J. Res. Islamic Econ., Vol. **2**, No. **1**, pp. 45-46 (1404/1984)

Zubair Hasan

Theory of profit: The Islamic Viewpoint

JRIE Vol.1, No.1

Comments: Salim Chishti

Applied Economics Research Centre
University of Karachi, Pakistan

Hasan[1] has raised several important issues about the theory of distribution from the perspective of Islam.

One of the issues he has raised about the origins of profit has been debated during the 50s and 60s.[2] Hasan has explicitly or implicitly rejected all the explanations in terms of uncertainty bearing, factor-organization, and decision making as given by Shumpeter, Knight, Bronfenbrenner and many institutionalist for the existence of profit as a return to a separate factor of production which may or may not be separated from other factors of production. He has identified himself with those who believe that profit is a non-functional surplus and does not correspond to any specific input. Its origin lies in dynamic change. In pure socialist tradition the existence of surplus is explained in terms of labor exploitation. But in the non-functional surplus view profit is not attributable to any specific function performed by land, labor or capital. It is the result of some exogenous dynamic change. If this view is accepted the obvious question is why labor and capital deserve this surplus as has been argued by him. Why should it not be passed on to the consumer? However, he did not explicitly discuss pricing of output though it is implicit in his analysis that output prices in the Islamic economic system are determined exactly as in a capitalist market system.

Hasan also claimed that wages are determined by the market mechanism but are adjusted later. He said:

Nor does the model interfere in any way with the working of the price mechanism: Y and W continue to be determined by the market-forces (Hasan: p.11).

However his claim does not seem to have any bearing on his model. If the profit is shared ex-post among factors of production the price of any factor of production cannot be determined ex-ante. In his 'final distribution equation conforming to the Islamic spirit

(1) Hasan Z. "Theory of Profit: The Islamic Viewpoint", *Journal of Research in Islamic Economics*, Summer 1403 AH. (1983).
(2) A critical survey of these issues can be found in Bronfenbrenner, M. "a Reformulation of Naive Profit Theory", *Southern Economic Journal*, April 1960.

and intent', W (which he calls market determined wage) can be given any arbitrary value without making any difference in the model. Labor's share is equal to W+(1 -K) P, where W and K are institutionally determined. Also P=Y- W-T where Y is determined in the output market, and T is institutionally determined. There is absolutely no role left for market forces (in the inputs market) to determine either returns to capital or to labor. Conceptually his market determined wage rate for labor is like market determined interest rate for capital. None of the two has any significance if the returns are determined ex-post. Supply and demand for borrowed capital as well as for labor will respond to the expected returns and not to the ex-ante determined market wage rate or interest rate. This is a logical consequence of requiring a symmetric treatment to all factors of production with a view to determining their returns.

Further he has also raised the issue of *due* wages. He defines due wages as follows:

Workers must have the fairest chance under the arrangement to receive their due: what they contribute to the value product of the firm.

But this is marginal productivity theory of distribution which he has already rejected calling it cruel and unjust. Contribution of any one input depends on the level of other inputs and cannot, therefore, be measured in any absolute sense. In the industrial sector of most of the less developed countries the share of labor is in the range of 20% to 35% of the value-added, whereas in most of the advanced market economies it is above 70%. The difference is largely explainable in terms of the labor productivity differential which is primarily due to the difference in the amount of capital, both human and non-human, with which labor works. What then is the due share of labor?

Secondly, even if contribution to the value product is precisely measurable, it may not necessarily conform to Islamic justice if it leads to large income in equality.

Thirdly, there is no indication in the quotation in his foot-note no.24, to interpret due wages as the contribution to the value product.

Lastly, he did not use this concept of due wages in his own model. The share of labor in his model is determined by K which is an institutional variable.

To sum up, Islam does not treat capital and labor symmetrically with regard to determining their rates of return It singled out interest specifically, making it unlawful. It did not say the same thing of the ex-ante determined wages. Neither does the socio-economic justice of Islam, nor its principle of *Gharar* demand the ex-post determination of all inputs prices. This, however, does not mean that ex-post profit sharing by all factors of production at a pre-negotiated rate is not allowed in Islam. It will, though, have only limited applicability, be cause the sector of hired labor on daily wages and the sector of hired labor where the output is not sold in the market for price is much larger than the sector which uses borrowed capital for investment.

Hasan's claim as he put it "Beyond minimum wages, presumably some sort of a labor participatory system alone can bring us closer to a distribution scheme that may be just to both labor and capital" is not substantiated either by theory or by practice in Islam.