

Assessing the Effectiveness of *al-Qard al-Hasan* Financing (A Case Study of *Baitul Misykat* Microfinance Institution in Aceh)

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Abstract

Al-qard al-hasan, a non-profit Islamic financing model, holds great potential in empowering marginalized communities. However, its practical implementation and long-term sustainability within Islamic microfinance institutions (IMFIs) remain limited in research, particularly in terms of integrating non-economic elements, such as spirituality. This study analyzes the effectiveness of *al-qard al-hasan* financing implemented by Baitul Misykat in Aceh, with a focus on spiritual development as a key strategy for economic empowerment. Using a qualitative phenomenological case study approach, data were collected through in-depth interviews, field observations, and document analysis. Findings show that *al-qard al-hasan's* financing significantly contributes to the economic empowerment of small traders. Effectiveness is influenced by four interrelated factors: strict beneficiary selection, continuous business monitoring, innovative non-monetary repayment incentives, and integration of spiritual development programs. These elements foster borrower discipline, ethical conduct, and business sustainability. The involvement of government officials, religious leaders, and economists enhances institutional capacity and community confidence. This study introduces a novel perspective by demonstrating how spiritual mechanisms can be synergized with Islamic finance to shape ethical entrepreneurial behavior. It offers a scalable and replicable model for IMFIs, suggesting that integrating ethical-spiritual education into financial systems may support poverty alleviation and inclusive development strategies in Muslim-majority societies.

Abstrak

Al-qard al-hasan, sebagai model pembiayaan sosial, memiliki potensi besar dalam memberdayakan komunitas marjinal. Namun, implementasi praktis dan keberlanjutannya pada lembaga keuangan mikro syariah (LKMS) masih minim kajian, terutama terkait integrasi aspek non-ekonomi seperti spiritualitas. Studi ini menganalisis efektivitas pembiayaan *al-qard al-hasan* yang diterapkan oleh Baitul Misykat di Aceh, dengan fokus pada pengembangan spiritual sebagai strategi utama dalam pemberdayaan ekonomi. Menggunakan pendekatan studi kasus fenomenologis kualitatif, data dikumpulkan melalui wawancara mendalam, observasi lapangan, dan analisis dokumen. Hasil penelitian menunjukkan bahwa pembiayaan *al-qard al-hasan* secara signifikan berkontribusi terhadap pemberdayaan ekonomi pedagang kecil. Efektivitasnya dipengaruhi oleh empat faktor yang saling berkaitan: seleksi penerima manfaat yang ketat, pengawasan usaha yang berkelanjutan, insentif pelunasan non-moneter yang inovatif, dan integrasi dengan program pengembangan spiritual. Unsur-unsur ini mendorong kedisiplinan, perilaku etis, dan keberlanjutan usaha. Keterlibatan pemerintah, tokoh agama, dan ekonom turut memperkuat kapasitas lembaga dan kepercayaan masyarakat. Studi ini menghadirkan pendekatan baru dengan menunjukkan bagaimana pembinaan spiritual dapat disinergikan dengan pembiayaan syariah untuk membentuk perilaku kewirausahaan yang etis. Temuan ini menawarkan model kebijakan yang dapat dikembangkan dan direplikasi oleh LKMS, serta menunjukkan bahwa integrasi pembinaan etika-spiritual dalam sistem keuangan dapat mendukung strategi pengentasan kemiskinan dan pembangunan inklusif di masyarakat Muslim.

Keywords:

Effectiveness; *qard al-hasan*; microfinance; community empowerment; poverty alleviation.

How to Cite:

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Introduction

Al-Qard al-hasan, or benevolent loan, is a unique instrument in Islamic finance, rooted in the ethical and spiritual principles of Islam. The Quran emphasizes the merit of providing qardh hasan as an act of altruistic support (e.g., Q.S. al-Baqarah: 245, al-Hadid: 11), where lenders extend financial aid without expectation of profit or material compensation. Junaidi (2017) contends that *al-qard al-hasan* is inherently non-commercial and based on cooperation (*ta'awun*); this is because in the *al-qard al-hasan* (contract), the borrower only repays the principal loan without any additional charges. It represents the broader Islamic moral economy, which aims to promote justice, compassion, and solidarity in financial relations (El-Gamal, 2006).

Unlike commercial loans or profit-sharing contracts, *al-qard al-hasan* is intended to address the immediate needs of the financially disadvantaged, offering an ethical alternative to exploitative lending methods (Obaidullah & Khan, 2011). While some scholars associate it with charity instruments like *sadaqah* or *zakat*, others emphasize its role as a revolving fund that promotes microentrepreneurs and marginalized communities (Haneef et al., 2013). Therefore, in Islamic financial institutions, the *al-qard al-hasan* is used as capital to assist micro/small businesses or the social sector (OJK, 2017).

Nowadays, *al-qard al-hasan* has been extensively implemented across various Islamic countries, with different levels of success and challenges. In Malaysia, *al-qard al-hasan* is implemented as a financing product in Malaysian Islamic banks. CALF Berhad offers *al-qard al-hasan* exclusively to its employees for specific non-commercial purposes such as marriage, childbirth, education, and emergencies (Abidin et al., 2011).

In Bangladesh, *al-qard al-hasan* has been successfully implemented, particularly through the Fael Khair Waqf (FKW) Program, which has had a positive impact on reducing multidimensional poverty. By integrating *al-qard al-hasan* with waqf and disaster recovery initiatives, the program has proven to be a powerful mechanism for alleviating poverty and promoting economic empowerment in vulnerable communities (Muneer & Khan, 2022).

Al-Qard al-hasan has been widely practiced in Indonesia, both at the grassroots and institutional levels, and has shown promising results in promoting financial inclusion and social welfare. Many Baitul Maal wa Tamwil (BMTs) or Islamic cooperatives offer *al-qard al-hasan* financing, which is derived from *sadaqah*, *infāq*, and *zakat*. These funds are distributed to microbusiness owners without requiring collateral or interest (Febianto & Ashany, 2015).

Meanwhile, *al-qard al-hasan* financing offers significant potential for empowerment and improvement in community welfare; it also faces challenges, including moral hazard, default risk, and funding limitations (Syahid et al., 2024). Moral hazard remains a critical challenge in *al-qard al-hasan* financing due to its altruistic and non-collateralized nature. Many cases show the recipients perceived *al-qard al-hasan* as charity rather than repayable financing, leading to non-compliance and weakened institutional trust. Thus, preserving program integrity requires efficient screening and follow-up procedures, ethical reinforcement, and social control (Rahman, 2010).

Default risk is also a significant issue, as these loans are often offered to individuals or micro-entrepreneurs from low-income or vulnerable backgrounds. To mitigate this risk, Islamic microfinance institutions must integrate risk assessments, financial education, savings incentives, and supportive repayment structures that align with the ethical and social spirit of *al-qard al-hasan* (Abidin et al., 2011). Another concern is about the sustainability of *al-qard al-hasan* due to its operational challenges. The lack of profit or service charges makes it difficult for Islamic financial institutions to cover administrative costs and remain viable (Obaidullah & Khan, 2011). Dusuki (2008) contends that without an integrated revenue stream, such instruments are unlikely to reach scale or systemic relevance.

Despite certain limitations and obstacles encountered in its application, *al-qard al-hasan* has demonstrably contributed to the advancement of community-based economic development and empowerment (Hasan et al., 2021). Furthermore, *al-qard al-hasan* also promotes sustainable development when it is incorporated into the entire shariah-compliant financial portfolio, such as zakat or waqf (Zahri et al., 2023). Abdullah & Ismail (2017) argue that cash waqf characteristics such as permanence, irrevocability, and perpetuity differentiate waqf from other types of donations. Therefore, cash-waqf-based Islamic microfinance can serve as an alternative source of funding for sustainable microfinance. As the donors of cash waqf do not aim to make financial profit, waqf-based Islamic MFIs will be able to provide low-cost capital to poor entrepreneurs. This condition requires good corporate governance as a vital element to ensure sustainability. Furthermore, to secure the perpetuity of the waqf, it is suggested that only revenue from the waqf property should be used for microfinance funds.

Social capital also plays a crucial role in the successful implementation of *al-qard al-hasan* within Islamic microfinance. Both concepts are closely linked, as they rely on trust, cooperation, and community empowerment to combat poverty and financial exclusion. Hadi Nurcahyono and Ghufonudin (2020) state that social capital, characterized by features such as networks, norms, and trust within social organizations, facilitates coordination and cooperation for mutual benefit. This was evidenced in the case of BMT Tumang, where social capital played a vital role in its growth and integration within the community. Islamic-based norms were instilled in both members and customers. At the same time, trust between the community and the institution was strengthened through the implementation of good corporate governance (GCG), reflected in its professional services. Reciprocity was built through the provision of financial assistance and sponsorship for community events. Community-based Islamic financial instruments, such as Bungkesmas (Tabungan Kesehatan Masyarakat/Public Health Saving), demonstrate how trust, collaboration, and digital innovation can effectively sustain outreach to low-income groups. However, as noted by Hidayati et al. (2024), sustainability is often threatened by operational fragility, limited digital access among people experiencing poverty, and the non-compulsory nature of enrolment, which leads to adverse selection.

The combination of financial capital and social capital also becomes a key factor in empowering poor women through Grameen Bank Patterns at BMT Ibadurrahman Sukabumi, West Java. This research demonstrates that Islamic microfinance has a significant relationship with poverty alleviation, and poverty can be overcome when economic development is grounded in human development (Sobana & Husaeni, 2019). Hassan (2014) also found that the Islamic microfinance scheme, through the integration of social, financial, and physical capital, contributed to raising environmental awareness and economic well-being of Bila Sudi-Qardh members in Andaman Island, India. This research demonstrates that social capital enhances the effectiveness of Islamic microfinance by promoting accountability and trust among participants.

Another concept closely related to social capital is spiritual-behavioral intervention. While social capital focuses on the networks, trust, and relationships within a community that fosters cooperation, spiritual-behavioral intervention centers on influencing individual behavior through religious or spiritual values. Although distinct, both play essential and complementary roles in strengthening the effectiveness and sustainability of Islamic microfinance initiatives. Rulindo and Pramanik (2013) found that integrating behavioral-spiritual elements—such as moral education and religious guidance—into Islamic microfinance enhances its overall impact. This study found that Islamic microfinance clients with higher spiritual levels tend, in general, to accumulate more wealth, while higher religiosity may also enhance clients' economic performance.

However, this behavioral-spiritual intervention has been practically implemented at Baitul Misykat, an Islamic microfinance institution operating in Aceh. Baitul Misykat has a

mission to liberate small traders from predatory loan sharks, also fostering community economic independence through *al-qard al-hasan* financing (Jazila, 2022). This institution distinguishes itself by incorporating spiritual awareness and guidance into its financing distribution and economic empowerment initiatives. Small traders often face challenges, including limited business capital, restricted business development due to knowledge and skill gaps, and restricted access to formal financial services. In response to these challenges, many traders often seek alternative financing, resorting to high-interest loans from informal moneylenders, which can lead to debt traps.

Loan shark practices are more prevalent within the network of small traders due to their convenient door-to-door approach and simple administrative procedures. However, this ease of access results in extremely high interest rates, which can reach 140% (Nurdin, 2018a). Providing capital loans with high interest rates certainly will not help the development of traders' businesses; on the contrary, it will damage their businesses and plunge them into prolonged debt traps. This will undoubtedly lead to exploitation and injustice for small traders. On the other hand, capital loans with certain interest rates are considered *ribā* (usury) in Islam, a practice prohibited due to their potential to generate economic inequality and harm (Hadisumarto & Ghafar, 2010).

Although *al-qard al-hasan* financing has been widely examined from both conceptual and institutional perspectives, limited research has explored its integration with behavioral-spiritual interventions and structured spiritual development. While studies such as Rulindo and Pramanik (2013) highlight the importance of incorporating religious and spiritual programs alongside *al-qard al-hasan*, these efforts often remain informal, dependent on individual religiosity. They are not systematically embedded within institutional management frameworks. This study addresses these gaps by conducting an in-depth case analysis to answer how effective the *al-qard al-hasan* model by Baitul Misykat is in achieving community empowerment, and what role does spiritual development play in supporting repayment discipline and ethical entrepreneurship.

Method

This research employed a qualitative case study approach to explore the effectiveness of *al-qard al-hasan* financing implemented by the Baitul Misykat Islamic Cooperative in Aceh. The cooperative was selected based on its rapid growth in assets, geographic outreach, and recognition as a model by the Aceh Cooperative Office (Harian Rakyat Aceh, 2022). The study focused on how *al-qard al-hasan* supports small traders in Lambaro Market, integrating both financial and spiritual development.

This research employed purposive sampling, selecting participants who were directly involved in or impacted by the *al-qard al-hasan* financing scheme. The sample included eight active loan recipients (small traders in Lambaro Market), one cooperative manager, and two field officer involved in mentoring and monitoring the businesses of consumers. The total number of informants ($n = 11$) was determined based on data saturation, where additional interviews no longer generated new insights. This sample composition enabled the triangulation of perspectives from both beneficiaries and institutional actors.

Data collection involved in-depth interviews, direct observations of daily operations, mentoring sessions, and analysis of supporting documents, including borrower records and financial reports. Interview protocols were designed to explore experiences related to empowerment, financial behavior, and program outcomes. Thematic analysis was applied, with data coded and categorized into key themes, then interpreted using Social Capital Theory and behavioral spiritual intervention as the conceptual framework.

Credibility was ensured through multiple forms of triangulation. Data triangulation was conducted by cross-checking participant narratives with observations and documents, while investigator triangulation involved incorporating insights from field officers to reduce researcher bias. Theoretical triangulation also supported interpretation by aligning emerging themes with established constructs of social capital, including trust, norms, and community networks. The research adhered to ethical standards by obtaining informed consent from all participants and ensuring anonymity. Confidentiality was maintained through the use of pseudonyms and the secure handling of data throughout the research process.

Table 1.
Summary of Data Sources and Validation Technique

No	Data Sources	Description	Validation Method
1	In-depth interviews	10 participants (8 traders, two institutional actors)	Data Triangulation with documents
2	Administrative documents	Program records	Sources triangulation
3	External observer insight	Media publication	Investigator triangulation
4	Theoretical framework	Social Capital Theory	Theoretical triangulation

Source: obtained from primary data

Baitul Misykat Activities, Financing, and Business Performance of Beneficiaries

Founded in 2016 by the Indonesian Islamic Business Forum (IIBF) Aceh chapter, the Baitul Misykat Islamic Cooperative, named after the Arabic phrase ‘a house that illuminates,’ was created with the primary objective of eradicating the entrenched practice of loan sharks that negatively impacts the community, especially within several traditional wholesale markets in Banda Aceh. The initiators of Baitul Misykat were concerned by the perceived inaction of authorities in addressing loan sharks, a practice classified as *ribā*, particularly given Aceh’s adherence to sharia (IIBF Aceh, 2020). Loan shark practices in these traditional markets have reached a concerning level, with some operators falsely presenting themselves as Islamic cooperatives and even non-Muslim loan sharks employing Islamic attire to gain trust (Jazila, 2022).

Driven by these concerns, the Baitul Misykat Islamic Cooperative aims to develop the community’s economy based on *mu’āmalah* (Islamic transactions) principles, focusing on the economic empowerment of lower-middle-class individuals within an Islamic economic framework. Its initial operating capital of Rp8.5 million rupiah was sourced from donations (*infāq*) by Muslim entrepreneurs seeking to counter the spread of *ribā*. This limited initial capital was allocated as working capital to 14 small traders in Lambaro Market, utilizing a *al-qard al-ḥasan* (interest-free loan) contract, requiring repayment of the principal amount only (Nuridin, 2018a).

Baitul Misykat offers two tiers of *al-qard al-ḥasan* financing: *jaroe* and *jroh*. Jaroe financing, the initial tier, provides Rp500,000 to Rp1,500,000 to eligible traders. Successful repayment of jaroe loans qualifies traders for jroh financing, with a limit of Rp2,000,000 to Rp3,000,000 (Zulhadi, 2022). Jaroe financing, meaning ‘hand’ in Acehnese, symbolizing the essential tool for labor and livelihood, is Baitul Misykat’s primary product, providing working capital to traditional market traders. This loan aims to support trustworthy, diligent, and honest

traders, deterring them from predatory loan sharks and encouraging those already indebted to transition to Baitul Misykat for sustainable business partnerships (Zulhadi, 2022).

Table 2.
Types of Businesses and Loan Amounts for Baitul Misykat Clients

No.	Business Type		Initial Loan	Subsequent Loan	Impact of Financing
R1	Vegetable trader		1,000,000	1.500.000	Increased Sale
R2	Vegetable trader		1,000,000	2.000.000.,	Increased Sales, diversified merchandise
R3	Vegetable trader		1,000,000	1.500.000	Increased Sale
R4	Vegetable trader		1,000,000	2.000.000	Increased Sales, diversified merchandise
R5	Vegetable trader		1,000,000	2.000.000	Increased Sales, diversified merchandise
R6	Vegetable trader		500,000	1.500.000	Increased Sale
R7	Sugar trader		2.000.000	3.000.000	Increased Sales, diversified merchandise, business expansion (additional market stall)
R8	Banana trader	Leaf	2,000,000	3,000,000	Increased Sales, diversified merchandise, business expansion (additional market stall)

Source: Results of interviews with respondents.

Table 2 shows a uniform initial loan amount ranging from Rp 500,000 to Rp 2,000,000. However, subsequent loan amounts were adjusted based on each trader's specific needs and repayment capacity (Zulhadi, 2022; Nurjannah, 2021; Darna, 2021; Yusriati, 2021; Masyithah, 2021; Dahliani, 2021; Nurazizah, 2021; Sapiah, 2021; Saripuddin, 2021). All financing provided had a positive impact on the beneficiaries' economic conditions.

Key Learnings from the Baitul Misykat Experience

Selection Process

Before providing *al-qard al-hasan* financing, Baitul Misykat conducts a selection process for potential recipients based on established eligibility criteria (IIBF Aceh, 2020; Ananda, 2025; Fachlian, 2022). This process includes conducting field visits and direct observations to evaluate the financial condition and personal character of the applicants. Eligible recipients are typically small-scale traders with a proven history of operating in traditional markets. Endorsements from respected market figures or trusted acquaintances are required. The financing is intended to support the growth of existing businesses or other

productive purposes, not for starting new ventures. The loan amount and daily repayment rates are carefully matched to the trader's financial ability to repay.

Upon fulfillment of these requirements, *al-qard al-hasan* financing is disbursed through the following stages/mechanisms:

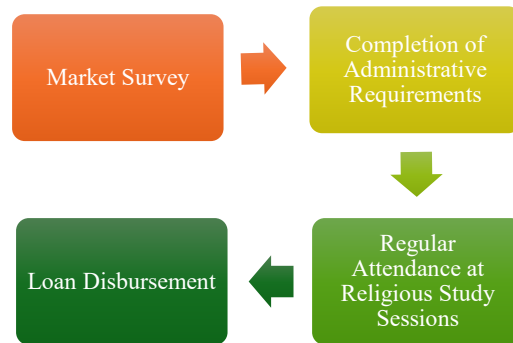


Figure 1. Jaroe Product Loan Disbursement Stages/Mechanisms

Figure 1 illustrates that the initial stage of the selection process is a market survey. This survey, conducted by Baitul Misykat's technical team, identifies eligible traders for Jaroe loans and gathers character assessments from market figures. The second stage involves administrative requirements. Selected traders must provide identification documents and complete business capital loan application forms, including details such as recipient name, address, business type, loan amount, and relevant skills or advantages.

Completion of administrative requirements is a prerequisite, but does not ensure immediate financing. Prospective recipients are required to attend weekly recitations consistently (2-3 sessions) as a crucial assessment for advancement to the subsequent stage (Nurdin, 2018b). The fourth stage, loan disbursement, is approved by the Baitul Misykat Treasurer. Loans are granted to traders with businesses that have been operating for at least two years.

The disbursement mechanism held by Baitul Misykat can serve as a feasibility study and risk mitigation strategy to prevent moral hazard. This selection process is essential for ensuring targeted loans that support business development. These processes are consistent with Rahman (2010), which states that for altruistic and non-collateralized financing like *al-qard al-hasan*, the efficient screening of clients is very crucial in preserving the program's sustainability. The requirement for prospective recipients to attend religious sessions or weekly recitations consistently, as a crucial assessment for advancement to the subsequent stage, is a form of social capital integration to instill Islamic-based norms in both members and customers, which has been proven effective in the case of BMT Tumang (Nurcahyono & Ghufrohudin, 2020).

Monitoring

One of the factors supporting the success of *al-qard al-hasan*'s financing is business monitoring. This process is a form of business control over the customers' enterprises. In the Baitul Misykat context, business monitoring is a regular assessment of borrower repayment behavior to prevent defaults.

Following disbursement, Baitul Misykat implements an ongoing support and monitoring system through regular monitoring. The field staff routinely visit beneficiaries from 09:00 to 11:00 PM, coinciding with traders' peak cash flow, to observe how their businesses are operating, collect daily instalments, and confirm that the funds are being used as intended.

During instalment loan repayments, Baitul Misykat provides flexibility by granting postponements for justifiable reasons. In rare instances, and at a minimal rate, debts are forgiven and written off for clients demonstrably unable to meet their obligations. This policy reflects the cooperative's commitment to ethical lending practices and seeks to protect clients from the exploitative practices of loan sharks.

Another form of monitoring and business control is business assistance through weekly religious sessions. Besides offering spiritual encouragement, these sessions serve as educational business controls, facilitating problem-solving and knowledge sharing among traders (Jazila, 2022). These programs enhanced traders' business competence and encouraged them to become Baitul Misykat donors, supporting other traders in need (Zulhadi, 2022).

Baitul Misykat employs a multi-layered monitoring system to ensure the *al-qard al-hasan* funds are used effectively, responsibly, and in alignment with Islamic ethical standards, as shown in Figure 2.

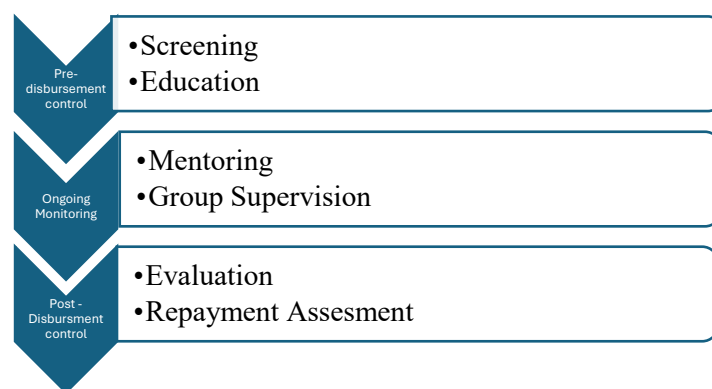


Figure 2.
Baitul Misykat Business Control System

From this monitoring system, Baitul Misykat conducts evaluations by reviewing repayment behavior and overall business performance to assess both financial outcomes and social impact. Clients who demonstrate strong ethical practices and business success may be eligible for continued support and additional funding. For those facing difficulties, Baitul Misykat provides advisory assistance and, when necessary, offers repayment flexibility. This compassionate approach is rooted in Islamic values of mercy (*rahmah*) and ease (*taysir*) when dealing with individuals experiencing hardship, in line with the guidance of Qur'an 2:280.

Baitul Misykat's proactive monitoring system, which integrates daily repayment collection with direct field-level engagement, enables the early detection of repayment issues and helps mitigate default risk. This practice aligns with the insights of Rahman & Dean (2013), who emphasize that continuous engagement is vital for sustaining non-Collateralized, altruistic financing models such as *al-qard al-hasan*.

Significantly, the monitoring process at Baitul Misykat extends beyond financial oversight; it also encompasses business mentoring and spiritual reinforcement. This reflects the integration of behavioral-spiritual interventions, as noted by Rulindo and Pramanik (2013), those who argue that spiritual development, alongside financial assistance, fosters discipline, honesty, and a stronger sense of accountability among borrowers. These outcomes contribute to the internalization of Islamic ethical values, which in turn reinforce repayment behavior and institutional trust.

In addition, a well-structured monitoring mechanism enhances the institution's credibility. Beneficiaries view the institution not merely as a financial provider but as a developmental partner committed to their personal and entrepreneurial progress. This perception fosters trust, loyalty, and reciprocity—key elements of social capital that, as

highlighted by Hadi Nurcahyono and Ghufronudin (2020) in their study of BMT Tumang is fundamental to the success of Islamic microfinance initiatives.

Incentive System of Good Repayment

Baitul Misykat's al-qard al-hasan financing features an incentive-based system. Traders who demonstrate trustworthiness and effective management of their initial *Jaroe* loan are eligible for a subsequent *Jroh* loan, which offers a higher loan amount (Rp 2,000,000 to Rp 3,000,000). Interviews with traders indicate a tiered loan progression. Initial loans are Rp500,000, with subsequent loans increasing to Rp1,000,000 - Rp1,500,000 following the first repayment and then Rp2,000,000 - Rp3,000,000 after the second (Sarifuddin, 2021). Baitul Misykat's tiered business capital loan structure serves as an incentive for traders who demonstrate punctuality and integrity in their repayments. Consistent repayment of initial loans signifies effective business management, commitment, and trustworthiness, thereby enabling access to larger capital loans (Zulhadi, 2022).

The non-monetary incentives repayment system employed in Baitul Misykat, such as access to repeat financing, increased loan amount, group recognition, and participation in religious sessions, does affect repayment rates and beneficiary behavior (Nurdin, 2018a). By this system, beneficiaries who repay on time are granted continued access to larger financing or additional services. The borrowers are encouraged to keep up their status by this acknowledgment, which serves as a positive reinforcement. As a result, Baitul Misykat reports high repayment rates with minimal reliance on coercive collection methods.

The incentive system practiced by Baitul Misykat aligns with the findings of Sanrego and Antonio (2013), which proved that social capital values embedded within Islamic microfinance-based groups influence the repayment behavior of people with low incomes. As a policy recommendation, Islamic banks should consider prioritizing partnerships with Islamic microfinance-based groups in the implementation of their linkage programs for the poor, in order to optimize the effectiveness of poverty alleviation initiatives.

Spiritual Awareness

The integration of spiritual development with financial services is a unique aspect of Baitul Misykat's model. These spiritual development programs primarily center around Islamic sessions (*pengajian*) and religious talks (*tausiyah*) that cover various aspects related to *mu'amalah* (social transactions), *akhlāq* (morality), and *tauhid* (monotheism). As part of its ongoing practice, Baitul Misykat holds weekly recitations that have garnered a growing congregation, encompassing loan recipients and local community members. These recitations provide traders with education on conducting *mu'amalah* in accordance with Islamic economic principles while discouraging *ribā*. Additionally, they aim to reshape traders' perspectives on debt and instill a mindset that prioritizes seeking blessings alongside material profit in business endeavors (Zulhadi, 2022; Fachlian, 2021).

The weekly recitations have a positive impact on traders' religious knowledge and financing compliance. This impact is seen in the increased loan installment payments and *infāq* made by traders upon final repayment, which are directed towards aiding other traders. This act of giving back stems from a sense of gratitude and recognition that the initial capital loans were derived from charitable funds, cultivating a culture of reciprocal assistance (Nurdin, 2021). The religious sessions represent an innovative approach to trader development, focusing on the mental and spiritual development of character. This educational and literacy initiative distinguishes Baitul Misykat from other Islamic microfinance institutions in Aceh.

Baitul Misykat's integration of spiritual development into financial services serves as a model of *maqāṣid al-sharī'ah* (objectives of Islamic law) in action, promoting not only economic justice and empowerment but also nurturing moral integrity and spiritual well-being. This conclusion is also supported by a study conducted by Effendi and Utami (2016), who demonstrated that social capital significantly influences repayment behavior in Islamic microfinance. Their study found that strong relationships with BMT employees, positive interactions with fellow customers, and participation in Islamic recitations had a positive and significant impact on clients' repayment rates. Conversely, factors such as recommendation-based membership and formal membership status had a negative and significant impact on repayment. Interestingly, income level—despite being a conventional economic indicator—did not show a significant influence on repayment, highlighting the stronger role of social and behavioral spiritual relational factors in determining financial discipline.

Effectiveness of *al-Qarḍ al-Ḥasan* Financing

Effectiveness refers to the achievement of predetermined goals or targets, measured by indicators such as program understanding, targeting accuracy, timeliness, goal attainment, and tangible outcomes (Hassan et al., 2021). The achievement of program understanding among traditional market traders is demonstrated by their effective use of *al-qarḍ al-ḥasan* financing. Recipients understand the loan's concept and purpose as business capital, ensuring its full utilization for business growth and complete repayment, including *infāq*. Traders also fully understand the importance of attending weekly recitations, which serve as a vital form of business assistance and contribute to lower loan default rates. This reflects their understanding of the goals of the religious sessions and the purpose of the provided capital loans.

To ensure accurate targeting and timely disbursement, the field team conducts direct market surveys to identify traders with demonstrable capital needs and a firm commitment to business management. This precise targeting ensures that *al-qarḍ al-ḥasan* loans reach the intended recipients. Furthermore, daily field team instalment collections facilitate timely loan repayments.

Concerning goal attainment, Baitul Misykat aims to liberate traders from *ribā*-based moneylenders by providing Sharia-compliant capital loans. The cooperative's success in achieving this goal is reflected in the growing number of financing clients, significant asset growth, and expanded operational area. Initiated in 2016 with 8.5 million rupiahs from IIBF Aceh entrepreneurs' *infāq*, Baitul Misykat's assets reached 1.2 billion rupiahs by August 2022. Initially operating solely in the Lambaro Market, Aceh Besar, Baitul Misykat Islamic Cooperative has successfully expanded its working area to encompass nine traditional markets across 7 (seven) regencies/cities, including Banda Aceh, Aceh Besar, Sigli, Blang Pidie, Subulussalam, Kutacane, and Takengon after 8 (eight) years of operation. This expansion has resulted in a significant increase in assisted traders, from 14 in the first year to 297 (Harian Rakyat Aceh, 2022).

These developments indicate that Baitul Misykat has achieved its objectives and experienced significant business growth through distributing Jaroe and Jroh loans. This indicates that Baitul Misykat's social financing model is both effective and profitable. Significantly, Baitul Misykat's provision of business capital loans has yielded measurable positive changes for traders. They have demonstrated improved business management, consistently repay their loans on time, and contribute *infāq* to assist other traders (Nuridin, 2021).

The successful fulfillment of all effectiveness indicators demonstrates the efficacy of Baitul Misykat Islamic Cooperative's *al-qarḍ al-ḥasan* financing for small traders in traditional markets. Furthermore, this business capital distribution program qualifies as a form of

community empowerment, specifically within the enabling and empowering levels. Enabling involves creating a supportive climate that facilitates community potential development by encouraging, motivating, and cultivating awareness. Empowering focuses on building community capacity by strengthening their existing potential (Ningsih & Prathama, 2021). This program yields not only material benefits but also significant community changes.

The organization also inspires traders to uphold halal business practices, steering them away from interest-based transactions. These educational sessions have been instrumental in nurturing ethical business behavior and combating predatory lending. Furthermore, the recitations contribute to deepening religious understanding among traders, fostering a genuine spirit of *infāq*. This is reflected in the rise of voluntary *infāq* contributions, which grew from Rp6.3 million at the end of 2017 to Rp8 million by May 2018. Traders voluntarily make these contributions as a form of gratitude for the support they receive and the financial progress gained through their engagement with Baitul Misykat (Nuridin, 2018a).

Baitul Misykat plays a key role in raising community awareness about sharia-compliant economic practices. Through routine recitations, participants are educated on how to conduct transactions in accordance with Islamic teachings, covering aspects such as capital management, appropriate use of profits, and ethical debt repayment. In traditional markets like Lambaro, where exploitative loan sharks were once prevalent and caused numerous complaints from traders, Baitul Misykat's consistent efforts have helped many traders escape these harmful practices. This shift has notably enhanced their economic stability and encouraged a transition to Sharia-based financing.

***Al-Qarḍ al-Ḥasan* as a Tool for Economic Empowerment and Poverty Alleviation**

From an Islamic law perspective, *al-qarḍ al-ḥasan* is an interest-free loan extended to help the borrower, without expecting any return beyond the principal. According to Islamic jurisprudence (*fiqh al-mu'amalah*), *al-qarḍ al-ḥasan* is permissible (*mubāḥ*) in terms of its fundamental legality and highly recommended (*mandūb*) or even virtuous (*faḍl*) due to its potential to fulfill the needs of others and reduce hardship; it embodies the Islamic values of compassion, cooperation, and justice. The lender is only entitled to the exact principal amount lent, and any additional return must not be stipulated in the contract. However, voluntary gratitude from the borrower is permitted as long as it is not pre-agreed upon. Even if it is not obligatory, it is highly meritorious and considered a form of *sadaqah* (charity) if the loan is eventually forgiven due to the borrower's hardship (Abidin et al., 2011; Wijaya, 2022; Maksum, 2023).

The practice of *al-qarḍ al-ḥasan* aligns with qur'anic guidance (e.g., QS. al-Taghābūn 64:17), which emphasizes charity and social welfare. This model can be practiced at a personal level or adopted by Islamic financial institutions. It can function as a financing scheme that supports the achievement of sustainable development (Hasan et.al, 2021). *Al-qarḍ al-ḥasan* financing, when implemented effectively, holds significant potential as a tool for economic empowerment and poverty alleviation (Sabiti & Effendi, 2017).

To develop micro-businesses and enhance the effectiveness of *al-qarḍ al-ḥasan* financing, a range of financial and non-financial services is essential (Salma et al., 2024). The Baitul Misykat case demonstrates that successful micro-business development and microfinance require both financial support and non-financial assistance. Adequate financing not only benefits small traders and reduces poverty but also minimizes financing risks and ensures the sustainability of Islamic microfinance institutions.

To minimize default risk, Islamic microfinance institutions (IMFIs) can collect savings alongside loan repayments (Machfudz & Kamila, 2019). This dual approach not only encourages financial discipline among clients but also fosters a stronger sense of responsibility

and commitment toward fulfilling repayment obligations. By integrating savings with financing, clients are more likely to view the microfinance relationship as a long-term partnership rather than a one-time charitable transaction. Moreover, regular saving builds a financial cushion for borrowers, enabling them to manage unexpected expenses better and reducing the likelihood of delinquency due to income shocks.

From an institutional perspective, the accumulation of savings can also enhance liquidity and support internal fund mobilization, which is particularly important for *al-qard al-ḥasan* models that rely on limited philanthropic capital. Empirical studies have shown that clients who actively save during loan cycles tend to have higher repayment rates and lower default probabilities, as the practice promotes self-monitoring and financial resilience (Rahman & Dean, 2013; Obaidullah & Khan, 2011). Therefore, savings-linked lending not only aligns with the Islamic principle of self-reliance (*ikhtiyār*) but also contributes to the sustainability and efficiency of Islamic microfinance institutions.

Fadilah and Ustanti (2024) recommend strengthening risk frameworks and social control mechanisms, such as community forums. *Al-qard al-ḥasan* lending—while rooted in social justice—requires robust operational frameworks to cope with risks. This interest-free financing can be effective if proper risk management, ongoing monitoring, adaptable repayment plans, and built-in social support accompany it. From an Islamic perspective, integrating spiritual and religious capacity building into *al-qard al-ḥasan* financing can substantially enhance its impact. While Islamic microfinance provides initial economic benefits, fostering increased spirituality and religiosity among clients can further optimize their economic performance. Consequently, short-term spiritual and religious enhancement programs can serve as a powerful tool to optimize the positive outcomes of Islamic microfinance (Rulindo & Pramanik, 2013). Religious capacity building serves as an integral component of risk management (Wulandari & Kassim, 2016). Islamic moral principles contribute to the development of key entrepreneurial character traits, including honesty, discipline, diligence, patience, piety, and social responsibility, thereby promoting ethical behavior and positive behavioral change (Bin Mislan Cokro Hadisumarto & Ghafar, 2010).

Another primary challenge facing this financing model is funding sustainability, as *al-qard al-ḥasan* loans are interest-free and typically rely on philanthropic sources, such as zakat, *infāq*, and waqf. While these sources align with the Islamic values of social responsibility and solidarity, they are naturally inconsistent and unpredictable. For institutions like Baitul Misykat, maintaining consistent loan distribution becomes challenging as the number of beneficiaries grows, especially in the absence of regular donations or institutional support. This dependence on charitable funding limits the institution's financial autonomy and exposes it to risks during times of economic instability or declining donor engagement.

To mitigate these issues and enhance sustainability and economic development, IMFIs can partner with charitable organizations that possess greater resources for deploying *al-qard al-ḥasan* funds, such as governance or zakat institutions (Zahri et al., 2023). In recent years, Baitul Misykat has collaborated with Baitul Mal institutions in distributing productive zakat funds as business capital for the beneficiaries (*mustahiq*) (Media Pos Aceh, 2023). The integration of Islamic philanthropy with microfinance institutions offers a sustainable solution to the inherent funding challenges of *al-qard al-ḥasan* (Ali, 2024). Haneef et al. (2013) proposed that Islamic Philanthropy, such as waqf, can be integrated with the Islamic microfinance model. Since both waqf and IMFI emphasize sustainability, waqf can assist in reducing the cost of capital in the operation of IMFI. This integration will ensure the utilization of the resources of Waqf and IMF institutions in alleviating poverty, an objective that both institutions share.

Nugraheni & Muhammad (2024) emphasizes integrating *al-qard al-ḥasan* with mainstream Islamic banking for sustainable impact and scaling up *al-qard al-ḥasan* financing.

By allocating a portion of their social responsibility funds or zakat portfolios to *al-qard al-hasan*, Islamic banks can fulfill their ethical mission without undermining their commercial operations. This hybridization creates a synergy between social justice and financial viability. The integration also opens the door for formalizing *al-qard al-hasan* as part of structured financial products. For instance, Islamic banks could offer *al-qard al-hasan* as part of emergency financing or educational loans with flexible repayment terms. Embedding these instruments within regulated banking frameworks can enhance transparency, governance, and scalability, which are often lacking in informal or community-based models.

Like other microfinance and community-based institutions, Baitul Misykat still faces limitations in technology, with its information systems and reporting processes remaining manual (Musa et al., 2022). This creates administrative risks and poses challenges in evaluating performance and ensuring transparent reporting to donors or external partners. The digitalization of financing management systems also plays a pivotal role in enhancing the sustainability of *al-qard al-hasan* schemes by improving operational efficiency, transparency, and institutional resilience. Automating processes such as loan application, disbursement, and repayment monitoring reduces administrative burdens and operational costs, enabling Islamic microfinance institutions (IMFIs) to serve a larger number of beneficiaries with greater efficiency.

Digital tools also provide real-time, auditable financial records, minimizing errors and fraud, thereby fostering greater accountability and building donor confidence—an essential element for funding continuity (Hasan et al., 2020). Furthermore, data generated from digital systems allows for more accurate risk assessment and borrower profiling, supporting proactive portfolio management and reducing the likelihood of defaults. Improved accessibility through mobile and web-based platforms also facilitates broader outreach and financial inclusion, particularly in remote or underserved areas. Additionally, digital interfaces enable better engagement with stakeholders by providing transparent impact reporting and facilitating crowdfunding efforts, which are vital in attracting sustained philanthropic contributions (Dusuki & Abdullah, 2007). Collectively, these technological innovations strengthen the operational foundation and long-term viability of *al-qard al-hasan*'s financing models.

Human resource development and training also play a critical role in ensuring the sustainability of microfinance institutions (MFIs) and charitable management boards (Syaiikh et al., 2021), particularly in models like Islamic microfinance or *al-qard al-hasan* financing. Skilled, knowledgeable, and ethically grounded personnel are crucial for effective operations, risk management, and maintaining community trust. Investing in human resource development is a strategic necessity for the sustainability of microfinance institutions. Trained and ethical staff enable the organization to maintain its mission, adapt to challenges, serve more clients, and manage resources effectively, particularly in values-based models like *al-qard al-hasan*.

In addition, the support of prominent community figures, Muslim religious leaders, and economists is crucial for ensuring the sustainability of *al-qard al-hasan* (Jihad et al., 2024; Widiyanto, 2011). Their endorsement fosters community confidence, enhances operational effectiveness, and lays the groundwork for the long-term sustainability of *al-qard al-hasan* as a compassionate and strategic tool for economic empowerment (Obaidullah & Khan, 2011). Poverty alleviation programs reliant on Islamic microfinance will face significant challenges without government involvement. Therefore, government political will, as demonstrated through supportive regulatory frameworks, is essential (Bin Mislan, Cokro Hadisumarto, & Ghafar, 2010). All this support system can promote *al-qard al-hasan* as a tool for economic empowerment and poverty alleviation.

Conclusion

This study highlights the effectiveness of Baitul Misykat's *al-qard al-hasan* financing model in supporting small traders, curbing dependency on high-interest loans, and promoting community empowerment through an integrated financial and spiritual approach. The success of this program is driven by four key factors: a rigorous client selection process, effective business control, a non-monetary incentive-based repayment system, and behavioral-spiritual development. These elements collectively reduce default and moral hazard risks while fostering a culture of discipline, ethical conduct, and trust.

The Baitul Misykat model of the *al-qard al-hasan* program has demonstrated effectiveness, as evidenced by positive outcomes in program understanding, targeting accuracy, timeliness, goal attainment, and tangible changes for both traders and the cooperative. However, the findings of this study are based on a single case in Aceh. They may not be easily generalizable to broader contexts without considering regional cultural and institutional variations. The strong influence of local Islamic traditions and community ties in Aceh may not be present in other regions. Therefore, further research should be conducted through comparative studies across different provinces or Islamic microfinance institutions to validate and refine the findings.

From a policy standpoint, Islamic microfinance institutions (IMFIs) and stakeholders are encouraged to replicate Baitul Misykat's integrated approach by embedding spiritual development and social capital strengthening within their financing operations. Policymakers and regulators should also consider digitizing *al-qard al-hasan* mechanisms to improve efficiency, monitoring, and outreach—particularly in underserved rural areas. Furthermore, partnerships with institutions such as BAZNAS and LAZ could enhance capital sources and program reach, maximizing the potential of zakat and waqf in financing sustainable microenterprises. Such integration may represent a viable strategy to scale up Islamic microfinance as an inclusive tool for poverty alleviation and ethical financial empowerment.

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