate.

Financial institutions will also benefit immensely from this study. Institutions offering Islamic finance like ABSA, Al-Baraka, FNB, etc can now develop profit loss sharing products to cater for SME financing. Financial institutions like Standard Bank, Nedbank, Capitec, etc that do not offer any form of Islamic financing now have an incentive to develop such products and cater for this burgeoning market.

The literature review indicates there is a need for more research and more scholarly discourse on the subject. The study adds to the disciplines of Islamic finance and SME financing.

1.3 Focus of the Study

Islamic finance is a huge discipline and the study will focus on the profit loss sharing financial instrument. Other financial instruments of Islamic finance will be left out. SME funding and financing options will be covered in this study.

1.4 Problem Statement

Small and Medium Enterprises (SMEs) face multiple barriers when trying to secure conventional financing. If they are able to secure the financing needed through conventional banking, SMEs shoulder the risk irrespective whether the venture is successful or not. The conventional financial institution's investment is secured via a predetermined rate of interest. Due to the barriers, a number of SMEs do not receive financing. An alternative source of funding is required for SMEs.

Islamic finance has a financial instrument called Profit Loss Sharing (PLS) where the investor and SME equally bear the risks and enjoy the rewards according to pre-agreed proportions. PLS will be an attractive alternative source of funding for SMEs.

Due to this assertion, the study sought to explore if there is a demand for short-term Islamic finance products amongst SMEs. The study will be limited to the greater-Durban area and will investigate the demand and scope of the market in SMEs with an annual turnover under R5 million.

The main research question is: Is there a demand for short-term Islamic finance products for small and medium enterprises with an annual turnover under R5 million in the greater-Durban area, KwaZulu-Natal, South Africa.

1.5 Objectives

The study seeks to explore the following objectives:

1. To establish whether SMEs would prefer an alternative source of funding rather than the conventional interest-based model.

2. To establish the perceptions of SMEs for Islamic finance.

3. To establish whether SMEs would prefer Islamic finance's profit loss sharing financial instrument rather than the conventional interest-based model.

1.6 Research Sub-Questions

Each objective of the study will be achieved in the study by answering sub-questions of the objective.

Research sub-questions for Objective One:

1. Do SMEs agree with the conventional finance model?

2. Do SMEs agree with paying interest?

3. Do SMEs agree with the business practice of providing suretyships?

4. Do SMEs agree with being personally liable if the business venture fails after securing financing from a conventional financial institution?

5. Would SMEs prefer an alternative source of funding rather than the conventional interest-based model?

Research sub-questions for Objective Two:

1. Would SMEs consider utilizing Islamic finance before this study?

2. Do SMEs agree with not paying interest under Islamic Finance?

3. Do SMEs agree with not providing suretyships under Islamic Finance?

4. Do SMEs agree with Islamic finance not being offered to non-shariah compliant industries such the pork, alcohol and gambling industries?

5. Do SMEs feel Islamic finance can be an alternative to the conventional interest-based model?

Research sub-questions for Objective Three:

1. In utilizing profit loss sharing, do SMEs agree with creating a joint venture with the financial institution and becoming business partners?

2. In utilizing profit loss sharing, do SMEs agree with sharing the profits in pre-agreed proportions of the joint venture with the financial institution?

3. In utilizing profit loss sharing, do SMEs agree with the financial institution bearing the financial loss of the joint venture if it fails?

4. Do SMEs feel the profit loss sharing financial instrument is a better alternative than the interest-based model?

5. Would SMEs utilize the profit loss sharing financial instrument?

1.7 Limitations of the study

The limitations of the study included:

1. The small sample size is a limitation of the study as there is a probability that it might not provide an accurate picture of the general views of businesses when considering using Islamic financial services.

2. A major disadvantage of mail surveys is that you cannot clarify what you meant by a certain question if the participant does not understand the question (Bezuidenhout, 2014). She adds illiteracy and semi-literacy, and language usage could also be a problem. Another disadvantage of mail surveys was some participants could have answered the questions without thinking too deeply (Onodera, 2012).

3. There was limited screening capability of participants due to the nature of the methodology. Questionnaires can only be disseminated to potential participants that have valid e-mail addresses (Onodera, 2012).

4. A lot of senior management of SMEs did not respond to survey due to work commitments and lack of time.

5. There was also some disadvantages of purposive sampling. This may include its low level of reliability and high levels of bias (Black, 2010).

6. A number of participants (34%) who did not live in the greater-Durban region responded to the survey. The survey was intended for participants in the greater-Durban region.

7. A number of participants (47%) who had a turnover of greater than R5 million responded to the survey. The survey was intended for participants with a turnover under R5 million.

8. Race and religion was another limitation. The majority of the participants were Indian and followed Islam. The study sought equal representation in race and religion.

9. The position held in the company was a limitation. 50% of participants stated to occupy an 'Other' position. It unclear what position this was. The study sought decision-makers of SMEs.

10. SMEs trading for less than a year (13%) was a limitation. The study sought SMEs who has been trading for more than year.

The delimitations of the study included:

1. Due to the large size of the target population, not all individuals could be surveyed.

2. Quantitative research methodology limits participants responses.

3. Descriptive research does not answer the why questions.

1.8 Conclusion

This chapter discussed the motivation for the study, focus of the study, problem statement, research objectives and research questions. The structure of the study was outlined by briefly explaining the contents of each chapter of the dissertation.

The next chapter examines the literature on the lack of access of finance for SMEs and the principles of Islamic finance.

CHAPTER TWO
LITERATURE REVIEW

2.1 Introduction

The literature review will focus on the lack of access to finance for SMEs and Islamic financial services.

In the lack of access of finance for SMEs, the various definitions of SMEs would be discussed. Then, the role and importance of SMEs to the economy would be examined. Thereafter, an overview of the demand for credit from SMEs would be discussed. The supply of credit to SMEs would also be analysed. The three different sectors providing SMEs with credit: the public sector; the commercial banking sector; and donors, NGOs and the private sector would be examined.

The credit and support gap would also be examined. The concepts of access to finance would be defined, the SME access to credit gap in South Africa would be examined and the poor initiative of SMEs would be articulated.

In the principles of Islamic finance, the two financial systems (conventional finance and Islamic finance) will be examined. The study will discuss the principles that are forbidden in Islamic finance, the role of ethics in Islamic finance and the role of Islamic finance in South Africa. Islamic finance concepts, the Shari'ah Supervisory Board and Shari'ah Departments will be examined.

2.2 The lack of access to finance for SMEs.

SMEs have experienced a lack of access to finance. In this aspect of the literature review the definition of SMEs, the importance of SMEs to the economy, the demand for credit from SMEs, the supply of credit to SMEs and the credit and support gap of SMEs will be discussed.

2.2.1 Definition of SMEs

Small Medium Enterprises (SMEs) can be defined in a number of ways. IFC (2009) states that SMEs can be defined as businesses with less than 200 employees. Mahembe (2011) states that SMEs' definition has reference to the number of employees, to turnover categories or a combination of both. The National Small Business Act 1996 allows for a variation of both but according to the industry sector. In Section One of the National Small Business Act of 1996 as amended by the National Small Business Amendment Acts of 2003 and 2004 (NSB Act) defines 'small business' as:

" … a separate and distinct business entity, including co-operative enterprises and non-governmental organisations, managed by one owner or more which, including its branches or subsidiaries, if any, is predominantly carried on in any sector or sub sector of the economy mentioned in Column I of the Schedule (Annexure A)".

Small business can be further broken down into five categories: survivalist, micro, very small, small and medium (NSB Act). It is from these five categories that the term "SMME" developed from to describe small, medium and micro-enterprises. The terms 'SMME' and 'SME' are commonly used interchangeably (Mahembe, 2011).

Table 2.1 Summarises the definitions of SMEs in the National Small Business Act.

Enterprise Size	Number of Employees	Annual Turnover	Gross Assets, Excluding Fixed Property
Medium	Fewer than 100 to 200, depending on Industry.	Less than R4 million to R50m depending upon Industry.	Less than R2m to R18m depending on Industry.
Small	Fewer than 50.	Less than R2m to R25m depending on Industry.	Less than R2m to R4.5 m depending on Industry.
Very Small	Fewer than 10 to 20 depending on Industry.	Less than R200 000 to R500 000 depending on Industry.	Less than R150 000 to R500000 depending on Industry.
Micro	Fewer than 5.	Less than R150 000.	Less than R100 000.

Adapted from Falkena, H. 2004. *Competition in South African Banking. Task Group Report for the National Treasury & the South African Reserve Bank.* Pretoria. South Africa.

The five categories of SMEs have distinct characteristics (Table 2.1). Survivalist enterprise's income is less than the poverty line (Falkena et al, 2001). This category includes subsistence farmers, hawkers and vendors. Micro-enterprises often lack formal registration and has a turnover less than R150000 per year (Falkena et al, 2001). There income is less than the value added tax (VAT) registration limit and employs no more than five people. This category includes minibus taxis, tuck shops and household businesses. Very small enterprises are categorised for employing fewer than ten paid employees, have access to technology and operates in formal markets (Falkena et al, 2001). It should be noted that if very small enterprises operates in the mining, construction, electricity or manufacturing industries, they will have a staff complement of up to 20 employees. Small enterprise's are more established and have complex business operations (Falkena et al, 2001). They employ up to 50 staff members. The final SME category is medium enterprises who employ up to 100 employees and can have a decentralized management structures (Falkena et al, 2001). It should be noted that it medium enterprise's operates in the manufacturing, electricity, mining or construction industries, they can have a maximum of 200 employees.

2.2.2 The importance of SMEs to the economy

SMEs have long been recognised for the important contribution they make to the economy. Academics have described SMEs as the drivers of economic growth (Mahembe, 2011) and the illustrious first step towards industrialisation (Fida, 2008). A flourishing and vibrant economy, often signifies a blossoming SME sector (Mahembe, 2011).

SMEs contribute to the development of economies in a number of ways. They creating employment, provide coveted sustainability, generate higher production volumes, increase exports, introduce entrepreneurship skills and innovate the economy (Mahembe, 2011; and Kungolo, 2010).

The Competition Commission (2004) estimates that 99.3% of South African businesses at some stage were SMEs (Msweli and Oni, 2014). Further, the Commission states SMEs accounted for 53.9% of total employment and contributed 34.8% to GDP.

However, the World Bank (2013) estimated that in South Africa the SME contribution to employment generation was 39% (Table 2.2). Table 2.3 shows SME participation and contribution to the economy in the world.

Table 2.2: Contribution of SMEs to the South African economy

%	Survivalist	Micro(0)	Micro (1-4)	Very Small	Small Enterprises	Medium Enterprises	Large
Numbers of Firms	19.6	31.3	19.8	20.5	6.8	1.3	0.7
Employment	2.2	3.5	6.5	13	15.7	13	46.1
GDP	5.8			13.9		15	65.2

Adapted from Falkena, H., Abedian, I., Blottnitz, M., Coovadia, C., Davel, G., Madungandaba, J., Masilela, E., and Ress, S. *SME' Access To Finance In South Africa.* A Supply-Side Regulatory Review. 2001. http://www.treasury.gov.za/publications/other/Access%20to%20Finance%20in%20South%20Africa%20-%20A%20Supply-Side%20Regulatory%20Review.pdf. Accessed on 22 August 2015.

Table 2.3: SME participation and contribution to the economy

	Structure of the MSME Sector (% of all MSMEs)			SME Participation in the Economy		
Country Name	Micro	Small	Medium	SMEs	SMEs per 1,000 people	SME employment (% total)
Brazil	93.9	5.6	0.5	4,903,268	27.4	67.0
China	n/a	n/a	n/a	8,000,000	6.3	78.0
Egypt	92.7	6.1	0.9	1,649,794	26.8	73.5
United Kingdom	95.4	3.9	0.7	4,415,260	73.8	39.6
Ghana	55.3	42.0	2.7	25,679	1.2	66.0
India	94.0	3.3	-	295,098	0.3	66.9
Malawi	91.3	8.5	0.2	747,396	72.5	38.0
United States	78.8	19.7	1.5	5,868,737	20.0	50.9
South Africa	92.0	7.0	1.0	900,683	22.0	39.0

Adapted from World Bank. 2007. *Finance for All? Policy Research Report. http://econ.worldbank.org/WBSITE/EXTERNAL/EXTDEC/EXTRESEARCH/0,,contentMDK:21546633~pagePK:64214825~piPK:64214943~theSitePK:469382,00.html. Accessed on 31st August 2015.*

Various academics claim that 91% of the formal businesses in South Africa are SMEs (Abor and Quartey, 2010; Kungolo, 2010). They further add that SMEs contribute between 52 to 57% to GDP and account for approximately 61% of employment. Furthermore, Herrington, Kew and Kew (2010) states that there is an interdependent relationship between the economic growth rate and the level of entrepreneurship in South Africa.

2.2.3 The demand for credit from SMEs

The lack of financing for SMEs is a well established phenomena. Herrington et al (2010) states like their global peers, SMEs in South experience a lack of financing options. The International Finance Corporation (2011) agrees and states that a major obstacle for SME growth internationally is the inability to access capital. Msweli et al (2014) also states that in order for the SME sector to strengthen, issues dealing with the access to finance need to be resolved.

Table 2.4: Funding requirements and growth phases of SMEs

	Start-up Phase	**Growth Phase**	**Stable/Consolidation**	**Exit**
Type of SME	**Source of Finance**			
Traditional small business provides employment for individual, family and friends.	Family, friends, savings, equity in residential property, loans underwritten by government.	Asset-backed finance, bank debt, factoring and trade credit.	Bank debt if required.	Not applicable
High potential. Possibly export business.	Angel finance, team's equity and some venture capital.	Venture capital, private equity, asset-backed finance and some bank debt.	Venture capital, high yield debt market and bank debt.	Exit via capital markets or direct access to stock market.
High-tech, information and life science and intellectual property.	Angel finance, venture capital and corporates.	Venture capital, corporates and asset-backed finance.	Corporates and bank debts.	Exit typically through trade sale.

Adapted from Falkena, H., Abedian, I., Blottnitz, M., Coovadia, C., Davel, G., Madungandaba, J., Masilela, E., and Ress, S. *SME' Access To Finance In South Africa.* A Supply-Side Regulatory Review. 2001. http://www.treasury.gov.za/publications/other/Access%20to%20Finance%20in%20South%20Africa%20-%20A%20Supply-Side%20Regulatory%20Review.pdf. Accessed on 22 August 2015.

As Table 2.4 indicates, the type of finance SMEs requires is dependent on its development phase. SMEs in the start-up phase generally rely on friends, families, personal saving or angel financing. SMEs in the growth or stable phase rely on bank loans, venture capital, private equity or asset-backed financing.

Stats SA established that there were approximately 2,4 million SMEs in South Africa in 2007. The survey defined small business owners as persons who are older than 15 years; employ fewer than 200 employees; and generate an income through small business activity. This is illustrated in Table 2.5.

Table 2.5: Number of Small Business in South Africa

	Category of employer/self-employed	March 2005	Sept 2005	March 2006	Sept 2006	March 2007
Business Owners	Number of persons of working age (15 – 65) working on their own or with a partner, in any type of business.	1,836,000	2,060,000	1,999,000	2,105,000	1,942,000
	Number of elderly persons (66+) who run or do any kind of business for themselves.	56,000	87,000	73,000	65,000	59,000
Subsistence Farmers	Number of persons of working age (15 – 65) working on their own small farm or collecting natural products from the forest or sea.	385,000	240,000	585,000	425,000	374,000
	Number of elderly persons (66+) who do any work in their own or the family farm, garden, cattle kraal, or help in growing farm produce or in looking after animals for the household.	64,000	42,000	89,000	71,000	57,000
	Total	**2,341,000**	**2,429,000**	**2,746,000**	**2,666,000**	**2,432,000**

Adapted from Statistics South Africa. 2008. *Quarterly Labour Force Survey.* http://www.statssa.gov.za/publications/P0211/P02111stQuarter2011.pdf. Accessed on 25th August 2015.

Falkena et al. (2001) gives a breakdown of the average loan size per SME category in Table 2.6. Survivalist businesses need an average of R500 loan and have no access to banking facilities. Micro (0) businesses need an average of R1000 loan and may have a personal banking account. Micro (1 – 4) businesses need an average of R7000 loan, has a personal banking account and employs less than five employees. Very small businesses need an average of R25000 loan, has a business bank account, operates in formal markets and employs below 10 employees. Small enterprises need an average of R70000, has a business account and employs up to 50 employees. Small enterprises is differentiated by some form of management structure. Medium enterprises loan size is dependent on sector, region and institution providing finance. The average required is R150000. Medium enterprises has a business account with additional facilities and employs less 100 employees (except for the mining sector). Finally, medium enterprises' decision-making is complex and decentralized.

Table 2.6: Average Loan Size by SME Category

Sector	Description	Number of employees	1. Annual Turnover 2. Loan sizes 3. Access to banking facilities
Survivalist	Income generated is below poverty line.	No employees	1. <R10,000 2. Average R500 3. None
Micro (0)	Turnover is less than VAT registration limit. Not usually formally registered for tax or accounting purposes.	No employees	1. R10,000 to R25,000 2. Average R1000 3. Possibly individual account
Micro (1 - 4)	Same descriptors as Micro (0) except the number of employees are 1 – 4.	Less than 5 employees.	1. R25,000 to R50,000 2. Average R7000 3. Individual account
Very Small	Operate in formal market.	Less than 10 employees.	1. R50,000 to R200,000 2. Average R25,000 3. Entry level business account
Small Enterprises	Distinguished by some form of managerial co-ordination.	Less than 50 employees.	1. R200,000 to R5,000,000 2. Average R70,000 3. Business Account
Medium Enterprises	Further decentralization of decision making. More complex decision-making. Increased division of labour.	Less than 100 employees (200 in mining).	1. R500,000 to R50,000,000 2. Loan size is dependent on sector, region and institution providing finance. Average R150,000. 3. Business Account with additional facilities.

Adapted from Falkena, H., Abedian, I., Blottnitz, M., Coovadia, C., Davel, G., Madungandaba, J., Masilela, E., and Ress, S. *SME' Access To Finance In South Africa.* A Supply-Side Regulatory Review. 2001. http://www.treasury.gov.za/publications/other/Access%20to%20Finance%20in%20South%20Africa%20-%20A%20Supply-Side%20Regulatory%20Review.pdf. Accessed on 22 August 2015.

2.2.4 The supply of credit to SMEs

SMEs are supplied credit by the public sector, the commercial banking sector and donors, NGOs and the private sector.

2.2.4.1 The Public Sector

A number of funding and financing programmes are provided by the South African Government. The Department of Trade and Industry (DTI) website (www.thedti.gov.za) provides a plethora of information on the various Government SME support programmes available. This includes government agencies that provide financial support to SMEs. Furthermore, information is also available on the respective programmes and agencies websites. However, SMEs awareness of these programmes and agencies have been low (DTI, 2008).

Government support programmes can be categorized into three classifications: market access, business support and access to finance. This study will focus on the access to finance classification. Two schemes identified in this study that provides financial support is the Khula Enterprise Development Fund (Khula) and the Thembani International Guarantee Fund.

Khula Enterprise Development Fund (Khula) was established in 1996 and operates as an independent agency under the auspices of the Department of Trade and Industry (Small Enterprise Finance Agency, 2015). The fund has developed the Khula Credit Indemnity Scheme that provides access to finance to people who want to start or expand. businesses. The Fund finances from R10,000 to R3 million. The applicant is responsible for payment for the duration of the loan.

The Thembani International Guarantee Fund (TIGF) as a non-profit organisation (NPO) in 1996. The fund partially guarantees up to 75% of loans from commercial banks to successful applicants (Thembani International Guarantee Fund, 2015). The loan period is between one to three years. TIGF does not lend money directly to applicants and requires both banks and applicants to share the credit risk. The Fund monitors the loans which must be repaid regularly.

2.2.4.2 The Commercial Banking Sector

Commercial banks view SMEs as a viable source of business. Commercial banks have developed an effective monitoring system such as credit scoring models to distinguish between high and low risk clients (Mahembe, 2011). Commercial banks outstrip most Government programmes funding at their own risk (OECD, 2006).

In South Africa, as of June 2015, there are 17 operating commercial banks and 14 local branches of foreign banks (South African Reserve Bank, 2015). There were three mutual banks and 39 representative offices of foreign banks (South African Reserve Bank, 2015).

Standard Bank, Nedbank, ABSA and First National Bank (FNB) account for 83% for the total banking sector assets (International Monetary Fund, 2015). An estimation of the total SME loan book reveals that FNB has the lowest market share at 12% and Standard Bank the highest at 35% (Falkena, 2004) (Table 2.7).

Table 2.7: Small business book of major banks

	Standard Bank	**Nedbank**	**ABSA**	**FNB**	**Total**
SME Clients	367,500	346,500	210,000	126,000	1,050,000
Total book			R2.6 billion		R13 billion
Average size of loan	R39,000		R47,000		
Market Share	35%	33%	20%	12%	100%

Adapted from Falkena, H., Abedian, I., Blottnitz, M., Coovadia, C., Davel, G., Madungandaba, J., Masilela, E., and Ress, S. *SME' Access To Finance In South Africa.* A Supply-Side Regulatory Review. 2001. http://www.treasury.gov.za/publications/other/Access%20to%20Finance%20in%20South%20Africa%20-%20A%20Supply-Side%20Regulatory%20Review.pdf. Accessed on 22 August 2015.

Commercial banks have increased their interactions with SMEs with paying attention to historically disadvantaged individuals (Mahembe, 2011). With the realisation that micro-enterprises can grow into lucrative corporates, commercial banks are investing into this cost intensive market segment for future pay offs (Mahembe, 2011). She adds that though the risk assessment process for SMEs may have not changed amongst commercial banks, there has been an increase in special funding schemes. This includes sector of industry focuses.

All of South Africa's major banks run workshops or seminars to help SMEs. In additional all the banks offer small business lending, support desks or portfolios.

South Africa's commercial banks barriers to accessing loans is very low (World Bank, 2007). Table 2.8, below, shows that South African commercial banks process an SME loan on average of 4.13 days. The international average is 11.03 days. However, SME applications take twice as long than other business loans (Mahembe, 2011). Academics have stated that is probably due to a lack of information provided by SME applicants (Falkena, 2004; and Mahembe, 2011).

Table 2.8: Barriers to loan services: business and SME loans

			Physical access	Affordability				Eligibility	
	Number of banks	Loan market share	Locations to submit loan applications (out of 5)	Minimum amount business loan (% of GDPPC)	Fee business loan (% of min. loan amount)	Minimum amount SME loan (% of GDPPC)	Fees SMEs loan (% of min. loan amount)	Days to process business loan applications	Days to process SME loan applications
Brazil	4	48.61%	4.85	19.19	2.10	8.08	2.10	10.32	3.63
China	2	23.63%	2.00	-	0.00	-	0.00	50.00	40.00
Egypt	2	32.08%	2.81	14.61	0.35	0.00	0.00	19.29	14.43
India	4	37.75%	2.44	57.77	0.93	145.17	0.84	19.98	10.75
Mexico	3	45.74%	4.20	101.93	1.27	87.80	1.61	15.70	9.86
South Africa	**3**	**69.39%**	**5.00**	**15.98**	**0.65**	**15.98**	**0.65**	**2.73**	**4.13**
United Kingdom	2	18.46%	5.00	26.12	1.32	6.05	1.32	12.32	10.47
Zimbabwe	4	43.45%	2.85	263.49	2.54	240.12	2.54	7.91	3.91
Minimum	1	5.61%	1.77	0.00	0.00	0.00	0.00	1.00	1.00
5th percentile	1	14.43%	2.00	0.00	0.00	0.00	0.00	1.99	1.99
Median	3	43.17%	3.05	55.28	1.26	39.86	1.28	10.64	9.09
Average	3	45.19%	3.23	2259.06	4.73	337.58	4.67	12.68	11.03
Maximum	6	100.00%	5.00	64216.77	100.35	3141.17	100.35	50.00	43.26
95th percentile	5	80.46%	5.00	9845.42	15.54	1876.04	16.13	31.54	31.54

Adapted from World Bank. 2007. *Finance for All? Policy Research Report.* http://econ.worldbank.org/WBSITE/EXTERNAL/EXTDEC/EXTRESEARCH/0,,contentMDK:21546633~pagePK:64214825~piPK:64214943~theSitePK:469382,00.html. Accessed on 31st August 2015.

2.2.4.3 Donors, NGOs and the Private Sector

International organisations have funded South African SMEs previously (Mahembe, 2011). Organisations such as Germany's Friedrich Ebert Foundation and German Co-operative and Raiffeisen Confederation have funded SMEs. Donor support has contributed to the development of funding programmes and spreading such programmes rural areas (Mahembe, 2011).

The micro-finance sector has emerged to service the survivalist, very small and small SMEs (Mahembe, 2011). Medium SMEs and corporates are usually tended to by the commercial banking institutions. The micro-finance institutions are either registered with the Microfinance South Africa (MFSA) or the Development Microfinance Association (DMA). MFSA has 1300 offices and has a membership of approximately 150,038 (MFSA, 2015). 14 development micro-finance institutions comprise DMA and has in the last 15 years reached an estimated 100,000 clients (DMA, 2015).

Finally, there has been a trend of larger corporates providing outreach programmes or development services for SMEs (Mahembe, 2011). These SMEs can be their suppliers, clients of some other target group. The programmes or services are in the realm of training programmes, procurement or voucher that can be used for discounts on service charges or products.

2.2.5 The credit and support gap

Amongst other factors, SME development is hindered by the lack of finance (Akoena and Gockel, 2002).

2.2.5.1 Defining concepts of access to finance

Demirguc-Kunt, et al. (2006) states that there are two main sources of external finance for new SMEs: equity and debt. SMEs desire small levels of financing which results in them not being to access external equity such as venture capital or the stock exchange. Due to the lack of external equity bank loans, overdrafts and supplier credit become new SMEs source of financing in the early stage of development. Debt financing is more popular with SMEs but SMEs' access to debt financing is limited (Mengistae, 2010).

The “financing gap” refers to a sector of economically active SMEs that cannot secure financing from banks, the public sector or capital markets (Mahembe, 2011). The Organisation for Economic Co-operation and Development (2007) state that the financing gap's definition is made up of two parts. Firstly, SMEs that lack finance have the ability to use the finance constructively if they were available but, secondly, SMEs are not financed due to “structural characteristics”.

2.2.5.2 The SME access to credit gap

SMEs have long viewed access to finance as a major problem (Turner, 2008). Mengistae

(2010) agrees and states that SMEs are unlikely to have access to finance. SMEs access to finance can be established by comparing the supply and demand for credit by SMEs. Access to finance for SMEs are influenced by internal and systemic factors (Beck, Demirgüç-Kunt and Pería, 2008).

Internal factors include surety, management skill and experience, separation of personal and business finance and networking (Barbosa and Moraes, 2004). The size of the SMEs also plays a role, as smaller the size the less likely an SME is to be successful for finance (Mengistae, 2010). Also, the smaller the firm, the smaller the amount an SME will apply for (Falkena, 2004). SMEs are less likely to apply for loans due to the high perceived rejection rates, not knowing the procedures or the hight interest rates (Chimucheka and Rungani, 2011). Experience of the business owner (Rudez and Mihalic, 2007), the ownership of the SME (Falkena, 2004), availability of information on finance (Falkena, 2004) and the age of the SME (OECD, 2007) are other borrower-specific factors.

Financial institutions that provide SMEs with credit will want the terms of the finance to be followed and that the SMEs act in a manner that will ensure that the finance will be repaid (Mahembe, 2011). However, this is difficult for SMEs to achieve. Research indicates once the borrower obtains the funds, they are likely to partake in risky behaviours to maximise profit (OECD, 2007). The lack of distinction between the SME owner's personal and business lives and information asymmetries is partly to blame for this situation.

External factors include offering finance at high interest rates that SMEs cannot afford, adverse credit selection, monitoring problems and asymmetric information (Beck et al., 2008). The business environment the SMEs operates also hampers in its efforts to access finance. The lack of transparency where there exists a high levels of informality in the economy effects SMEs (OECD, 2007). This is manifested when SMEs operate outside of the formal system. A weak legal system is another factor. Mahembe (2011) states that South Africa has a relevantly inefficient legal system as compared to other developing countries. Crime and corruption also impacts SMEs. The World Bank (2007) found that South African SMEs rate crime as a major hurdle on investment and are less likely to invest in their businesses.

2.2.4.3 Poor initiative of SMEs

As discussed in the supply of credit to SMEs above, there are ample available funds to SMEs from both the private and public sectors. However, there exists a lack of awareness of these programmes (DTI, 2008). Mahembe (2011) states that South Africa does not sufficiently promote the growth and sustainability of SMEs. The Department of Trade and Industry (2010) has noted this, stating that a single centralized source of information is needs.

2.3 The principles of Islamic Finance.

Islamic finance lays the foundations of a fair and ethical financial system that has socio-economic impacts in the market it operated in. It does not only cater for the needs of the Muslim population but can service anyone regardless of their race, nationality, ethnicity or religious beliefs.

2.3.1 Financial Systems

The banking system is divided into Islamic finance and conventional banking systems which is examined below.

2.3.1.1 Conventional finance system

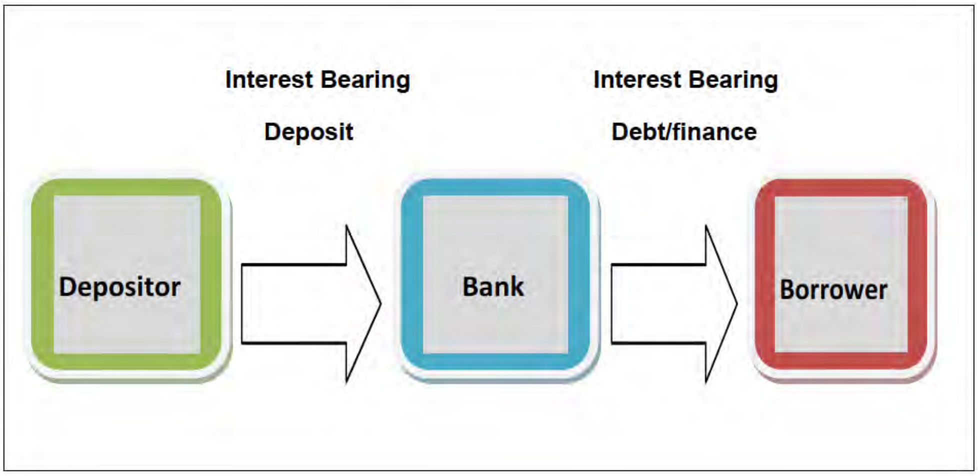
The conventional finance system is viewed as a lender and borrower of funds (Kettell, 2012). Even if its capital fails to bear interest, a conventional bank will not stop charging interest to its clients. Figure 2.1 explains the conventional banking approach.

2.3.1.2 Islamic finance system

Islamic banking is the financial services based on the principles of the Qur'an (Kettell, 2012). The Islamic financial system is unlike conventional banking in a number of ways.

The key difference is that Islamic finance does not deal in interest but rather a profit share arrangement is agreed upon. Islamic finance does not deal in the alcohol, tobacco, gambling, pork products, prostitution, insurance and conventional banking (Noormahomed, 2013; and Kettell, 2012).

Figure 2.1: The Conventional Banking System



Adapted from Kettell, B. 2012. *Frequently asked Questions in Islamic Finance*. United Kingdom. John Wiley and Sons.

Islamic banking is based in accordance with the Shari'ah law (Noormahomed, 2013). Shariah law guides the way Muslim conducts their lives including their financial affairs. Islamic banking is has oversight by an independent Shari'ah Supervisory Board who conducts audits of the processes of Islamic financial products when they are conceptualised and offered (Kettell, 2012). Figure 2.2 describes the Islamic banking approach.

2.3.2 Differences between an Islamic and conventional financial institution

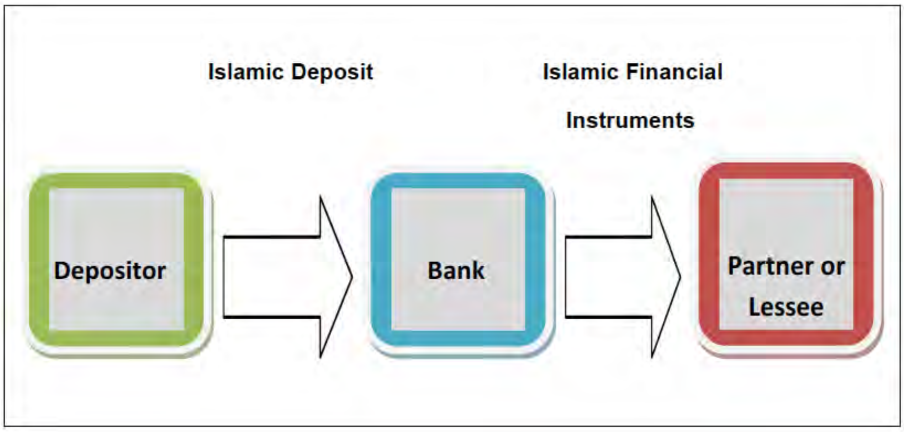
The differences between Islamic and conventional financial institution are summarised below:

2.3.2.1 Islamic Financial Institution

In Islamic financial institutions, money is not viewed as a commodity but rather it is valueless and cannot be leant at a price (Regent, 2012). Therefore, interest cannot be charged.

All financial activities must be backed by tangible assets such property (Regent, 2012). No transactions can have an element of uncertainty regarding timing of execution or delivery (Noormahomed, 2013). Any transactions that are against the Shariah is prohibited such as gambling and prostitution (Regent, 2012). Furthermore, penalties for late payments are prohibited (Noormahomed, 2013). If such penalties are levied, they must be donated to charity.

Figure 2.2: The Islamic Banking Approach



Adapted from Kettell, B. 2012. *Frequently asked Questions in Islamic Finance*. United Kingdom. John Wiley and Sons.

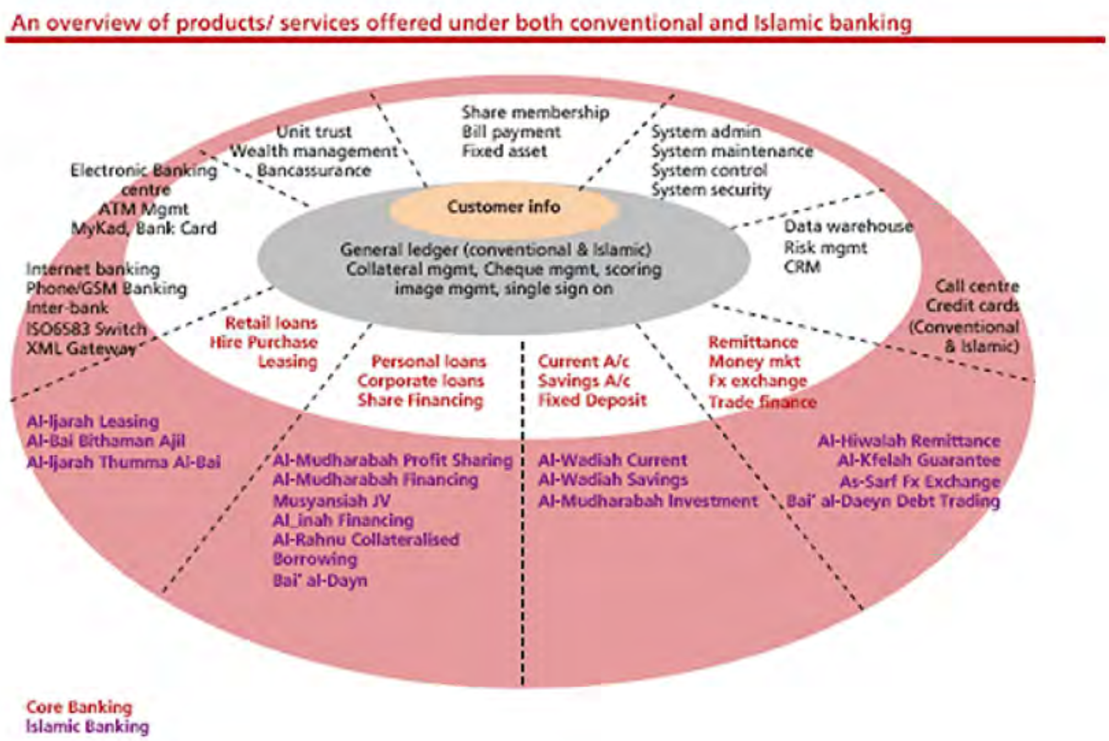
2.3.2.2 Conventional Financial Institutions

In conventional banks, financing activities need not be backed by tangible assets (Noormahomed, 2013). Money is valued based on opportunity cost, time value of money and the level of risk (Regent, 2012). It is common practice to exchange cash in terms of interest. In conventional banking, risk management and uncertainty are ingrained in the system (Noormahomed, 2013). It is common practice to charge for fees for late payments.

2.3.3 Products offered by a conventional and Islamic financial institution.

South Africa financial institutions have embraced Islamic finance in recent years, although they are not advance in innovating products and services as some international Islamic financial institutions (Noormahomed, 2013). Their products and services can be divided into four categories: asset financing, hire purchase and leasing; trade and foreign exchange services; investments; and personal and corporate loans (Figure 2.3).

Figure 2.3: Products offered by conventional and Islamic financial institutions internationally.



Adapted from Malaysian Islamic Finance. 2013. Overview of Products/Services offered by Conventional and Islamic Banking. Available on: http://malaysianislamicfinance.com. Accessed 15 October, 2015.

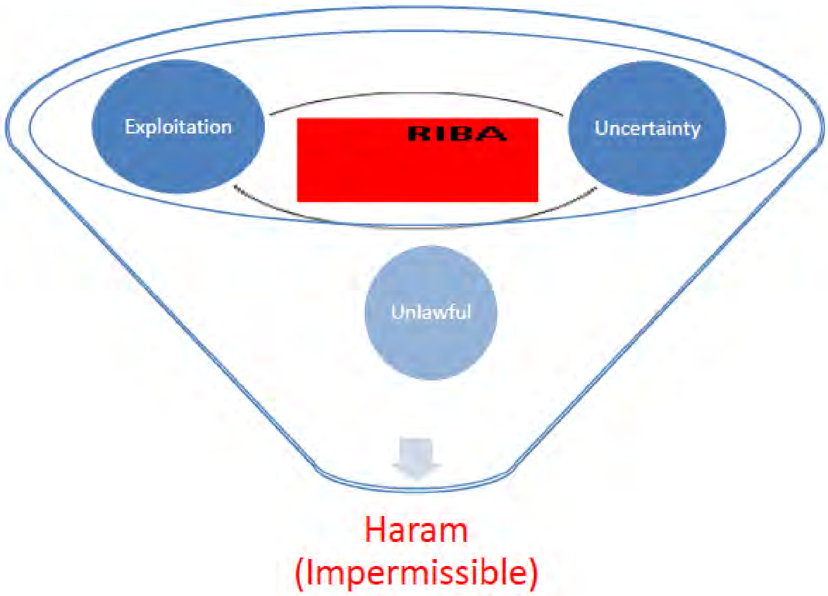
2.3.4 Principles that are prohibited in Islamic finance.

In Islamic finance there are fundamental principles that are prohibited such as

1. Riva (interest);
2. Unethical and unlawful activities;
3. Uncertainty;
4. Injustice and exploitation.

Figure 2.4 illustrates the principles that are prohibited in Islamic finance.

Figure 2.4: Principles that are prohibited in Islamic finance.



Adapted from ABSA. 2011. *Islamic Business Banking Products.* ABSA Guide: South Africa.

2.3.4.1 Riba

In Islam, 'riba' refers to interest or usury and is forbidden. Absa (2011) states that all transactions involving interest is invalid.

The Quran, Islam holiest book, has extensively commented on interest and usury. "Those who devour usury will not stand except as stands one whom the evil one by his touch has driven to madness". The Quran continues: "Trade is like usury but Allah hath permitted trade and forbidden usury. Those who after receiving direction from their Lord desist shall be pardoned for the past; their case is for Allah (to judge); but those who repeat (the offence) are companions of the fire: they will abide therein (for ever)" (Quran, Surah II: 275).

2.3.4.2 Unethical and unlawful activities

Unethical activities refer to behaviours that are immoral such as pornography (Absa, 2011). Unlawful activities refer to activities are impermissible or forbidden (Absa, 2011). Examples of unlawful activities include alcohol, gambling or consuming pork.

2.3.4.3 Uncertainty

In Islamic finance, any dealing that has a degree of uncertainty would render the contract void. Transparency is key to all dealings (Absa, 2011). For example, in a partnership, if the profit sharing ration is unknown that the partnership will be invalid.

2.3.4.4 Injustice and exploitation

In Islamic law, ethics is a central component and justice is imperative in all transaction (Absa, 2011). Therefore, honesty, fair trade and humility are virtues that are urged.

2.3.5 The role of ethics in Islamic finance

The demand for Islamic finance has been driven by ethical factors. Butcher (1998) states that ethical decision-making is need in society and must be an obligation to all social institutions including government, business and our lives. Mancosa (2011) states that ethics is what is good or bad, right or wrong, obligatory, responsible or irresponsible oral principles and rules of conduct in life. Ethics influence character and conduct, and is associated to care, compassion, guilt, empathy and resentment. Mancosa (2011) further adds that ethics defies and concise and clear definition.

Ethical factors are complicated because of extended consequences (Noormahomed, 2013). This results in ethical dilemmas and there are several approaches to resolve them. This includes the utilitarian, justice and moral rights approaches. When solving ethnical dilemmas there are a number of actions and their related consequences. Noormahomed (2013) states that ethical dilemmas are difficult, due to making value judgements which by their nature are blurred. Ethical decisions requires one to make a decision that one will champion the most important values. But, at times, when making a decision may result in other values being violated. Ping (2010) states that the best solution to an ethical dilemma is to champion the important values whilst breaching few other values as possible.

The three main subjects of ethics are

1. Religious tradition
2. Self-interest; and
3. Conscience.

2.3.5.1 Religious tradition

Religion has always been a source of morality. Noormahomed (2013) states that in religion, 'morality has found its authority and the fundamental reason for its existence'. Mancosa (2011) states that God is the perfect authority on ethics. God knows right from wrong and has ordained it to be so. Noormahomed (2013) states that Shariah law, particularly relating to business, is derived from God and is all that is good.

Muslims are guided by this belief and it is much easier to decide what is right or wrong because God says so. Mancosa (2011) states that all the major world religions have upheld the similar basic principle which has had a strong influence on ethical dilemmas.

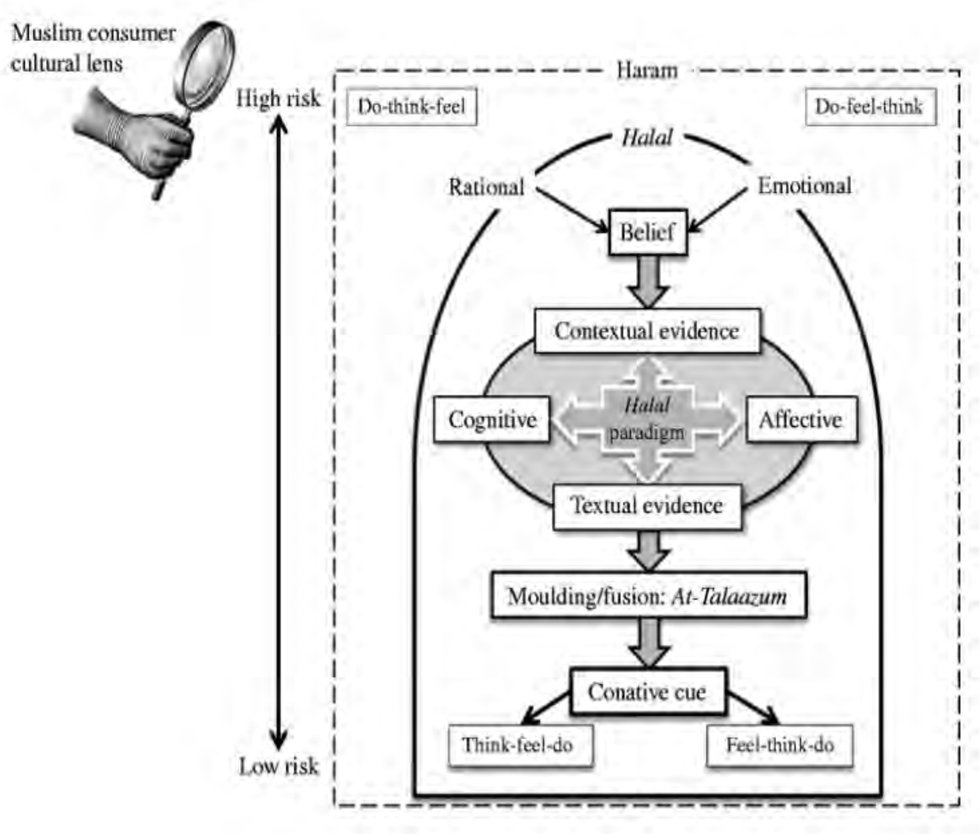
2.3.5.2 Self-interest

Self-interest refers to be interested in one's own good or benefit (Noormahomed, 2013). To be self-interested, is to act with advancing one's own benefits. Mancosa (2011) states that self-interest justifies the desire to achieve one's own interests.

2.3.5.3 Conscience

Conscience relates to the inner voice within oneself that decides what is good and evil, right and wrong (Noormahomed, 2013). Everybody has a conscience. Noormahomed (2013) further adds that at some period in one's life, every person experiences a judgement call identifying right and wrong from one's inner voice. Figure 2.5 analyses what is Halaal (permissible) versus Haram (forbidden).

Figure 2.5: A conceptual analysis of Halaal (permissible) versus Haram (forbidden)



Adapted from Emerald Insight. 2012. *Muslim Consumer Lens.* Available from: www.emeraldinsight.com Accessed 15 October 2015.

2.3.6 Islamic finance in South Africa

Islamic financial institutions in South Africa have a turbulent past. Two majors setbacks tainted Islamic finance. Jaame Limited, a financial institution based on Islamic principles, failed in the mid-1990s. So too did the Islamic Bank Limited failed when it liquidated in 1997. Noormahomed (2013) states that these Islamic finance institutions failed due to allegedly failing to fulfil corporate governance principles and not due to the principles of Islamic finance. Regent (2012) states since then Islamic financial institutions in South Africa faced an uphill battle in gaining the trust of its clients but have made much progress in recent times.

Presently, Albaraka Bank is the only Islamic financial institution that operates in South Africa. A number of conventional banks such Absa, First National Bank, Investec and HBZ have entered into Islamic finance. Noormahomed (2013) states that this domain has become increasing competitive and has been growing substantially.

2.3.7 Islamic finance instruments

Figure 2.6 illustrates a segmented view of an Islamic Financial Institution.

Figure 2.6: Segmented view of an Islamic Financial Institution.

Adapted from Iqbal, Z and Mirakhor, A. 2007. *An Introduction to Islamic Finance. Theory and Practice.* John Wiley & Sons. Singapore.

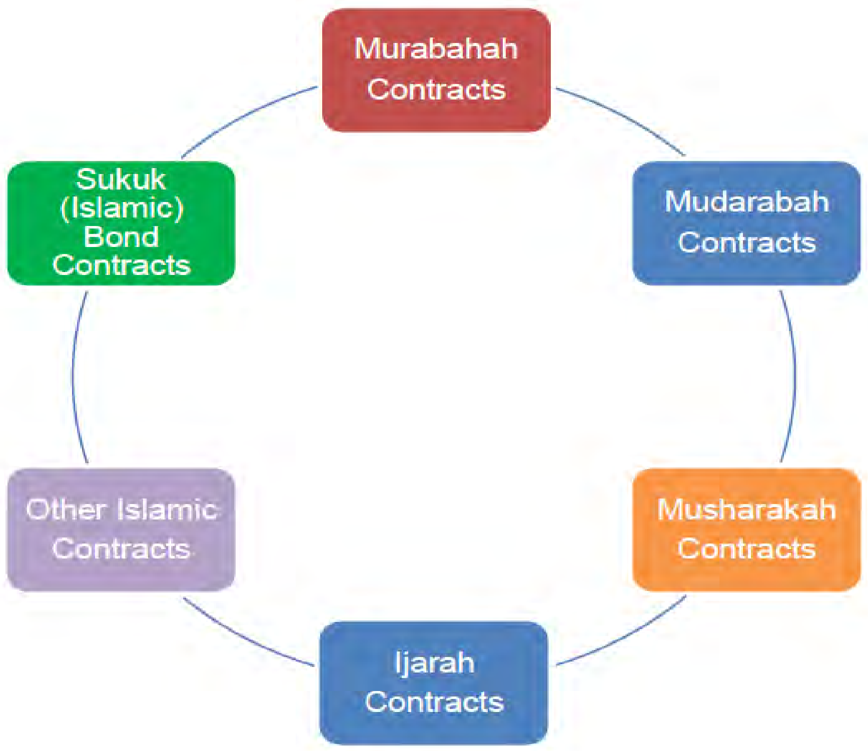
Islamic finance aims to perform financial contracts which are restricted to financial instruments developed within the framework of Shariah law (Sunni Path, 2012). The financial contracts relate to investments, trade and loans.

The instruments include:

1. Murabahah contracts;
2. Mudarabah contracts;
3. Musharakah contracts;
4. Ijarah contracts;
5. Other Islamic contracts; and
6. Sukuk (Islamic) bond contracts.

Figure 2.7 illustrates Islamic finance instruments and concepts.

Figure 2.7: Islamic finance instruments and concepts



Adapted from Kettell, B. 2012. *Frequently asked Questions in Islamic Finance*. United Kingdom. John Wiley and Sons.

2.3.7.1 Murabahah contracts

The 'Murabahah' contract is similar to a leasing contract. It is a type of sale where the sellers buys an item such as wheat and then trades it at a profit (Noormahomed, 2013). Murabahah involves the purchase of goods and therefore does not make a profit on money lending. In Islamic finance, the bank purchases an item (like a property) on behalf of its client and then sells it to the same client, at a profit (Kettell, 2012). The client will pay the bank in staggered monthly amounts.

2.3.7.2 Mudarabah contracts

Mudarabah contracts are partnership loans between bank and its clients (Kettell, 2012:

297). The bank provides the finance whilst the borrower provides the effort and expertise. Losses are completely borne by the bank whilst profits are shared at a predetermined ratio. The entrepreneur is covered by limited liability provisions (Noormahomed, 2013). Kettell (2012) notes that whilst the entrepreneur has final control over the business, major investment decisions, has to be approved by the bank. In this study, Mudarabah contracts is the chosen financial instrument.

2.3.7.3 Musharakah contracts

Musharakah contracts refers to a situation where the bank invests into the clients business. Profits and losses are distributed among the investors according to each investor’s equity stake (Noormahomed, 2013). Musharakah contracts are applied with deposits or investment accounts that do not have a fixed return but rather profit-loss sharing. Kettell (2012) states that such investments or deposits are linked to a 'specific investment account on the asset side of a bank’s balance sheet' or linked to the bank's profit level.

2.3.7.4 Ijarah contracts

Ijarah contracts are similar to leases. In this contract, the bank retains ownership of the assets and rents it to its client for a fee (Noormahomed, 2013). Ijarah contracts are used commonly used in home financing and vehicle financing. The bank usually sells the asset to the client on the expiry of the lease.

2.3.7.5 Other Islamic contracts

There are several other contracts such as Qardh (loan); Bai al Salam; Istisna (progressive financing); and Takaful (Islamic insurance). These are summarised below (Regent, 2012):

1. In Qardh (loan), the depositor grants a loan to the bank and does not receive any share in the profit or loss of the business.

2. Istisna refers to the purchase of goods by order, were monies is paid as the progress of the job or service is done.

3. Takaful is based on the Quranic principle of mutual assistance and is a type of insurance. Takaful provides mutual protection of assets by offering joint risk shared in the event of loss by one of its members.

2.3.8 Structure of Shariah board and Shariah Department

The Shariah Supervisory Board (SSB) and a Shariah Department are the core structure of an Islamic finance institution. They review and approves all transactions.

2.3.8.1 Shariah supervisory board

An independent Shariah Supervisory Board (SSB) is mandatory for any institutions offering Islamic financial services. Islamic scholars make up the SSB. The scholars are experienced and knowledgeable in Islamic finance and economics (Noormahomed, 2013). Regent (2012) states that the Shariah Board "reviews and approves the products, processes and contracts presented to ensure that they meet the requirements of Islamic banking principles and Shariah."

2.3.8.2 Shariah Department

The Shariah Department reviews all transactions to ensure that they are Shariah compliant (Noormahomed, 2013). They perform the following tasks, Regent (2012):

1. Shariah Audit Reports - prepared to ensure Shariah compliance.
2. Shariah Audits and Reviews
3. Shariah Checklists – to ensure all proper procedures are followed.

2.3.9 Conclusion

This chapter reviewed the literature on the lack of access to finance for SMEs and Islamic financial services.

In the lack of access of finance for SMEs, the various definitions of SMEs was discussed. Then, the role and importance of SMEs to the economy was examined. Thereafter, an overview of the demand for credit from SMEs was discussed.

The supply of credit to SMEs was analysed. The three different sectors providing SMEs with credit: the public sector; the commercial banking sector; and donors, NGOs and the private sector were examined.

Finally, the credit and support gap was examined. The concepts of access to finance were defined, the SME access to credit gap in South Africa was examined and the poor initiative of SMEs was articulated.

In Islamic financial services, the financial systems were discussed. The differences between conventional and Islamic financial services were examined. Thereafter, an overview of products offered by conventional and Islamic financial institutions were examined.

The principles that are prohibited in Islamic finance, the role of ethics and the role of Islamic finance in South Africa was analysed. The Islamic finance instruments were discussed. Lastly, the Shari'ah supervisory board and Shari'ah department was examined.

The next chapter is deals with research methodology used in the study. The research design, research instrument, population and sampling method used will be discussed.

CHAPTER THREE
RESEARCH METHODOLOGY

3.1. Introduction

In this chapter, the research methodology will be discussed. The chapter will focus on the aim and objectives of the study; the participants and the location of the study; the data collection strategies; the research design and methods; and finally, how the data will be analysed.

3.2. Aim and Objectives of the Study

The aim of the study is to determine if there is a demand for short-term Islamic finance products for small and medium enterprises with an annual turnover under R5 million in the greater-Durban area, KwaZulu-Natal, South Africa.

The aim of the study will be accomplished by achieving the study's three objectives:

1. To establish whether SMEs would prefer an alternative source of funding rather than the conventional interest-based model.

2. To establish the perceptions of SMEs for Islamic finance.

3. To establish whether SMEs would prefer Islamic finance's profit loss sharing financial instrument rather than the conventional interest-based model.

3.3. Participants and the Location of the Study.

The data was sourced from a database of 5000 businesses. The SMEs have an annual turnover of under R5 million. SMEs in this bracket experience a lack of capital and do require financing. Due to the stringent financing criteria, many SMEs do not qualify for conventional interest-based financing. There exist a market for an alternative source of financing.

In terms of religion, the participants will come from all faiths. The reason for the specification of religion is due to the fact that Islamic finance is associated with the Islamic religion and participants from other faiths may have a perception that they are not eligible to receive such finance on religious grounds, though this is not the case.

In terms of gender equality, there will be an equal representation of male and females. Racially, the study strived to have a population that is proportionally Indian, White, Black and Coloured. Only South African citizens will be surveyed eligible to participate in this study. The participants will be 18 years and older.

In terms of hierarchy, the decision-makers of the SMEs will be surveyed including the owners, managing directors, chief executive officers and chief financial officers. These individuals primary make the financial decisions of the companies.

All industries will be surveyed, excluding those that are non-sharia compliant including: SMEs involved in the alcohol, pork and gambling industries. Non-sharia compliant industries will not be eligible for Islamic finance.

SMEs will be harnessed from the greater-durban area which encompasses Verulam to the north, Hilcrest to the west and Amanzimtoti to the south.

3.4. Data Collection Strategies

3.4.1. Electronic Mail Survey

In this study, the data will be collected from electronic mail surveys. Electronic mail survey is a quantitative data collection tool (Bezuidenhout, 2014). In electronic mail surveys, questionnaires are sent to the participants in the sample who fill it at their leisure and return it by a given date (Bezuidenhout, 2014). The participant fills in the questionnaire on their own (Onodera, 2012; Dillman, et al; 2009). The researcher does not help the participant to fill in the questionnaire. Thus, the electronic mail survey can be called a "self-administered survey" (Bezuidenhout, 2014).

When sending electronic mail surveys, "you can either attach the questionnaire (via e-mail) or you can send your potential respondent a hyperlink that will take him or her to a secure website to complete the questionnaire," (Bezuidenhout, 2014, p.150). In this study, a hyperlink was sent to participants to complete the questionnaire. The website www.questionpro.com was utilized to generate the hyperlink.

There are a number of advantages using electronic mail surveys as you can collect a lot of data from an individual respondent at any time and it is versatile (Bezuidenhout, 2014). Due to the versatility of the electronic mail survey, a number of participants can fill in the questionnaires at the same time. There is no queueing system. Geography is also not a problem (Pollock; 2004). Bezuidenhout (2014) agrees that the questionnaires can be completed in almost any setting.

Electronic mail survey are relatively inexpensive and less time consuming. (Bezuidenhout, 2014; Pollock, 2004). Furthermore, the survey needs “few human resources” (Bezuidenhout, 2014, p.150) to be administered. Another advantage of electronic mail surveys is that it is easier to ask difficult questions and draw out participants’ true opinions (Onodera, 2012). This is due to the interviewer not being present. Onodera (2012) has noted that participants may avoid difficult questions and refuse to answer them when the interviewer is present. With the interviewer not being present, there is also no interviewer bias (Pollock, 2004).

Turnaround time is also fast. Pollock (2004) has stated that once the questionnaire been programmed, the sample processed and entered into the system, the system allows for detailed printouts at any time during the survey. The final advantage of conducting electronic mail surveys is that the pace of the interview is not dictated by the interviewer. Pollock (2004) states that the pace of the interview is set by the participant.

3.4.2. Likert Scale

The electronic mail surveys will utilize the “Likert Scale”. The likert scale requires a participant to indicate their degree of agreement or disagreement with a variety of statements related to an attitude or object (Bezuidenhout, 2014; Jamieson, 2004). Cohen et al (2000) agrees and states that likert scales provides a variety of responses to questions or statements. Bertram (2007) also agrees and adds that the likert scale is “a psychometric response scale to obtain participant's preference or degree of agreement with a statement or set of statements”. Furthermore, Bertram (2007) states that the likert scale only measures a single trait in nature and is non-comparative.

The Likert scale is made up of two parts: the item and the evaluation. The item is a statement whilst the evaluation is where the participant disagrees or agrees, and to what degree (Bezuidenhout, 2014). The evaluation part usually consists of a five or seven-point scale (Bertram, 2007; Bezuidenhout, 2014; Jamieson, 2004; Page- Bucci, 2007). In this study a five-point scale will be utilized. The scale is composed of “completely disagree”, “somewhat disagree”, “neutral”, “somewhat agree” and finally, “ completely agree”.

Each level on the scale is designated a numerical value (Bertram; 2007). The responses to individual items are added in order to create a total score for the participant (Bezuidenhout, 2014). Page- Bucci (2007) agrees: “The number beside each response becomes the value for that response and the total score is obtained by adding the values for each response”. In this study, “completely disagree” is assigned one, “somewhat disagree” is assigned two, “neutral” is assigned three, “somewhat agree” is assigned four and finally, “completely agreed” is assigned five. The electronic mail survey was administered to the sample of participants from the 1st August - 31st August 2015.

There are a number of advantages using the likert scale in this study. According to Page-Bucci (2007), the likert scale is simple to construct and each item is of equal value. Participants are scored rather than judged on each item individually. Furthermore, Page-Bucci (2007) states that the likert scale produces “a highly reliable scale” which is “easy to read and complete”.

3.4.3 Sampling Technique

In this study, non-probability sampling was utilized. Non-probability sampling refers to participants being selected from the population in a non-random manner. (Bezuidenhout, 2014). Fox (2010) agrees and adds that in non-probability sampling the participants are chosen in a manner that does not involve randomness or chance. Non-probability sampling is used when it is nearly impossible to determine who the entire population is or when it is difficult to gain access to the entire population. (Bezuidenhout, 2014). Kumar (2011) agrees and states that non-probability sampling are used when the number of elements in a population is either unknown or cannot be individually identified.

Due to the non-random manner in which participants are chosen, Bezuidenhout (2014) states participants will not have an equal opportunity to form part of the sample. Fox

(2010) agrees with the principle of inequality in non-random sampling and adds that conclusion derived from such samples may not be representative of the population as a whole. Bezuidenhout (2014) argues that though the sample may be unrepresentative, the focus is more on how many participants are interviewed to allow us to gain an in-depth understanding of the research problem we are exploring.

In non-random sampling, the sample size is “predetermined” (Kumar; 2011) and participants are selected from an accessible population (Bezuidenhout, 2014). Furthermore, Bezuidenhout (2014) adds that the selected population can recommend other possible participants to participate in the study.

3.4.3.1 Purposive Sampling

This study will utilize purposive sampling. In purposive sampling, the researcher will purposefully select the elements that they want to include in the sample (Bezuidenhout, 2014). The elements are based on a list of characteristics. Kumar (2011) states that the focus of purposive sampling is the researcher's judgement as to who can provide the relevant information to achieve the objectives of the study. Tongco (2007), Bernard (2002) and Lewis & Shepard (2006) also states that purposive sampling is the deliberate choice of an informant due to the qualities the informant possesses.

The selection process is imperative in purposive sampling. The researcher selects a sample from the population that have these characteristics and will disregard those that do not (Bezuidenhout, 2014). Kumar (2011) agrees and stated the researcher will only go to the sample from the population that are likely to have the required information and will be willing to share it with the researcher.

Purposive sampling has a number of advantages. It ensures that each element of the sample will assist with the research (Bezuidenhout, 2014). This is due to every element fits with the population parameters. If the element did not fit, the researcher will disregard it. With purposive sampling the researcher can construct a historical reality, describe a phenomenon or develop something about which only a little is known (Kumar, 2011). Another advantage is that the inherent bias of purposive sampling contributes to its efficiency (Tongco, 2007).

3.5. Research Design and Methods

3.5.1 Description and Purpose

The study is concerned with investigating the demand of short-term Islamic finance products for small and medium enterprises with an annual turnover under R5 million in the greater Durban area, KwaZulu-Natal, South Africa. It is specifically intended to investigate whether Islamic finance products can be an alternative to conventional interest-based financial products. Such issues are best investigated through quantitative method of data collection. Quantitative research is explaining phenomena by collecting numerical data that are analysed using mathematically based methods in particular statistics (Aliaga and Gunderson, 2002). Kumar (2011) further adds that quantitative study designs are specific, well structured, have been tested for their validity and reliability, and can be explicitly defined and recognised. Furthermore, Burns and Grove (2005) agrees and states that quantitative research is an objective, formal, systematic process in which numerical data are used to gather information about the world. The design enables the researcher to quantify the problem and understand how prevalent it is by looking for projectable results in a large population.

There is a number of advantages with quantitative research designs. The findings through quantitative study design can be replicated and retested (Kumar, 2011; Balsley, 1970). Williams (2007) agrees and states if the methods are explained in detail it easy to replicate and will have a high reliability. In quantitative research the introduction of research bias is less than in other designs (Kumar, 2011). Kealey & Protheroe (1996) agrees and states quantitative research eliminates subjectivity of judgement.

Quantitative research is more suited to finding out the extent of variation and diversity of any aspect of social life (Kumar, 2011). It focuses to measure the magnitude of an aspect of social life (Kumar, 2011). The results can be reduced to a few numerical statistics and interpreted in a few short statements (Williams, 2007). The results are objective and can be measured so comparisons can be made (Williams, 2007; Matveev, 2002).

Quantitative research focuses on clarity and distinctions between designs and methods of data collection (Kumar, 2011). It specifies both the independent and the dependent variables under investigation (Williams, 2007). Quantitative research also corrects the holistic fallacy. This refers to the perception by the researcher that all aspects of a given situation are congruent, when in fact only those persons interviewed by the researcher may have held that particular view (Matveev, 2002).

3.5.1.1. Positivistic Approach

The study will follow the positivistic approach. The positivistic approach states that the researcher is independent and objective of the research being conducted (Bezuidenhout, 2014). Angen (2000) states that the positivistic approach assumes that there are real world objects apart from the research, hence there is an objective reality. Creswell (1998) further adds that the researcher knows this reality and uses symbols to describe and explaining this objective reality.

There are many advantages using the positivistic approach in this study. By separating the subject and object of our knowledge, the positivistic approach provides an objective reality that the researcher will be able to compare their claims and determine the truth (Angen, 2000). Prediction and control can be achieved. Guba and Lincoln (1994) state that there are common trends of cause and effect that can be used as a foundation for predicting and controlling natural phenomenon. The researcher aims to discover these trends. The positivistic approach achieves empirical verification. The researcher can rely on their perception of the world to provide accurate data (Creswell, 1998). Angen (2000) further adds that the research can be assumed to be value-free. This is achieved is strict methodological processes are followed. In other words, the research will not be influenced by bias and will be objective.

3.5.1.2. Descriptive Research

The study will be descriptive in nature. Descriptive research describes the characteristics of phenomena, relations between variables or relationships between phenomena as accurately as possible (Bezuidenhout, 2014). Kumar (2011) states that descriptive research provides information about certain phenomena. Descriptive research is used to observe, describe and document facets of a situation as it naturally occurs. In the study, the desirability of Islamic finance by SMEs will be investigated.

There are many advantages using the descriptive research in this study. There is no experimental manipulation in the data, as there is in experimental research. (Polit & Hungler, 1999). In descriptive research, often the research data are available which makes it inexpensive and efficient to use (Grimes and Schulz, 2002). Finally, descriptive research employs specific forms of data collection (Polit et al, 1999). These include studies, observations and surveys. In this study, surveys will be utilized.

3.5.2 Construction of the Instrument

In this study an electronic questionnaire was utilized. The research has three objectives to answer the research problem. Five questions were utilized to answer each objective. A total of 15 questions where asked in the survey. In order not to lead the participant to any conclusions, the questions where asked in a random order.

Each question contained only one idea. All the questions were written with neutral language to avoid leading the participant to a specific answer. The questions utilized language that enabled less educated persons to easily understand the question. Using the likert scale, the questions contained response options that are simple, clear, consistent, and include the full range of responses that might occur.

The survey included information on the focus and aims of the research project. It disclosed how the participants' data will be utilized and ensured the participant that there personal information will be confidentially utilized. The survey also indicated the length of the survey. Furthermore, an informed consent letter and letter to gate-keeper was also provided to the participants.

3.5.3 Recruitment of Study Participants

The data was sourced from a database of 5000 businesses. Only SMEs with an annual turnover of under R5 million was considered. The SMEs were harnessed from the greater-durban area which includes Verulam to the north, Hilcrest to the west and Amanzimtoti to the south.

In terms of religion, the participants from all faiths participated. In terms of gender equality, the survey was available to both male and females. Racially, the survey was made available to Indian, White, Black and Coloured. The survey was only available to South

African citizens.

In terms of hierarchy, the decision-makers of the SMEs that was surveyed included the owners, managing directors or chief executive officers and chief financial officers. Only participants that were older than 18 years old participated. All industries were surveyed, excluding those that are not sharia-compliant including: SMEs involved in the alcohol, sex, interest, pork and gambling industries.

3.5.2 Pretesting and Validation

In this study, various techniques was utilized to determine reliability and validity of the research data. These techniques were demonstrated in the pilot study.

3.5.2.1 Reliability

Reliability refers to when another researcher is able to retest the study's data and obtain the same results (Bezuidenhout, 2011; Welman, Kruger and Mitchell, 2006). Mouton (1996: 144) agrees and states that “reliability refers to the fact that different research participants being tested by the same instrument at different times should respond identically to the instrument”.

In establishing reliability, the researcher determined agreement, stability, equivalence and consistency of the research. In terms of agreement, the researcher used the inter-rater technique. This refers to using the same research instrument but different participants (Bezuidenhout, 2011). The researcher conducted the electronic mail surveys but on a group of twelve participants outside of the study's sample population.

In terms of stability, the researcher utilized the test-retest technique. The test-retest technique refers to using the same participants but the same instruments is administered at different times (Bezuidenhout, 2014). The researcher broke the sample group of 12 participants into three groups of four participants. The researcher administered the electronic mail survey to a different group a week apart.

In terms of equivalence, the researcher used the “parallel forms” technique. This technique refers to using different participants and a different research instrument at the same time

(Bezuidenhout, 2011). The researcher used telephonic survey as a different research instrument. Telephonic surveys refers to calling participants and verbally going through the questionnaire (Bezuidenhout, 2014). The researcher conducted telephonic surveys on a group of five participants outside of the pilot sample.

In terms of consistency, the researcher utilized internal consistency. Internal consistency refers to correlating the performance on each item with the performance across participants (Bezuidenhout, 2014). The researcher compared the performance on each item of the electronic mail survey with the performance of all participants. Table 3.1 summarises the reliability techniques applied in the pilot study.

Table 3.1. The reliability techniques applied in the pilot study.

Reliability Techniques			
No	*Techniques*	*Description*	*Application*
1	Agreement: Inter-rater	Using the same research instrument but on different participants.	The researcher conducted the electronic mail surveys but on a group of twelve participants outside of the study's sample population.
2	Stability: Test-retest	Using the same participants but the same instruments is administered at different times.	The researcher broke the sample group of 12 participants into three groups of four participants. The researcher administered the electronic mail survey to a different group a week apart.
3	Equivalence: Parallel Forms	Using different participants and a different research instrument at the same time.	The researcher conducted telephonic surveys on a group of five participants outside of the pilot sample.
4	Consistency: Internal Consistency	Correlating the performance on each item with the performance across participants.	The researcher compared the performance on each item of the electronic mail survey with the performance of all participants.

3.5.2.2 Validity

Validity refers to determining whether the research measured what it was supposed to measure (Benzuidenhout et al, 2014). She further adds that the research instrument that was utilized in the study actually reflects the reality of the construct that was being measured. In other words, do the findings of the research demonstrate what is happening in the given situation (Babbie and Mouton, 2001; and Collis and Hussey, 2003).

In establishing validity, the researcher ascertained face validity, content validity, construct validity and criterion validity. Face validity refers to how representative a research project is ‘at face value,' and if the project is good (Shuttleworth, 2009). In terms of face validity, the researcher determined if the questionnaire looked like what it is supposed too and if it was well designed.

Content validity refers to the estimate of how much a measure represents every single element of a construct (Shuttleworth, 2009). In terms of content validity, the researcher asked participants in the pilot study if the questionnaire is representative of the sample population and if the measurement represents the specific content.

Construct validity refers to how well a research instrument measures up to its claims (Shuttleworth, 2009). In terms of construct validity, the researcher asked participants in the pilot study if the questionnaire measured the demand of short-term Islamic finance for SMEs with a turnover under R5 million. The researcher also questioned the definition of Islamic finance and related concepts are acceptable.

Criterion Validity assesses whether a research instrument demonstrates a certain set of abilities (Shuttleworth, 2009). In terms of criterion validity, the researcher determined if the questionnaire accurately predicted future behaviour and the accuracy of the electronic mail survey in comparison to a telephonic mail survey. Table 3.2 summarises the validity techniques applied in the pilot study.

Table 3.2 The validity techniques applied in the pilot study.

Validity Techniques			
No	*Techniques*	*Description*	*Application*
1	Face Validity	How representative a research project is ‘at face value,' and if the project is good.	The researcher determined if the questionnaire looked like what it is supposed too and if it was well designed.

2	Content Validity	Refers to the estimate of how much a measure represents every single element of a construct.	The researcher asked participants in the pilot study if the questionnaire is representative of the sample population and if the measurement represents the specific content.
3	Construct Validity	How well a research instrument measures up to its claims.	The researcher asked participants in the pilot study if the questionnaire measured the demand of short-term Islamic finance for SMEs with a turnover under R5 million. The researcher also questioned the definition of Islamic finance and related concepts are acceptable.
4	Criterion Validity	Assesses whether a research instrument demonstrates a certain set of abilities.	The researcher determined if the questionnaire accurately predicted future behaviour and the accuracy of the electronic mail survey in comparison to a telephonic mail survey.

3.5.2.3 Pilot Study

This study utilized a pilot study in order to increase the reliability and validity of the study. Pilot studies refer to pre-testing the research instrument (Benzuidenhout et al, 2014). In the pilot study, the researcher tests a small segment of the actual population that is drawn from the sample (Benzuidenhout et al, 2014). However, these participants are not from the actual research project sample.

The pilot study detects possible errors with the research instrument. The research can then modify the research instrument based on feedback from the pilot study (Du Plooy, 2002). The pilot study also helps the researcher to guarantee that there will be mutual understanding of the terms used in the research instrument (Hundley and Teijlingen, 2001).

The pilot study was administered from June 1 to June 22, 2015. A total of 17 participants were drawn from the research population. These participants did not form part of the actual research project sample. The pilot study can be found in Appendix E.

The pilot study was a success and provided a number of informative changes and detected a number errors in the questionnaire. The pilot study proved that the electronic mail survey was adequate research instrument for this study. The pilot study successfully demonstrated that the study is feasible. It assisted in developing the research protocol and demonstrated that it is realistic and workable. The pilot study reflected that the sampling frame and technique are effective. It demonstrated that the recruitment approach is a success.

The pilot study determined what resources should be allocated to the study, namely, in terms of time, finance and technology. The pilot study demonstrated that the data analysis techniques is effective. It helped develop the research question and research plan.

The pilot study revealed a mistake in the title of the research project. It helped remove redundant words and sentences. It helped made the language used in the questionnaire clear and concise. It clarified ambiguous terminology and enhanced the understanding on the terms and concepts used in the questionnaire.

In terms of the questions, a number of questions where rephrased to enhance understanding and remove ambiguity. The questioning techniques were revised. All closed -ended and contingency questions where removed and was replaced with the likert scale. The number of questions where increased from eight to 15. Questions that did not fit in with the research project where removed. Finally, the order of the questions where revised to not lead the participants to a particular conclusion.

3.5.3 Administration of the Questionnaire

The questionnaire was released using an independent online research firm called www.questionpro.com. The survey was uploaded on August 1, 2015. The informed consent letter and the letter of gate-keeper letter was uploaded and attached to the questionnaire. When the questionnaire was released, Questionpro sent out an e-mail survey invite to the participants. If the participants wants to participate in the study, they click on a link that leads them to the questionnaire. They complete the questionnaire and have the option to forward the survey invite to other participants they may know.

The survey invite was released to an initial database of 100 potential participants on August 1, 2015. For the subsequent nine days, the survey invite was released to 500 participants. In total, the questionnaire was sent to 5000 participants in the sample. Of the 5000 participants that received the survey invite, only 94 participants completed the questionnaire. The vast majority did not respond to the survey invite. A number of participants contacted the researcher and indicated that they are ineligible to participate in the study or queried questions that they did not fully understand. The survey was closed on September 1, 2015.

3.6 Analysis of the Data

The analysis of data involves the transformation of raw data into useable, useful, and understandable information (Roberts, 1998). The quantitative method of analysing data was used in this study. The data collected through questionnaires were verified, edited and coded before being incorporated into an excel spreadsheet by the researcher. The data was then provided to a statistician who transferred it into a Statistical Package for Social Sciences (SPSS) software for data analysis purposes. The data was compared and contrasted to the research objectives. The survey instrument was assigned a number that corresponded to each business that had participated in the study. Data collected was finally compiled and presented through graphs and frequency tables.

3.7 Validity and reliability

Cooper and Schindler (2003) state that approaches of reliability are related to the perspectives of time and conditions of stability, equivalence and internal consistency. The research instrument has high reliability if the results obtained are consistent over time that it is used to measure a phenomenon. Validity refers to the strength of final results and whether they can be regarded as accurately defining the real world (Shuttleworth, 2009).

Cronbach's Alpha coefficient was utilized in the study to calculate the internal consistency or reliability of the data. The coefficient measures the internal consistency and reliability that is the average of all possible splitting of the scale items (Malhotra, 2004).

According to Malhotra, Cronbach's Alpha value may lie between 0,4 and 0,6. This value is an acceptable indication of internal consistency. If the value of Cronbach's Alpha is between 0,7 and 0,9 it implies a high correlation between items. However, if Cronbach’s alpha exceeds 0,9 it is deemed unacceptable. If Cronbach’s Alpha value is high, it will provide added confidence in the category. Reliability indicates whether results can be repeatable or be reproducible (Monsen, 1992).

The survey questionnaire of this study consisted of 15 items. Cronbach’s Alpha was > 0.73, which indicated that the scale was reliable.

3.7.1 Bias

The participants may have not disclosed sensitive information which will give an untrue picture of reality.

3.7.2 Validity

Some participants excluded during the sampling process could have responded differently.

3.8 Ethical considerations

Saunders (2007) defines ethics as the standards of behaviours that guide moral choices of people's behaviour and their relationships with others. Research ethics, according to (Noormahomed, 2013), relates to the way the researcher “formulates and clarifies the research topic, designs research and gains access, collects, processes and stores the data, analyses data and writes up the research findings in a moral and responsible way.” Therefore, the research design must be morally defensible and methodically sound.

The ethical considerations were maintained in the current study by:

1. The surveys were self-administered through email via Questionpro with no personal interaction.
2. Participants were given the option to voluntarily accept or decline.
3. Questionnaire surveys did not ask for respondent’s names, address and contact details to maintain anonymity.
4. Contact with participants were limited to emails and telephone with sufficient time provided to avoid stress and discomfort.

5. Researcher remained neutral (Saunders et al., 2007).

3.9 Elimination of bias

Bias is any effect at any stage of investigation or inference tending to produce results that depart systematically from the true values (Thakur, 2003).

The researcher maintained objectivity throughout the study whilst the survey incorporated the following fundamentals:

1. The researcher remained neutral.
2. The research was open to all religions, race groups, ethnicities, gender and ethnicity.
3. The use of closed ended questions to eliminate bias.
4. The surveys were self-administered thus preventing interview bias and provided for more honest feedback.

It is difficult to completely eliminate bias in a research, although possibility to minimise.

3.10 Conclusion

This chapter covered the research methodology and design used in the study. The aim and objectives of the study, and participants and the location of the study were discussed. The sample, data collection and data analysis were explained. Finally, the validity and reliability and elimination of bias of the study was discussed.

The next chapter deals with the presentation, interpretation and discussion of the study's results.

CHAPTER FOUR
PRESENTATION OF RESULTS AND DISCUSSION

4.1. Introduction

This chapter presents and discusses the findings of the survey which examines the desirability for short-term Islamic finance products for SMES with an annual turnover under R5 million in the greater-Durban area, KwaZulu-Natal, South Africa. Data analysis is essentially the process of inspecting, cleaning, transforming and modelling data with the goal of discovering useful, suggesting conclusions and supporting decision making (Ader, Mellenbergh and Hand, 2008).

Firstly, the chapter presents the research instrument. Thereafter, the sample characteristics are discussed. The analysis of the response variables are presented descriptively. Data was analysed using quantitative methods of data analysis.

4.2. Research Instrument

The research instrument consisted of 15 items. Cronbach's Alpha was > 0.73, which indicates that the scale was reliable (Table 4.1).

Table 4.1: Outcome of reliability test

Reliability Statistics	
Cronbach's Alpha	N of Items
.730	15

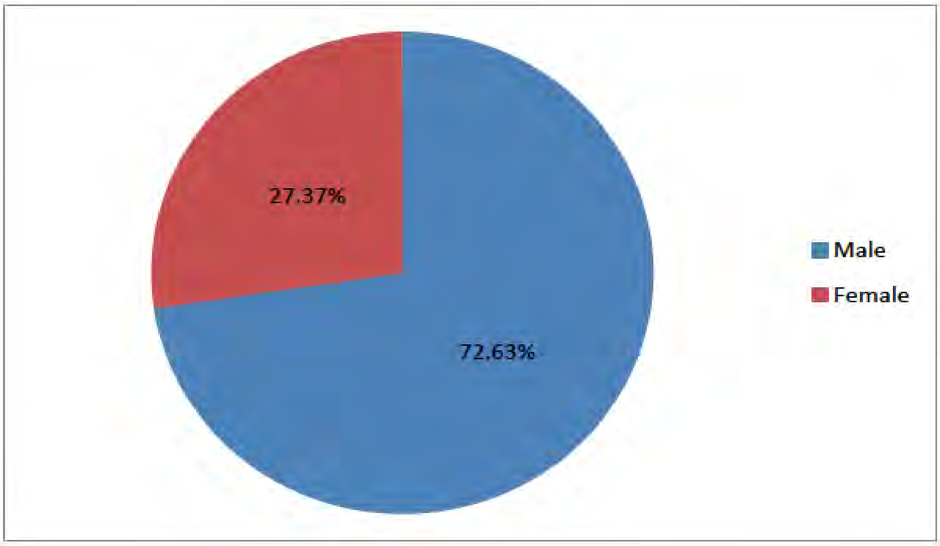
4.3 Sample characteristics statistics

4.3.1 Gender of Participants

There were a total of 94 participants completed the questionnaire. It was found that the majority were male (73%) (Figure 4.1). 27% of participants were female.

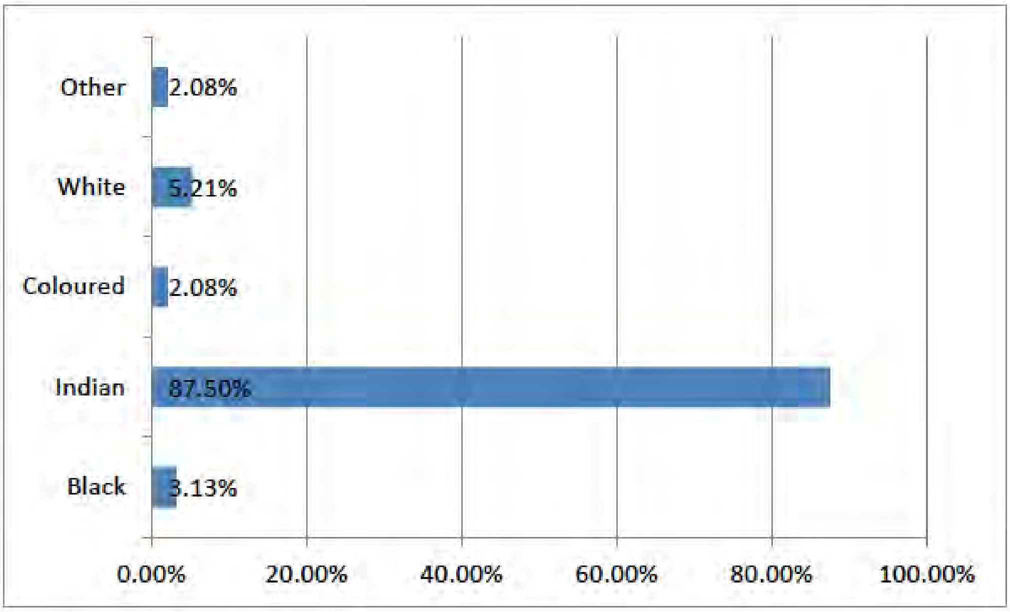
The above analysis indicated that SMEs were dominated by men. The trend is that whilst men were still dominant in business, there is an increase in female executives that are making key decisions such as the need for Islamic financial services.

Figure 4.1. Sex Distribution



4.3.3 Race of Participants

Figure 4.2. Distribution of Race



The majority of participants were Indian (87%) (Figure 4.2). This was followed by white (5%), and Black (3%). 2% of participants were Coloured and 2% identified themselves as

Other.

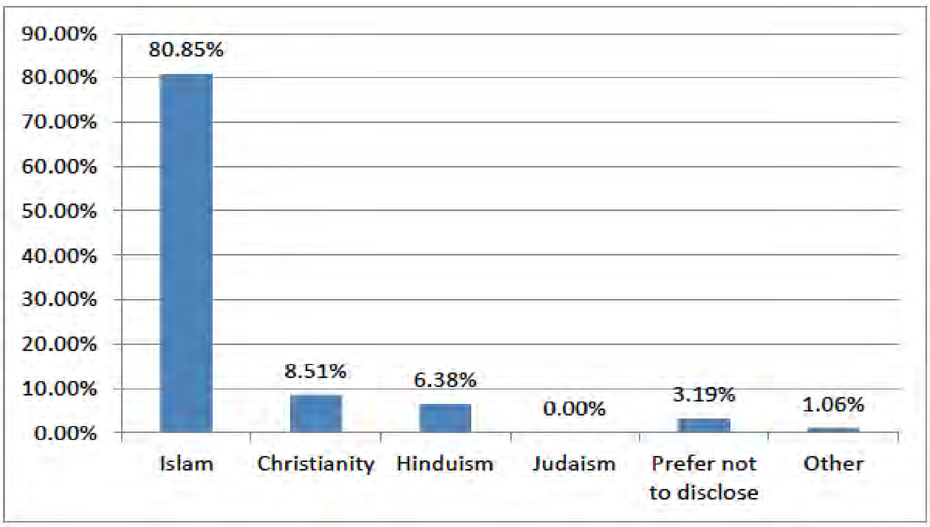
The survey indicated that SMEs were majority Indian owned. It is not uncommon that a large percentage of SMEs were Indian, as Durban has a high concentration of Indians living in the city. Also, majority of the Muslim population is of Indian descent. Furthermore, Indian businesses tend to be family-owned enterprises passed on from generation to generation.

4.3.4 Religion of Participants

The majority of the participants were Muslim (81%), followed by Christianity (8%) and Hinduism (6%) (Figure 4.3). 3% of the participants preferred not to disclose their religious affiliation, whilst 1% stated that they followed religions/beliefs not specified.

It is not surprising that 81% of the participants were Muslims. Islamic finance is the financial services based on the principles of the Qur'an (Kettell, 2012). Naturally, members of the Islamic faith will be drawn to it. Islamic finance does not only cater for the needs of the Muslim population but can service anyone regardless of their race, nationality, ethnicity or religious beliefs. This assertion was demonstrated by participants of other religions participating in the survey.

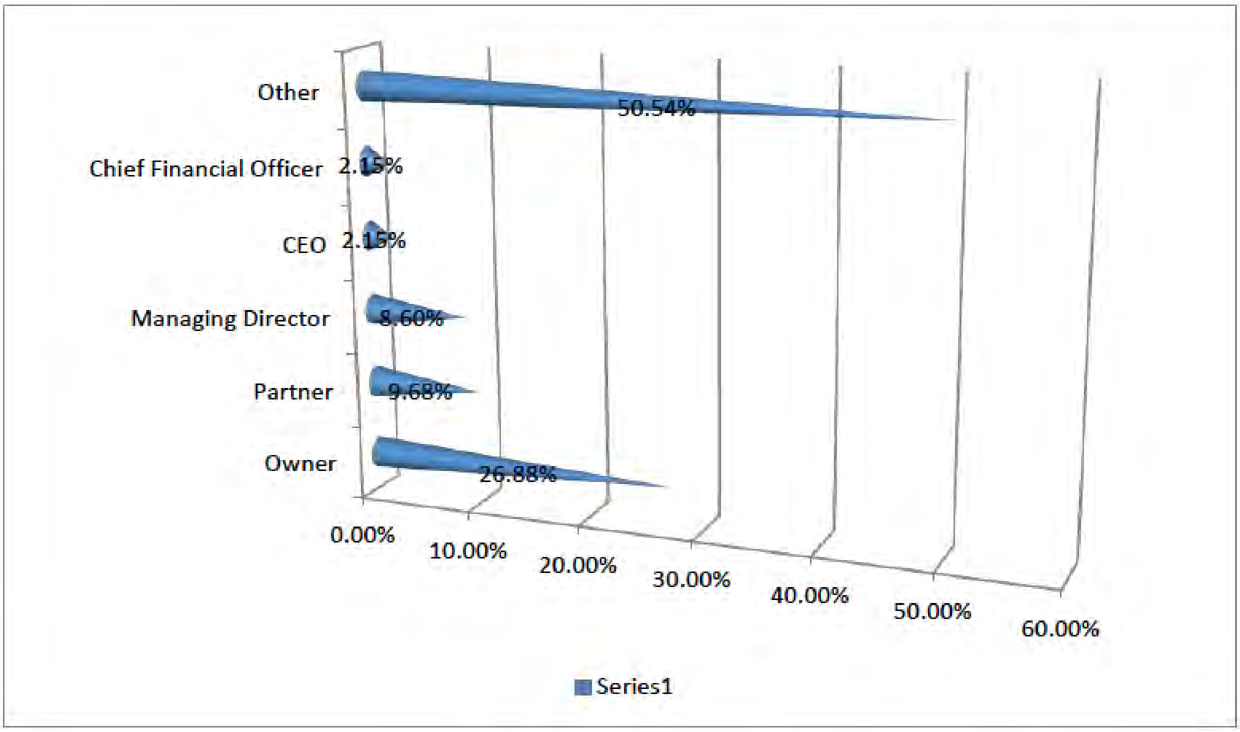
Figure 4.3. Distribution of Religion



4.3.5. Current position of respondents in the organisation

Results showed that over a quarter of the participants were owners, and 10% mentioned of being in a partner in the business (Figure 4.4). 9% of participants stated that they were Managing Directors, 2% were Chief Executive Officers and 2% were Chief Financial Officers. Over 50% of participants stated they held other decision-making positions which is worrisome because we do not know whether they hold a decision-making ability in the SME.

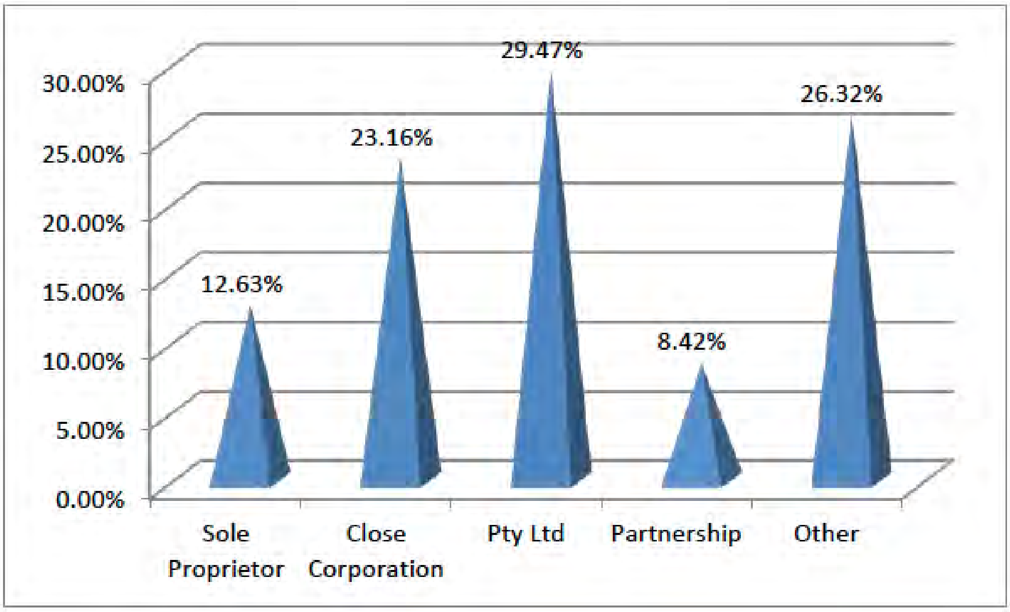
Figure 4.4. Position held in the company



4.3.6. Type of Businesses

The survey indicated that more than a quarter of participants had PTY (Ltd) businesses, whilst 23% had Close Corporations (Figure 4.5). 13% of participants were Sole Proprietors and 8% belonged to Partnerships. Over a quarter of participants stated they belonged to other forms of businesses.

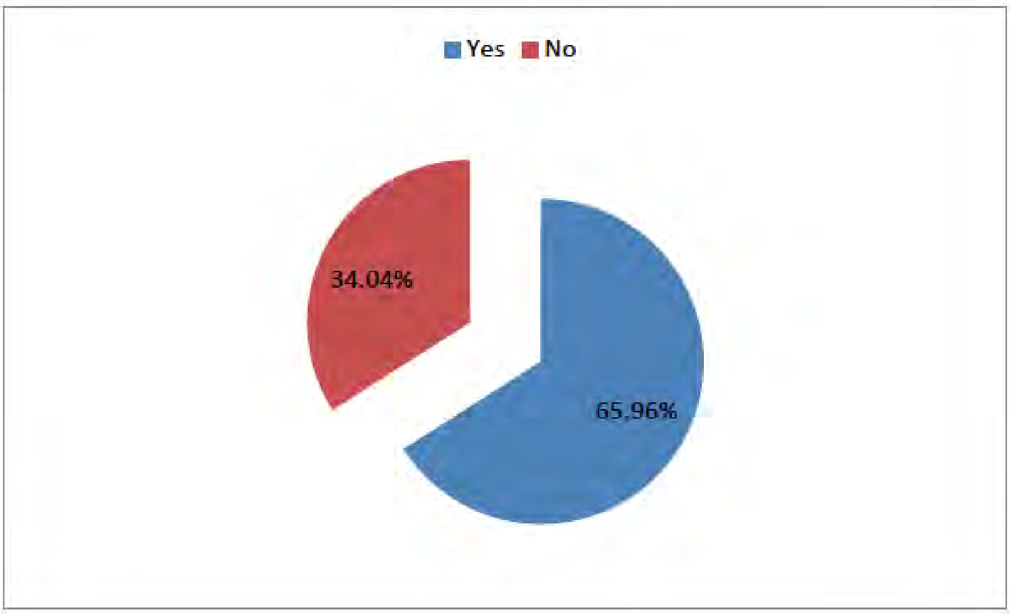
Figure 4.5. Type of Businesses



4.3.7. Businesses that operated in the greater-Durban area.

The survey indicated that 66% of participants operated a business in the greater-Durban area (Figure 4.6). 34% of participants operated a business outside of Durban.

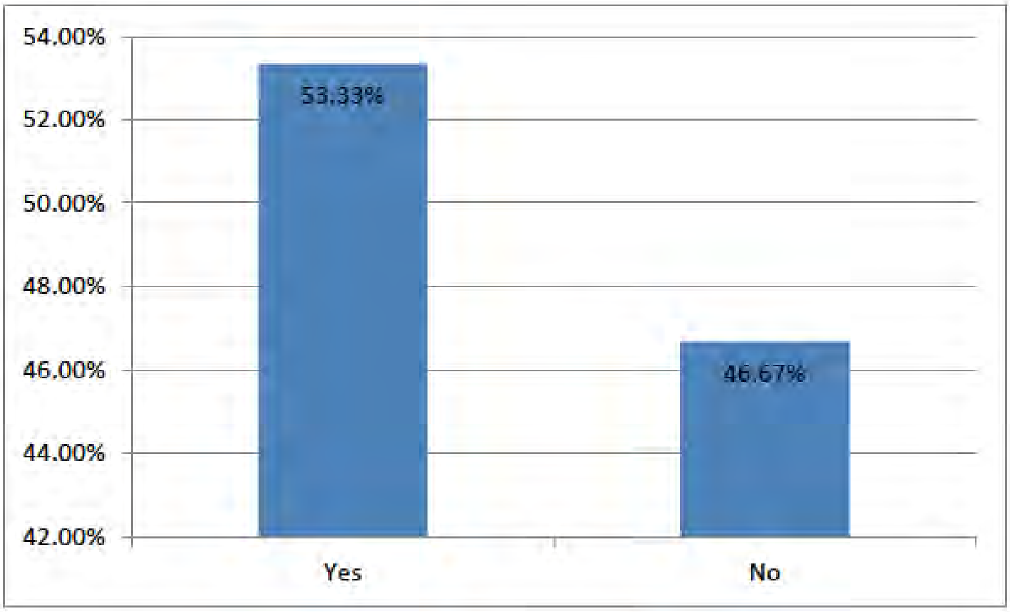
Figure 4.6. Businesses that operated in the greater-Durban area.



4.3.8. Turnover under R5 million

The survey indicated that more than half of the participants (53%) had a turnover under R5 million (Figure 4.7). 47% of the participants had a turnover over R5 million.

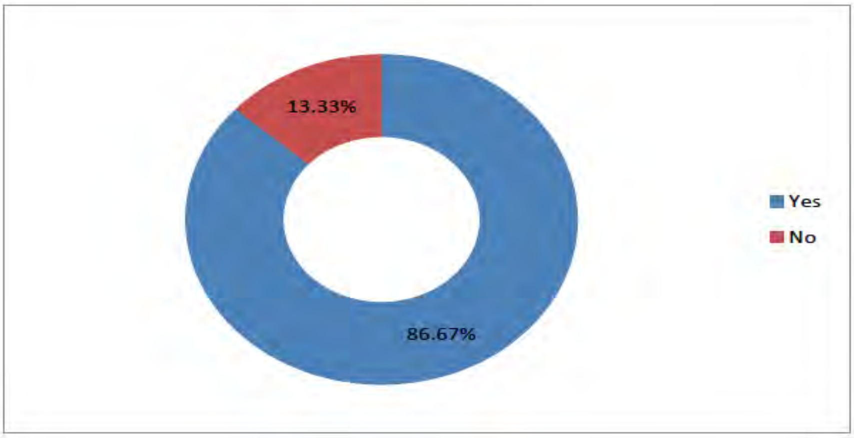
Figure 4.7: Turnover under R5 million



4.3.9. Trading for more than a year

The majority of the participants (87%) highlighted that they were in the business for more than a year (Figure 4.8). 13% of participants were trading for less than a year.

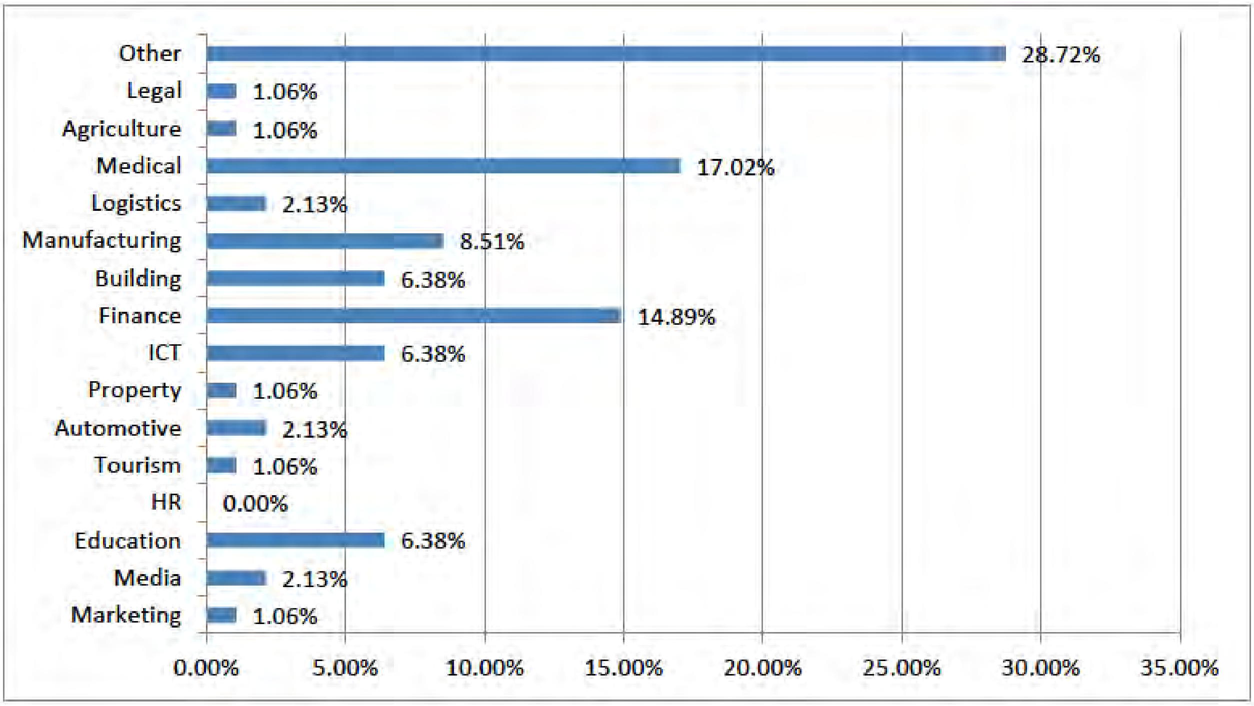
Figure 4.8: Trading for more than a year



4.3.10. The organisations business segment (Industry)

The survey indicated that 17% of the participants were from Medical industry followed by Finance (15%) and Manufacturing (9%) respectively (Figure 4.9). 6% belonged to the Education, Building and ICT sectors respectively. Logistics, Automotive and the Media industries held 2% respectively. Legal, Agriculture, Property, Tourism and Marketing industries held 1% respectively. Finally, 29% of participants stated their industries belonged to the 'Other' category.

Figure 4.9: The organisations business segment (Industry).



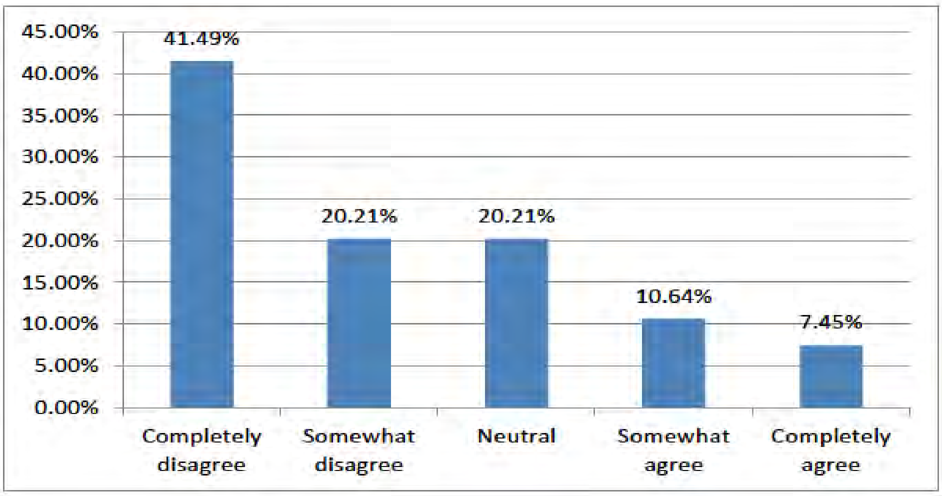
4.4 Descriptive Statistics

4.4.1. Participants agreement with the conventional finance model

Majority of participants (41%) completely disagreed that they agreed with the conventional finance model. This was followed by somewhat disagreed (20%), neutral (20%), somewhat agree (11%) and completely agree (7%).

More than 61% of participants did not agree with the conventional finance model, whilst 18% of participants agreed (Figure 4.10). The lack of agreement of the conventional finance model stems from the practice that conventional financial institutions charge interest rates that SMEs cannot afford (Mahembe, 2011). Other factors include financial institutions that provide SMEs with credit will want the terms of the finance to be followed and that the SMEs act in a manner that will ensure that the finance will be repaid (Mahembe, 2011). However, this is difficult for SMEs to achieve this.

Figure 4.10: Participants agreement with the conventional finance model



4.4.2. Participants agreement with paying interest

The survey indicated that the majority of participants (75%) completely disagreed with paying interest (Figure 4.11), and 80% completely agreed with not paying interest under Islamic Finance (Figure 4.12).

7% of participants somewhat disagreed with paying interest (Figure 4.11). This was followed by neutral (6%), somewhat agree (9%) and completely agree (2%). In Figure 4.12, participants somewhat agreed (8%) not to pay interest under Islamic finance. This was followed by neutral (10%), somewhat disagree (1%) and completely disagreed (1%).

82% of participants disagreed with paying interest (Figure 4.11) and 88% agreed not pay interest under Islamic finance (Figure 4.12). In Islam, interest and usury is forbidden. Any transaction that deals with interest is null and void. Beck et al. (2008) states that high interest rates that SMEs cannot afford is one of the systematic problems why SMEs do not have access to finance. The lack of desirability of interest by participants indicates that an alternative financial model is needed.

Figure 4.11: Participants agreement with paying interest

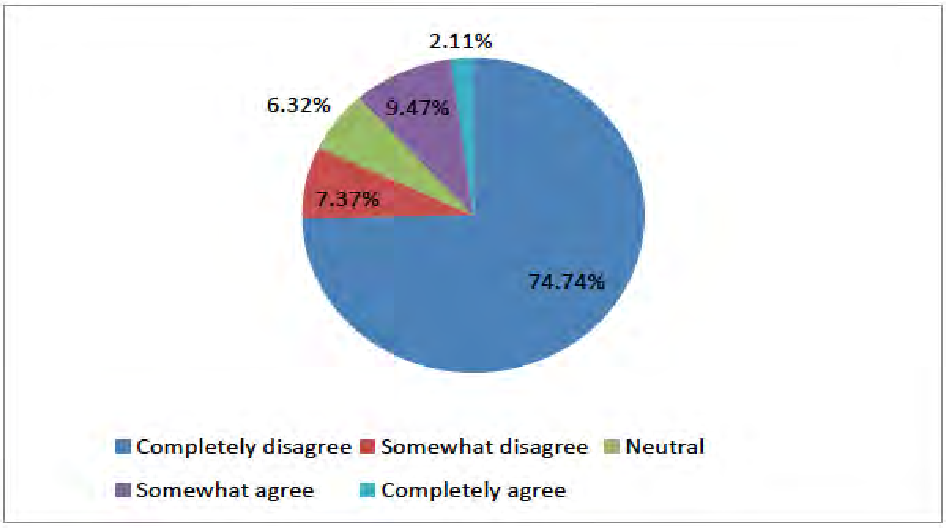
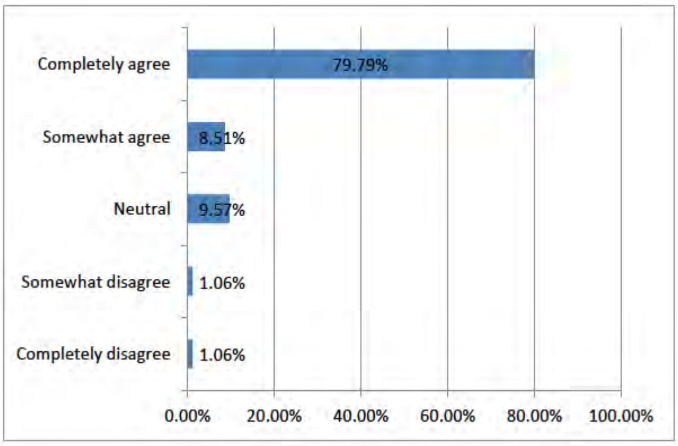


Figure 4.12: Participants agreement with not paying interest under Islamic Finance.



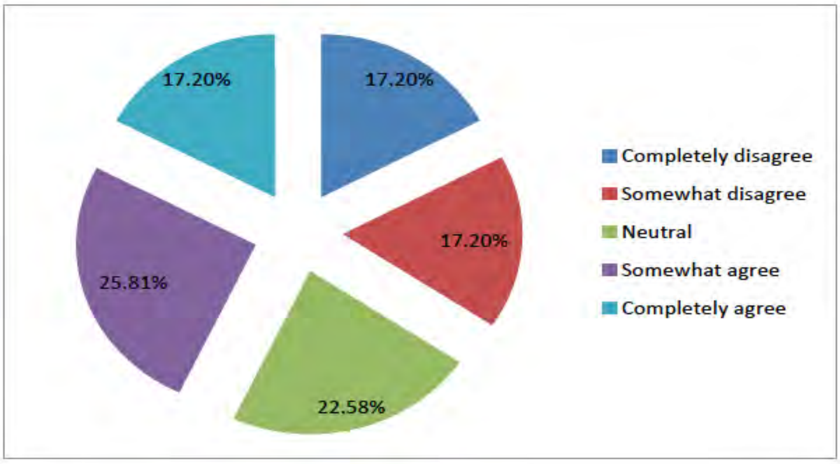
The Quran, Islam holiest book, has extensively commented on interest and usury. “Those who devour usury will not stand except as stands one whom the evil one by his touch has driven to madness”. The Quran continues: “Trade is like usury but Allah hath permitted trade and forbidden usury. Those who after receiving direction from their Lord desist shall be pardoned for the past; their case is for Allah (to judge); but those who repeat (the offence) are companions of the fire: they will abide therein (for ever)” (Quran, Surah II: 275).

4.4.3. Participants agreement with providing suretyship

Majority of the participants (26%) somewhat agreed with providing suretyship (Figure 4.13). This was followed by neutral (23%), completely disagree (17%), somewhat disagree (17%) and completely agree (17%) respectively.

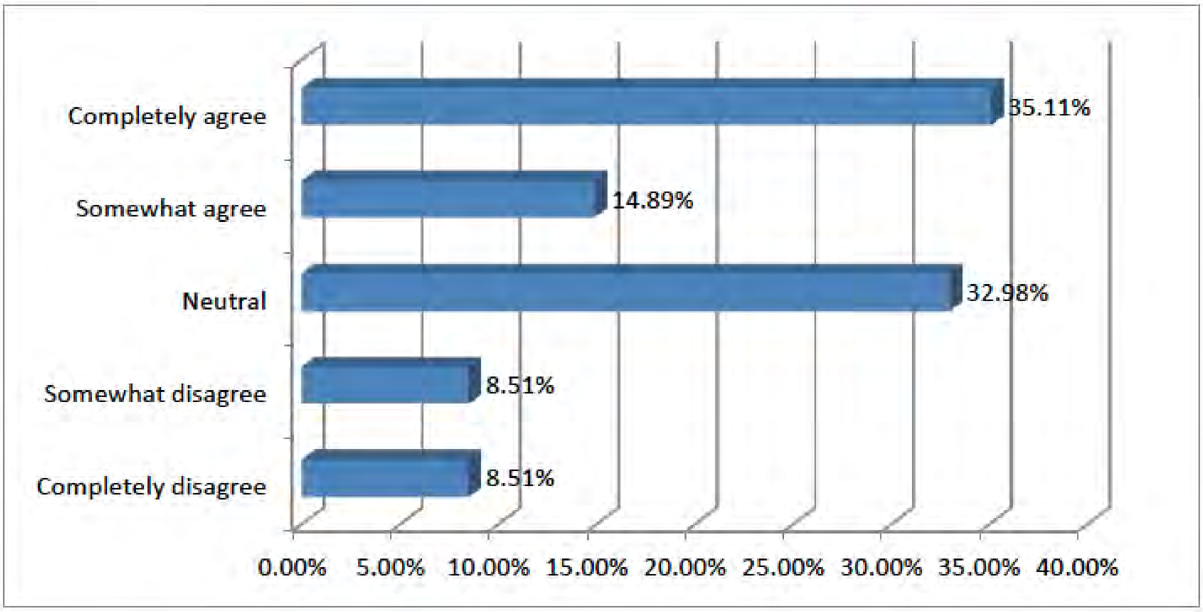
In Figure 4.14, 35% of participants completely agreed with not providing suretyship under Islamic finance. This was followed by neutral (33%), somewhat agree (15%), somewhat disagree (8,5%) and completely disagree (8.5%) respectively.

Figure 4.13: Participants agreement with providing suretyship



The survey indicated about a third of the participants (34%) disagreed with the business practice of providing suretyships (Figure 4.13). Half of the participants (50%) agreed with not providing suretyships under Islamic Finance (Figure 4.14). When conventional banks finance SMES, in addition to charging high interest, their terms include SMEs to provide suretyship as a guarantee for the finance. In most cases, the suretyship is equal to the amount of the loan. If the SMEs fails to repay back the loan, conventional banks are entitled to the suretyship. In Islamic finance, suretyship does not exist as both the parties (the Islamic financial institution and the SME) enter the relationship as partners (Noormahomed, 2013). The Islamic finance institution bears the risk to provide finance to the SME.

Figure 4.14: Participants agreement with not providing suretyships under Islamic Finance.

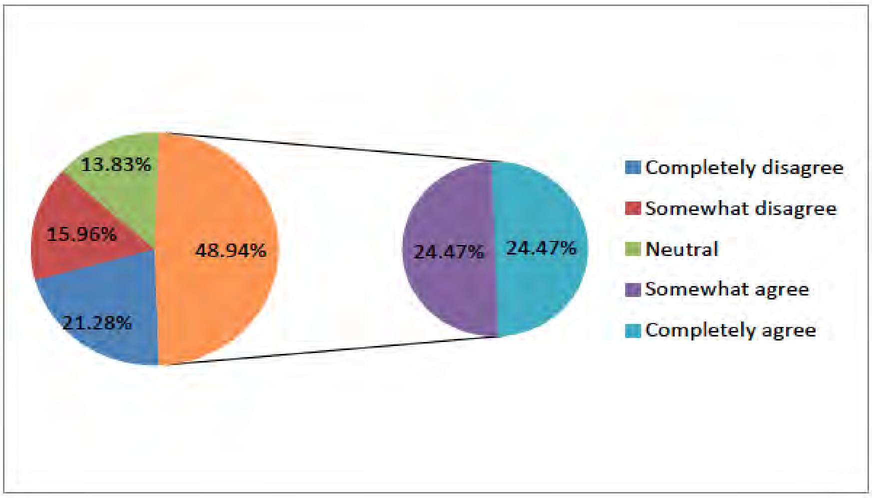


4.4.4. Participants agreement with being personally liable if the business venture fails after securing financing from a conventional financial institution.

The survey indicated that 24% of participants either completely agreed and 24% of participants somewhat agreed with being personally liable if the business venture fails after securing financing from a conventional financial institution (Figure 4.15). This was followed by completely disagree (21%), somewhat disagree (16%) and neutral (14%).

According to Figure 4.15, 49% of the participants agreed with being personally liable if the business venture fails after securing financing from a conventional financial institution. In Islamic law, ethics is a central component and justice is imperative in all transaction (Absa, 2011). Therefore, honesty, fair trade and humility are virtues that are urged. SME owners feel morally obligated to be personally liable if the business venture fails and will pay back the conventional bank the finance amount. However, as indicated earlier, they do not want to pay interest or provide suretyship on the amount owed.

Figure 4.15. Participants agreement with being personally liable if the business venture fails after securing financing from a conventional financial institution.



4.4.5. Participants preference for an alternative source of funding rather than the conventional interest-based model.

The majority of participants completely agree (74%) that an alternative source of funding rather than the conventional interest-based model is needed (Figure 4.16). This is followed by somewhat agree (19%), neutral (5%), and somewhat disagree (2%) respectively.

Figure 4.16. Participants preference for an alternative source of funding rather than the conventional interest-based model.

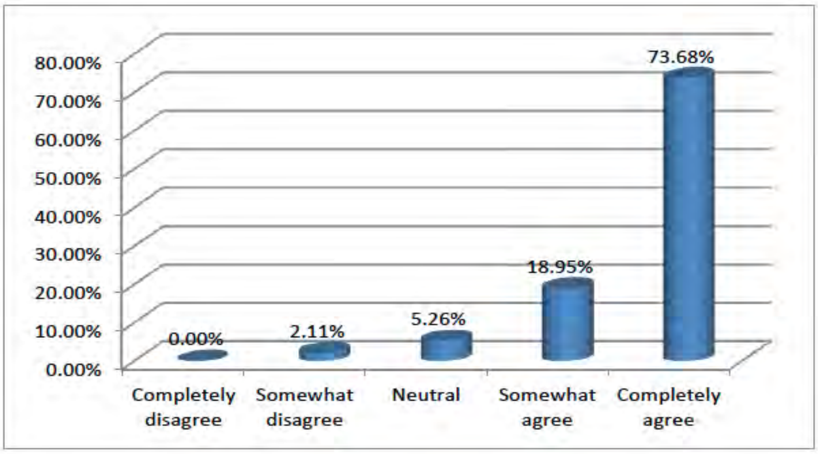


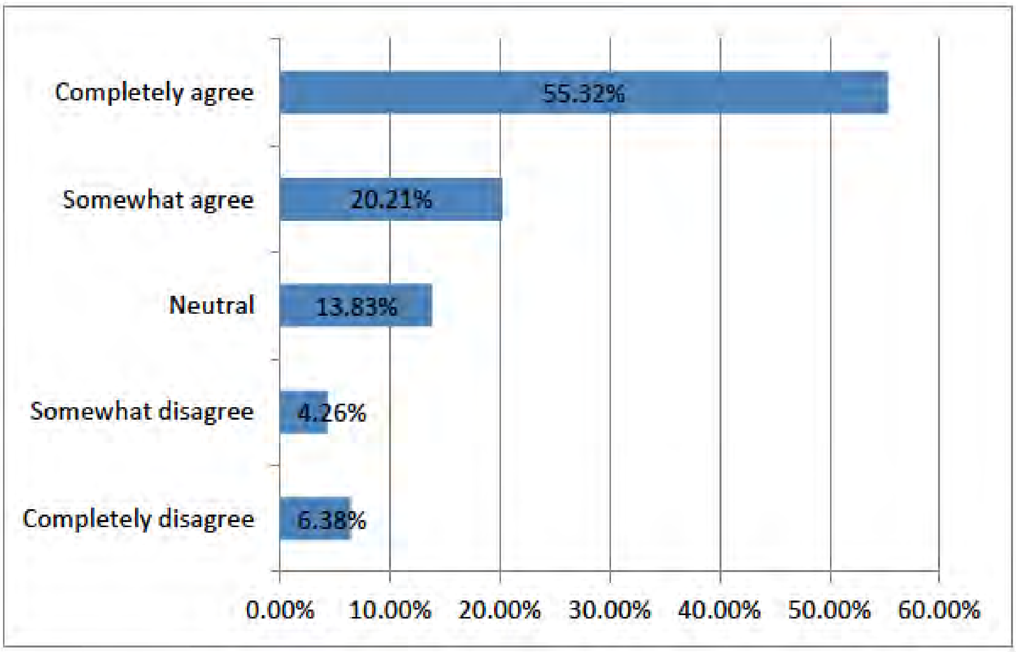
Figure 4.16 shows that 93% of the participants completely agreed that they would prefer an alternative source of funding rather than the conventional interest-based model. Herrington et al (2010) states like their global peers, SMEs in South experience a lack of financing options. Furthermore, there is a sector of economically active SMEs that cannot secure financing from banks, the public sector or capital markets (Mahembe, 2011). An alternative source of funding will plug the financing gap.

4.4.6. Participants utilization of Islamic finance

Majority of participants (55%) would have utilized Islamic finance before this study (Figure 4.17). This is followed by somewhat agree (20%), neutral (14%), completely disagree (6%) and somewhat disagree (4%) respectively.

More than 75% of the participants agreed that they would consider utilizing Islamic finance before this study (Figure 4.17). This is not surprising as 80% of participants belonged to the Islamic faith. Islamic finance is derived from the Shariah law which in turn is derived from the Quran, the holiest book in Islam.

Figure 4.17: Participants utilization of Islamic finance

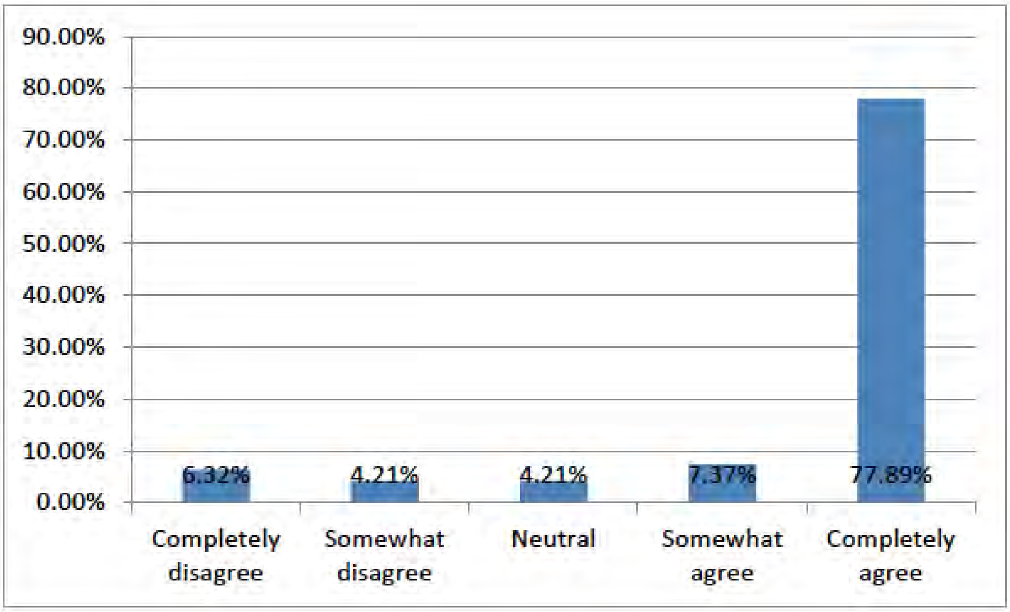


4.4.7. Participants agreement that Islamic finance not being offered to non-shariah compliant industries such the pork, alcohol and gambling industries.

The survey indicated that the majority of participants (78%) completely agree that Islamic finance not being offered to non-shariah compliant industries such the pork, alcohol and gambling industries (Figure 4.18). This is followed by somewhat agree (7%), completely disagree (6%), neutral (4%) and somewhat disagree (4%) respectively.

The result showed that 85% of the participants completely agreed with Islamic finance not being offered to non-shariah compliant industries such the pork, alcohol and gambling industries (Figure 4.18). Islamic finance does not deal in the alcohol, tobacco, gambling, pork products, prostitution, insurance and conventional banking (Noormahomed, 2013; and Kettell, 2012). These industries are against the Shariah law and furthermore, can be deemed unethical. Furthermore, since the majority of participants are of the Islamic faith, they would naturally be supportive of Islamic finance being offered to non-shariah compliant industries.

Figure 4.18: Participants agreement that Islamic finance not being offered to non-shariah compliant industries such the pork, alcohol and gambling industries.



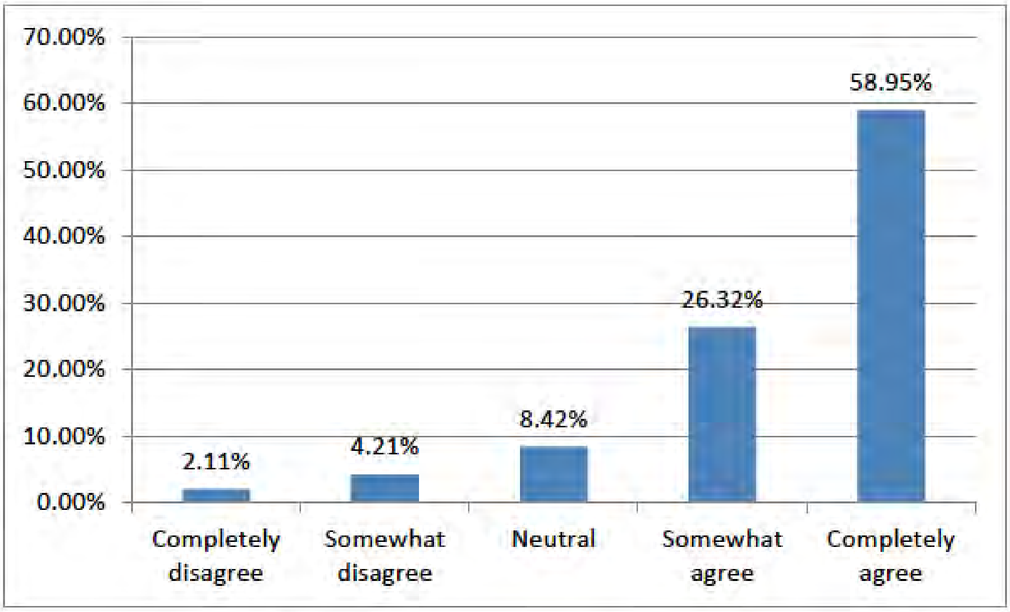
4.4.8. Participants utilization of Islamic finance's profit loss sharing financial instrument.

The majority of participants completely agree (59%) that they would utilize Islamic finance's profit loss sharing financial instrument (Figure 4.19). This is followed by somewhat agree (26%), neutral (8%), somewhat disagree (4%), and completely disagree (2%) respectively.

The result showed that the majority of the participants would utilize the profit loss sharing (PLS) financial instrument (85%) (Figure 4.19). PLS is used in the mudarabah contracts which are partnership loans between the financial institution and its client (Kettell, 2012: 297). The bank provides the finance whilst the borrower provides the effort and expertise. Losses are completely borne by the bank whilst profits are shared at a predetermined ratio.

PLS is attractive as the SME will not have to provide suretyship or pay interest but has to provide expertise to the partnership. The Islamic financial institution will further bear the risk of the venture.

Figure 4.19: Participants utilization of Islamic finance's profit loss sharing financial instrument.

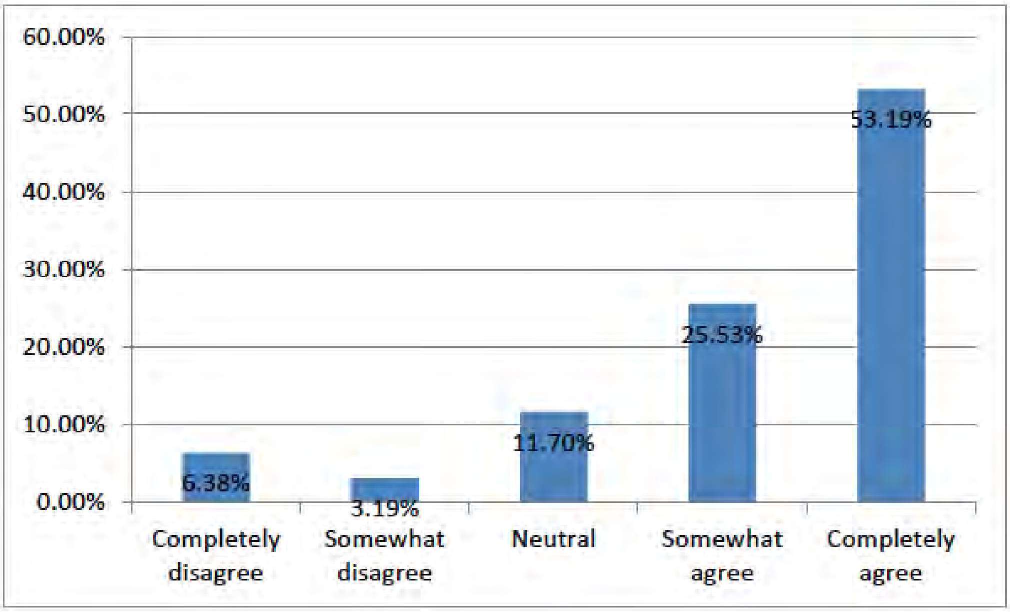


4.4.9. Participants agreement in creating a joint venture with the financial institution and becoming business partners when utilizing Islamic finance.

The survey indicated that 53% of the participants completely agree with creating a joint venture with the financial institution and becoming business partners when utilizing Islamic finance (Figure 4.20). This is followed by somewhat agree (25%), neutral (12%), 6% completely disagree and somewhat disagree (3%) respectively.

In utilizing profit loss sharing, more than three-quarters of the participants (78%) completely agreed with creating a joint venture with the financial institution and becoming business partners (Figure 4.20). Rather than viewing the financial institution as a creditor, the majority of the participants are open to the financial institutions being a valued partner.

Figure 4.20: Participants agreement in creating a joint venture with the financial institution and becoming business partners when utilizing Islamic finance.

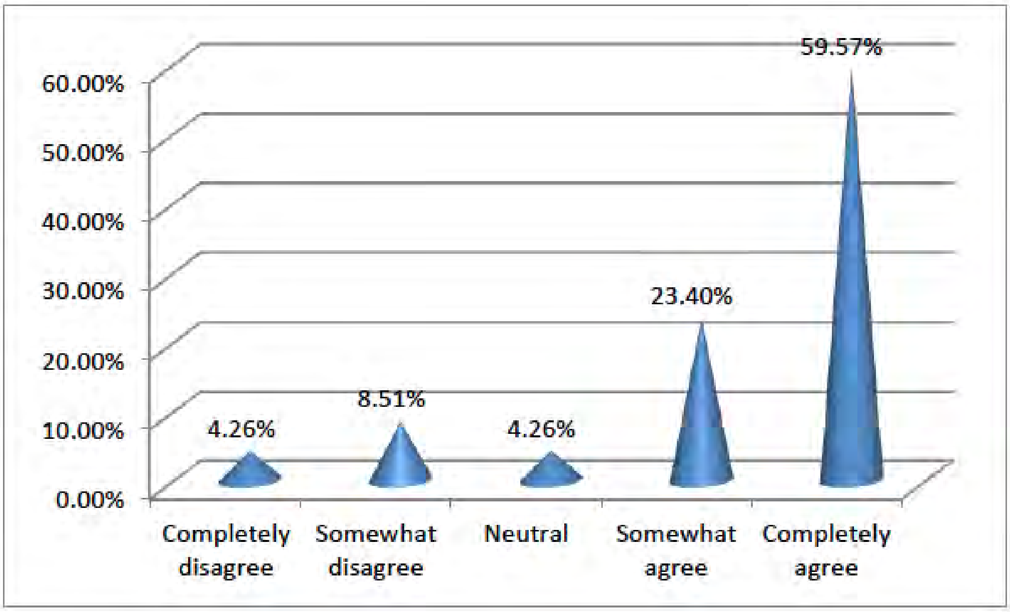


4.4.10. Participants agreement with sharing the profits in pre-agreed proportions of the joint venture with the financial institution.

The majority of participants completely agree (60%) with sharing the profits in pre-agreed proportions of the joint venture with the financial institution (Figure 4.21). This is followed by somewhat agree (23%), somewhat disagree (8%), neutral (4%) and completely disagree (4%) respectively.

In utilizing profit loss sharing, the majority of the participants (83%) agreed with sharing the profits in pre-agreed proportions of the joint venture with the financial institution (Figure 4.21). This confirms that participants are opened to the profit-loss sharing financial instrument. The amount of profit the financial institution receives or losses it bears is dependent on the amount of capital it injects into the SME. Kettell (2012) notes that whilst the entrepreneur has final control over the business, major investment decisions, has to be approved by the bank. This ensures that the bank's investment is safeguard from risky behaviour.

Figure 4.21: Participants agreement with sharing the profits in pre-agreed proportions of the joint venture with the financial institution.

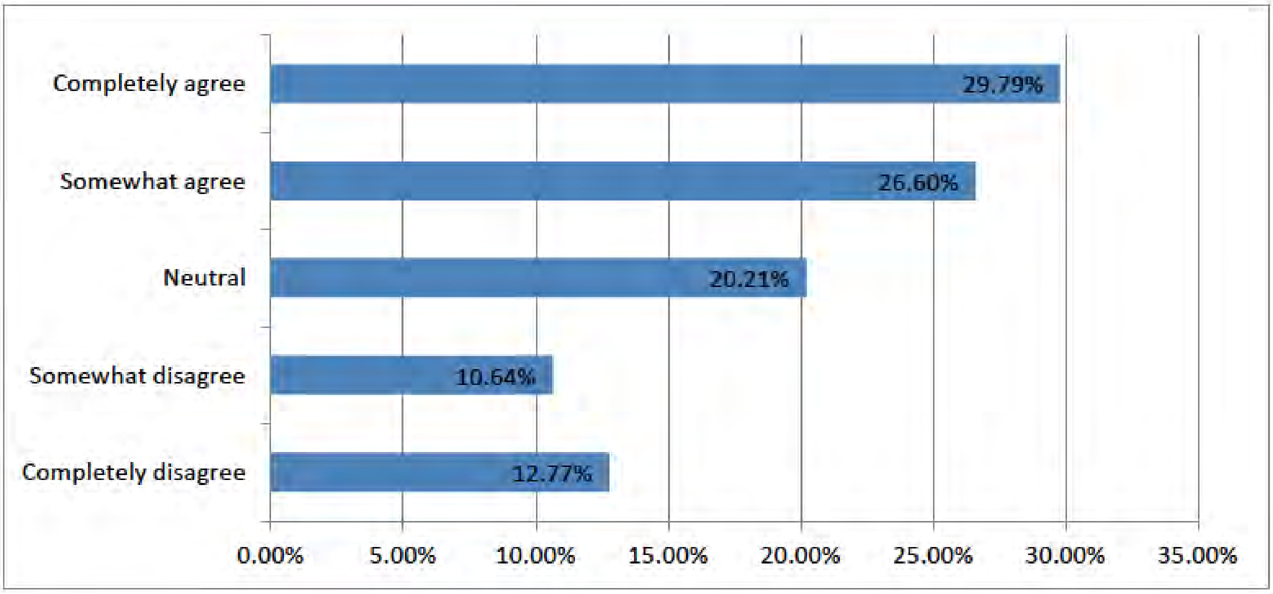


4.4.11. Participants agreement with the financial institution bearing the financial loss of the joint venture if it fails when utilizing Islamic finance.

30% of participants completely agree with the financial institution bearing the financial loss of the joint venture if it fails (Figure 4.22). This is followed by somewhat agree (27%), neutral (20%), completely disagree (13%), and somewhat disagree (11%) respectively.

Just over half of the participants (57%) agreed that in utilizing profit loss sharing, the financial institution bears the financial loss of the joint venture if it fails (Figure 4.22). The bank provides the loan whilst the SME provides the effort and expertise. Thus, the bank bears the risk.

Figure 4.22: Participants agreement with the financial institution bearing the financial loss of the joint venture if it fails when utilizing Islamic finance.

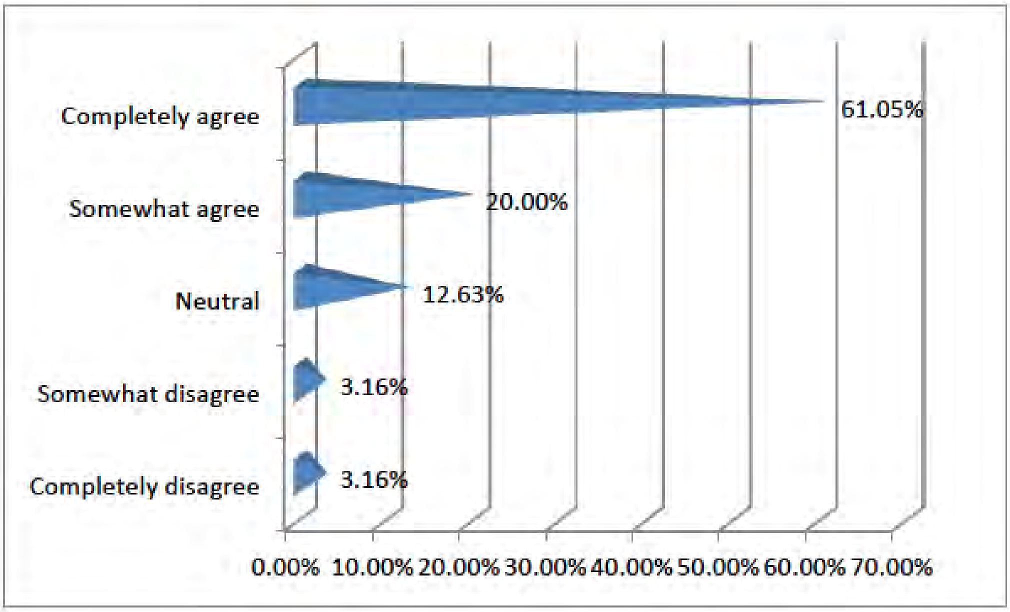


4.4.12. Participants view on whether profit-loss sharing financial instrument is a better alternative than the interest-based model.

The majority of participants completely agree (61%) that profit-loss sharing financial instrument is a better alternative than the interest-based model (Figure 4.23). This is followed by somewhat agree (20%), neutral (13%), somewhat disagree (3%) and completely disagree (3%) respectively.

The majority of the participants (81%) positively reported that the profit loss sharing financial instrument is a better alternative than the interest-based model (Figure 4.23). This confirms that there is a demand for Islamic finance and unhappiness with the interest-based model. 6% of participants stated that they are not inclined to use Islamic financial services and 20% of participants are unsure.

Figure 4.23: Participants on view whether profit-loss sharing financial instrument is a better alternative than the interest-based model.



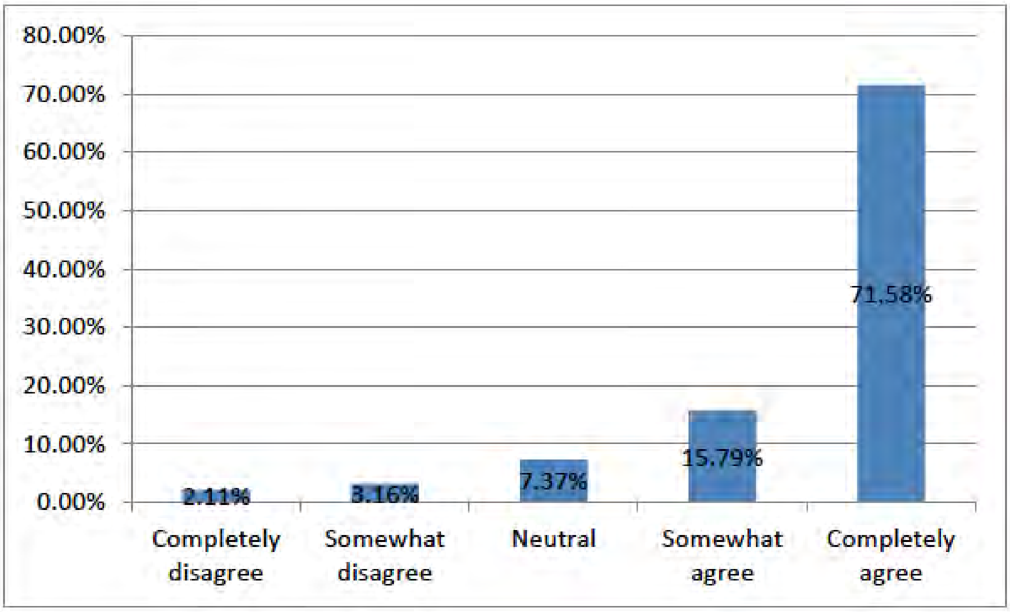
4.4.13. Participants view on whether Islamic finance can be an alternative to the conventional interest-based model.

The survey indicated that the majority of participants (72%) completely agreed with Islamic finance being an alternative to the conventional interest-based model (Figure 4.24). This was followed by somewhat agree (16%), neutral (7%), somewhat disagree (3%) and completely disagree (2%) respectively.

When asked about whether Islamic finance can be an alternative to the conventional interest-based model, 88% of the respondents agreed to the statement (Figure 4.24). 5% of participants disagreed with Islamic finance being an alternative to conventional finance, whilst 7% were unsure.

Some assumptions why participants would not be inclined to use Islamic financial services in future and moreover for those who were unsure could have possibly been due to some participants feeling that the Islamic banks or conventional bank offering Islamic finance products in South Africa did not have a compelling enough Shariah compliant offering. South Africa is a non-Islamic state and conventional banking services are the standard banking approach in the country.

Figure 4.24: Participants view on whether Islamic finance can be an alternative to the conventional interest-based model.



4.4.14. Association between agreeing with paying interest and religion of the participant

Chi-squared test of association was used to find any association between demographic variable with the statements regarding Islamic banking. It was found that more participants with religion of Islam completely disagreed with regards to paying interest ($p<0.01$).

Religion was also associated with 'do you feel the profit loss sharing financial instrument', 'would you prefer an alternative source of funding', 'would you utilize the profit loss sharing financial', 'do you feel Islamic finance can be an alternative', and 'would you consider utilizing Islamic finance before (Table 4.2). No other variable were associated with the statements regarding Islamic finance.

Table 4.2: Association between agreeing with paying interest and religion of the participant

Statements		Religion		Chi-Square	p-value
		Other	Islam		
Do you agree with paying interest?	Completely disagree	5	66	39.76	<0.001
	Somewhat disagree	6	1		
	Neutral	2	4		
	Somewhat agree	6	3		
	Completely agree	0	2		
Do you feel the profit loss sharing financial instrument is a better alternative than the interest-based model?	Completely disagree	1	2	22.51	<0.01
	Somewhat disagree	2	1		
	Neutral	6	6		
	Somewhat agree	7	12		
	Completely agree	3	55		
Would you prefer an alternative source of funding	Somewhat disagree	2	0	22.50	<0.01
	Neutral	1	4		
	Somewhat agree	9	9		
	Completely agree	7	63		
Would you utilize the profit loss sharing financial	Completely disagree	0	2	20.22	<0.01
	Somewhat disagree	3	1		
	Neutral	2	6		
	Somewhat agree	10	15		
	Completely agree	4	52		
Do you feel Islamic finance can be an alternative	Completely disagree	1	1	21.26	<0.01
	Somewhat disagree	2	1		
	Neutral	2	5		
	Somewhat agree	8	7		
	Completely agree	6	62		
Would you consider utilizing Islamic finance before	Completely disagree	2	4	17.02	0.002
	Somewhat disagree	2	2		
	Neutral	7	6		
	Somewhat agree	4	15		
	Completely agree	4	48		

4.5 Conclusion

This chapter presented and discussed the findings of the survey. The study was significant since it confirmed the need for Islamic financial services amongst SMEs with a turnover under R5 million in KwaZulu-Natal. The need was primarily driven by religious beliefs and the need to conform to Shariah. Islamic finance was regarded as an alternative approach to conventional finance since it excluded interest and suretyship which was prohibited by Islam.

Based on the above premise, Islamic finance is an alternative to the conventional interest-based model. Financial institutions should endeavour develop Islamic finance products for SMEs.

The chapter presented the sample characteristics and descriptively presented the rest of the data from the participants. The next chapter presents the final chapter of the study and discusses the findings from the literature review and from the research. Recommendations and implications of the study with concluding remarks will be discussed.

CHAPTER FIVE
CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter presents the findings of the study, conclusions, implications of the study and recommendations. The final section contains recommendations for further research and the summary of the chapter.

5.2 Finding from the study

The section below discussed the findings from the literature review and findings of the survey.

5.2.1 Findings from the literature review

The literature review provided the researcher with a comprehensive understanding of the nature of SMEs, the demand and supply of credit to SMEs, and the credit and support gap to SMEs. The financial approaches and differences including the overview, theory and concepts related to Islamic financial services was also examined. The survey questions was formulated from characteristics and themes of the findings in the literature review.

The literature review discussed the various definitions of SMEs, the role and importance of SMEs to the economy and an overview of the demand for credit from SMEs. Depending on the size of the SME, their needs for credit will vary. In the supply of credit, three different sectors providing SMEs with credit: the public sector; the commercial banking sector; and donors, NGOs and the private sector. Though there is a huge demand for credit by SMEs and their exists various options to supply the credit, there exists a credit gap. SMEs either do not qualify for financing or cannot afford the high interest rate attached to credit from a conventional bank. Islamic finance is poised to fill the credit gap.

The literature also examined the principles that are prohibited by the Shariah law. They included unethical behaviour, interest, uncertainty, injustice and exploitation of the needs of others.

SMEs with Muslim owners will benefit from Islamic financial services by virtue of their Shariah compliant status. These owners would be at peace knowing their financial dealings are permissible from an Islamic point of view. Non-Muslim SMEs are also keen to transact in an ethical manner. They also will utilise Islamic finance products for their social and economic needs.

Financial institutions will greatly benefit from developing Islamic finance products as it will lead to greater revenue streams and retention of existing clients. The Islamic finance market is largely untapped in South Africa. Failure to take advantages will result in financial institutions losing out to their competitors.

5.2.2 Findings from the primary research

The findings below from the survey are presented below in relation to the research questions.

The objectives of the study were:

Objectives 1

To establish whether SMEs would prefer an alternative source of funding rather than the conventional interest-based model.

Literature review pertaining to objective 1

1. The literature review articulated that due to the existence of a credit gap in the financing of SMEs, an alternative source of funding is required for SMEs. Chimucheka and Rungani (2011) states that SMEs are less likely to apply for financing due to the high interest rates. This is further confirmed by Beck et al (2008). An alternative source of funding where interest is not a factor is needed.

2. SMEs are also more likely to partake in risky behaviours once they receive credit via the conventional finance model (OECD, 2007). Thus, the financial institutions needs to play a greater role in the operations of the business to prevent SMEs from partaking in risky behaviour. This is not the case in the conventional interest-based

model.

Data analysis

1. An overwhelming majority of participants, 61% (41% completely disagree and 20% somewhat disagree) in the survey indicated that they disagree with the conventional finance model reflecting a strong need and desire for an alternative source of funding.

2. Interest is a central component for the conventional finance system. 82% of participants disagreed with paying interest, reflecting a strong need for an alternative source of funding where interest does not play a part.

3. The majority of participants, 93%, agreed that they would prefer an alternative source of funding rather than the conventional interest-based model.

Objectives 2

To establish the perceptions of SMEs for Islamic finance.

Literature review pertaining to objective 2

1. The literature review established the need for Islamic finance by emphasising the role that ethics plays in Islamic finance through consciousness, religious tradition and self-interest. Religion is considered a primary driver towards the consideration of Islamic finance (Mancosa, 2011).

2. The need for Islamic finance is driven primarily by a desire to ensure that finance is within the confines of Shariah Law. Certain principles within conventional banking are prohibited including interest, nature of uncertainty, unethical behaviour, injustice and exploitation. Islamic finance offer an alternative banking solution to conventional banking which is permissible for to use in a Shariah compliant manner (Absa, 2011).

Data analysis

1. More than 75% of the participants agreed that they would consider utilizing Islamic finance before this study. This is not surprising as 80% of participants belonged to the Islamic faith. Islamic finance is derived from the Shariah law which in turn is derived from the Quran, the holiest book in Islam.

2. The majority of participants, 88%, agreed they would not pay interest under Islamic finance. In Islam, interest is forbidden. Beck et al (2008) states that high interest rates that SMEs cannot afford are one of the systematic problems why SMEs do not have access to finance. The lack of desirability of interest by participants indicates that an alternative financial model is needed.

3. Half of the participants (50%) agreed with not providing suretyships under Islamic finance. In Islamic finance, suretyship does not exist as both the parties (the Islamic financial institution and the SME) enter the relationship as partners (Noormahomed, 2013). The Islamic finance institution bears the risk to provide finance to the SME. An arrangement favoured by SMEs.

4. The survey indicated that 85% of the participants completely agreed with Islamic finance not being offered to non-shariah compliant industries such the pork, alcohol and gambling industries. Islamic finance does not deal with these industries (Noormahomed, 2013; and Kettell, 2012). These industries are against the Shariah law and furthermore, can be deemed unethical. Furthermore, since the majority of participants are of the Islamic faith, they would naturally be supportive of Islamic finance not being offered to non-shariah compliant industries.

5. The majority of participants, 88%, viewed Islamic finance as an alternative to the conventional interest-based model. This indicated a favourable perception of Islamic finance.

Objectives 3

To establish whether SMEs would prefer Islamic finance's profit loss sharing financial instrument rather than the conventional interest-based model.

Literature review pertaining to objective 3

1. Profit loss sharing financial instrument is implemented in Mudarabah contracts. This refers to partnership loans between bank and borrowers (Kettell, 2012). The bank provides the loan whilst the borrower provides the effort and expertise. Losses are completely borne by the bank whilst profits are shared at a predetermined ratio. Kettell (2012) notes that whilst the entrepreneur has final control over the business, major investment decisions, has to be approved by the bank.

Data analysis

1. More than three-quarters of the participants (78%) completely agreed with creating a joint venture with the financial institution and becoming business partners. Rather than viewing the financial institution as a creditor, the majority of the participants are open to the financial institutions being a valued capital-contributing partner.

2. The majority of the participants (83%) agreed with sharing the profits in pre-agreed proportions of the joint venture with the financial institution. This confirms that participants are opened to the profit-loss sharing financial instrument.

3. Just over half of the participants (57%) agreed that in utilizing profit loss sharing, the financial institution bears the financial loss of the joint venture if it fails. The bank provides the loan whilst the SME provides the effort and expertise. Thus, the bank bears the risk.

4. The majority of the participants (81%) positively reported that the profit loss sharing financial instrument is a better alternative than the interest-based model. This confirms that there is a demand for Islamic finance and unhappiness with the interest-based model.

5. The majority of participants completely agree (85%) that they would utilize Islamic finance's profit loss sharing financial instrument. This indicates a strong desire of PLS over the conventional interest-based instruments.

5.3 Implications of the study

The researcher makes the following recommendations to stakeholders based on the findings:

- Financial Institutions
- SMEs

5.3.1 Financial Institutions

Financial institutions should develop and innovate Islamic financial products and services in the following manner:

1. Many SMEs do not qualify or cannot afford conventional interest-based finance. There exists a niche is the market to provide Islamic finance to SMEs. Currently, there are only limited options for Islamic finance.

2. The study has confirmed that an alternative source of funding is needed for SMEs. SMEs confirmed in this study that Islamic finance is an attractive option. Financial institutions need develop Islamic finance products or finance products that do not evolve interest and are morally sound.

3. Financial institutions should consider repositioning themselves as investors, rather than financiers. SMEs are open to creating joint venture with financial institutions, where the risk and reward are shared jointly.

4. There needs to be a diversification of Islamic finance products. Currently, no institution of the profit loss sharing financial instrument. Financial institutions need develop other Islamic finance products as well.

5.3.2 SMEs

1. SMEs should turn to financial institutions offering Islamic finance products and services for financing. High interest rates and suretyship is a contributing factor to the decline of SMEs who undertake financing through the conventional interest-

based model. The ethical nature of Islamic finance will strengthen their businesses and profit margin.

2. Islamic finance is only offered to businesses that are shariah compliant. SMEs who wish to be finance by Islamic finance should strife to make their businesses shariah compliant.

5.4 Recommendations to solve the research problem

The research problem stated that SMEs face multiple barriers when trying to secure conventional financing. If they are able to secure the financing needed through conventional banking, SMEs shoulder the risk irrespective whether the venture is successful or not. This study sought to explore if Islamic finance's profit loss sharing financial instrument can be alternative source of funding to the conventional interest-based model.

Recommendation to solve the research problem include:

1. Test out other Islamic financial instruments to see if they are better suited as financing options for SMEs.

2. There exists other financial instruments other than conventional interest-based and Islamic financial instruments that can solve financing conundrums for SMEs. They need to be tested to see if they are suitable.

3. Government and the NGO sector can provide interest-free financing to SMEs.

5.5 Recommendations for future studies

The researcher recommends that further research be undertaken on Islamic finance products. More scholarly knowledge is needed in this sector and the needs of the South African market need to be explored.

Islamic finance products offered internationally need to be compared with local offerings. South Africa is not an innovator in Islamic finance products and the need to develop local distinguished offerings with the framework of the Shariah law is needed.

Furthermore, the researcher recommends that a sample of SMEs be provided financing using the PLS instrument by a financial institution and resulting interaction be studied. This study had 80% of participants that belonged to the Islamic faith. Future studies need to have a more representative sample. This study did not engage in a comparative study of Islamic financial products available in South Africa. Future studies should compare the local offerings.

5.6 Conclusion

The study contributed to the existing body of knowledge in the field of Islamic financial services which acknowledges the sustainable growth of Islamic financial services in KwaZulu-Natal. The study also contributed to the existing body of knowledge in the field of SME financing and addressed concerns of the lack of access of financing SMEs experienced.

The study found that there is a demand for short-term Islamic finance products for small and medium enterprises with an annual turnover under R5 million in the greater-Durban area, KwaZulu-Natal, South Africa. Profit loss sharing financial instrument is a perfect financing instrument for SMEs as it mitigates the financial risk. This will positively contribute to the SMEs survival rate. Furthermore, Islamic finance products alleviate the SME financing conundrum.

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APPENDIX A – Ethical Clearance Approval

UNIVERSITY OF KWAZULU-NATAL
INYUVESI YAKWAZULU-NATALI

01 September 2015

Mr Aarif Saib (205500227)
Graduate School of Business
Westville Campus

Dear Mr Saib,

Protocol reference number: HSS/0730/015M
Project title: Investigating the demand of short-term Islamic finance products for small and medium enterprises with an annual turnover under R5 million in the greater Durban area, KwaZulu-Natal, South Africa

Approval Notification – Amendment Application

This letter serves to notify you that your application and request for an amendment received on 03 August 2015 has now been approved as follows:

- Change in Research Instrument (Questionnaire)

Any alterations to the approved research protocol i.e. Questionnaire/Interview Schedule, Informed Consent Form; Title of the Project, Location of the Study must be reviewed and approved through an amendment /modification prior to its implementation. In case you have further queries, please quote the above reference number.

PLEASE NOTE: Research data should be securely stored in the discipline/department for a period of 5 years.

The ethical clearance certificate is only valid for period of 3 years from the date of issue. Thereafter Recertification must be applied for on an annual basis.

Best wishes for the successful completion of your research protocol.

Yours faithfully

....

Dr Shenuka Singh (Chair)

/ms

Cc Supervisor: Dr Abdullah Kader
Cc Academic Leader Research: Dr Muhammad Hoque
Cc School Administrator: Ms Zarina Bullyraj

Humanities & Social Sciences Research Ethics Committee
Dr Shenuka Singh (Chair)
Westville Campus, Govan Mbeki Building
Postal Address: Private Bag X54001, Durban 4000
Telephone: +27 (0) 31 260 3587/8350/4557 **Facsimile:** +27 (0) 31 260 4609 **Email:** ximbap@ukzn.ac.za / snymanm@ukzn.ac.za / mohunp@ukzn.ac.za
Website: www.ukzn.ac.za

APPENDIX B – Informed Consent Letter

UNIVERSITY OF KWAZULU-NATAL

Graduate School of Business and Leadership

Dear Respondent,

Master Of Commerce In Leadership Research Project

Researcher: Aarif Saib (071 896 7876)

Supervisor: Dr Abdullah Kader (082 901 0225)

Research Office: Ms E Ximba 031-2603587

I, Aarif Saib, am a Masters of Commerce in Leadership student in the Graduate School of Business and Leadership, at the University of KwaZulu-Natal. You are invited to participate in a research project entitled Investigating the demand of short-term Islamic finance products for small and medium enterprises with an annual turnover under R5 million in the greater Durban area, KwaZulu-Natal, South Africa.

The aim of this study is to determine if short-term Islamic finance products can be an alternative source of funding for small and medium enterprises with an annual turnover under R5 million.

Through your participation I hope to understand is Islamic finance is an alternative to conventional financing for SMEs, what is the scope of the market and what types of Islamic finance products is best suited for SMEs. The results of this survey is intended to contribute to scholarly research on Islamic finance and SME funding. The study is also indented give a basis for financial institutions to offer Islamic finance to SMEs.

Your participation in this project is voluntary. You may refuse to participate or withdraw from the project at any time with no negative consequence. There will be no monetary gain from participating in this research project. Confidentiality and anonymity of records identifying you as a participant will be maintained by the Graduate School of Business and Leadership, UKZN.

If you have any questions or concerns about participating in this study, please contact me or my supervisor at the numbers listed above.

It should take you about 10 minutes to complete the questionnaire. I hope you will take the time to complete the questionnaire.

Sincerely

Investigator's signature______________________________ Date__________________

UNIVERSITY OF KWAZULU-NATAL
Graduate School of Business and Leadership

Master Of Commerce In Leadership Research Project

Researcher: Aarif Saib (071 896 7876)

Supervisor: Dr Abdullah Kader (082 901 0225)

Research Office: Ms E Ximba 031-2603587

CONSENT

I____(full names of participant) hereby confirm that I understand the contents of this document and the nature of the research project, and I consent to participating in the research project. I understand that I am at liberty to withdraw from the project at any time, should I so desire.

____________________ ____________________

Signature of Participant Date

APPENDIX C – Letter to the Gatekeeper

December 17, 2015

To Whom It May Concern:

PERMISSION TO CONDUCT RESEARCH AS PART OF MASTER OF COMMERCE IN LEADERSHIP

Name: Aarif Saib Student No: 205500227

Dissertation Topic: Investigating the demand of short-term Islamic finance products for small and medium enterprises with an annual turnover under R5 million in the greater Durban area, KwaZulu-Natal, South Africa.

We confirm that the above student is registered at the University of UKZN for the MASTER OF COMMERCE IN LEADERSHIP Programme. It is a requirement of their Programme that the student undertakes a practical research project in his final year of study.

Typically, this project will be a "practical problem solving" exercise, and necessitates data gathering through questionnaires or personal interviews.

Your assistance in permitting access to your organization for purposes of conducting the research is most appreciated. Please be assured that all information gained from the research will be treated with the utmost confidentiality. Furthermore, should you wish any result/s or findings from the research "to be restricted" for an agreed period of time, this can be arranged. The confidentiality of information and anonymity of personnel will be strictly adhered to by the student.

If permission is granted, kindly confirm this by signing off on the following:
"I am aware of the nature and extent of the document and I am satisfied with all the obligations imposed therein."

Please note that additional information or conditions can be supplied by you.

Name in Full: ____________________

Designation: ____________________

Company Name & Stamp: ____________________

Thank you for your assistance in this regard.

Yours sincerely

____

Dr. A Kader

APPENDIX D – Questionnaire

University Of KwaZulu-Natal
Graduate School of Business and Leadership

Master Of Commerce In Leadership Research Project

Researcher: Aarif Saib (071 896 7876)

Supervisor: Dr Abdullah Kader (082 901 0225)

QUESTIONNAIRE

Dear Respondent,

The topic of my research is: “Investigating the demand for short-term Islamic finance products for small and medium enterprises with an annual turnover under R5 million in the greater Durban area, KwaZulu-Natal, South Africa.”

Islamic finance adheres to the principles of the Sharia Law (the moral code and religious law of the Islamic religion). A key concept of Islamic finance is the prohibition of the charging and acceptance of interest. Due to interest being forbidden, Islamic finance has developed a financial instrument referred to as profit loss sharing (PLS). PLS is a contractual arrangement between two or more transacting parties, which allows them to pool their resources to invest in a project to share in profit and loss. In Islamic finance, the financial institution and the entrepreneur have an equal stake in the outcome of the business.

For example, Company XYZ wants to develop a new product but needs R1 million. Bank ABC provides Company XYZ with the R1 million in terms of Islamic finance. The monies are not a loan but rather an investment. Bank ABC and Company XYZ agrees that if the venture is successful Bank ABC will be paid back the investment and R100000 of the profits to be paid over a period of two years. If the venture fails, Bank ABC will lose their investment and Company XYZ will lose their time and effort developing the product. Company XYZ will not be held liable to pay back the investment.

In addition to interest being prohibited, Islamic finance cannot be offered to non-shariah compliant industries such the pork, alcohol and gambling industry.

Now with a clear understanding of the profit and loss financial instrument of Islamic finance, please answer the following questionnaire and e-mail the responses to saib.aarif@gmail.com.

PERSONAL PARTICULARS									
Name				Surname					
Age		Date of Birth		Sex		Male		Female	
Race	African		White		Coloured		Indian		Other	
Religion	Islam		Christianity		Hinduism		Judaism		Other	
Nationality	Yes	No	If not a South African citizen, please do not proceed with the questionnaire.						

CONTACT DETAILS									
Work Number		Cell Number		Fax Number					
E-mail Address									
Position held within the company									
Owner		Partner		MD		CEO		CFO	
If you do not have an equity stake in the business, please get consent from the owner via the letter to gate-keeper document attached.									

COMPANY PARTICULARS									
Name of Company									
Trading Name									
Registration No									
Business Type									
Sole Proprietor		Close Corporation		Company		Partnership		Other	
Business Address									
If the business operates outside of the eThekwini region, please do not proceed with the questionnaire.									
Turnover		If the turnover is above R5 million per annum, please do not proceed with the questionnaire.							
Trading History	___Years	If the trading history is below one year, please do not proceed with the questionnaire.							
Industry Type									
Marketing		Media		Education		HR		Tourism	
Automotive		Property		ICT		Finance		Building	
Manufacturing		Logistics		Medical		Agriculture		Legal	
Other (specify)									
If the business is involved in alcohol, pork and gambling industries please do not proceed with the questionnaire.									

QUESTIONNAIRE											
1	Do you feel content with the conventional interest-based model?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
2	Do you agree with the profit loss sharing financial instrument's principle of creating a joint venture with a financial institution?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
3	Do you agree with the interest paying model?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
4	Do you agree with not paying interest under Islamic Finance?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
5	In utilizing profit loss sharing, do you agree with sharing the profits in pre-agreed proportions of the joint venture with the financial institution?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
6	Do you agree with not providing suretyships under Islamic Finance?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
7	Do you agree with being personally liable if the business venture fails after securing financing from a conventional financial institution?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
8	In utilizing profit loss sharing, do you agree with the financial institution bearing the financial loss of the joint venture if it fails?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
9	Do you agree with Islamic finance not being offered to non-shariah compliant industries such the pork, alcohol and gambling industries?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
10	Do you agree with the business practice of providing suretyships?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
11	Do you feel the profit loss sharing financial instrument is a better alternative than the interest-based model?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
12	Would you prefer an alternative source of funding rather than the conventional interest-based model?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
13	Would you utilize the profit loss sharing financial instrument?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
14	Do you feel Islamic finance can be an alternative to the conventional interest-based model?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	
15	Would you consider utilizing Islamic finance before this study?	Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	

Please e-mail the responses to saib.aarif@gmail.com.

For any queries about the questionnaire, please contact Humanities and Social Sciences Research Ethics Committee:

Mariette Snyman
Tel: +27 31 260 8350
Email: hssreclms@ukzn.ac.za

APPENDIX E – Pilot Study

UNIVERSITY OF KWAZULU-NATAL

Graduate School of Business and Leadership

Master Of Commerce In Leadership Research Project

Researcher: Aarif Saib (071 896 7876)

Supervisor: Dr Abdullah Kader (082 901 0225)

QUESTIONNAIRE

Dear Respondent,

The topic of my research is: "Investigating the demand for short-term Islamic finance products for small and medium enterprises with an annual turnover under R5 million in the greater Durban area, KwaZulu-Natal, South Africa."

Islamic finance adheres to the principles of the Sharia Law (the moral code and religious law of the Islamic religion). A key concept of Islamic finance is the prohibition of the charging and acceptance of interest. Due to interest being forbidden, Islamic finance has developed a financial instrument referred to as profit loss sharing (PLS). PLS is a contractual arrangement between two or more transacting parties, which allows them to pool their resources to invest in a project to share in profit and loss. In Islamic finance, the financial institution and the entrepreneur have an equal stake in the outcome of the business.

For example, Company XYZ wants to develop a new product but needs R1 million. Bank ABC provides Company XYZ with the R1 million in terms of Islamic finance. The monies are not a loan but rather an investment. Bank ABC and Company XYZ agrees that if the venture is successful Bank ABC will be paid back the investment and R100000 of the profits to be paid over a period of two years. If the venture fails, Bank ABC will lose their investment and Company XYZ will lose their time and effort developing the product. Company XYZ will not be held liable to pay back the investment.

In addition to interest being prohibited, Islamic finance cannot be offered to non-shariah compliant industries such the pork, alcohol and gambling industry.

Now with a clear understanding of the profit and loss financial instrument of Islamic finance, please answer the following questionnaire and e-mail the responses to saib.aarif@gmail.com.

PERSONAL PARTICULARS									
Name				Surname					
Age		Date of Birth		Sex		Male		Female	
Race	African		White		Coloured		Indian		Other	
Religion	Islam		Christianity		Hinduism		Judaism		Other	
Nationality	Yes	No	If not a South African citizen, please do not proceed with the questionnaire.						

CONTACT DETAILS									
Work Number		Cell Number		Fax Number					
E-mail Address									
Position held within the company									
Owner		Partner		MD		CEO		CFO	
If you do not have an equity stake in the business, please get consent from the owner via the letter to gate-keeper document attached.									

COMPANY PARTICULARS									
Name of Company									
Trading Name									
Registration No									
Business Type									
Sole Proprietor		Close Corporation		Company		Partnership		Other	
Business Address									
If the business operates outside of the eThekwini region, please do not proceed with the questionnaire.									
Turnover		If the turnover is above R5 million per annum, please do not proceed with the questionnaire.							
Trading History	___Years	If the trading history is below one year, please do not proceed with the questionnaire.							
Industry Type									
Marketing		Media		Education		HR		Tourism	
Automotive		Property		ICT		Finance		Building	
Manufacturing		Logistics		Medical		Agriculture		Legal	
Other (specify)									
If the business is involved in alcohol, pork and gambling industries please do not proceed with the questionnaire.									

QUESTIONNAIRE				
Have you ever been granted a financial facilitating by a lending institution	Yes		No	
Did you agree with the interest paying model?	Yes		No	
Did you agree and are you comfortable with the business practice of providing suretyships?	Yes		No	
Would you prefer an alternative source of funding rather than the conventional interest-based model?	Yes		No	

Have you heard of Islamic finance before this questionnaire?							Yes		No	
Would you consider utilizing Islamic finance? *If no, please discontinue this questionnaire.*							Yes		No	

The profit and loss financial instrument is better than the interest-based model									
Strongly Disagree		Disagree		Neutral		Agree		Strongly Agree	

Please e-mail the responses to saib.aarif@gmail.com. For any queries about the questionnaire, please contact Humanities and Social Sciences Research Ethics Committee: Mariette Snyman - +27 31 260 8350.