



Issues and Challenges of Financial Inclusion Among Low-Income Earners In Rural Areas of Malaysia

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Abstract: Financial inclusion (FI) appears to be one of the main global agendas as it is an essential way of reducing poverty and increasing the economic growth of a country. FI is the provision of financial services to all segments of society in a more convenient, quality, and affordable way. In this study, the authors analyzed the issues and challenges faced from the two perspectives of the Financial Institutions (FIs) and the rural B40 group concerning the way of pursuing the exclusive of FI. Primary data was collected by conducting semi-structured interviews with four expert bankers from the Financial Institutions (FIs) in Kuala Rompin, Pahang, and two representatives from the B40 customers in the rural areas of Pekan, Pahang, Malaysia. Based on the findings, barriers faced by the supply sides of the FIs include 1) high risk of cost and security, 2) barriers in communication and lack of financial education, and 3) lack of proof documents. The other challenges are 1) competition with the conventional institutions, 2) default risk due to non-payment, and 3) internet connection problem. On the demand side, the issues and challenges found include 1) lack of confidence, 2) lack of proof documents, 3) misuse of capital, and 4) lack of financial literacy. Henceforth, the findings have significant implications for the Islamic banking and finance industry in exploring the current barriers faced in delivering financial inclusion to the lower segment of the society in Malaysia.

Keywords: Financial Inclusion, rural areas, poverty, Financial Institution, Malaysia

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Introduction

Malaysia is one of the highest-earning countries among the middle-income countries that receive financial inclusion. According to Bank Negara Malaysia (BNM), out of the 22 million adult population in Malaysia, 92% own bank account(s) in 2015, in which 59% have an account at a single institution, while 33% own accounts at multiple banking institutions. This commendable achievement is the result of the effort of many authorities in Malaysia in ensuring long-sustainable growth through higher financial inclusivity. However, due to the pandemic of covid-19, the crisis has led to the economic disruption which hits the most vulnerable households and business entities. The government has provided many of the stimulus packages including the cash payout to increase the spending and stimulate the economic activities. As a result, there are active involvements by the people with the online retail payment services, fostering the financial access by the people towards the financial services.

Irrespective of the importance of the financial inclusion and the development of the payment system, the issues and challenges are remained by a small segment of people particularly among the elderly, women, and poor people living in this country. Therefore, this study provides the future contribution to Islamic Financial Institution, microfinance institutions as well as the regulatory framework in recognizing the issues and gap of the financial inclusion among the rural and poor people given this current pandemic challenges and thus enhance their strategy to cater to this problem. The paper aims to observe the state of financial inclusion among the B40 in the rural areas of Malaysia. Furthermore, the paper analyzes the barriers of the Financial Institutions (FIs) in attracting the rural people to be more involved in the Islamic financial sector. Secondly, it also analyzes the issues and challenges of the rural B40 in assessing the financial services provided by the financial institutions.

Literature review

Financial Inclusion as a Significant Tool to Alleviate Poverty

Financial inclusion (FI) is one of the significant tools in helping poor people to come out of the state of poverty. In regards to the objective of the FI to ensure all of the segments of society have financial access to the financial products and services, many past literature reviews discuss the significant relationship of FI with the reduction of poverty, increase the income distribution and maintain the sustainable growth of the economy in a country. Besides, several factors affecting the effectiveness of financial inclusion across the countries are also being studied.

Firstly, Young Park and Mercado (2015) look at the role of financial inclusion to address the issue of poverty and income equality by focusing on the development of Asian economics. The study adopted the quantitative methodology and the researcher used their financial inclusion indicator considering various macroeconomics and country-specific factors that affect the degree of financial inclusion on 37 selected developing Asian economics. Besides, the researcher also tests the impact of financial inclusion together with the control variable of poverty and income inequality. From the result, it is recognized that financial inclusion reduces both poverty and income inequality. Several factors that significantly affect the financial inclusions in developing Asia include the per capita income, characteristic of the demographic, -in which the economics with the larger population tend to have more access to the financial services. Second, the role of good governance in the provision of high-quality regulation also is important as it will reduce the financial exclusion on a large segment of the society.

Besides, the increase in the provision of delivering facilities of the financial services by the FIs is among the significant attributions in increasing the financial access to the poor people specifically those who are living in the rural areas. By evidence, Williams, Adegoke and Dare (2017) investigate the impact of financial inclusion on poverty reduction and economic growth in the developing economy, specifically refer to Africa. By using the quantitative methodology, the model of the log-linear specification framework was used to extract the data from Nigeria. Based on the result, it is shown that the increase of the ATMs, bank branches, and government expenditure are the several factors that reduce the poverty of people in several selected countries in Africa. It is observed that the increase of the active ATM is giving a positive impact on the GDP and the reduction of poverty in particular in the rural areas of the country. Similarly, Thulani, Chitakunye and Chummun (2014) examine the usage of mobile money as a strategy in accelerating financial inclusion among rural communities. This study used the mixed methodology where the survey questionnaire and focus group discussion has been conducted in collecting the data. From the result, it is observed that mobile money service has a significant complement role in increasing the financial access on the financial services towards the rural people.

Challenges of Financial Inclusion

Demand Side

There are a few past studies (e.g Aggarwal, R, 2014; Dupas, P., Green, S., Keats, A and Robinson, 2012) deliberate on the issues and challenges of financial inclusion faced by the poor people living in the rural areas. Among the challenges faced by

them are 1) Lack of financial illiteracy consisting of lack of knowledge on the significant role of financial services such as takaful and insurance, banking transaction instruments, and capital market. 2) Negative perception towards the financial system also becomes their limitation in assessing the financial services such as the high-cost financial transaction which is not appropriate to the lower-income people. 3) Lack of proof on various formal documents 4) Irregular Income 5) Lack of Trust 6) High distance between the rural areas and the town with adequate financial facilities also is the common difficulty to reach the financial services. 7) Lack of understanding of the formal language used by the formal financial system.

Supply Side

Many past studies (e.g Subbarao, 2009; Bhuvana & Vasantha, 2016) have also discussed the barriers and challenges of the financial inclusions towards the poor people living in the rural areas by taking into the perspective of the supply side of the Financial Institutions. Subbarao (2009) states that several barriers faced by the Financial Institutions (FIs) in the provision of financial inclusion towards poor rural customers include the high cost, lack of infrastructure, lack of communication, and the language barrier. Besides, Bhuvana and Vasantha (2016) further state the three main barriers faced by the FIs which are high cost, policy regulations, and inappropriate products.

Besides, a few studies (Tunde & Adeoulu, 2017; Abdul Rahman & Dean, 2013; Tania Lopez & Adalbert Winkler, 2017) investigate the challenges faced by the microfinance institutions, given its significant role that are more approachable towards the small segment of the society of the poor people. Tunde and Adeoulu (2017) examine the challenges faced by microfinance in the provision of financial inclusion for the developed SME in Nigeria. Among the challenges faced is 1) high operating cost. This challenge refers to the small unit services that incurred the high operating cost such as the process of the microcredit application, manage and monitor of many accounts 2) Repayment Problem in which the default risk by the customers towards the microfinance institutions since there is no collateral provided 3) Inadequate Experience Credit Staff where there is a need for the experienced staff in planning the product development and effective engagement with the participants 4) Lack of financial literacy- which lead to the problems of record-keeping and ability to make the decision. Similarly, Abdul Rahman and Dean (2013) conducted a study on the challenges faced by the Islamic microfinance institutions (MFI) regarding the provision of financial inclusion. Among the barriers and challenges faced by them were high administrative cost, lack of fund mobilization and low market penetration.

Issues and Gaps

Based on the previous literature review discussed above, most of the past researchers are deliberating more on the issues and challenges of financial inclusion in the rural areas of Africa and India's countries. However, in Malaysia, there is less study discussed on this particular topic. Therefore, this study highlights the issues and challenges of financial inclusion particularly among the customer of the B40 in the rural areas of Pahang, Malaysia. The data collection of the challenges faced takes into considerations from the two opinions of the supply and demand side to recognize the real prominent issues that occurred in regards to the current practices of financial inclusion in this country. As for the suggestion, the future study may develop the sample area of the study into the other rural areas situated in Malaysia as the result may be different due to the demographic and cultural practices in those types of particular areas.

Data and Methodology

The study use qualitative methodology conducting face-to-face interviews with both the supply side (each of the expert bankers from four different financial institutions) and demand sides (customers; the rural B40 community consisting of Malay and Indigenous). Consequently, the sample of the study from the supply side is in Kuala Rompin, Pahang. For the demand side, it consists of two rural areas which are i) Village of Iban- residing by Indigenous ethics and ii) Village of Permatang Tepung - residing by Malay Ethnics. Both of these rural areas (demand side) are located in Pekan, Pahang, and are merely selected because of their nearest location with the financial institutions (supply side) located in Kuala Rompin, Pahang. Typically, those of the sample areas of the study mentioned above are mainly selected due to the familiarization of the authors among those communities.

In general, the following figure is the open-ended questions that been addressed to the participants in answering the objectives of the study:

1. State of Financial Inclusion in Malaysia

- Based on your observation, can you explain to me the state of financial inclusion of the rural B40 based on their ownership of a bank account and subscribing to the takaful products with your institutions?

2. Barriers and Challenges Faced by the Banks in Delivering the Financial Inclusion to the Rural B40 Group.

- What are the challenges faced by your institutions in providing the financial services towards the rural B40?

3. *Issues and challenges faced by the rural B40 communities in Assessing the Financial Inclusion.*

- What are the challenges faced by the rural B40 in assessing the financial services provided by the FIs?

General profile of the respondents are as follows:

Table 1.

General Profile of the Respondents (Supply side)

Respondent	Financial Institution	Position	Year of Experience
Respondent 1	Financial Institution 1	Assistant Manager	8
Respondent 2	Financial Institution 2	Save Advisor of Home Financing, Personal Loan and ASB	3
Respondent 3	Financial Institution 3	Assistant Manager	7
Respondent 4	Financial Institution 4	Manager	5

Table 2.

General Profile of the Respondents (Demand side)

Respondent	Rural B40 People	Position	Year of Experience
Respondent 5	B40's Representantive (Malay)	Deputy Head of Amanah Ikhtiar Malaysia (AIM)'s Members	8
Respondent 6	B40's Representantive (Indigenous)	Head of NG of Indigenous People	3

Finding of the study

Current State of Financial Inclusion of B40 in the rural areas.

Research Objective 1: To observe the current state of the financial inclusion of B40 in the rural areas of Malaysia.

There have been several indexes and indicators used in measuring the degree of financial inclusion in which they are different accordingly across the country and the globe. According to the World Bank Group (2020), two indicators used in the measurement of the level of financial inclusion are the ownership of the bank account and the subscription of an insurance or takaful policy either directly through

the Takaful Company or through the Financial Institutions (FIs). For the first finding, Question 1 from the first set of the interview question is designed to attain the research objective mentioned above. Particularly, each of the respondents from the four of the FIs is asked regarding their observations whether the customers of the rural B40 people own the bank account and subscribe to takaful products. Those ascertainment are asked as both elements are the two basic indicators in determining whether the people have access to financial inclusion.

From the result, it is observed that most of the rural B40 people of the selected study on savings accounts and subscribe to the takaful products. Respondent 1 explained:

“There are quite many of them that have a bank account here. This is because we are doing more on the CSR project such as zakat endowment which then becomes compulsory for them to open the bank account with us. For the takaful products, we are an agent of the takaful company in Malaysia.

While Respondent 2 explained:

“Many of them come and open the bank account when they get the stimulus package of BRIM and BSH - and yes, most of them have the bank account because of that particular reason. As for takaful, we also provide certain takaful products however, we do not have the person in charge for takaful products here. They recently came from the main branch to convince the B40 in subscribing to the takaful products. To conclude, yes, many of them have subscribed to takaful from us”.

While Respondent 3 explained:

“For the poor Indigenous people, beforehand, they did not have the awareness to open the bank account. However, after we collaborated with AIM, most of them already have the bank account with this financial institution. For the B40 Malay, most of them specifically the student has the bank account due to the need of the basic financial services when they entered the school and universities.

“For takaful, most of them subscribe takaful when they apply the financing with the banks for the additional protection in case of unpredictable accidents.

While respondent 4 explained:

“Most of them open bank accounts with us because in those particular rural areas, their main activities are agriculture such as paddy fields and so on, hence for those who want to apply financing for the agriculture activities, they will open the bank account for the receiving of the cash of their financing.

Indeed, each of the respondents explains the reason for the rural B40 customers to open a bank account and subscribe to takaful products offered by the FIs. Respondent 1 and Respondent 2 state that most of them own bank account due to the social finance assistance provided by FIs such as zakat as well as the stimulus packages from the government. Those of the financial assistance given need them to open a bank account. Another reason is because of the non-strict requirement of the documentation and their satisfaction with the services provided. While Respondent 3 states that their collaboration with the AIM in the rural areas encouraged the rural B40 in opening bank accounts for the microcredit financing purpose. Finally, respondent 4 states that the application of the financing products by the customers are requiring them to open a bank account.

As for takaful, all the respondents opine that most of the rural B40 subscribe for takaful when they are applying for financing products. According to the respondent, the FIs always encourage them to apply takaful together with the financing merely for them to cover the financial obligation in case of unrepresentable events to have occurred.

To conclude, it is highlighted that the state of financial inclusion in those rural areas selected in the study is good as most of them have achieved the two financial indicators of ownership of a bank account and subscription of takaful products. Yet, it still has not achieved the inclusive of financial inclusion. This is due to several challenges faced which are deliberated in the following sections.

Respondent 1 remarks as following:

“If I was given the choice to put the level of the financial inclusion among them, it is above the medium, still not access to all of the areas”.

Barriers and Challenges Faced by the Banks in Delivering the Financial Inclusion to the Rural B40 Group

Research Objective 2: To analyze the barriers and challenges faced by the financial institutions in delivering financial services to the B40 people in the rural areas of Malaysia.

The first set of questions are specifically designed to answer this second research objective in which Questions 2 are the lead questions for the barriers and challenges faced. While for question 3, it is being asked based on the open opinion from the respondents without any guide questions provided. Therefore, based on the results of the interview, the challenges faced are:

a) High Risk of Cost and Security

The idea is to ascertain with the FIs on their opinions in regards to the barrier of the high cost for the provision of ATM, a basic financial facility in the rural areas where the demand sides of the rural B40 customers lived. Two of the respondents opined that the establishment of the ATMs services incurred higher costs. Indeed, both respondents state that the cost incurred includes the cost of the establishment of an ATM and its maintenance that would require a huge budget due to its far location from the town. Apart from that, a high-security risk is another reason why the barriers exist. The provision of this facility requires stringent security controls as a lot of money in the ATMs expose to the higher risks of theft and robbery, especially in such remote areas.

Respondent 1 explained:

“A few of them request us to open the ATM. However, to open the ATM, we will conduct the research and different types of aspects need to be tolerated such as lack of security, high request from the population and high cost.”

While respondent 3 explained:

“There are quite a number of them who already request the provision of an ATM in their place. However, we rejected the application although there is quite a high population there. This is due to the high maintenance cost of the ATM, accessibility of the server, and security”.

However, when the respondents are asked about the possibility of the provision of an ATM in the future, two of the respondents have answered that there is an opportunity for it. It is explained by one of the respondents that there is an opportunity for its provision when the FIs get the higher penetration of the market. As the customers are supporting FIs and more involved in the financial services provided, the revenue from the deposit, investment, and financing of the customers becomes more sufficient to cover both the cost and security.

Respondent 3 explained:

“Yet, there are possibilities for the provision of ATMs there when there is high penetration of the market and get the support from the customers. This is because all of the cost will be borne by the branch banks and for the banks to cover the cost, it will take the profit from the financial transaction’s fees and financing from the customers

Meanwhile, the respondents explain the setting up of the agent bank, an alternative for the provision of the basic financial services such as withdrawal of money, opening the bank account, bill payments, and money-saving. Through the agent bank, FIs appoint an agent from the small groceries and shops located in the rural areas to provide the basic financial facilities. However, two of the respondents argue on the challenges of the agent bank itself. It is observed that the small retailers must prepare their deposit in advance for the money withdrawal. Hence, it has become a difficulty as there is uncertainty on their daily cash flow income. Also, it increases the safety risks of the agent banks themselves as many would consider the small kiosks and shops have a lot of money.

Respondent 2 argued:

“AB is a good alternative in helping the poor people who are staying far away from the town to make basic financial transactions such as money withdrawal. However, there are complaints from the kiosk and small shops themselves in which they need to make use of their money first. They do not prefer to use that method as they claim that the sale revenue received may not be enough to circulate and use for the agent banks services”.

Respondent 3 argued:

“AB has many slack because the retailers must use their own money to make the basic financial transaction with the customers. Furthermore, it will increase the risk of the non-safety of the agent banks themselves as the surrounding people will have the perception that the agent’s banks have a lot of money”.

Likewise, one of the respondents sees that the agent bank’s services are merely effective in helping the people who are staying far away from the town to make the basic financial transactions. According to the respondent, their institution does not have any problems as mentioned above. Unlike other FIs that choose small shops and groceries randomly as their agent banks, our institution has several criteria for the retail outlets who want to be appointed as our agent. The criteria, such shops must first be registered with the agencies of the cooperative and ministries of Malaysia. Then, they are eligible to be appointed as the agent banks of our financial institution. Yet, according to the respondents, another problem is faced when no eligible person is wanting to manage these facilities. Plus, there are sometimes internet connection problems that cause the transactions to be slower.

Respondent 4 explained:

“As for the provision of the agent bank, we do not have the problems with that service facility as we think that this initiative effectively works to help the people who are staying far away from the town to make the basic services of money withdrawal. Only sometimes, there is no one to manage the facilities and the internet connection problems”

To conclude, it is observed that one of the main barriers for the banks to untapped this lower segment of society in providing them the basic financial facility of ATMs is because of the higher cost incurred by the financial institutions. The higher cost of its establishment, maintenance as well as the requirement of having higher security make the ATMs unable to be provided as the FIs need to bear the higher expenses as compared to the revenue received. As for alternatives provided by the government which is the agent bank, these financial facilities also have several factors hindering its benefit to the particular rural B40 people such as the lack of capital, risk of insecurity, and lack of mobile network services.

Barrier in Communication and Understanding of Financial Education

Another challenge faced is the lack of financial education among the customers of B40 in the rural areas.

Respondent 1 explained:

“The level of their understanding is below par because there are quite many of the Indigenous people transact with us. Hence, because of their low level of education and financial literacy, it is quite hard to explain to them. But for the government employees, such as the teachers, they are easy to understand with our explanation on the financial products and services.

While respondent 2 explained:

“As mentioned before, there is no involvement from the B40 from the rural areas itself, but for the B40 employees who work on the plantation, yes, they are easy to understand on the products itself”.

While respondent 4 explained:

“Most of them who have basic education such as the teachers, formal employees, yes it is easy to communicate with them, but for the lower educated people such as Indigenous people, they do not apply the financing with us maybe because of their

lack of awareness by them. And for the Indigenous people, the one who remains on the traditional way of practice will not understand very well but for the modern Indigenous people, they have some of the understanding”.

Furthermore, one of the respondents had explained that, for the lower educated people, the use of their local daily language is preferable to communicate with them as they become more comfortable and easier to understand.

Respondent 3 explained:

“Most of them are easy to understand the basic financial services provided as long as we are speaking the common language used by them.”.

Respondent 3 explained:

For other investment products such as unit trust, most of them reject these products because of their preference with the low risk, low return and secure. However, for ASB, as such, there are quite a number of rural B40 people who open ASB with us. They know these products from the mouth and mouth and promote from POS LAJU as such”.

While Respondent 4 explained:

“For the B40 from the Indigenous people, until now, none of them apply the financing with us maybe because of their lack of awareness by them”.

Accordingly, all the respondents agree that the financial education difficulties only happened to those lower educated people encompassing the customers of B40 people from both Indigenous and Malay. Hence, there is a gap between the lower educated and moderate to higher educated people in which the educated people are easier to understand when they are well-explained by the bank’s staff. However, most of the respondents opined that the lack of financial education is more crucial among the rural B40 of the Indigenous community thus hindering them to be more involved in the financial services provided by FIs. It is observed that, in communicating with them, it is preferable to use their common language as it creates some benefits of stronger relationships between the FIs and the rural B40 communities. Thus, the feeling of camaraderie attracts them to be more involved in the financial industries.

c) Lack of Proof of Document

The lack of proof documents by the rural B40 customers is another barrier faced by the FIs. The proof of document is important for the FIs for the identification process and the eligibility of the customer to get the financing from the FIs. In dealing

with the customers, several assessments need to be done as several risks need to be encountered from the perspective of the supply side. Therefore, in this part, the respondents are asked about this barrier faced.

Respondent 2 explained:

“When they want to apply for home financing, some of them have difficulties in fulfilling the document requirement such as the statement bank. This is because most of them are working in private, then, they need to request first from the head of the village unit for the payment slip endorsement. Even when they are having the payment slip, some of them received the payment in cash and not saving it in the banks. Hence, we are having the difficulties to match between the bank statement and the payment slip. However, in this case, the applicant is still processed but will take more process”.

While respondent 3 explained:

“Regarding the lack of proof documents, as I mentioned before, there are no strict requirements on the basic transaction of opening the bank account. However, for other financing products applied by employees from the private sectors, we will look into their annual income statement of KWSP. For the self-business, we will reject the application of the personal financing if they cannot provide the documents required. But for home financing, we can still tolerate it”.

While respondent 4 explained:

“Another barrier faced is their lack of document required. As our bank’s principles are more on agriculture, then we must face the higher risk when dealing with the customers. Some of them do not have the formal sale records, hence, it will take a longer process for the financing to take place since we must educate them first to make the sale records. On the other hand, some of them who are practicing the business in the traditional way, do not even have the bank statement because they are saving their money on their own”.

In view of that, all the respondents agree that most of the rural B40 can provide the basic proof document of the identity card for the opening of bank accounts. Also, for the financing products as such, most of them fail to provide so due to more requirements from the customers. The problems occur when they are having difficulties in providing formal documents such as the sales record, payment slip, and bank statement. Thus, the lack of their proof documents will consume more time for the processing of financial products. It is becoming worse when one of the respondents stated that their application will be rejected if they fail to fulfill the document required by the banks.

Other Challenges

Apart from the challenges mentioned above, the respondents are also being asked about the other barriers and challenges faced by the banking institutions in achieving the inclusive of financial inclusion. Thus, the barriers faced are:

a) Competition with the Conventional Counterparts

In general, this challenge is identified and obtainable from the second respondent of the Financial Institution 2. As the bank serves both the conventional and Islamic financial products to their customers, hence, it is recognized that the Islamic home financing products are offered a higher financing rate and amount of financing than the conventional parts. According to the respondent, the low-income customer will be only offered on the conventional home financing products first as it offers the lower financing amount. If the customer wants to get a higher amount of financing, then he/she will give the choice to opt for either conventional or Islamic home financing. Consequently, these situations later cause negative perceptions by the customers towards Islamic banking products.

However, the respondent from Institution Four has opined that the Islamic banking products are not offered at a high rate since there is a ceiling price for the financing amount and there is no interest charge if exceeding the capped amount. Differ with Islamic, although the beginning financing amount of the conventional might be lower, however, the price may increase further based on the change of base financing rate (BFR). Hence, according to the respondent, this perception must be corrected and well-explained to the customers when they want to apply for financing by the bank staff.

Respondent 4 argued:

“I opined that the Islamic banks’ financing is actually cheaper than conventional because we have the ceiling price and will not exceed the above ceiling price. As for conventional, the price may further increase based on the BFR. Furthermore, although our financial institution is not a governmental institution, we are offering a much cheaper financing amount as we have received much help from the government. With this advantage, the customers will get the subsidies and have to pay only a small amount of the financing”.

The fourth respondent from Institution 4 also stated that other barriers faced by their institutions are the competition with the conventional counterparts in attracting the customers. However, the respondent stated that they are reaching higher performance in the meantime.

To conclude, it is identified that some of the financing products offered by the Islamic FIs are having a higher rate than the conventional ones. Thus, it leads to the negative perception and lack of involvement by the customers of rural B40 into the Islamic Financial Industry. However, it is arguable that this perception must be corrected and explained to the customers. Besides, as the IFIs are not practicing the interest (riba), there is a ceiling price if the BFR increases where the extra financing amount is up to the selling price only. In contrast, the conventional total payable loan amount might be uncertain as it does not have the limit of ceiling price when the BFR increase.

b) Default Risk due to Non-Payment

This challenge of the default risk is related to Financial Institution 4 which its mandated role is on agriculture. Accordingly, this institution is offering financing to the customers of the rural B40 who are involved in the agriculture activities of plantation agriculture and farming. Thus, this institution is facing agricultural risk as the success of the financing is dependent on climate change itself.

During the interview, the respondent explains the certain agriculture-based financing and microcredit products which are specifically designed to meet the financial need of the rural B40 people. However, it is identified that they must bear with the risk of failure of debt payment by the customers. Therefore, they have conducted a strict assessment when they want to approve the financing. Respondent 4 explained:

“We are facing the risk of default of payment in case their agriculture business activities are not succeed. As for financing for B40, they do not have to provide the collateral, then we are assessing their financial positions by details. Given the current impact of the covid-19, we are also affected by it as most of our customers are from agriculture and tourism-based activities”.

In conclusion, the barrier faced by this financial institution is the credit risk in which there is the potential risk of default specified by the customer of the rural B40. Indeed, the respondent explains that the issue of the default payment happens when the poor farmers, for instance, fail to fulfill their financial obligation due to the crop failure of their plantation activities.

c) Internet Connection Issues

Respondent 3 remarks:

“Another challenge we faced is on the internet issues/electricity. Here, there are always problems with no internet. Consequently, the financial transaction process will get stuck and make it a longer process”.

As the FIs of the selected study is located in a small town, all of the respondents agree that the internet connection problem is one of their barriers as it reduces customer satisfaction. Accordingly, the respondents stated that the slower internet connection makes the transaction take an even longer time than normal. By evidence, there are several cases of break of the internet connection that cause their customer's transaction to be stunted.

Demand Side

State of Financial Inclusion

Research Objective 1: To observe the current state of the financial inclusion of B40 in the rural areas of Malaysia.

Question 1 from the second set of questions is specifically designed to answer the first research objective mentioned above. Particularly, the researcher is attaining the personal view and experience from the demand side: customers of the B40 in the rural areas of Kuala Rompin, Pahang, Malaysia. Accordingly, a representative from the rural B40 of indigenous people is selected as the respondent in representing their opinion on the state of financial inclusion among them. Referring to the previous finding of the interviewees of the supply sides, indigenous communities are the ethnics who have the higher exclusive of financial inclusion in these remote areas. Thus, by conducting the interview, it is expected that the researcher will get an in-depth insight into the current circumstances of financial inclusion among the B40 communities. In detail, the respondent is asked whether the rural B40 Indigenous are having the two basic financial services of saving bank account and takaful products as they are the two basic indicators in determining the state of financial inclusion.

Hence, in terms of owning the saving bank account, the respondent believes that 50% of them own the saving bank account while the remaining does not have any of the saving bank accounts.

Respondent 5 explained:

“From my observations, 50% of them have the bank account for the savings purposes while the remaining of the 50% are saving their cash money in hand”.

The respondent further adds, 50% of the B40 of the Indigenous communities own the saving bank account due to the purpose of further education by the children.

They are required to open the saving bank account for the education and school administration fees. Apart from that reason, there is financial assistance provided

by the Indigenous Development Department (JAKOA) for their academic purpose. Henceforth, it is a requirement for them to have the saving banks account to receive financial assistance.

As for takaful products, the respondent stated that 70% of them subscribe to the takaful products while the remaining one is still declining on this protection services provided by takaful institutions.

Respondent 5 explained:

“70% of the communities in this particular rural area have the takaful products and the remaining 30% do not have the takaful products.”.

On average of both two financial inclusion indicators, about 40% of the rural B40 of the indigenous communities are severely financially excluded. As for the saving bank account, about 50% of them are not own the saving bank account due to their preference to save money while for takaful, its penetration in this particular rural area is quite high due to the social influence among the community. Thus, each of the issues and challenges faced is discussed accordingly in the following sections.

Issues and Challenges faced by the rural B40 communities in Assessing the Financial Inclusion

Research Objective 3: To analyze the issues and challenges faced by the rural B40 communities in assessing the financial services provided by the Financial Institutions in Malaysia.

The second and third sets of questions are specifically designed to answer the third objective of the study. The second set of questions are asked on the rural B40 of indigenous communities on their challenges of financial inclusion towards the Financial Institutions. While the third set of questions are asked on the rural B40 of the Malay people. This part is discussing the issues and challenges faced by the rural B40 communities towards Amanah Ikhtiar Malaysia (AIM)-a microfinance institution in Malaysia.

Respondent 5: Rural B40 of Indigenous People

Based on the result, it is observed that the issues and challenges faced are as follows:

a) Lack of Confidence

Based on the respondent's observance, lack of confidence is one of the main factors which hinder the B40 of Indigenous in this rural area to be more involved with the underlying financial infrastructure provided by the formal financial institutions.

Respondent 5 explain:

“They lack confidence when it comes to the formal financial transaction. Specifically, they are feeling uncertain whether the transaction that they are doing is as accurate as the truthful way of financial practice”.

Accordingly, their low-esteem behavior is influenced by two factors of low-level financial education as well as the lack of financial ability in fulfilling the financial obligations. The second reason, their lack of confidence is because of the social isolation which hinders them from being involved in the financial sector. Most of them are working in the informal sectors and self-employed, thus, they have no fixed-income. By this means, they lack the ability in paying back all the debt obligations consistently. For instance, although most of them are aware of subscribing to takaful products, they are having difficulties with the consistent pay for the takaful monthly contributions.

b) Lack of proof of documents

Another challenge is their lack of proof of documents. As for the basic transaction of opening the bank account, it is not difficult for them as there is not much proof of document requirements requested by the FIs. However, certain financing products, are not eligible for them.

Respondent 5 explained:

“As for the employees in the formal works, they do not have the problems in fulfilling the requirement as they have the formal payment slip and bank statement. However, for the people who are working on their own such as in agriculture activities, they do not have these two important documents, thus, they are not eligible for the financing products offered by FIs”.

Thus, it is observed that the strict requirements by the FIs are another challenge faced by them specifically in terms of the financing product. Most of them are unable to provide several proof documents needed by the FIs such as payment slips and the bank statement. With regard to the non-exist of either one of the documents, they are unable to provide proof of a stable income. Though some of

them are self-employed and have the payment slip, some of them fail to provide the account statement bank as they are saving the money with cash in hand. This problem is becoming worse as their non-eligibility to get the financing makes this segment of the society further left behind in financial access.

c) Lack of Financial Education

The third challenge is their lack of financial education. According to the respondent, this difficulty they are facing is dependent based on the knowledge gap. As for the people who have basic education, it is easier for them to understand the basic financial services of opening a savings bank account, investment and financing product as well as the takaful product compared to the lower educated people.

Respondent 5 explained:

“As for the communication, it depends on their academic level as well as their awareness on the significance for each of the financial products offered by the FIs”.

Besides, the respondent is also asked about the participation of the rural B40 of Indigenous communities with AIM (a microfinance institution) in that particular rural area as well as any issues and challenges faced.

Respondent 5 explained:

“From my observation, there are only 15% who are currently participating in the micro credit financing provided by AIM. This is because of their lack of skill in managing the money and business”.

To conclude, it is observed that the state of the financial education of the rural B40 people from the communities is between low to moderate level. According to the respondent, though they have the basic education of the primary school, however, when it comes to the matter of financial services, they do not have the knowledge on it. Furthermore, it is indicated that there is less involvement by them in the microfinance institution as there are only 15% of them who participate in the AIM. This is due to the lack of understanding of financial education as well as their lack of awareness of the privilege provided by the micro institutions. From the rural B40 people of the Indigenous communities who are currently participating, some of them are effectively getting benefits from it while some of them are not able to circulate the money in generating income due to their lack of skill in financial management.

Respondent 6: Rural B40 people of Malay Community

The idea for this part of the finding is to get the viewpoint of the rural B40 people towards the microfinance institution as it is the informal entity that is more approachable among the B40 people in the area. Thus, a respondent who is positioned as the AIM's representative members is asked about the particular issues and challenges faced among the participants (which is called SAHABAT) when they are dealing with the microfinance institution. Based on the result, among the challenges are:

a) Misuse of Capital

Based on the respondent's observance, the misuse of capital is one of the core challenges faced by the rural B40 people when they applied for micro-financing by the AIM.

Respondent 6 explained:

“One of the challenges is the misuse of capital provided to them. For instance, during the registration, they put a type of business in the registration form but the real business they do are otherwise. These issues will become the problem in case there are problems raised in the real business they do, then, they will be problems in the claim process.

Second, the misuse of capital happens when they apply the financing for another person (between the families). In case the person responsible already dies, then the loan will be given as a gift (hibah) to the dead person (SAHABAT). Eventually, the real person who is receiving the microcredit financing will be free from paying the debt. We are monitoring strictly any misuse of the capital but sometimes, they are hiding the information from us. But now, we are becoming stricter and trying to find the real practice of them. These challenges will not resolve but we can control the problems from becoming worse”.

In view of that, the misuse of capital for the microfinancing provided by the AIM is among the core issues needed to address. Particularly, this behavior happens because of the lack of common sense and responsibility among them. As such, those of the AIM's members (SAHABAT) are using the borrowed money as their permanent financial desires and not for generating income purposes from the business activity. Besides, the lack of integrity is present when they do not strictly follow the rules of AIM itself. Thus, these behavioral actions become one of the bad attitudes that need to change and positively improve.

b) Lack of Financial Literacy

Another challenge faced is the lack of financial literacy by the means of their lack of education regarding the knowledge of the financial. The respondent opines their lack of financial literacy is due to the two reasons of the financial management as well as the lack of communication and understanding. The details of the challenges are discussed in detail in the following sections.

i. Financial Management

By the definition, financial management is the process of making a financial decision on the analysis of the money and investment. According to the respondent, some of the SAHABAT do not have the skill on how to manage their money and generate income from the business activities. As such, there is a case of SAHABAT who is working on the self-business who cannot repay his debt obligations towards his retail supplier because of the responsibility of repaying the debt to AIM every week. However, the respondent further argued that this issue happened not due to the ineffectiveness of AIM itself, but it is because of the lack of financial management skills by the applicants themselves.

As quoted by the respondent:

“That is because they don’t have the knowledge on how to use the financing amount given to them”.

ii. Lack of Communication and Understanding

The next challenge is their lack of communication and understanding. In practice, they are quite difficult to understand when the information is delivered using social media. Hence, weekly meetings are only suitable timing for the AIM’s representative to explain and educate them. However, it can be observed that there is a gap between the educated and uneducated people in the level of their understanding as according to the author, this challenge occurred only to the non-educated people.

To end with, one of the crucial challenges faced by the rural B40 communities is the lack of financial literacy. This includes the lack of financial management as well as the lack of communication and understanding of financial education itself. However, the respondents emphasize the gap of financial knowledge in which the issues mentioned above only occurred to those who are having low educated people while for the moderate to a high level of educated people, it is easier to explain to them

Conclusions

The progression of financial inclusion in Malaysia has brought about a significant impact to alleviate poverty, particularly among the B40 in the rural areas of Malaysia. Based on the finding of the study, it is observed that the penetration of the financial inclusion among the rural B40 in the selected study shows the positive result as most of them have fulfilled the two indicators in determining the assessment of the financial inclusion, which are own the bank saving account and takaful. However, there are remains untapped rural B40 group that not fully utilize the financial services offered by FIs such as the financing and investment products. This is due to several issues and challenges faced by the supply side (FIs) as well as the demand side (rural B40 customers). The involvement of this untapped society with the financial industry is important as it enables them to step out of poverty and in the meantime decrease the issue of inequality in the society. Looking into the wider perspective, financial inclusion not only helps to boost up the financial position of an individual or a family but also empowering the communities and helps to invigorate economics. Therefore, by recognizing in detail the current challenges faced, the finding of this study is expected to contribute towards the Islamic financial institution, microfinance institutions as well as the regulatory framework in recognizing the gap of the financial inclusion among the rural and poor people and thus enhance their strategy to cater with this problem.

Recommendations

Based on the challenges of financial inclusion mentioned in the previous part, there are several recommendations to increase the penetration of the financial products and services to the rural B40 customers. First, with regards to the access of the financial services in the rural areas, it is observed that several factors are hindering the effectiveness of the agent bank in those selected rural areas includes lack of capital, lack of management, and security control.

Thus, there is a need for the regulator and the FIs to revise back its operation and enhance the operation of agent banking across the country. By using agent banking, the rural B40 customers can benefit from it as no need for them to travel far from home only to make the basic financial services such as withdrawal of money. Second, a lot of initiatives must be created towards improving financial education among the communities. Through financial illiteracy, it will increase the understanding and awareness of the rural B40 communities towards financial products and services. For that reason, financial management as one of the financial knowledge needs to be a concern as it will help the customers in making the appropriate financial decision.

Pertaining to the issues of the lack of confidence, it is encouraged for the financial institutions as well as the microfinance institutions to make the social engagement activities with the rural B40 communities at least twice a year. By having more on the community's activities, it will strengthen the relationship between both sides that will later give them comfort and self-confidence when dealing with the formal financial institutions. It is also encouraged to use the common local language of the communities in the rural areas to understand them in detail. On the other hand, from the perspective of strict requirements of the proof of documentation, it is advisable to leverage this requirement process with the fintech technology.

Looking into the perspective of the microfinance institutions provided in the selected rural areas which are Amanah Ikhtiar Malaysia (AIM), it is observed that one of the main challenges faced among the b40 rural customers is the misuse of capital. To resolve this issue, it is encouraged for AIM to have the higher strict monitoring on the members of the AIM themselves. By making the regular monitoring and deepening assessment on misuse of capital by them, therefore, these issues will be managed to reduce.

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