Profit Theory: the Islamic viewpoint

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Theory of Profit: The Islamic Viewpoint

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Introduction

Much of the literature on Islamic economics in the realm of distribution has so far been mainly concerned with questions relating to interest. Rent and, at times, wages have also been discussed. But the subject of profit continues to remain in a state of almost total neglect. References to it have made occasional appearance in the discussions on *mudarabah* or the principles of trade. The present paper, therefore, makes a preliminary attempt to look at profit theory from the Islamic viewpoint.

Implicit in this endeavor is the recognition that there is a basic affinity between the economic scheme of Islam and the capitalistic system: for, profit as a distributive share, is extrinsic to the socialist way of thinking. Islam, like capitalism, permits private ownership of property including the means of production[1] and grants freedom of enterprise. It holds trade and therefore production in high esteem[2]. Islam is neither opposed to competitive effort nor is averse to the operation of the market forces. Yet its theory differs from that of capitalism both in matters of thrust and content. Islam places more emphasis on mutual cooperation and social gain in relation to competition and self-seeking; it has no liberal overtones[3]. Islamic theory cannot make a segmental approach to human existence nor can it stay amoral. The social code of conduct cannot be determined or altered, as in capitalism, by the collective will of the people, it is God ordained and hence not flexible. In addition, there are vital differences on some specific issues like interest, speculation, treatment of uncertainty, and so on.

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(1) For example the Holy Qur'an prescribes the rules for inheritance (2:180,240,4:7-9, 19,33, 176; 5:109-111), allows the individual the sale and purchase of goods (e.g. 2:188; 4:29). and condemns hoarding of wealth (3:180; 9:34) and so on.

(2) The Qur'an permits legitimate trade even when on pilgrimage (2:198). "The merchant who is sincere and trustworthy will on the Day of Judgment be among the prophets, the just, and the martyrs". Tirmidhi, *Abwab-ul-Buyu*, quoted in Hifzur Rahman.

(3) Islam rather makes it obligatory on the part of the state to intervene effectively in the economic life of the people if the larger social interest so demands. There is virtually no limit to such intervention including public ownership of property (Qur'an 3:16). takeover or nationalization, wage regulation, price control, anti-monopoly measures, trade curbs and soon. See Hifzur-Rahman, pp.8,42 and 390; Yusuf Ali, notes 510-511 on Surah 4, Verse 5, Maudoodi, p.77.

In view of this unique relationship of affinity and divergence between Islam and capitalism part one of this paper takes a rapid look at the current state of profit theory in economic science. Part two then attempts a reformulation in the light of Islamic injunctions.

The discussion is cast in general frame. The underlying assumption is that of large scale production meant for the market. The approach is theoretical; the basic frame is that of text book economics. Factual confirmation of or departures from abstract formulations are not given weight; for there seems to be some distinct advantage in this self-imposed restraint. As there is no economic system at present run entirely in accordance with the Islamic requirement this can help us avoid the pitfall of comparing capitalist 'reality' with the 'ideal' Islamic model.

It may be mentioned here that there is one peculiar difficulty in assessing or formulating a theory concerning profit. Unlike wages, rent, or interest, profit is not a thing by itself. Being a residual category, it is vitally influenced by the manner in which these other factor rewards are determined. Excursions into the area of profit theory may sometimes necessitate the opening up of the entire distribution question.

Lastly, no finality is claimed for the observations made or the conclusions arrived at. They are presented here primarily with a view to initiate discussion and encourage debate.

Profit Theory - Some Issues

Profit plays a pivotal role in the working of free enterprise economics. Price theory, the core of economic science, can hardly stand erect if its basic assumption of profit maximization is removed, and few growth models would look neat without some profit concept. Yet to questions like what is profit, what causes, shapes or determines it, to whom does it really belong. etc., economists have failed to provide satisfactory answers. Modern text books either do not discuss this vital subject or relegate it to some dusty corners[4]. Learned discussions on profit have been few and far between. Above all, orthodoxy has not relented enough to accommodate in full measure the ramifications of the metamorphosis market economies have undergone during the past hundred years.

However, instead of discussing each profit theory as a separate unit, let us examine some of the main issues in the field. This would help save space and better focus on the prevailing confusion regarding the subject.

Profit Concept: In free enterprise economies the sum of the contractual factor payments when deducted from the revenue product of the firms leaves a surplus that goes to the entrepreneurs. This surplus is akin to the accounting gross profit. A part of it represents capital compensation which incidentally the market forces are powerless to determine. Capital compensation, however arrived at, is taken out of the gross profit to arrive at its 'net' component.

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(4) Stigler, Ferguson and Watson have for example no chapters on the subject of profit.

In accounting net profit the economists isolate 'implicit' returns comprising of rent, interest, wages and the risk-premium accruing to the entrepreneurs for the supply of corresponding inputs by them to the firms. Put together, these returns are called 'normal' profit which is then treated as an element of production costs. Net profit minus implicit returns gives the final surplus the so-called 'pure' profit. Monopoly revenue is often kept out of this surplus[5] on the plea that it accrues to those scarce factors on which monopoly power rests, not to the entrepreneurs. Today, economic theorists writing on the subject attempt to explain the emergence of 'pure' profit without using the adjective 'pure' any longer.

This definition of profit is too abstract and microscopic. The concept of normal profit has an ethical import. But in the real, dynamic situation normal and pure components of the surplus are extremely difficult to separate, even conceptually[6]. The same is true of monopoly revenues. Indeed, profit can be viewed only as an integrated whole having many and varied elements that are inextricably intermixed. Text book economics seems to endorse this view though one may like it to make its notion of profit a little more explicit.

Source of Profit: For explaining the emergence of profit (pure) the economists generally start with a no-profit model as the limiting case wherein the remuneration of the various factor services would exhaust the total revenue product of the firm such that profit tends to zero. These no-profit models are well known[7]. In any event, despite the differences in their range and implications, they all tend to converge, in the ultimate analysis, to the classical design of perfect competition. Undaunted by the enormous qualitative difference between situations within and outside these models, their makers search for the source of profit in what causes the failure of the ideal profitless exchange.

It is agreed that the real cause of this failure is dynamic change. But, interestingly, each economist in his attempt to formulate his theory of profit has seized upon that rudiment of dynamic change that suited his own predilections or scheme of work. Thus, for J.B. Clark and many others it was risk inherent in change. But Knight threw overboard all the risk theories of profit on the plea that risk is measurable uncertainty and can be insured against (Knight, pp.35-38, 148). Indeed, it was he who first made the risk-premium an element of the production costs. To him profit arises because of the immeasurable uncertainty - the true risk - that divides factors of production into hired and unhired ones (entrepreneurs). How this approach makes qualitative departure from the risk theories of profit is difficult to observe. But in the process Knight threw up more than one theory of profit and the profit concept or measure is not found to be the same in each case (Hasan, P.33). This apart, his analysis has been stretched to demonstrate that he could help only in identifying a windfall element resulting from the "errors of forecasting" in all the factor incomes (Weston, p.158).

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(5) This view is shared by Mrs. Joan Robinson, Chamberlin and Schumpeter, though with some differences. However, Schumpeter at a later stage gave up the distinction between profit and monopoly revenue, treating the two as one.

(6) By no stretch of imagination is normal profit less uncertain than pure profit under dynamic conditions. It is illogical to measure normal profit by the contractual rates that are guaranteed payments. The advantage of an uncertain given income cannot be measured by the loss of the same amount.

(7) For example, J.B. Clark's static state' Frank H. Knight's version of 'perfect competition'. and J.A. Schumpeter's 'circular flow'.

Schumpeter placed emphasis on technological change, symbolized by innovations that were crucial for triggering the economy on the road to development. Innovators were his entrepreneurs and profit was their reward. (Schumpeter, 1934, Ch. IV). But as he realized that (he function of innovation had already been institutionalized he threw his notion of entrepreneurial profit into the pile of 'obsolete ideas' (Schumpeter, 1942, pp.131-138). However, he did a service by linking profit to productivity.

Thus rudimentary analysis could succeed in presenting only a welter of profit theories explaining at best partial truths about the emergence of profit. In fact, dynamic change in all its ramifications is the real source of profit.

Profit and Entrepreneurs: Economists have invariably regarded profit a functional return - the reward for entrepreneurial services, however, defined. Knight provides the leading example that still seems to underlie the text book view of the subject. He argued that since uncertainty breeds risk that cannot be eliminated or met at a cost, every one is not equally inclined or equipped to assume the role of decision maker in the realm of business. Only those who have confidence in their own judgment as well as the ability to put their opinion into operation, specialize in decision-making and are ready to bear the consequences. They are the entrepreneurs.

The entrepreneurs translate their decisions into action by hiring the other factors of production. The services of the hired factors do not involve, says Knight, the exercise of judgment in the same sense as it does in the case of the entrepreneurs (Knight, pp. 270-72). They work for the entrepreneurs in return for their contractual payments. The objective requirement for entrepreneurship, according to Knight (pp. 198, 363-64) is the possession of property since no empty handed person can ensure contractual payments to the hired factors of production. This view of the entrepreneur makes profit the reward for making business decisions in the face of uncertainty, and is a legacy of the classical model of the tiny owner-operated business units. It fits well even today to cases of small business. But since the rise to dominance of the modern corporate form of organization both the functions and the identity of the entrepreneurs have come under heavy fire. Put briefly, the argument is follows:

The promoters bring the corporation into existence and the stockholders provide the risk capital which is often supplemented by institutional finance. The decision making function and the ownership of the organization are in quite different hands. Ordinarily those who make decisions are the salaried people and they do not bear the consequences of their decisions. Further, decision-making is divided among a large number of fairly independent functionaries all of whom may not have the same aims or motivation. Who then are the entrepreneurs and what functions do they perform in era of corporations?

One could attempt an escape out of the difficulty by saying that real control goes with responsibility. It consists in making decisions not about things but in the judgment of men's ability to do things. The exercise of this judgment - the entrepreneurial function - may be spread over the whole hierarchy of the corporate enterprise but in the ultimate analysis it lies in the hands of the owners of the organization - the stockholders[8]. After all who appoints the managers and to whom are they accountable?

(8) Indeed, Knight himself visualized the difficulty and attempted to provide an answer along these lines. (pp. 291-300).

Small, closely held corporations are no different from the proprietary business in this matter. In the large corporations the ownership rights of the small, widely dispersed, and unknown stockholders may have become formal, representing a mere claim to a 'wage' for their capital determined by the management (Means, p. 262). But the rights of the owners of large blocks of stock are real in the sense that they may often manage to acquire effective control over the affairs of their corporations. The perfection of the proxy machine and some other techniques tend to help in the emergence of 'control-ownership' in the case of large corporations[9]. Though the control may rarely pass into the hands of a single person[10], (the possibility of a small group of stockholders enjoying such power is always there. Presumably, there is no other form of property today that people may strive to acquire with greater zest and vigor than the control over a modern corporation.

Thus the entrepreneur survives as a unit of interest and control despite the corporations, though his entity as a managerial unit may be doubted (Galbraith, pp. 70-71). Text book economics has rightly stuck to the tradition: for with the entrepreneur goes the motivational base of the capitalistic organization run by the market forces. The advent of large corporations has only made the profits of the firm a non-functional surplus in the hands of the entrepreneurs.

In Summary: It comes about that profit defined as a surplus of business earnings over contractual payments is a non-functional surplus whose origin lies essentially in progressive dynamic change. The real issues in profit theory are (i) whether contractual payments, specially wages, as determined by the market forces. can be shown to be just and (ii) whether the utilization of the residuum in the hands of the entrepreneurs is always proper.

The marginal productivity theory of distribution is illogical and unrealistic; it fails to ensure natural justice[11]. Profit appropriation is largely institutional; market is no arbiter in this matter. And economic theory has chosen to stay neutral toward ends[12]. Under the circumstances no firm opinion could be ventured on either of the above mentioned issues. But Islamic economics, imbued as it is with ethical values, cannot afford escapism Let us now see what formulation in the area of profit theory can meet its approval.

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(9) "As is well known, the widespread diffusion of stock ownership and the development of the proxy machine, have operated to remove the stockholder from significant control over the corporate enterprise. At the same time it has, as a practical matter, placed ultimate control over the enterprise in the hinds of a management which owns only a small fraction of the outstanding stock", (Means. p. 254).

(10) Even in a corporation where stock holdings are widely spread "at a certain stage of growth.... power is concentrated in some one who exercises command over the enterprise. Thus appears in classical form the figure of the entrepreneur". (Galbraith, 1968, pp. 87,89 *passim*).

(11) "It is not true that a system in which each factor receives an income equal to its marginal product corresponds to some kind of natural justice according to which what each factor gets is what it contributes to total output (because) it is not its productivity but its scarcity relative to the other factors that determines the marginal productivity of each." (Robinson and Fatwell, p.88).

(12) Some economists consider this so important as to express the fact in the very title of their book, e.g., Lipsey.

Profit in the Islamic Perspective

Islam exhorts the believers to excel in this life no less than in the life hereafter. It urges them to engage in almost every material pursuit. especially trade and eulogizes profit as God's bounty[13]. But Islam is not unaware of man's inordinate love for wordly gains (Qur'an l00:8). So it instructs people to observe moderation in the drive for profit[14], behave in a prescribed way[15], and acquire only the legitimate, not the maximum. It advocates absolute honesty in business to the extent that one is enjoined not to falsely praise his merchandise, but to reveal to the customer[16] any defects in it. The Islamic concept of *Halal* and *Haram* is quite adequate to keep people on the right track (Maudoodi, pp.82-89 and Hafizur Rahman, pp.63-67). In case of conflict between wealth and virtue one has to be content with whatever can be acquired rightfully even though it may be little (5:103). There are a number of Qur'anic verses and traditions that remind man of the transient nature of this world and its possessions relative to spiritual ends, and seek, by implication, to bring the pursuit of profit under Islam's moral discipline (The Qur'an: 4:77, 28:77, 29:64, 57:20-21 and elsewhere).

However, subliming the profit motive through moral persuasion, though important, is relatively a small matter. Of real significance is the scheme of distribution that seems to emerge from the Islamic notion of economic justice in the face of uncertainty shrouding the outcome of the business operations.

Norms of Justice and Uncertainty: The Islamic ideal of economic justice seems to be the achieving of a situation wherein what each factor ultimately gets is what it contributes to total output. The Qur'an explicitly declares: "God created the heaven and the earth for just ends, and in order that each soul may find the recompense of what it has earned" (45:22). Islam aims at shaping all exchange relations among people on the principle of cooperation, mutual benefit, and fair play (4:29-30). It directs men not to expose themselves or inflict on others loss that is possible to avoid[17]. This principle lies at the heart of the celebrated Islamic notion of *gharar* (indeterminacy, hazard).

Contractual relations must be, as far as possible *gharar*-free. The Prophet is reported for instance to have instructed not to sell fruits on trees until they show clear signs of maturing, or standing crops before the ears have turned golden and the danger of damage through natural calamities has reasonably passed, nor to sell things one does not possess at the time of making the contract (Ahmad, vol.2, pp. 399,403 and Rodinson, p.16). For deals such as these have the potential of causing harm to one of the parties. Little care can prevent this harm.

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(13) The Qur'an: (2:198, 62:10, 73:20 and elsewhere). A tradition says: "If you profit by doing what is prescribed, your deed is a *Jihad* (i.e., equivalent to fighting or any other vigorous effort in the service of God's Cause).... and truly a *dirham* lawfully gained from trade is worth more than ten *dirhams* gained in any other way" Quoted (from Zaid Ibn Ali 'Corpus juris'.... ed. E. Griffini, Milan, 1919, n. 589) in Rodinson, pp.16-17.

(14) The Prophet - peace be on him - is reported to have said: "Fear God and be moderate in your pursuit of wealth take only that which is allowed and leave that which is forbidden". Ibn Majah Vol 2, p.725: 2144.

(15) Islam forbids practices that are fraudulent in one way or the other, together with trade in things it considers impure like wine, pigs, animals that have not been properly slaughtered. and also in goods that are regarded as common to all i.e., water, fire, grass. It insists on having proper weights and measures, and on their correct use(11:84, 17:35, 26:181-183, 57:25, 83:1-4).

(16) See for example Ghazali pp 68 and passim, quoted in M. Rodinson, p.251 note 24: Maudoodi, pp.82-89 and Hifzur Rahman. pp.63-67.

(17) According to tradition the guiding principle in all matters is: "no injury (deliberate or otherwise) and no reprisal" (quoted by Hifzur Rahman, p.210).

For the same reasons Islam may not approve the existing forms of insurance or forward trading and does not permit speculation, specially in food grains (Hifzur Rahman, pp. 260-263). Incidentally it is now being increasingly asked if unbridled speculation does more good than harm to the socio-economic fabric of the community. A modern text book makes the observation: "The main economic role of a stock exchange is the preservation and expansion of the rentier wealth, rather than the provision of finance to industry or government". (Robinson and Eatwell, p.226).

One need not envisage the 'horror of risk' afflicting Muslim societies in the Islamic notion of *gharar*[18]. If at all, the real progeny of horror are the institutions of interest, limited liability, preference shares, the stock exchange escape route, etc., and these are distasteful to Islam. *Gharar* signifies the Islamic concern to ensure every one his rightful due in the process of production. This becomes all the more evident from the Islamic attitude towards the determination of various distribution shares - an issue to which we now turn.

The Interest Question: Barring a few discordant voices, learned opinion in the Muslim world holds, as an axiom, that the prohibition of *riba* is total and complete in Islam. The verdict makes no distinction between usury and interest, between its simple and compound forms, between productive and unproductive loans, or for that matter between money and commodity borrowings[19]. It is not of much relevance here to re-examine the entire argument but, the consensus being what it is, one aspect of the ban deserves further investigation. In the framework of a business firm both interest and profit are payments for the use of capital, yet interest is not allowed in Islam while profit is, why?

Islam recognizes the productive attribute of capital and does not intend to deprive it of its due reward[20]. But, to begin with, is interest commensurate with productivity? The level of interest rates is mainly determined by the state of opinion in the market for placements - the stock exchange - and manipulation of monetary policy[21]. What has the productivity of capital to do with either of them? Again, all the funds are intermixed in the asset formation of the firm and are, from its viewpoint, equally productive and exposed to the same type of risk and uncertainty in its business. How does the productivity of the borrowed and the equity parts of funds differ? Further - and this is crucial - why should the firm make different payments to capital for identical functions, one at the predetermined rate (interest) and the other (profit) variable with the results of the business operations? Financial expediency need not meet the ends of justice.

The non-symmetry clearly invokes the principle of *gharar*. Market economies are characterized by business fluctuations where interest rates invariably lag behind price variations. The result is that the loan- equity mix in the capital structure of the business

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(18) For one such interpretation see for example Rodinson, pp. 161-163, where he quotes a number of writers without rhythm or direction, in his argument which is even self-canceling at places.

(19) For an argument along these lines see, for instance, Sheikh Mahmood Ahmad, Ch. 11 on interest. Further. see Qureshi. Ch. 2 entitled: "Islamic Theory of Interest".

(20) Otherwise, Islam would not have allowed *mudarabah* as a form of business organization.

(21) Robinson and Eatwell. p. 281). They do not regard the rate of profit on capital as well as related to the productivity of capital. This rate, they hold-and rightly so depends broadly on the state of technology and the lever real wages.

firms proves, in general, unjust to the lenders during periods of inflation and hurts the equity holders when the economy is going down the hump. Islam obliterates the inequity by the abolition of interest so that the capital participates in the productive ventures on equal footing - the proportionate sharing of profit.

A little digression may be allowed to dispel one apprehension. Will not the millions of those people who may prefer a relatively safe, even if small, income through the lending of their savings feel hesitant, after interest is abolished, to join in bearing the risk and uncertainty of modern business? Will that not reduce savings and retard investment thus hampering economic growth? Habits of thought and experience of taste have perhaps made the utility of the interest institution so self- evident that the danger may look real. However, a little reflection is enough to remove the doubts. First, the hope for profit is presumably stronger and more enduring in men than the fear of loss, the lure of riches often overcomes safety searching timidity. Second. if some options are closed once and for all men have shown remarkable competence to adapt themselves to those that remain open. Last but not least, institutions on the pattern of the Unit Trust of India, for example. can always be evolved to offer people opportunities for indirect participation in the equity capital of business firms with hardly any risk involved. Once the transition is over, the logic of an interest - free system can indeed be shown to work for faster and more orderly economic growth[22]. But let this not detain us further.

Form of Rent: The question of private ownership of cultivable land has been among the hotly debated issues in Islamic economics[23]. Those who allow private ownership of cultivable land have a clear edge over those who do not but they continue to be divided on the issue of rent. It is agreed that the best course for a person having land in excess of what he himself uses is to give it to his landless brother for cultivation free of charge. However, if rent is to be taken there is no consensus regarding its form. Some permit only cash rent, some only share-cropping i.e. *muzara'ah* and there are still others who allow both.

On balance, share-cropping is considered to be the best (Maudoodi, p.219). For the outcome of cultivation being uncertain, predetermined, absolute rent may only be a kind of *riba*. For example, Professor Smith writes (p. 107): ".... these religious proponents..... cannot even understand that the prohibition of interest, if taken seriously would include the prohibition of land rent and of the whole landlord system- would mean precisely the socialization of agriculture in the interest of those who labor on land" (quoted by S.M. Ahmad, p. 32). He is perfectly right in case the tenants are charged a fixed rent in cash or kind. "Here the landlord is to the same extent indifferent to the actual yield from land as the banker is to the actual return from industry or commerce". (S.M. Ahmad, p. 33). Fixed rent may turn out to be unjust to either of the parties to the contract when the outcome of cultivation becomes known. The objection can be overcome only if the rent is settled as some reasonable proportion of the crop i.e., *muzara'ah* is the arrangement.

(22) At least to the extent that Keynes has held interest to be a hindrance to both. See his *General Theory*, pp. 136, 137, 140, 144, 145, 322 and 323 taken together help make a clear argument.

(23) For arguments in favor of private ownership in land see for example, Maudoodi, pp.189-219 and Zafar Ahmad Usmani. Vol.71 Nos. 4 and 5 (April, May. 1953). pp. 245-286 and 325-340 respectively.
For the opposite viewpoint see, for instance, Nasir Ahmad Sheikh. and Syed Manazir Gilani. Vol. 70 no.6. (December, 1952) pp. 405-422, and Vol.71 (Jan., 1953) pp.5-22. The articles by Usmani are a rejoinder to those of Gilani.

Thus it comes about that in the area of mass production where business outcome is characterized by uncertainty, the Islamic ends of justice can be met only when interest is abolished and all capital participates in profits of the enterprise on an equal basis. In manufacturing, land partakes the form of capital. But even in agriculture where land is important there is, as we have noted, strong presumption that Islam does not permit prefixed rent in cash or kind and prefers share-cropping to make the landlord-tenant relation free of *gharar*. These conclusions have great inferential significance for the determination of the remaining distributive share - the wage for labor.

The Wage Issue: Islam is not opposed to wage labor but it does insist that the wage contract should be an equitable one. Workers must have the fairest possible chance under the arrangement to receive their due[24], i.e., what they contribute to the value product of the firm. This also implies that payment to them is not excessive either.

The difficulty is: How can predetermined wages meet the norm of justice in the face of uncertainty? How would one justify non-symmetry in the treatment of interest and prefixed rent on the one hand and wages on the other? Why can't wages be also made in some way variable with the results of the enterprise? Or, is there some insuperable difficulty in making the scheme of such variation a part of the social arrangement independent of the market?

In the area of mass production a pre-set wage as determined by the market forces, or for that matter in any other *wage* is indeed no better than *riba*. Both are prices - one paid for the use of labor, another for the use of capital[25]. There seems to be no compelling reason why workers alone should be singled out as an exception to the sharing of the uncertainty of business outcome. It may be argued that wages cannot be negative or fall to zero; for, the workers are human beings and have to be sustained in any case[26]. True, but this requirement can be taken care of in the Islamic system by the provision of a minimum wage. Islam grants all people an equal right to livelihood. One can argue that the right to a living can be guaranteed by society whereas the wages are paid by the employer. How does the sanction for a minimum wage follow from this Islamic injunction? However, the point here is that if society takes the responsibility for maintaining its out-of-work members why can't it make obligatory on the employer to ensure at least a minimum of living to those who work for him? In any case, will it be un-Islamic if society chooses to do so? Those who may like to answer in the affirmative will have to provide valid and acceptable reasons.

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(24) This follows from the tradition which says, "Three persons are sure to incur God's displeasure on the Day of Judgment... and one who engages a worker to do a job, takes full work out of him but does not pay him his due wages" Bukhari (Ibn Hajar: Fath-al-Bari. Kitab al-'ijarah).

(25) A similar question is raised for example by Wadi A. Kabli. See Zarqa, p. 7.

(26) Zarqa in the note quoted above gives reasons as to why does Islam permit pre-fixed wages for labor but not a fixed payment (interest) for capital. And this is one of his reasons. My argument below does not negate what he says, nor does it oppose market wage. What it insists on is the adjustment in payment to a just reward to capital as well - when the result of the enterprise in the area of mass production becomes known. The scheme designed here checks the capitalist's temptation to exploit the worker for his gain but at the same time it does not permit the workers to run away with their fixed wages without observing their responsibilities in production - mark the (W - W) adjustment in the model presented in the following sections.

Even some of the capitalist countries have minimum-wage legislation and business firms or other institutions cannot pay wages below that minimum. The argument, given at times, that the minimum wage legislation may deprive some people of work, thus increasing the burden on society does not cut much ice. Can we condone robbery because its prevention involves cost to the state?

With land being of little consequence in industry and interest banned, the distribution problem boils down to the sharing of the value product between Labor and Capital. Islam allows the capitalists to share their part of the value product among themselves only in proportion to their contributions. This is true in all cases, whether the business takes the form of *mudarabah* or is of one of the usual types. In return, loss would always fall on their capital. As regards the apportioning of the value product between capital on the one hand and labor on the other the use of the pre-set wages for the purpose cannot be proved to meet the ends of Islamic justice. Beyond minimum wages, presumably some sort of a labor participatory system alone can bring us closer to a distribution scheme that may be just to *both* labor and capital.

The above conclusion stems clearly from the first principles of Islam - the principles of equity and *gharar*-free contractual relations. But let me set up a supplementary argument.

An Analogy: Take the case of *mudarabah* where one of the partners, say A, supplies capital and the other, say B, works and uses his talent to make the investment bear fruit; both agreeing to share profits in certain proportions while A alone will bear the loss, if any. What is the intention in so framing the scheme other than the desire to be fair to both? Otherwise. why can't A employ B on fixed wages to work for him? Are not the wide spread, small, inactive shareholders in modern corporations doing just this when they leave their business to be conducted by the salaried managers? Again, if production takes time as it does and B has no means whatsoever to support himself from where will resources come to provide even a minimum of living to B during the interval if not from the funds supplied to business by A? If that is to be the source, how will it be unfair on the part of A to claim from the resulting profit before he shares it with B the money so spent? If the deduction is justified the amount becomes an element of cost.

The analogy provides further support to the inference stated earlier that distributive justice as visualized by Islam is hard to achieve without labor participation in the fruits of business. It makes clear that the entire value product minus minimum wages must be treated as profit to be apportioned between labor and capital. *Mudarabah* to my mind cannot be taken as just one design of business contract allowed by Islam in isolation of the logic and spirit on which it is based.

While profit sharing is a matter of principle the question of the division ratio belongs to the institutional domain. "Some Maliki jurisprudents" in case of *mudarabah*, for example "Went so far as to give the employee an equal share of profit. The employer provides all capital and the workman does the work. The two efforts are equal and accordingly they are entitled to equal share in profit" (Qutub, p. 135). History bears testimony that this type of relationship between capital and labor "was designed to undergo enormous expansion" in Muslim societies around the thirteenth century, (Rodinson. p. 51).

The Model: We may now formulate a macro-level model of distribution that emerges from the above discussion. Let Y be the aggregate value product of the business firms, P the profit, W the minimum wage, and T the business taxes.

$$Y = P + W + T \qquad (1)$$

Suppose P is shared between capital and labor in the k and (l - k) ratios respectively, where k is an institutional variable. We have:

$$Y = kP + (l - k)\ P + W + T \qquad (2)$$

However. the market wage, say W, already paid to the workers will invariably be more than the minimum wage W. Equity demands that the excess amount paid to them must be adjusted to their share of the profit (l - k) P. Equation (2) then becomes:

$$Y = kP + |\ (l\text{-}k)\ P - (W - W)\ | + W \pm T \qquad (3)$$

Let us put | (l-k) P- (W-W) | = B, where B may be called the bonus payable to the workers. This gives us the final distribution equation conforming to the Islamic spirit and intent:

$$Y = kP + W + B + T \qquad (4)$$

where kP is to be shared by the capitalists among themselves (W + B) goes to the workers, and T to be the state.

In the case of individual firms suffering losses B may well be negative. This may be debited to a special account to be charged (i) against the workers' future share of profit. or (ii) to the reserves built through deductions from P prior to its distribution.

In the above model P is the net of business taxes and a mutually agreed policy of profit retention may be enforced to take care of the financial requirements of the industry.

The more inquisitive may perhaps like to ask: But what is the *theory* involved in the scheme of the model? It has to be pointed out that Islam does not believe in idle theorizing. It presents to the believers; a comprehensive action program (13:29). As such. the principles of Islamic economics can only be the principles of economic policy. The above model is not afflicted with atomistic analysis of profit. The definition of P is objective and precise. Profit is viewed as a surplus that cannot be ascribed to some unique functions performed by the waning entrepreneurs. Nor does the model interfere in any way with the workings of the price mechanism; Y and W continue to be determined by the market forces. W and k are the policy variables. Islam has no objection. would indeed welcome, if the business enterprises evolve for themselves a code of conduct that includes these variables. Otherwise, the state cannot become oblivious of its responsibility in ensuring distributive justice. Even in the capitalistic economies the appropriation of profit is a matter of the firms' policy decision and governmental regulation of business affairs for safeguarding social interest has increased to an extent that the system now looks more 'managed' than 'free'.

Conclusion

The profit view presented in Part Two is in line with the fundamental Islamic principles of unity, harmony, mutual trust and cooperation, individual freedom with social responsibility and fair play. It attempts to face the issues which the capitalistic profit theory leaves open as shown at the end of Part One The two differ primarily because economic science has a *positive* stance while the Islamic approach to economic issues is loaded with *normative* considerations.

Presumably a different juxtaposition than the one presented here is difficult to erect in the light of the available literature on profit theory on the one hand, and the Islamic rationality and injunctions on the other. Nevertheless, the paper raises as many questions as it attempts to answer in the hope of stimulating, even provoking, the learned. Any improvement over this preliminary effort will be a step forward in a rather difficult area of Islamic economics.

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