UNIT-5

The Islamic Economic System

Learning Outcomes

By the end of this unit the learner will be able to:

- ✓ Define Islamic Shari'a and Its Objectives
- ✓ Explore the Various Features of Islamic Economic System
- ✓ Recognize the Difference between moderation and State involvement

Unit 5

The Islamic Economic System

Introduction

Islamic economic principles can become a basis for promoting a balance between the social and economic aspects of human society, the self and social interests, and between the individual, family, society and the State. At the global level, it could be helpful in eliminating sources of instability, thus making the world a happier place with harmony among followers of various religions. Although the aspects directly related to the subject of this course pertain to banking and finance, it is worthwhile to discuss the overall framework of Islamic economics within which the Islamic financial system is supposed to work. Accordingly, this unit will discuss the fundamentals of the Islamic economic worldview having a direct or indirect impact upon the business of Islamic financial institutions and the markets.

Islamic Shari'a and Its Objectives

Before we discuss economics and economic aspects of human beings in the light of Islamic Shari'a we should explain what Islamic Shari'ais and what its objectives (Maq¯asid) are. This is because all business and financial contracts in the framework of Islamic finance have to conform to the Shari'a rules with the objective of helping to achieve Maq¯asid al Shari'a. Shari'a refers to a code of law or divine injunctions that regulate the conduct of human beings in their individual and collective lives. In addition to some general rules there are some specific branches of these injunctions which are: Aq¯aid, or matters of belief and worship; Akhl¯aq, or matters for disciplining one's self; Ahkam, or socio-economic and legal systems; Fr¯aidh, or obligations; and Naw¯ahi, or prohibitions. Islamic economics directly or indirectly deals with all these disciplines.

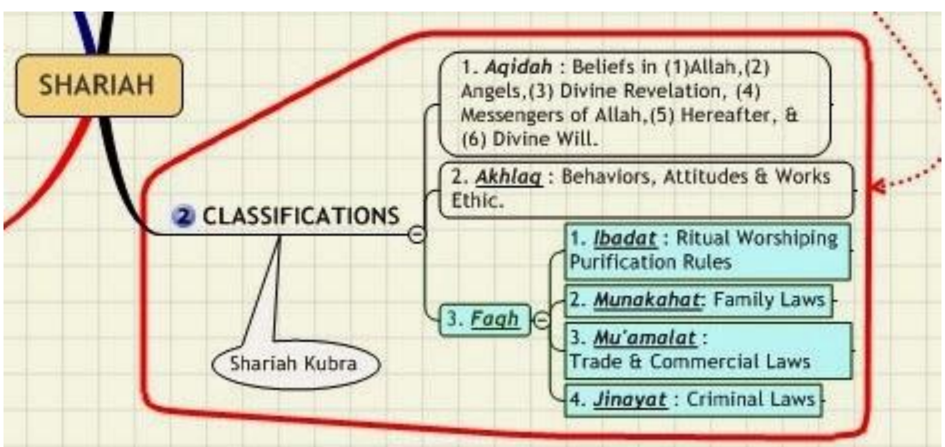


Fig: 5.1

Sources of Shari'a Tenets

The primary source of the divine law is the revelation – the Holy Qur'¯an and Sunnah of the holy Prophet (PBUH) (Muslims believe in terms of Qur'¯anic injunctions that an established Sunnah of the prophet (PBUH) is based on the revelation). Accepting the revelation as the source of tenets and information requires complete submission to Shari'arules. According to Islamic belief, the Qur'¯an is the last revealed book from the Almighty, free from any tampering until the Hereafter (Qur'¯an; 15: 9); obedience to the injunctions contained in it is considered necessary by all Muslims, at least conceptually. The Sunnah, which consists of the sayings of and the actions done and/or approved by the holy Prophet (pbuh), is an equally important source of information in Islamic law. The importance of sticking to the Sunnah is obvious from the following verse of the Holy Qur'¯an: Allah says, "Indeed you have in the Messenger of Allah an excellent example for the one who hopes in Allah and looks to the Last Day" (33: 21). The Exalted also says: "So if you obey him (i.e. Muhammad, pbuh), only then you will be guided" (24: 54). All Muslims believe that obedience to the orders of the holy Prophet (PBUH) is necessary for being a Muslim.

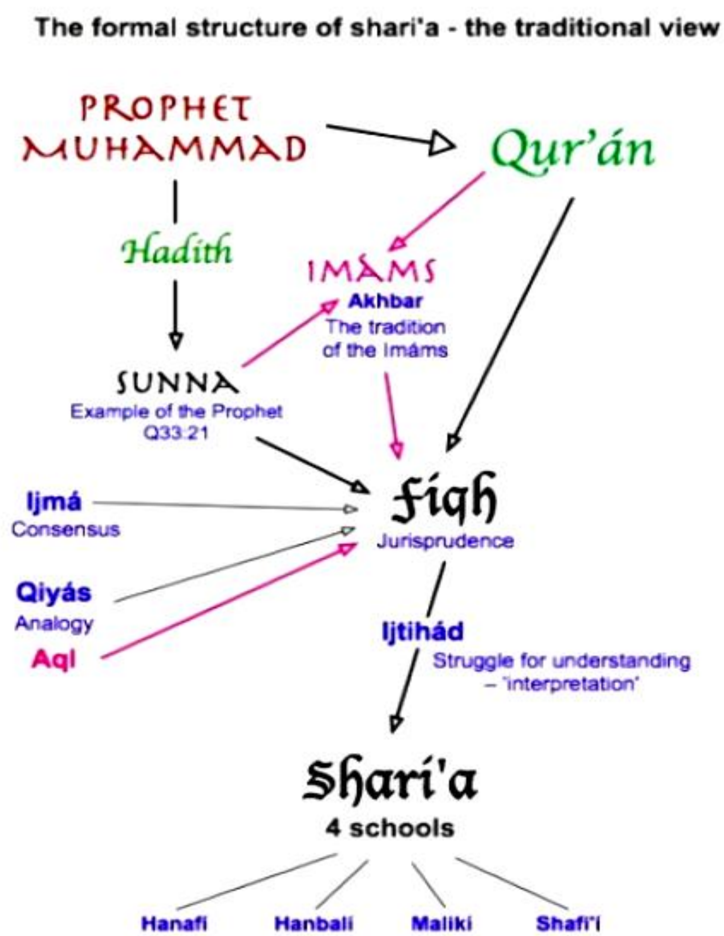


Fig: 5.2

The other sources of Shari’atenets are Ijma‘a (consensus) and Qiy¯as (analogy), which are based on Ijtihad. Ijtihad, the mental effort of scholars having juristic expertise to find solutions to emerging problems and issues, and Qiy¯as, or finding solutions through analogy in the light of the text of the Qur’¯an and Sunnah, are the secondary sources for derivation of rules and regulation for any upcoming events or issues. Ijma‘a of the Companions of the holy Prophet(PBUH) is considered by the overwhelming majority of Muslims an important source for the derivation of laws subsequently.

Shari’arules can be divided into Dos (orders to undertake any act) and Don’ts (prohibition from some acts), which can further be divided into the rituals (matters of worship) that are considered as rights of Allah (SWT) and the matters for disciplining human life that constitute the rights of human beings. While the former acts (rituals or matters relating to belief and worship in the form of Fr¯aidh or obligations) have to be accomplished strictly according to the Shari’atenets, the latter matters that pertain to socio-economic rights and obligations are governed by the rule of “General Permissibility” (Ib¯ahatul Asliyah), which means that all acts and things which have not been expressly prohibited by the original sources of Shari’aare permissible. Further, it is a cardinal principle of Islam that everyone is accountable for his acts and the accountability is individual, both in rituals and in socio-economic contracts.

Objectives (Maq¯asid) of Shari’a

The study of objectives is significant, as they reflect the spirit of the Shari’aand help jurists in determining the prohibition or permissibility of any matters on the basis of Ijtihad and Qiy¯as. Catering to the well-being of the people in the worldly life as well as in the Hereafter or relieving them of hardship is the basic objective of Shari’a. Islam takes a positive view of life considering man as the viceroy of God. Virtue does not mean abandoning the beauties of life, but enjoying those while remaining within the framework of the values through which Islam seeks to maximize human welfare. It requires living a morally responsible life, earning only by fair means and considering wealth as a stewardship for which account is to be rendered to Allah Almighty.

According to conventional economics, livelihood is the fundamental problem of man and economic development is the ultimate goal of human life. According to Islamic economics, livelihood is necessary and indispensable but is not the true and the only purpose of human life; the life hereafter is the real factor to be taken care of. This way, Islam also caters for the welfare of man in the Hereafter. Wealth in all its possible forms is created by Allah, it belongs to Allah; He has delegated the right of property to man for use and He has the right to demand that man subordinates his use of wealth to the commandments of Allah. “He it is who made you vicegerents in the earth” (6: 165) and “does the man think that he will be just left to himself” (75: 36). Wealth has to be used in such a way that it ensures success in this world and the world hereafter.

The overall objective of Shari’a behind these injunctions is the happiness and well-being of human beings in this world and the world hereafter. The concept of happiness from the Islamic perspective is different from the concept of pleasure – the major objective of positive economics. Accordingly, everything which guarantees well-being and fulfils the supreme interests of mankind is included in the objectives of Shari’a. The objectives can be divided into primary and secondary objectives.

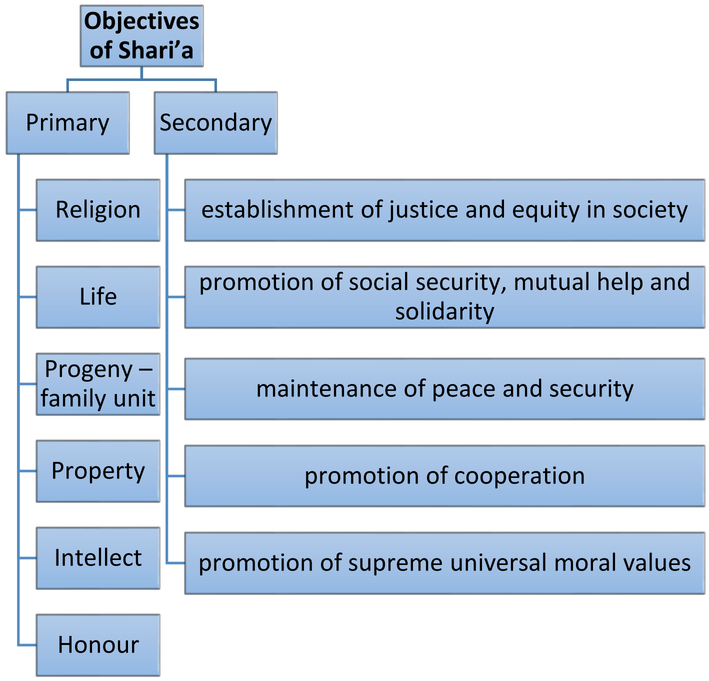


Fig: 5.3

Primary Objectives

The primary objectives that Shari’a tends to realize are the protection and preservation of:

1) Religion.
2) Life.
3) Progeny – family unit.
4) Property.
5) Intellect.
6) Honour.

The protection of religion means achieving the purpose of worship of Allah (SWT). In Islam there is a comprehensive system of beliefs and Shari’a makes it the responsibility of the State to implement Shari’a requirements in respect of beliefs. The protection and preservation of human life refers to the sanctity of life as emphasized in the Qur’¯an and Sunnah. There is the law of Qis¯as to punish those who cause any harm to human life. This objective also refers to the provision of basic necessities to all human beings.

The protection of progeny or the family unit relates to marriage and the family institution, whose purposes are: procreation, protection against lack of chastity and the proper upbringing of children, enabling them to become good human beings and Muslims and to bring peace and tranquility to society. Means to realize this objective are the promotion of the marriage contract, tenets relating to family life and the prohibition of adultery.

The protection of wealth and property refers to the sanctity of the wealth of all members of society, with an emphasis on valid (Halal) earning and discouragement of a concentration of wealth leading to a vast gap between the poor and the rich and the inability of the former to meet their basic needs of food, health and fundamental education. For this purpose, Islam provides a comprehensive law governing Mu‘¯amal¯at or transactions among members of a society.

The promotion of human intellect refers to acquiring knowledge, thus enabling people to differentiate between good and bad and to play their part in enhancing the welfare of human society as a whole.

The protection of human honour and dignity refers to the prohibition of false accusations, the right to privacy and the sanctity of private life.

Secondary Objectives

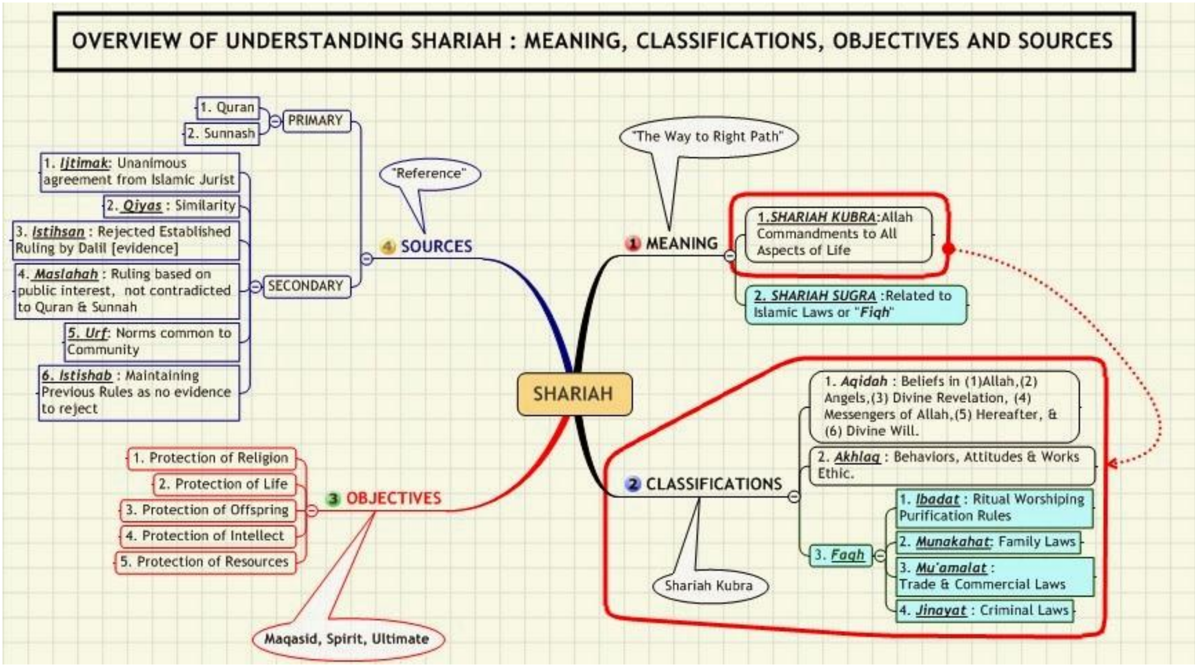
The above primary objectives of Shari'a lead to a number of secondary objectives, which are:

1. The establishment of justice and equity in society.
2. The promotion of social security, mutual help and solidarity, particularly to help the poor and the needy in meeting their basic needs.
3. The maintenance of peace and security.
4. The promotion of cooperation in matters of goodness and prohibition of evil deeds and actions.
5. The promotion of supreme universal moral values and all actions necessary for the preservation and authority of nature.

From the study of the Qur'¯an and Sunnah, some basic socio-economic rights of human beings have been identified. These rights are:

(a) The right to safety.
(b) The right to be informed.
(c) The right to choose.
(d) The right to be heard.
(e) The right to satisfaction of basic needs.
(f) The right to redress.
(g) The right to education.
(h) The right to a healthy environment.

Islam requires rulers and various regulators in the system to protect the masses from harm and hardship caused by unscrupulous factors in society through strong and effective laws, and they should be respected in the sense of fulfilment of all socio-economic rights. The State must also curb institutional and other malpractices.



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Why Study Islamic Economics?

Studying economics is important for the dual purpose of having better sustenance and religious imperatives. Islam does not like the concept of the "pious person" as distinct from the "worldly person". It enjoins a system of devotions/worship as well as guides on the economy, political affairs and international relations. Regarding this integrated approach, the Holy Qur'¯an says:

It is not righteousness that ye turn your faces towards East or West; but it is righteousness to believe in Allah and the Last Day, and the Angels, and the Book and the Messengers; to spend of your substance, out of love for Him, for your kin, for orphans, for the needy, for the wayfarer, for those who ask, and for the ransom of slaves; to be steadfast in prayer, and practise regular charity, to fulfil the contracts which we have made; and to be firm and patient, in pain (or suffering) and adversity, and throughout all periods of panic. Such are the people of truth, God fearing. (2: 177) Professor Dr Anis Ahmad explains beautifully the implications of the above verse of the Holy Qur'¯an by saying:

Thus, Islam emphasizes fair and equitable distribution of resources and meeting the needs of economically feeble people as part of devotion, worship and faith. It induces its followers to relate their piety (Taqwa) with social realities. It persuades a person to share the blessings and bounties of Allah with others as a matter of obligation by declaring that Taqwa encompasses not only the love of Allah, but also the love of fellow human beings, who should be treated as part of an extended human family. This refers in a way to the need to study the economic aspects of mankind.

As the main theme of the Islamic economic system revolves around care for the poor and socio-economic justice, studying Islamic economics should be a strategic activity for economists and policymakers. The Islamic economic system can be studied properly only in the context of the Islamic way of life as a whole. The Holy Qur'¯an gives broad principles of values regarding the economic aspects of man's life, like an owner's attitude towards his property, society's attitude towards the needy, the cooperative basis of the economic relationship and the bias against a concentration of wealth. The individual must be mindful of other ends while planning for economic ends. He has to subject each and every activity to thorough scrutiny, avoiding all those forms which are injurious to social interest.

Islamic Economics: What Should It Be?

To understand the possible structure of Islamic economics, enabling a society to realize the objectives identified above, we may first of all discuss the concepts of economics proper and normative economics. Economics proper, which is also called positive economics, is concerned exclusively with the scientific explanation of behaviour under conditions of scarcity. It is a science, value neutral and is concerned with empirical and not normative aspects. Even where it deals with values and purposes, it deals with them objectively as facts, which, along with other relevant data, determine what is or may be, but not what should be. It describes, but does not prescribe. The definition of "Economics" by Lionel

Robbins is an example of positive economics.

The second kind of economics is normative or welfare economics, which is sometimes called "political economy". In the case of normative economics, policy recommendations must involve some value judgements. The Islamic approach is that economic development and creation of abundant wealth are means to satisfy human needs and support society. These are not sought for boasting or spending in offence, arrogance or oppression. Linking this world with the Hereafter, Islam enjoins Muslims to seek the Hereafter through what they earn and not to forget their share of the worldly life. The Holy Qur'¯an says:

"And seek the abode of the Hereafter in that which Allah has given you, and do not neglect your portion of worldly life, and be kind as Allah has been kind to you, and seek not disorder/corruption in the earth". (28: 77)

Therefore, Islamic rules of economics make it binding for human beings not only to abide by the Shar¯ı´ah tenets relating to dos and don'ts but also to keep in mind the impact of their activities on others and society as a whole. To realize the goal, the State should try to control the wants of the people through a filtering process, motivate the people to abstain from activities injurious to others and restructure the socio-economic system for the transfer of resources from one use/sector to others to ultimately realize the dual objective.

It is the welfare content which makes normative economics different from positive economics.

Islamic Economics Defined

Islamic economics has been defined differently by different economists/scholars, keeping in mind specific aspects of human life. To Ibn Khaldun, economics meant the desire for food and other requirements and efforts to obtain them; and a science which deals with management of households and cities in accordance with dictates of reason as well as ethics, so that the masses may be directed towards a behaviour that leads to the preservation and performance of their species.

Mohsin S. Khan, a senior economist at the IMF, says:

"Broadly speaking, the term 'Islamic Economics' defines a complete system that prescribes a specific pattern of social and economic behaviour for all individuals. It deals with a wide-ranging set of issues, such as property rights, incentive system, allocation of resources, types of economic freedom, system of economic decision-making and proper role of the government. The over-riding objective of the system is social justice and specific patterns of income and wealth distribution and consequently economic policies are to be designed to achieve these ends."

This implies that Islamic economics is a social science which studies the economic problems of people in the light of the values of Islam. One way of looking at Islamic economics would be the use of resources for the welfare of the people within the framework of Shari'a. Once a framework of the Shari'a has been adopted, it will determine various aspects of economic management like the contents of production, trade, finance, distribution and many other things.

Islamic economics deals with issues like how to create, distribute, own and enhance property and wealth, how to spend and dispose of it for the benefit of individuals as well as societies. The means of production of goods are almost the same for all nations, as economic science is universal for all nations. As such, an Islamic economy would also be producing/providing all goods and services required for the "welfare" of mankind. But the economic system that determines how to distribute the wealth and how to possess, spend or dispose of it, is different for different nations depending upon their ideology, and here lies the difference between the Islamic economic system and the capitalistic or the socialistic systems.

The integrated model of the Islamic social framework is based, among other things, on the following criteria, which provide a positive motivation for economic activities, steered by the concept of a fair balance between material and spiritual needs and between the individual's and social needs:

a. Equilibrium between work and worship.
b. Human equality.
c. Mutual responsibilities in society.
d. Distributive justice.
e. Balanced and beneficent use of the "bounties of God".
f. 6. Limited sovereignty of individuals in terms of "self interest" for the benefit of fellow beings and society.
g. 7. The principle of co-existence.
h. 8. The freedom of conscience.

Paraphernalia of Islamic Economics

The objective of the Islamic economic system, like any other economic system, is the realization of efficiency and equity in allocation and distribution of resources, for which it recognizes the role of market forces and the freedom of individuals. But it also recognizes the possible adverse impact of the totally unregulated market on various sections of society, particularly the poor and the disadvantaged.

The urge for maximization of wealth by individuals without taking care of its impact on the well-being of others or society as a whole cannot generate long-term sustainable growth and well-being of individuals or societies. Therefore, both positive and normative objectives are to be realized through market functioning supported by State facilitation and intervention aimed at realization of socio-economic goals like need-fulfilment, an optimum and stable growth rate, equitable distribution of income and wealth with class and ecological coherence.

As indicated above, an economic system has to be discussed as a thought based upon any ideology, while economic science should be considered a science which deals with the creation of wealth. An economic system relates to the management of wealth distribution in a society and enables or restricts its members from utilizing the means of production and satisfaction. Production of goods and services and their distribution among various groups in society, sources of funds for the State and their spending were the main areas of Islamic economics and the system up to the Middle Ages. Commercial activities of that period depicted a number of techniques of production, distribution, trade, payment and mobility of money and credit.

Thus, the system comprises the following three main elements:

1. Ownership of commodities and wealth.
2. Transfer of the ownership.
3. Distribution of wealth among the people.

The variables and thoughts used in economic analysis include the determinants of the level of income and employment, money and banking, fiscal and monetary policies, national income accounting, economic growth, demand and supply of money and stability. Details may also include expenditure, the savings–investment relationship, the savings–income relationship, consumption and investment functions, the potential level of output, employment, labour force and profit as aggregate variables. All these determinants will correspond to principal Islamic values and tenets.

The abolition of interest (Riba), promotion of trading and other real business activities, establishment of profit-sharing as a tool, **the application of Zakat** and avoidance of wasteful consumption (Isr¯abf) along with an effective overseeing role of the State constitute the key macroeconomic features of an ideal Islamic economy. Study of these variables would indicate the state of any Islamic economy, its stability, weaknesses and strengths and various relationships among producers and users of resources.

Ownership of Resources and Property Rights

Islamic economics, based on the paradigm of socio-economic justice, takes its roots from the belief that all resources in the world belong to its Creator, One God; human beings are holding these resources in trust. Behaving as vicegerent of the Creator, they are free to earn and spend the wealth according to His orders given to mankind through His Messengers.

Man has to enjoy and use wealth under Allah's command. Islam has given the individual the freedom to earn a livelihood. Likewise, Islam has given every individual the right to enjoy whatever wealth he has earned by legal means and whatever wealth he has received through the Islamic law of inheritance.

Ownership by man is thus Divine permission for utilizing the goods and assets. The Holy Qur'¯an says: "And give them from the M¯al of Allah, which He gave to you." (24: 33). It also says: "And spend from what He put you in charge of " (57: 7). As such, Islam has set the limits and the means through which individuals, groups, the public and the State can possess property in such a way that acquisition in varying degree is within reach of all the people, despite disparities in their abilities. These limits are in terms of the quality or the means of acquiring and not in terms of quantity of wealth, as this resists human beings' strife to work diligently. Limits in terms of quality are necessary; otherwise human greed could corrupt the economy and cause chaotic relationships in society. It also conforms to human nature so as to satisfy their basic needs and enable people to benefit from comforts.The following are the means of possessing goods: work, inheritance, purchasing/obtaining property for sustenance, properties granted as gifts and the State granting possession of something to the citizens. To facilitate the acquisition of property and wealth, Islam has indicated legal means of ownership and its transfer through a variety of contracts. General rules for these contracts have also been defined in detail with the possibility of resolving any contemporary issues through Ijtihad, subject to observance of allowed limits. These rules allow man to utilize the resources by consuming them, benefiting from them or exchanging them via a number of contracts like sale, loan, lease or gift. Rules pertaining to investment of wealth/property have also been laid down.

Along with property rights, income and profit entitlement are established in Islamic economics. This must occur through the effort, work or taking responsibility (Dham¯an) and distribution by means like partnership, trade, joint ventures, loans, various vehicles of transfer incomes like grants and Zakat and the control of waste. Hence, the Islamic economy has a linkage between the market functions of productive involvement and growth and the institutional functions of policy and control.

Islamic Welfare Approach

The concept of welfare in Islam is neither exclusively materialistic nor absolutely spiritual. It has rather dovetailed the spiritual and material aspects of life so that they may serve as a source of mutual strength and as the foundation of true human welfare and happiness. Study of the teachings of the Holy Qur'¯an and Sunnah leads us to some basic principles of the economic system of Islam, which encourage human beings' development, enforce justice, stop exploitation and tend to set up a contented and satisfied society that can be termed a real welfare society. In addition to achieving optimum produce in both public and private sectors, allocation and distribution of resources and produce must take a course that fulfils the basic human needs of all, irrespective of the colour, race and/or creed of the people. The fulfilment of basic needs makes society tranquil, comfortable, healthy and efficient, and able to contribute properly towards the realization and perpetuation of human welfare. On account of the crucial importance of need fulfilment, it needs to be discussed in detail. As indicated above, the economic system of Islam tends to ensure the satisfaction of all the basic needs (food, clothing and housing) of every individual, without any distinction, and to provide resources to enjoy from living in a particular society. So individuals and society are both important to make a contented and happy economy and society. All individuals are linked with one another by certain relationships in social and economic dealings. Therefore, the standard of living in an Islamic society has to be raised by securing the basic rights for every individual in terms of need fulfilment side by side with enabling them to secure comforts and prosperity. In order to meet the basic needs of each and every member of a society, Islam urges all to earn and seek the provisions for use by mankind. Islamic economy achieves this objective by obliging each capable person to work, enabling him to fulfil his and his dependents' basic needs. A number of verses of the Holy Qur'¯an and traditions of the holy Prophet (pbuh) reveal that Islam obliges individuals to earn and use the wealth so as to develop the economy for the betterment of society. It is the State's responsibility to take measures and adopt policies to enable those who are willing to work and anxious to work to find employment.

If some individuals are unable to earn and fulfil their needs, Shar¯ı´ah obliges their fellow beings – depending upon the nature of the relationship like neighbours, relatives, etc. – to support them in fulfilling their basic needs. If there is nobody to support such people, Islam obliges the State to be responsible for the support of all citizens, particularly mentally or physically disabled people and the destitute. The holy Prophet has said: "The Imam (ruler) is incharge (R¯a'iee) and he is responsible for his citizens." As regards basic needs, there is total agreement among Islamic economists that it is the most important objective of the Islamic distributive policy. However, there may be some difference of opinion as to which needs should be guaranteed and how these should be fulfilled. Nevertheless, maximization of Falah (welfare in this world and the Hereafter) has firm relevance with the Islamic concept of development, which can be achieved through obedience to Allah (SWT) in worship (Ib¯ad¯at) as well as Mu'¯amal¯at, including all kinds of economic activities related to production, consumption, exchange and distribution. As long as seeking the pleasure of Allah is set as the final goal, the latter will be in perfect conformity with the former.

The Factors of Production

The Qur'¯anic injunctions on distribution of wealth help a lot in introducing a broader basis of the distribution of income and wealth and require that in the process of distribution, none of the factors of production is deprived of its share nor does it exploit any other. Land, labour and capital jointly create value. As a result, the land-owner, the labourer and the owner of capital should jointly share the produce. The distinctive feature of the Islamic system is that capital has to bear the loss, if any. In addition to this, Islam compulsorily retains a portion of the produced wealth as **Zakat for those who are prevented from contributing their share in production due to any social, physical or economic handicap.**

Capitalism has four factors of production:

1. Capital – the produced means of production – its compensation is "interest".

2. Land that includes all natural resources – things which are being used as means of production without having previously undergone any process of human activity – its compensation is the rent.
3. Labour – any effort or physical exertion on the part of human beings – its compensation is wages.
4. The entrepreneur or organization – which brings together the other three factors, makes use of them and bears the risk of profit and loss in production – its compensation is "profit".

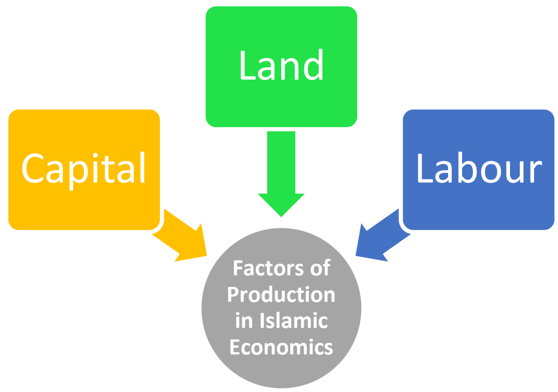

Fig : 5.5

The factors of production in Islamic economics are:

1. Capital – includes those means of production which cannot be used in the process of production until and unless they are either wholly consumed or completely altered in form during the production process; it cannot fetch any rent. "Profit" is compensation of capital in the Islamic framework, but it comes with responsibility or liability. So the profit on any capital is the residual revenue of a business conducted with that capital after making payment to all other parties; if the residual is negative, the capital owner has to suffer a loss that is the shortfall in the principal employed in the business.
2. Land – all such means of production which is used in the process of production in such a way that their corpus and original form remains unaltered. Their compensation is rental; these can be lent or leased. For example, an owner of a factory would claim rent of land and that of the installed machinery and plant; similarly, owners of houses, vehicles, machines, etc. are entitled to rent.
3. Labour – that is, human exertion, whether physical or mental and also includes organization and planning. Its compensation is wages.

Profit, according to Islamic theory, is the result of the productivity of capital that an entrepreneur has invested or a reward for his workmanship or for shouldering responsibility. It is not a reward for capital or for enterprise *per se*. An entrepreneur who, for example, brings together factors like land, labour, machinery and uses his own financial resources (money capital), has to pay wages and rental for the use of land or machinery as per agreed terms; he will make a profit on his capital or reward for his entrepreneurship only if there is some residual after payment of the rental, wages and other expenses on raw materials, etc.

If the money capital is taken as a loan, the entrepreneur is bound to repay the same amount of loan without any addition or shortfall, irrespective of the fact that he earned a profit or incurred any loss in the business. In a case where the whole or a part of the money capital is taken from anyone else who wants a profit on it, and the business suffers a loss, the money capital would pro rata reduce and the provider of the capital would be obliged to accept the shortfall or erosion of the whole amount. Therefore, a capital provider or an entrepreneur is not entitled to profit simply by virtue of being a capital owner or an entrepreneur. All participants in a joint business have similar rights and liabilities according to the nature of the activity or the terms of the agreement.

Restrained Individual Freedom

The “laissez faire” that is the basis of conventional economics has a built-in possibility of distortions in the smooth functioning of the market economy, mainly on account of the unbridled “profit motive” leading to a focus on enrichment without any care for the impact on others or society. Even though the Great Depression and the resultant Keynesian revolution tended to undermine this faith in the efficacy of market forces, the recent disenchantment with a large government role in the economy has restored it and there is a call for liberalism or return, as early as possible, to the classical model with “minimum” government intervention.

State intervention with a secular approach cannot produce long-term solid results for society either. This is because the “profit motive” in the absence of any ethical norms, finds loopholes for misdeeds, injustice and corruption. Even socially undesirable professions like gambling and sex-related industries become part and parcel of public policy, leading to socio-economic problems as most capitalists invest their money in lucrative unhealthy practices and not in socially desirable sectors like education, health, housing and commodity producing sectors including agriculture and industry.

Islamic economics is not devoid of money matters, because those form the greater part of any economy. However, it maintains a balance between production and consumption and cares about distribution. It draws a line of demarcation between good and evil or lawful and unlawful. The overall message that we derive from the literature on the philosophy and the nature of the Islamic economic system is that it is a means to achieve development in terms of complete human personality from all dimensions – material, world and ethical, of individuals and of society as a whole. It pays due attention to causes, effects and consequences of actions.

There are certain curbs and some checks imposed by Shar¯ı´ah on consumers’ behaviour.

Individuals are not at large to exercise their own will in terms of choice. Some basic rules have been laid down to govern intensity of wealth-gaining and income-consuming activities of society. It does not stand neutral as regards ends and means. It is religion-based, valuation oriented, morality-judged and spiritually-bound. It is positive and normative science, as it links materialistic and moralistic requirements of changing nature. Thus, the scope of Islamic economics is the administration of scarce resources in human society in the light of the ethical concept of welfare in Islam.

All types of work except those leading to indecency or socio-economic loss to other individuals and society are permissible. A basic principle of the Islamic legal system is that an activity or a commodity that is not prohibited through the Shar¯ı´ah texts is permissible.

Thus, man has to observe the prohibitions only. Islamic economics would mean undertaking all activities individually or collectively that are not prohibited and that could add to the welfare and happiness of human beings. The most important prohibitions in the field of economics are the prohibition of interest, hazard and gambling due to their extremely harmful impacts on society. Such limitations are necessary for the fulfilment of the overall objectives of the Shar¯ı´ah for making society happy and satisfied, both materially and spritually.

Liberalism versus State Intervention

The individual self-interest of conventional economics leads to maximization of wealth and want satisfaction, independent of its impact on the rest of society. The concept of "positiveness" has been expressed in terms of unrestrained individual freedom, making economics "entirely neutral between ends". Further, it is believed that market forces will themselves create "order" and "harmony", and lead to "efficiency" and "equity". The government should hence abstain from intervening.

The concept of Pareto efficiency in conventional economics is based on the assumption that the market will automatically take care of "equity" and that the market equilibrium will be a Pareto optimum, leading to realization of normative goals at least in the long run. It leads to the common belief of modern economics that any intervention in the framework of Pareto optimality would lead to less efficient results. This framework is, however, based on some assumptions like harmony between individual preferences and social interest, equal distribution of income and wealth, a true reflection of the urgency of wants by prices and perfect competition. Since no real world market is likely to satisfy these assumptions, there is a considerable distortion in the expression of priorities in the markets. Hence, the Pareto efficiency or Pareto optimality concept that generates conflict in society does not fit properly in the philosophy of Islamic economics. It reflects a built-in bias against the realization of normative goals if reliance is placed primarily on prices for allocation and distribution of resources.

Society is for the individuals who are responsible for their actions and accountable to the one creator for their conduct. The individual has a right to participate in economic activities for his sustenance and the tasks relating to social well-being, subject to the limitations and injunctions of the Qur'¯an and the Sunnah. The crucial involvement of individuals for the collective benefit of society has been aptly described by the holy Prophet (pbuh) in a parable, as reported by Imam Bukhari in his "Sahih" and as given below:

"Those who accept and abide by the limits ordained by Allah and those who transgress may be likened to two groups sharing a boat; one group occupying the upper deck and the other the hold. Whenever those in the hold required water they had to go up to draw it. So they thought among themselves; why not have a hole in the bottom and thus save inconvenience to those in the top? Now if those on the top do not dissuade and prevent them, all are lost. If they do, all are saved."

This shows that society cannot remain as a silent spectator to any harmful act of individuals and individual freedom does not imply unrestricted power to endanger the health of society as a whole. Social authority in the form of the State is recognized by Islam for the prevention of exploitation and moral degeneration as well as for the promotion of the material and spiritual interests of men and women. The Holy Qur'¯an says: "O ye who believe! Obey

Allah, obey the Messenger and those of you who are in authority.” Thus, a purposeful relationship based on goodwill and cooperation is found in the individual–State relationship.

The rulers cease to deserve obedience should they transgress the Shar¯ı´ah. The holy Prophet (PBUH) has said: “Obedience, (to rulers) is not valid where a disobedience to Allah is involved”. As such, Islamic economics requires balanced growth in any society encompassing both material and spiritual satisfaction of the individual as well as society. Material wealth, industrial inventions, technological development, etc. are important factors in Islamic economics, but the spiritual and social aspects like the patterns of relationships amongst human beings and between man and God and the emerging perceptions about affairs of life are equally important factors, leading to optimal realization of the objectives of the Islamic Shar¯ı´ah.

The State can introduce necessary laws to ensure social justice and to put an end to economic exploitation and oppression and the Holy Qur’¯an gives the Islamic State the necessary legal authority to do so (see Qur’¯an; 22: 41). The Islamic economic system gives an important overseeing role to the State and regulators in order to create harmony between individuals and social benefits. Freedom available to individuals for undertaking economic activities does not mean that anyone can engage in trade and business that is harmful to society. Belief in one God and accountability in the life hereafter is the central point of all human activities, which can mainly be divided into the rights of the Creator and the rights of fellow beings. All human beings are accountable to Him in the Hereafter with regard to both types of rights and will be rewarded or punished according to the individuals’ deeds without any injustice.

In an Islamic economy, the State is bound to take measures not to allow forces with vested interests to distort the functioning of market forces.A large number of references from the Holy Qur’¯an and the Sunnah reveal that Islam has accepted the law of demand and supply as a principle but has subjected it to some limitations to avoid any moral and social ills and problems. The ultimate objective of an Islamic economy is to establish social justice. The other objectives, such as best use of resources, freedom of work and business, meeting the requirements of the deprived and establishing human dignity, etc. are only there to assist in achieving the ultimate objective. Therefore, it is not lawful to allow the operation of such economic activities that might disturb the balance and real and genuine economic and social justice.

The literature on Islamic economics emphasizes four types of action by government in economic life. These are:

1. Ensuring compliance with the Islamic code of conduct by individuals through education and, whenever necessary, through compulsion.
2. The maintenance of healthy conditions in the market to ensure its proper functioning.
3. Modification of the allocation of resources and distribution of income affected by the market mechanism by guiding and regulating it as well as direct intervention and participation, if needed, in the process.
4. Taking positive steps in the field of production and capital formation to accelerate growth. The Islamic State can impose some limitations with a view to avoiding distortions and keeping in mind the well-being of society as a whole. All members of a society, regardless of differences in gender and religion, are allowed to undertake any of the permissible (Halal) businesses, but this is subject

to the condition that it should not harm others. Once the Pious Caliph, Umar Farooq (Allah be pleased with him) asked a person who was selling a commodity at a much lower price than the market price to increase the price/rate or to leave the market.

Ibnul Qayyim has explained the functions of an Islamic State in the following words:

“Allah has sent down Prophets and revealed Books to establish justice which is the fundamental and basic objective of the whole creation. Everything revealed by Allah proves that the ultimate goal of revelation is the establishment of a just and balanced way of life. In whatever way the law may be made it must aim at establishing justice and fair play. The most important thing is the purpose and objective of law and not how it has been derived or enacted. But Allah, by giving us a number of laws, has set examples and reasonable basis for framing and enacting laws. The lawful government policies and directives are, therefore, considered a part of Shar¯ı´ah and not a violation of it. To define them as government policies is only a matter of terminology, but these are, in fact, a part of Shar¯ı´ah; the only condition is that such government policies and directives must be based on justice and fair play.” (Il¯amul Muwaqqi’in) It is, therefore, established that the responsibility of the government is to maintain a balance of economic activities and services. If the balance is distorted by economic agents with vested interests, the State has to restore the balance. Qur’¯an’s disapproval of the concentration of wealth (59: 7) and emphasis on justice (14: 90) is beyond any doubt. On account of this, one of the important duties of an Islamic government will be to recover wealth usurped through illegal means and return it to its genuine owners or to deposit it with the State exchequer. For checking all irregularities, Islamic economics introduces the institution of “Hisbah” that must be run by people of high integrity. Umer Chapra has listed the following functions of the State in the field of economics andfinance:

1. Eradication of poverty, maintaining law and order, ensuring full employment and achieving an optimum rate of growth.
2. Economic planning.
3. Ensuring social and economic justice.
4. Stability in the value of money. This is vitally important not only for the continued long-term growth of an economy but also for social justice and economic welfare. The Holy Qur’¯an says: “And give full measure and weight with justice” (6: 152). “So give full measure and weight without defrauding men in their belongings and do not corrupt the world after its reform” (7: 85; see also, 11: 84–85, 17: 35 and 26: 181). Money being a measure of value, any continuous and significant erosion in its real value may be interpreted in the light of the Qur’¯an to be tantamount to corrupting the world because of the adverse effect this erosion has on social justice and general welfare, which are among the central goals of the Islamic system. In the mutually interdependent global economy of today, it may not be fully possible for the small and open economy of an individual Muslim country to achieve the desired stability. However, what it does imply is that an Islamic state should itself be clear about its role with respect to price stability and should be determined to contribute whatever it can to the attainment of that goal.

5. Harmonizing international relations and national defence. The Islamic State should encourage and support any constructive move towards peace, and should honour all treaties and agreements to which it is a partner. Nevertheless, it should do its utmost to strengthen its defence so as to prevent or frustrate any aggression against its faith, territory, freedom and resources.

As a corollary, governments and the central banks/monetary authorities would be required to ensure that banking and non-banking financial institutions function smoothly and the interests of all stakeholders, particularly small savers and the masses in general, were protected and the cartels and monopolies did not exploit them. Regulators would also ensure that the institutions did not get involved in antisocial activities injurious to individuals, society and human beings at large.

Leaving the most strategic sector of money and finance to market forces without any effective overseeing role is bound ultimately to generate disastrous effects for the long-term health of economies. Governments/regulators must devise and adopt fiscal and monetary policies in their respective ambits in such a way that an expected rate of return emerging from real sector business in the economies becomes the benchmark and an effective signal for the efficient allocation of funds to various sectors.

Further Reading:

- ✓ ***Consistency and Viability of Islamic Economic Systems and the Transition Process By John Marangos***
- ✓ ***Contemporary Islamic Economic Thought: A Selected Comparative Analysis***