Zakat Based poverty eradication in Bangladesh:

The Millennium Development Goal is exceed able

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Abstract

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Poverty alleviation has been a priority in Bangladesh's development plans and programmes since 1972. Official and NGO efforts based primarily on IRD (integrated rural development) and micro-credit models, by 2000 succeeded in eradicating dire poverty and reducing the overall level to around 50 per cent of the population. Since then Bangladesh has adopted the UN sponsored MDG which aims to reduce poverty level by half by 2015. A carefully crafted strategy (PRSP) through much local and international consultation is essentially based on the elements which succeeded in the 1980s and 1990s.

It is surprising that Zakat, an expressly designed poverty eradication tool, clearly prescribed in the Holy Quran and Sunnah, has been completely ignored in all poverty alleviation plans and programmes in Bangladesh, where more than 85 per cent of the population are Allah- fearing Muslims. Also, there is confusion and ignorance about true practices of zakat in the mind of these people, which resulted in lasting benefits not accruing to the traditional zakat receivers.

In 2005, the Institute of Hazrat Mohammad (SAW) in Dhaka proposed a new methodology of zakat payment and utilization, to achieve optimal success in poverty eradication, This paper shows, on the basis of some simulation analysis using household income and expenditure data, that following the proposed methodology of converting zakat from a temporary consumption item to investable wealth, utilizing it in both micro projects, like pisciculture in a village, and macro projects such as an IT software company in Dhaka, through a dedicated and professional Islamic institution, poverty can be eradicated in Bangladesh in 10-12 years. This would exceed the MDG by a long shot. It could also pave the way for the existing interest based micro-credit programmes to make a transition to interest free Islamic micro-finance as well as macro-finance.

1. Poverty alleviation strategies of Bangladesh, 1971-2005

Bangladesh was born poor. The country emerged as an independent state in 1972 after years of neo-colonial exploitation culminating in a genocidal civil war which destroyed most of its fragile infrastructure and shattered the economy. In spite of its fertile soils, plentiful water resources and an intelligent, homogenous population, the newly born state was desperately poor with a per capita income of only USD 140, the second lowest in the world at that time; and over 70 percent of the population was estimated to be living below the poverty line. Little wonder therefore that poverty alleviation featured high on the agenda for development in Bangladesh.

Fortunately, international sympathy for the new state was high and the World Bank jumped in with a billion dollar aid package. Other multilateral and bilateral donors followed snit. Along with the tasks of restoring the infrastructure and rehabilitating the war victims, poverty alleviation strategies were formulated at macro levels on the basis of 5-yearly plans, and the annual development plans within their broad framework.

During the first decade since liberation poverty alleviation efforts moved along three principal dimensions: governmental, NGO and academic. At the government level, macro level efforts laid emphasis on water resources development to assist integrated rural development (IRDP) based on the famous Comilla 2-tier cooperative model for agricultural growth. There was also a vigorous population control programe based on family planning. The underlying logic of this approach was the trickle-down hypothesis based on Harrod-Domar growth models on the one hand, and identification of rapid population growth as the main cause of poverty, on the other. The

government also introduced a number of safety net programmes to address the need of the most vulnerable groups, such as Food-for-work (FFW), Vulnerable Group Feeding (VGF), Vulnerable Group Development Programme (VGDP), etc.

The Liberation war of 1971 was instrumental in generating a phenomenal growth of NGOs in Bangladesh. Many well trained professionals, such as university teachers, medical doctors, engineers and corporate executives, voluntarily joined the liberation struggle, some of them even participating as freedom fighters. They were transformed by the experience and found it difficult to go back to their old professions . They become the prime movers of some of the most notable NGOs established soon after Liberation. BRAC was established in remote Sylhet; Jobra, the precursor to Grameen Bank, started to operate around the Chittagong University campus; and Gono-Shasthya (People's Healthcare Centre) was being set up in nearby Savar.
BRAC experimented with a variety of rural development models and eventually settled on informal/non-formal education, healthcare extension (eg the famous 'lobon-gur' oral rehydration programme that drastically reduced cholera deaths) and an integrated rural development programme underpinned by micro-credit. Grameen Bank eventually emerged with its well formulated micro-credit programme that became a model for most other NGOs to follow. Essentially, it was the provision of small quantities of institutional credit without collateral to the rural poor, mainly women, who had till then been denied such credit and were thus vulnerable to exploitation by the traditional money-lenders. Grameen Bank worked like magic for a decade and had a definitive impact on poverty alleviation. Another NGO that deserves to be mentioned was Swanirvaar (self reliance) Bangladesh which concentrated on developing an institutional framework

seeking to decentralize administration and devolve political power with the aim to deliver rural development without depending on foreign assistance.

The third dimension of poverty alleviation strategies during the 1970s was at the academic level. A major effort was made at the Bangladesh Institute of Development Studies (BIDS) through a large scale long term study programme combining statistical methods with social anthropological methods. It aimed to understand the genesis, perpetuation and ways of alleviation of poverty. The BIDS studies by and large supported decentralization of administration and devolution of political power as essential for achieving rapid poverty alleviation. The large scale nationalization of industries, banks and trading houses were found to have had a detrimental impact on the economy; and lesser bureaucratic grip on the economy was, on the whole, found to be desirable. The BIDS studies also came in favour of donor support for the NGOs. On the population front, fertility was found not to be an act of mindless reproduction, but deliberate family decisions rooted in the need for supplying labor to a traditional low technology production system and the absence of security to life both through diseases as well as social predation. Avoidable mortality needed to be avoided before births were to be prevented.

On the whole, the 1970s ended on a positive note of economic growth and perceivable dent on poverty.

In the 1980s there was as accelerated move towards privatization and the ready made garment (RMG) industries emerged as a prime mover in the export sector. It generated large scale employment for peri-urban low income families and contributed towards family planning success and female literacy. Another macro economic measure that contributed towards poverty alleviation was a revolutionary new drug policy, mainly engineered by

Gono-Shasthya Kendro that reduced drastically the prices of all essential life saving drugs and brought them within the reach of the poor.

The next decade (1990s) saw further invigoration of the economy and the end of a long period of autocracy. The private sector began to operate more vigorously. During this decade poverty was estimated to have declined by about 1 percent each year, till it reached 50 percent in 2000. Several leading NGOs acquired productive assets and were well on their way to becoming self- financed.

2. The Millennium Developments Goals (MDG)

The UN held a Millennium Summit in September 2000 where eight development goals, expressed as numerical targets, were set to be achieved by 2015. These are known as the Millennium Developments Goals (MDGs) which included halving headcount poverty, achieving universal primary education, reducing infant and child mortally by two-thirds, reversing the spread of HIV/AIDS and other communicable diseases etc. Bangladesh adopted the MDGs; and in respect of poverty reduction it implied reducing headcount poverty from the estimated 50 percent in 2000 to about 25 percent in 2015.

In 2005 the World Bank carried out a multivariate analysis on determinants of poverty and found it to be strongly related to land ownership and adult schooling. Economic growth was found to be a strong factor in poverty reduction and the association was almost one-for-one, ie one percent increase in economic growth would reduce poverty by one percent. On the other hand, consumption inequality was seen to be positively correlated with poverty, so that the benefits of economic growth could be easily wiped out

by income inequality. The World Bank concluded that achieving the MDG in respect of poverty in Bangladesh is feasible through a combination of sector specific interventions. In fact, the World Bank believed that a sustained annual real economic growth of 4 percent would itself allow Bangladesh to meet its Millennium target on poverty, provided there was no increase in consumption inequality.

3. Absence of Zakat in the poverty alleviation strategies of Bangladesh

A very unusual feature in Bangladesh's poverty alleviation strategies over the last three and half decades is that nowhere: neither government, nor NGOs, nor private sector and not even in the academic circle, has there been any systematic consideration given to any Islamic strategy, such as zakat or waqf. It is indeed surprising that in a country where over 85 percent of the populations are Muslims, mostly God-fearing and religious, even if not always rigorous in religious practice.

As a result zakat, which is absolutely tailor-made and designed for poverty eradication (not merely alleviation), has been entirely left out as a voluntary private act. It has surely been followed by a large majority of the Muslim population, but almost doubtlessly, at a fraction of what is recommended by the Holy Quran and Sunnah.

There are in fact several explanations why this has happened. Firstly, it is a lack of knowledge by the majority of Muslims in Bangladesh about the religious importance of zakat and its calculation. As a result most people willingly or unwillingly gets away without paying what they would have paid, had they known.

Secondly, there was a strong anti-religious sentiment prevailing in intellectual quarters since the Liberation War when Muslims were spilling Muslim blood and Hindus were giving shelter and protection to the displaced Muslims. This to a large extent explains the adoption of secularism as a fundamental principle in the Constitution of Bangladesh.

Thirdly, the planners of poverty alleviation strategies, both in the government and the NGO sectors, were western-educated elites who were by training brought up to consider any religious idea as non-progressive. In fact, being an atheist was tacitly considered to be smart and intellectually mature.

Fourthly, and most importantly, 9/11 had not yet happened. The thesis of the clash of civilizations pushed all Muslims living in the West, specially the younger ones, to dig deep into their religion and find the basic tenets of Islam directly from the Quran and Sunnah. Also Islamic finance had not yet emerged as an important subject in Western academia and business circles.

The concept of a Zakat-based Poverty Eradication Project (ZPEP) was first mooted by the Institute of Hazrat Mohammad (SAW) about two years back at a Conference on Islamic Banking in Dhaka. This paper fully develops the concept and illustrates, on the basis of simulation exercises, how this can be achieved and within what period of time.

4. Clarification about some basic concepts on zakat

The importance of zakat in Islam can be gauged firstly by the number of times it is mentioned in the Holy Quran and making it clear that without zakat, salat is not established. The Prophet Mohammad (SAW) further

emphasized its importance by referring to it as one of the five pillars of Islam. If we analyze all the Quranic verses relating to zakat, some basic points emerge clearly:

- It is a religious obligation of the rich to give and a right of the poor to receive. It is not a voluntary act of charity.
- Reward for giving is manifold and the punishment for not giving severe: and the both the reward and the punishment are to be expected in this world as well as the hereafter.
- The eligible categories of zakat receiving people are eight, but the poor and the destitute are top priorities.
- The Quran enjoins everybody to be generous, but also assures that religion is not meant to be a burden.
- The Sunnah and Hadith make it clear that zakat is both a wealth tax (eg 2.5 percent on gold and silver) as well as an income tax (eg 5 percent on agricultural produce with irrigated water and 10 percent when rain fed). For resources underground, the Hadith is not clear and tend to imply 20 percent for hidden treasures and 5 percent in case of extracted minerals.

The most important lesson from Prophet Mohammad (SAW)'s practices is that he preferred to give productive assets as zakat rather than cash or items of immediate consumption. This principle has been adopted in the proposed ZPEP.

5. Elaboration of ZPEP Strategy

It involves six basic steps:

Step 1: Carry out a simple household economic survey in every geographical area to be covered by ZPEP to identify the two categories of families, ie those that are liable to pay zakat and those that are entitled to receive it, based on the calculation of surplus or deficit income.

Step 2: Carry out a massive information, education and motivation (IEM) campaign on zakat, using the media as well as all the educational institutions inclusive of mosques and madrasas; and encourage people to pay zakat through credible institution(s).

Step 3: Pool all zakat receipts trough a countrywide network of one or more Islamic banks to create a fund; and issue share certificates of the zakat fund to the recipients as may been specified by the zakat payers.

Step 4: Find innovative micro projects in villages and macro projects in urban/industrial areas which offer a maximal return on investment, keeping an eye on the creation of employment opportunities for the shareholders based on their skills and qualifications.

Step 5: Calculate profit and pay a part of it as dividend as per prior agreement, plowing back the rest into the fund, thus increasing the equity of the shareholders.

Step 6: Carry out the above steps with accumulated funds, both old and new (as new funds are received every year). Calculate the dividend and the employment income for each zakat recipient family at the end of each year and ascertain if its deficit income has been wiped out, at which point this family will seize to receive further zakat.

As a family graduates out of poverty (ie earns more than it spends) it should continue to retain its investment in the zakat fund for a number of years, ie till such time when every family graduates out of poverty. At this point poverty eradication, defined as the wiping out of all deficit incomes, will be achieved.

6. Simulation Exercises

Four simulation exercises, following the steps described above, are carried out with two objectives. First, it will demonstrate how the proposed zakat fund would systematically reduce poverty by making available to zakat eligible families, not zakat in cash or items of immediate consumption but, income derived as dividends and employment wages, resulting from the zakat fund investments. Second, by assuming different parametric values for the return on investment (r), the proportion of profit reinvested (p) and the proportion of investment received as wages and salaries by the zakat eligible families, it would be possible to estimate the varying lengths of time in number of years required to eradicate poverty under the different schemes.

All four simulation exercises start from Table-1 (see Annexure 1) which shows the average monthly incomes and expenditures of around 24.35

million families in Bangladesh, categorized by their average monthly income. Several interesting statistics may be derived from this table. It is seen that families with deficit incomes who, according to the definition adopted in this article, are poor, constitute 55 percent of the total families. It is a common human tendency to overstate expenditure and understate income. If adjusted for this factor the proportion would be very close to 50 percent, which coincidentally is the World Banks poverty estimate for Bangladesh in 2000. The estimated total surplus income is, as per the respondents own admission, around BDT 328.41 billion, 2.5 percent of which is about BDT 8.21 billion. Considering the under estimating tendency of the respondents, additional zakat likely to be received from companies and for computational ease in the simulation exercises, BDT 10 billion is taken as a reasonable estimate of annual zakat contribution if every eligible person pays his/her minimum due.

This then is the starting point in all four simulations shown in Tables 2A through 2D (See Annexure 2 through 5).

In estimating the period of time required to eradicate poverty, three parameters are crucial; these are

r = the percent profit made on investments from the zakat fund;
p = the proportion of profit reinvestment into the zakat fund every year; and
m = the proportion of the zakat investment that accrues as employment income for the zakat eligible families.

It is fairly obvious that higher values of each of these parameters would reduce the time needed for poverty eradication. The actual values would depend on three factors, namely

- the type of project selected for investment;
- management efficiency; and
- market uncertainties.

For example, in a rural fishery project the returns may be very high if the project is well managed, but the risk of fish mortality through disease or malafide acts of neighbors could mean heavy losses. Rice production, on the other hand, could provide safe though smaller returns. Investment on large industries would mean nil return for the first few years, followed by high profits in later years. So, portfolio selection has to be made on the basis of sound knowledge of the involved technologies and product markets as well as skilled management. In general, micro projects such as fishery, transport and petty trade, could yield net profits in the range of 30-80 percent annually. While micro projects such as a nursing college or a private English medium school could yield 50-100 percent profit after 2-3 years. The simulated values of parameter 'r' have been assumed from a range of 15 to 30 percent, which is rather conservative but safe.

The parametric values of 'm' is primarily dependent on the labour intensity of the technology involved in the selected investment project. Generally, rural agricultural and small scale transportation projects, such as fisheries, rickshaws, or taxicabs, would be highly labour intensive. The adopted values of 'm' in the four simulations range between 15 to 30 percent.

Finally, the parameter 'p' is a deliberate choice of the investors, in this case the zakat recipient poor families. The value range of 'p' can be quite large, since there exists in Bangladesh a wide range of safety net programmes to cover the dire needs of the poor and the destitute, such as Food-For-Work (FFW), Vulnerable Group Feeding (VGF), pension for the elderlies, etc. There are also various socio-religious arrangements such as traditional alms, waqf, "moosti chaal" etc. The parametric range of 'm' in the simulations is

between 50 and 80 percent. It is expected that once the zakat recipient families begin to appreciate the long term benefit of investment into well selected projects, they may go for almost 100 percent reinvestment of their annual zakat receipts and returns on earlier investments.

In each simulation, the assumed set of parameters are held constant year after year, and the process of poverty eradication occurs at intervals as the additional income, dividends and wages from zakat investment, keep increasing till it exceeds the deficit for one (or more) income category. This category of families then ceases to receive zakat from next year onwards by becoming 'non-poor'.

Once this happens, the number of zakat eligible families diminishes, and so does the total cumulative zakat fund, because the shares of the fund belonging to the poverty crossing families become withdrawable. However, they would possibly benefit more by keeping their shares invested in the zakat fund, rather than withdraw and invest on ventures of their own choice. The process will continue in this fashion till the zakat eligible families have all graduated out of poverty.

The entire simulation exercise under each set of assumed parametric values are presented in tables 2A through 2D (see Annexures). It can be followed with ease if one is first familiar with the 12 different variables in abbreviated codes, which appear from left to right in the top row of each table. These are sequentially explained below:

a. WZi = withdrawable cumulative zakat fund in year i
   = Σ(TZFi ÷ ZEFi) *APCFi
b. NCZi = not withdrawable cumulative zakat fund

= ΣZi - ΣWZi

c. Zi = zakat receivable in year i
= 2.5% of surplus income in year i
(held constant for simplicity)

d. PRi = last year's profit reinvested in year i
= (r * TZFi-1) * p

e. TZFi = total zakat fund invested in year i
= NCZi + Zi + PRi

f. DZEFi = last year's dividend distributed to ZEFi in year i
= (r * TZFi-1)(1 - p)

g. EZEFi = employment income for ZEFi in year i
= TZFi * m

h. TIZEFi = total zakat fund income for ZEFi in year i
= DZEFi + EZEFi

i. ZEFi = zakat eligible families in year i
= no. of families with deficit income (ref Table-1)

j. AZIZEFi = average zakat fund income per ZEFi in year i
= TIZEFi ÷ ZEFi

k. CPCFi = cumulative poverty crossing families in year i

l. ACPCFi = additional poverty crossing families in year i

[Note: * indicates multiplication]

The last variable APCFi is ascertained by constant reference to Table-1 and checking for which category of families deficit incomes are being wiped out by AZIZEFi.

7. Time for poverty eradication:

The time needed to achieve poverty eradication under the four simulation exercise are shows below with the corresponding assumptions regarding values of parameters r, p and q.

Parameters	Simulations			
	1	2	3	4
r = rate of profit	15%	20%	25%	30%
p = proportion profit reinvested	50%	60%	80%	80%
m = proportion employment income	15%	20%	25%	30%
T= time for poverty eradication (years)	17	12	11	13

Simulation-4 with 30 percent rate of profit on investment 30 percent employment income and 80 percent profit reinvestment appears to provide the shortest route to poverty eradication, which turns out to be 9 years only. It may be noted that it far exceeds the MDG in that it is only 9 years for complete eradication while the MDG is 15 years for achieving only half of it.

8. Conclusions

a. How realistic are the simulations?

It has to be understood that a simulation exercise is not a prediction of reality. It is only a delineation of happenings under certain assumptions about some crucial parameters and variables. The parametric values adopted in the simulations shown earlier range between 'somewhat pessimistic' to 'somewhat optimistic'. For example, 15 percent profit is not the worst case scenario in some large scale projects, such as a textile mill, nor is a 30 percent profit wildly optimistic in many micro projects, such as operating a rickshaw. The same observation would apply to the employment content of investments. The assumptions regarding the proportions of profit to be reinvested are also quite realistic, particularly since it is entirely in the hands of the investors and does not depend on the market.

b. Need for Pilot Demonstration

The more critical question is about the number of people that would pay their true zakat. To a large extent, it would depend on the quality of the campaign. Every human being wants to do something great at least once in their life. Fortunately, poverty eradication has a noble ring about it. So, motivation could snowball once people are convinced about the honesty and integrity of the organization and the efficiency of the people associated.

An effective demonstration of the above will then have to be carried out through several carefully selected pilot projects before expanding it nationwide. The organizational overheads have to be kept low and transparency meticulously ensured.

c. From Grameen's micro-credit to Islamic microfinance

The micro-credit programme innovated by Professor Yunus has undoubtedly contributed towards poverty alleviation and reduction of income inequality in Bangladesh. It has been acclaimed worldwide and replicated in several countries including the USA. The final recognition came recently through the award of the Nobel Peace Prize. Nonetheless, a time may soon be reached in Bangladesh when the basic premise of microcredit will need to be reexamined. After all, interest is prohibited in Islam; and an undercurrent of discontent has been brewing for some time among two disparate groups of intellectuals: the die-hard Maoist and the Islamic Sharia hardliners. There has been restraint in expressing too much criticism because of its obvious beneficial impacts, particularly during the initial phases. Now the Nobel award will allow micro-credit another round of widespread popularity. But a backlash is likely to happen after a few years, particularly if the present effective rate of interest rises any further. But such a situation need not arise at all. The world renowned micro- credit programme could transform beautifully and become Islamic micro-credit.

How? That should be the subject matter of another conference!

Table 1: Household Income and Expenditure Data of Bangladesh 2000

Annexure -1

Monthly household income group	Number of families	Average no. of families	Average no. of earners	Average monthly income/family	Average monthly expenditure	Monthly average excess/ (deficit)income (Tk)	Yearly average excess/ (deficit)income (Tk)	Total excess/ (deficit) income (m tk)
a	b	c	d	e	f	g	h	i
750	*435,322*	*2.68*	0.82	443.97	2,266.66	(1,822.69)	(21,872.28)	(9,521.48)
750 - 999	*416,313*	*3.14*	1.00	871.65	1,853.42	(981.77)	(11,781.24)	(4,904.68)
1000 - 1249	*607,674*	*3.63*	1.02	1,132.62	1,865.17	(732.55)	(8,790.60)	(5,341.82)
1250 - 1499	*727,651*	*3.68*	1.07	1,374.80	1,810.44	(435.64)	(5,227.68)	(3,803.93)
1500 - 1999	*2,245,545*	*4.03*	1.16	1,756.07	2,072.13	(316.06)	(3,792.72)	(8,516.72)
2000 - 2499	*2,526,380*	*4.34*	1.22	2,240.14	2,481.66	(241.52)	(2,898.24)	(7,322.06)
2500 - 2999	*2,567,121*	*4.70*	1.28	2,740.15	3,035.67	(295.52)	(3,546.24)	(9,103.63)
3000 - 3999	*3,871,670*	*5.14*	1.44	3,463.57	3,505.47	(41.90)	(502.80)	(1,946.68)
Sub Total	*13,397,676*							(50,461.00)
4000 - 4999	2,755,180	5.41	1.54	4,470.50	4,371.77	98.73	1,184.76	3,264.23
5000 - 5999	2,040,524	5.82	1.58	5,462.59	5,271.22	191.37	2,296.44	4,685.94
6000 - 6999	1,331,372	5.98	1.66	6,469.27	5,916.97	552.30	6,627.60	8,823.80
7000 - 7999	926,077	6.04	1.64	7,456.59	6,496.75	959.84	11,518.08	10,666.63
8000 - 8999	772,638	6.32	1.71	8,490.19	7,890.29	599.90	7,198.80	5,562.07
9000 - 9999	585,374	6.42	1.78	9,506.97	8,154.08	1,352.89	16,234.68	9,503.36
10000 - 12499	900,778	6.40	1.83	11,103.30	9,525.04	1,578.26	18,939.12	17,059.94
12500 - 14999	490,571	7.01	1.93	13,615.36	11,194.36	2,421.00	29,052.00	14,252.07
15000 - 17499	287,407	7.36	2.17	16,145.93	13,215.09	2,930.84	35,170.08	10,108.13

17500 - 19499	181,046	7.34	1.82	18,777.90	15,234.27	3,543.63	42,523.56	7,698.72
20000 +	678,504	7.59	2.27	50,277.53	21,195.70	29,081.83	348,981.96	236,785.66
Sub Total	10,949,471							328,410.55
All groups	24,347,147	5.18	1.45	5,841.88	4,881.01	960.87	11,530.44	277.549.55

Source: Bangladesh Bureau of Statistics (BBS)