

Empowering Strategies of SMEs in West Africa by the Islamic Development Bank for Sustainable Development and Poverty Reduction

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ABSTRACT

Objective: This study examines the challenges and competitiveness of small and medium-sized enterprises (SMEs) in West Africa, focusing on the funding support provided by the Islamic Development Bank (IsDB) to address critical socio-economic issues such as poverty and unemployment in the region. **Method:** The research utilizes empirical evidence from previous studies conducted by the World Bank and other multilateral institutions, analyzing key obstacles to the successful implementation and sustainability of SMEs in West African countries. **Results:** The findings reveal significant challenges that hinder the growth and sustainability of SMEs in the region, including limited access to financing, inadequate infrastructure, and regulatory barriers. However, the support provided by IsDB plays a crucial role in overcoming some of these challenges, promoting the success of SMEs in the region. **Novelty:** This study contributes new insights into the role of the IsDB in supporting SME growth in West Africa, offering practical recommendations to enhance the success and prosperity of SMEs in the region. The paper emphasizes the importance of addressing structural barriers to ensure the long-term sustainability of SMEs in the context of West Africa's socio-economic challenges.

INTRODUCTION

The Islamic Development Bank (IsDB) is an intergovernmental financial institution based in Jeddah, Saudi Arabia, established in 1974 under the Articles of Agreement [1]. The bank's primary goal is to support the development of its member nations through various initiatives, including funding projects in the private sector, infrastructure, agriculture, and technology. With 57 member countries worldwide, IsDB continues to play a pivotal role in promoting economic growth and poverty reduction [2]. This paper focuses on IsDB's efforts to empower and promote Small and Medium-Sized Enterprises (SMEs) in West Africa, exploring both the opportunities and challenges facing the SME sector in the region. Additionally, it examines key obstacles, particularly from both conventional and Islamic financial perspectives, and offers recommendations to ensure the continued growth and success of SMEs under IsDB's stewardship [3].

IsDB's Commitment to Financing the SME Sector [4]

IsDB is deeply committed to supporting SMEs and fostering entrepreneurship among its member countries, guided by the principles of Islamic finance [5]. The bank provides substantial financial support through instruments such as Qard Hasan (benevolent loans), as well as other Islamic financial modes like leasing, Murabaha, Mudarabah, and interest-free loans. The bank's financial reports from 2002 to 2019

demonstrate its ongoing dedication to empowering SMEs across developing nations. Many West African countries have benefited from significant funding for small and medium-sized businesses, leading to notable poverty reduction and job creation in the region [6]. Over the past seven years, rural farmers and labor markets have seen increased productivity and income due to IsDB's support.

In October 2018, the IsDB Board of Governors convened in Burkina Faso to discuss financing for developmental projects in West Africa. At this meeting, IsDB approved a \$3.5 billion funding package for various sectors, including SMEs, with the primary goal of reducing poverty and addressing disparities between urban and rural areas. This aligns with IsDB's long-term objectives, as highlighted in its 2002 agenda, which prioritized support for SMEs as a key strategy for sustainable economic development. Other priority areas in IsDB's framework include primary healthcare, infrastructure development, and promoting intra-regional trade [7].

In 2017, IsDB signed a \$100 million Islamic funding agreement with several West African nations, including Guinea, Ivory Coast, Burkina Faso, Mali, and Senegal, to promote the growth of SMEs. Notably, in January 2019, IsDB signed a \$16.25 million agreement with Guinea to support rice production, helping reduce the country's reliance on rice imports. This initiative has not only improved the livelihoods of small-scale farmers but has also boosted the national economy.

According to IsDB-ICD's 2018 Annual Report, the IsDB-ICD partnership allocated \$32.2 million to projects in Mali, Nigeria, and Yemen under the Women Entrepreneurship Finance Initiative (We-Fi) [8]. These projects aim to support women-owned SMEs by enhancing capacity building, fostering business resilience, and integrating these enterprises into value chains. IsDB's focus on gender inclusivity in the SME sector reflects its commitment to addressing the longstanding economic disparities faced by women in the region.

In 2018, Nigerian banks such as Fidelity Bank and the Bank of Industry received \$40 million each from IsDB-ICD to support SME and private sector initiatives [9]. Similarly, Banque Islamique du Senegal (BIS) received €50 million to strengthen SMEs and private sector development in Senegal. This funding is part of IsDB's broader vision to stimulate liquidity, cash flow, and Foreign Direct Investment (FDI) in the region. IsDB's strategic focus on SMEs underscores its growing recognition of the sector's potential to drive economic growth and financial stability in West Africa and beyond [10].

The Concept of SMEs

Before delving into the main topic of this paper, it is important to highlight that there is no universally accepted definition of Small and Medium-sized Enterprises (SMEs). According to the World Bank Group's 2003 review on SME finance, "The definition of an SME based on specific criteria is not uniform across countries. For example, one country may define an SME as an enterprise with fewer than 500 employees, while another may set the threshold at 250 employees" (WBG, 2003) [11]. For the purposes of this paper, we will focus on the definition commonly used in West

African countries, such as Nigeria. In this context, SMEs are businesses with a workforce of up to 250 employees and relatively limited assets on their balance sheets. The key factors in defining SMEs are therefore the number of employees and the scale of the company's assets. SMEs are often characterized by innovation and entrepreneurship, and they play a vital role in promoting economic stability and social justice within local communities [12].

RESEARCH METHOD

Literature Review

In relation to the topic of the Islamic Development Bank's (IsDB) efforts to promote SMEs in West African nations, there is limited information and data available [13]. While there is a body of qualitative analysis documenting the funding provided by IsDB from 2002 to 2018 in countries such as Senegal, Guinea, Nigeria, Ivory Coast, and Niger, there is a lack of academic research explaining the importance of supporting and introducing SMEs in the region. There are, however, two main schools of thought on this subject [14]:

1. **Support for Promoting SMEs:** A group of scholars emphasizes the urgency and importance of promoting SMEs in both developing and developed nations. For example, Harvie and Lee (2002) and Beaver and Prince (2004) argue that SMEs play a critical role in job creation, innovation, exports, and private-sector production. These contributions are essential in both developed economies and emerging markets.
2. **Challenges Faced by SMEs:** Another group focuses on the challenges facing SMEs in West Africa, including a lack of capital, mismanagement of funds, corruption, insufficient liquidity, poor infrastructure, and weak governance. These obstacles hinder the effective functioning of SMEs in the region.

RESULTS AND DISCUSSION

Why SMEs?

Many financial experts justify the importance of SME programs, citing their role in creating jobs and stimulating the domestic economy, particularly in developing nations [15]. Aulia (2012) notes that SMEs play a significant role in employment creation and GDP growth in developing countries. Furthermore, new data from international financial institutions indicate that SMEs contribute up to 60% of new jobs in developing nations. For instance, Ayyagari, Demirguc-Kunt, and Maksimovic (2014) found that SMEs in the formal sector account for 50% of employment in these countries (SME Finance, 2017). Given their crucial role, SMEs are often seen as engines of economic growth, fostering rapid industrialization and development, especially in regions like West Africa [16].

In West Africa, SMEs have had a positive impact on rural farmers and small family businesses. These programs have led to the construction of schools, clinics, market areas, and recreational centers in many parts of the region. As a result, local markets have

seen improved cash flow and increased economic activity [17]. Moha (2011) explains that SMEs are instrumental in improving income distribution, creating jobs, reducing poverty, and contributing to rural development. In particular, micro and small enterprises have become vital engines for rural economic development and the wellbeing of local communities.

SMEs are also regarded as a strategy for poverty reduction. When more individuals participate in the labor market, productivity increases, leading to higher tax revenues, improved financial well-being, and the potential to escape poverty [18]. Sokoto (2013) notes that one of the major concerns for leaders and development practitioners in mixed economies has been not just promoting economic growth, but also providing a strong institutional framework for establishing and sustaining viable SMEs as a means of achieving sustainable poverty reduction. In countries like Liberia, Guinea, and Ivory Coast, SMEs have helped alleviate poverty and hunger among rural farmers.

Promoting SMEs in the region has the potential to drive infrastructure development, such as roads, bridges, hospitals, schools, and homes. Additionally, SMEs contribute to regional development and the expansion of export markets due to their agility compared to large corporations [19]. According to Abdelrahman Elzahi Saaid Ali (2013), IsDB member countries should encourage the establishment of SMEs to stimulate economic growth and reduce poverty through job creation and income generation. Countries investing in SMEs have seen improvements in farmers' incomes, strengthening local businesses and reducing dependency on government handouts.

However, despite these positive outcomes, there are several challenges to implementing and supporting SMEs in the region, especially under the guidance of IsDB. These challenges include legal and regulatory risks, corruption, a lack of skilled labor, poor connectivity, weak banking and financial infrastructures, and insufficient capital investment [20]. Ayyagari et al. (2011) and Banerjee and Duflo (2005) highlight that small firms are typically less productive than large ones, due to manual production methods, lack of skilled workers, outdated machinery, and limited access to modern IT processes. Overcoming these challenges requires collective efforts from local authorities, residents, and IsDB.

Islamic financial institutions are well-positioned to address the challenges that conventional financial systems, such as those employed by the World Bank, European Union, China, and African Union, have faced. By creating a financial system tailored to risk management, long-term projects, liquidity control, and cost management, SMEs can thrive in the region. As Sahar Nasr (2013) notes, emerging SME finance models can significantly improve the outreach, viability, and risk management of SME financing in the MENA region. To support this, SMEs need access to long-term credit products, equity, working capital loans, trade finance, payment services, liquidity management, risk management tools, and insurance.

One effective strategy employed by IsDB to boost SME productivity in the region is fostering regional cooperation. By promoting knowledge and talent exchange among small farmers, IsDB has facilitated coordination between small and medium-sized enterprises in countries like Liberia and Guinea. For example, the Smallholder Agricultural Productivity Enhancement Program (SAPEP) funded by IsDB in 2013

supported five West African countries with \$68.54 million. This program improved smallholder agricultural productivity through knowledge-sharing and cooperation [21].

To address the challenges faced by SMEs, IsDB and other organizations like the UN, World Bank, IMF, and EU can diversify their financing models to support different types of small businesses in the region. Potential sectors for investment include internet cafes, purified water companies, transportation, mining, used car businesses, and restaurants [22]. Md. Shahnur (2013) highlights that SMEs are not only concentrated in low-tech, traditional, or agro-based sectors but have also expanded into non-traditional manufacturing and service sectors. By financing these diverse sectors, SMEs will generate employment, stimulate regional economic growth, and reduce poverty and unemployment.

CONCLUSION

Fundamental Finding : This study highlights the essential role of small and medium-sized enterprises (SMEs) in fostering economic stability and poverty reduction in West Africa. It emphasizes the Islamic Development Bank's (IsDB) crucial contributions through financial support, skills development, and policy recommendations aimed at overcoming key challenges facing SMEs, such as liquidity shortages, low productivity, and lack of managerial skills. **Implication :** The findings suggest that IsDB's continued focus on providing transparent liquidity, investing in skills development, and introducing a credit scoring system could significantly enhance SME growth in West Africa, leading to job creation, increased economic activity, and social inclusivity, especially for marginalized groups like women. **Limitation :** The study primarily draws on existing literature and empirical evidence from other multilateral organizations, which limits the scope of direct primary data from SMEs in the region. Further case studies or longitudinal research would provide deeper insights into the effectiveness of IsDB's interventions. **Future Research :** Future research could explore the long-term impact of IsDB's SME initiatives on poverty alleviation and regional economic development. Additionally, investigating the effectiveness of specific interventions, such as credit scoring systems or targeted support for women entrepreneurs, would offer valuable insights for enhancing SME sustainability and growth.

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