Consumption Function in Islamic Economics

*Syed Iqbal Mahdi**

M. Fahim Khan, "Macro Consumption Function in an Islamic Framework," *Journal of Research in Islamic Economics* (JRIE), Vol. 1, No. 2, Winter 1404/1984, pp. 1-24.

Prof. M. Fahim Khan's paper suffers from a number of deficiencies which may be grouped under the following categories:

1. Inaccuracies in the description of positions relating to modern secular economics.
2. Questionable interpretation of Islamic positions.
3. Technical and logical errors in model construction.

I shall take up these points in turn.

To begin with, Prof. Khan's description of the premises of modern economic theory of consumer behavior and its subsequent critique is inaccurate. According to him, "Modern economic theory studies consumer behavior under the following premises: i) It is assumed that a consumer will decide what to consume and how much to consume only to gain the material benefits and satisfaction. ii) It is generally assumed that all his consumption is geared to satisfy his own needs. He is not bothered to satisfy anyone else's needs. iii) It is assumed that a consumer behaves rationally. This among other things, means:

(a) the consumer will neither be a miser nor an unnecessary spendthrift.

(b) he will not hoard his wealth." (p. 2)[1]

Modern economic theory of consumer behavior does not assume any of the said premises given by Prof. Khan. What modern theory assumes is that a consumer with given income allocates his spending on different goods and services in such a way that he maximizes his utility or satisfaction. According to modern theory, it does not matter whether a consumer is a miser, spendthrift or a hoarder. Also it does not matter

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*Syed Iqbal Mahdi is Professor and the Head of Economics Department, Benedict College, Columbia, South Carolina. He holds Ph.D. in Economics from the University of Massachusetts.

[1]Page numbers given in the text of these comments without reference, refer to Prof. M. Fahim Khan's article in JRIE, Vol. 1, No. 2.

what cultural values or religious preference he has. For example. according to modern theory, a Muslim consumer whose marginal utility for Haj is far greater than his marginal utility for a new car is perfectly rational by deciding to spend his money on Haj rather than on a new car even though all his satisfaction is spiritual.

In the modern economic theory of consumer behavior, utility is a subjective and psychological phenomenon and is not restricted to material benefits as contended by Prof. Khan. A couple of quotations from one of the textbooks used currently in American universities will make this point clear.

> . . .Economically rational behavior, or economic rationality, is any action that people take to make them better off or to prevent them from becoming worse off.
>
> Rational behavior need not be totally selfish. Good things come in many different packages. Self-interest, then, has a broader meaning in economics than it does in common usage. People not only consider themselves better off when they add to their stock of material goods but also feel better off when they believe that they have done the right thing.
>
> Actually, most individuals base decision on social, political and ethical considerations as well as on personal gain. Also what people do may be strongly affected by habit, custom, and tradition. Every society weaves a fabric of institutions that guide its economic behavior.[2]
>
> . . . All such behavior may be entirely rational to the consumer who engages in it, whatever you, or we, or the rest of the world may think about it.[3]

Prof. Khan's statements and interpretation of some of the Islamic positions are questionable. Consider the author's distinction between E_1 and E_2; E_1 being "spending to achieve satisfaction in this world" and E_2 being "spending for others with a view to earn reward in the hereafter." (p. 7)

The above statements are not in conformity with Islamic principles. A Muslim is always a Muslim, no matter what he is doing. If he spends his money on himself and his family (E_1), or on others (E_2), he does so following the commands of Allah with a view to earn a reward in the hereafter. Now consider Prof. Khan's following statement:

> ". . . The more a person is God-fearing. . .more of the total spending will go to E_2." (p.9)

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[2]M. Bronfenbrenner, W. Sichel and W. Gardner, "Microeconomics," Houghton Mifflin, Boston, 1984, pp. 21-22.

[3]*Ibid.*, p. 111.

It appears from this statement that the author considers E_2 as a measure of God-fearingness. Such a position is questionable from Islamic point of view. Whether a person spends more or less proportion of his income toward E_2 depends on a number of factors like his income, size of family, personal and family needs and other special family concerns and responsibilities; such as chronic illness in the family requiring unusual medical care, large education expenditures, etc. Individual circumstances vary from person to person. Thus a person who has allocated relatively a low proportion of his income to E_2, is not necessarily less God-fearing. Only Allah has the complete knowledge of all circumstances to make such a judgment. However in the Holy Quran we get clues to the factors which will determine the reward in the hereafter. These factors include a number of things such as the five pillars of Islam, taqwa, tawakul and good deeds in general. Thus Zakah and charity are not the only facts determining God-fearingness and the reward in the hereafter.

Finally the paper gives the impressions that Islam urges Muslims to earn more and more in order to spend more and more on E_2; also that Zakah and charity are the only or major sources of earning reward in the hereafter. Consider the following statements:

> The desire to increase income is strong for a Muslim consumer because he would like to spend in the way of Allah and earn a reward in the hereafter. Also, it is a Muslim's religious obligation to improve his economic condition so that he becomes a Zakah payer rather than a Zakah receiver. (p. 12)

> ... But this population knows that to be always in the receiving class of Zakah and charities is not encouraged in Islam and that he has to improve his economic condition. Also he wants to earn reward by spending in the way Allah as the upper income groups are doing. So he will make efforts to increase his income. (p. 15)

This kind of overemphasis on earning or increasing income is questionable from an Islamic point of view. This makes the plight of a human being in Islamic society resemble very much his counterpart in the materialistic societies of capitalism and socialism in which the man becomes a money-making machine, though for a different reason.

With respect to the statements on Zakah and charity, it should be mentioned that they are obligations only on those who can afford. Allah asks haves to share wealth with have-nots, but does not make it obligatory to earn more and more. One does not have to become rich or Zakah payer to earn a reward in the hereafter.

There are logical and technical errors especially in the formulation of microeconomic model of consumer behavior. The referee of this article, Dr. Zaraqa, is right in pointing out that the marginal utility of E_2 can not be constant, and the law of diminishing marginal utility applies to E_2 just the same way as to E_1. Logically speaking, an additional dollar spend on E_2 will bring far greater satisfaction to a person who has not spent enough on E_2 in the past, than to the one who has more than fulfilled the obligation of Zakah.

The author's contention that "the assumption of declining marginal utility of E_2 being supposed to have no effect on the conclusions" (p. 9) is unwarranted. This is so because the conclusions are not derived from this model. The author does not pursue microeconomic analysis beyond this point and he moves to macroeconomic formulation, and furthermore both models are independent of each other.

There is a mathematical inconsistency in the model which might have resulted by not being careful in selecting letters for variable names in the micro and macro versions. Consider the following equations:

(1) $Y = E_1 + E_2$ (p. 8)

(2) $E_1 = Y_u - E_2$ (p. 14)

(3) $Y = Y_u + YL$ (p. 12)

Substituting the value of E_1 (eq. 2) into eq. 1, gives:

$$Y = Y_u$$

which is not consistent with eq. 3. This problem could have been avoided by selecting upper case or capital letters for the macro model and lower case letters in the micro version.

The following equation on p. 13 is inaccurate:

$$\triangle Y_u = I/K$$

Change in income ($\triangle$Y) results from change in investment ($\triangle$ I) rather than from total investment I. This equation should be:

$$Y_u = \triangle I/K$$

There is a discrepancy or a typographical error in the presentation of the same equation on p. 13 and p. 16:

$\triangle Y_u = I/K$ (p. 13)

$\triangle Y_u = l/K$ (p. 16)

To conclude it should be mentioned that in spite of the problems discussed above, Prof. Khan's attempt toward quantitative model building in Islamic economics is commendable. Trials should not be forsaken for the fear of errors.