

POVERTY ALLEVIATION, DEMOCRACY AND INSTITUTIONAL  
REFORM IN ISLAMIC COUNTRIES

BY  
MURAT ÇİZAKÇA  
FATİH AND BOĞAZİÇİ UNIVERSITIES  
ISTANBUL

**Introduction:**

The relentless hostility and the ever widening cleft between the secularists and Islamists in countries like Algeria and Turkey, has created a most difficult situation. While one of the hostile camps believes in the total rejection of our traditional institutions, the other one wishes to return to the pristine origins. I would argue that both of these policies are wrong. What the Islamic countries need, is a complete re-ordering of the institutional matrix that would both meet, head on, the economic and social challenges imposed by the contemporary modern world, and also at the same time, be in harmony with the basic teachings of Islam.

In this paper, I wish to point to some of the characteristics of such a system. The two most important constraints of the system are the market efficiency and harmony with the basic teachings of Islam. Efficiency is absolutely necessary if these countries are to survive the ruthless competition imposed by Western capitalism and achieve sustained economic growth. Harmony with Islam is needed for the new system to obtain the approval of the masses. This also implies a democratic system within an Islamic framework. In short, democracy, market efficiency and harmony with Islam constitute the pillars of this new institutional framework. It will be argued here that it is this particular institutional framework that is best suited for poverty alleviation in the modernizing Islamic countries of today. The basic specific outline of the institutional framework will also be presented.

**1. Why Democracy?**

Nearly all the developed countries in the world with more than \$ 15.000 GNP per capita are democracies. If we look at the statistics from the perspective of economic freedom, all the top income countries enjoy high levels of economic freedom. Therefore, it would not be wrong to argue that democracy and economic freedom are strongly related to successful poverty alleviation. This impression is confirmed by another finding which has yielded a strong correlation between *the Average Growth Rate of Per Capita GDP* and *Economic Freedom Grade*: put differently, not only are those countries with the highest rates of economic freedom already rich, they also get richer the fastest. Indeed, whereas countries, which get an A from economic freedom have succeeded to grow by an average of 3.3% in the period 1980-1994, those which score the lowest in economic freedom, have experienced *negative* growth in the same period. Our countries, Algeria and Turkey, both do badly: whereas out of a ranking comprising 102 countries, Turkey is 70th, Algeria occupies the 100th position (Gwartney and *et.all.*, 1996).<sup>1</sup>

Since after the liberal Özal reforms, Turkey has reversed its economic policy, there is no doubt that it must have fallen to lower levels. Put differently, I would like to argue that just as an improvement in democratic performance and economic freedom leads to faster rates of economic growth, a deterioration of these criteria also leads to a poorer growth performance. The increased military interference in public life in 1998, has been definitively followed by poor economic performance. It cannot be a mere coincidence that the Republic of Turkey is experiencing the second worst economic crisis of its 78 years of history. The Turkish economy experienced negative growth in both 1999 and 2001. The annual GNP growth rate in the second quarter of 2001 has collapsed to a shocking -11.8%.<sup>2</sup> Thus, there is no doubt that Turkey's position in Gwartney's index has substantially deteriorated since 1998.

As implied above, the linkage between democracy and economic freedom is not a straight forward one. This is because, certain countries in East Asia (Hong Kong, Singapore, Malaysia and Thailand) have achieved high levels of economic freedom without becoming full-fledged democracies. If we disregard these special cases, however, of the top ten countries with the highest grades of economic freedom, six are functioning democracies. These six functioning democracies, New Zealand, USA, Switzerland, the UK, Canada and Japan are also among the richest countries of the world.

Among the special cases of the Pacific rim, the first two, i.e., Hong Kong and Singapore, though not full-fledged democracies, are controlled by merchant oligarchies and enjoy very high rates of economic freedom (Gwartney and *et.al.* 1996: xx). Other successful examples of small city-states governed by merchant oligarchies have also been observed in European history. The so-called Italian quadrilateral, Venice, Milan, Genoa and Florence as well as others in Flanders constituted the richest zones of medieval/late medieval Europe. These historical examples from Europe share the following trait with the modern city-states of the Far East: in each, the state was (is) controlled by merchants, who insist on economic freedom. The result is once again economic growth.

To sum up, most of the richest countries of the world are functioning democracies, which also enjoy very high rates of economic freedom. But some countries of the Pacific rim have successfully penetrated among the ranks of these countries by establishing economic freedom without, however, achieving full-fledged democracy. Thus, economic freedom emerges as the *conditio sine qua non* of poverty alleviation or economic growth. The implication for Islamic countries is clear: economic freedom must be established. The question is whether we should do so by also establishing democracy or without it. In this paper, I shall argue for the former due to the following observations.

Besides this very strong correlation between economic development and democracy, there are also other very important merits of democracy. Political scientists, for instance, have observed that democracies never fight wars against each other. In such countries the political process to declare war is so difficult that a democracy does not expect a surprise attack from another democracy nor does it declare war easily on another democracy. Since the battle of Waterloo in 1815, all the wars that took place were between non-democratic countries or between democracies and non-democratic countries. In this period of 175 years, there has been no war between a democracy and another democracy (Ahlmark, 1998-1999: 187-189).

Famines are also not observed in independent and democratic countries. Moreover, this observation applies not only to the rich democracies, but also to the poor ones. Famines occur either in colonies or in non-democratic dictatorships. The worst famines of our times occur in

Sudan and North Korea, both of which are dictatorships (Sen, 1999). Democracies also create trust among the citizens by institutionalizing distrust (Sztompka, 1998 (a) and (b)).

Finally, democracies generate economic growth in the long run by achieving a faster evolution of economic institutions (Çizakça, 2001).

Thus, to summarize, democracies successfully avoid wars (at least among themselves) and famines, they generate trust among their citizens, and finally, they generate economic freedom and long run economic growth by allowing a faster evolution of economic institutions. Putting all of these factors together, it is no wonder that nearly all the most developed countries in the world are democracies. In view of all this, I argue that modern Islamic countries should aim at establishing democracies if they are to alleviate poverty.

## 2. Islam and Democracy

The problem in this statement, however, is that there is not a single Islamic country in the world that can be called truly democratic. Indeed, some of the most important Islamic countries today, i.e., Algeria, Turkey, Egypt and Indonesia are all governed by secularist elites who fear that true democracy would simply bring Islamic fundamentalists to power and that, once these groups come to power through elections, they would "hijack" democracy and quickly revert to an Islamic dictatorship. The implicit assumption here is that Islam and democracy are incompatible and that liberal democracy in Islamic countries would simply lead to Islamic dictatorships. We will now examine this assumption and look at the relationship between Islam and democracy.

First of all, we need to address the observation that none of the Islamic countries in the world is a full-fledged democracy. Is this fact, however, due to an inherent incompatibility of Islam with democracy or, rather, due to specific historical circumstances? We will address this question first by examining the relationship between Islam and democracy and then by briefly looking at history.

In this context, the first thing we note is that Islam has a negative view of dictatorship. This is because, Muslims who believe in the unity of God and his omnipotence, cannot easily accept a hierarchical society. A Muslim considers every other Muslim as his equal before God. If, on the other hand, men are equal to each other *vis a vis* God, then this implies a brotherhood of men and not a dictatorship. Sabri Orman reaches to the same conclusion via the prohibition of interest. As is well known, one of the purposes of the *riba* prohibition is to base economic life on partnership. The Qur'an sends us an implicit message here, which is this; if economy must be based on partnership, then the social life must be based on brotherhood. Put differently, a business life that is based on partnerships, is reflected on society as a community that is based on brotherhood. Thus, an Islamic economy must be based on partnerships and an Islamic society on brotherhood (Orman, 2000: 236-237). This view is also confirmed by the fact that a contract plays such an important role in Islam: just as a contract is the foundation stone of a business partnership, the contract is also the foundation stone of Islam itself. Indeed, the most basic relationship of Islam, that is the relationship between man and Allah is also considered as a form of contract (Al-Attas, 1995: 144-145). To sum up, in a society of which economy is based on partnership and its entire social matrix is based on brotherhood, citizens must enjoy equal legal status. That all the citizens of an Islamic society must be of equal legal status *vis a vis* each other is therefore normal and

rational. The leader's position in such a society is described as *primus inter pares*, i.e. first among equals. The person, who is the first among equals cannot enjoy this position forever. There must be a rotation and other brothers must also be given the chance to lead also. Therefore, in an Islamic society the categories of the leader and the led are not absolute but temporary (Orman, 2000: 236-237).

Moreover, since absolute sovereignty belongs to Allah, the next question we face is how to translate this to the political arena. Modern Islamic political thought solves this problem through the concept of chalifate. As it is well known, throughout Islamic history the chalifate was an hereditary office that was transmitted from father to son. With the abolishment of this office by the Turkish republic, however, modern thinkers of Islamic political theory came to consider chalifate not as a hereditary office but as an agency. Indeed, it is argued, if man is the most advanced creature of this earth, he is entrusted with the responsibility to take good care of this magnificent trust. Thus, mankind is seen as agents of God and the earth is entrusted to each individual or to the society in general. On the other hand, if earth is entrusted to each man, then men are equal in front of God. This is the starting point for Islamic democracy (Esposito and Voll, 1996: 26).

Entrusting not a single man but the whole society with the responsibility of Allah's agency is also confirmed by the Islamic Council of Europe (1980: 6). Consequently, the fact that the responsibility of agency is given to the whole society, renders all dictatorships in the Islamic world as void and illegal. This is because, a dictator who is ruling the whole society must face the question as to from where he is getting his authority. Put differently, does the authority to rule come from God or from the society? Modern Islamic political thought answers this question by arguing that the authority to rule comes from Allah but reaches to the ruler via the society. And the process by which this authority is transmitted by the society to the ruler is nothing but democracy (Binder, 1988: 135; Ramadan, 1993: 153). Consequently, according to these authors, those who assume the power to rule without going through the process of elections are not legitimate rulers.

Moreover, the *shura*, i.e., consultation that is mentioned in the Qur'an, has been misunderstood in history as the duty of the ruler to consult his ministers. It has been argued, however, that the *shura* that is mentioned in the Qur'an is consultation among equals. Therefore, those who disregard this and refuse to consult the entire society are, once again, illegitimate dictators (Rahman, 1986: 90-91).

Other traditional Islamic concepts being considered by the modern political scientists are the *ijma'a*, consensus and *ijtihad*, independent decision. As it is well-known, both are based upon Prophet Muhamad's *hadith*: "My community does not agree on wrong". But this *hadith* has also been misused and the right to interpret and to offer solutions to a social problem has been left to a select group, the *ulema*. This has meant that the interpretation of Islamic law to find solutions to social problems was given to the learned jurists rather than to the people themselves. Once the jurists, acting in splendid isolation, reached a consensus, the subject was over and a renegotiation of the problem was closed. The result has been a striking conservatism and rigidity of law in a vast Islamic community that faced ever changing circumstances and challenges. By contrast, in some Western societies the right to interpret the law was given through the parliamentary system to the people themselves. The result was a highly sensitive body of jurisprudence to the actual problems faced by the population. There is no doubt that parliamentary systems created jurisprudence that allowed a much faster rate of institutional evolution. Since institutional

evolution is considered to be the most important factor leading to economic growth (North, 1999), it has been argued that the sluggishness of Islamic law in responding to the challenges and the resulting stagnant rate of institutional evolution are directly responsible for the poverty of the Islamic world (Çizakça, 1996; Çizakça, forthcoming; Kuran, 2000).

Already during the 1930s Muhammad Iqbal had been writing that the authority to exercise both *ijma'a* and *ijtihad*, should be taken away from the *ulema* and be granted to the people themselves, i.e., to the parliament. The conclusion reached by Iqbal and a host of other twentieth century Islamic political scientists is that a republic governed by parliamentary democracy is the most suitable political system for an Islamic community (Esposito and Voll, 1996: 29). Therefore, the secularist argument that if Islam comes to power through democratic means it would hijack democracy is baseless. This does not mean, however, that such hijacking is never going to happen. It simply means that if it does happen, the hijackers would violate not only democratic rules and basic decency, but also the basic Islamic principles.

Thus, having established that Islam, as such, has no objection to democracy, we must now explain why it is that full-fledged democracies are all in the West and that there is not a single genuinely democratic Islamic country in the world.<sup>3</sup> This is a more a difficult task, as it involves delving deep into the history of democracy in the Western world. Obviously volumes can be written on this subject and this is not the appropriate venue to discuss such complex historical phenomena.

But just a few brief observations can be made. First, sustained democracy<sup>4</sup> developed in medieval Western Europe under special circumstances. These circumstances and the institutions that emerged to deal with them were highly specific to Western Europe (Tierney, 1982 and 1996, Çizakça, forthcoming). Vast regions of Europe remained outside the democratic system. But a cross-cultural borrowing of democracy has been proved possible. This is demonstrated by the fact that not only many previously non-democratic Western European countries such as Germany and Spain but also a Pacific country like Japan have successfully democratized. Moreover, Eastern Europe, recently released from the Soviet system, is also successfully democratizing.

So, it is proposed here that the Islamic world can also borrow democracy. This would be, in a way, Western Europe's way of paying back for the institutions that it has borrowed from medieval Islam (Çizakça, 1994; 1996). The problem that the Islamic world faces in borrowing democracy is basically one of distrust, which originates from the fact that most modern Islamic societies are ruled by secularist elites who fear the masses. This situation has led to a path dependency out of which it is very difficult to escape. This is because, a minority supported by a powerful army can hold on to power indefinitely against the masses.

Historical studies have discovered that such conflicts can best be solved through elite settlements. Elite settlements occur when rival groups in a society suddenly and deliberately start reviewing their relationships *vis a vis* each other and decide to agree on some basic issues. Such settlements are rare in history but when they do happen, they profoundly and radically change the societies by leading them to genuine democracy.

Moreover, such elite settlements appear to be *conditio sine qua non* for the successful establishment of democracies. That is to say, even in a society where most conditions for democracy have been satisfied, a failure to reach to a settlement among the elites leads to democratic failure. This has been painfully confirmed by Turkey, which had allowed in 1946 several political parties and successfully transferred power from the leading party to the

opposition in 1950. Thus, having satisfied some of the most obvious criteria, Turkey seemed well on its way to full-fledged democracy. Some well-known political scientists had even declared that the country had successfully become a full-fledged democracy (Rustow, 1970). To Rustow's intense embarrassment and everybody else's disappointment, shortly after his article was published the military took over! What had gone wrong? According to Burton and Higley, Turkey had attempted to become a full-fledged democracy without reaching an elite settlement. Therefore a democratic failure was inevitable (1987: 303).

If Burton and Higley are right and an elite settlement is indeed a *conditio sine qua non* for reaching full-fledged democracy, how then an elite settlement can be achieved? A careful study of the successful elite settlements in history has revealed the following characteristics of these settlements:

- a. The rivalry and conflict among the elites must have continued for a long time prior to the settlement, leading each elite to desperation and the conclusion that it cannot win.
- b. A major crisis looming on the horizon, often acts as a catalyst to bring together the rival elites.
- c. Once the leaders of the rival elite groups decide to settle their differences, they do so relatively fast. All the successful settlements in history have been concluded at less than a year.
- d. Initial settlements do not occur between the groups. First, the leaders come together, often secretly, and after reaching an agreement, seek to persuade their groups. This is the most difficult part of the process as each leader is immediately accused as a traitor. Consequently, only individuals with great leadership qualities can achieve such settlements.
- e. Once the settlement is reached this is documented officially.
- f. Even if all the above are fulfilled, it is absolutely necessary that each group adheres to the conditions of the settlement. Cheating by any group quickly destroys the settlement.

Elite settlements in Algeria and Turkey, if they are to take place at all, may be expected to occur among the moderate Muslims and the secularists. Turkey is in a more advantageous position in that there is a consensus in the country to join the European Union. Consequently, both elite groups are under pressure to reach an agreement. To reach such an agreement, however, both groups need to review their positions and reinterpret some principles, which they have long believed in.

Let us now assume that elite settlements have taken place and the rival groups, that is, the secularists led by the armed forces and moderate Muslims<sup>5</sup> have agreed on the basic features of the democratic process. This means that the armed forces would not interfere in the elections and accept the decision of the electorate. We can assume that free elections in both Algeria and Turkey would bring Muslim democrats to power. These, on their part, must accept that once in power, they would obey the democratic rules and agree to leave the government in the next elections if they are not successful.

The next question that comes to mind is the basic structure of a concrete program to be pursued by moderate Muslims in order to come and stay in power. We will focus on this question in the remainder of this paper. I will argue here that the program to be pursued by Muslim democrats should fulfill the following conditions:

- a. The program should not contradict the basic teachings of Islam. Failure to do so would lead to serious legitimacy problems. But the program should also not try to implement the Qur'an literally. What is needed is a modern and dynamic program that is *inspired* by the way the Qur'an and the Prophetic traditions have solved the problems of the seventh century Islamic community (Rahman, 1984: 19, 20).
- b. Muslim democrats need to incorporate the basic concerns of the secularists into their program. This is necessary both to win the elections and to comply with the conditions of the elite settlement.
- c. The program must be dynamic and meet modern economic challenges. The most important economic target of the program must be to eradicate poverty.
- d. In the case of Turkey, the program should also be in harmony with the goal of joining the European union. Failure to do so, would deprive the party of secularists' votes.

Let us now focus on the main traits of such a program.

*Property Rights:* All modern economies and democracies respect property rights. Moreover, treating property rights with utmost care and respect does not contradict Islam. On the contrary, Islam considers property as one of the five values that a Muslim must protect.<sup>6</sup> Moreover, Islam imposes no upper limit to the amount of wealth that a Muslim can accumulate. The Qur'an confirms that wealth is not distributed equally among the mankind (3:14; 43:32). Yet, the way this wealth that can be accumulated by a Muslim without any upper limit is put to use by him, is regarded as a most important test. Wealth that is simply kept and hoarded without serving the mankind, is considered a great sin. Such wealth is sure to send the Muslim to the gates of hell (9:35; 10:58; 17:26). In short, while property earned through legitimate means is considered to be completely legal, using this wealth for the good of humanity is given great importance.

Both the state (59:7) and well-to-do individuals can redistribute wealth in the society. But while state action by imposing taxes is not emphasized, voluntary giving through *sadaqah* or the waqf system is greatly emphasized. Indeed, there are more than 50 verses in the Qur'an that emphasize the importance of voluntary giving. In short, Islam emphasizes the redistribution of wealth in the society but prefers that this is done on voluntary basis by private individuals, themselves, as part of their religious duty.

Concerning land ownership, a special but very important aspect of property rights, Islamic sources as well as Islamic economic history yield important information. We are informed, for instance, that both state ownership as well as private ownership of land are permitted. This is because, as it is well known, Chalif Omar did not follow the Prophet's *sunna* in land ownership: whereas the Prophet had definitively permitted private ownership of land, Omar established a more complicated land ownership probably influenced by Roman and Sasanid traditions prevailing in Mesopotamia. He was able to override the Prophet's *sunna* by basing his decision on the Qur'an (59:7) and arguing that the situation had changed.

Thus, since Islamic economic history informs us that Islam permits both state and private ownership of land, which type of ownership should a modern Islamic government prefer? A return to the system established by Omar would be out of question. There are several reasons for this. First, under intensive Western pressure during the 19<sup>th</sup> century, Omar's system was abandoned in most of the Islamic world and was replaced by private ownership of land. Thus, under democratic conditions, an attempt to return to that system would be tantamount to a political suicide. This is because, most lands are now privately owned and a return to Omar's

system would necessitate massive confiscations. Moreover, such a return would not be desirable also from the perspective of productivity. For, as comparative studies in agricultural economics have shown, private ownership of land is far more efficient than state ownership. This is confirmed not only by well-known comparisons of the American and Soviet agricultural systems but also by studies of the third world agriculture (Boyce, 1987).

In view of all this, the agricultural policy of Muslim democrats should be clear: They should opt for private ownership of land. This policy would be in harmony with the Prophet's *sunna* as well as the 20<sup>th</sup> century experience.

*Commercial Policy:* As it is well known, the Qur'an has permitted trade but prohibited *riba* (2: 275). Muslims are also ordained to put their wealth into good use and freely trade with it (4:29). It was Omar II, who, based upon these and other verses (14:32; 2:164; 10:22), established Islamic commercial policy formally. This commercial policy was based on free trade, whereby the state was not supposed to obstruct the free flow of goods by excessive customs duties or other means (Gibb, 1955: 1-16).

The preference of classical Islam for free trade, suits perfectly to the prevailing contemporary situation. Thus, the free trade agreements already signed and to be ratified in the future by both Algeria and Turkey with various European countries, do not contradict the basic teachings of Islam. Islamic economic history, however, warns us to be cautious about possible exploitation of free trade by others. Reference should be made here to the disastrous impact of free trade on Islamic countries when the Ottomans pursued a policy of free trade with the Europeans, while the latter practiced mercantalism. Thus, the free trade policy to be pursued by the contemporary Islamic countries should be based upon reciprocity. History warns us that when we practice free trade while others protect their economies, the result can be ruinous. This is confirmed by both Ottoman and Indian economic history (Çizakça, 1980; İnalçık, 1979-80; Rothermund, 1988).

*Labor and Industrial Relations:* What would be the characteristics of a modern system of industrial relations that do not contradict the basic teachings of Islam? First of all, we need to remember that Islam recognizes income differentials and confirms that while some individuals can be employers others will be employees (Qur'an, 43: 32). While establishing this, Islam ordains the employers to pay their workers market wages, *ajr al-misl*, promptly. Payments made to workers can be in the form of wages or profit shares or both. There is plenty of historical evidence that these principles were extensively applied by Islamic societies of the past (Çizakça, 1996).

Other more militant labor market institutions such as collective bargaining and strikes, however, are alien to Islam. The efforts of some leftist Islamic economists notwithstanding, such institutions are not accepted by Islam. The objection to such practices originates from the important role assigned to contracts in Islam. Once the employee and the employer mutually agree on the terms of a contract, and both parties adhere to these terms, third parties are not permitted to interfere. The implication here is that trade unions can act on behalf of the workers only through *vekalet*, i.e., agency or representation.

The preference accorded by Islam to a mutually agreed contract rather than militant labor market practices such as collective bargaining, or particularly strikes, should not surprise us. The importance attached to contracts is also attested by the very nature of Islam. Naquib Al-Attas has argued that even the most fundamental relationship in Islam, i.e., the position of a Muslim *vis a vis* Allah is a contractual relationship (1995: 144-145). Moreover, this contract assumes a personal responsibility and, in comparison to Christianity, goes much deeper. That is to say, whereas Jesus Christ can act on behalf of a good Christian and ask God for his forgiveness, a



Muslim is strictly responsible for all his deeds. If he violates the covenant, he pays for it and nobody, not even Prophet Muhammad, can act on his behalf. Thus, if the concept of contract plays such an essential role in the very philosophy of Islam, it is only natural that industrial relations should also be governed by it.

To sum up, a democratic Muslim government would leave the wages to be determined by the labor market. Moreover profit sharing schemes would also be encouraged. In a labor market where strikes and collective bargaining are discouraged, profit sharing schemes assume special importance. Let us now focus on these schemes. It will be argued here that profit sharing schemes would be particularly appropriate in an Islamic economy.

A worker's claim of the profit generated by his firm is based upon the *mudarabah* concept. *Mudarabah* is a capital-labor partnership between the principal, who provides the capital and the worker, who provides labor. In all Islamic partnerships profit is shared according to mutual agreement, while loss is shared according to the capital contributed. Based upon this, it was Sarakhsi who ruled that investment can be made not only in the form of cash but also as labor (Udovitch, 1970: 68). Moreover, it was also recognized that in such partnerships each worker would contribute different quality and quantity of work. Under these conditions, providing that profit and loss ratios have been determined and agreed upon by all the parties *ex ante*, a labor-capital partnership would be legal according to Islamic law. There is no reason why such partnerships already accepted by the classical jurists, should not be modernized and expanded into massive industrial partnerships comprising hundreds even thousands of workers.

It is interesting to note that Western economists are also interested in profit sharing contracts in the industry. These economists, concerned about chronic unemployment observed in Western societies, argue that if the workers were paid in profit shares or a mixture of wages and profit shares, rather than purely in wages, the employers would hire more workers. This is because while, in the long run, profit share firms equilibrate at excess demand for labor, standard wage firms equilibrate with zero demand for labor. Thus the characteristics of a share economy are the following:

- a) All compensation systems have the same long run equilibria.
- b) In the long run, share firms equilibrate at positive excess demand for labor while wage firms equilibrate at zero excess demand for labor.
- c) A share system maintains full employment while reacting to small disturbances. A wage system responds to deflationary shocks by creating unemployment in the short run (Weitzman, 1983 and 1984).

Thus, not only does the share economy lead to greater employment but these greater levels of employment would also be maintained in deflationary situations.

Unfortunately, the share economy model has not been perfected yet. Some of the major problems associated with it have been summarized by Ekkehart Schlicht as follows: First, labor may demand to have a say in management.<sup>7</sup> This would lead us to the Yugoslav model. Second, when the management wishes to hire new workers, as it should according to the theory, how would this affect the overall productivity of the existing workers? Existing workers may want highly productive workers to enter into the firm as this would enhance the overall productivity and hence increase the share wage of every worker in the firm. But, if this overall productivity is low, the productive worker would have little incentive to enter into this particular firm, which pays relatively little reflecting its overall poor productivity. So, there may be clash of interests. This

whole problem has been referred to by Schlicht as "lack of standardization of labor in a team context". And, it is precisely because of this problem that labor-centered ownership structures are not prevalent in market economies (Schlicht, 1997). The problem boils down to the difficulty of assessing the marginal product of labor and determining his corresponding share in the total profit generated.

To what extent the share economy model and its criticisms would be relevant within an Islamic framework, should constitute a special area of research. But, it is clear that this constitutes a promising area of research into which Islamic economists should also be contributing.

To conclude this section, in modern democratic Islam, labor may be employed in the industrial sector by market wage rates or by a system of profit sharing. Since collective bargaining and other third party interference is not allowed in Islam, a system of payments based upon profit sharing would be particularly appropriate. Thus, when the theoretical problems associated with this system are finally resolved, modern democratic Islam should be the very first to apply it.

#### *Financial Sector:*

As it is well-known, Islam has imposed the most stringent prohibition of the rate of interest.<sup>8</sup> Consequently, Muslim democrats will need to prohibit interest if they wish to be considered legitimate. The problem, however, is that no Islamic country, even Islamic dictatorships like Iran and Sudan, has been able to successfully eliminate interest from the economy. Even in history, during the classical age of Islam, there is evidence that interest was not completely eliminated despite the severity of the prohibition.

Thus, a much more realistic goal would be to reduce the prevailing rate of interest to the absolute minimum. This reduction, and not the complete elimination, should constitute the backbone of the economic policy of the Muslim democrats. This policy would be supported by both devoted Muslims as well as the secularists.

We can approach this policy from both macro and micro-economic perspectives. Considering the former first, a policy of interest minimization would necessitate a series of reforms in the economy. Prevailing interest rates can be reduced only when the government budget is balanced and the government borrowing is reduced drastically. With government borrowing reduced to a minimum and the government paying its debts regularly, purchasing a government bond would become a rational investment, as a result, bond prices would increase and the rate of interest would be reduced.<sup>9</sup> The most striking example of this was observed in England after the *Glorious Revolution*, during which, radical institutional reforms were made. These institutional reforms, primarily the establishment of the Bank of England and subjecting the king to stringent borrowing criteria, led to a renewed confidence in the ability of the state pay back its debts. This led to a massive inflow of capital from continental Europe to England, which increased bond prices and reduced rate of interest to a bare minimum despite the fact that the state was borrowing heavily to finance its wars (North and Weirgast, 1989).

The policy of reducing government expenditure to a bare minimum necessitates a massive process of privatization. The state would have to withdraw from all non-essential economic activities and production. Moreover, a withdrawal from industrial production would not suffice and the state would even have to withdraw from the service sector. This would be in perfect harmony with the basic teachings of Islam and Islamic economic history. The latter informs us that for centuries, the most essential services, such as health and education, have been provided in Islamic societies not by the state but by the waqf system (Çizakça, 2000).

Looking into the waqf system more closely, thus turning our attention now to micro and institutional economics, we note that waqfs finance and manage the most essential services in the

economy through private capital. Thus they achieve two goals simultaneously, by shifting the burden of service provision to the private sector they help reduce government expenditure substantially and by channeling private capital to the service sector, they redistribute wealth in the economy in favor of the poor. It might be noted here that withdrawal of the state from the service sector is already a fact of life in the West. This trend that has started in the USA is rapidly

spreading to Europe as well. In view of all this, Muslim democrats should aim at a massive waqf reform and eradicate all the factors obstructing the smooth functioning of the waqf system. To achieve this, both the centuries' long Islamic waqf tradition as well as the latest developments in the Western nonprofit sector should be taken into account. Knowledge for both is available (Çizakça, 2000; Salamon and Anheier, 1997; Salamon and *et.all.* 1999; *The Economist*, August 18<sup>th</sup>, 2001: 67-69).

Another institutional reform to reduce interest rates involves the banking system. This involves transforming the investment portfolio of the Islamic banks from one of *murabaha* dominated to a *mudaraba* dominated one. A successful policy along these lines would in fact transform these banks into venture capital organizations. Within the limited scope of this article further details cannot be given. It should suffice here to say that the conditions and the know-how as to how to achieve this reform are well-known (Çiller and Çizakça, 1989).

Finally, Muslim democrats can create another powerful financial institution that operates without the rate of interest thus reducing the need for interest in the economy further. A successful example of this institution can be found in Malaysia. Introduced, for the first time, by Ungku Aziz, the *Tabung Haji* organizes the annual pilgrimage. Those Muslims who wish to go to the pilgrimage must open profit sharing accounts with the *Tabung Haji* and they are permitted to go only if they have saved a certain substantial amount. From the day of the account opening until the maturity, the savings are invested in several projects and the profits are distributed proportionally to the capital contributed (Ungku Aziz, 1959). By the year 1990, the *Tabung Haji* had successfully collected from 1.7 million pilgrim candidates a total of 1 billion dollars. It was estimated that within the next ten years the number of pilgrim candidates would increase to 4 millions and their savings would reach 5.2 billion dollars (*New Straits Times*, 2 November 1990: 10).

To sum up Muslim democrats should approach the financial sector from both macro and micro perspectives. Their primary policy objective would be to minimize the prevailing rates of interest in the economy. Once this is declared as the primary policy objective, however, a series of institutional reforms must be carried out. Both the policy objective and the associated institutional reforms would be supported by the hulk of the population, Muslim democrats and the secularists alike.

*Taxation:* We have noted above that in Islam, redistribution of the accumulated capital is to be realized primarily by voluntary means. That taxation is given only secondary importance as a distributive tool, is revealed by the fact that the Qur'an specifically mentions only two taxes the *zekat* and the *jizya*. The former is a modest tax and the areas for which it can be spent is determined by the Qur'an and highly specific. Actually, even the fiscal nature of *zekat* is controversial. For, it is preferred that *zekat* should also be distributed voluntarily by the Muslims themselves. In any case, the fiscal nature of this "tax" is limited to the so called "collectors of *zekat*". The "collectors of *zekat*" constitutes only one of the eight categories of recipients and implies that the state can spend only one-eighth of the total amount of *zekat* collected and it can spend this amount only for financing the collection expenses. Thus, in short, the *zekat* would

provide a very modest revenue for the state. The other tax mentioned in the Qur'an is the *jizya* (9:29). But, this is a discriminatory tax designed to allow non-Muslims to keep their heads on their shoulders ! In an age when the residents of the occupied territories belonging to other religions were routinely massacred, the *jizya* was a highly civilized means of saving the lives of the conquered people against the payment of higher taxes. But, today, although murdering individuals for their religious beliefs is still observed in certain parts of Europe and elsewhere, applying discriminatory taxation is considered to be totally unacceptable.<sup>10</sup> Thus, the *jizya* cannot anymore provide a modern Islamic government with any revenue. If so, how can an Islamic democratic government finance its expenses ?

Most Islamic economists agree that the natural resources a country is endowed with can be exploited by the state. So, obviously, this would constitute a considerable income particularly for the oil rich Islamic countries. But for those not endowed with such resources, the situation would be quite challenging. Faced by this challenge, nearly all the Islamic economists have argued that a modern Islamic government would be entitled to impose additional taxation. Only two economists, Kahf and Çizakça have challenged the conventional wisdom. While Kahf's disagreement is based upon a careful study of the original sources of Islam, Çizakça approaches the problem from a totally different angle.

Kahf has reached the conclusion that not only the Qur'an but also the authentic Prophetic traditions are silent about either allowing or forbidding additional taxation. Nor is there any sound analogy (*qiyas*) to legitimate such taxes. But there are plenty of original and clear texts protecting private property from aggression whether by the state or by individuals. After having made these observations, Kahf has found in Inam Malik, one of the classical sources of Islamic jurisprudence, some specific rules laying down as to under what conditions the state may impose additional taxation. These rules may boil down to a basic one; emergency defense expenditure. If such a situation occurs, providing that the state budget is incapable of meeting these expenses and providing that the taxes are imposed temporarily and progressively, i.e., primarily upon the rich, then additional taxes may be imposed (Kahf, 1995: 117-119). In short, unless faced by a national emergency, a modern democratic Islamic government concerned about its legitimacy, would find it difficult to impose additional taxes beyond what it collects through the *zakah* and natural resources. For, to do so, would contradict the basic teachings of Islam.

My own argument, on the other hand, is based upon the observation that only a few taxes are mentioned in the Qur'an. Moreover, we have just discussed how these taxes cannot be applied in modern societies. Under these conditions, most Islamic economists have shifted the argument to the imposition of extra taxation and the legitimacy of such policies. I argue in this context that these economists are missing the message given in the Qur'an. The silence of the Qur'an as well as the Prophet on the issue of additional taxation can mean only one thing: that Islam prefers small revenues and, consequently also, small government. In this age of global privatization, the modernity of the Qur'an is therefore striking.

Obviously, a state used to lavish spending cannot immediately adjust itself to much lower levels of spending. Therefore, Muslim democrats would face considerable fiscal problems if they came to power. In my opinion, just like in the case of interest prohibition, this problem can also be solved, by a gradual approach. Muslim democrats can and should declare the reduction of the tax burden as one of their primary economic goals. Such a goal would be supported by all the segments of the civil society. If the government can apply strict fiscal discipline and gradually but decisively reduce the tax burden, the results, according to the Mundell-Laffer hypothesis, would be felt

rapidly in the economy in the form of lower cost inflation, increased consumers' and producers' surpluses, which lead to growth without inflation (Wanninski, 1975; *The Economist*, 1997: 20).

A radical and substantial tax reduction, however, cannot be carried through unless this policy is accompanied by a thorough waqf reform. For, tax reduction necessitates that the government must withdraw not only from industrial production but also gradually from the service sector as well. Thus a waqf reform emerges not only as an essential policy for reducing the interest rate but also

the tax burden. Islamic economic history informs us that a total withdrawal of the state from the service sector is not just a wild dream. Research has shown that the Ottoman state during the classical age did not spend anything on essential services and that these were financed entirely by the voluntary sector (Barkan, 1953). Obviously a complete and immediate withdrawal of the state from the service sector is not recommended here. Instead, a gradual approach giving tax advantages to the donors and a gradual withdrawal as the waqf sector expands, is recommended. It will be argued here that a thorough waqf reform would also contribute to the democratic process. It should be remembered in this context that, due to complex reasons, Islamic societies do not have a well established aristocracy. It has been argued way back during the 18<sup>th</sup> century that citizens in such a society, where between an omnipotent state and the citizenry no intermediate institutions exist, would be crushed by the state and become extremely dependent on it for all their needs. This argument was made by Alexis De Tocqueville. De Tocqueville was concerned for his country France, where the aristocracy had perished under the *gijotin*. He was observing another country, the United States of America, which also did not have an aristocracy. What fascinated De Tocqueville about the US was that despite its lack of aristocracy, Americans were neither crushed by their state nor did they need it for their social needs. For De Tocqueville the answer was in the existence of a powerful civil society and the obsession of the Americans to be self sufficient and to solve their problems through associations and foundations, i.e., waqfs. In short, in a society without an aristocracy that can curb and control the power of the state it is the associations (waqfs), which take over this function of control (De Tocqueville, 1961: 376-379). Since Islamic societies also do not have aristocracies, waqfs are needed for contributing to the checks and balances and freeing the citizens from being over dependent to the state.

#### Conclusion:

Islam is not against democracy, on the contrary, it favors it. Therefore, it is the historians' task to explain the fact that there is no full-fledged democratic Islamic country. The answer must be sought in history and not in the basic teachings of Islam. The "hijack" argument of the secularists is therefore baseless. Notwithstanding this, Muslim democrats should assure the secularists about their sincere belief in democracy. This can best be done through an elite settlement.

If as a result of such settlement Muslim democrats do come to power, their economic/social program must be *inspired* by the Qur'an and the Prophetic traditions. The term "inspired" is emphasized because establishment of a modern system based upon a literal interpretation of the Qur'an can lead to grave mistakes. A socio-economic system *inspired* by the Qur'an, on the other hand, can be highly modern and dynamic. Such a system can face both the challenge of the global competition and, at the same time, be approved by the masses as well as the secularists.

## Sources:

- Ahlmark, Per.** "Conclusions from the 20th Century: How War, Mass Murder and Famine Are Related to Democracy and Dictatorship", *Wissenschaftskolleg Jahrbuch*, 1998-1999.
- Al-Attas, Syed Muhammad Naquib.** *Prolegomena to the Metaphysics of Islam* (Kuala Lumpur: ISTAC, 1995).
- Al-Qusi, A.M.M. Riba,** *Islamic Law and Interest* (Philadelphia: Temple University Ph.D. Dissertation, 1981-82).
- Barkan, Ömer Lütfi.** "Miladi 1527-1528 Yılına Ait Bütçe Örneği", *İstanbul Üniversitesi İktisat Fakültesi Mecmuası*, cilt 15, no. 1-4, 1953.
- Binder, Leonard.** *Islamic Liberalism: A Critique of Development Ideologies*, (Chicago: The University of Chicago Press, 1988).
- Boyce, K. James.** *Agrarian Impasse in Bengal: Institutional Constraints to Technological Change*, (Oxford: OUP, 1987)
- Burton, Michael G. and John Higley.** "Elite Settlements", *American Sociological Review*, 1987, Vol. 52, June: 295-307.
- Çiller Tansu ve Murat Çizakça.** *Türk Finans Kesiminde Sorunlar ve Reform Önerileri* (İstanbul: İstanbul Sanayi Odası, 1989)
- Çizakça, Murat.** "Price History and the Bursa Silk Industry: A Study in Ottoman Industrial Decline?", *The Journal of Economic History*, vol.XL, 1980, No.3, 533-550.
- Çizakça, Murat.** "Economic Islamization of Medieval Eurasia: An Institutional Framework", *Library of Mediterranean History*, Vol.1, Number 1, 1994: 47-75.
- Çizakça, Murat.** *A Comparative Evolution of Business Partnerships: The Islamic World and Europe, with Specific Reference to the Ottoman Archives* (Leiden: E.J. Brill, 1996).
- Çizakça, Murat.** *Demokrasi Arayışında Türkiye: Laik-Müslüman/demokrat Uzlaşmasına Bir Katkı* (forthcoming).
- Esposito, John L., and Voll, John O.,** *Islam and Democracy*, (Oxford: Oxford University Press, 1996).
- Gibb, H.A.R.** "The Fiscal Receipt of Umar II", *Arabica* 2, (1955).
- Gwartney, James, Lawson, R., Block, W.** *Economic Freedom of the World* (Vancouver: Frazer Institute, 1996).
- İnalçık, Halil.** "Osmanlı Pamuklu Pazarı", *METU, Studies in development*, 1979-80, Special Issue.
- Islamic Council of Europe.** *Universal Islamic Declaration* (London: Islamic Council of Europe, 1980).
- Kahf, Monzer.** "Taxation Policy in an Islamic Economy", *IRTI/IDB, Readings in Public Finance in Islam* (Jeddah: IRTI/IDB, 1995), pp. 117-119.
- Kuran, Timur.** "The Muslim Commercial Retreat: Causes, Consequences, Responses", paper submitted to the MESA conference convened in Orlando, Florida in November 16-19, 2000.
- North, Douglass C. . Barry W. Weingast** "The Evolution of Institutions Governing Public Choice in 17th Century England", *Journal of Economic History*, 49:803-32, 1989.
- Orman, Sabri.** "Müzakereler", ISAV, *İslam ve Demokrasi* (İstanbul: ISAV, 2000).
- Rahman, Fazlur.** *İslâm and Modernity. Transformation of an Islamic Tradition* (Chicago: The University of Chicago Press, 1984).
- Rahman, Fazlur.** "The Principle of Shura and and the Role of Ummah in İslâm", Mumtaz Ahmad (ed.), *State, Politics and İslâm* (Indianapolis: American Trust Publications, 1986)
- Ramadan, Abdel Azim,** "Fundamentalist Influence in Egypt.....", *Fundamentalisms and the State: Remaking Politics, Economies, Militance*, Marty and Appleby, eds., (Chicago: University of Chicago Press, 1993), pp. 152-183.

- Rothermund, Dietmar.** *An Economic History of India* (London: Croom Helm, 1988).
- Rustow, Dankward.** "Transitions to Democracy: Toward a Dynamic Model", *Comparative Politics*, April 1970: 337-63.
- Salamon, Lester and Helmut Anheier.** *Defining the Non-Profit Sector, A Cross-national Analysis* (Manchester: Manchester University Publications, 1997).
- Salamon, Lester and et.all.** *Global Civil Society, Dimensions of the Nonprofit sector* (Baltimore: The Johns Hopkins Center for Civil Society Studies, 1999).
- Sen, Amartya.** *Development as Freedom* (Oxford: Oxford University Press, 1999).
- Ekkehart Schlicht,** *On Custom in the Economy*, (Oxford: Clarendon Press, 1997).
- Sztompka, Piotr.** "Trust, Distrust and Two Paradoxes of Democracy", *European Journal of Social Theory* 1998(a), 1(1):19-32.
- Sztompka, Piotr.** "Mistrusting Civility: Predicament of a Post-communist Society", J.C.Alexander (ed.), *Real Civil Societies* (London: Sage, 1998b).
- Tierney, Brian.** *Religion, Law and the Growth of Constitutional Thought, 1150-1650* (Cambridge: Cambridge University Press, 1982)
- Tierney, Brian.** *The Crisis of Church and State, 1050-1300* (Toronto: University of Toronto Press, 1996 reprint).
- Udovitch, Abraham L.** *Partnership and Profit in Medieval Islâm* (Princeton: Princeton University Press, 1970).
- Ungku Aziz,** "Pilgrims Economy Improvement Plan", *Cmd. 22 of 1962 Federation of Malaya Presented to the Parliament by Command of His Majesty ... 14th August 1962. Report of the Pilgrims Economic Welfare Committee, Appendix I.*
- Weitzman, Martin.** "Some Macroeconomic Implications of Alternative Compensation Systems", *The Economic Journal*, vol.93, Dec. 1983, pp. 763-783
- Weitzman, Martin.** *The Share Economy, Conquering Stagflation*, (London: Harvard University Press, 1984)

<sup>1</sup> I do not intend to state the obvious and define democracy here. So, let me simply state the conditions without which a functioning democracy cannot exist.

1. Members of the parliament as well as the executive branch must be selected through fair elections.
2. At least two parties must compete in these elections.
3. Political parties must not be closed down by any other power.
4. At least half of the population should vote in the elections.
5. The political party in power must yield to its rival if so demanded by the electorate

<sup>2</sup> For further details consult [www.dic.gov.tr](http://www.dic.gov.tr)

<sup>3</sup> Even Turkey, which is considered to be the most democratic Islamic country in the world, is not a full-fledged democracy. The following factors render a democracy an incomplete one:

- a. If a large segment of the population is not represented in the parliament
- b. If the elections are impeded
- c. If checks and balances cannot be properly established and one institution in power dominates the others.
- d. If the constitution can be interpreted in an arbitrary manner.
- e. If the appeal courts are absent or access to them are obstructed.
- f. If the armed forces and the police do not obey the law and are corrupt.
- g. If there is no free press or the press is controlled by certain groups.

<sup>4</sup> The democracy that emerged in ancient Greece was relatively short lived and disappeared during the Roman era. The democracy that evolved in medieval Western Europe, by contrast, was sustained and survived into the modern times.

<sup>5</sup> The term "moderate" may imply different things in each country. Therefore we will prefer to muse the term "Muslim democrats". Muslim democrats are individuals who are both sincere Muslims and democrats. They also need to have a flexible view of the Shari'a. This is because in most Islamic countries today changing the prevailing Civil Law for the Shari'a is not acceptable to the secularists.

<sup>6</sup> Other values that must be protected are mind (hifz al-aql), religion (hifz ed-din), self (hifz el-nefs) and the next generations (hifz el-nesl). Bulk of the Islamic criminal and family law is derived from these values.

<sup>7</sup> If labor has a say in management this would enhance productivity by reducing information asymmetry.

<sup>8</sup> Other monotheist religions have also prohibited interest. But Islam has imposed the most stringent prohibition (Al-Qusi, 1981-82).

<sup>1</sup> Bond prices and interest rates are negatively correlated. If interest yielding government bonds are not desired, the government can issue bonds that are related to the profitability of certain government assets. Such government bonds should be issued as registered bonds. Such bonds are not usurious due to the uncertainty involved in the life span of their owners. Government bonds become usurious when they are issued as bearers' shares. For more details about how government bonds have been used to finance Ottoman domestic borrowing see, Çizakça, 1996, ch.5.

<sup>2</sup> The kharaj another major classical Islamic tax applied in agriculture also falls into the discriminatory category and is therefore irrelevant for a modern Islamic government.