Rationality in Economic Theory: A Critical Appraisal

Syed Omar Syed Agil

Economics is the study of man. Capitalist economics is the study, not of man in general, but of economic man, whose behavior arises from the scarcity of means to achieve given ends. More precisely, in order to provide a simplistic model of human behavior and ensure a predictable pattern of behavior of markets, the economic man is assumed to be rational in all his endeavors. Although, in reality, his behavior at times may not be rational, for theoretical purposes he is treated as if it were. “The distinction between rationality in fact and rationality in theory is blurred.”

Thus, economics is the study of rational economic man. Rationality, being at the heart of neoclassical economics, is invariably a fundamental assumption underlying an economic model in modern theory, and the capitalist system cannot live without it. This paper attempts to redefine rationality in economic theory. It sketches the historical development of the concept of rationality and highlights the fact that, despite the unchallengeable view that the egoistic model of human behavior is unrealistic, economists still maintain their commitment to it. The latter part of the paper covers the Islamic world view and alternatives to the present perception of rationality, as viewed by Muslim economists. Finally, the implications of the Islamic view on behavior of economic agents are presented.

MEANING OF RATIONALITY

At the outset of our discussion, it seems appropriate to clarify what economists mean when they say that a decision made by an economic agent is rational, for rationality may mean different things to different people. An individual consumer can make a decision that is rational in his view, while it is irrational to others. Similarly, individuals of different societies may view rationality differently as a result of different beliefs and cultures. “Rational” becomes confusing, as it can mean so many things: dispassionate, reasonable, logical, explainable, purposeful. It is not always made quite plain what is intended.

Even among social scientists, rationality has become a controversial subject, and there is no definite meaning that can be accepted by all. It is only a slight exaggeration to say that what an economist or statistical theorist regards as a ‘rational decision process’, a psychologist might regard as ‘habitual behavior’; while what a psychologist regards as ‘rational choice’, an economist would refuse to regard as rational at all.

In the literature, economic agents are assumed to be rational in the following senses.

a) People know what they want, are able to order their wants from most preferred to least preferred, and are able to act consistently “on the basis of that ordering so as to maximize some general welfare notion such as utility.” Individuals satisfy a basic set of postulates that characterize rational behavior.
b) Both the ends and means of an activity break with tradition and are based on reasoning. Oskar Lange refers to this as methodological rationality when it is based from the point of view of the economic agent himself.\textsuperscript{7}

c) Rationality should lead toward the quantification of end and means in monetary units. This quantification leads to calculation and the tendency to maximize the aim of activity (e.g., profit\textsuperscript{5}), and more is preferred to less.

d) In capitalist modes of production, rationality means the satisfaction of the principle of greatest efficiency and economy of means. There is room neither for sentiment for traditional values not quantified in money, nor for traditional slackness in gainful activity.\textsuperscript{9}

e) Individual rational behavior in pursuing the satisfaction of self-interest will lead to social good.\textsuperscript{10}

f) A person's choices are rational if and only if these choices can all be explained in terms of some preference relation consistent with the revealed preference definition, i.e., if all his choices can be explained as the choosing of most preferred options with respect to a postulated preference relation.\textsuperscript{11}

In short, rationality in most economic literature means self-interest\textsuperscript{12} and at the same time consistency in making choices, with an aim that can be quantified toward the maximization of some general welfare notion.

**FORMS OF RATIONALITY**

**Egoistic Rationality**

Edgeworth asserts in his *Mathematical Psychics* (1881) that "the first principle of Economics is that every agent is actuated only by self interest,"\textsuperscript{13} a conception of rationality that persists in contemporary economic models. A producer will express this principle in the form of maximizing profit, either by maximizing output or minimizing costs, while a consumer will choose consumption bundles that maximize his utility. In order to solve this maximization problem, egoistic rationality also assumes perfect rationality an assumption that the economic agent possesses all necessary knowledge. A consumer knows all the options and commodity bundles available to him and what their qualities and their prices are so that, given his income, he is able to choose the optimal bundle that maximizes his utility. Similarly, a producer has full knowledge about the "past performance, present conditions and future developments in the environment of the firm, [and] knows with certainty its own demand and cost functions."\textsuperscript{14}

In other words, under egoistic rationality, economic man is rational and is guided by self-interest in his maximizing behavior. And this is not far from the views of such early microeconomists as William Jevons or such philosophers such as Jeremy Bentham, who subscribed to the utilitarian notion that man acts only in response to his 'interest'.\textsuperscript{15}

**A Historical Phenomenon**

Historically, the egoistic conception of rationality is a consequence of economic and religious compulsions that became an important factor in the development of capitalism. In the early Mercantilist period, merchants were discouraged from acquiring high profits by policies that maintained monopolistic privileges to the benefit of great merchant companies and by the religious atmosphere stemming from the teachings of the Catholic Church. "As far as the Church was concerned, merchants were going to Hell."\textsuperscript{16}
By the late seventeenth century, the capitalist market economy was rapidly being extended into most significant areas of production and commerce, demanding self-seeking, acquisitive behavior to function successfully. In this context new theories about human behavior began to emerge, writers began to assert that "selfish and egoistic motives [are] the primary if not the only ones that [move] men to action." Protestant ethics were then formulated to support and justify the self-interest motive in capitalist economy.

As a result of these changes, individualist and egoistic doctrines began to dominate economic thinking. It is clear that the egoistic conception of rationality is the result of a revolt against state regulations and injunctions as well as of an anticlerical attitude that prevailed during that time. The world has witnessed a change from a philosophy of mercantilism to that of free trade and economic liberalism. "The principle [of economic rationality] shows itself here in full for the first time in the history of the development of human economic activity. It could not show itself earlier, i.e., in natural economy."18

The conception of rational man in economics that is derived from this historical process does not take into account important human characteristics like sympathy for others, moral concern, religious impulse, or aesthetic endeavor. Acquisitive behavior, in a sense, is necessary to achieve social good. In a perfectly competitive system, each individual, in pursuing his own self-interest, is led by an "invisible hand" to a course of action that increases the general welfare of all. "It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own self-interest."19

It is this model of human behavior, based on the assumption of egoistic rationality to which economists are still committed, that lies at the heart of neoclassical economics. However, this assumption of rationality has been criticized on a number of grounds, leading gradually to the development of other conceptions of rationality. We will first examine criticisms that have been forwarded by contemporary economists and proceed from there to highlight some suggested alternatives to the egoistic rationality assumption.

CRITICISMS OF EGOISTIC RATIONALITY
Too Demanding and Too Restrictive
The egoistic conception of rationality has been criticized on two major fronts.20 First, in assuming perfect rationality it is too demanding, since individual producers or consumers are required to perceive, evaluate, and calculate with absolute precision. It is not realistic to assume that a consumer has perfect knowledge of the goods available in the market and of their relative prices and is able to solve the constrained maximization problem. Neither is it possible, in this world of uncertainty, that a producer knows with exact precision its own demand and cost functions and produces the level of output where \( MR = MC \) so that marginal profit is zero.

Second, in limiting attention to narrow self-interest as the sole motivator of an individual's actions, egoistic rationality is too restrictive. The egoist will not accept anything other than the maximum achievement of his self-interest and is willing to suppress his emotions so as to have either a neutral or negative attitude toward benevolence and altruism. He is not moved in his decision making by either of these factors. However, it is not reasonable to assume that an individual undertakes an economic activity, either in production or consumption, with the sole objective of maximizing self-interest, since in reality he is also a social being who is part of an interdependent social system.
Not an Actual Man

Another flaw of the egoistic rationality assumption is that it does not represent the behavior of an actual human being. The egoistic rationality assumption creates an abstract, shadowy being who is a self-seeking individualist. Some economists admit that this is not a realistic model of human behavior. They claim that what is important is the ability of the model to predict market behavior accurately. This view is debatable.

Another simple fact is that man is not merely a tool devoid of emotions. Adam Smith, in trying to give the egoistic behavior its 'rational' attribute, seems to conform to the logic that since society can be defined as an aggregate of individuals, to maximize society's interests is to maximize the interests of each of its individual members. It is another form of the 'adding-up' controversy. Human beings in this sense have been reduced to mere figures that can be added up by the 'invisible hand' to reach a maximum.

A Case of Market Failure in the Urban Renewal Problem

Although "some people find it puzzling that individual self-seeking by each should produce an inferior outcome for all," there exist factors that may cause markets to achieve non-optimal results. An illustration of the urban renewal problem in game theory will show that "the very individual rationality that makes the market work so well often destroys the optimality of its results."

In the urban renewal problem, a prospective tenant who thinks about renting an apartment takes into account the attractiveness of the neighborhood, which depends on the characteristics of nearby properties. Thus, the rent obtainable by one landlord may be affected by the condition in which neighboring landlords keep their properties. Consider four possible cases between two adjacent owners, A and B.

<table>
<thead>
<tr>
<th>Landlord A ...</th>
<th>does not invest:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Landlord B ...</td>
<td>invests: 7(A), 7(B)</td>
</tr>
<tr>
<td>invests:</td>
<td>3(A), 10(B)</td>
</tr>
<tr>
<td>does not invest:</td>
<td></td>
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**Case 1.** If both landlords invest in redeveloping their properties, both can earn a rate of return making the additional investment worthwhile. Each benefits from the fact that the other has made improvements, because tenants are willing to pay higher rents for apartments in improved neighborhoods than for apartments in unimproved ones.

**Case 2.** Landlord A can obtain higher rents without redeveloping, provided that neighboring landlord B does redevelop. A's rate of return might even be higher in this case than in the first, because he can obtain higher rents without investing any additional capital.

**Case 3.** If neither of the landlords redevelops, both continue to earn a rate of return lower than they could obtain if both redevelop.

**Case 4.** If A develops his property while B does not, A's rate of return might actually drop below what it would be if neither he nor B undertook redevelopment.

When deciding whether to invest in redevelopment, landlord A must consider two possibilities—that B will also redevelop and that B will not. Looking at these two possibilities, he sees
that in either case he would be better off not investing. In the first situation, he could earn 10 percent by not investing (case 2) but only 7 percent by investing (case 1). In the second situation he could earn 4 percent by not investing (case 3) but only 3 percent by investing (case 4). His rational decision is therefore not to invest. However, since landlord B as an individual owner is logically in the same position as A, he too decides not to invest, and no redevelopment occurs.

Clearly, society benefits most when both A and B invest in redevelopment. But the actual outcome may well be that neither individual will do so. Each individual's rational egoistic decision is not to invest, which makes the society worse off. Here, we are travelling in the realm of rationality in welfare economics. Game theory exposes the need for cooperation rather than self-interest motives in economic life.

Another factor that can lead to non-optimal results in the capitalist market economy is in the case of externalities. Although the equilibrium condition is the position in conformity with rationality, we will see that the existence of externalities can prevent this condition from achieving optimal results. There are various forms of externalities, but for the purpose of this study the point will be illustrated with an example of externalities in production only. We will again observe how the conception of rationality that sets a condition for equilibrium for the individual economic agent fails to work and destroys the optimality of its results.

Let us assume that alcohol is manufactured in a perfectly competitive market (figure 1). Each firm is in equilibrium (at which rationality for the individual firm is achieved) when \( P_x = MC_x \), where \( x \) is alcohol.

![Fig. 1. Alcohol manufactured in a perfectly competitive market.](image)

The \( MC_x \) is the marginal (private) cost incurred by the firm to produce one extra unit of \( x \). It does not include the marginal (external) cost that the firm creates in the form of pollution, accidents, injuries and deaths, and the like.

Now, suppose that the health department obtains an estimate of all these costs to the society. Then \( MSC = MC_x + MEC_x \), where \( MSC \) is marginal social cost and \( MEC \) is the marginal external cost.

In this case it is obvious that \( MC_x < MSC_x \). Thus, given the equilibrium condition \( P_x = MC_x \), the production of alcohol at this level will not be socially optimal due to the fact that \( MSC > MC_x + P_x \) and \( MSC > P_x \), if the full costs of the production of alcohol (costs to firm plus
costs to the society) are taken into account.

Thus, rationality in this instance indicates that the firm should have produced less (to be socially optimal) than the initial equilibrium when the external costs are not taken into consideration.

Based on the $P_x = MC_x$ equilibrium condition, the level of production of alcohol is $X_0$. This level of production is excessive and socially undesirable if the full cost ($MSC_x$) is taken into consideration, where $X_1$ would be the optimal and desirable point.

We should not exclude the possibility, given the above analysis, that the optimal level of the production of alcohol is zero. This is true if the marginal social cost is very high, and this can happen in reality (figure 2).

If the $MSC$ curve is $MSC_{x_2}$ at $P_x = MSC_{x_2}$ the optimal level is obviously zero. Thus, at $MC_x = P_x$ the $X_0$ level would be non-optimal.

Egoistic rationality, in this case of externality for the perfectly competitive firm, results in the misallocation of resources and the breakdown of the market system.

**Content of Choices**

Another difficulty in accepting the rationality assumption is that it frequently defines rationality as synonymous with consistency of choices and actions that will lead to utility maximization. Although this is a necessary condition, it is not at all sufficient. An individual is regarded as rational if his choices and actions reveal consistency: “If you are consistent, then no matter whether you are a single minded egoist or a raving altruist or a class conscious militant, you will appear to be maximizing your own utility in this enchanted world of definitions.”

One important aspect pertaining to the consistency of choices and actions is that it neglects the content of individuals' choices, which is clearly an important ingredient in determining their rationality. Choices should not be detrimental to oneself or to others, because if this happens then, naturally, maximizing the interest of each individual in the society will not lead to the maximization of the interests of society as a whole. An economic agent is considered rational only when both the consistency and the content of his choices are taken into consideration.
Thus, a producer is considered rational not only in the sense of being able to answer the question "Can a product be produced?" in his quest for profit but also in answering the question "Should it be produced?" A consumer should not include in his content of choices alcoholic drinks, for example, when he acknowledges them as injurious, or he will be considered irrational.

However, egoistic rationality fails to consider these points. Thus, "it is not surprising that capitalist production continues to indulge in irrationalities persistently,... capitalist production tends to generate such irrationality consistently as part of its normal functioning." Irrationality exists, for example, in the fact that capitalist society provides food products that, rather than providing nutrition, are detrimental to health.

In other words, rationality should include qualitative as well as quantitative elements in the evaluation of individuals' choices and decisions. It is rational for an individual to desire more of a good if he finds that it is of high quality. Nevertheless there should be a limit to preferring more of a particular good than less if its excess leads to detrimental effects on the individual and the society.

**Too Materialistic**

For theoretical purposes, economics regards man as a calculating machine who will not hesitate to achieve a higher material gain through his economic decision making. Naturally, this assumption is faulty, since there is always a limit to what a person wants. His objective of achieving a higher utility or profits is not only constrained by his level of income and price levels, in the first case, or by his capital outlay and level of production, in the second, but by existing laws and regulations, traditional values, and moral or social responsibilities. In other words, even though he could achieve the optimum level of profits or utility with a given set of constraints as prescribed in economic theory, there are other considerations that will bring the actual level down. This is to ensure greater cohesiveness and equity in the society by eliminating those acquisitive modes of behavior among individuals that, if allowed to persist, would deter the achievement of a society's welfare goals.

Critiques of the egoistic rationality assumption have led to new developments in the rationality assumption underlying economic theory. Although these contributions have given a better picture of the rational economic man, they are not an alternative to the egoistic rationality assumption.

**NEW DEVELOPMENTS IN RATIONALITY**

**Bounded Rationality**

The unrealistic assumption that economic agents have access to all the necessary knowledge and information to make decisions under perfect rationality has led to the incorporation of human imperfection into the theory of rationality. This form of rationality is called bounded rationality. In other words, there are constraints, such as lack of ability to identify optimal actions or lack of information relevant to the decision at hand. These constraints affect decision making as a result of either the existence of costs in information gathering or exogenous factors. An individual who recognizes these limitations of his will not be able to maximize his satisfaction or profit but settles for a satisfactory level: "a consumer 'satisfices' rather than optimizes."

Another significant challenge to the egoistic rationality assumption is the view that what is important is the serious effort to focus on knowledge rather than on rational choice, which assumes that economic agents know with precision what they are supposed to know. This leads to the view that rational economic agents follow not the dictates of rational choice but the rules
of scientific method. In other words, “man is not an optimizer but a scientist” who behaves based on incomplete and limited knowledge.  

**Altruism**

A majority of economists recognize the existence of altruism in man’s behavior. Adam Smith was no exception.

> How selfish soever man many be supposed, there are evidently some principles in his nature which interest in the fortune of others and render their happiness necessary to him though he derives nothing from it except the pleasure of seeing it.

In other words the truly rational man of economics is not a man devoid of emotion but a man who is sensitive to his surrounding and to the problems of his fellow beings. But how can we reconcile the theoretical model of human behavior that assumes egoistic rationality with the natural altruistic instinct within man? The apparent existence of altruism has been seen by many as a strong challenge to the egoistic model of human behavior.

Some economists try to reconcile these attributes of human nature by defending the egoistic rationality assumption as being compatible with an altruistic attitude. Altruism is a means to achieve maximization of utility, and this can happen in two ways.

i) The act of giving itself produces utility. “A consumer may get pleasure by sacrificing his otherwise desired consumption pattern for others....Individuals are assumed to select that one which maximizes utility.” Such an assumption should not be taken as a denial of the prevalence of philanthropy or of benevolence toward others: “some individuals undoubtedly derive utility from ‘doing good’.” This type of charitable behavior implies the existence of real altruism which, according to some economists, is still unexplained.

ii) The other way to incorporate altruism into egoistic rationalism is to claim that such behavior may build a reputation for the donor within a community. Thus, altruism fits into the picture in enhancing the move toward utility maximization by improving the image of the rational economic man in the eyes of the public.

These attempts to incorporate altruism into the egoistic rationality assumption have failed to explain the existence of genuine altruism as a result of one’s commitment as part of behavior may lead a person to choose an act that “will yield a lower level of personal welfare to him.” In the theory of rationality, such an act is considered irrational.

Closely related to altruism is the doctrine of social responsibility, in which a firm establishes itself not only for profits but also to improve the quality of life of the society in which it operates. The firm includes in its objectives non-egoistic behavior, though not without a selfish purpose, given that such behavior will improve the firm’s image in the eyes of the public and further the firm’s aim of profit maximization.

Thus, it is clear that neither altruism nor the doctrine of social responsibility are alternatives to the egoistic rationality. Rather, both strengthen the neoclassical assumption that man is rational when he is actuated by self-interest. These new developments have failed to answer the criticisms of rationality as it exists in economic theory today.

The above criticisms pose a tremendous challenge to the very foundation upon which modern economic theory is built. If this is the case, then the present general and faithful acceptance of the theory and conventional economic system should be questioned and replaced if necessary.
**ISLAMIC WORLD VIEW**

Given that present economic theory and the conception of rationality embodied in it no longer hold, there is no alternative but to resort to the Islamic world view and see how individual behavior within its realm is rational. The reasons for such a proposition are as follows.

i) In the Islamic world view, the problem of a blurred distinction between rationality in fact and rationality in theory does not exist. This is also true with regards to ambiguity of definition. The Islamic world view provides indispensable norms that guide a Muslim toward rational behavior.

ii) An individual, given his acceptance and sincere application of the Islamic world view, is tied to a set of beliefs that minimize inconsistencies of choices and promote qualitative elements in the content of the choices. This is true because consistency and quality of choices are direct applications of this belief. In fact, they are integral to it.

iii) Unlike rationality in present economic theory, where altruistic behavior of benevolence is a means to achieve a long-run material goal, the Islamic world view regards such behavior as unacceptable and replaces it with that which is based on commitment to the precepts of Islam. Some Western economists seem to reject this form of altruism as well. Stigler, in support of Archbishop Richard Whately's view that "the man who acts on the principle that honesty is the best policy...is a man who is not honest," points out that "he who behaves honestly because it is remunerative is simply an amoral calculator; an honest man is one whose principles of right conduct are adopted independently of their consequences for him." 34

Islamic writers generally replace the rational man of economics, who is materialistic and created as a result of historical and theoretical phenomena, with the Islamic man ('ibad al-Rahman 35), whose behavior and actions are consistent with principles of the Qur'an and Sunnah.

The behavior of the Islamic man is considered rational because it is in conformity with the rules of Shari'ah which aim at creating a balanced society. This Shari'ah-abiding behavior arises when an individual ponders the universe and comes to the conclusion that Allah (s.w.t.) is its creator and only he qualifies to prescribe the laws that lead toward the success of man in this life and the hereafter. As a result of this conclusion, in the domain of economics the Islamic man's behavior arises when he submits to the economic principles prescribed by his creator alone.

In contemporary economic theory, the term "rational consumer", for example, refers to an individual who spends his income in such a way as to achieve maximum satisfaction, even though a portion of this may be allocated for the consumption of alcoholic beverages. Such a consumption pattern is irrational in an Islamic society because it is detrimental to the consumer and society as a whole and because the belief that the transgressor will be punished on the Day of Judgement is enough to deter a person from doing it.

This type of economic decision, which stresses the qualitative nature of the content as required by rationality, is compatible only with the character of the Islamic man.

And there are men who say: "Our Lord! Give us good in this world and good in the hereafter and defend us from the torment of the fire!" 36

Say: "Not equal are things that are bad and things that are good, even though the abundance of the bad may dazzle you. So fear Allah, O you that understand, that |so| may you prosper." 37
Thus, the consumption bundle of an Islamic individual or household will exclude detrimental items such as alcoholic beverages, which are clearly prohibited in the Qur'an.

O you who believe! Intoxicants and gambling, [dedication of] stones and [divination by] arrows are an abomination, of Satan's handiwork. Eschew such [abomination] that you may prosper.38

Moreover, not only will the content of economic choices be qualitative in nature, it will also be consistent due to the fact that the Islamic world view develops the inner self of an individual to fear Allah (s.w.t.). The nature of the choice is such that it is consistent without regard to time or place, whether it is in the open or hidden, because a Muslim realizes that “He is with you wheresoever you may be. And Allah sees well all that you do.”39

The Islamic world view educates an individual so as to imprint in him a sense of accountability.

O you who believe! Fear Allah, and let every soul look to what [provision] he has sent forth for the morrow. Yea, fear Allah, for Allah is well-acquainted with [all] that you do.40

The Islamic man is not materialistic, for he takes into consideration social interrelationships that are functioning continuously in human society. Thus he is kind-hearted, benevolent, and concerned over the welfare of others. At times, he enters into the realm of impossibilities by his willingness to sacrifice and accept a much lower material satisfaction just to satisfy others.

They ask you what they should spend [in charity]. Say: “Whatever you spend that is good is for parents and kindred and orphans and those in want and for wayfarers. And whatever you do that is good, Allah knows it well.”41

Thus, rationality is a goal by itself, so that man, despite his weaknesses, must seek to achieve it and must walk consistently on the path that leads to it. Furthermore, this altruistic behavior is genuine, having no ulterior motive of long-run material gain as in the doctrine of social responsibility. A firm will not sacrifice its current profits simply for the purpose of improving its public image with the hope of achieving higher profits in the future. A Muslim’s benevolent character is based on his sole commitment to achieve the pleasure of Allah (s.w.t.), otherwise his sacrifice will not be accepted.

Those who spend their wealth for increase in self-purification
And have in their minds no favor from anyone for which a reward is expected in return
But only the desire to seek for the countenance of their Lord most high
...soon will they attain [complete] satisfaction.42

It is clear that the Islamic world view satisfies the conditions of economic rationality with respect to consistency in economic choices, content of choices, and such external factors as true altruism and social interactions that contemporary economic theory has neglected, or at least failed to explain clearly.

RATIONALITY IN ISLAMIC ECONOMICS

Hopefully, our discussion at this juncture has conclusively highlighted the weaknesses of economic rationality in present economic theory and some strengths of the Islamic world view.
However, we have not dealt with the alternative to the present perception or view of economic rationality, which is based on the maximization hypothesis.

Generally, Muslim economists prefer to accept the term ‘rationality’ as it is used in the conventional economic literature but in a different context in order to incorporate Islamic norms and ideals.

Siddiqi, in reference to Knight’s definition of a rational man as “the man knows what he wants and orders his conduct intelligently with a view to getting it,” argues that the assumption of Islamic norms is in no way inconsistent with rationality so defined. He defines a rational Islamic individual as an “individual who would order his behavior with a view to achieving maximal conformity with the Islamic norms.”43 The crux of the matter is that in Islamic economics rational behavior does not necessarily imply maximization.44

Thus, in his view rationality in consumer behavior implies that demand for alcoholic drinks and other prohibited goods and services, and therefore production of these goods, would fall to zero; the tendency of luxury goods to multiply would be checked and demand for them would decrease; and demand for necessities and for some comforts would increase. Since the motivation of the Muslim consumer or entrepreneur is not solely to maximize self-satisfaction but to act in accordance with Islamic principles, any conflict that might occur between the maximization objective and Islamic injunctions is expected to be decided in favor of the Islamic principles.45

Anas Zarqa, on the other hand, uses a simple diagram showing interaction of consumption and reward to model consumer behavior. Using a three-level hierarchy of consumption (dharurah, hajah, and kamalah) and the principle of moderation, he concludes that “rational Islamic behavior would lead the individual to settle somewhere between the sufficiency threshold and the prodigality frontier.”46

Anas Zarqa’s ingenuity lies in the fact that he is able to make use of virtually all the principles of Islam in consumption and its relation to Islamic ‘aqida and arrive at a simple but practical model of rational behavior for an Islamic consumer.

There is no contradiction, in principle, between what has been forwarded by Siddiqi and what has been drawn up by Anas Zarqa pertaining to the implications of rationality on a Muslim consumer’s behavior. Any difference is just a matter of approach. Siddiqi uses a general framework to discuss the effect of the Islamic spirit on the behavior of the consumer, while Anas Zarqa’s approach is more graphic in nature, with the framework as outlined by Siddiqi.

Thus on Anas Zarqa’s model a rational individual will neither settle before the attainment of the sufficiency threshold (if he can afford it), because he will be penalized for engaging in harmful asceticism, nor settle beyond the prodigality frontier, because he will be penalized as well for indulging in excessive refinements.47

Nevertheless, Anas Zarqa has left out, deliberately or not, discussions of saving and the behavior of a rational Muslim consumer in relation to it. The availability of savings is a crucial question, which has an effect on the behavior of the consumer (micro level) and the Islamic economy as a whole (macro level).

The inclusion of savings in the theory of consumer behavior has been taken up by Fahim Khan and Monzer Kahl.

In discussing economic rationality, Monzer Kahl replaces this term with what he calls ‘Islamic rationalism’ which is consistent with Islamic values. The basic elements of Islamic rationalism are the concept of success, the time scale of consumer behavior, and the concept of wealth. All these elements justify behavior of the mu’min as rational. Income uses that are excluded from the secular consumer’s spending pattern may have positive utility in Islamic rationalism. For example, donating to a mosque has its justification based on the time scale of
consumer behavior, where the outcome is based not only on the immediate effect but also on its later effect in the life to come.

Thus, donating a portion of income to a mosque is rational in this sense, although it is irrational in the conventional sense. The desire to maximize his reward encourages the *mut'a* to donate. Monzer Kahf prefers to define Islamic rationalism as the maximization of *fikrah* by the consumer or producer rather than maximization of self-satisfaction.

Fahim Khan maintains that in an Islamic economic system a Muslim consumer has to be rational in all his spending. Unlike the secular economic assumption of consumer rationality, the axiom of rationality required for Islamic economic theories of consumer behavior is derived from the moral norms of Islam. It is something that a Muslim has to learn and acquire.46

Rationality requires that the spending behavior of a Muslim consumer conform with the teachings of Islam, which has several implications:

i) A consumer is rational only if he spends in moderation: "Make not your hand tied to your neck, nor stretch it forth to its utmost reach, so that you become blameworthy and destitute."49

ii) A consumer is rational only if he spends not only for worldly goods but also in the way of Allah (s.w.t.): "And render to the kindred their due rights, as [also] to those in want and to the wayfarer. But squander not [your wealth] in the manner of a spendthrift."50

iii) A consumer is rational only if, *ceterus paribus*, his consumption basket is smaller than that of a secular consumer, as the former includes only permissible things and excludes prohibited things: "He has only forbidden you dead meat and blood and the flesh of swine and that on which any other name has been invoked besides that of Allah. ...."51 "O you who believe! Intoxicants and gambling, [dedication of] stones, and [divination by] arrows are an abomination, of Satan's handiwork. Eschew such [abomination], that you may prosper."52 "Those who, when they spend, are not extravagant and not niggardly but hold a just [balance] between those [extremes]. ..."53

iv) A consumer is rational only if he does not hoard his savings, but channels them toward investment. This is so because in an Islamic economy savings that are not invested are penalized by *zakah* on hoarding.

Thus, the total spending of a rational Muslim consumer can be classified as:

v) Spending to achieve satisfaction in this world. This includes immediate consumption and savings or investment for future consumption.

vi) Spending for others with a view to earning reward in the hereafter. This includes what is immediately consumed by the recipients, what is invested for social purposes or community benefits and what is saved by the recipients for their own investment.

Denoting (v) as $E_1$ and (vi) as $E_2$, the utility maximization problem of a Muslim consumer is not based on consumable goods only (like that of his secular counterpart) but specifically on $E_1$ and $E_2$. In short, a consumer is rational, in this sense, if he maximizes $U = F(E_1, E_2)$ subject to the constraint of his income $Y = E_1 + E_2$ and other constraints (as in [i] and [iii]).

Monzer Kahf's study of the rationality of consumer behavior based on Islamic principles concludes that the goals of the consumer include the enrichment of his life in the hereafter as well as the enjoyment obtained from material consumption.54 Replacing the term 'consumption' with 'final spending', which is composed both of spending on goods and services that bring about immediate satisfaction in this life and spending for the sake of Allah (s.w.t.), which in conventional analysis has been excluded from the term consumption itself, he summarizes the
consumer's decision of income allocation between saving and final spending which will maximize the consumer's overall satisfaction (in both this life and the next) as $U_{\text{max}} = U(FS, S)$ subject to $FS + S = Y$ and $DW = S > Z(W + S)$, where $U$ is consumer’s utility, $W$ is the consumer’s wealth, $Z$ is the zakah rate and $D$ is the time derivative.

The above decision of the consumer is rational, based on the main assumptions that, first the consumer is not only constrained by his income but also by the minimum amount of wealth that he wants to maintain and second, the institution of zakah is established and riba is eliminated, and both of these factors affect the decision of the consumer in the following sense. Prohibition of interest raises current final spending in relation to saving. Institution of zakah will reduce the utility of the consumer by reducing savings (part of income not used for final spending) that are not invested. Thus the rational thing to do is to invest the savings.

The Prophet (s.w.t.) said “Invest the mal of the orphans so that it does not vanish because of the deductions of zakah.”

Thus, rationality for the Muslim consumer implies having a higher portion of final spending in his income, relative to savings and integrating investment considerations in the decision to save.

CONCLUSION

Rationality is one of many methodological issues frequently discussed in conventional economics literature. This paper has attempted to review the issue by looking at various definitions, implications, and models of rationality and critically evaluate them on the basis of recent works. The author is of the opinion that rationality is an implicit element in the Islamic world view and not a separate assumption. Thus, it is also the purpose of this paper to highlight the meaning, implications, and strengths of the rationality element ingrained in the Islamic world view. It is hoped that this discussion has been successful in justifying the need to replace the rationality assumption (which is not as rational as conventionally believed in the profession) in economic theory and in providing an Islamic alternative to the perception and implications of rationality.

We believe that any view based on human reasoning has its weaknesses, and rationality is not an exception. We hold strongly to the view that rationality connotes behavior that should lead toward fitrah, a comprehensive concept meaning success in this world and the hereafter, and that can only be achieved if behavior is compatible with Islamic norms.

It has not been the intention of this paper to claim that what has been forwarded by Muslim economists is Islamic in the full sense of the word (thus accepting that there is room for improvement). It is nevertheless hoped that the discussion in this paper has provided a systematic exposure to what is available in the Islamic economic literature as an alternative to present economic theory for further research on the subject.

NOTES

Syed Omar Syed Agil is a lecturer in economics at the International Islamic University.

1. This description of economics is similar to the one given by Robbins, in which he claims that “Economics is the science which studies human behaviour as a relationship between ends and scarce means which have alternative uses” (quoted in A Dictionary of Economic Quotations, comp. Simon James).

such critiques have indeed been forcefully prosected. In defence of the assumption that actual behaviour is the same as rational behaviour, it could be said that while this is likely to lead to mistakes, the alternative of assuming any particular type of irrationality may very likely lead to even more mistakes" (Ethics and Economics [London: Basil Blackwell, 1987]).

3. This is Quiggen's terminology (1987); it can be used interchangeably with 'self-interest' or 'selfish interest'. Although rationality in economic theory, as elaborated by Sen in Ethics and Economics, can be characterized as internal consistency of choice or maximization of self-interest, the author prefers to use 'egoistic rationality' to mean the latter.


8. Ibid., 161.

9. Ibid., 167.


15. According to Jeremy Bentham, "Nature has placed mankind under the governance of two sovereign masters: pain and pleasure. It is for them alone to point out what we ought to do, as well as to determine what we shall do. ... They govern us in all we do, in all we say, in all we think. ... The principle of utility recognizes this subjection, and assumes it for the foundation of [its social theory]" (Introduction to the Principles of Morals and Legislation, quoted in E. K. Hunt, History of Economic Thought [Los Angeles: Wadsworth Publishing Co. Inc., 1979], 114). Similarly, William Jevons states in his Theory of Political Economy: "Pleasure and pain are undoubtedly the ultimate objects of the Calculus of Economics. ... To maximize pleasure, is the problem of Economics" (quoted in A. Schotter, Free Market Economics: A Critical Appraisal [New York: St. Martin's Press, 1985], 14).


18. Lange, 169.


22. Since the paper deals with rationality, arguments against the validity of this view are not presented here.

23. Sen, Choice, Welfare and Measurement, 103. The most famous problem used by economists to demonstrate self-defeating aspects of rational competition is the prisoner's dilemma; interesting expositions of this problem are found in Schotter's Free Market Economics and Hamlin's Ethics, Economics and the State. Another example of egoistic rationality's reduction of social welfare is the case of price-cutting in the economic warfare of oligopolies; for details, see Samuelson and Nordhaus, Economics, appendix 25.

24. Schotter, 47.
27. Hamlin, 15.
30. Loasby, 208.
37. Surah al-Ma'ida (5): 100.
38. Surah al-Ma'ida (5): 90.
44. Siddiqi, *Some Notes on Teaching Economics in Islamic Perspective*, 5.
46. The former delineates a consumption level that covers important conveniences that are sufficient to make one unlikely to depend on others financially, able to remain content with one's lot, and able to provide a 'sufficiency threshold' for one's dependents. The latter corresponds to maximum permisssible refinements, beyond which Islam disapproves.
49. Surah Bani Isra'il (17): 29.
52. Surah al-Ma'ida (5): 90.
55. Ibid., 31.