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# PSYCHOLOGICAL BEHAVIOUR AND ECONOMICS: THE NEED FOR NEW THEORIES AND REDEFINITION OF BASIC CONCEPTS IN ISLAMIC ECONOMICS

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## ABSTRACT

*This study attempts to posit the nexus between psychology and economics. However it is not the purpose of the paper to focus on all aspects of psychology and its various theories. It is also not the purpose of this paper to trace the historical development of economics, its various schools and the economic ideas that emerged. It discusses only those areas that are relevant to the development of economic thought particularly with regard to motivation and psychological behaviour. It traces the historical experience of western economics and psychology through three phases, which inevitably led to secularism and the separation of both disciplines from morality. This study considers the emergence of the egoistic and selfish motives underlying assumptions as the cause of the predicament and confusion in the body of knowledge present in modern economics and psychology and other behavioral sciences. Due to the inextricable link between culture, motivation and psychological behaviour, this paper also attempts to synthesize psychology and economics within the framework of the Islamic system and how the Islamic model of man influences motivation and human actions. It is the contention of this paper that the Islamic synthesis between psychology and economics is significant as it suggests the need for reformulation of economic concepts, models and policies and theories which may differ from those of neoclassical economics. Therefore as a corollary, this paper also suggests that a holistic approach to man, development and development policies should be implemented to ensure effectiveness in the enhancement of man's material and spiritual well being and his quality of life.*

**KEY WORDS:** Psychology, Economics, Self-interest motives, Rationality, Islamic economics, Islamic psychology, Man of Islam

## INTRODUCTION

Psychology comes from the Greek words psyche which means 'breath' and 'logos' which means 'knowledge of'. The term psyche was used by Greek philosophers to refer to the vital principle in man (Reese, 1983). However it was not until 1590 that the word 'psychology' was introduced by Goclenius to mean 'the science of the soul' (Reese, 1983). The history of Western psychology reveals a cyclic process (Kantor, 1963) going through a naturalistic and scientific treatment initially systematized by Aristotle (known as biopsychology or scientific psychology) in his *De Anima*, proceeding towards the medieval period where psychology was devoid of scientific investigation in the midst of preoccupation with the Christian faith and finally, influenced by the scientific renaissance, it emerged as an independent discipline in the mid-nineteenth century from what was before a branch of speculative philosophy (Corsini, 1984). It can be observed that there were remarkable similarities in the historical experience of western economic tradition, not only in the sense of it being a social science, but the existence of the interplay of artificial influences especially that of political, scientific and religious factors have brought the discipline along parallel lines (Rima, 1978).

Economics comes from the Latin word 'Oeconomia' which means household management. In Greek, Oikonomia comes from the words 'oikos' which means 'house' and 'nemein' which means 'to distribute or manage'. Although the term economics was coined around 1870 and popularized by influential neoclassical economists such as Alfred Marshall as a substitute for the earlier term political economy, it

was used as long ago as the fourth century by Aristotle, as can be seen in the first book of 'The Politics' in which he defines it as household management. However, the word is now used in a wider sense. Economics studies human welfare in terms of production, distribution and consumption of goods and services but, as a social science, economics is concerned with the intricate and complex actions and motives of man and is therefore closely related to ethics (Hastings, 2003). Although the present connotation of the term is given a materialistic emphasis in the spirit of 19th Century economic thought, in the sense of being defined as aspects of human behaviour that are concerned with production, allocation, ownership and consumption of goods and services, a closer observation will disclose the indispensability of moral considerations in affecting man's conduct in the economic sphere of life. However, if we were to study the history of economic thought, especially in the work of Adam Smith and beyond, the psychological concept of rationality, which studies the economic man and his self-interest motives in making economic decisions, has been given an emphatic note.

### **Psychology and Economics: The Nexus**

The relationship between psychology and economics is clear and precise. As was mentioned earlier, both disciplines were branches of moral philosophy. Psychology, in the traditional view is, defined as the science of the soul, and a thorough reading of history and the philosophy of science will reveal to us the fact that philosophical doctrines in the past and present have had a major impact and influence on the conception of man, and particularly the soul, and this has become the basis for the formulation of different ethical theories. Before the industrial revolution and the separation of economics as a separate discipline, economics was part of moral philosophy, as it dealt with the means to attain ultimate happiness and not the end in itself. Thus it is not surprising to see the discussion on economics in Aristotle's works appearing not only in 'The Politics' but also in his 'Nicomachean Ethics' where it is mentioned with remarkable consistency. There is no doubt that the human psyche (soul) plays an important role in Aristotle's ethical theory (Flew, 1979). The relationship between psychology and economics, human psyche and ethical theory as well as happiness runs through the history of man and human civilization until the inevitable separation occurred, although psychology emerges as a separate discipline much later than economics due to the emphasis on and man's obsession with the acquisition of wealth as an end (Ingrid & Richard, 1978).

Another issue of considerable importance that provides the link between the two disciplines is the emphasis on the connection between the contents of the inner self in the form of inner motives and human actions and decisions, 'What motivates men to action' is the inevitable question that governs one's thoughts and is the point of departure in understanding social sciences, especially in economics, although the responses to such a seemingly easy task differ throughout the ages in lieu of the differences in philosophical thought and worldview that govern men and their decisions. Greek and Medieval thought conceive motivation as being derived from ultimate happiness, which is the activity of the soul in bringing about virtuous actions (contemplation, as in Aristotelian thought) and understanding God in the Christian faith (as in Medieval Christian philosophy, which was predominantly shaped by St. Augustine and St. Thomas Aquinas who were themselves influenced by Platonian and Aristotelian thought respectively). However, with the advent of the Reformation and the Renaissance, there was a move towards 'naturalization of the soul' (Kantor, 1963) and human actions were attributed to inner motives within the realm of the material world. From Hobbes onwards, there has been a tradition which seeks to discuss human motivation almost entirely in the light of general conceptual considerations about desires, passions, pleasure and pain. Thus, the development in psychology, especially as it emerges into a separate discipline, has had considerable impact on various economic theories especially in microeconomics, which deals with assumptions about the behaviour of individual economic agents in various economic functions. Concepts in economics such as utility, preference and choices are filled with psychological postulates because they relate to the way individuals make decisions.

The factors that motivate man to action or those that influence his behaviour and decisions, although they can be expressed in physical terms as observed, originate from the mental attitudes of men toward the things in questions, and this fact should be used to explain social phenomena, rather than depending entirely on the behaviourist approach to explanation where the conclusions of events are drawn based on

objective facts in the special narrow sense through observations of the physical processes. 'Facts' are constantly shown to be different from 'appearances' (Hayek, 1979).

Partly influenced by discoveries in natural sciences, various schools of psychology emerged which influenced economics and finally led to the emergence of the so-called 'rational economic man', who has been described in economic literature as a man devoid of sympathy and social considerations and who works solely for the purpose of self-interest maximization. In the 19th century, a philosophical movement called positivism arose, basing itself squarely on the Newtonian concept of science and seeking to extend this scientific method to social science and social control (Corsini, 1984). The positivist provided enough support for the justification of behaviorism, a school of psychology founded by John Broadus Watson, who ruled out *introspection* and the *study of consciousness* and proposed a *mechanistic* view of man in which the goals of psychology were the prediction and control of behaviour in humans and animals alike (Corsini, 1984). The most influential view in psychology in the twentieth century, which provides further support for egoistic motives in individual economic decisions, was the psychoanalysis method developed by Sigmund Freud (1856 - 1939). Freud became concerned with the role of unconscious motivation and argued that the unconscious was where the instinctual motives and emotions were contained and drove men to action. The ego had a basic instinct for self-preservation, and Freud stressed that reason could control but never finally dominate our passions. *The purpose of psychoanalysis is to strengthen the ego.*

Surprisingly, despite recent findings in the field of psychology that negates egoism as the only motive that drives men to action and affirms the existence of benevolence and altruistic behaviour in human decisions, economists insist on maintaining the egoistic rationality assumption in economic theories and models, an assumption derived from nineteenth century psychology, which was formulated in the light of historical events (industrial revolution, scientific discoveries and crisis in the Christian faith) which were interrelated during that particular period. However, one of the outstanding works that link ethics with actual behaviour is by A. K. Sen (1987). He provides the framework that bridges economics and ethics. Sen argues that there are two central issues that make it impossible for the separation of ethics and economics; namely the motivational aspect relating to the ethical question of 'How should one live?' and secondly the criterion for social achievement, which is based on ethics. He maintains that economics can be made productive by paying explicit attention to the ethical considerations that shape human behaviour and judgment.

In the early twentieth century, a new discipline in social science emerged known as economic psychology, but the growing interest in the coordination of theoretical and research efforts between economics and psychology is evidenced only in recent years. Nevertheless, this integrated and interdisciplinary approach, needless to say, is a discipline with a mechanistic and materialistic outlook and devoid of the indispensable character which forms the basis of Greek and Medieval thought. This is evident in the definition provided by the standing committee of the European Group of Researchers in Economic Psychology (MacFadyen, 1986). Economic psychology as a discipline thus studies the psychological mechanisms and processes that underlie consumption and other economic behaviour. It deals with preferences, choices, decisions and factors with respect to the satisfaction of needs. Furthermore, it deals with the impact of *external economic phenomena* upon human behaviour and well-being. These studies may relate to different levels of aggregation from the household and the individual consumer to the macro level of whole nations. Furuham and Lewis (1986) define psychological economics simply as 'work, mainly by economists, that employs psychology to improve and expand the discipline of economics'.

The preceding deliberations show the significance of psychology and its inextricable link with economics. The concepts of *unity* and *preference choices* in economics is related to several psychological postulates and thus changes in response to them. Based on the behaviouristic approach to psychology, one's preference is implied from one's choices of economic goods which maximize one's utility or satisfaction (in a sense, happiness). Once the soul is separated from any consideration in achieving happiness, what is left is bodily needs, and the tendency towards maximizing one's own self-interest.

Thus, the need to rephrase the relationship between psychology and economics is in order. In essence, the relationship between the two disciplines is a relationship between the science of the soul (traditional definition), the concept of happiness and material acquisition.

### **The Influence of Psychology in Western Economics: An Appraisal**

In Greek, 'eudaimonia' means 'to be prosperous or well -off' as well as 'to be happy'. In Greek teleology, everything was made for some end and found its satisfaction (or happiness) in fulfilling its function, in realizing its idea or its notion. In essence, happiness is acquired through the fulfillment of function. In Greek and Medieval thought, happiness is achieved through the activity of the soul. Habits and decisions involve a rational assessment of each new situation and a choice made in the light of a conception of what it is men should aim at and what they should regard as constituting happiness. In elaborating views concerning the soul and its relations with happiness and acquisition of wealth, the *soul-body* relation is a fundamental issue.

Before Socrates and Plato, the Greeks had no idea with regard to the immortality of the soul. To them only Gods were immortal because their bodies were also immortal. With Socrates and Plato, the revolutionary idea of the conception of the immortality of the soul emerges in Greek thought. To Socrates, the soul is man's true self and he thus propagates the idea that men should care for their soul in the best manner at all times. Plato, in giving the soul its scientific form, asserts that it is the only thing which could move itself and other things without being itself moved by anything else. Man is a soul using a body. It was *prior to the body* and the *efficient cause* of everything good and bad. Both see the body as the prison-house of the soul and that the soul does not need a body for its existence. This approach to soul-body relations is known as the theory of the soul as substance (Quasem, 1981).

With Aristotle the soul - body relation is in a different form. He considers the body as the instrument of the soul, for matter is only a *potency* necessary for the *realization* of a form (perfection of the soul). It is related to the body as form to matter and can have no life apart from the body. To him, the soul is the cause of the body in three ways (Corsini, 1984).

- (1) It is its efficient cause in that reference to some concept, such as desire, is required to explain *movement*.
- (2) It is the formal cause in that *behaviour* is explained as the exercise of a *capacity* or *tendency*
- (3) It is the final cause in that reference must be made to 'the *reason* for the sake of which movements of the body take place. In *choice*, for instance, means are worked out and adapted to attain an end'.

In *De Anima*, appetite is the primary basis of action, and aided by nutritive sensitive and imaginative actions. To Aristotle appetite is the genus of which desire, passion and wish are species, and this notion forms the basis of the conception of motivation, with intellect taking a dominant role. This is evident in his classification of the soul into rational and irrational; the irrational part is the seat of the appetites and desires while the rational soul exercises control on the desires. We can therefore deduce the following:

- (1) Material acquisition in Greek thought is a means to achieve happiness, and not an end. The emphasis on material satisfaction in the writings of Plato and Socrates is much less and there is a tendency towards neglecting one's material being, as the emphasis is on the development of the soul to achieve happiness. The existence of dualism between the soul's true welfare and all earthly concerns is very obvious in their thought. They believe that a minimum amount of wealth is essential to the good life.
- (2) With Aristotle, although there is such a thing as psychological dualism, ( Quasem, 1981) the existence of the relationship between the body and the soul supports the evidence that, although happiness is attained with the intellect and the highest form is contemplation, the body must also be emphasized in order to assist the soul to achieve perfection.

Thus, in his *Nicomachean Ethics* he mentions that man requires a moderate equipment of external goods for virtuous actions; which must be in themselves pleasant, good and noble. He equates the virtuous activities of the soul with happiness because a man who is good and wise (and happy) bears all the chances of life and makes the best of circumstance. He defines choice (an important concept in economics) not in relation to pleasure and pain (as in the Utilitarian philosophy which influences modern economics) but a means that is closely bound up with virtue. He propagates the *golden mean* with respect to choice, which is relative and determined by rational principle. In terms of actions, this means doing the right thing in the right way to the right person to the right degree (Reese, 1983). In relation to this he defines the *liberal man*, in term of wealth acquisition and spending, as a praise-worthy person.

A liberal man will use riches in the best manner in accordance with the golden mean principle, and thus he is almost the most loved of all virtuous characters. The liberal man lives in accordance with his needs and thus anticipates the *basic-needs approach to development*. Thus, Aristotle represents the height of Greek Thought, with its unity of psyche, or soul and body, as well as its clarification on the concept of wealth and its relation to the soul.

(3) Man is the 'instrument of a Divine reason, but owing to the existence of the body, he is hindered from the pursuit of goodness and truth. Thus, the proper thing to do is to control the desires. Plato sees happiness in harmony between the three parts of the soul (reason, spirit, and appetite). Aristotle stresses the importance of controlling passions and other desires to achieve moral virtue (Hasting, 2003). This approach is in contradiction to Hedonism, especially utilitarian ethics, which has had a considerable influence on the western economic tradition, in the sense that economic decisions in Hedonism are based on the principle of pleasure and pain.

(4) The advent of the middle ages witnessed the birth of the Christian soul. The soul was no longer simply an aspect of the body's function but a separate entity independent of the laws of nature governing the physical body (Corsini, 1984). The nature of psychology is introspection, which together with revelation will lead to the knowledge of God and ultimate happiness. St. Augustine believes that the true man is the soul and the soul is the guardian of the body to bring it towards the order of God. He believes that the soul can become evil if the *body is given too much care*. He defines happiness as 'joy in truth' (Maurer, 1982). His rejection of materialism, however, led to the retardation of science.

St. Thomas Aquinas was more attracted to Aristotle's conception of the soul and emphasizes that human nature requires a body to achieve wholeness (or perfection). To him, man cannot obtain happiness unless his soul is united with the body. With this, he emphasizes what is known as psychosomatic unity. He equates the working of reason with the natural tendency in man, and propagates the supremacy of reason and will over desires, which is compatible with our nature. He includes appetitive among the powers of the soul, which he regards as a cognitive entity. An appetite is a passion and a desire which involves some intention and only with the supremacy of the will in the soul can man achieve morality. The implication of this notion is the rational justification for the satisfaction of human needs. St. Thomas Aquinas and the scholastics' conception of man led to their condemnation of the pursuit of wealth and propagated the idea that economic activities should be in accordance with one's status in society. Due to the revival of trade and industry in the 12th and 13th centuries, the scholastics formulated rules of conduct in order to inhibit the growth of commercial practices that were said to contradict Christian doctrines. Like Aristotle, St. Thomas Aquinas, condemned the practice of usury, an activity which will lead to the state of unhappiness of the soul.

The advent of the Renaissance created a tremendous transformation and change in the outlook of man, especially in connection with the soul body relation, man's conception of the world and his place in it, economic inquiry and the acquisition of wealth. During this period, the world witnessed the changes in intellectual or philosophic outlook that laid the foundations for the development of modern science. Secularization occurred in every sphere of human life, which led to the emergence of economics as a separate discipline as a result of factors, which have been mentioned earlier. One consequence of the Renaissance was the humanistic attitude, which stresses man, his nature and needs, as man became significant. As a result there was a change in the postulates of psychology from an exclusive preoccupation with soul to the study of *besouled* man, and a trend towards the appreciation of feelings and passions. The capitalist market economy, which was rapidly being extended into the most significant areas of production and commerce, demanded self-seeking and acquisitive behaviour to

function successfully. In this context new theories about human behaviour began to emerge. Writers began to assert that selfish and egoistic motives were the primary if not the only ones that moved men to action (Hunt, 1979).

Hobbes regarded the idea of the soul as contradictory. William Wundt, one of the founders of experimental psychology, viewed the soul as a process rather than a substance and this became the basis for the emergence of psychology as a separate discipline. Happiness is conceived, not in relation to the soul but to pleasure and pain, in accordance with the aim of gratification of desires, which are regarded or defined as the 'inner motives' of man. Pleasure, in its psychological sense, is taken to be a pleasurable feeling towards an object but not in the sense the object itself is pleasant. Happiness, in this sense, is not attained throughout one's life but limited with varying degrees depending upon the satisfaction of one's desires for material goods in the worldly life. This will lead to a relative conception of happiness due to the subjective nature of evaluating objects or goods and one's aim in life. A person may judge his own inner motives strictly from his own view point on a purely individualistic basis, and act in accordance with the satisfaction of his desires. This transformation in European society during and after the Renaissance resulted in the birth of the *economic man*, and the fundamental element in his personality, which has been assumed to be universal, is self interest.

Jeremy Bentham in his Introduction to the Principle of Morals and Legislation states that: Nature has placed mankind under the governance of two sovereign masters; *pain* and *pleasure*. It is for them alone to point out what we ought to do, as well as to determine what we shall do... They govern us in all we do, in all we say, in all we think.... (Hunt, 1979) Similarly, William Jevons stated in the Theory of Political Economy: 'Pleasure and pain are undoubtedly the ultimate objects of the Calculus of Economics, to maximize pleasure, is the problem of Economics' (Schotter, 1985). The most influential voice, however, comes from Edgeworth, when he asserts in his Mathematical Psychics; that 'the principles of Economics is that every agent is actuated only by self-interest' (Sen, 1982). In the utilitarian sense, happiness can be achieved with the principle of 'greatest happiness to the greatest number', which means the 'greatest sum of pleasures' from the societal point of view. It is this psychological postulate applied at the individual level and societal level, separated from the activity of the soul and its ultimate happiness, which finally led to the state of unhappiness and misery in man.

One of the most important impacts of the Renaissance on psychology was the emergence of materialism which (1) ceased sensitivity to the biological and physiological nature of man, which encouraged the study of the readings and condition of mental processes. (2) reduced the importance of psychic and transcendental factors in psychological factors. (3) considered instinct and innate sources of behaviour to be based on biological characteristics. (4) included feelings among the types of mentality (Kantor, 1963).

The impact of the Renaissance on economics begins with the emergence of Mercantilism, in which statecraft and economic policy became a primary instrument to promote the simultaneous development and growth of the economy and the state (Rima, 1978). However, a reaction to mercantilist views began to appear in the second half of the 17<sup>th</sup> century with concerns for increasing liberty and the belief that greater freedom from government restrictions would be advantageous to themselves as well as to the economy. The Physiocrats propound and elucidate a philosophy that it is both unnecessary and undesirable for governments to regulate, and conformity to the laws of the natural order will insure maximum happiness, whereas infringement of the fixed laws of nature will call forth correspondingly disastrous consequences. Using the process of abstraction they were the first to seek out the existence of general laws according to which economic phenomena behave and they laid the groundwork for the systematic study of social phenomena on an empirical level. This attitude reflected the gradually evolving idea that the economic system is a self-generating autonomous organism which does not require management from above, but functions best when allowed to regulate itself. A hedonistic psychology which regarded material self-interest as being not only proper but essential to prosperity, as opposed to the medieval view of the virtue of self-denial, was also gaining acceptance (Rima, 1978). Economic progress thrives under the stimulus of self-interest and higher levels of personal consumption. Clearly, in the history of production, man must pass beyond the stage of bare subsistence before a surplus of any kind is a possibility. Later 17<sup>th</sup> and early 18<sup>th</sup> century writers gave ideological expression to these beliefs in the doctrine of *laissez-faire* and sought to discover the laws which govern the functioning of self-

regulating economic systems. Adam Smith's view is that the concern of moral philosophy is human happiness and well-being and the pursuit of riches as merely one aspect of every individual's desire to better himself. Self-interest is thus seen as manifesting itself in every aspect of man's behaviour and activity. In the economic sphere, it prompts the division of labor and the accumulation of capital, thus enhancing productivity (Rima, 1978).

Newton's system in deriving general laws that govern the motions of planets had a profound influence on the writings of Adam Smith. He was concerned with attempting to arrive at general laws of human behavior in his study of social phenomena. Humans differ as individuals, and societies differ in their cultures, but it is still possible to state propositions about behavior that are universally valid if human beings are similar to one another in their basic natures. Impressed with the development in the natural sciences, Adam Smith formulated the method of economic science based on empirical evidence and theoretical analysis. Similar to Newton's principle of gravitational attraction, Adam Smith attempted to arrive at the principles that govern human nature in association (attraction) with others. In his *Moral Sentiments*, man is characterized as rational, sympathetic and benevolent towards others, while in the *Wealth of Nations*, he is considered to be rationally motivated by self interest. Although both conceptions appear contradictory, some writers have made reconciliatory remarks that, in the efforts to better his conditions, man does consider the welfare of others. This view is accepted by all Scottish philosophers including Hume. In the sense it is the reconciliation between egoism and benevolence which Hobbes had failed to recognize when he stated that individuals in a society are motivated by self interest even when submitting to a social order. He extended the idea of general laws governing natural phenomena to economic processes by stating that individuals' attempts to satisfy their own self-interest eventually bring about an unintentional natural harmonious order in the economic system, due to the existence of 'general laws' which he called 'the invisible hand' (Myer, 1983).

Given the presence of self-interest and sympathy in Adam Smith's writings, it is an irony that the literature on the development of economic thought attempts to show that, as a consequence of the Reformation and Renaissance, Adam Smith was credited with the emergence of the self-interest assumption in modern economic theories. However, assiduous research on the economic ideas of Adam Smith indicates that he accepted the existence of altruism in man's behaviour when he wrote 'How selfish man may be supposed, there are evidently some principles in his nature which interest in the fortune of others and render their happiness necessary to him though he derives nothing from it except the pleasure of seeing it' (Coase, 1984). Each individual, independently seeking to maximize what he considers to be his own selfish interest, will nevertheless contribute to the social welfare. Philosophically speaking, most post-Smithian economists were of Utilitarian persuasion. But their economic analysis was more specifically predicated on the Smithian conception of the psychology of individual behaviour, which emphasizes the natural inclination of people to maximize their personal gains, including those which come to them in monetary form, if they are free to do so (Rima, 1978). Nevertheless, John Stuart Mill was highly critical of the view that human behaviour was entirely governed self-interest, as Bentham implied, and even ventured to suggest that the reason why Bentham attached little importance to sympathy and benevolence as influencing conduct was because he himself was devoid of these characteristics (Rima, 1978).

Theoretical economists after John Stuart Mill were more concerned with the formulation of economic laws than with policy prescriptions. They sometimes began with assumptions about the institutional setting and human behaviour which did not always coincide with observable reality. Though their abstractions were intended to facilitate the establishment of propositions which represented only a first approximation of the truth, and which therefore required amendment and qualification, there was sometimes a tendency to overlook the tentative nature of their conclusions. The ideal was sometimes equated with reality; and as a result the body of economics which developed after Mill occasionally appears to have an apologetic bias in favor of the system of private capitalism (Rima, 1978). While the Physiocrats conceived of political economy as the science which sought the laws governing the distribution of wealth, the Classicists believed that their laws were a scientifically arrived at and universally applicable body of principles which depicted the operation of the economic system regardless of time, place or existing institutions. Institutions were regarded as being largely an expression of simple and universal laws of human behaviour and therefore irrelevant to the functioning of specific societies. This is consistent with



the hedonistic psychology on which Jeremy Bentham constructed Utilitarianism, even though the laws of classical economics do not themselves rest on utilitarian foundations (Rima 1978).

Alfred Marshall and the neoclassical tradition seek to study the economic aspects of human behaviour in order to scientifically derive laws and generalizations governing the functioning of the economic system. Marshall recognizes the complexity of the economic system he is studying and the motives of human behaviour so diverse that it is necessary to devise techniques for their systematic study. He emphasizes the psychological factors affecting behaviour in the economic system which he says are measurable in terms of money.. Among the features of the neoclassical tradition which are of interest in this study is the recognition that the psychological factors equating optimizing behaviour with the hedonistic pleasure maximizing, pain minimizing choices of Utilitarian ethics. Under Marshall's influence the doctrine of economic harmony, as being inherent in the functioning of a system guided by self-interest, gained new adherents (Rima, 1978).

The dominance of neoclassical tradition for at least the first three decades of the 20<sup>th</sup> century, did not go unchallenged. It came from the German School and the Institutionalists. One of the issues of dissent against the neoclassical tradition was directed towards the psychological and philosophical premises from which economic laws are derived and the use of the deductive method (Rima, 1978). The Veblenian challenge from the German historical school came in the form of questioning the assumption that man has the inherent ability to calculate the economic gains and losses that result from his choices among the alternatives available to him. Human behaviour is, in Veblen's, view dictated by the cultural setting of which economic activity is a part and within which it takes place. In other words, Veblen rejects the concept and modus operandi of 'economic man', which he says does not approximate the man of the real world (Rima, 1978). Like Veblen, John Maurice Clark is concerned with emphasizing the shortcomings of the psychology on which neoclassical theory is founded. Clark maintains that the human mind is subject to myriad outside influences, particularly from advertising. Behaviour to Clark is not entirely the result of continuous calculation but also habit and routine.

The German historical school directed its criticism against classicism by arguing that economic laws, if they can be discovered at all, must necessarily be relative to time and place. Because economic laws operate within the framework of constantly changing environments, they argued that it was necessary to replace the classical method of deduction by induction in order to discover the nature of these environments. Induction would, they felt, also shed new light on the motives of human conduct, which, in their view, the classicists interpreted all too simply as being only the product of self-interest.

However several economists, such as Frank Knight and John Hicks from the philosophical movement known as Logical Positivism, made an attempt to provide counterarguments to the criticisms. Frank Knight defended neoclassicism. He agreed with Veblen that the determinants of man's behaviour are multifaceted but insists that it is sufficient to incorporate only those aspects which are relevant to explain economic behaviour. The modern welfare theorists on the other hand, were concerned with returning to the central thesis of *The Wealth of Nations* namely that the divergent interests of consumers and producers as well as those who supply and those who hire factors of production are reconciled in a competitive market. The choices that each participant makes, guided by the equimarginal principle, will insure that optimum conditions will be satisfied though each participant acts in his own self-interest (Rima, 1978).

Price theorists such as Chamberlin and Robinson continued to consider the basic premise that businessmen are concerned first and foremost with the maximization of profit which they said depends very much on the structure of the market. Numerous writers such as Herbert Simon and Joan Robinson have, in recent years, challenged the traditional assumption of profit maximization on various grounds. Herbert Simon has suggested that firms 'satisfice' rather than maximize profits. The emergence of the principles of game theory demonstrates that rationality in an oligopoly position does not necessarily require the maximization of net profits. A major figure and an outstanding economist in the 20<sup>th</sup> century, John Kenneth Galbraith Galbraith was widely known for his trenchant opposition to mainstream neoclassical economics. Nearly all of the characteristics of the institutionalist school apply to his many

works. His evolutionary approach explores changing conditions and examines the need to change our ideas to fit new situations. He says that the reason why obsolete neoclassical ideas have been able to survive is because the 'neoclassical system owes much to tradition - it is not implausible as a description of a society that once existed...'

Given the above deliberations, it is clear that the rationality assumption of the neoclassical economists, that man acts merely in accordance with his self-interest, is not as relevant as claimed by many modern economists and it has its own adversaries even among western economists. In other words the true nature of the rational man of economics is not a man devoid of any feeling and emotion or merely concerned with the pursuit of his own well being, not sensitive to the problems of his fellow beings and, being materialistic as he is, merely focussing his actions and decisions on maximizing his utility function or profits.

This fact has led some recent economists to undertake the study of the psychological factors affecting human decisions which influence their choices of consumption bundles, especially the nonegoistic motives which emphasize altruistic and cooperative forms of behaviour, as human decisions are also influenced by values, culture and traditions.

Even in contemporary business practice there are diverse theories of motivation which have considerable influence on the decisions that individuals make:

- (1) Maslow's Hierarchy of needs, which states that an individual is motivated by the tendency to achieve a hierarchy of needs,
- (2) Alderfer's ERG Theory of needs which is a slight variation of Maslow's hierarchy.
- (3) McGregor's Theory X and Y which presents two opposing views concerning people and their attitudes toward work, and helps to explain the controversy between the *traditionalists* and *behaviorists*
- (4) Argyris's Mature Man which emphasizes the natural tendency of man towards maturation and achieving *good mental health*.
- (5) Herzberg's Two-factor motivation Theory which constitutes the *hygiene factor* and *job satisfaction* factor as sources of motivation.
- (6) Rensis Likert and Robert Blake's proposed specific leadership models, to manage people based on the above mentioned theories.

Although there are some similarities to the Islamic form of motivation, especially concerning 'needs' as an important source, nevertheless the concept of happiness in Islam influences the concept of needs and pulls it far apart from the concept of needs from the Western perspective (Nusair, 1983).

In economic jargon, a thing is called a 'good' (or an economic good) based on the individual's psychological feeling of pleasure without any moral basis to distinguish whether the economic good is good or bad in the true sense, proper or improper, as long as the thing can bring him to a state of satisfaction at that particular moment in time.

Based on the preceding elaborations, there is sufficient evidence for us to conclude that there are several flaws in Western social science and economics, particularly as a consequence of the influence of the methodology of natural sciences, which emphasizes reason, observation and experimentation as the sources of knowledge and the only acceptable method of scientific inquiry. However, despite these flaws, it remains the dominant body of knowledge in contemporary conventional western economics and continues to be imparted to each new generation of students, with the false presumption that it is universally accepted and valid across the globe. The consequences of such a blind acceptance are too great to be measured.

It is this model of human behaviour, based on the assumption of egoistic rationality which the economists are still committed to, which lies at the heart of neoclassical economics. However, this assumption, which attempts to universally characterize human psychology, can be criticized on a number of grounds, which has gradually led to other forms of rationality explaining human behaviour. Firstly, it is too demanding in the sense that perfect rationality is assumed and individuals as producers or consumers are required to perceive, evaluate, and calculate with absolute precision. Secondly, it is held to be too restrictive, in the sense that it limits attention to narrow self-interest as the sole motivator of an individual's actions. It does not represent the behaviour of an actual human being. The self-interest assumption underlying human psychological behaviour creates an abstract shadowy being who is a self-seeking individualist. Some economists admit that this is not a realistic model of human behaviour. There is no way to tell whether the predicted behaviour of a consumer or a producer is the actual behaviour, as an analysis will only tell us how rational the individuals are. This psychological assumption of human behaviour does not even consider diversity in cultural and religious orientations, which do influence human motives.

Professor Wiarda (1981) in his article 'The Ethnocentrism of the Social Science: Implications for Research and Policy' asserts very strongly that 'the vast bulk of our social science findings, models, and literature, which purport to be universal, are in fact biased, ethnocentric, and not universal at all. They are based on the narrow and rather particular experiences of Western Europe (actually a much smaller nucleus of countries in central and northwest Europe) and the United States, and they may have little or no relevance to the rest of the world.'

This brings us back to the issue of the objectivity of the social scientist in conducting his research in his own environment, and the biasness that flows into his findings. The relation of the social to the natural sciences philosophically has been a matter of continuing controversy. Peter Winch, for example, in his *The Idea of a Social Science* (1958) argues that the concepts appropriate to the analysis of social phenomena are demonstrably incompatible with those used in natural science, and F.A Hayek, in his *The Counter-Revolution of Science* (1955) complains of the great harm that has been done by modeling the study of social phenomena after the natural sciences (Gordon, 1991).

It would be foolish to claim that scientists are totally detached from their particular cultural environments. Galileo was, no doubt, a cultural deviant in some ways but, in most, he was a Renaissance Italian and shared a common culture even with the officers of the Holy Inquisition. Some historians of science have laid great stress upon the cultural conditioning of the scientist and the connection of his theories with the socioeconomic environment. Numerous scholars, for example, have expressed the view that the Darwinian theory of natural selection reflects the competitive capitalism of the nineteenth-century English economy.

Others have argued that while the scientist himself may be objective, the acceptance of his theories depends upon their serviceability to powerful political or economic interests or ideologies (Gordon, 1991).

Understanding the philosophical and cultural basis of education is relevant in the context of attempting to relate the subjectivity of the social scientists and economists with their theories and models. Since a liberal arts education is essentially Western education, it means that any set of concepts, ethics, norms and experiences which are integrated into it have their philosophical basis in Greco-Roman and Jewish-Christian traditions and European history. Due to the influences of natural sciences and the cultural context in which the social scientists are conducting their research, concepts such as rationality, society, progress, success, happiness, religion, man, wealth, work, development, justice and others which they have identified and adopted are defined based on these influences and traditions. These traditions influenced and shaped the thoughts of the Rationalists such as Descartes, Spinoza and Leibniz; the Empiricists such as Francis Bacon, John Locke and Hume, economists such as Adam Smith and John Stuart Mill; psychologists such as Sigmund Freud; sociologists such as Durkheim, Mark and Comte and biologists such as Darwin and others who then propounded their social theories and concept of man in their writings.

The salient features of their social thought and economic ideas are as follows:

1. Economic ideas are molded according to the intellectual, socio-political and economic milieu of the time.
2. Most of these economic thinkers, philosophers and scholars had limited knowledge of the history, cultural traditions and religious beliefs of societies beyond European and American borders
3. Much of the empirical evidence they acquired was confined to the location and milieu in which they were conducting their work, and their universal applications are doubted.
4. These social scientists were impressed with the method of scientific inquiry of the natural sciences and in the preciseness of the scientific theories and discoveries of Copernicus, Kepler, Galileo and Newton and, in their enthusiasm, imitated the scientific method without considering the distinctiveness of the subject matter for both sciences.

In studying the development of social science and economics the rise of modern science was of crucial importance. When the social sciences began to develop, they were inspired by the achievements of the natural sciences and attempted to apply to human sociality the new conceptions that the natural sciences had been successfully using in the investigation of natural phenomena (Gordon, 1991). It also led to the emergence of modern philosophy and a modern outlook on the world, man and society, a new *weltanschauung*. The approach taken by a social scientist and an economist, then, becomes identical to the approach of a physicist, defining a social fact as an object, separating it from the environment in the process of studying its physical qualities devoid of any external influences. If this method of inquiry is applied to economics, the preciseness and validity of the theories and models will be questioned due to the existence of interdependent relations between man, the actions of others and the environment. What we will have is a caricature of an 'object' with no feelings and emotions and whose behavior is not affected by the actions of other human beings and the changes in culture or environment. A body of knowledge having these models and theories, which are constructed based on these unrealistic assumptions about man, are definitely unreliable as they are unable to make realistic predictions. Social science literature is laden with these caricatures - economic man, political animal, social animal, psychological man and humanistic man - all are individually too incomplete to represent a true model of a human being and his psychological behaviour.

Economics, as a social science, is not an exception and the psychological behaviour of economic man as assumed in modern economic textbooks seems separated from other facets of human existence and therefore requires a revisit and revision. Such new perspectives will require a redefinition of basic economic theories and a reformulation of economic models based on a different psychological perspective or we will be imparting knowledge to students of economics which are no longer relevant to 21<sup>st</sup> century society and not applicable in those societies which are based on different religious and cultural values. In the case of an Islamic society, a redefinition and reformulation of these concepts and theories, which are pervasive in modern economic textbooks, is indubitably a religious obligation to Muslim economists, especially those who are currently teaching economics to Muslim students and using economic textbooks which explicate theories and models built on the psychological behaviour of self-interest motives and other assumptions which may be irrelevant to the modern world and contrary to the Islamic faith.

### **Psychology And Economics : An Islamic Synthesis**

This paper finds it a necessity, as stated above, to study the various approaches to psychology adopted by thinkers from the Greek period until after the Renaissance which were influenced by philosophy and science, and examine them critically in the light of the acknowledgement and acceptance of Revelation and the Prophetic Tradition as the source of true knowledge, in the 'Quranic System' (Al-Attas, 1989, 1990, 1992), which is not a source of knowledge or method for modern science and philosophy.

A clear exposition of the interesting nature of the synthesis is carried out through a systematic and unified analysis of the term 'din'. The primary significations of the term not only provide a conclusive explanation of the comprehensive character of Islam, but also clarify the existence of a concrete interrelationship between its components which gives rise to the interdisciplinary nature of the various branches of knowledge. It is as though God had placed everything into one complete whole, united and

existing within the existence of a single source never again to be separated, which is extended to the relationship of the components of the macro cosmos with God as the source of it. It shows unity, perfection and order.

From the term 'din', the linkage between psychology and economics becomes more obvious. 'Dana', a verb derived from 'din' conveys various meanings which are applicable only in a cosmopolis where economic activities are indispensable for its existence (Al-Attas, 1989). From the same term 'dana', which means 'being indebted', a definition of psychology is derived. Man is indebted to God for bringing him into existence, and this is obvious from the acknowledgement of his soul (Al-Attas, 1992). The repayment of his debt means to fulfil the function in accordance with the purpose of his existence and creation, a natural inclination, which is manifested in the form of his consciousness and willingness to serve his Creator.

Man is a 'rational animal' (Al-Attas, 1992) who is both soul and body, who is at once physical being and spirit. 'Man of Islam' is a microcosmic representation of the macrocosms (Al-Attas, 1989, 1990) in the sense, the rational soul (al-nafs al-natiqah) controls the animal soul (al-nafs al-hayawaniyyah) and manifests it externally by the action of the body, obeying God's law in all spheres of life. The concept of justice, then, implies that 'the real man can only in fact be his rational soul' (Al-Attas, 1989) as a fulfillment of his natural obligation with reference to the contract which his soul has established with God prior to his existence. The soul-body relation as specified here provides a firm psychological foundation for the economic activities of 'man of Islam' described 'as a city dweller, a cosmopolitan, living a civilized life according to clearly defined foundations of social order and codes of conduct is he to whom obedience to Divine Law, endeavour towards realizing true justice and striving after right knowledge are cardinal virtues' (Al-Attas, 1992). At this juncture, it is possible to define *Islamic psychology* as the 'intention of the soul, to submit to Allah and to worship Him in order to display his duties imposed by the Creator, the way of life to be displayed in full submission through the religion of Islam'. It is the science of the soul as described in the Qur'an (Al-Attas, 1992) and it is the 'rational soul' that is required to play a dominant role towards the attainment of this aim and in the process controls the animal soul. The development of the rational soul towards the attainment of its highest stage of perfection, (al - nafs al-mutmainnah) or the tranquil soul, and concomitantly fulfilling man's purpose of creation and existence, is therefore indispensable and indeed a necessary approach to ensure that God's law governing economic activities are manifested outwardly in the life of man as a manifestation of obedience to God, and to ensure justice (adl) with regard to the requirements of the material, or physical part of the body (placing it in its right and proper place) (Al-Attas, 1992) as a means to achieve the final purpose in life. In the Hedonistic sense, the animal soul which is motivated by the gratification of desire to maximize pleasure manifests itself outwardly in the form of accumulation of wealth based on self-interest, at the expense of public interest. This is peculiar to the nature of the animal soul which is endowed with motive and perceptive powers. As the arouser of action, it directs movement by what it considers beneficial or harmful to it. As an actuator, it initiates and communicates movement, starting the operation of the nerves, muscles, tendons and ligaments towards fulfilling its purpose in accordance with what it desires or opposes (Al-Attas, 1990).

The man of Islam will not allow the animal soul, which gives rise to passions and desires, to have control over the rational soul or body and cause fatal economic activities to emerge in a society. To function effectively as an individual and collectively as a community, to serve God, the rational soul has to be developed, in a sense that will ensure the realization of this goal.

The consequence of this realization is the attainment of happiness by man, and this quest for happiness is the aim of all men, only what constitutes it and the means to achieve it differ. Happiness, 'refers not to the physical entity in man, not to the animal soul and body of man nor is it a state of mind', but a condition known as 'adl' or justice where peace, security and tranquility of the heart is acquired. The description of the 'man of Islam', as mentioned earlier, provides us with a comprehensive outlook on the concept of happiness.

Imam al - Ghazali relates happiness with the conditions of soul and it is the happiness of the hereafter, al-sa'adah al-ukhrawiyya, which should be the aim of man. He regards worldly goods as a means to this end but they should not be used more than is necessary. He accepts necessities in the form of food, clothing and shelter as requirements for the body but condemns pleasure as the aim of human life. Due

to this he regards spiritual happiness as being superior to physical happiness. He attacks views that consider any form of worldly thing as a goal of life, such as those of the sensualists who consider happiness in the gratification of desires, or those that consider happiness in the accumulation of wealth, or respect, influence, and fame. Imam al-Ghazali emphasizes four factors as a means of achieving the ultimate aim in human life. 'al-sa'adah al-ukhrawiyya'

1. al-fada'il al-nafsiyya.
2. al-fada'il al-jismiyya
3. al-fada'il al-kharijiyya
4. al-fadail al-taufiqiyya

Man is the focus in Al-Ghazali's concept of happiness. The satisfaction of his internal and external needs, material and spiritual needs is the main drive and requirement towards achieving the state of happiness. As for happiness being a condition in the soul Imam al-Ghazali mentions that it is the state where the faculty of justice in the soul, maintains equilibrium between the faculties of knowledge, anger and desire. He rejects the view that happiness can be attained by uprooting desire and anger which according to him is neither necessary nor possible. The soul will be in a continuous state of happiness if the means is preserved in all affairs and desire yields to reason and the Shari'a.

The relation between the needs of the body and spiritual happiness can be rationalized through the Nutritive Faculty of the soul. The Nutritive Faculty is for the service of the body because the existence and well-being of the body helps reason in its function (Abdul Quasem, 1977). The importance of material requirements to the body is deduced from the definition of knowledge in the epistemological sense as the arrival of the soul of the meaning of a thing or at the meaning of a thing (Wali-ur Rahman, 1937). The meaning of a thing is first perceived by the external senses of the particulars in the external world, and the inadequacy of the bodily material requirements will naturally affect the perception and retention by the internal senses and strength of the intellect and eventually inhibit the development of the soul towards a higher stage.

The Arabic term for happiness is Sa'adah, derived from the word Saida which means the feeling of satisfaction and enjoyment (Al-Attas, 1989). Despite the fact that otherworldly happiness (al-Sa'adat al-ukhrawiyya) is better than worldly happiness (26:89, 93:4, 43: 35-35) because the pleasure of this world is limited to a specific period of time, the Qur'an insists that a man who inhabits the world should seek worldly as well as otherworldly happiness. This is evident in many verses of the Quran, such as in the prayers of the prophets (Moses, 5 : 156, Ibrahim 2, 126), Qur'anic recognition of basic needs and comforts as gifts of God to man (16 : 80-81), the character who seeks worldly happiness and the evil consequences (2 : 200), the model of a character who seeks both worldly and otherworldly happiness (2 : 201) .

There are other verses that request man to seek his own livelihood in this worldly life, such as whatsoever is underneath the earth is for man (2 : 29) , to enjoy the sustenance of God (67 : 15), permissibility of trading (2 : 275) agriculture (13 : 4) and industry (16 ; 80-81).

Worldly happiness not only describes the needs and comforts that have material implications but they should assist man to attain spiritual happiness in the sense, the soul is able to attain its spiritual perfection as specified in the covenant that it has made with God. God condemns those who engage themselves in the pursuit of worldly gains and do not fulfill their covenant with God in accordance with their purpose for existence (14 : 3).

The tradition also conveys the same message with reference to the pursuit of worldly goods, and the status of the soul, 'There is nothing wrong with wealth in the hands of the fearful'

In another hadith, the Holy Prophet says 'Poverty leads to Kufr'. Although there are various interpretations to this hadith, nevertheless, an insufficiency in a man's basic material needs cannot be excluded from the meaning of poverty in the context of this hadith. This is also evident in the concept of Dharuriyyah which emphasizes the fulfillment of the five basic elements of human life - faith (al-din) life (al-nafs), intellect (al-'aqli'), property (al-mal) and posterity (al-nasl) . If man in modern economics is driven by self-interest, then man in Islamic economics or Homo Islamicus is not only driven by the

pursuit of his self interest but also, as a social being, his motives for action also includes his concern for the welfare of his fellow beings and public interest, as outlined by Islamic Law, and his understanding of happiness not only in the context of this world but also the hereafter.

In essence we have outlined a general framework that primarily provides a psychological base conducive to the understanding of the nature of the discipline of Islamic Economics with reference to the economic behaviour of man that demands the formulation of concepts, models and policies from a different framework. Due to the different form of motivation and goal in life that influences and shapes the conduct of the 'man of Islam' in his economic sphere of life, where his quest for happiness is in a sense *two-dimensional* consisting of worldly and otherworldly happiness rather than a consequence of worldly pleasure, the various concepts that provide the structure of modern economics, which are based on a single dimension theory of motivation in pursuit of self-interest maximization and gratification of desires, such as utility (based on mono utility approach), rationality, profit maximization, ceteris paribus, concept of needs, the goals of the Islamic Economy, the functions of the market and the whole methodological and institutional framework, have to be reviewed in the light of a different psychological basis as expounded earlier.

The approach to development and developmental policies should be multidimensional encompassing the spiritual, material and physical domains and not restricted solely to material inclinations so as to ensure that the happiness of the individual and the community (collection of individuals) as defined in the Quran and the Tradition can be attained through the creation of an environment and provision of basic needs conducive for man to perform his role in accordance with the purpose of his existence and creation.

The term 'progress' reflects a definite direction that is aligned to a final purpose that is meant to be achieved in life. Change, development and progress, in the Islamic view is the return to the genuine Islam enunciated and practiced by the Holy Prophet (may God bless and give him Peace !) and his noble companions and their followers (blessings and peace be upon them all) and the faith and practice of genuine Muslims after them, and these concepts also refer to the gradual improvement of the self and its return to its original nature and religion (Islam) (Al-Mu'jam, 1989).

It is appropriate, in fact, desirable to see stages of development (Al-Attas, 1992) and the effectiveness of developmental policies with reference not only to material enhancement as a measurement of improvement in social welfare but also in terms of the stages of development of the soul; from the lowest stage al-nafs al-ammarah bi-l-su to al-nafs al-lawwamah and finally to the highest stage al-nafs al-mutma'innah which will place man at a level compatible with the purpose of his existence (Nyang, 1976). Thus, Islamic economics and development put man and the psychological factors that influence his actions and decisions at the centre of the entire process and activity. Finally, it is fervently hoped that the attempt made in this paper to synthesize and lay out an extricable link between psychology and economics will lead towards an interdisciplinary and multidisciplinary approach to Islamic Economics as part of our mission as economists and social scientists to critically evaluate the current body of knowledge and provide realistic theories, concepts and models.

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