

The Effect of Excluding Interest, in an Islamic Economy, on the Rate of Growth of Output and Achieving a Fair Return for Monetary Capital

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Abstract

The Islamic economic system, like other economic systems, aims to achieve efficiency in allocating resources. Questions arise about the ability of this system to achieve this efficiency in the absence of interest on monetary capital in this economy, as it is considered usury forbidden in this system. This research studies in a comparative framework with the traditional economy, some aspects of efficiency, analyzing and proving the ability of the Islamic economic system, which excludes interest on capital as it is forbidden usury, to maximize the rate of growth of output and achieve a fair return on monetary capital that financing economic activity.

Keywords

The Islamic Economic System, Interest on Capital, Efficiency, the Growth Rate of Output, Distributional Justice

1. Introduction

The Islamic economic system, like other economic systems, aims to achieve efficiency in allocating resources. The exclusion of interest on monetary capital raises doubts about the ability of the Islamic economy to achieve this efficiency in the absence of interest on monetary capital in this economy, as it is considered usury forbidden in this system. This research, studies in a comparative framework with the traditional economy, some aspects of efficiency, analyzing the ability of the Islamic economic system to maximize the rate of growth of output and achieve a fair return on monetary capital that finances economic activity.

The research discussed the difference in the value judgments controlling hu-

man behavior between the capitalist and Islamic economies, and the implications of this for the concept of efficiency and distributional justice in the Islamic economic system compared with that in the traditional economy. This is reflected in the framework in which the hypotheses of this research are analyzed.

2. Research Methodology and Plan

This is theoretical research, and by God Almighty's will, we will use a comparative descriptive approach to test the research hypothesis:

The first hypothesis: The Islamic economic system can achieve the goal of maximizing the rate of growth of output in the absence of interest.

The second hypothesis: The Islamic economic system can achieve a fair return for monetary capital in the absence of interest.

Accordingly, we will divide the research into two sections:

The first section: The ability of the Islamic economic system to achieve the goal of maximizing the rate of growth of output in the absence of interest.

The second section: The ability of the Islamic economic system to achieve a fair return for monetary capital that finances economic activity, in the absence of interest.

Then, considering these two sections, we present the results of the research.

This is in addition to an appendix to explain the concept of efficiency and distributional justice from an Islamic perspective as part of the analytical framework of the research.

3. Previous Studies

There are many studies on the efficiency of resource allocation, from which we extract the following recent research which is related to the two research hypotheses:

1) Kato, T. (2022)

The research applies new econophysics models of wealth exchange and redistribution to quantitatively compare these characteristics to those of capitalism and evaluate wealth distribution and disparity using a simulation. The research found that prohibiting interest in the Islamic economy is effective in reducing disparity and the structure in which only one economic agent bears the profit and loss increases disparity in the loan interest model. Based on simulations using the joint venture model, exchange alone, even a reciprocal joint venture, cannot avoid increasing disparity, and redistribution is essential. As for the difference in the profit/loss ratio, the results showed that prohibiting *gharar* and promoting parties' active involvement in each other's affairs in *mudarabah* deter the speculation that would normally increase the disparity.

The researcher decides that this research utilizes an econophysics approach to indicate some of the underlying causes of disparity in exchange and redistribution, it is limited in its recommendations of practical policy or effective policy implementation. Such attempts remain for future empirical studies in econom-

ics, political science, and sociology.

Our research is distinguished by the fact that it used a comparative descriptive approach regarding the ability of both the Islamic economic system and the traditional economic system to achieve a fair return on monetary capital. Also, this current research did not analyze the comparative ability of the Islamic economic system to maximize the rate of growth of output.

2) *Meirison, Tuti Unani, Kasmidin (2021)*

This paper aims to describe the socio-economic justice concept taught by Islam, which wants a proportional income distribution.

Some perspectives and opinions stated that the similarity of the socio-Islamic justice system with socialism was not entirely true; there were more mistakes; conducted a literature study and a qualitative descriptive analysis approach. After comparing various schools of thought and the ulama's views (Jurists) on social justice and poverty epistemologically in Islam, a usual standard of life is found in Islam. The Hadith of the Prophet PBUH supports this. It has described the basic needs of a Muslim as not many as has been imagined so far.

The research concludes that Islam has a solid legal basis in regulating justice and the balance between rights and obligations. It regulates the relationship between the individual and society. Islam also regulates the spiritual and the physical and between this world and the hereafter. The Islamic economic system's essential characteristics are described in the Al-Qur'an verse, namely in Surat Al-Hashr, verse 7. Islam has explained the standard of living for its people and does not live in excess. Following the Prophet, Peace be upon him, the pattern of life, and his pious companions and scholars will solve many economic problems Muslims face at this challenging time.

This research provided an Islamic reference for justice in the Islamic system, but it did not provide an analysis of the ability of the Islamic economic system to maximize the growth rate of output and determine a fair return on capital in the absence of interest.

3) *Alizadeh Emam Zadeh, M. R. (2020)*

Given the importance of fair distribution as a measure of Islamic economic justice and equal distribution of income in Islamic countries, the present study investigated the economic convergence of income distribution as an index of Islamic justice in selected Islamic countries.

The research is applied research indicating that income distribution in 20 countries under study was convergent at the rate of 0.31 and was significant at 1%. The results of conditional beta convergence implied convergence of the Gini coefficient in these countries. The inflation rate and per capita GDP had positive effects on the Gini coefficient.

This research did not address the theoretical analysis of the ability of the Islamic economy to achieve a fair distribution of returns on monetary capital, nor is it one of its objectives to analyze the ability of the Islamic economy to maximize the growth rate of output.

4) *Ghaith, Magdi Ali, Al-Hakim, Munir Suleiman (2018)*

The research presented jurisprudential literature and philosophical references and did not provide a scientific analysis of how the Islamic economy achieves the ability of the Islamic economy to achieve output maximization. Regarding the return on cash capital, it stated that the method of participation in investment achieves a fair return on cash capital compared to the interest rate mechanism, and it did not provide an analysis of that.

5) *Bello, Hashim Sabo, Ali, Abubakar Tatari, Ahmad Nura, Saleh Aminu, Galadima, Ibrahim Suleiman (2018)*

This review paper examined some economies derived from Islamic value premise in nations such as Iran, Malaysia, and Saudi Arabia as alternative solutions to economic crises emanating from conventional economies. This research shows that the innovation brought about by the structuring of Islamic economics and its financial products would contribute to the creation of a new asset class that will be available to customers of all faiths. The introduction of Islamic finance models such as the Mudarabah, Murabaha, Sukuk, and Istisna'a which have been tried and tested in other countries would further strengthen the financial system in both conventional and Islamic economies thereby creating risk diversification against possible and future financial crises.

This research is reference research that did not analyze the ability of the Islamic economy to achieve economic efficiency. Regarding the effect of excluding interest, it sufficed in explaining the effect of introducing Islamic mechanisms on reducing risk and investing in investment activity.

6) *Al-Faris, Jassim and Ibrahim, Ahmed (2010)*

This research showed the impact of the difference in ideological and cognitive references on the work of economic activities. It turned out that the traditional economy, which operates under the dominance of the market mechanism, moves in the light of interest driven by selfishness and pleasure, and is supported by a philosophy that glorifies individualism and conflict, while the Islamic economy operates under the provisions of Sharia, and its values. Its goal is to rebuild the world and man in the light of divine justice. The research also revealed the fact that the efficiency of the economic resource in traditional economic theory is achieved through material return, independent of any value judgments.

Therefore, the opportunity cost is the goal of the resource that operates according to the scale of market forces that operate independently of any values other than maximizing returns and consumer tastes, while resources in the Islamic economy have been made available by God Almighty to people, so they are (a trust), and they must be used accurately in light of the purposes of Sharia and its laws in Building the earth and human well-being, scientifically and economically, is the measure of his efficiency.

In addition to the fact that the research did not provide an accurate description of the concept of economic efficiency in the Islamic economy, the research

did not address the ability of the Islamic economy to achieve efficiency.

4. What Does Our Search Add?

Our research has proven through a scientific approach that:

1) The Islamic economic system can achieve the goal of maximizing the growth rate of output in the absence of interest on monetary capital, this is within the framework of the concept of efficiency in this economy.

2) Our research also demonstrated, through a scientific approach, the superiority of the participation mechanism adopted in the Islamic economic system in achieving a fair distribution of returns between monetary capital and the production factors participating with it in economic activity, compared to the interest mechanism.

5. Research Related Concepts

5.1. Halal

It is permissible ... what God has permitted in His holy Book is halal, and what God forbids is taboo, and what is silent about it is pardoned (i.e., It is permissible to do or not to do). It can be said, in light of the Holy Qur'an and the Noble Prophet's Sunnah, that what is permissible is everything that is objectively beneficial and pure, and that what is forbidden is everything that is objectively harmful and what is objectively unbeneficial, and whose harm is greater than its benefit.¹

5.2. Priority in Fulfilling Needs

It is intended to classify the degree of importance of goods in terms of their entitlement to fulfill them, so they are arranged in descending order, starting with the necessary, then the quasi-necessary, then the improvements. Goods are divided in this way based on their service for a necessary, quasi-necessary, or improvement purpose.

Priorities also mean the classification of uses for individual expenditure in terms of the degree of entitlement to whom the spending is directed. They are arranging a descending arrangement that begins with the person spending on himself and his dependents, then spending on the owners of merit expenditures from his relatives, then spending for the sake of God in general, then saving. These priorities, with their two branches, are based on the guidance and purposes of Islamic Sharia, and do not leave entirely to the discretion of the individual without a guide from Sharia (Islamic Law).

5.3. Moderation in Spending

In fact, the broad concept of moderation in spending includes, among other things, taking care of priorities and achieving sufficiency in meeting needs.

¹See, for example, Qur'anic verses No. 219 of Surat Al-Baqarah and 32 and 157 of Surat Al-A'raf.

However, in our analysis, moderation will be limited to a narrow concept related only to the scope and amount of spending. So that spending is characterized by moderation if it does not include spending on taboos, and it is within the framework of what is known about the likes of this individual, and the care of right justice between the needs of the present and the future, and finally, if this spending does not absorb all of the income unless this income is already insufficient, except to achieve sufficiency of the necessities.

5.4. Commitment Returns and Legitimate Utility

Commitment return is intended, in this research, an indirect return estimated by the individual, resulting from his commitment to the requirements of Islamic Sharia in his economic decisions. This return expresses the state of contentment and conscience comfort that a Muslim sense from his feeling that he has fulfilled what God has commanded in terms of halal and moderation in spending and caring for rights and priorities within the framework of ability.

This does not negate the material return that can result from this commitment, which may be represented, for example, in preserving health because of moderation. It also does not negate the blessings that an individual can get, as well as the reward in the hereafter, but we exclude it because it cannot be subjected to analysis.

As for legitimate utility, it is intended as a direct return that the individual also appreciates, and that results in making various economic decisions. Utility derives the adjective “legitimate” from its permissibility in the Islamic Sharia.

5.5. The Concept of “Right Justice”

Right justice is based on giving everyone who holds a right his right, as defined by Islamic Sharia, and is based on combining and reconciling different rights, as well as between moral principles and material interests. So, it does not recognize absolute rights and freedoms but rather sets controls for these freedoms and rights that will establish a balance that does not bias a party without a party.

Right justice is the characteristic of Islam in everything, not just in allocating resources (See, for example, verses Nos. 18 of Surat Al-Imran, 159 and 181 of Surat Al-A’raf, and 60 of Surat Al-Nahl). The right justice concept in resource allocation is aimed at achieving justice in meeting needs, that is, moderation in meeting needs according to priorities and within the framework of achieving sufficiency for all people (See the verse 29 from Surat Al-Baqarah).

5.6. Sufficiency Level in Meeting Needs

The amount of this level is determined in a way that is sufficient for the moderate fulfillment of needs with its three levels of necessities, quasi-necessities, and improvements. This moderation in fulfilling the needs is determined in light of the income available to the individual, and that is for those who achieve his sufficiency by themselves or the sufficiency of the likes or (if the likes cannot be

found) with the sufficiency of the middle class, and that is for those who achieve part of their sufficiency, or all of his sufficiency, from the distribution institutions In the Islamic system.

The duration of sufficiency is determined in a way that achieves the sufficiency of life for those who can achieve the sufficiency of themselves but lack a tool for work or capital for trade, for example, and in a way that achieves the sufficiency of a Hijri year for the incapable of earning such as the blind, or the one who gains what is not sufficient for him.

5.7. Equilibrium in Fulfilling Needs

“Equilibrium in fulfilling needs” means justice in meeting needs between the present and the future in an Islamic economy.

5.8. The Concept of “Al-Mudarabah”

Mudarabah in the Islamic system means one of the legitimate ways of using cash capital, in which money is on one side and work on the other side. The profit between the worker and the owner of the cash capital is known in proportion. It is agreed for each of them on a percentage of the profit when it is achieved. If a loss occurs, the owner of the cash capital is the one who bears the loss, unless the worker is a transgressor or dissipater.

5.9. “Al-Mudarabah” Ratio

It is the ratio of profit that is agreed upon for the owner of the cash capital in “Al-Mudarabah”.

5.10. Expected Rate of Return of Financing

An analytical tool is provided by the author to calculate the probable cost of cash capital for allocating it among different uses. It is calculated by multiplying the “Al-Mudarabah” ratio by the expected rate of return on investment in the branch of activity under consideration (in the “Mudarabah” market).

Section 1

6. The Ability of the Islamic Economic System to Achieve the Goal of Maximizing the Rate of Growth of Output in the Absence of Interest

It is well known that there are common points where different systems meet, these systems meet, on that the ultimate goal of allocating resources is to fulfill needs. Also, different economic systems converge when targeting macroeconomic goals, which allows for a comparative analysis of the effect of excluding interest on these goals.

In our current analysis, we will consider the following new classical model (Edgmand, 1979) which assumes:

- 1) That investment is always equal to the level of full employment of saving,

and then full employment is assumed since the beginning of the analysis.

2) The saving (s) is a fixed part of the product so that:

$$S = sY \quad (0 < s < 1) \quad (1)$$

where labor force and population size grow at a constant rate (n) which is independent of real wages and other economic variables.

3) The production function assumes the possibility of substitution between the factors of production.

4) The economy can be described by the Douglas Cup production function² as follows:

$$Y = Ae^{rt} K^\alpha N^{1-\alpha} \quad (0 < \alpha < 1) \quad (2)$$

where (Y) is the output, (K) is the capital stock, (N) is the number of workers employed (Ae^{rt}) represents the effect of technology with (A) representing a positive constant, (e) the natural e from mathematics, (r) the growth rate of technology, (t)time, (α) and ($1 - \alpha$) represent the partial elasticities of production for both capital and labor respectively. Thus, it is assumed that technology improves at the constant rate r .

From the production function, we can conclude the growth rate of output,

$$q = r + \alpha h + (1 - \alpha)n \quad (3)$$

That is, the growth rate of output (q) has a positive relation with the technology growth rate (r), the capital growth rate (h), and the labor growth rate (n).

In line with the aim of our research, we limit ourselves to analyzing the effect of excluding interest on the growth rate of capital and then on the growth rate of output by assuming other things are equal.

Hence, a competency comparison in this respect is a comparison of the ability of the allocation tool concerning capital. We start by analyzing the comparative ability of interest, both in the case of its existence or its non-existence, on achieving a greater growth rate of cash capital. In the case of stable dynamic equilibrium; and with we initially assumed that the labor supply is growing at a constant rate (n), and we know that the net investment (I) equals a fixed part of the output (s), hence,

$$I = \Delta K = sY$$

If we divide sY , ΔK by K , we get, $(\Delta K/K) = s(Y/K)$ or,

$$h = s(y/k) \quad (4)$$

Since s is a constant, the ratio of Y to k must also be constant for the capital stock to grow at the constant rate, h . therefore income Y must grow at the same

²This function was formulated by American economists Cobb and Douglas in 1928 in a paper entitled "The Theory of Production" based on their experimental research. It is a first-order homogeneous function that describes the constant return to scale. According to Chambers and Ray (2021, 22), "The Cobb-Douglas production function remains a classic example of empirical evidence inspiring a theoretical formulation of a production function that has served as the gold standard in neoclassical production economic theory for decades. From:

https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4163627

rate as the capital stock (the constant return to scale).

Assuming that (K) is equal in both the Islamic and capitalist systems, then the value of (h) depends on the value of (sY), that is, on the value of the saved part (the invested part) of the income. This saved part (sY) of income is determined if the non-saved part (cY) or (C), consumption, is determined. So, it can be said that the rate of capital growth depends on the value of (C) or consumer spending. The lower the percentage of income spent on consumption (C) the more the rate of accumulation was greater. The question arises: Which of the Islamic and capitalist systems achieves less consumer expenditure? and that is considering equal income in both systems and light of the equality of other factors affecting in this regard, except for the difference in the values provisions of both systems.

The writer proposes an answer to this question by analyzing two effects: The first of which is analyzing the effect of substitution of the expected rate of return on financing (Abul Fotouh Nagah, 2022), as an alternative mechanism for the allocation, proposed by the author, activates the value judgments of Islamic economy instead of interest on money capital which activates value judgments of Capitalist economy; And the second by analyzing the impact of Zakat in the Islamic economy on the marginal and average propensities to consume.

6.1. The Effect of Substitution of the Expected Rate of Return on Financing Instead of Interest on Money Capital on Saving

We can say that in the capitalist system, the value of (C) is determined in the framework of achieving the maximum possible utility from the distribution of consumption between the present and the future, a distribution in which interest plays an important role as a tool to deduct future utilities to compare them with the present utilities from consumer spending. A decrease in the interest rate increases the utilities of present consumption compared with future consumption, which increases the value of the present consumption (C). This situation despite the assumption that it achieves the greatest possible utilities from both present and future consumption (within the framework of the concept of utility in the capitalist economy), actually causes two things to happen:

- 1) The possibility of the value of (C) or present consumption exceeding the limits of moderation.
- 2) The growth rate of capital (h) decreases.

In the opposite case, higher interest rates lower the utilities of present consumption compared to future consumption, which reduces the value of (C), and increases the rate of accumulation (h).

In the Islamic system, we assume theoretically that spending on necessities, semi-necessities, and improvements is distributed between the present and the future within the framework of achieving equilibrium in fulfilling needs. An equilibrium is governed mainly by the criteria of moderation, priority, and justice between the present and the future. The alternative allocation tool (the rate of return on financing) plays, in this, a limited role in the framework of these criteria. If the expected rate of return of financing increases, it is differentiated

between two cases:

(A): In which the remaining amount of income (S) after moderate spending in the original period is sufficient, or more than, the amount necessary to achieve a level of fulfillment of all needs in the following period equal to at least the level of fulfillment this needs in the first period; in this case, the amount of (S) may increase if the individual decides to lower his spending (C) to the lowest limits of the moderate area to take advantage of the higher rates of return.

(B): In which the remaining amount of income after spending in the original period is not sufficient to achieve an equilibrium in meeting needs between this period and the following period; in this case, the rising in the rate of return of finance increases the amount of the expected return on savings-investment, and hence increases expected income in the following period, which reduces the need to lowering spending in the first period but. In both cases, the spending in the first and second period does not exceed the moderation, and it can be less than it (Abul Fotouh Nagah, 2022).

If the expected rate of return for financing falls, if we are in the case (A) then this decrease may cause the insufficient of the amount saved to achieve an equilibrium in meeting needs and then cause a reduction in spending in the first periods, and if we are in the case (B) then this decrease leads to a further reduction in current spending, and hence a greater decrease in the value of (C).

If we assume, for comparison, that the pattern of income distribution is unified in both a capitalist economic system and an Islamic economic system, and the substitution of the expected rate of return of financing within the framework of moderation and equilibrium in meeting the needs, instead of interest rate in the framework of utilitarianism and individualism. This results in a lower level of total consumer spending in the Islamic economy than in the Capitalist economy for at least two reasons:

The first reason is that consumer spending in the Islamic economy is always moderately framed and may even decrease below moderation if the amount of residual income from moderate spending in the original period is insufficient to achieve the same level, at least, of meeting needs in the period next. The second reason is that even if we assume that consumer spending in the capitalist economy will avoid extravagance and luxury consumption, there will still be consumption of taboos, such as alcoholic drinks, and tobacco.

If we exclude the assumption of unifying the pattern of the income distribution, which is the closest thing to reality, given that the Islamic economy is assumed to inherently tend to approximate the income and wealth inequalities. Hence analyzing the effect of excluding this assumption requires in the beginning to know the degree of inequality in both systems, which can differ from one case to another from comparison cases. But we can assume in general that the degree of inequality in the capitalist economy is greater than in the Islamic economy, noting that in the Islamic economy, the inequality in the distribution is available, even if it differs in its degree.

The effect of the difference in the degree of inequality in the income distribution on the total consumption depends, among what depends, on the degree of variation in the marginal and average propensities to consume for the different income groups, which cannot be determined theoretically. However, it is assumed that marginal and average propensities to consume of people with similar income groups are lower in the Islamic economy than in the capitalist economy, due to the commitment of spending behavior in the first economy to moderation and excluding the consumption of taboos and due to the Low simulation effect.

But what we can propose is that the value of (C) in the Islamic economy, whether greater or smaller or equal to the value of (C) in the comparative capitalist economy, this value, and hence the growth rate of capital, is assumed to be determined in light of moderation and equilibrium in meeting needs within the framework of sufficiency, which achieves, according to our assumptions, the maximization of meeting needs at the macro level. And that if it is possible in some cases that the value of (C) in the Islamic economy be greater than that in the capitalist economy, this does not decrease the efficiency of the Islamic economy within the framework of the efficiency criteria for this economy, as long as this value is determined in light of the present consumption commitment to moderation, and achieving equilibrium in meeting needs between the present and the future.

6.2. The Effect of Zakat on the Option of Consumption and Saving

It is well known that zakat is taken from the rich and given to the poor and needy. This is the general trend for zakat spending, whether this poverty is original, temporary, or casual. If we assume that the marginal and medium propensity to consume of the rich is less than those of the poor, then transfers from the rich to the poor in the frame of zakat will lead, assuming the other things being equal to an increase in the level of aggregate consumption and a decrease in the level of aggregate saving. However, the matter may require a more detailed and accurate analysis.

On the one hand, zakat may not be given to the poor and needy in the form of cash, but in the form of production tools, a craft machine, or capital for trade, for those who can work and earn, and they achieve their adequacy by themselves. Also, zakat may be transferred to the wealthy if it is paid, for example, to pay a debt of “Gharim” (a debtor is unable to pay), and it is paid in this case to a creditor who is likely not to be poor. Likewise, some of the zakat categories are “those working in the Foundation of zakat” and they may not be poor either. Finally, what is paid to a category “in the necks” (i.e., Releasing slaves), regarding what is paid to the slave’s master, usually, turns into rich people ...and so on.

On the other hand, the degree of the impact of zakat transfers on both the level of total consumption (increasing it) and aggregate savings (decreasing it) depends on many other factors, the most important of which is the degree of fair-

ness of income and wealth distribution. It is reasonable to assume, with other factors remaining the same, that this effect will be in the case of a higher degree of equitable distribution (which is the closest position to the assumption in an Islamic economy) less than in a lower degree of equitable distribution. It is also reasonable to assume, with other factors remaining the same, that the degree of this effect, if the Zakat collected constitutes a certain percentage of the total income, will be less than if the Zakat collected constitutes a greater proportion of this income.

In any case, even if the level of aggregate savings is reduced because of zakat transfers, what is important is the effect of this on social efficiency. As long as this decrease is within the scope of justice in fulfilling the needs of all people in society under consideration and within the framework of moderation and fostering priorities, and achieves optimizing of saving in a manner that meets the needs of the future at a level equal to at least the level of meeting needs in the present, this decrease in the level of aggregate savings is in favor of achieving social efficiency where justice is a pillar of it.

The study of the consequences of Zakat on the option of consumption and saving requires that we address the issue of exempting “Oroud Al-Quanya”³ from Zakat; does this not encourage the option of spending on these “Al-Ourod” at the expense of the saving and investment option? The acquisition of “Oroud Al-Quanya” is a necessary need, and therefore spending on them, even if affected by their exempting of zakat, it is spending on a real need, it is also assumed that the Muslim is committed to moderation in meeting needs. And fulfilling needs within the framework of moderation and fostering priorities are at the heart of efficiency in the Islamic economy.

Section 2

7. The Ability of the Islamic Economic System to Achieve a Fair Return for Monetary Capital Which Finances Economic Activity, in the Absence of Interest

In the traditional economy, distribution justice is achieved concerning the cash capital which participates in economic activity, according to the marginal productivity theory of distribution, if the capital gets the value of its marginal productivity, in the form of a predetermined fixed return. As for the Islamic economy, at the beginning of the period, a potential return on cash capital is determined as a percentage of the expected net profits. This ratio is determined in the “Mudarabah” market when the demand and supply of funds are equal in this market and in the context of general economic equilibrium. Then the actual return of cash capital is determined after the activity result is achieved, multiplying this percentage by the actual net profits of the activity in question.

The marginal productivity theory of distribution depends, within the scope of

³“Oroud Al-Quanya” in jurisprudential terminology, is the confinement of money for use, not for trade, and Oroud Al-Qnya, everything other than gold, silver, and cash, that taken for use, not for trade.

justice, that it achieves the principle that cash capital (as well as other factors of production) gets the value of its contribution to the production process; and this principle is consistent with the teachings of justice of Islam but does the applying of this theory, in Its reality in the capitalist economic analysis, achieving this principle? To answer this question, we begin by referring to the difficulties surrounding the determination of the in-kind marginal productivity in reality, and we provide analytical observations:

First:

To say that cash capital gets the value of its marginal productivity is an inaccurate statement that involves fallacies. The productivity that is achieved is the productivity of in-kind capital, not cash capital. It is true that cash capital is used to obtain in-kind capital, and therefore its productivity can be attributed to it, but the saying neglects the risks involved in the decision to convert cash capital into in-kind capital and then convert it back into cash capital. From that the risk of a decrease in the value of the in-kind capital or its technical obsolescence, and this statement also neglects the role of making this decision and other entrepreneurship decisions (the role of the entrepreneur) without which the productivity of the cash capital will not be achieved. Also, to determine the net capital productivity value the value of capital depreciation must be deducted and the maintenance and operation expenses.

Second:

From the analysis of the production function, the total output is the result of a combination of production factors, under a specific production technique' and hence the marginal productivity associated with the change in the quantity of a particular production factor, with the assumption that other things remain constant, this marginal productivity cannot be accurately said that it is the result only of the factor whose number of units has been changed one unite. But accuracy requires that we say that the change in the total product has resulted from the change in the amount used from the variable production factor within the framework of a specific proportion between the factors of production. That is, marginal productivity does not, in fact, reflect the contribution of the variable factor to the product, but rather the relative scarcity of the factor in the combination of factors of production (Hassan Zubair, 1983).

Third:

The dependable factor in calculating the return is the value of the product, which is the outcome of multiplying the product's quantity by the sale price per unit. If it is possible, to a large extent, to determine the amount of the in-kind product, then the matter is not so concerning the selling price, which will not be known with certainty except after operation, and production actual sale; and therefore the value of the total product is necessarily probabilistic, and the value of marginal productive for each factor involved in the total production is also probabilistic. So even if we accept that the marginal capital value of the cash capital reflects its contribution to the production process, this value is by its nature is probabilistic value, because it is only realized after a certain period which is, in

production, period of establishment, producing and selling, and therefore this value is necessarily subject to conditions of not certainty.

Thus, the marginal productivity theory, as a basis for calculating the justice return of cash capital, may not accurately reflect the fact of its contribution to the production process and the achievement of its outcome. And therefore, it may not achieve the requirements for equitable distribution.⁴

Likewise, the analysis of the opportunity cost shows that the return of cash capital, in its alternative uses in economic activity, is a potential return and is common with entrepreneurship. Capital in its monetary form does not generate a return but a decision is required to convert the cash capital into some form of investment use that allows the possibility of achieving a return for it. This process inherently implies a degree of uncertainty associated with the use of cash capital in economic activity. It includes transferring the cash capital to other forms that are less liquid and then returning it to its liquid form. It also includes, in the fact, that the result of the activity in which the cash capital is used, after its conversion, is achieved after a period during which the circumstances surrounding the activity in question may change unpredictably, this is in addition to exposure to predictable risks and that makes the return of using cash capital a potential return that requires the synergy of entrepreneurship efforts with it, and this is the characteristic of the return of cash capital in the income-generating use.

This was clarified concerning investing in partnership with others in the field of production, as it was clear, also, in our analysis of Al-Mudarabah in the field of trade, and it can also be evident from the analysis of the direct investment. Let us suppose that the owner of the cash capital invested it directly in conducting commercial operations. In this case, the need arises to make decisions regarding the form and size of the commercial activity, and the capital is transferred from its cash shape to less liquid assets such as goods and services. The result of the activity is not achieved until after a period that is necessary for the establishment of the project, and the period between buying and selling, with the exposure of a degree of risk and uncertainty involved. In this case, the owner of the cash capital will have played the role of the entrepreneur and alone bear the risks and uncertainties involved in the activity that he engages in; hence he will receive the whole profit which in this case consists of a functional return and a risk-return for both the capital and the entrepreneurship.

⁴The point of attention when it comes to distributive justice differs from it when it comes to choosing the production technique. When choosing the production technique, the focus of attention is that a certain change in the output accompanies a certain change in the amount of a particular production factor while keeping the other factors constant, regardless of the real reasons for the change in the output. As well as the cost of each production factor is taken as a given when choosing the production technique.

Concerning the fairness of distribution, the focus of attention is the analysis of the real causes of the change in output when the amount of the production factor under consideration changes by one unit, and the analysis of the nature of the return of monetary capital in the return-generating use Is it a probabilistic return or a fixed return that is predetermined?

Even in cases where the owner of the cash capital can obtain a predetermined return, such as buying a machine and renting it to others in exchange for a constant fixed agreed return, the final return for it is also probabilistic, and it also requires entrepreneurship efforts. That is, when the owner of the cash capital, transforms his capital into an in-kind capital and rents it for use in a specific activity, he has made an entrepreneurship decision and bears the risks involved in this decision of converting the capital to a less liquid form and the risks of technical obsolescence, which can be reflected on total return achieved over the life of the machine, in addition to deducting the machine's depreciation costs from this return.

The conclusion that we can conclude is that the return on cash capital, in the yield-generating use, is a potential return and is common with entrepreneurship efforts. Considering this, the Islamic economy could be in a better position, in this respect, in terms of justice distribution. In the capitalist economy, interest, as a fixed and predetermined return, may not be in line with the probabilistic and common nature of the return of cash capital. If we concede that the interest can reflect the average justice proportional share for cash capital from the expected net return on investment, in a way that achieves a justice division of this return between capital and entrepreneurship; how can that justice be achieved if the actual return on investment differs from the expected return, by increasing or decreasing? Why, in the circumstances of uncertainty associated with economic activity, a fixed return is determined for cash capital from a probabilistic return in its nature?

The truth, in our mind, is that these questions have no place in the Islamic economy. In this economy, and under the participation mechanism, it is conditioned for both capital and entrepreneurship, at the beginning of the period, a relative share of the expected net return of the activity in question, while each of them gets, at the end of the period, this relative share of return, but is calculated based on of the actual net return, and not the expected, which is consistent with the nature of the return of cash capital in terms of being a potential return, and common with the entrepreneurship effort. Thus, the participation mechanism may be more capable than the fixed interest mechanism in achieving distributional justice concerning the return of both cash capital and entrepreneurship.

Research results:

We can suggest, within the framework of the Islamic system's value judgments that are reflected in its concept of efficiency and justice, that:

- 1) The Islamic Economy can achieve the goal of maximizing the growth rate of output in the absence of interest.
- 2) The Islamic Economy can achieve a fair rate of return for monetary capital that finances economic activities in the absence of interest.

Conflicts of Interest

The author declares no conflicts of interest regarding the publication of this paper.

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Appendix No. 1

The Concept of Resource Allocation Efficiency in the Islamic Economy

It is known that the concept of resource allocation efficiency in the traditional economy includes achieving:

- 1) Static efficiency, that is, achieving the maximum possible amount of product from a certain number of available resources, provided that this product is a preferable combination.
- 2) Dynamic efficiency requires that the economy achieves an optimal expansion across time.
- 3) Distributional efficiency, that is, the income distribution associated with the achieved product is fair.

This concept of efficiency is applicable in all contemporary economic systems at this level of abstraction. But if we move to a lower level of abstraction, the matter may differ from one economic system to another as a result of the difference in concepts of a preferable combination of products, the optimal rate of growth, and the fair distribution of income, because these concepts are determined within the framework of value judgments, that lead social preferences and may differ from one economic system to another.

Likewise, the prices that on the basis of the alternatives are arranged in the selection are not sacred or have a purely objective structure that is not affected by value judgments, but rather this structure is necessarily affected by the value judgments through the effect of these judgments on the behavior that lies behind the supply and demand tables that prices are determined by their interaction.

From this previous definition, economic efficiency assumes the presence of alternative uses of a particular thing and then chooses the alternative that achieves the best possible result, that is, there is a behavioral process that includes a choice among the options that result in the allocation decision and aims to make the best decisions. Value judgments play a role in guiding human behavior in the selection process and defining the best choice concept.

It is supposed that human behavior is framed in Islam by the Creed and Sharia of Islam, and this behavior, when framed by that, becomes rational behavior.⁵ Thus, human behavior, which controls the process choice, is framed by Sharia and derives criteria of what is best for the result of the allocation.

It is supposed that production is applied to fulfill legitimate needs moderately and according to their priorities across time. It is also supposed that the evaluation of fulfilling needs is achieved by the care of legitimate priorities in the first stage and an individual one in a later stage. In the first stage, the allocation is done between spending in the present and future on one hand, and then among the groups of necessities, semi-necessities, and improvements, according to their

⁵This is based on numerous pieces of evidence, including verses from the Holy Qur'an, numbers 186 and 256, Surat Al-Baqarah, and 146, Surat Al-A'raf.

priorities. In this stage, the criterion of allocation is mainly⁶ represented in the legitimate obligation by limiting the choice in the halal circle and using the criteria of legitimate priorities, moderation, and balance between the present and the future within the framework of income as it represents the ceiling of available capacity. In a later stage, allocation takes place within groups, and at this stage, individual preferences and relative prices can play a key role.

Thus, there is a major role for the priorities derived from the purposes of the Sharia: moderation, and balance, and in general the legitimate obligation, along with the level of income, about determining the main ratios in individual spending, as well as on the level of the economy as a whole, not only in the present but also in the allocation between the present and the future as well. Then in a later stage, which we might call the Sharia neutrality stage, the choice among alternatives within groups can be influenced mainly, in addition to real income, by relative prices and individual preferences.

Thus, the difference between the concept of efficiency in the Islamic economy, as we see it, and the concept of resource allocation efficiency in the traditional economy is, in fact, in the concepts of the words “preferred”, “optimal, and” just “, which are mentioned in the definitions of static, dynamic, and distributive efficiency. These words mean value judgments in the light of which criteria for evaluating allocation behavior are determined, and hence the difference between the concept of resource allocation efficiency, as presented by the author, and the concept of resource allocation efficiency in traditional economics, is a difference in value judgments.

The criterion of what is “better,” “optimal,” and “fairer,” meaning the criterion of efficiency in the traditional economy is that a person does whatever he wants with his wealth, and it is a saying that means that the individual is the source of value judgments. The allocation process and this is the case, does not answer an important question: Are the utilities which subject to maximization the first utilities among all the utilities? or are they only the utilities that have the ability to pay? Failure to answer this question means in some way ignoring the issue of fairness of distribution.

Whereas in the Islamic economy, as we see, the criterion for this preference, idealism, and fairness is derived from Islamic Sharia and is determined considering the criteria of justice. So, the evaluation of the outcome of the allocation process is not entirely left to the individual preferences, but rather these preferences are within the framework of justice criteria. This is reflected in the fact that the allocation behavior, in The Islamic economy, is driven by two mechanisms, instead of one mechanism, which is the mechanism of maximizing the return of commitment to Sharia, and within its framework, the mechanism of maximizing the legitimate utility operates, which makes distribution fairness a criterion of efficiency, not an economic policy goal that may conflict with con-

⁶Because changes in prices can play a role in this stage of allocation if they are in such a way that they have an impact on the real income, which represents the ceiling of the ability in the allocation.

siderations of pure efficiency.

In this regard, and at this lower level of abstraction, we can suggest the following about the concept of efficiency in the Islamic economy, a proposal that has its Sharia rooted:

1) Justice in Islamic economics, unlike traditional economics, is an internal variable in the efficiency system that works on the combination of output and the decision to save and invest.

2) Justice is represented in that allocation achieves the level of sufficiency for all members of society, and this is considered a condition for achieving efficiency in the Islamic economy. Efficiency does not only mean maximizing the satisfaction of needs but also includes the scope of these needs. Reaching a situation in which it is not possible to improve the situation of some without putting others in a worse situation, which is known as the Pareto optimization, can serve as a criterion for judging efficiency in Islamic economics if the Sharia rulings related to the acquisition, use, and spending of money are applied in the economy under consideration, and if the concept of “improving the situation of some” is defined in the framework of achieving sufficiency, and the concept of “the worst situation” is harming achieving sufficiency by decreasing it. This gives us a guide concerning economic policy: if the transfers are made from the surplus of people’s money, it does not affect their sufficiency and are given to others to complete their sufficiency, then these transfers would improve the position of efficiency in the Islamic economy, and this is by assuming that other factors remain the same.

3) Likewise, the criterion for saving optimizing, at the individual and macro levels, is fairness in meeting the needs between the present and the future, in a manner that considers changes in income and needs as well as considers the interests of the generations in succession. Justice in this regard is represented in meeting the needs of the present and the future in a framework of moderation and taking care of the priorities in light of the income and data of each period so that the level of consumption in the future is greater or equal to the level of consumption in the present. This does not negate the possibility of a role for the rate of return on savings, but it is a role governed by the criterion of justice in meeting needs. This criterion can provide us with a guide about the economic policy when evaluating its consequences on saving (Abul Fotouh Nagah, 2022).

4) In Islamic economics, it is possible, for economic policy purposes, to build structures for social priorities guided by the five objectives of Islamic law, including the preservation of religion, soul, offspring, money, and mind, and based on the degree of their importance in serving these objectives, and this can provide us with a guide for the economic policy concerning investment options.

5) The return of Islamic economic activity that is intended to be maximized is not only a financial return, but in addition to the material return there is also a

non-material return represented in the feelings of satisfaction that Muslim senses when he adheres to what God enjoined upon him in the economic field, and we call it “the return of commitment”.