Islam & Human Development

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PRESENTED AT FIRST INTERNATIONAL CONFERENCE ON DIVINE ECONOMICS, AZAD KASHMIR, 2013
Outline of the Presentation

**Microeconomic Perspective on Development**
- Concept of Human Development in Islam
  - Mathematical Presentation
  - Functional Presentation

**Macroeconomic Perspective on Development**
- Long Run Growth Determinants in Theory
- Appraisal of Development Theories
- Growth & Governance Stimuli in Islamic Economy
  - Private Property Within Accountability Framework
  - Factors Contributing to Productivity & Progress

**Is Islam the Cause of Underdevelopment?**
- Exceptional & Qualified Evidence
- External Factors of Underdevelopment
- Role of Interest Based Loans on Development
Human welfare in Islam encompasses economic welfare, but comprises much more than that.

The achievement of human welfare is sought in both aspects of human life, i.e. worldly life and eternal life hereafter.

In recent years, even the western concept of development has recognized the wider dimensions of human development and the role of institutions (Mirakhor & Askari, 2010).
Concept of Human Development in Islam

- Mathematical Presentation

\[ W_h = f (\alpha W_t, \alpha^m W_e) \]

Where

- \( W_h \) is total human welfare in both aspects of human life.
- \( W_t \) is human welfare in worldly life.
- \( W_e \) is human welfare in eternal life hereafter.
Mathematical Presentation: Continued

\[ W_h = f(\alpha W_t, \alpha^m W_e) \]

\[ W_t = f(Z_t) \]

Where \( Z_t \) is a vector of variables which belong to the category of ‘individual specific positive utility gaining choices’.
Concept of Human Development in Islam

• Mathematical Presentation: Continued

\[ W_t = f(Z_t) \]

Constraint Sets

\[ C_S = \{ C_{worhip} \} U \{ C_{self} \} U \{ C_{society} \} U \{ C_{people} \} \]

\[ C_{worhip} = \{ \text{Sala’t, Ramzan fasting, obligatory charity, hajj pilgrimage once} \} \]

\[ C_{self} = \{ \text{Acts which harm a person’s own ethical and spiritual existence} \} \]

\[ C_{society} = \{ \text{Acts which harm society and its institutions} \} \]

\[ C_{people} = \{ \text{Acts which harm other people, their rights, freedom or property} \} \]
Mathematical Presentation: Continued

- \( W_h = f(\alpha W_t, \alpha^m W_e) \)

- \( W_e = f(Z_e) \)

Where \( Z_e \) is a vector of variables which belong to the category of ‘following Allah’s commands which will bring non-decreasing positive utility gain in life hereafter’.
Mathematical Presentation: Continued

- \( W_h = f(\alpha W_t, \alpha^m W_e) \)

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Concept of Human Development in Islam

- **Optimization**

The achievement of lasting happiness and non-decreasing positive utility will only happen through maximizing both the functions, especially the eternal life function.

For ensuring no corner solution, we shall have both $W_t > 0$ and $W_e > 0$.

Islam does not permit monasticism and does not encourage celibacy. Hence, $W_t > 0$, but also achieve a threshold ‘w’ where the ‘w’ represents welfare from minimum level of standard of living.
Concept of Human Development in Islam

- Tradeoffs & Incentives for Ethical Conduct

In tradeoff between $W_t$ and $W_e$, the trial is to choose the right path ordained by Allah so as to achieve the maximum human welfare in the eternal life.

Things that we enjoy in this world will be replaced by similar things in afterlife, but they will provide much more utility.

The difference between the utility of same bundles traded off in this life for afterlife will be given by the positive multiplier in the exponent of parameter ‘$\alpha$’ that is part of eternal life function.
Concept of Human Development in Islam

- Functional Mathematical Presentation
  - Leontief Perfect Compliments
  - Second Party Preferences
  - Family or Relational Utility
  - Lexicographic Utility
Concept of Human Development in Islam

- Functional Mathematical Presentation
  - Leontief Perfect Compliments

\[ U(x, y) = \min (\alpha X, \beta Y) \]

Here, ‘x’ may represent ‘material consumption bundles’ and ‘y’ may represent ‘socially desirable choices’.
Concept of Human Development in Islam

- Functional Mathematical Presentation
  - Second Party Preferences

\[ U = U_i(x_i, y_i, U_j) \]

Here, person ‘i’ and ‘j’ are different.

Even if scarcity in material resources is a problem to cope up with, one way is to selfishly choose consumption bundles to the extent of seeking exclusivity and satisfying self-esteem with Veblen goods.

The other way is to cope up with scarcity in a shared and socially responsible way.
Concept of Human Development in Islam

- Functional Mathematical Presentation
  - Family or Relational Utility

  \[ u = u_i(x_i, y_i) + \sum_{j=1}^{n} r_j u_j \]

  Here again, person ‘i’ and ‘j’ are different.

  ‘r_j’ measures closeness of relation.

  This closeness will depend upon relational, emotional, social and communal closeness between person ‘i’ and ‘j’.

  Islamic principle of brotherhood and equality can further boost the value of ‘r’ beyond just family relations.
Concept of Human Development in Islam

- Functional Mathematical Presentation
  - Lexicographic Utility (Proposed by Dr. Asad Zaman)

- Every bundle of goods $x$, is evaluated using two functions $(U(x), V(x))$.

- Given bundles of goods $x$ and $y$, comparison between them is done first on the basis of $U(x)$ and $U(y)$.

- If $U(x) > U(y)$, then $x$ is preferred to $y$. If $U(x) = U(y)$ then comparison is done by looking at the second component of the utility function, with $x$ being preferred to $y$ if $V(x) > V(y)$.

- An allocation $(x_1, x_2, ..., x_n)$ of commodity bundles to individuals with utility functions $(U_i, V_i)$ for $i = 1, 2, ..., n$ is socially preferable to an alternative allocation $(y_1, y_2, ..., y_n)$ if either (a) $U_i(x_i) > U_i(y_i)$ for all $i$, with strict inequality for at least one $i$, or (b) $U_i(x_i) = U_i(y_i)$ for all $i$, and $V_i(x_i) > V_i(y_i)$ for all $i$ with strict inequality for at least one $i$. 
Long Run Growth Determinants in Theory

- High Rates of savings and capital formation.
- Low population growth rates
- Higher ratio of non-agricultural output
- Public and complimentary investments
- Investment in physical and human capital
- Strong social infrastructure and institutions
- Strong governance and property rights
Appraisal of Development Theories

- Rostow’s growth theory considers religion to be a source of primitiveness, whereas, in an Islamic society, religion is the core.

- Only savings that result in investment contribute to growth. Essentially, what leads to growth is investment. Savings are only the source of investment funds.

- Structural Adjustment forced by Washington Consensus proved to be incorrect.

- Kuznets’s (1955) inverted U-hypothesis also seems to be missing support from empirical data.

- Inequality in USA, China and India increased even after the economies experienced continuous rise in per capita incomes.

- In fact, the empirical data supports the view that inequality is the cornerstone of economies following maxims of neoclassical counter-revolution. The result is best described by Stieglitz who calls this kind of economics, the ‘trickle up’ economics than ‘trickle down economics’.

- Neo-colonial Dependence Model, False-Paradigm Model, and Dualistic-Development Thesis are all effective explanations as contributing causes of underdevelopment, especially of South Asian, African, Latin American & Middle East countries.
Trickle Up Economics

Income inequality
Gini coefficient, 1=perfect inequality

Source: The Economist & OECD
Private Property Within Accountability Framework

- Islamic economic principles honor private property rights and their protection. It implies that market mechanism is admissible and government intervention besides regulation and policy making is not needed in active entrepreneurship or business management (Tahir, 1995).

- Islam has a very clear view on certain institutions like ‘interest based lending’ which has been chiefly responsible for concentration of wealth, rising inequality and even poverty and is an exploitative form of earning money.

- Islam by disallowing interest based earnings, exploitative forms of trade and disallowing imposition of excessive taxes from the state beyond Zakat ensures individual freedom in a much wider sense.
Factors Contributing to Productivity & Progress

- Factors of low labor productivity: lack of education and hence lack of employable skills, poor health, malnutrition etc.

- Islam has made it obligatory for every Muslim, men and women, to educate themselves.

- In Islam, there is proportional tax on income and wealth which is neither too low nor too high. Zakat on wealth limits concentration of wealth and encourages circulation of wealth either through Infaaq or through entrepreneurial activities in both consumption and capital goods.

- Zakat discourages keeping money idle and prohibition of interest encourages entrepreneurship.

- Increase in investment through entrepreneurial activities will increase the labor demand and wages.

- Increase in wages will improve the standard of living of poor labor class and enable them to improve their productivity further.

- Productivity may also rise with increase in capital per worker.
Is Islam The Cause of Underdevelopment

- Muslim countries achieved progress even in western sense of the term. E.g. Malaysia & Turkey.

- Countries like Bangladesh and Indonesia have improved on several development indicators.

- Millions of Muslims that live in Europe and North America have contributed to their respective nations and achieved professional success in diverse areas including academics, science, technology, commerce and public offices.

- Increased acceptance of Islam in the developed world supports the notion that modern education and science has not given any reason to not believe in Islam.

- Critics like Timur Kuran make a common mistake of equating Muslims history or Muslim civilization of past or present as representative of Islam.

- Islam will not be reflected by how it is received, taken and followed by Muslims.

- Mirakhor & Askari clarified that the claims of any society to call itself Islamic must be validated by the existence and effective operations of the institutional structure (rules of behavior).
Is Underdevelopment Solely Driven Internally?

- Biases in international trade.
  - Farm Subsidies
  - Restricted Market Access
  - Tariff Escalation
  - Non-Tariff Barriers (TBT, SBT etc)
  - Distribution Matters in Gains from Trade
  - Cross Subsidies

- Debt servicing takes up almost one half to $2/3$rd of tax revenue.

- One-Size fit all approach in SAPs.

- Political and policy interference.
Importance of Agriculture & Farm Subsidies

Agriculture Share in Less Developed Countries

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<tr>
<td>In Employment (%)</td>
<td>79.5</td>
<td>76</td>
<td>70.8</td>
<td>68.6</td>
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<tr>
<td>In GDP (%)</td>
<td>30</td>
<td>29.5</td>
<td>30.2</td>
<td>28</td>
</tr>
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Source: World Development Indicators 2008, World Bank

Agricultural subsidies
Producer support, % of gross farm receipts

Source: OECD

Source: The Economist
Is Underdevelopment Solely Driven Internally?

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- Debt servicing takes up almost one half of tax revenue.
- One-Size fit all approach in SAPs.
- Political and policy interference.
Effects of Interest Based Loans on Development

- Sub Saharan Africa receives $10 billion in aid but loses $14 billion in debt payments per year (Africa Action, 2008).

- Many African countries spend more on debt than either on health or education.

- Regrettably, 7 million children die each year as a result of the debt crisis.

- Ajayi & Oke (2012) found in an empirical study for Nigeria that external debt burden had an adverse effect on the per capita income and led to devaluation of the currency, increase in unemployment, social strife and poor educational system.

- Easterly (2002) showed negative effect of indebtedness on growth. Even concessional financing, a form of debt relief also failed to reduce net present value of debt.

- Cunningham (1993) collecting evidence for the period 1971-1987 from 16 HIPC found a significant negative relationship between the growth of debt burden and economic growth in these countries.

- Malik et al. (2010) provided the empirical evidence for Pakistan’s economy which shows negative and significant relationship of external debt with economic growth. Currently, Pakistan pays around Rs 1,100 billion in debt servicing which is far below its development spending.
Thank You

For Feedback & Queries

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