Book Review: "Teaching Economics in Islamic Perspective" By M.N.Siddiqi

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1998

Islamic Economic Studies
Vol. 6, No. 1, November 1998

BOOK REVIEW

Muhammad Nejatullah Siddiqi
Teaching Economics in Islamic Perspective
Scientific Publishing Centre, King Abdulaziz University
Jeddah, Saudi Arabia

Published 1998, pp. xxv + 244

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1. INTRODUCTION

Despite efforts over the years, Islamization of knowledge has barely taken off the ground in social sciences, save in economics. Even in economics, the progress has been patchy and uneven. Finance, in its widest sense, has attracted bulk of the scholars' attention, while many areas remain untouched. More than that, the process of Islamization seems to have reached a plateau, and is in imminent danger of dissolving into the new current of thought.[1] At this juncture appears Muhammad Nejatullah Siddiqi's recent work *Teaching Economics in Islamic Perspective,* which Elgari hails in his foreword to the book as "one step in the long road to Islamization of knowledge" (p.v.).

However, on the question what Islamization of knowledge really means the views are not very clear, and differ considerably. Two shades of thought implicit in scholarly writings on the subject are discernible. First, there seems to be the view which insists on what may be called an all-or-nothing approach to Islamization. It requires that Islamic economics must not allow any intrusions that the orthodox interpretation of *shari'ah* would not book. The underlying assumption of writings in this vein is of a performing Muslim society being in existence. In this case Islamization results in producing pure economic models rarely depicting the

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[1] The rise to dominance of financial capitalism after the eighties has swept across the world to establish a new world order whose main economic elements are privatization, free capital movements, and abolition of trade barriers with a view to integrate nations into what it fondly calls the 'global village'. These developments are having their toll on Islamic economic thinking. The impact is vivid even on *Teaching*.

ground realities.[2] Such models, though of immense value, have invariably been the target of much criticism in the literature.[3] In contrast, the second view seems to look at things in a rather pragmatic way. It would prefer a step-by-step approach for the eventual achievement of perfection in a rather evolutionary frame. It conceives a gradual but progressive modification of the prevailing secular structures, and advocates for reopening the doors of intellection *(ijtihad)* in the light of contemporary needs and compulsions. In his writings, probably until late eighties, Siddiqi seemed to be largely following the first approach for Islamizing economics. It is, therefore, interesting that in the work under review, one finds him using essentially the second. He is no longer talking of Islamizing economics, as he earlier did.[4] Instead, he is just explaining as to when and how can one inject the Islamic elements while doing a course with the students in mainstream economics. However, the distinction is merely analytical, not classificatory.[5]

Siddiqi has been among the pioneers of Islamic economics. He is a prolific writer, and his writings are rarely devoid of depth and range. The author's scholarship is well recognized, and his services for promoting the cause of Islamic economics have won him the highest awards. He has inspired many to enter and work in the area of Islamic economics. His present book is the result, as he says, of a decade's thought and effort. His list of acknowledgements contains, from all over the world, the names of more than eight scholars who 'have contributed to the formation of ideas expressed' in the volume' (p.xv). And finally, the work has been published by the Scientific Publishing Centre, King Abdulaziz University, which is reputed for the quality of its publications. Thus, the book has all the credentials to raise the readers' expectations for what it contains. We shall henceforth refer to it as the *Teaching* for brevity. Also, the pages quoted in the following discussion are of the book, unless indicated other.

Instructions for teaching, irrespective of their perspective, are usually expected to exhibit a clear awareness of the students' needs, of job market demands, and of current developments in the discipline. They are inevitably constrained by the curricula frames, and structure of courses including their level, mutual linkages, and duration. Surprisingly, the *Teaching* is altogether silent on these vital issues.

[2] Pure models, however, play an important role in the process of Islamization of knowledge. They fix the direction of movement, help identify the relevant variables and analyze their inter-relationship, and provide a benchmark from which to measure departures in practice. The mainstream economics too widely uses such models, perfect competition being the leading example.

[3] See for example the comment on the reviewer's article 'Distributional Equity in Islam' by Erfan Shafe in Munawar Iqbal (ed.) 1988.

[4] His contribution 'Islamizing Economics' in 1984 was in a different vein as compared to his *Teaching*.

[5] The point is not that if one is following either of the approaches at one time he never follows the other or is opposed to it.

The lapse makes the selection of topics for discussion in each area somewhat arbitrary, and at places, tends to mar the sense of proportions and/or level in exposition. Also, the *Teaching* is devoid of any diagrams explaining Islamic departures from mainstream positions, or showing their significance. The use of mathematics is rare and at places dubious.[6] One justification for these omissions could be that the *Teaching* is for university level teachers who are supposed to be well-versed in the mainstream positions, which occupies most of the space in the book. The extraneous coverage seems to have taken a toll on the focus and clarity in writing. However, one may consider Siddiqi's work within its own framework. Let us have a brief look at its structure and content.

2. STRUCTURE AND CONTENT

Apart from a brief introduction (pp.xi-xiv), the *Teaching* consists of six chapters spread over 215 pages. It provides two reading lists: one for Islamic economics, and the other for mainstream economics in the form of appendices. The introduction mentions for Islamic economics two basic points of departure from conventional analysis: The first is the non-acceptance of behaviour aimed at maximizing private benefit on the part of an economic agent under any circumstance, and the second is the rejection of minimizing the role of the state in the working of an economy as a doctrinal plank (p.xiii).

Essentially committed to the neoclassical-Keynesian synthesis, the *Teaching* does not touch upon the modern developments in the field of mainstream economics which now form a significant part of even undergraduate courses in the universities. These developments are perhaps, in many cases, no less challenging for imparting an Islamic perspective than what is discussed. For example, chapter one, devoted to microeconomics broadly covers methodology, markets, distribution, production, and consumption as major categories. It typically ignores departures from Marshallian economics, especially the increasing formalist approach to the constructing of economic theories, recent developments in the area of monopolistic competition, the impact of Chicago school on the discipline, the treatment of risk and uncertainty, in particular the problem of moral hazard,

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[6] In his macro economic variables Siddiqi includes moderation principle (m), social goals of investment (φ), social objectives of employees (λ), and social considerations of labourers (λ) (p.44). There symbols he then uses in specifying the Islamic functional forms for consumption (p.51), investment (p.54), and wages (p.58). How these variables would be quantified so as to make the function operable is not clear. No effort has been made even to explain in which direction positive or negative, will the variables affect the function in each case. Functions of the sort are clearly of little value. Presumably, a better way of bringing in qualitative considerations like moderation into the picture would be to pack them in the 'other things being equal' clause of model, and explain the consequences as assumptions are withdrawn.

growing importance of financial markets and unbridled speculation, the relative shift in focus towards policy, growing concerns about environment, new directions in welfare economics, and so on. Even in the areas the chapter covers, one may not always be inclined to take Siddiqi's comments on secular positions without a grain of salt. We shall have occasion to refer to the matter later.

The modern undergraduate courses in macroeconomics are mostly structured around the issues of increasing economic instability, output-inflation relationship, slowing growth with rising unemployment, and the two-gap implications. The course outlines usually cover the classical and Keynsian system, monetarist revolution, new classical economics, fresh Keynesian directions, fiscal and monetary policies, recent model extension, and problems of open economies. Chapter two of the *Teaching* on macroeconomics touches only the fringe of this vast area. It opens with a brief albeit erudite introduction, fixes up the variable symbols, and prefers to open the discussion with examining the nature and role of money, rather than with the customary income determination. It then moves on to consumption, savings, and investment, and their role in the determination of income,[7] fiscal policy including *zakah*, inflation stabilization and growth, and the fiscal and monetary policy. It talks of movement from a capitalist to an Islamic economy, and eventually closes with an epilogue.

Chapter three deals with public finance, a branch of economics where normative and art aspects of the subject overshadow its positive bearings and make it more open to Islamic intrusions. This is the lengthiest, and a better written chapter of the book. It opens with a net and compact introduction, and coveys in a systematic way a vast spectrum. The chapter is divided into broad sections including (i) Goals and functions of an Islamic state. (ii) Fiscal functions where the argument opening with a discussion on priorities is followed by those on distribution, growth, resource allocation, and stabilization functions. The section closes with touching on the issue of the fiscal-monetary policy mix in a rather fuzzy way.[8] (iii) Expenditure policy discusses spending categories, supply of goods

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[7] In mainstream economics consumption and investment are aggregates of aspects of individuals' action, they as persons do not make these exclusive categories. The expenditure of the same individual may in part appear in consumption, and in part in investment. The *Teaching* sees, with the abolition of interest, "an integration between the decision to consume and the decision to invest which is (regarded) entirely different from the choice between a decision to consume now and a decision to consume in the future." (p.39). In the chapter under discussion the author is all at sea to take the integration to its logical conclusion. See also note 36 below.

[8] "Arguably, monetary policy in an open economy is best used to influence the external sector, while fiscal policy is most effective in influencing the domestic sector, although the pairing of objectives with instruments remains a controversial theoretical issue in the economic literature. Often, contradictory fiscal policy being combined with expansionary monetary policy depending on the economic conditions," Ariff, 1998, p.11. The *Teaching*

versus their production through the public sector, and project evaluation, the author advising the teacher to review the literature available on the subject in Islamic economics (iv) Sources of public revenue covers the topics dealing with public property, withdrawals from the private sector including their economic impact, and the *shari'ah* justification for taxes. (v) Taxes and their impact covers taxes on persons, corporations, expenditure, capital gains, wealth, inheritance, gifts, payroll, sales, production, and local and state level levies. The inclusion of *zakah* in the discussion has been incorporated where appropriate. Under 'income tax with *zakah*' a worth considering scheme of adjustment between the two is proposed for ensuring equity (pp.101-102). The crucial issue of incidence of taxation is ignored. (vi) The topic 'full employment, price stability, and fiscal policy' includes discussion on fiscal policy in a sharing economy. A clarification is needed: sharing here means the division of profit among the suppliers of capital, not between labour and capital. It is unclear why the author talks later of "an economy where profit sharing is the dominant mode both in the financial sector and in the labour market" (p.113 emphasis added). The next section (vii) deals with fiscal policy and economic development. It takes up the issues of development priorities, deficit financing, debt versus taxation, financing by money creation, foreign debt, and the outstanding public debt, (viii) Lastly, the chapter touches on the interdependence of modern economies with reference to exchange rates and tariffs, and intertwined jurisdictions before coming to (ix) Conclusion.

International economics deals with the economic interdependence among nations which has increased in volume and variety at a much faster pace after the seventies for a number of reasons. Chapter four covers the relevant topics for an undergraduate course including international trade theory and policy in the context of welfare and growth; the balance of payments and accompanying adjustment problems; open-economy macroeconomics, exchange rate and capital movements; and international monetary system. At places the treatment voices Islamic and developing countries' concerns. In view of the current turmoil the East Asian economies are facing, and the difficulties even the developed world is in, the analysis may look stale, but one must note that the *Teachings* was published much earlier. However, one thing is somewhat puzzling. Why did the learned author felt it necessary to bring in the issue of world view at this stage, why not earlier ? For, it is the world view differences that essentially make the mainstream and the Islamic economic positions often irreconcilably divergent from one another, not in trade alone but in almost every sphere of economic activity.

The concept and content of economic development has undergone significant changes in the mainstream literature over the past decades. Growth in per capita gross national product (GNP) remains important, but no less important have

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does not take note of the point in discussing the issue of policy mix. Hence the lack of clarity.

become concerns for distributive equity, eradication of poverty, promotion of self-esteem, empowerment of the weak, and grass root participation.[9] These developments are welcome from Islamic viewpoint. Yet, the Islamic notion of development differs from the mainstream construct in an important way. An integrated growth of spiritual, moral, and material aspects of human personality is the essence of development in Islam. Islam welcomes the material achievements of man only to serve as a means of attaining solace in the hereafter, his ultimate abode.[10] Chapter five in the *Teaching* on economic development takes note of these facts, though it retains growth at the centre of stage. The section on 'historical background' makes some interesting observations on the controversy concerning the contribution of the colonies in the past to the development of the parent countries and vice versa. But the debate now matters little "as historical instances do not quite fit the current scenario" in the developing countries (p.163). After discussing theories of growth and the strategies for development, the author passes on to the 'mobilization of resources' briefly covering taxation, borrowing-internal and external and deficit financing. In the case of deficit financing, he ignores the possibilities of using the instrument to divert resources from current consumption to capital formation for economic development.[11]

In the discussion on human resources covering education, training, and manpower planning Siddiqi does not consider the present population sizes, and rates of demographic growth of the Asian and African countries to be a hurdle in their economic development (p.182), though the explosion of numbers is taken as one of the major factors contributing to their non-achievements in many areas and cases. Family planning is viewed as a sensitive issue for Islamic economics, but a stand has to be taken, especially after the 1992 Cairo deliberations focusing on the matter, and the environmentalists blaming much of the problems on the size and growth of the third world population. Surely, the learned author was better equipped than many other Muslim economists to take up the issue, but he does not.[12]

Under the section on 'trade and development', the chapter discusses topics like commercial policy, and foreign capital, both equity and loans. This is followed by observations on 'planning'. Here, one gets the impression that planning has almost become redundant with the failure of experiments in socialism. But let one not be oblivious to the fact that socialist ideology is alive in not a few countries of Europe,

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[9] On this see Zubair Hassan, 1995, pp.83, 85.

[10] In the Islamic system it is the all pervading concept of *amanah* that "seeks to convert the material ambitions of man into the means of attaining spiritual heights i.e. his ultimate goal." (The Qur'an 28:77). Zubair Hasan, 1988, p.41.

[11] For example, the Indian Five-Year plans experimented with deficit financing to mobilize resources for capital formation, and it was quite successful during the fifties.

[12] A brief discussion on the issue is available in Zubair Hasan, 1995, pp.100-102.

that the experiment in communist practices still survives in China, Cuba and North Korea, that socialistic ideas are not entirely unknown in the Islamic world, and that economic planning continues in most of the developing economies, albeit with emphasis changing from the state participation in enterprise to its regulation. The chapter touches on the stabilization issue in a developing economy, and on the dependency theorem[13] before drawing to a close.

The last chapter of the book is on money and banking. After dealing with what money is and what money does in the introduction, it briefly focuses on monetary equilibrium, repeats familiar arguments on the prohibition of interest, elaborates on financial intermediation including international monetary arrangements, explains the main features of Islamic banking, but does not tell how profit sharing ratio can be effective as a policy instrument in view of the crucial objection that unlike the rate of interest it is not a price.[14] Financing government deficits appears once more in the discussion.[15] The chapter closes with inflation and indexation after providing a critique of conventional banking and monetary reform proposals.

One hopes that the foregoing sketch of the *Teaching* is not an unfair depiction of what it contains, and what its main thrust is in the diverse areas it traverses. It speaks of the versatility and depth of the author's scholarship that he could handle such a difficult terrain with ease and conviction. The *Teaching* provides a worthwhile base for carrying forward the work it has initiated. It deals with a large chunk of hard core economics, and no single reviewer can do justice to the analyses it presents. We may, however, seek to clarify a few of the issues the teaching raises. These include the question of methodology, the efficacy of extremum solutions in economics, the determination of wages, replacement of interest with profit, the treatment of *infaq, zakah* and moderation in macroeconomics models, and the role of state in the economic life of the community.

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[13] There are various interpretations of dependency. The literature is dominated by sociologists and political scientists who charge economists of neglecting social and political factors in their construction of dependency theories. Islamic economists will do well to pay more attention to their arguments, because it is basically the socio-political structure and institutions of Islamic economic system that are likely to condition economic development in Muslim countries.

[14] The point was raised by Arrif,1982, p.22.

[15] The issue was discussed earlier in the chapter on public finance (pp.116-117). In both places the apprehension expressed is of its misuse by the government leading to inflationary pressures or resource wastage in the economy. However, if the state as per assumption underlying the *Teaching* is Islamic in the Islamic system none of the fears is valid. Moreover, one must also take the fact into account that in such a system the credit creation power of banks will be much less as compared with the mainstream system. Unfortunately, the *Teaching* chooses to by-pass these important points.

3. METHODOLOGY AND METHODS

Methodology of economics remains in a rather muddled state, more so in the Islamic version of the discipline. The confusion mainly finds expression in a failure to keep the issue of methodology distinct and separate from that of methods. Methodology *per se* belongs to the philosophy of economics, and the relationship between the two is of the same sort as between *usul fiqh* and *fiqh*. Broadly, methodology consists of a set of criteria, rules, and procedures which the philosophers of the subject have evolved over the years to examine the nature, scope, and performance of the subject. It is concerned with methods, but does not belong to their category. Rather, it is an abstract sort of undertaking which seeks to examine from outside the department of economics, what methods are the right ones for the economists to use, what the proper way of using them is, and what kind of results they are capable of yielding. For this purpose, methodology uses certain principles expressed in the form of criteria and rules. Investigators employing the same method, i.e., using the same steps in their research and analysis, may hold very different methodological positions, while supporters of the same methodological principles may decide to use very different methods depending on their judgement concerning various aspects of the problem under investigation. There are a number of differences between the methodologies of the two economic disciplines-mainstream and Islamic. Presently we cannot discuss them all. But a crucial one may be stated: Methodology of mainstream economics essentially is a posterior development, and has without fail sought to rationalize what economists have actually been doing over the centuries to fortify the evolving doctrine of freedom of enterprise and what goes with it. In contrast, for Islamic economics the doctrine is already contained in the revelation. To discover it has been and still remains, the task of methodology in Islamic economics. Here, unlike the position in mainstream economics, the glide essentially is from methodology to economics, not vice versa.

Under methodology (pp.3-12), the *Teaching* puts together the topics: assumptions, rationality, institutional framework, goals of the Islamic economy, implications of economic analysis beyond the market, motives, some tools of analysis, and laws of economics, with the conspicuous absence of any mention of methods. Some of the discussion under individual headings provides useful insights into the chosen subject. But taken as a whole, how far this potpourri of unlinked topics would enlighten the readers on the important issue of methodology is difficult to see. And if methodology means a work plan, the term is misleading, unless the meaning is made explicit. Islamic economics still awaits a scholarly discussion on the subject.[16]

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[16] The main weakness of the writings in the area is not to note down the points of departure of methodology in Islamic economics from its mainstream counterpart. On this, see Zubair Hassan, 1998 (section-4).

4. EXTREMUM SOLUTIONS

The nature and content of economic theory has been much influenced over the years by the view that man is actuated only by the desire to promote self-interest, and that he invariably attempts to enlarge his gain as much as possible. The proposition is the basis of extremum solutions, which accord precision and a scientific import to economic theory. To maximize individual gain – utility, satisfaction, or profit, for example – in considered as the epitome of rational economic behaviour. In this connection, Siddiqi observes:

> The maximization hypothesis is not very helpful in understanding the economy, any economy. But it is entirely unacceptable as an aid to the understanding of an Islamic economy, any Islamic economy. Even some understanding of Islam and some compliance with its teachings is sufficient to create a society which defies the maximization hypothesis. Some thing else is needed." (p.xiii, see also pp. 17 and 28).

What that 'some thing else' is, the author does not spell out. It would not perhaps be unfair to demand elaboration, or documentation on the point. There is, of course, a sizable literature on the scientific limitations of the hypothesis, but there perhaps is even more that finds it efficacious. The important question is: why has economic theory continued to retain the hypothesis despite so much of scathing criticism?

The notion of self-interest and extremum solutions, both in business and consumption, go together. Therefore, as a preliminary, let us note that right from the days of the classical writers to most recent times, mainstream economists have explicity maintained that the conclusions of economics are based upon a certain number of initial premises chosen deliberately, and that the said conclusions are only provisionally true. Economics borrows its notions of exchange, demand and supply, capital and revenue, and the like from actual life, and out of these conceptions it builds the ideal or abstract type upon which the economists exercise their power of reasoning to establish the laws of economics.[17] These laws rest on presumptions concerning human behaviour as constrained by some simplifying assumptions. To make the laws more universal, the economists search for bases of uniformity in human conduct. Our behaviour is affected not only by the action of fellow human beings but also by the laws of the physical world that surrounds us. These laws are supposed to be universal and permanent for the simple reason that the elementary needs of the people have always and every where been the same. Every individual desires well-being through need fulfillment, and so will be possessed of wealth. But this never implied the denial of the existence, in addition

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[17] See Gide and Rist p.360.

to self-interest, of other motives operating in the economic world. The motives here, as elsewhere, are recognized to be extremely varied. Vanity, the desire to glory, altruism, pleasure afforded by the work itself, the sense of duty, pity, benevolence, love of kin, or simply custom, all come in. Still, what brought self-interest to the fore is that the primary aim of economics is to study the relevant phenomena en masse: the crowd, not the individual.[18] Mainstream economics holds that of the numerous motives that influence economic conduct, the one that is relatively universal, and stable is that of self-interest. It is difficult to prove them wrong. The propriety of the proposition is implicit in the very institution of private ownership of property which both the secular (capitalist) and Islamic systems grant. Seeking personal gains without harming others is in no way prohibited by Islam. The *Teaching* is explicit on the point.

The pursuit of self-interest as economic goal does not deny the existence of other motives-moral, spiritual, or ethical-that may spur people into action; it only relegates them to the consideration of other sciences or to the ceteris paribus bin. The question is of discretion, not of elimination. Furthermore, it is not correct to always equate self-interest with selfishness. Selfishness implies deficiency in the consideration for others; self-interest can be pursued, especially under Islamic norms of behaviour along with sympathy, and benevolence. The pursuit of self-interest (economic gain) can be combined with noble objective. In fact, in a world based on division of labour and economic interdependence pursuit of self-interest makes it, in a measure, imperative to care for the interests of others. Therefore, self-interest *per se* is not, the *Teaching* agrees, something untouchable in Islamic economics. However, to quantify the extent of its 'singe minded pursuit' (p.8) for comparison is well nigh impossible. The condemnation of self-interest in the literature is often stretchy and misplaced. But what about the maximization of personal benefit?

Under dynamic uncertain conditions, which characterize real world phenomena, maximum private gain is rarely a known precise quantity that an economic agent – firm or consumer – may attempt to achieve. Economic diagrams depicting optimal solutions have no time dimension; they show the direction for movement, not the elusive destination. Even in their static frame, the quantum of a maximum (or minimum)[19] they indicate is only relative: it depend on the assumptions underlying the model. In the case of perfect competition, for example, the maximum profit a firm can earn in the long run is apparently no more than normal and hence

[18] *ibid.* pp.396-398.

[19] Problems of maximization can be seen as problems of minimization and vice versa. For example, given the inputs one may think of maximizing the output, while to achieve the same output one can think of minimizing the value of inputs. Without extremum solutions the concept of efficiency of which the *Teaching* talks so often, loses precision and objectivity.

considered (morally) legitimate. But in monopoly, the maximum is denounced as exploitative of the workers and/or consumers. Furthermore, mainstream economic theory retains the maximization hypothesis despite its dubious character essentially for two reasons.

First price theory, the core of economic science, cannot stand erect once the maximizing assumption is withdrawn. Siddiqi wants the teacher to impress upon the students, the significance of the point that shows the equilibrium of demand and supply in price formation (p.15). Presumably, the most obvious message is that, *ceteris paribus*, the point gives a price which maximizes consumers' satisfaction as also the producers' profit simultaneously. The second reason is that the critics of the conventional assumption have not so far been able to propose an alternative behavioural rule which could have the same, if not superior, predictive value, and lead to empirically testable conclusions. The reviewer has ventured the argument in an earlier writing that we in Islamic economics too need not throw away the baby with the bath water. He demonstrated that in business, the consequences of profit maximization can be quite different and welcome in an Islamic model in contrast to a secular one.[20] Maximization *per se* is value neutral: what is maximized, how, and for whom are the real issues. Interestingly, Siddiqi, having spent the last bullet in his arsenal on the proposition, decides to put it on oxygen: "We dilute the assumption of maximization of profit in case of the producer by admitting motives other than profit, including motives that relate to others – labour, consumers, other producers, or the entire society." (p.9 emphasis added). 'Dilution' is not advisable. More so, when it is possible to accommodate in *ceteris paribus* all the Islamic considerations in price formation without any tampering with the hypothesis.[21] The simple maximization micro model based on the assumption of rational individuals has potentially infinite applications and recent years have seen it used in widely diverse areas, even outside economics.[22] The abandonment or dilution of the proposition will both require a total rewriting of Islamic economics in an all-or-nothing mould. The *Teaching* is not compatible with such a requirement. In later discussion it clearly relies on or upholds the hypothesis (see p.56, for example). Presumably, this is why in the epilogue, Siddiqi waters down his position considerable when he says: "Economic agents...are assumed to care for others and take the interest of the society into consideration while trying to serve their own interest by earning as much as possible in a decent manner subject to these considerations" (p.40, [23] emphasis added). 'These considerations' may better be

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[20] See Zubair Hassan 1992, especially pp. 248-251.
[21] *ibid*. pp.244-247.
[22] Presently, the hypothesis is being increasingly used in psychology, political science, and sociology also.
[23] Any modern text book on Managerial Economics will testify that such goals no long lie outside the ambit of the mainstream literature on economics. See for example Keat and Young pp.28-31, where profit maximization is seen constrained by such considerations.

covered by 'other things being equal'. In the following discussion the *Teaching* clearly relies on the hypothesis.

Let us now turn to the treatment of consumers' demand. The neoclassical theory which postulated that as price falls, the quantity demanded will increase was based on assumptions about utility maximization. It assumed that the utility one gets from consuming a good depended exclusively on its quantity consumed, that cardinal measurement of utility was possible, and that the principle of diminishing marginal utility was true. These assumptions were additional to those covered under the usual 'other things remaining the same' phrase. The theory was questioned on the basis that cardinal measurement of utility was not possible, that the view of diminishing marginal utility was not valid, that empirical evidence in the matter was contradictory, and that the theory rested on a hedonistic psychology. The evolution of indifference curves eliminated the first two of these objections. It was shown that a generalized utility function allows for substitute and complementary relationships which could accommodate, contrary to Siddiqi's view (p.38), the hierachy of human needs. The decomposition of price effect into the, substitution, and income effects that the technique permits provides useful insights into consumers' demand.[24]

Since the indifference curve is a theoretical construct devoid of empirical content, the theory of consumer behaviour becomes tautological. The revealed preference approach did try some improvements, but could hardly do anything on this score: it only endorsed that what was actually purchased was also preferred. Also, as the consumer was assumed to maximize, purchase equaled maximizing.[25] Two recent developments in utility theory-the inclusion of risk, and modification of concepts could also not ameliorate the situation.[26] And a tautological theory of course does not tell us anything about consumer behaviour. However, most modern mainstream economists continue to use the indifference curve technique, despite recognizing its limitations. Siddiqi mentions a number of Islamic requirements which he wants "to be taken into consideration in discussing consumer equilibrium in Islamic perspective." (p.40). But since he has all along been very critical of the indifference curve analysis, and if used, wants many modifications not provided for in mainstream text books, one would not be unreasonable to expect from a scholar of his stature a demonstration of equilibrium without using the unacceptable techniques, or at least showing the path to needed modifications in the

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[24] It makes our understanding clearer about why, and when the demand curve may depart from its normal downward slope, and show a positive relationship between price and quantity demanded i.e. the distinction between inferior, and Giffen goods is made possible.

[25] Landreth and Colander p. 440.

[26] *ibid.* pp.441-443.

conventional diagrams. Indeed, that would have been a great service to the teaching of Islamic economics.[27]

5. DETERMINATION OF WAGES

Determination of factor rewards has always been a fascinating, yet very controversial, area in economics. Lumping together the factors of production, economists generally reduce them to broad categories of labour and capital. The issue of factor rewards thus virtually boils down to the determination of workers' wages, the remaining value product going to the owners of capital as profit including interest. Assuming perfect competition, and the supply of labour schedule as given, mainstream economics demonstrates that the market determined wages are 'just' as well, for they equal their contribution to the value product of the firm. The instrument used for the demonstration is the celebrated marginal productivity theory of income distribution. Since Islam too upholds payments according to contribution as just, Islamic economists mostly tend to support and use the theory. Siddiqi is no exception. He only wants that its pros and cons should be explained to the students, and the theory "may continue being used in the study of wages as relevant for the long-run competitive equilibrium" (p.21). Thus, on wages, Siddiqi hardly moves out of the mainstream groove. Certainly, any university level teacher must have already been taking care of the points he raises. What one expected, but finds missing or muddled in his *Teaching* is the imparting of any worthwhile Islamic content to the theory of wages. Some modifications are suggested (p.21-22), but remain qualified by the phrase "should the situation call for such a measure". Had the author provided a few illustrations of 'the situations', he had in mind and explored the feasibility as also the possible repercussions of the indicated modifications the readers would have probably been better enlightened. Any how, situation specific cases do not make the rule.

It has to be noted that mainstream economics continues to retain not a few obsolete concepts and untenable theories conventionally or because they are able to maintain the facade supportive of the capitalist doctrine. Marginal productivity theory falls in this group. It was developed as a reaction to the emergence of some socialistic ideas in the area of income distribution.[28] One virtue of perfectly competitive markets was shown to be that each factor of production would receive the value of its marginal product. This return measures, it was argued, the contribution of a factor to the product in question as well as to the society. Thus,

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[27] Apart from the Keynesian consumption function, the Islamic economists will do well to look at the later developments in the area. For example, the exploration of the life cycle hypothesis may lead to some interesting insights from an Islamic viewpoint.

[28] "J. B. Clark's development of marginal productivity theory ... might be explained as a reaction to economic ideas of Henry George and Karl Marx". Landreth and Colander p.247. The elaboration there is quite insightful.

profit, the return to capital, was justified by the fact that capital was productive, and profit was only normal: it was not the fruit of exploitation. Rent, the return to land, was in the same way not an unearned income, but a payment for the productivity of land. The same was true for wages, the return to labour. In sum, the distribution of income brought about by perfect competition was an ethically correct distribution as it rewarded the factors of production according to their economic contributions to the social product.[29]

There are endless arguments in the literature about the assumptions that underlie the theory, let alone about what the theory actually predicts, and how well it has faired. What has not been much in focus is the fact that the theory is misleading on its own terms. First, the output of a firm, industry, or the economy is the result of combinative effort of various factors of production, and it is impossible to separate out their marginal products without being arbitrary. Second, even if individual factor productivity could somehow be ascertained, payments based on it could not always be 'just' on the basis of contribution. For, it is not the contribution of a factor to output, but its scarcity relative to other factors that determines both its marginal product and reward. Third, the demonstration that under long-run competitive equilibrium, each factor is paid the same amount as the value of its marginal product does not mean that marginal product determines the factor income. This follows from the famous Marshallian dictum that marginal uses and costs do not govern value but are governed together with value by general forces of demand and supply. Fourth, perfect competition on which the theory rests, is not only unreasonable, more than that it is self-destroying.[30] The real world market situations are dotted with monopoly elements, weak or strong, scattered throughout the modern economies. Once the average revenue product curve for a factor is separated from that for its marginal revenue product, and lies above it over the relevant arrange of output, payment equal to marginal revenue product would only be exploitative of the factor.

It comes about that there is no valid ground for pretending that the doctrine of marginal productivity can be put forward as a theory of wages, though it does throw into light one of the causes that govern wages. Its retention in Islamic economics would certainly conflict with the Islamic norm of distributive justice. The key for an Islamic solution to 'just' wages lies in some sort of profit sharing arrangement with capital, subject to a minimum wage constraint.[31] Such models for

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[29] *ibid.*, p.248.

[30] For an explanation of self-liquidating character of perfect competition see Zubair Hassan, 1992, p.241.

[31] It is interesting to note that Bastiat (180-1850) was long back quick to "expose the patent contradiction involved in guaranteeing a minimum revenue to the landed proprietors and capitalists by the establishment of protective rights, while refusing a minimum wage to the workers." (Guide and Rist, p.356). The resistance to their fixation in recent times has

sharing exist in the literature, both mainstream and Islamic, and must be scrutinized for the purpose. They may also help put the theory of profit in a correct Islamic perspective.[32]

However, it may not be impertinent to look at the demand for, and supply of labour functions as formulated in the *Teaching* before closing this section. The functions are put in an inverse form as it has some explanatory advantages. "Since marginal productivity of labour depends on the level of employment, given K (capital), we have

$$w = (N,\lambda) \text{ demand for labour function}$$
$$w = (N,\lambda') \text{ the supply of labour function}$$

w in the above equations stand for real wage rate, so that w = W/P, the money wage rate W divided by the price level P." Equating demand with supply, one gets the equilibrium values of w, and N (p.58). Now, λ represents social objectives of employers, and λ' the social considerations before the workers (p.44). Since these variables cannot be quantified, they are taken as given. However, that leaves both functions specified in one variable N. How will the solution be done, what shall determine the shape, and slope of the curves, and how? Even if one could obtain the demand function through the horizontal summation of the relevant marginal value product curves in the conventional way, to specify the supply function still remains. It is considered to be:

> "a complex affair, since an individual supply curve of the usual shape, sloping upward from left to right, involves the assumption that all work involves pain (or disutility) which increases as hours increase. This is not always true, irrespective of the loss of income ..... useful work is a basic human need. To try to by-pass this issue by using indifference curves between leisure and hours of work does not help as leisure is not a substitute for the kind of work noted above." (pp.19-20).[33]

True, people may not always work for a money reward, but it is more true that they do not always work independent of monetary considerations i.e. in most cases.

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almost crumbled for a variety of reasons, not necessarily always economic, and grant of minimum wages tends to become universal. (See Zubair Hassan, 1995b, Section 5). It is astonishing that, despite the spirit of the *shari'ah* being not opposed to the measure, Islamic economists mostly continue to denounce the same. Siddiqi chooses to shun the discussion on the point.

[32] On this see Zubair Hassan, 1983.

[33] It is not clear what is meant by "the kind of work noted above." For, the work not carried out for pecuniary gain simply lies outside the domain of economics, mainstream or Islamic.

In general, there is a trade-off between work and leisure with reference to wage level.

Siddiqi mentions a number of factors including availability of grants on the basis of needs as affecting an individual's choice between work and leisure (p.20), but *zakah*, he says, may not have any significant effect on it (p.110). The reason for difference in the effect of the two-grants and *zakah*- on the choice is not clear, if it is recognized "that the major portion of *zakah* in a modern Islamic state is to be spent (also) on need fulfilment" (p.110). Be that as it may, the argument remains: "At the level of the economy as a whole the shape of the supply of labour curve involves the whole population, its composition, and its rate of growth. It is unrealistic even to try to capture this complex reality in a simple curve" (p.20). Where do we go from here? How to explain the upward sloping shape of the supply of labour curve?

The *Teaching* provides the reply: "The upward rising supply curve may be justified on the ground that as higher wages are offered in a particular industry, labourers are attracted away from other industries to this particular industry..." (p.20). This could be true in a full employment economy, and in the short run. In the competitive long run equilibrium which lies at the heart of Siddiqi's argument, and in over populated developing economies the plea is untenable. On the determination of wages, the *Teaching* tends to obfuscate.

6. INTEREST EQUILIBRIUM AND PROFIT EXPECTATIONS

A few observations on the role of interest in macro models and the effort at replacing it with expected rate of profit might not be out of place. To begin with, mainstream economic theory justifies the payment of interest, in essence, as the time value of money. Abolition of interest in an Islamic system demands that no income must have even the semblance of this value. The *Teaching* approvingly mentions the all pervasive practice of Islamic banks of buying goods ordered by clients and selling the same to them on hire-purchase by adding a mark-up to earn profit (pp.49, 207, and 210). In the garb of fixed margins over cost, is being charged, one may suspect, the time value of money, a rate of interest. It may be argued that the mark-up is justified to enable the banks cover their costs for rendering the service. If the surplus earned through the practice is no more than the sum of these costs is a matter for empirical research; but it intuitively looks much more.[34] One way to ensure the removal of every trace of interest from the revenue and ensure transparency is worth exploring. It is to institute periodic pay-backs of

[34] The bulk of the transactions in Islamic banking, about 73% according to an estimate, fall in this category. Hence, the importance of looking into the matter afresh, as also the efficacy of the suggestion.

the estimated surplus over costs to the clients in the form of purchase dividend on a pro rata basis as is sometimes done in consumers' cooperatives.

Again, factors affecting money demand in the economy are not identical in different macro models. For example, the classical view of money focused simply on its role in transactions, and, therefore, neglected the role of interest rate in determining money demand. On the other hand, the Keynesians took note of the role money plays as an asset, as an alternative store of wealth to bonds, and held that money demand does depend on the rate of interest. To replace i, the rate of interest, with p the average expected rate of profit, and set up the money demand function (p.50) as $M^d = (Y, \rho)$ is too simplistic, and requires explanation. It leads the reader no where in the absence of a demonstration of its uses and their implications in different sorts of models.

Next, in mainstream economics, the rate of interest adjustments tend to maintain the product and money markets together in a state of equilibrium, and can be shown to contribute to its stability in varying degrees depending on the model one is using.[35] In general, the policy of moving interest rate directly with profit expectations tends to dampen the latter during inflation, and to stem their fall when the economy is slowing down. How, and to what extent, will the replacement of the interest rate by average profit rate do the job is a point the *Teaching* could have done well to consider.

Lastly, assuming that banks share the entrepreneurial (rate of) profit π in the ration ϕ, and the depositors also share banks' profit in the same ratio, Siddiqi rightly shows the depositors' rate of profit as equal to $\phi^2\pi$. But one is not sure if it would be more appropriate take ρ, the average rate of profit, as equal to the entrepreneurial rate of profit π, or, following Siddiqi, as equal to the return to deposits, i.e. $\phi^2\pi$, for setting up the Islamic money demand, and investment

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[35] Macroeconomic models differ from one another with reference to their definitions, the aggregates they use the way they fix their variables and constants, the policy implications that follow from them, the objectives they address, and the predictions they are supposed to make. For example, in the classical model money supply alone affects aggregate demand, fiscal policy i.e. a change in government purchases of goods and services or in taxes has no effect on the variable. In contrast, even the simple Keynesian model treats fiscal policy influences and those emanating from the rest of the world as dominant factors in the situation; a change in the money supply is seen to affect aggregate demand only indirectly through its impact on investment via the interest rate. In the customary sense, chapter two hardly contains a macro model- Islamic or mainstream- although it talks of the model more than once. In fact, it is because of non-specification of the model frame in the chapter that one may not always find it easy to understand, much less appreciate, its argument.

functions. For, ρ is a function of π, not π of. ρ.[36] In any case, he perhaps leaves too much for the uninitiated teacher to deal with in asking him to explain to the students the determination of ρ and Y by the simultaneous equilibrium of the markets, and also make a comparison of the Islamic construct with the mainstream IS-LM model (p.56). But what about making an IS-LM model with the Islamic variables: will it not be possible? The *Teaching* leaves the question open.

7. TREATMENT OF *INFAQ*, *ZAKAH* AND MODERATION

In the simple Keynesian model a central notion is that for a level of output to be an equilibrium level requires that output, (GNP) Y, be equal to aggregate demand Y^d, or desired expenditure on output. Aggregate demand (Y^d) has three components: household consumption (C), desired business investment demand (I), and the public sector's demand for goods and services (G). Thus, in equilibrium we have: $Y = Y^d = C + I + G$. As national product, Y is also taken to measure national income, we can write: $Y \equiv C + S + T$, where S stands for aggregate savings, and T for taxes collected. The equation is an accounting definition or identity. It states that national income, all of which is assumed to be paid to households in return for factor services, is either consumed, paid out in taxes, or is saved. We may combine the identity and the equation to state the equilibrium condition as under

$$C + S + T \equiv Y = C + I + G$$

Now, this formulation will hold good (in a balanced budget situation) only if desired investment (I) equals the realized investment (I_r), i.e. the voluntary holding of inventories is zero. For, then alone will the desired savings, and desired investment be equal. Siddiqi introduces one more variable E, the expenditure in the way of Allah, in the formulation (p.60), but it cancels out from both sides in the process of simplification to yield the equilibrium condition $I = S + (T - G)$. What Islamic impact the introduction of E then is expected to make on the model is unclear. Presumably, it would be appropriate to merge or treat E with *zakah* payments in the process of model modification. Total amount of *zakah*, Z, payable in a year is the z fraction of the sum (say T), of three entities that are chargeable to *zakah* at different rates and belong to the payers: capital assets K_n, current income Y_n, and savings current as well as past S_n. Fraction z is the weighted mean of the respective rates z_k, z_y and z_s so adjusted that each becomes applicable to total value of the entity $(T - K_n + Y_n + S_n)$ with the payers. For example, if we multiply z_k by the ratio K_n/T, z_k would be appropriately reduced to say z_k, to make $z_k K_n = z_k' T$.

Of course, this much Siddiqi could leave to be worked out by of the teacher. The real difficulty is with his treatment of savings (p.64). First, the entity S_n

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[36] One may point out that it is not appropriate to use p as the rate of expected profit instead of π in the discussion on 'inflation stability and growth' as well (p.67).

includes by definition both the past and current savings, but *zakah* is taken as paid only from the payers' current income Y_n (p.63). Now, in calculating *zakah* on income not even the current savings are taken out from the latter. Thus, current savings are put to charge twice: once as part of S_n, and again as part of Y_n. One is not sure if to levy *zakah* twice on part of Y_n is the *shari'ah* requirement[37]. In any case, *zakah* being chargeable on all three of the items- the stock of capital, savings, and income- the fact that the percentage share of *zakah* in national income should vary directly both with the capital-output ratio, and propensity to save is probably too obvious to warrant the algebraic exercise on pp.62-65. More importantly, the policy importance of the result is neither clear nor explained.

An important point concerning the nature of *zakah* was put into focus by Naqvi when he regarded it as a proportional tax and therefore regressive. It was then argued, that a tax system should be judged not on the basis of individual taxes but as a whole for its efficacy with reference to equity[38]. The *Teaching* endorses the argument (p.111). The plea is valid but smells a bit apologetic. Islamic economists would do well to look into the debate on proportional versus progressive taxation for building a positive argument.[39]

8. ROLE OF STATE

An attempt to organize, or restructure, an economy according to Islamic requirements, especially facing major development problems, would have to decide on the respective roles of the state and the market. The question which way the choice would, or should, tilt does not belong to the terrain of a priori reasoning. The Islamic emphasis on ethical conduct and social concern may or may not minimize state intervention in the economy. Ground conditions matter. Also, under the same level of commitment, temporal or developmental priorities may cause differences. However, under the Islamic dispensation, the role of the government in economic matters is likely to remain relatively large even if economic agents are, on an average, adequately committed to ethical norms and societal priorities in other systems as well. Some of the reasons are quite obvious.

To begin with, the fulfilment of basic needs of all the members of the community, Muslim and non-Muslims, is the prime requirement of an Islamic economy. This would necessitate a significant departure from the usual profit guided resource allocation, and change in strategy of development, a task which free markets may not accomplish. Again, defence, self-reliance, and expansion of

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[37] It is easy to see that because of double treatment of zakah in Siddiqi, his calculation of Z would be larger by $z_y.S_N$.

[38] Iqbal, Munawar (ed.), 1988, p.251.

[39] An interesting and helpful discussion, for example, is available in Browning, and Browning, 1994, pp.378-380.

infrastructure in today's Muslim countries may demand more investment in heavy industries, prospecting, and basic research. Local private enterprise may neither be equipped nor willing for taking up the challenge. Public sector may have to step in. The *Teaching* indiscreetly advises the Muslim countries to avoid the policy of expanding the public sector to include key industries like steel, cement, electrical goods, fertilizers, machines, and machine tools with a view to accelerating economic development. The plea is that policy of the sort adopted in a number of developing countries in the past has largely failed to deliver the goods (p.84). The book does not provide a single example, and as a general observation the statement has little scientific worth. Presumably, the author has the single criterion of profitability in mind to judge the success or failure of such public sector industries. The areas they open up, the employment they generate, the self- reliance they promote, the economic independence they confer, and the expansion of consumer goods industries they facilitate – in short, the overall social benefits that eventually flow from these projects must be carefully weighed against their business profitability before one passes judgement concerning their efficacy. Of course, it is nobody's case that considerations of efficient performance are not relevant for such projects.

Take, for example, the case of India, a country which chose to start economic development from the end of investing in capital goods industries, fundamental research expansion of infrastructure, and technology. There have been wastes, failures too. But eventual benefits have been tremendous.[40] Siddiqi himself observes in his reference to dependency theories that "the emerging economies of China and India have changed the very scenario on which these theories were based." (p.192). In fact, he implies a vast public sector for an Islamic economy if one carefully scrutinizes the range of functions he expects an Islamic state to perform. He thinks it advisable to point out that the state will have to levy taxes additional to *zakah* in view of the large public expenditure including that needed for social security, defence, capital formation, and economic development (p.96). There is nothing sacrosanct about any particular strategy concerning development; it may differ from case to case.

Lastly, it may be mentioned that the state has a special duty to ensure distributive justice both with reference to income and wealth. How to bring about more equitable distribution of wealth is more important, and yet more complicated.

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[40] It would have been difficult to achieve self-sufficiency in food production, expand transport, meet substantial defence needs, install energy network, and establish many other capital and consumer goods industries. Notice that the private sector was not able to double just one plant in the iron and steel industry during fifty years prior to independence of the country. Today after less than fifty years since 1947 it has four more, to take just one example, of the public sector's endowment to the Indian economy.

It is here that Islamic economics has one of its unfulfilled tasks, in the *Teaching* as well.

9. CONCLUDING REMARKS

This review had set out of comment on Siddiqi's *Teaching* of economics in Islamic perspective but spread out in the process to have a closer look on some of the important issues that emanate from the work. It is a useful path breaking book, and an interesting reading despite weaknesses in structure, and argument. It attempts at *Teaching* the reader "to appreciate how morally oriented individuals supervised and assisted by a state bound by Divine guidance can conduct their economic affairs largely through markets and yet avoid the inequities of capitalism." (p.194). The problem is how to establish such states?

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