

Salam, a Proposed Model for Financing Agriculture in Nigeria

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Abstract

The objective of this paper is to provide awareness of Salam as a proposed financing model that would serve as an alternative for financing agriculture in Nigeria. Since agriculture serve as a machinery towards economic growth and development of a Nation where Nigeria is not in isolation. However, the Nigerian Agricultural sector also has a problem of Agriculture financing that lead to the issues which includes unemployment, exploitation and insecurity among others. This paper intent to provide free interest Agriculture financing which features with full employment, investment, market stability among others, Equally the paper is conceptual because it is library oriented that extract data from textbooks, write up from Nigeria Incentive-Based Risk Sharing System for Agricultural Lending (NIRSAL) and Bank of Agriculture (BOA) as well as Newspapers and magazines. With Nigeria weaving the food basket, this paper recommend that policy makers should adopt Salam finance which will create a harmonious atmosphere of financial involvement that is expected to fertilise Nigerian agricultural Initiatives better than ever before.

Keywords: Agriculture; Salam finance; Financial Institution.

Introduction

Agriculture remain the backbone of the global economy as it serves a sustainable way of getting employment, food supply to man and raw materials to the industries mostly in developing economies with a large population density. Also, agricultural productivity is a source of livelihood and income to the individual farmers and the government for economic growth. Equally, Mohammed and Umar (2017) discussed agriculture as a business management in relation to the crop production, animal rearing with the aim of supplying food to population and raw materials to the industries. Likewise, developing economies are mostly an agriculture-based among including Africa and South America among others, As such, Nigeria as an agrarian country which is located in the western part of Africa with 181,748,044 estimated population in 2015 (National Population Commission (NPC), 2017). The Nigerian agricultural sector is playing a vital role as it is the major contributor to Nigeria's Gross Domestic Product (GDP) as it provided 24.18% to GDP in 2017 (Central Bank of Nigeria (CBN), 2018).

Furthermore, Mohammed and Yahuza (2017) looked into Farm credit as a major ingredient for enhancing the growth of the farm output equally, the strategic role of financial credit in accelerating agricultural production in Nigeria as one of the most important determinant of growth in agricultural output. However, the Nigerian government provided a lot of policies in order to finance the sector including Nigeria Agricultural and Cooperative Bank (NACB), Corporate Affairs Commission (CAC) Anchor Borrowers Programme (ABP), The Nigeria Incentive-Based Risk Sharing System for Agricultural lending (NIRSAL), Bank Of Agriculture (BOA) among others, and yet, agriculture financing is fluctuating, as such poor food supply is emerged which also lead to social crime and insecurity. Therefore, this study intends to introduce an alternative mode of agriculture financing (*Salam Finance*) which has a feature among include provision of free interest agricultural financing. Salam finance is a Shari'ah product popularly used in financing agriculture and related productivity. *Salam* financing is a sale finance which involves at least two parties where two homogeneous or heterogeneous products are exchanged against commodity or money. As such, the following objectives are the target of the current paper.

1. To provide awareness of the concept of *Salam* in the agricultural sector of Nigeria
2. To show the importance of *Salam* a free interest towards the improvement of agricultural sector of Nigeria
3. To show how the applicability of *Salam* in the agricultural sector of Nigeria.

Literature Review

Agriculture is a science of crop production, forest management, caring of animal; fishery management, processing and marketing of farm produce. It is a subject that deals with the soil utilization for food to the human beings and it is fed to the animals and reservation of forest for human gratification and economic growth. Equally, Yahuza, Muhammad and Uba (2017) discussed it as an act of soil cultivation for the purpose of food supply and raw materials to the industries as well as goods and services. Anthony (2010) Researched, the growth of agriculture output or farm output refers to the higher gross of agricultural output after successful selection of the farm input or factors of agricultural production. Mohammed et al. (2016) discussed agriculture as a catalyst of the world food security, individual and public income and the supply of raw material to the industries for the production good and services for human satisfaction and poverty reductions.

Futhermore, factors of production which include; capital (farm credit), land labour and entrepreneur (farm infrastructure) are the key sources of the farmer's income, food security, employment generation, market and industries as well as major channel of poverty reduction. More so, agriculture remain a source of food supply, employment opportunities, market and infrastructure in Nigeria as the country is blessed with 98 million hectares of arable land and 2.5 million hectares of irrigable land out of which 83million hectares are suitable for cultivation. Equally, the inclusion of farm credit support agriculture, and is observed to have a positive and significant influence on agricultural output of smallholder farmers which leads to increase in the amount of output growth. Farm credit is defined as a financial transaction set to enhance farming activities with due respect to the received and repayment conditions over a period of time. It can also be described as an amount of money ready to release by the formal and informal money market for enrolment of agriculture production based on repayment conditions. Additionally, it can be regarded as a systematic procedure of power acquisition of control money for a purpose of agricultural activities within a designated period and conditions. Since Bank credit, remains important machinery for farm produce and economic growth (Chisasa, 2015).

Salam Finance (Forward Sale)

The arabic word Salam is a noun derived from the verb "Aslam" which means to advance. Therefore, Zaabi (2010) discussed Salam finance as a mode of transaction in which price is paid before delivery of product, the word "Salf" is also used as synonym for Salam. Salisu and Mohammed (2017) researched that Salam financing is a shari'ah compliant transaction, approved from the sayings of the holy prophet SAW. It is a special sale finance in which the subject matter does not exist or has not come into existence at the time of payment of the price. Salam financing is a sale finance which involves at least two parties where two homogeneous or heterogeneous products are exchanged against commodity or money. If two homogeneous commodities are exchanged, they shall be equal in quantity and exchange should be hand to hand, while in case of exchange of heterogeneous products the quantity can be different, but the condition of hand to hand exchange remains intact. On the other hand if the commodity is exchanged with money price will be decided by mutual consent of both financing parties. Specifically, Jinji (2014) researched Salam finance as an Islamic financial product utilize by the Islamic financial institutions to finance agricultural output and investment for economic growth and development. According to jurists the finance of sale is permitted from the Qur'an with supporting evidences from Sunnah and Ijma.

Mohammed et al. (2016) researched Shari'ah legality of sale finance or trading indicated that object must be in physical or constructive possession of the seller. This condition has three ingredients; first, the object must be in existence, second the seller should have acquired the

ownership of the object and third, mere ownership is not enough, meaning that in addition to ownership, the object must be in possession of the seller, either physically or constructively. If the seller owns an object but he has not taken its delivery himself or via agent, he cannot sell it. There are two exceptions to the above mentioned general principle of Islamic jurisprudence. The first exception is bay Al-salam (Salam finance) and the other bay 'Istisna' (advance payment and deferred delivery of the product). Zambi (2010) discussed both are sales of a special nature and have acquired the status of an exception to the general principles of sale finance. Before the prohibition of interest, farmers used to get interest based loans for growing crops and harvesting. After prohibition of interest, they were banned to take interest based loans because of this prohibition of interest, farmers and specifically small scale farmers faced liquidity problems, therefore, in time of the prophet SAW, farmers were allowed to take advance price of what farmers are going to grow. This helped them to get money in advance for their needs. The legitimacy is provided by the holy Qur'an and Sunnah, and also from the sayings of companions of prophet SAW and *Ijma* (consensus of the jurists). In addition ALLAH Almighty says in the holy Qur'an:

"O Believers! When you finance a debt for a fixed term, you should put it in writing"
(2:282).

Likewise, in Sunnah, the prophet SAW has forbidden the sale of everything which is not in possession of vendor, but he made an exception in the case of *Salam*.

The prophet SAW said:

"When a man involves in Salam and pays for goods to be delivered later, the parties should settle the weight and measure and date of delivery of goods"

Abdullah bin Abi Uffi says that "in times of the holy prophet SAW and Abu Bakar (R.A) we used to sell wheat, barley, dried dates, and dried grapes on "*Salp*". *Salam* financing mode is unanimously declared legitimate mode of transaction by all schools of thought, with mere differences in duration issues. Zaabi (2010) discussed According to all schools of thought, a transaction in which price is paid in advance for the later delivery of goods is *Salam*. The person who pays the price in gold, silver, or currency is called *Musalim* or *Rab-ul salam*. The person who delivers the goods after a fixed period is called "*Musalim playa*". The goods sold are "*Musalim fee*" and the price paid is known as "*Raas-al-maal*" of *Salam*. If a man enters into a finance of sale of wheat with another person and makes a prompt payment of price to him upon promise of delivery of wheat later, the transaction would be called *Salam*.

Conditions of Salam Finance

Following are the conditions which should be considered while practicing the *Salam* financing

- Offer and acceptance of *Salam* finance is executed between the buyer and seller of the commodities
- There should be a buyer and a seller of the commodity
- The quantity and features of the commodity should be known
- Price of the commodity should be accepted at the place of finance
- Price of the commodity should be paid in advance in full at the time of finance
- *Salam* is practiced for only those products which are not scarce in the market
- Each characteristic of the product should be mentioned at the time of finance
- Dates, barley, wheat, and grapes were initially allowed in the time of prophet Muhammad SAW later, olives and dry grapes were also included
- Price should preferably be paid in cash but commodities can also be used to pay price. But if *Salam* product is wheat the wheat cannot be used as price.
- Guarantee for the delivery of product can be taken from the seller in the form of a written signed paper or in form of any product.

- Finance can be terminated if the seller dies before delivery of the product or if the products before delivery get destroyed. In both cases, buyer has the right to take back the price paid.
- Seller is not allowed to change the quality, quantity, at the point of exchange of product once the finance is signed and price is paid.
- Both parties in *Salam* financing can alter or completely cancel the finance by mutual consent.
- *Salam* product cannot be specified, e.g. wheat of specific part of the land, doing so invalidates the *Salam* financing. (*Source: Islamic Banking Operations, 2016*)

Risk Management of the Model

Obaidullah *et al.* (2017) discussed It is necessary to know the risks involved in this proposed model and how to mitigate them. Following are the risks involved in the above mentioned *Salam* agriculture financing model.

Delivery/Default Risk: This risk is prominent in the model because of the delayed delivery of the product. There is a possibility that the farmer could default in delivering the product, even though the crop may not have been destroyed by any catastrophic event. The risk can be mitigated by taking some mortgage security or gold etc. as guarantee.

Commodity Risk: This risk involves the possibility of non-delivery of the crop due to any catastrophic damage to that crop e.g floods, draught etc. This risk can be mitigated through indulging in *Takaful* service for the crop. *Takaful* would compensate the farmer financially in case of any damage to the crop.

Price Risk: Financier faces the risk of uncertain price movements of the product during the 6 months period finance whose price is already paid. There is a great uncertainty that the price of crop to be financed through *Salam* declines.

Quality Risk: This risk can occur if the quality of the crop decided in the finance of *Salam* is not exactly the same which is to be delivered by the farmer.

Methodology

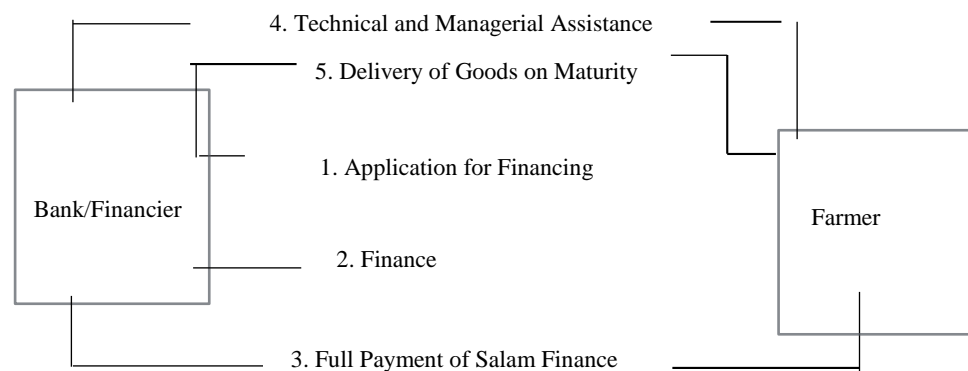
The study is based on data extract from library, magazines, handbooks and newspapers, also, statistics were not involved. This indicates that the methodology used is a conceptual research approach.

Application of *Salam* to Agricultural Sector

Salam model is an encouragement for those farmers who sometimes stay away from banks and other financial institutions because of the element of interest. It is necessary to introduce *Salam* mode of financing agriculture. In this model there are two parties, one is farmer, or seller of the product and the other is financier/buyer of the product. Farmer and financier both enter into a finance of *Salam* for the agricultural product i.e. wheat, the farmer owns 10 acres of land and requires financing for that land in order to sow wheat, financing will be provided for the period of one crop, which is estimated to be 5-6months. Financier, which is a company, bank or any other institute, hires an inspection team (specifically agricultural specialists) who will inspect that 10 acres land and estimate its production capacity. On the basis of the report provided by agriculture specialists, the quantity of wheat will be decided in order to mention it in the *Salam* finance. This estimate of production capacity can also be seen from the average production per acre land of that area and it shall reduce the cost of hiring agriculture specialists. Once the quantity of wheat is decided, the price of wheat which is to be paid in lump sum at the time of finance is set, for evaluation of price; economic experts can be hired to forecast the price of wheat after 5 months when the wheat is actually available. In order to forecast the price of future wheat a trend can be set up via analysing the previous 5 to 10years'wheat prices. This provides a very clear picture for anticipating the future price. It is normally proposed in *Salam* financing literature to discount the market prevailing price and pay that discounted price to farmer so that the financier is able to earn

profit at the time of crop delivery (Farrukh, 2011). Forecasting the price through past 5 to 10 years' prices will help the financier as well as the farmer to set mutually agreed and beneficial price. This is a simple technique which does not necessarily require any economic specialist to forecast the future price. Therefore, a specific amount of price is set and paid at the time of finance.

At the time of signing *Salam* finance, quality of the product should also be mentioned along with the quantity of the product. Decided quality mentioned in the finance cannot be changed by the farmer at the time of delivery of the product, but mere differences can be ignored by the financier in case of quality parameters. Date of delivery shall be decided at the time of finance and farmers obliged to deliver the product at the due date. Guarantee can also be taken into consideration so that the product is delivered in time and of same quality. However, in order to ensure the quality of product and its timely delivery, the financier or donor should send any of its employees, preferably agriculture specialist, to inspect the crop on monthly or bi-monthly basis. This helps donor to be satisfied with the performance of farmer and also ensures the crop delivered at the time of finance completion is same, which financier's inspectors and inspecting. Such inspection should also include proper and effective suggestions to farmers in order to increase the efficiency of their work. This increases the efficiency of their work. This in turn will help the farmers to get acquainted with modern technologies and parameters of agricultural activities and procedures.



Process flow of *Salam* Finance

At the time of finance completion, the financier can either hire an agent to receive the product from the farmer (which is allowed as mentioned above in the conditions of *Salam*) or it can be the farmer himself to sell the product directly to the financier, but the financier cannot sell that product if it has not yet come under his possession. It is allowed in shari'ah that buyer or farmer (with new finance not contingent on the *Salam* finance) can act as agent of seller and take possession of the product which he is supposed to buy/deliver on behalf of financier. Once the wheat comes under constructive possession of the financier, he can sell it to flour mills or crop markets. Other possibility can be that the flour mill only takes possession of wheat, grinds it into flour and charges its service fee. Flour remains in the possession of financier and he can sell it to someone else or arrange his own distribution centres or outlets to sell. This situation helps the financier to earn more profit. Another possibility is that financier holds the wheat for some time and then sells it in market but with the condition that the wheat in times of storage does not get scarce in the market (*Source: Islamic Banking Operations*)

Conclusion

This paper provide awareness of *Salam* Finance and its application to the agricultural sector of Nigeria as it serves as an alternative to the agricultural financing given to small scale farmers. This free interest mode of financing agriculture is characterise with free gambling and exploitation. Equally, Shari'ah legitimacy is also thoroughly discussed in this article. In this model small and also large scale farmers can avail the finances for their crops in advance and

have the liberty of selling crops on prices which they desire. This model also assist from the side of financial provider has an advantage of purchasing particular commodity at a relatively lower price and on the other hand, the farmer gets early price of those commodities which have not been produced yet, this may help him meet the working capital requirements etc. As such, *Salam* mode of financing agriculture is to replace the farm credit given by the current agricultural banks in Nigeria in which include, ABP, NIRSAL, BOA, CAC as well as farm credit from Nigerian Conventional Banks. Thereby, this model is novel because not only it shows concerns about the financial stability of the farmer but also focuses on enhancement of technical skills of the farmer, this would empower farmers financially and technically and eventually will increase productivity leading to economic growth and investment, economic development which is important for economic welfare.

Additionally, this study proposed a framework to the field of agriculture, agribusiness as well as agro-allied and financial services. This paper recommend that policy makers, stakeholders and financial institutions should adopt *Salam* finance towards supporting agricultural productivity as well as to improve economic growth and development.

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