

MORALITY & ECONOMICS

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الحمد لله والصلاة والسلام على رسول الله، وآله وصحبه وسلم.

Excellencies, scholars of economics and Shari'a, and all distinguished guests,

On behalf of the IAIE, I welcome and greet you with Assalamu alaikum. I thank the IDB Group and IRTI for their continued partnership with IAIE in this conference. I also thank the Qatar Foundation and its Faculty of Islamic Studies for their gracious sponsorship, hospitality and clockwork organization. I welcome SESRIC as a new partner. Special thanks to each and every sponsor.

The IAIE was created to construct a new branch of economics, namely, Islamic economics that provides an integrated analysis of economic activities under the adherence to Shari'a, a moral structure, based on belief, as well as the institutional structure of the Islamic economic system. Economics has two schools of thought in methodology. The positive school claims that analysis should be void of ethics in order to remain unbiased. Ethics come only in the development of economic policies. The normative school recognizes the impossibility of isolating analysis from ethics. Islamic economists belong to the normative camp.

The proponents of the normative school includes Joan Robinson, who objected to the analysis based on pure utilitarianism, the claim to the invisible hand, and supported the call by Kenneth Arrow, to adopt a moral obligation.

Positive analysis assumes free markets, laissez fair and utility and profit maximization. Homo-economicus is selfish and utilitarian. I have heard Kenneth Baulding say he would not marry his daughter to such a man.

Economics was never devoid of ethics from the beginning, as it adopted utilitarian values and selfishness, which lead to the conflict and rivalry, with the extremely rich on the one hand and the extremely poor on the other.

If we take into account that economics is a social science, that studies the behavior of individuals toward the phenomenon of scarcity, and concludes that good allocation of resources is the safest way to deal with this phenomenon, then human behavior cannot be isolated from the moral boundaries by going inside.

It is interesting that James Alvey the economist from New Zealand reminds us that the economics is part of the philosophy of ethics, and reinterprets Adam Smith and Western economists before the twentieth century, as advocates of moral economics. Economists' rejection of ethics during the twentieth century is not consistent with its history, and development of normal development. It is an

attempt to mimic natural sciences and their use of mathematics. Nonetheless, natural science deals with matter, while economics deal with human behavior.

As an example of the connection between economics and ethics, Jacqueline Best and Wesley Widmaier point to the division of economics into two branches: microeconomics and macroeconomics. The former focuses on the interest of the individual and the latter on the interest of society. The classical analysis focuses on the interest of individuals and the single state alone, while Keynesian analysis focuses on policies that promote the social interests that exceed the sum of individual interests.

A number of modern economists have addressed the absence of ethics from the analysis. Others have constructed monetary measures of the ethical factors considered by agents, e.g., Joseph Eisenhower. Others, such as Freitas and Wagner, resorted to the development of models of economic behavior that include ethical aspects, The methodology of Islamic economics focuses on providing economic analysis under the provisions of moral obligation derived from the Shari'a, as formulated by former scholars, such as the judge Abu Yusuf, Ibn Abidin, Al-Shatby, Ibn Taymiyah, and al-Ghazali, which they deducted from the founders of schools of Islamic jurisprudence.

An example of combining economic analysis and moral judgments can be drawn from monetary and financial

economics. Muslims believe that lending at a rate of interest implies great injustice to the individual and society. Islamic economists came to provide the detailed analysis, and to put the economic rationale of ethical behavior. Interest-based lending deprives individuals and communities from seven important economic advantages.

The first is that Islamic finance, unlike conventional finance, does not encourage people to substitute real resources for money in transactions in order to maximize their interest income, which reduces production and dampen economic efficiency. This means that Islamic finance is more capable to achieve efficiency.

The second is an Islamic financial institution should be more stable, because it does not guarantee payment of principal and interest on the liability side as does the conventional financial institution, and thus shocks on the asset do not lead to shocks on the liability side that could demolish the financial establishment.

The third is that the debt resulting from Islamic finance is paralleled by delivery of goods and services. Such debt is not subject to increase nor is it negotiable. There is no integrated debt market that works as a source of instabilities caused by movements of hot money, and carriers of the contagion from one country to another. Besides, Islamic finance does not cause inflation, because it finances both supply and demand in parallel.

The fourth is that Islamic finance offers mostly partnership or delivery of goods and services, and does not provide funds to borrowers. It is therefore less subject to information asymmetry and consequently to risks of adverse selection and moral hazard than conventional finance. Exceptions are Mudaraba and Wakala, which must be mixed with other finance modes, to minimize such risks.

The fifth, is that conventional finance can be likened to spectators games such as football, where a small group of professional players are active in the field, while a crowd of spectators watch from outside. This fragments the national economy, exposing it to collapse. Meanwhile, Islamic finance is like participatory sports such as cross-country race. Everyone plays and no one watches.

The sixth is that Islamic finance contributes to the achievement of social justice directly through the collection of Zakah on shareholders' funds, and charity from donors, and giving them to the needy. It stands ready to be a repository of Zakah, and entrusted to use part of the proceeds to finance micro projects for the poor. This makes Zakah a tool for economic development and social justice at the same time.

The seventh, is that Islamic finance is more sustainable. The value of its resulting debt is fixed at the time of sale finance, and is not subject to penalty interest due to insolvency, but rescheduled without any increase. In contrast, interest-based debt, increases in value by compounding interest, and by

exuberant late payment fees, forcing the debtor to seek aid or bankruptcy.

Money is a social institution that owes its existence to general acceptability casted by members of society. It is not right morally or logically that a person lends money to another at an interest rate. Monetary authorities should not allow banks to create money and lend it, under the fractional reserves, for this confiscates the right of society to benefit bank shareholders.

Islamic economists have pulled economics from the pit of individualism and selfishness and brought it to the wider sphere of social sciences, which take into account higher ethical values. Islamic economics starts with the Maqassid, derived from Islam and introduces them to macroeconomics. Then it ties the results with human behavior in microeconomics. To the contrary, conventional economics start with the individualistic and selfish objectives of humans in microeconomics, and then link them to macroeconomic analysis.

Islamic economists have criticized the superficial treatment of the global financial crisis. The main source of the problem is conventional finance, i.e., trading money for money, coupled with the transformation of financial markets to gaming casinos. Insolvency cannot be confronted with pumping money into banks to protect them from collapse. Banks hoarded the money they got for fear of increased risk, leading

to recession. Instead, it would have been better to directly help the insolvent to pay their dues to the banks, so they can continue in production, earning and spending. This way, the economy does not become stagnant. Instead of rebuilding economic institutions on bold new bases, to rid the banking system from interest-based lending and to bring back financial markets to their original function of fund mobilization for enterprises, they prescribe only, limited tighter controls on lending. Thus, they have wasted an historic opportunity to reform the global monetary system.

To conclude, economics began as a social science intertwined with ethics, then attempts have been long to separate them, but it was absurd, because it did not achieve absolute impartiality, but committed to economics to utilitarian ethics and selfishness. And then, a group of economists worked on helping economics to rein still ethical principles in the analysis. Islamic economists provide a genius example of building the economic analysis on the ethical principles of Islam.

Sharia scholars have taken the lead in formulating the ethical rules of Islamic finance. Islamic economists, through economic analysis, providing many examples of morally defective transactions, based on their economic consequences, for example:

Any transaction that amounts to the sale of money for money, like Tawarruq and 'Eina. Such would be a ruse to circumvent the prohibition of usury.

Sale of monetary debt for a value that differs from its nominal value, as it would be a sale of money for money.

2. Finance trading in securities for the purpose of speculation (not investment), the treatment of defective, causing immeasurable harm to the economy.

3. Finance that exceeds the capacity of the customer to repay would lock him into debt for life.

4. Funding that encourages conspicuous consumption, extravagance and luxury.

5. Funding luxuries before basic needs are met.

6. Funding of anything that harms all living organisms and the environment.

Thank you for your attention,

والسلام عليكم ورحمة الله وبركاته.