

Economic Systems in the World

Capitalism,
Socialism/Communism
&
Islamic Economic System

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Introduction

1. Economic problems of mankind have always been a key issue in the history. Every nation on the face of the earth irrespective of its belief and ideology strives to achieve at least a reasonable level of economic and social well being as per its ambitions.
2. This quest to resolve the economic problems have resulted in many economic systems; but they have either completely failed or partially succeeded in finding an equitable and balanced solution. Islam has also provided an economic system to keep the economic life of the individual and nation as a whole on the lines of equity and prosperity.

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Why Do We Need an Economic System?

- ~ To engage in economic activities peacefully is vital to our survival
- ~ To earn the reward of ones labor, expertise, and efforts
- ~ A market place that determines our demand and supply phenomenon in a free and fair environment
- ~ A system that ensures labor rewards and eradicate the curses like slavery and victimization
- ~ A system that accommodates the innovative ways of doing things (trading over the internet without having sophisticated infrastructure)
- ~ To ensure self satisfaction, achievement and security
- ~ To raise the quality of life and living standard to a level where no body would feel deprived.

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The existing economic system?

Some of the known economic systems are;

- ~Capitalism
- ~Socialism
- ~Communism
- ~Islamic economic system

Capitalism

- ~ A system based on private ownership of factors of production
- ~ A system based on economic freedom
- ~ A free market economy that will determine the demand and supply of the system and rewards based on individual's skills, ability, and effort.
- ~ A system that operates more close to human psychology of ownership and liberty.

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Capitalism

Types of Capitalism

Degree of competition, role of the government interventions and regulations, and scope of public ownership leads towards various forms of capitalism, i.e.

1. Laissez-faire capitalism
2. Welfare Capitalism
3. State Capitalism

1. Laissez-faire capitalism

Laissez-faire is an economic environment in which transactions between private parties are free from government restrictions, tariffs, and subsidies, with only enough regulations to protect property rights.

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2. Welfare Capitalism

Welfare capitalism refers to capitalist economies that include comprehensive social welfare policies. Alternatively, welfare capitalism refers to the practice of businesses providing welfare services to their employees.

3. State Capitalism

~ State capitalism is characterized by the dominance of state-owned business enterprises in the economy.

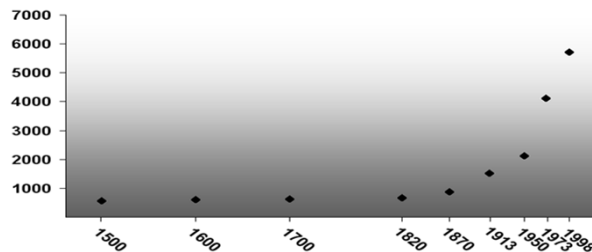
~ An economic system in which commercial economic activity is undertaken by the state, with management and organization of the means of production in a capitalist manner - maintaining the conditions of wage labor arising from centralized ownership.

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Advantages of Capitalism

Proponents of capitalism argue that it creates more prosperity than any other economic system, and they claim that its benefits are mainly to the ordinary person.

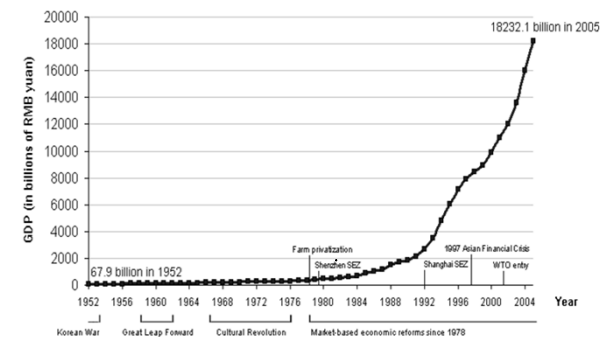
World GDP per capita between 1500 and 1998 expressed in the 1990's International dollars



Graph is derived from data in Table B-18, (World GDP) and Table B-10, (World Population) published in The World Economy: A Millennial Perspective by Angus Maddison, OECD, Paris 2001 ISBN 92-64-18998-X (<http://en.wikipedia.org/wiki/Capitalism>)

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People's Republic of China's Nominal Gross Domestic Product (GDP) Between 1952 to 2005



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Advantages of Capitalism

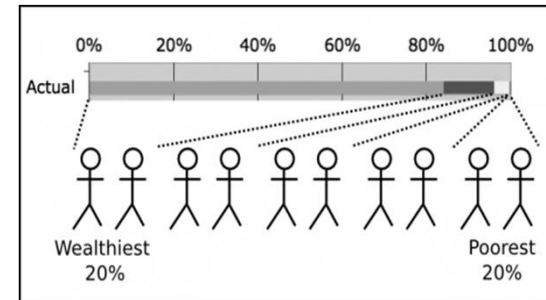
Increasing GDP per capita has resulted in

- ~ Improved living standard
- ~ Availability of basic needs of the society, i.e. food, housing, clothing, and health care.
- ~ More opportunities for the entrepreneurs to initiate new business ventures.
- ~ Right to own factors of production
- ~ Profit maximization
- ~ Economic freedom, free market and competition (if healthy competition it leads towards economic growth and innovation)
- ~ Banking and financial institutions and markets for smooth international transactions

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Disadvantages of Capitalism

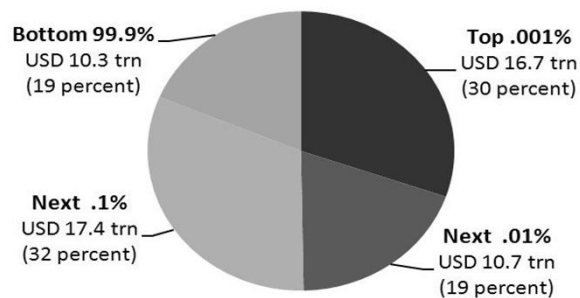
Disparities in distribution of wealth



Actual U.S. distribution of wealth. Data from Holder and Arieli (2011)

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Global Distribution of Wealth



James S. Henry, 2012

http://www.taxjustice.net/cms/upload/pdf/The_Price_of_Offshore_Revisited_Presser_120722.pdf

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Disadvantages of Capitalism

Unrestricted and uncontrolled economic freedom and uncontrolled right of private ownership has resulted in exploitation.

- ~ Labor is exploited by the capitalist
- ~ Farm worker is exploited by the landlord
- ~ Poor is exploited by the rich
- ~ Servant is exploited by the master
- ~ People are exploited by the rulers

Wealth is the objective of everyone through fair or foul means.

Cut throat competition in the market leads towards the mergers of smaller businesses into big organizations and thus monopolize the market.

Monopoly results in inflation and create obstacles for the new businesses thus leads to unemployment.

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Islamic Economic System Versus Capitalism

Right to own property

- ~ Capitalism believes in the private ownership of the means of production, distribution and exchange which are managed and controlled by individuals or groups of individuals for private profit. And it leads to the concentration of wealth in few hands.
- ~ Islamic concept of ownership is unique, i.e. Allah is the real owner of everything.
- ~ Islam allows legal ownership subject to moral obligations.
- ~ Laws of inheritance also distribute the wealth among the heirs to avoid concentration of wealth.

Economic Freedom

- ~ In Capitalism Every individual has an unbridled liberty to engage in any kind of profitable businesses moral or immoral such as gambling, prostitution, smuggling, black marketing, profiteering, hoarding, speculation, fraud, adulteration, etc. Wealth becomes the religion and faith which lead to selfishness, hatred, mistrust, etc.
- ~ Islam allows freedom but within the bounds of Shariah. Halal and Haram are made clear in all economic activities. Interest, bribery, embezzlement, prostitution, sale of wine, narcotics, short weighing and measuring, gambling, speculation, monopoly, extravagant spending, etc. are not allowed in Islam.

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Islamic Economic System Versus Capitalism

Monopoly

- ~ Under capitalism greed of wealth leads the businesses to monopolize the markets and charge higher prices and leads to the destruction of small businesses which result in unemployment.
- ~ Islam strictly forbids unhealthy competition and monopolies. Prophet (pbuh) said, "whoever monopolies is a sinner." Commodities and services of common interest are strictly not allowed to be monopolized.

Institution of Banking and Interest

- ~ Interest based financial institutions are the back bone of the capitalism. Financial institutions or banks are the sources of capital for all the business activities.
- ~ Islam categorically condemns the interest based businesses and institutions rather it encourages trade.

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Islamic Economic System Versus Capitalism

Exploitation

- ~ In a capitalist society every dominant part of the society (with few exceptions) exploit the poor or weak in the society.
- ~ Islam strictly prohibits every tool of exploitation such as usury, bribery, gambling, etc. The weaker classes of the society like women, orphans, slaves, laborers, tenants, consumers, etc. have been protected against their exploiters through legislation by Islam.

Distribution of wealth

- ~ In capitalism polarization into rich and poor takes place in the society. People are divided into different classes based on the wealth they possess. It can result into chaos and riots among the people in the society.
- ~ Islam ensures fair and equitable distribution of wealth and economic resources. System of Zakat and Sadqat is in place, hoarding of wealth is prohibited

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Socialism and Communism

Characteristics of Socialism and Communism

- | | |
|--------------------------|-------------------------|
| 1. Definition | 8. Political Structure |
| 2. Ideas | 9. Social Structure |
| 3. Philosophy | 10. Free Choices |
| 4. Religion | 11. Way of Change |
| 5. Economic Coordination | 12. Private Property |
| 6. Economic System | 13. Ownership Structure |
| 7. Key Elements | 14. Discrimination |
| | 15. Means of Control |

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Definition

Communism

A theory or system of social organization based on the holding of all property in common, with actual ownership ascribed to the **community or state**.

Ideas

Communism

Human societies have always been divided into warring classes. The Industrial Revolution has enriched the wealthy and impoverished the poor. The workers must overthrow the bourgeois.

Socialism

A theory or system of social organization based on the holding of most property in common, with actual ownership ascribed to the **workers**.

Socialism

All people should be given an equal opportunity to succeed. Workers should have most say in their factory's management. The free market suffers from problems like tragedy of the commons. Government regulation is necessary.

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Philosophy

Communism

From each according to his ability, to each according to his needs. Free-access to the articles of consumption is made possible by advances in technology that allow for super-abundance.

Religion

Communism

Abolished

Socialism

From each according to his ability, to each according to his contribution. Emphasis on profit being distributed among the society or workforce in addition to receiving a wage

Socialism

Freedom of religion

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Economic Coordination

Communism

Government controls all business, as well as business decisions.

Socialism

Planned-Socialism relies principally on planning to determine investment and production decisions. Planning may be centralized or decentralized. Market-socialism relies on markets for allocating capital to different socially-owned enterprises.

Economic System

Communism

Wealth redistributed so that everyone in society is given equal shares of the benefits derived from labor. All means of production are controlled by the state.

Socialism

Wealth redistributed so that everyone in society is given somewhat equal shares of the benefits derived from labor, but people can earn more if they work harder. Means of production are controlled by the workers themselves.

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Key Elements

Communism

An enhanced form of the principle of "Production for use".

Political System

Communism

No leader, directed directly by the people. This has never been actually practiced, and has just used a one-party system.

Socialism

Economic activity and production especially are adjusted to meet human needs and economic demands. "Production for use": useful goods and services are produced specifically for their usefulness.

Socialism

Multiple parties, but the ruling party usually goes by the name "Socialist".

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Social Structure

Communism

All class distinctions are eliminated.

Free Choice

Communism

In real communism, where a leader does not exist, everything is chosen freely. In those that have been practiced though, all choices, including education, religion, employment and marriage, are controlled by the state.

Socialism

Class distinctions are diminished

Socialism

All choices, including education, religion, employment and marriage, are up to the individual. All health care and education is provided free to everybody

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Way of Change

Communism

Government in a Communist-state is the agent of change rather than any market or desire on the part of consumers. Change by government can be swift or slow, depending on change in ideology or even desire.

Socialism

Workers in a Socialist-state are the agent of change rather than any market or desire on the part of consumers. Change by the workers can be swift or slow, depending on change in ideology or even whim.

Private Property

Communism

Abolished

Socialism

Two kinds of property, private property, such as land, houses, clothing, etc. owned by the individual. Public property, factories, and means of production owned by the state but with worker control.

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Ownership Structure

Communism

The means of production are commonly-owned, meaning no entity or individual owns productive property. Importance is ascribed to "usership" over "ownership".

Discrimination

Communism

In theory, all members of the state are considered equal.

Socialism

The means of production are socially-owned with the surplus value produced accruing to either all of society (in Public-ownership models) or to all the employee-members of the enterprise (in Cooperative-ownership models).

Socialism

The people are considered equal, laws are made when necessary to protect people from discrimination.

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Means of Control

Communism

Proletariat engages in violent rebellions.

Socialism

Proletariat engages in taking charge of the factories and means of production.

Estimated number of victims

Since these systems are not compatible with the human nature so there was a fierce resistance from the public particularly the capitalists, entrepreneurs, and farmers. In his book "The Black Book of Communism" Stéphane Courtois claims that total death toll reaches 94 million during its implementation. The breakdown of the number of deaths given by Courtois is as follows:

65 million in the People's Republic of China
20 million in the Soviet Union
2 million in Cambodia
2 million in North Korea
1.7 million in Africa
1.5 million in Afghanistan

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Estimated number of victims

- ~ 1 million in the Communist states of Eastern Europe
- ~ 1 million in Vietnam
- ~ 150,000 in Latin America (mainly Cuba)
- ~ 10,000 deaths "resulting from actions of the international Communist movement and Communist parties not in power."
- ~ Courtois claims that Communist regimes are responsible for a greater number of deaths than any other political ideal or movement, including Nazism. The statistics of victims includes executions, famine, deaths resulting from deportations, physical confinement, or through forced labor.

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Factors of Production in Islam

Learning outcomes

After this lecture you will be able to

Understand the conventional concept of factors of production, i.e. land, labor, capital, and entrepreneur.

Understand the concept of factors of production in Islamic economic system.

Role of money as of being a factor of production.

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Factors of Production in Islamic Economic Framework

First we see what are the factors of production in conventional economic system:

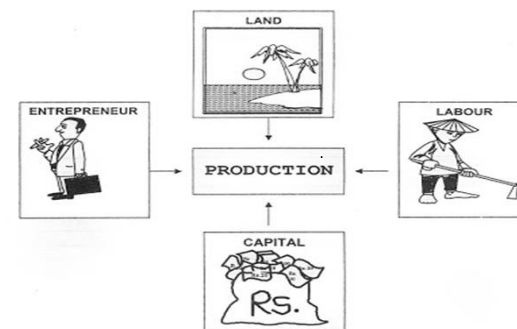
~ Factors of production are the Inputs that provide a productive service in a production process.

~ Conventional economic theory suggests four factors of production, i.e.

1. Land
2. Labor
3. Capital
4. Entrepreneur

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Factors of Production in Conventional Economic System



Production is a co-operative process and not a job of any single factor.

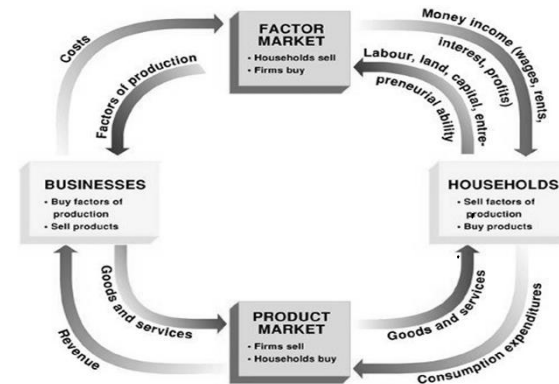
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Factors of Production in Conventional Economic System

Name of the Factor	Owner of the Factor	Reward of the Factor	Nature of the Factor
Land	Landlord	Rent	Natural resources
Labor	Laborer	Wages	Human factor
Capital	Money Lender	Interest	Man made factors
Entreprise	Entrepreneur	Profit	Man made factor

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Factors of Production in Conventional Economic System



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Factors of Production in Conventional Economic System

“Capital is recognized as money and physical capital.

“Reward of capital is interest rate which suits the money capital but it is treated as price of the physical capital too. Logic suggest that physical asset should earn rent per machine or per capital asset.

Factors of Production in Islamic Framework

All productive inputs are grouped into two categories;

1.Factor inputs: those inputs that don't get consumed in the production process.

2.Consumed inputs: those inputs that are consumed during the production process and lose their original nature and shape, e.g. fuel, raw cotton, plastic, etc.

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Factors of Production in Islamic Framework

Money as factor of production:

“Money is recognized as “consumed input” and become useful only when converted into consumed input or factor input.

“Money itself is not considered a factor of production but it has the potential to become a factor of production.

Rewards for the Factors of Production

“Hired Factors of Production (HFP): all those factors that earn ujrut (wage or rent), e.g. labor earns wage, land earns rent, machinery earns rent etc.

“Entrepreneurial Factors of Production (EFP): the factors that face risk instead of earning a fixed wage or rent, e.g. entrepreneur, capital assets employed in the production process.

“Factor inputs can become HFP or EFP.

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Rewards for the Factors of Production

~ For factor inputs that opt to become HFP the reward is ujrat or rent; money not being a factor input can not earn any ujrat or rent (interest). All the consumable inputs can neither be rented nor they can earn any ujrat.

~ Those factor inputs that opt to become EFP the reward is profit (or loss) against the risk associated with new business venture.

Entrepreneurial Factors of Production (EFP)

~ EFP is the combination of human and non-human resources that are willing to bear risks involved in initiating or participating in a productive economic venture.

~ EFP's are economic resources when confronted with a choice to work for wage or to have their own work, decide in favor of their own work. Sometime economic resource have no choice but to become an EFP, e.g.

1. A person having money can't earn interest (ujrat) on it.

2. Sometime wage rate or rent rates are so low that the person prefer not to sell the labor or rent out the property.

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Entrepreneurial Factors of Production (EFP)

~ Decision making and risk bearing are two entrepreneurial functions, where decision making is solely upon human resources while the risk bearing can be done by the human resources and physical or monetary resources as well.

~ Entrepreneurship is to visualize an opportunity and decide to initiate a productive activity in an innovative way and face all the associated risk with it.

~ An entrepreneur may not be a good manager, so this type of organizational capabilities (managerial, clerical, security etc.) can be hired against an ujrat.

~ Organizers earn ujrat while entrepreneurs earn profits (face the risk of loss)

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Hired Factors of Production (HFP)

~ All the resources that offer productive services for a definite reward known in advance are called HFP's.

~ All factor inputs can become HFP but none of the consumed inputs can become HFP ("Organization" and "managers" as factors of production too are treated as HFPs as long as they are not willing to bear the entrepreneurial risks).

~ HFP's are employed by EFP's, i.e. employment opportunities will increase with the increase in entrepreneurial activities. Demand and supply of HFP's will determine the ujrat and rent.

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Hired Factors of Production (HFP)

~ HFP's include land, labor, physical capital good and human capital (monetary resources are excluded).

~ HFPs are derived from the same resources which can offer themselves as entrepreneurial resources.

~ The supply and demand for HFPs thus competes with the supply and demand of EFPs.

~ All these resources have to make a choice whether to opt in favor of becoming an HFP and get an Ujrat or to become an EFP to enjoy the profits.

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Resources			To Satisfy Unlimited Wants	Individual Perspective		
Factors of Production				Yes / No & R / NR		
Name of the Factor	Owner of the Factor	Nature of the Factor	Reward of the Factor	Capitalism	Socialism / Communism	Islamic Economic
Land	Landlord	Natural Resources	Rent			
Labor	Laborer	Human Factor	Wages			
Capital	Money Lender	Man made Factors	Interest			
Enterprise	Entrepreneur	Man made Factor	Profit			

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Major Differences among the Systems	Capitalism	Socialism / Communism	Islamic Economic
Liberty to Earn			
Liberty to Own			
Distribution of Wealth			
Reward for Labor			
Innovativeness of System			
Social Structure			
Ways of Change			
Religion			

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You are required to fill Slide No. 37
Comparison of Economic Systems on
Factor of Production

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You are required to fill Slide No. 38
Major Differences Among
The Economic Systems

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