

**CULTURAL ASPECTS ON THE ISLAMIC MICROFINANCE: AN EARLY
OBSERVATION ON THE CASE OF ISLAMIC MICROFINANCE INSTITUTION
IN BANDUNG, INDONESIA¹**

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ABSTRACT

Microfinance has been widely accepted as one of the tools to eradicate poverty. The stories of *Grameen Bank* in Bangladesh, *Bank Rakyat Indonesia (Indonesian People Bank)* in Indonesia, *Self-Help Group* in India show the extent to which microfinance can eliminate poverty. The success story has been accepted also with the contribution of Islamic Microfinance Institutions. (Seibel:2008). Yet, it is unfortunate not many studies have been conducted in order to investigate the impact of culture to the development of microfinance in Indonesia. The cultural factor itself is believed to also influence the existence of poverty (Goode and Eames, 1996 & Lewis, 1998). According to Mohammad Obaidullah (2008) the cultural and religious sensitivities of the Islamic world are somewhat unique and these must be given due emphasis in any attempt to build inclusive financial systems and bring the over one-billion Muslims into the fold of formal financial systems. Research conducted by Deubeul (2003) on microcredit on Mali showed how culture can be integrated in developing microfinance. The success of *Grameen Bank* is also due to the bank's understanding of cultural factor embodied in women as their main client (Varghese, 2001). Another research done by Phlong (2009) on informal credit system in Cambodia also indicates that the understanding of local culture assist the effectiveness of microfinance in a society. Latest research by Rana (2008) in Bangladesh also confirmed the need to have cultural orientation in managing the microfinance. These findings leads to the need of diversification in empowering the microfinance institution as well as the Islamic MFIs.

Islamic MFI need to diversify product range and design product to cater the financial needs of the poor segment of the economy. This diversification refers to the diverse financial requirements with regards to the cultural differences. The innovative designs of a range of sharia-compliant products and services would provide greater financial access to a broader segment of islamic microfinance customers. (Karim, Tarazzi and Reille :2008). In Indonesia itself, despite of the fact that Indonesia consists of various different cultures, such research are still very limited. The living culture of poor fisherman for instance, will obviously differ from that of poor farmer and poor fellow in an urban city. Thus, eventually the culture is predicated to have an impact on the success or failure in financing distribution of islamic microfinance.

This paper attempts to examine the extent to which cultural factor affect the Islamic microfinance development, particularly in Indonesia. Using sample quantitative and qualitative data and approaches of Islamic MFIs in Bandung, this paper attempts to observe and find the evidence that cultural aspects should be incorporated in the development and management of Islamic MFIs. Finding of this research however indicates the extent to which Islamic microfinance institutions tend to deny the importance of cultural differences and thus this prevent them from providing cultural specific products. Interview conducted with Bambang Ismawan yields that two factors are associated with such attitude i.e. the banking regulation and Islamic normative traditional discourses that seems not considering the cultural aspects of the people. These finding thus needs to be further investigated in order to provide a more detailed understanding of the issue.

INTRODUCTION

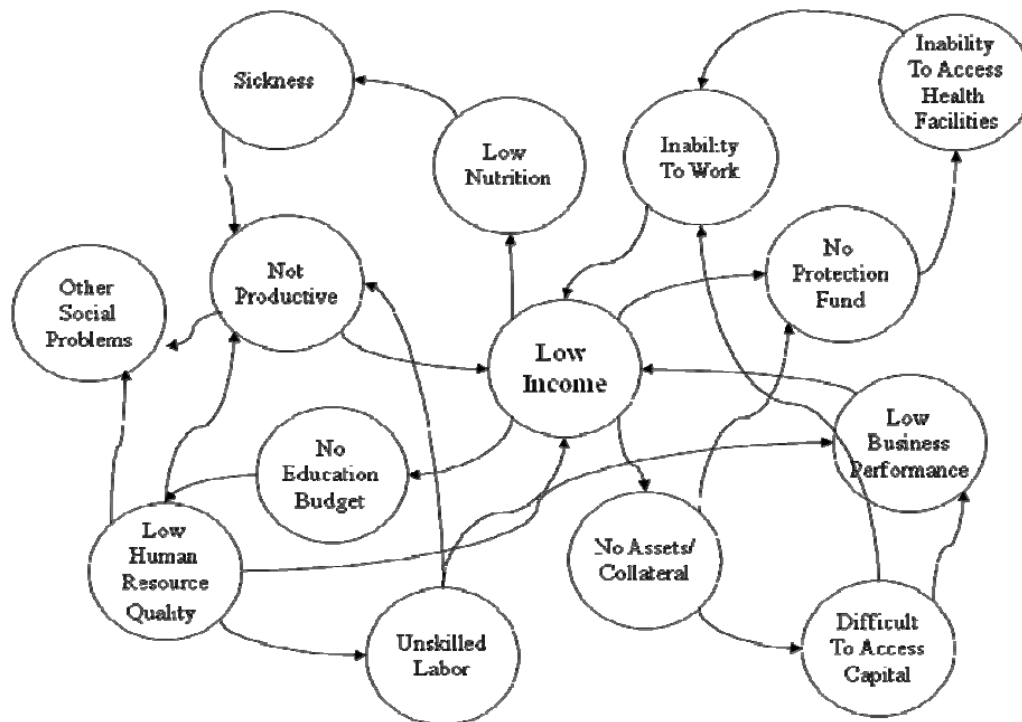
This paper attempts to explore cultural aspects in Islamic microfinance. Microfinance has been widely assumed to help poverty eradication. The successes of microfinance in such programs have been shown in various countries including Indonesia. Islamic Microfinance has also been recognized for its successes in supporting micro sectors to develop. In Indonesia, Islamic microfinance has been developing very progressively since 1990's. Microfinance is normally operated in the formal institutions such as Islamic banking and Syariah banking/ bank perkreditan rakyat syariah (BPRS) and non banking institutions such as BMT, Kopontren, etc. Various research have investigated the successes of Islamic microfinance yet only limited studies so far have been conducted in order to identify cultural aspects in Islamic microfinance. While researchers such as Goode & Eames (1996), Lewis (1998), and Mohammad Obaidullah (2008) have shown the extent to which poverty is very much related to cultural aspects. . Other studies conducted by Deubeul (2003), Phlong (2009) and Rana (2008) also indicate the impact of culture in the development of Islamic microfinance. It is unfortunate that despite of the fact that Indonesia consists of various different culture, research that aim to investigate the impact of cultural aspects in microfinance are still very confined. This paper follows the ideas of Seibel (2005) and SMERU (2005) who claim the stagnant of Islamic microfinance development in Indonesia is due to lack of attention to the cultural aspects. This paper attempts to elaborate the impact of cultural aspects in Islamic microfinance by using literature review as well as empirical study gained from qualitative observation and interview from selected Islamic microfinance in Bandung, Indonesia. This paper will be commenced by defining poverty, microfinance, and Islamic microfinance in Indonesia. Then, it will explain the methods adopted for this study

followed by analysis of the data. Findings of the research are expected to provide an insightful understanding to the development of Islamic microfinance in general and that of in Indonesia.

Poverty and Microfinance

Poverty is one of the most fundamental problems in today's society. Despite of the disputes around factors that contribute to poverty, it is undeniable that poverty can lead to other social problems. Hunger, death, and criminals are among some of the problems associated with poverty. The problems of poverty are so pervaded that the United Nations has listed poverty eradication as one of the goals in the Millennium Development Goals. Poverty does not only prevent people from having healthy nutritious food, but poverty also contributes to the low quality of life. Below picture illustrates social problems associated with poverty

Figure 1
Poverty and Social Problem Net



Microfinance is assured as one of the tools that can decrease as well as eradicate poverty. Microfinance might assist people in providing cash that can be utilized to change their life. The function of the cash provided by microfinance institutions vary from short term benefit as well as long term benefit. Short term benefit is when the cash used for consumption i.e. basic primer needs, while long term benefit occurs when the cash is utilized as a capital in order to initiate business thus help the people to improve their life.

Numbers of research have been conducted in order to measure the success of microfinance. The stories of *Grameen Bank* in Bangladesh, *Bank Rakyat Indonesia (Indonesian People Bank)* in Indonesia, *Self-Help Group* in India show the extent to which microfinance can eliminate poverty. Obaidullah (2008) has also done research that attempts to identify the glory of microfinance. Another research that aims to investigate the impact of microfinance in eradicating poverty has been conducted by Chowdhury (1996). Chowdhury (1996) studied the extent to

which microfinance can improve the nutritional status of people from economically underprivileged group. Another research conducted by Hulme and Mosley (1996) focus on the impact of microfinance to the income of the borrowers. Their research yields that microfinance does have a positive impact to the income of the borrowers 30% more compare to that of those who do not take credits from microfinance. Other similar research have also shown the impact of microfinance in erasing the poverty (Pitt & Khandaker, 1996; Halder, 1998; Zohir, 2000; Hakim, 2000; Latif, 2000; Chowdhury & Bhuiya, 2004).

The impact of microfinance is not only confined to economic aspect. The microfinance has also positively affected the gender issue as well. Obaidullah (2008) cited the research done by Pitt and Khandaker (1996) and Zaman (2001) that reveals this issue. The research of Pitt and Khandaker (1996) indicates that microcredit has given positive impact of the program on women employment, total per capita weekly expenditure, and women's non-land assets. Moreover, using sample of Bangladesh Rural Advancement Committee's (BRAC) clients, Zaman (2001) research show the extent to which microfinance can improve women's income, decision making process as well as decrease gender disparity.

Poverty, Microenterprises, and Role of Microfinance in Indonesia

Indonesia is the fourth highest population in the world after China, India, and the United States of America. With around 245 millions of people, Indonesia is still facing difficulties in the poverty alleviation. Table below show the data of poverty in Indonesia from 1998 to 2007.

Table 1
Poverty in Indonesia 1998-2007

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
BPS*										
Number in Millions	49,5	47,9	38,7	37,9	38,4	37,3	36,1	35,1	39,3	37,2
Percentage	24,2	19,1	18,4	18,2	17,4	17,4	16,7	16	17,8	16,6
USD1-PPP/cap/day**										
Number in Millions	n.a	24,9	20,9	19,7	15,5	14,5	16,5	13,6	19,5	15,5
Percentage	n.a	12	9,9	9,2	7,2	6,6	7,4	6	8,5	6,7
USD2-PPP/cap/day***										
Number in Millions	n.a	135	125,3	125,2	115,6	110	109,1	102,1	113,8	105,3
Percentage	n.a	65,1	59,5	58,7	53,5	50,1	49	45,2	49,6	45,2

Source: Badan Pusat Statistik Indonesia (Indonesia's Institution for Statistical Center) and The World Bank from various period.

Note:

Poverty Line is converted to the real value, considering that the purchasing power of USD 1 will different from one country and another

*Poverty Line of BPS : Rp 166,697 /capita/month (USD 17,54 in real value using Rp 9500 /USD)

**Poverty Line of USD 1 of WB : Rp. 121,352/capita/month (USD 12,77 in real value using Rp. 9500/USD)

***Poverty Line of USD 2 of WB : Rp. 242,704/capita/month (USD 25,54 in real value using Rp. 9500/USD)

The above table obviously shows that according to Indonesia government standard of poverty lines, around 16,6 % or 37,2 million of Indonesia people are living under poverty line with USD 17,52 as their monthly income. If the standard used is that of the World Bank, then the monthly income real value becomes USD 12,77, with approximately 6,7 % or 15,5 millions people are living under poverty lines. But if we increase the daily standard to USD 2 per person, then half of Indonesian population (45,2 %) or 105,3 millions live are living under poverty lines.

Microfinance institutions in Indonesia have also given significant impact in combating the poverty. The approach of microfinance institution in Indonesia involves a diversity of

regulated financial institutions. According to Ismawan and Budiantoro (2005)³ microfinance institutions in Indonesia can be divided into two types: banking and non banking institutions. The banking institutions can be divided into two categories: commercial banks and rural banks. This commercial banks and rural banks have been regulated by the Central Bank of Indonesia for their principles and operations, including the monitoring. Bank Rakyat Indonesia, perhaps is the oldest institution in Indonesia that has served in the micro level of financial services.

The non banking institutions can be divided into formal and non formal institutions. For formal category, there are cooperative institutions, Lembaga Dana dan Kredit Pedesaan (LDKP/rural credit financing institution), pawnshop, and Badan Kredit Desa (BKD/rural credit association). LDKP gets their formal status from the local government while BKD is an institution supported by Bank Rakyat Indonesia on behalf of Central Bank of Indonesia (Bank Indonesia). In the non formal category, microfinance institution carried out by NGOs and Self-Help Groups. According to Obaidullah (2008)⁴ the NGOs type of microfinance institution dominated by member-based cooperatives while The Self-Help Groups (SHGs) are completely informal organizations. Hundred of thousands of informal SHGs with savings and credit activities exist in Indonesia. Many are spontaneous groupings based on traditional forms of association. Many other SHGs have been founded by government and community organizations in connection with government programs. For instance, there was a Pola Hubungan Bank dan Kelompok Swadaya Masyarakat (PHBK), a program of linking Banks with Self Help Groups. However, the existence of this linkage is not longer continued⁵.

³ Bambang Ismawan and Setyo Budiantoro, 2005, Mapping Microfinance in Indonesia, Jurnal Ekonomi Rakyat, can be accessed at http://www.ekonomirakyat.org/edisi_22/artikel_5.htm

⁴ Obaidullah, Mohammed. 2008. *ibid.* p.50

⁵ This program has been succeed to reach the economically active poor people. The program was built based on joint cooperative between Commercial Bank with the local institution through credit without collateral and joint liabilities scheme. With a non formal managerial approach, the program succeeded to serve more than 1 million people with

Numbers of research have also been conducted with regard to the impact of microfinance in eliminating the poverty in Indonesia. Among these researches are done by Rudjito (2003)⁶ and SMERU (2005)⁷. Rudjito (2003) explained the successful of Bank Rakyat Indonesia using their microfinance programme such as BKD (Bank Kredit Desa/Village Credit Bank), P4K (Program Peningkatan Pendapatan Petani dan Nelayan Kecil/*Fishery and Farmers Income Generating Project*), and BRI Unit. Using cultural approach, BKD has built more than 4,500 microfinance institutions and served more than 700 thousands of people, only in Rural Area of Java and Madura Islands. The P4K has served the people by lending credit by more than 683 billion rupiahs to more 170 thousands group of people in the rural area, with non performing loan only 6,78 % on 2002. The BRI Unit which started since 1984 has achieved more than 25 millions of people in saving and serve more than 4 million of people in credit services. Different with Rudjito, SMERU, A Research Institute Indonesia, specifically did specific research on microfinance in the 2005, and found significant contribution of microfinance to the poverty alleviation. The research was named as Sulawesi Agriculture Area Development Project (SAADP) and funded by the World Bank. The project is an economic-commercial project whose aim is to reduce poverty in Central Sulawesi and Southeast Sulawesi. The result of the research reveals that SAADP had a positive impact on increases in all types of agricultural perspectives among farming respondents. The greatest effect was on knowledge about land management and the use of fertilizer. The program had also a positive impact on changes in farming practices. Most of SAADP respondents said that their nominal household income had risen as a result of

an outstanding recovery rate of 97 %. However, since the implementation of new banking regulation in 1992, the program is no longer active.

⁶ Rudjito, 2003, Peran Lembaga Keuangan Mikro dalam Otonomi Daerah Guna Menggerakkan Ekonomi Rakyat dan Menanggulangi Kemiskinan: Studi Kasus Bank Rakyat Indonesia. Can be accessed at http://www.ekonomirakyat.org/edisi_13/artikel_3.htm

⁷ SMERU, Vol 13-2005, The SMERU Research Institute

their participation on project. The above instances had shown how microfinance contributes the poverty alleviation programs in Indonesia.

Otero in Ismawan (2009)⁸ defined Microfinance as Micro Enterprise Finance. The role of microfinance in the society, particularly in Indonesia is not only giving the poor and poorest people with money to help them fulfilling their primary needs, but also how to enhance their livelihood to becoming better by making them economically active. To reach this objective, the potential economic activity run by this group should also be supported by microfinance. In this case, microfinance plays a vital role in supporting the economically active poor with capital. This group of economically active poor usually named as microenterprises, eventhough microenterprises not merely run by the poor. In many cases, the microenterprises run by wealth people in Indonesia, since its market is very large. According to Indonesian Law No. 20 Tahun 2008 microenterprises is a business entity which has asset maximum of 50 million rupiahs excluding land and building with maximum turnover of 300 million rupiahs per year. The type of business that mainly run by the microenterprises are:

- a. **Primary and secondary activities** : agriculture, plantation, animal husbandry, fisheries (all is implemented in limited scale and subsistent), small craftsmen, tailors, snacks producers, etc.
- b. **Tertiary activities** : transportation (in varied kinds), renting activities of houses, land, production tools, etc.
- c. **Distribution activities** : small traders in markets, peddlers, retail distributors and agent, and the like.
- d. **Other service activities** : street singer, shoes polisher, haircutter, mechanics, garbage laborer, street photographer, and so on.

⁸ Bambang Ismawan, Microfinance in Indonesia: Challenge and Opportunity, Paper presented in the the Workshop on Integrated Microfinance Management and Development in Indonesia, Joint Cooperation between Padjadjaran University of Indonesia, Leiden University of Holland, and Medditeranian Agronomic Institute of Chania, Greece in Bandung-Indonesia, 20 May 2009.

According to the 2008 data of Indonesian Institute of Statistical Center (BPS) as cited by Tati & Kurniawan (2009)⁹, the number of these microenterprises is about 98 % of total of Indonesian Business Players. It means that these microenterprises are dominant player in the economic activities in Indonesia. Table 2 below shown how the number of enterprises in Indonesia with their financing patters. It is obvious that the microenterprises represent almost 50,7 million of Indonesian people. The main sources of their funding are from government support scheme such as Community Empowerment Program (PNPM), Small and Microenterprises Program, etc. Even though this microenterprises group represent majority of business player in Indonesia, however, they still lack of capabilities. They are lacking of capital access, lack of financial skills, and lack of law and regulatory framework. This shortcomings, later on will be explained as one of the factor contributing the decline of microfinance performance.

Table 2
Enterprises in Indonesia and It's Financing Patterns

Type of Enterprises	Number & Percentage	Assets Criteria	Financing Patterns
Large Companies	4,370 (0,01%)	> 50 billion rupiah	Capital Market, Banks, etc
Medium Enterprises	39,660 (0,08 %)	200 million – 50 billions rupiah	Banks, SME Credit Programs
Small Enterprises	520,220 (1,01%)	50 – 200 million rupiah	Banks, SME Credit Programs, Community Empowerment Program (PNPM),etc
Micro Enterprises	50,70 million (98,90%)	< 50 million rupiah	Micro Enterprises Program, Own Source, Money Lenders, People Effort Credit (KUR), etc

Source: Tati & Kurniawan (2009), adapted from BPS

⁹ Tati Soehartati Joesron & Kurniawan Saefullah, Applied Economics and Microfinance Development in Indonesia, Paper in the Workshop on Integrated Microfinance Management and Development in Indonesia, Joint Cooperation between Padjadjaran University of Indonesia, Leiden University of Holland, and Medditeranian Agronomic Institute of Chania, Greece in Bandung-Indonesia, 20 May 2009

Critics on the Microfinance and the Cultural Aspects in Microfinance

Though numbers of research have indicated the impact of microfinance in eliminating poverty, some studies have challenged these. Fernando (2004)¹⁰ and Robinson (2000) claim that instead of eliminating poverty, microfinance is in fact perpetuating it. Cited from The Consultative Group to Assist the Poor (CGAP) in 2003, Fernando argues that “ The users of microfinance are generally those who are living within poverty lines, and those who are among the poorest in the society remain neglected and invisible by the microfinance”. The requirement set by microfinance cannot be fulfilled by the poorest or extremely poor groups in the society. Kalpana in SMERU (2005)¹¹ notes four factors responsible for the fact why the poorest or extremely poor group are in fact marginalized from microfinance. They are 1) inflexible loans that need to be paid in the weekly basis as well as the unavailability of the saving accounts 2) power relations between microfinance’s staff and the borrowers created the borrowers as the others 3) Evaluation between member systems, and 4) the possibility of the high interest rate. The example follows will illustrate the extent to which those four factors can exclude the poorest and extremely poor groups in the society. In Indonesia, farmer and fishermen are among the poorest groups in the society. A farmer can only produce in his farmer after 3 months of the initial planting. While the fishermen decision to sail will also be very much depending on the circumstances such as weather. Thus, they are in a difficult situation if faced with the rigid of payment time. This phenomenon is sustained and reinforced by microfinance’s staffs’ inability to understand their clients’ positions. This illustrates what Kalpana mentioned as inflexibility of payment time with a rigid weekly basis payment.

¹⁰ Fernando, Nimal A. (2004) Microfinance Outreach to the Poorest: A Realistic Objective? Finance for the Poor. ADB Finance for the Poor. Volume 5 No. 1 March 2004

¹¹ SMERU, Vol 13-2005, The SMERU Research Institute, Indonesia

This situation might be derived from the staffs' lack of understanding of the whole issues and problems faced by their clients. Matin, Hulme dan Rutherford¹² state that microfinance can only develop by having a comprehensive and holistic idea about poverty itself. Because without an understanding of poverty itself it will be difficult for microfinance to completely eradicate poverty. Woodley, et.al (2006)¹³ argues that despite of the fact that development planners aim to optimize development and reduce disparity between the rich and the poor, but they often do that without acknowledging the indigenous people's food and livelihood systems. It is no wonder that the definition of poverty used by The Commission on Legal Empowerment of the Poor (CLEP) and United Nations' Millennium Development Goals, do not totally reflect or represent the indigenous peoples' realities and priorities. The development planners often do not consider the cultural aspect of the indigenous people. If they too take into account cultural aspects, they are often reduced into cultural products such as movies, book, and so forth. They tend to ignore cultural aspects in term of people's tradition, ceremonies, food systems, and local wisdom. Hence, Hendricks (2000) believes that development programs should be value laden rather than value free. Development strategies are embedded within their culture of origin and tend to leave out the cultural environment of the society in which the development is to be applied. Many times development strategists are simply passing on, sometimes despite themselves, ideas, modes of organization, values and forms of expression which are typically Northern, and which have little in common with the lifestyle of the local communities into which they are imported. This cultural 'bias' is rooted in the inability to imagine development models other than those within which the originator is accustomed to working and whose legitimacy is indisputable.

¹² Matin, Imran, David Hulme and Stuart Rutherford. "Financial Services for the Poor and Poorest: Deepening Understanding to Improve Provision". *The University of Manchester*. October 1999. www.sed.manchester.ac.uk/idpm/publication/archive/fd/fdw.pdf

¹³ Ellen Woodley, Eve Crowley, Jennie Dey Pryck, and Andrea Carmen, 2006, Cultural Indicators of Indigenous Peoples' food and agro-ecological systems, SARD Initiatives, Paper on the 2nd Global Consultation on the Right to Food and Food Security for Indigenous Peoples, 7-9 September 2006, Nicaragua

Consequently projects are often designed which are irrelevant to the cultural situation and donors then become concerned about the lack of local ownership¹⁴. As cited in the Wikipedia online reference, Lewis (1998) and also Goode and Eames (1996)¹⁵ conform that poverty is indeed related to culture. Therefore, development plans including the implementation of microfinance should involve the cultural factors. As Lewis states:

The people in the culture of poverty have a strong feeling of marginality, of helplessness, of dependency, of not belonging. They are like aliens in their own country, convinced that the existing institutions do not serve their interests and needs. Along with this feeling of powerlessness is a widespread feeling of inferiority, of personal unworthiness. This is true of the slum dwellers of Mexico City, who do not constitute a distinct ethnic or racial group and do not suffer from racial discrimination. In the United States the culture of poverty of the Negroes has the additional disadvantage of racial discrimination. People with a culture of poverty have very little sense of history. They are a marginal people who know only their own troubles, their own local conditions, their own neighbourhood, their own way of life. Usually, they have neither the knowledge, the vision nor the ideology to see the similarities between their problems and those of others like themselves elsewhere in the world. In other words, they are not class conscious, although they are very sensitive indeed to status distinctions. When the poor become class conscious or members of trade union organizations, or when they adopt an internationalist outlook on the world they are, in my view, no longer part of the culture of poverty although they may still be desperately poor. (Lewis 1998)

Similar perspective is also provided by Misbach (2009). Misbach cites Azhari (1982) who distinguishes poverty into three categories i.e. natural poverty, structural poverty, and cultural poverty. The cultural poverty is culture that may contribute to the people's tradition, hampering people to make economic progress such as laziness, consumptive, and present not future oriented¹⁶. The lack of attention given by the development planners might also be derived from the fact that culture itself is not something that can be easily defined. As argued by Raymond Williams in Chris Jenks (1985), Culture is one of the two or three most complicated

¹⁴ Larry Hendricks. 2000. Microfinance and Culture: A Case Study Of Ghana, Paper, Canadian International Development Agency (CIDA).

¹⁵ Oscar Lewis. 1998. The culture of poverty. *Society*. 35 (2):7 and Goode, Judith, and Edwin Earnes. 1996. "An Anthropological Critique of the Culture of Poverty". in G. Gmelch and W. Zenner. *Urban Life*. Waveland Press as cited at http://en.wikipedia.org/wiki/Culture_of_poverty

¹⁶ Muhammad Lufie Misbach, Masalah Kemiskinan dan Beberapa Pendekatan Penanggulangannya di Provinsi Jawa Timur, Majalan Ekonomi, Tahun XIX, Agustus 2009

words in the English language¹⁷. Thus, culture is idea consist of process, differences, and even paradox. Kohls and Wederspahn¹⁸ also define culture as a set of value in a group of people. Kohls defines culture as an *integrated system of learned behaviour patterns that are characteristic of the members of any given society. Culture refers to the total way of life for a particular group of people. It includes [what] a group of people thinks, says, does and makes—its customs, language, material artefacts and shared systems of attitudes and feelings.* While Wederspahn defines culture as the shared set of assumptions, values, and beliefs of a group of people by which they organize their common life.

Based on these definitions of culture, I attempt to divide culture in the context of microfinance into two things. The first one is internal culture which in microfinance named by Leonard¹⁹ as institutional culture or organizational culture. In this case, culture refers to a system of shared meaning held by members that distinguishes the organization from other organizations²⁰. The second one is external or society culture that is associated with culture adopted by the people in relation to their daily values and judgements. These two cultures, I believe need to be understood in order to have microfinance effective in eliminating poverty. Institutional Culture is related to the capability of the microfinance while external culture of the society needs to be understood in order to help microfinance institutions assist their clients.

Several researches have been conducted in order to show the impact of cultural understanding in managing microfinance institutions (Deubel, 2003; Rana, 2008; and Phlong,

¹⁷ Chris Jenks, 1993, *Culture: Key Ideas*, Routledge

¹⁸ Robert Kohls and Gary Wederspahn in *Culture Matters: The Peace Corps Cross-Cultural Workbook*, Peace Corps Information and Collection Exchange, ISBN 0-9644472-3-1

¹⁹ Matt Leonard. Microsave Focus Note No. 20, www.MicroSave.org

²⁰ Stephen P Robbins, 1996. *Organizational Behavior: Concepts, Controversies, Applications*, 7th edition, Prentice-Hall International, p. 681

2009). Research conducted by Deubel (2003)²¹ on microcredit on Mali shows how culture can be integrated in developing microfinance. The success of *Grameen Bank* is also due to the bank's understanding of cultural factor embodied in women as their main client (Varghese, 2001). Rana (2008)²² in Bangladesh also confirmed the need to have cultural orientation in managing the microfinance. By using institutional culture, Rana shows how evaluation systems used by microfinance institution should include the cultural aspects. Rana concludes that using sample in Bangladesh taht Bangladesian culture is unique and very much influenced by religion and colonial legacy. If the management of microfinance in Indonesia is based on western management control system, Rana believes it will be less effective. Hence to include the cultural factor is necessary for microfinance institutions to sustain.

Islamic Microfinance in Indonesia and Cultural Aspects of Islamic Microfinance

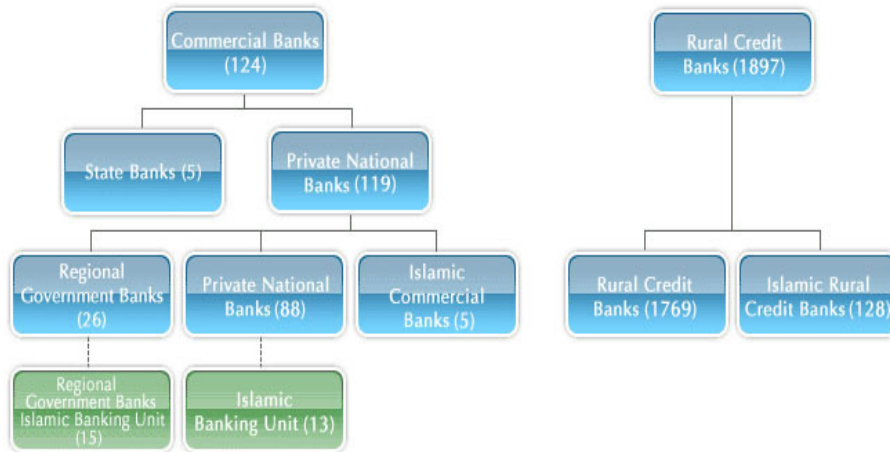
Indonesia implements a dual financial system that allows both conventional (mainstream) and Islamic financial system to coexist. In general Islamic microfinance in Indonesia is divided into two categories: banking sectors and non banking sectors. Banking sectors can be categorized as Islamic Banks and Islamic Rural Banks (BPRS). Below Figure 2 shows the number of Islamic microfinance as well as conventional banks in Indonesia based on the data given by Effendi (2009)²³.

²¹ Tara.F. Deubeul.2003, Banking on Culture:Microcredit as incentive for cultural conservation in Mali, on Microfinance: Perils and Prospects, Routledge Series on Economic Development,2006, edited by Jude L Fernando

²² Mohammad Baktiar Rana, 2008, Cultural Oriented Management Systems of Microfinance Institutions in Bangladesh

²³ Nury Effendi, 2009, Current State of Financial System in Indonesia, Paper in The Workshop of Integrated Microfinance Management and Development in Indonesia, UNPAD-LEIDEN-MAICH

Figure 2
Number of Banks and Islamic Banks in Indonesia



Source : Nury Effendy (2009)

While for non banking systems, they involve Islamic Takaful, Islamic Cooperatives (BMT), and so forth. According to Seibel and Agung (2005)²⁴ Islamic finance in Indonesia has evolved since 1991, eventhough in the existence of Islamic finance informally has existed in Islamic boarding school in Indonesia since 1980's in the form of Islamic Cooperatives of Islamic School (Koperasi Pondok Pesantren/Kopontren)²⁵, yet its management are limited to members of the school only and thus its effect cannot be completely felt by the local people in general. Seibel and Agung also divide Islamic microfinance into Islamic commercial banks, commercial banking units, rural banks, and financial cooperatives. Indonesia also has one of the most differentiated micro- and rural finance sectors among developing countries, comprising both formal and non-formal financial institutions. Obaidullah (2008)²⁶ elaborates the characteristics of Islamic

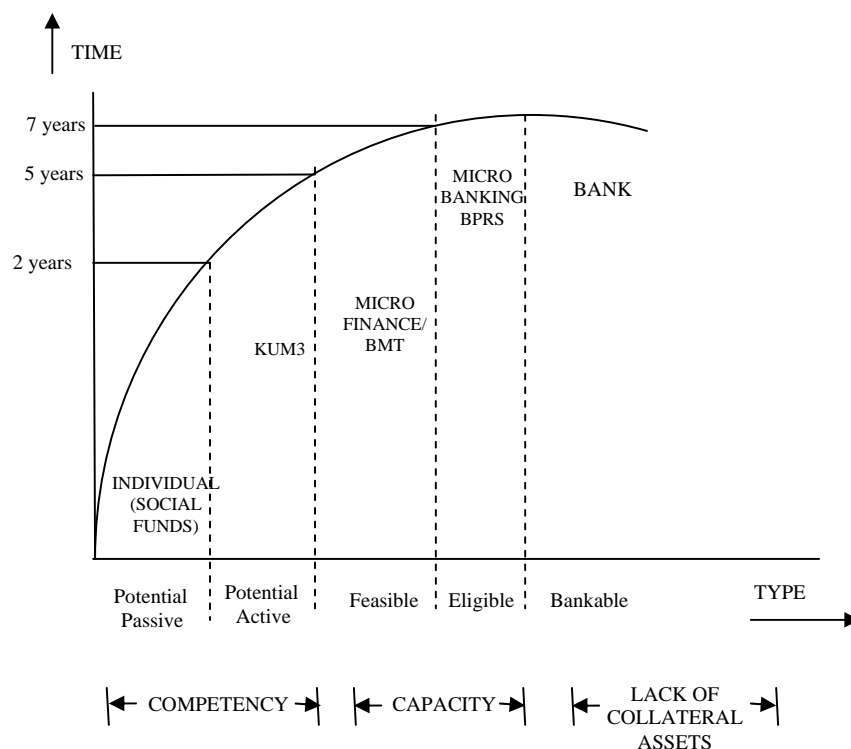
²⁴ Hans Dieter Siebel and Wahyu Dwi Agung, 2005, Islamic Microfinance in Indonesia, Paper of University of Cologne Devopment Centerm

²⁵ Pradjarta Dirdjosanjoto,1994, Memelihara Umat: Kyai di antara usaha pembangunan dan mempertahankan identitas local di daerah Muria, Dissertation, Vrije Universiteit of Amsterdam

²⁶ Obaidullah, Mohammed.2008. ibid. p.46-57

financial institutions in Indonesia by explaining the relationship between various Islamic microfinance institutions in Indonesia and what the roles of Central Bank, Supporting Organizations, to linkage of Islamic Banking between banking sectors and non banking sectors as suggested by Bank Muamalat Indonesia (BMI) as BMI Microenterprises Development Program. Below picture 3 illustrate the linkage between various Islamic microfinance institutions in Indonesia:

Figure 3
BMI Microenterprises Development Program



Source: Mohammad Obaidullah (2008)

Since from institutional level, Islamic finance in Indonesia is extremely varied, hence they also distinct in term of their performances. As stated by Seibel (2005), the performance of syariah micro finance is low compared to the performance of Islamic Rural Bank (BPRS) which is

considered to be stagnant, despite of its fast development. For example in Aceh, a province that has implemented Islamic law in its governance has 5 Islamic rural banks (BPRS) and 76 Islamic Cooperatives (BMT), and yet only less than 20 banks perform well. Here is the conclusion from Seibel and Agung on Islamic finance institutions performance in Indonesia (Seibel, 2005)²⁷.

Table 3
Islamic Microfinance Conditions in Indonesia

Type of Microfinance Institutions	Conditions
Islamic Rural Banks (BPRS)	<ul style="list-style-type: none"> - Regulated Islamic and conventional rural banks have evolved over almost the same time period, 13 and 15 years, respectively - Islamic rural banks have remained small. The volume of their services is negligible, compared to conventional rural banks, accounting for only 4% in number, 1.5% in assets as well as outreach, and 1.2% of deposits - Islamic rural banks growth in numbers has stagnated in recent years; and their growth in assets has remained far behind that of conventional rural banks - Lack of popular demand for Islamic banking services, absentee ownership, lack of young dynamic management, lack of mastery of overly complex Islamic banking practices, and emphasis on the informal sector and the poor to the neglect of more profitable market segments are among the many reasons for their retarded development
Islamic Cooperatives (BMT, Kopontren, etc)	<ul style="list-style-type: none"> - The whole cooperative sector has historically suffered from a complete lack of regulation and supervision, paralleled by excessive government interference and subsidies which have distorted rural financial markets and undermined self-help - The majority of Islamic cooperatives are reportedly dormant or technically bankrupt - Outreach and volume of services of Islamic cooperatives are negligible compared to conventional cooperatives, which are also in a state of acute but undiagnosed ill-health - The savings of depositors are at great risk; cooperatives should not be authorized to accept savings of non-members - No remedy is in sight

Source: adapted from Seibel & Agung (2005)

²⁷ Hans Dieter Siebel and Wahyu Dwi Agung, 2005, *ibid.* pp 35-38

The last data on microfinance institution performance is also not promising. According to Bank Indonesia²⁸, the total Non Performing Loan in financial sector tends to increase. Based on December 2009, the number of Non Performing Loan (NPL) of all sectors is about 47,58 trillion rupiahs, and almost half of it is in the micro sector (24,79 trillion rupiah or about 47 % of total NPL in 2009). This data gives a pessimistic picture toward microfinance's attempt to eliminate poverty.

To conclude, Seibel and Agung (2008) sum up the development of Islamic microfinance in Indonesia as follows: Islamic rural banks's (BPRS) development is quite stagnant even lower than conventional rural banks. While Islamic financial cooperatives (BMT) which underwent a rapid development in 1990, in the present are also deteriorating with less than 20 % from their total numbers can operate well. This might be predicated on the unavailability of effective regulation and supervision

Beside those factors mentioned above, I also pay particular attention to the cultural aspects which have been tended to be ignored in Islamic microfinance institutions. As Mohammad Obaidullah (2008)²⁹ states, the cultural and religious sensitivities of the Islamic world are somewhat unique and these must be given due emphasis in any attempt to build inclusive financial systems and bring the over one-billion Muslims into the fold of formal financial systems. How far the cultural aspects should be considered in the Islamic Microfinance Institutions, the next sections will explain the early evidence from some of Islamic microfinance institutions in Bandung of how effective culture affects the Islamic Microfinance Institutions.

²⁸ Tabloid Kontan, No. 23-XIV – 2010, March 2010 Edition

²⁹ Mohammad Obaidullah, 2008, *ibid.*

METHODS

This research is conducted in order to identify perception from Islamic microfinance institutions managers on the importance of cultural aspect in Islamic microfinance from institutional culture and external culture. For institutional culture, I attempt to modify instrument used by Rana (2008) despite of the fact that the data collected using structured interview. While for external culture, I try to explore the extent to which the managers of Islamic microfinance consider the cultural aspects in managing the Islamic microfinance. The questions asked adopted from indicators provided by Lewis (1998) as well as Misbach (2008) on the characteristics of local people versus migrants, people's characteristics in term of their ethnics, profession and gender. This paper based on an early observation on the 5 Islamic microfinance in Bandung, Indonesia which are observed since December 2009 until Februari 2010. The institutions are BMT Syarah, BMT ISEG, BMT Daarut-Tauhiid, BMT asdad, and BPRS Salman. The data collected using observation as well as structured interview to the managers of each institutions from Desember 2009 until February 2009.

RESULTS: EARLY EVIDENCE OF CULTURAL ASPECT ON THE ISLAMIC MICROFINANCE IN BANDUNG CITY, INDONESIA

Brief Introduction about Bandung

Bandung is a capital city of West Java, a province whose population is the third largest in Indonesia. The population of Bandung is 2, 4 millions. Bandung was famous for organizing Asia Africa Conference in 1995. Bandung is a very diversified city. Its people's population vary from teachers, lecturers, bankers, factory labours, as well as farmers in its countryside. Bandung is also known as the melting polt between its indigenous and migrant people. Before 2000,

Bandung was recognized a manufacture city because of its textile production, But since the crisis that hit Asian in 1997/1998, many textile companies collapse and thus Bandung transformed into a service city since 2000 by using its Dutch associated heritage building as one of its main attraction. Now, Bandung is also known as educational, food and Leisure City.

The majority of its people are Muslim, comprises 78% of the total population, followed by Christian, 18 % and the other 4 % such as Buddhism, Hindu, and so forth. Despite of the fact, Bandung is indeed a diversified city, it celebrates differences.

Bandung is also known as an initial place for the development of Islamic microfinance in Indonesia. BMT Salman or Teknosa is an Islamic microfinance institution established by universities students in early 1980's. After BMT Salman, then followed by BPRS Amanah Robbaniyah in the late 1980's before the birth of Bank Muamalat Indonesia in 1991. It is however during this stage the development of Islamic microfinance is limited to cooperative only. As mentioned by Seibel dan Agung (2005), the development of microfinance is stagnant particularly for BPRS and BMT.

The profile of Five Islamic Microfinances in Bandung

I did observation to 5 Islamic microfinances in Bandung, from Desember 2009 to Februari 2009. The choice of these 5 institutions is because of their degree of consent. They are willing to participate in this research while other microfinance institutions are reluctant to participate. It is however understood that their reluctant might be due to unavailability of proper data in their institutions that makes them defensive to be studied. This research is designed in order to understand the importance of cultural aspects in term of institutional culture and external culture.

Table 4
Brief Introduction of Five Islamic Microfinance in Bandung

Name of Institutions	Location	Characteristics of Society around the MFI
BPRS Salman	Masjid Salman, Jalan Ganesha Bandung (Nearby Bandung Institute of Technology) Center Area of Bandung	Students, Educator, Street Trader, Horse Riding Service Provider, Book Store Trader
BMT Daarut- Tauhiid	Jalan Gegerkalong Girang Bandung (Nearby Campus of Indonesia Education University) North-West Area of Bandung	Students, Educator, Street Trader, Small Restaurants, Urban Migrants, Housewife
BMT Syarrah	Jalan Raya Cibiru (Nearby Campus of Islamic University of Sunan Gunung Djati) Eastern Area of Bandung	Students, Educator, Urban migrants, Housewife
BMT ISEG	Jalan Dipati Ukur (In the University of Padjadjaran) Center Area of Bandung	Students, Educator, Street Trader
BMT El-Tazkiyyah	Jalan Maleer V (Nearby Traditional Market) Southern Area of Bandung	Traditional Market Trader, Street Trader, Broker, Housewife,

Source: Primary Data Survey (2009)

The table indicates that despite of commonalities shared by the clients of these 5 Islamic microfinance institutions, there are also existed differences, particularly for BMT El-Tazkiyyah. The other four Islamic microfinances are university campus based. This is strengthen the assumption that Islamic microfinance was developed by students' activist. This can be traced to the history of Islamic Finance in Indonesia that was initially developed by Indonesian Muslim Students Association/ Ikatan Cendekiawan Muslim Indonesia (ICMI) by BJ Habibie in 1990. These ICMI activists train university students. Hence those who support were also mainly university student activists. The discipline of Islamic microfinance in Indonesia is also exist in universities such as University Indonesia, University of Airlangga, Universitas Padjadjaran, Universitas Islam Indonesia (UII), dan lain-lainnya. This production of knowledge also takes place at students' level, by establishing Islamic Economics Students Forum/ FOSEI which

conduct annual meeting to share recent development of Islamic microfinance. The last meeting was conducted last March 2010 in Medan, Northern of Sumatra.

BPRS Salman is Islamic Rural Banks in Salman Mosque, a mosque with long history on its national activists such as Imaduddin Abdulrahim (allahuyarham), Endang Saifuddin Anshari, Jalaluddin Rakhmat, etc. BPRS Salman has only been two years become BPRS after previously known as Islamic financial cooperatives or BMT. The managers consists general people and university campus activities as well as lecturers. The users of this BPRS vary from students, lecturers and entrepreneurs in campus area.

BMT Daarut-Tauhiid is Islamic finance cooperatives established in 1992 with its capitals were only 300 thousand rupiahs by Abdullah Gymnastiar. It developed very fast with its clients vary from students, lecturers, housewives, and traders. They are also able to finance their own business from clothings to radio stations. However its performance is continued to be deteriorated since 2006. Their assets are now estimated only hundred millions rupiah followed by its clients decrease in numbers³⁰.

BMT Syarrah is Islamic microfinance cooperatives established by lecturers in Islamic \ Sunan Gunung Djati Univesrity in Bandung around two years ago. Its assets are estimated around 117 millions rupiah in Februari 2010³¹. However this institution is also facing a high non performing finance around 36,27 % in bulan Februari 2010. For new institution, this needs to gain particular attention.

³⁰ There is indication that the declining performance of this Islamic Microfinance Cooperatives refers to the declining of the Islamic Boarding School (Pesantren) Daarut Tauhiid, caused by the decision of its leader, Abdullah Gymnastiar who run for poligami. Most of followers of this school are woman, in which they were not ready to accept the poligami decision.

³¹ BMT Syarrah is the only institution in this observation who opened and gave detail information regarding the financial matters compare to other institutions. The author several times asked for the financial informations to the other institutions, however, they were unable/not ready to share the informations.

BMT ISEG is Islamic finance cooperatives established by students at Faculty of Economics, Padjadjaran University Bandung in 2006. Their main clients are students who attempt to become young Muslim entrepreneur. It also provides scholarship to local people particularly for their children education. Their assets in 2009 are only 2 millions rupiahs. Most of the money is distributed to people thus the investment is not developed very fast. One of the obstacles is due to the activities of its managers as students that prevent them from giving full time attention to its institutions.

BMT El-Tazkiyyah is non university based Islamic finance cooperatives. Its clients vary from traditional market traders, housewives, and street trader. The observation yields that this institution are facing serious problems in its human resources. The managers of this institution are only 2 people while the clients are continued to be increasing.

Institutional Culture : Power Distance, Uncertainty Avoidance, Individualism, and Gender Relation Issues

On the Power Distance

Power distance in this research is relationship between top leaders and his/her staff in the institutions. Structured interview indicates that the power relations are so pervaded and normative in nature. The roles of the leaders are so central that allows them to make decision making though they also recognized the need to include his/her staff in the process.

On the Uncertainty Avoidance

Uncertainty avoidance is related to the risk faced by Islamic microfinance. The leaders in these 5 institutions agree that innovation needs to be adopted in order to enable them to face

changes in the society. Result from structured interview however indicates innovation is difficult to be taken because of their fear it may not be in line with Islamic principle. In some cases they were unable to transform the innovation into actions. However, according to (Karim, Tarazzi and Reille (2008), innovation through the innovative designs of a range of sharia-compliant products and services would provide greater financial access to a broader segment of islamic microfinance customers.

On the Individualism versus Collectivism

Individualism versus Collectivism refers to reward provided by the institution to its staffs. Despite of the fact that they all agree rewards need to be given yet, the managers continue to believe that they also can force their staffs to do their tasks. Such approach is very risky because it might lead to conflict. Lack of reward in the institution might be derived from an understanding that working in Islamic microfinance is already rewarded by Allah and thus sincerity in doing the tasks is necessary. It is quite paradoxical to note that despite of their attempt to eliminate poverty in the society, their staffs level of income is under minimum wage determined by Bandung city council³².

On the Issue of Gender Relation Issues

Gender Relation Issues are also found in this research. There are differences in the approach found to gender in this study. Gender relation issue here is confined to the leadership issues. Since BMT El Tazkiyya is lead by a woman and thus she assumes such issues are not important because women too can lead the institutions. While other four institutions in this research i.e. BPRS Salman, BMT Daarut Tauhiid, and BMT Syarrah prefer to maintain the

³² One of our respondents stated that they are paid about 500 thousands (equals to USD 65) per month, even though she is acting as a manager of the institution

differences. It can be found in their practices which keep women in the front line and let the managerial care be taken by males.

External Culture : Ethnicity, Urban-Migrants, Profession, and Gender Disparity

On the Issue of Ethnicity

Findings of this research indicate that the managers in the institution tend to claim that the issue of differences caused by ethnicity is irrelevant in their institution. Findings however also reveal that BPRS Salman and BMT Syarrah tend to provide service only to people with similar ethnicities. This shows the degree of ambiguity and conflict within the managers of Islamic microfinance institutions.

On the Issue of Local versus Migrants People

While the subjects in this research resist the idea of differences between local versus migrant people, yet their practices show the extent to which this issue is relevant. BPRS Salman claims that such differences do not exist and also the perspective of BMT ISEG. BMT Daarut-Tauhid and BMT El-Tazkiyya however agree on the existence of the differences between local and migrant people yet it doesn't affect their practice and product as well. BMT ISEG takes an extreme approach by giving priority to local people. Despite the fact that BPRS Salman disagrees on the existence of this issue, yet they do admit that there are differences in attitude shown by local and migrants' people in terms of managing the loans. This is contrary to what is suggested by BMT Daarut-Tauhid which claims such differences have never been seen. The perspective of BPRS Salman is similar to that of BMT El-Tazkiyya which also claims differences between local and migrants' people in borrowing and payment attitudes.

On the Issue of Profession Characteristics

All the participants in this research tend to agree that cultural differences might be the result of differences in their clients' professions. Such differences bring variations in term of performances shown by their clients. The institutions however attempt not to make discrimination on their products as the result of these differences. Thus, the products offered are mostly typical such as wadiah, mudharaba, musyaraka, and so forth. They have not attempted to create various products that may respond to the differences caused by professions.. One of the factors prevent them from doing these is their fear such actions might be departing from Islamic principles of microfinances. Only BMT ISEG that has attempted to provide profession based product by specifying their products to their mostly students clients.

On the Issue of Gender Disparity

The managers of the Islamic microfinance institutions in these researches do not agree if gender disparity issue needs to be taken into consideration. It is predicated on their belief that such differences are not exist. This finding is indeed very much interested considering of the fact that from the mainstream understanding of Islam, women tend to be seen as subordinate to men. The managers continue to believe that there is no need to create gender specific products. Yet however they also admit that women borrowers are more discipline in term of the payment. This again illustrates the degree of ambiguity in their attitudes toward the issue.

Bambang Ismawan on Cultural Aspects on the Islamic Microfinance

The result of structured interview indicates the extent to which ambiguity is found in the research participants. Most of the research participants tend to deny the fact that differences in term of gender, profession, local versus migrants' people are exists. Thus, I do another structured interview with Bambang Ismawan, microfinance practitioners in Indonesia for more than 47 years³³. The interview reveals that two factors are associated with the resistance shown by Islamic microfinance institutions managers to admit cultural differences in their clients. The first factor is derived from banking regulations in Indonesia which provide little space for innovation and the second factor is a discourse within Islam, normally associated with traditional normative Islam that do not give space for innovation. Any innovations might be considered as a depart or deviation from the true teaching of Islam. Moreover, based on the case of microfinance institution in Bali Province³⁴ and West Sumatra Province³⁵, he concluded that the declining of microfinance institutions in both provinces was caused by the lack of cultural consideration in microfinance institutions.

³³ He is known as social entrepreneur who has served in the microfinance for 47 years. His institution, Bina Swadaya has trained over 10,000 community leaders, spawned the creation of more than 12,000 grassroots self-help groups serving 3.5 million people. Launched 650,000 microfinance institutions with 13.5 million members

³⁴ In Bali, there is an institution named Lembaga Perkreditan Desa (LPD) in every Banjar (Village) that was successfully brought the microfinance institution in alleviating poverty. However, the sustainability now is declining since the government invent the new type of microfinance institution based on the new regulations implemented after 1998, and allowing commercial banks to operate in microlevel using banking system approach. According to Bambang Ismawan, the new invention of the government instead of bringing the poor people runaway from the poverty, yet it brought the poor people difficultied in accessing the money.

³⁵ In West Sumatra, there is an institution named Lumbung Pitiah Nagari (LPN) who owned, managed, and operated by the people using the Nagari (name for Village in West Sumatra) Tradition Approach. The performance was indeed successful. However, since the invention of new type of institution such as People Rural Bank (BPR), Koperasi Simpan Pinjam (KSP), etc, the institution was declined in operations. According to Mr. Bambang Ismawan, the LPN was more representative in reaching the poor rather the later.

Conclusion

Finding of this study reveals that in general research participants fail to recognize the importance of culture in Islamic microfinance. In the institutional culture, the Islamic microfinance institution tends to have a rigid organizational culture with the domination of male on female contributions. Collectivism is under consideration however the attention to the individual contribution seems insufficient to bring the institution to sustain. Innovation is accepted to be one of key factor to make the Islamic microfinance institution, but the institution tends to face difficulties in implementing it. In the external culture, they tend to deny that there is indeed differences in their clients characteristics in term of their gender, profession, and local versus migrants people while at the same time their practice indicate the extent to which such differences are indeed exist. By not recognizing the cultural differences, the Islamic microfinance in this research thus do not provide cultural specific products that may correspond to the particular needs of their clients. While reviews of literatures show the importance of cultural aspect in the development of Islamic microfinance, the findings show vice versa. Since this study is an early study of the issue, it thus opens up the possibility for further investigations and studies in the future that may provide us with more detailed understanding of these.

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