



Developing the African SME Market through Islamic Crowdfunding

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SME Market in Africa

- North Africa, more opportunity-driven
 - Mindset to create and develop economic activity by blending risk-taking, creativity and/or innovation with sound management, within a new or existing organization
- Sub-Saharan Africa, more necessity-driven
 - Driven by need to generate income for a living due to lack of job opportunities

Major Constraints Facing SME Market

- Include: informal sector, taxes, political instability
- Most importantly, access to finance
 - The missing middle is almost totally underserved, “too big for microfinance, too small for venture capital funds and too risky for banks”
- According to World Bank Enterprise Survey, in Sub-Saharan Africa:

	Small	Medium
Companies identifying access to finance as their major constraint	47.9%	41.1%
Companies with line of credit or loan from financial institutions	16.2%	31.9%

SME Market Status

- Vast majority of SMEs/Entrepreneurs, need access to capital
- Vast majority of potential investors have limited capital and are looking for similar investment opportunities as available to the big industry players
- Burden on governments too high, loss of opportunities, and brain drain
- Big percentage of Islamic population
- Urgent need to develop an alternate, non-banking, ethical, Islamic finance tool to respond to SME /societies needs
- Opportunity to tackle the problem through increasing the pool of financial assets available to the missing middle through crowdfunding

Crowdfunding Basics

- Crowd funding refers to a **collective cooperation** of a network of people to gather mainly financial resources in the form of donations or investments to support the initiatives of others willing to establish, build or develop a specific business or project.
- Relying thus on the “power of the crowd” and **utilizing the internet**, social media and e-payment gateways
- According to Massolution, the total Crowdfunding market valued at \$5.1B in 2013 – it kicked off in 2009

Types of Crowdfunding

- Reward-based crowd funding
 - Backers receive an appreciation or product for supporting an initiative
- Lending-based crowd funding
 - Investment vehicle through which crowd investors provide loans in exchange for returns in the form of interest payments
- Donations-based crowd funding
 - Support initiative from philanthropic perspective without expected compensation – mainly used in micro financing
- Equity-based crowd funding
 - Investors receive shares in the venture financed and are part of a profit-and-loss sharing agreement with the funded startup

Shariah-compliant Crowdfunding offers

- An opportunity to utilize crowdfunding in a Shariah-compliant manner underpinning the core ethical, social dimensions of Islamic finance, and the demand for it
- Realistic solution for a major SME constraint
- A new asset class for remittances and smaller investors instead of savings, real estate and domestic stock markets

World Bank Migrant remittance Inflows (US\$ million)	2010	2011	2012e	Remittances as a share of GDP, 2011 (%)
Egypt, Arab Rep.	12,453	14,324	20,515	6%
Jordan	3,641	3,453	3,643	12%
Lebanon	7,653	7,531	7,472	18%
Morocco	6,423	7,256	6,894	7%
Tunisia	2,063	2,004	2,198	4%

Equity-based Crowdfunding Advantages

- Is based on a **profit and loss sharing basis**
- Providing **access to capital** to a wider range of entrepreneurs
- Opening up **a new asset class** for small and medium investors
- **Minimizing risk** through splitting limited capital across multiple start-ups
- Promoting **innovation**
- **Creation of jobs** through the established start-ups/SMEs
- **Keeping the talent locally** instead of mind migration
- Supporting the growth of ventures to enterprises and **possible future IPOs** in new sectors such as the technology and health sector which are almost non-existing in the public equity markets in Muslim countries and thus increasing diversification for fund managers

Shariah-compliant Equity-based Crowdfunding

- Main requirements
 - Investments have to be **social responsible and ethical**
 - Companies have to be **operating in Shariah-compliant business** and have no income from non-compliant activities
 - **Legal restrictions** to ensure that the startups do not raise interest-based debt, deposit cash, invests in non-compliant instruments, or extends the product and service portfolio to include non-compliant activities in the future
 - **Shareholder structure** and investor protection requirements have to be designed to adhere to Shariah principles

Equity-based Crowdfunding Challenges

- Regulatory Framework
- Political Insatiability
- Market Maturity
- Lack of success stories and exists

Shariah-compliant Crowd Funding Models

Financing For	Crowd Model	Potential Beneficiary	Instrument With End Client
Savings	Saving	Personal MSMEs	Saving
Islamic Charity	Donation	Microfinance	Hiba Qard-Hasan Murabaha
Product	Reward	Microfinance Small Enterprises Startups	Sale Salam
Investment	Debt	Microfinance	Murabaha
		Small Enterprises	Ijarah
	Equity	Small Enterprises	Diminishing Musharakah Musharakah
		Startups	Musharakah

Thank You

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