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# Islam and Economics

A Research Paper

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# Islam and Economics



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## A Research Paper

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**Islam and Economics**

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**Overview**

The tumultuous disturbances in the Islamic world over the past year raise the real prospect that substantial changes will take place in the institutions of Islamic countries and in the way these countries interact with each other and with the non-Muslim world.

The Islamic revival could presage a shift away from the mix of modern Western and traditional Muslim practices that has evolved in most developing Islamic countries. Many of these countries may decide to move, or be forced to turn, toward a more introverted, orthodox Muslim way of life that would be radically different from Western standards and experience.

This paper takes one aspect of Islamic life—economic relations—and examines its role in the Muslim vision of a completely Islamic existence. It describes some unique Muslim economic customs, laws, and concepts, and shows what impact Muslim orthodoxy may have on economic relations with the West.

*The above information is Unclassified.*

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**Islam and Economics** **Introduction**

Muslim countries, bypassed by the industrial revolution of the past two hundred years, are finding it difficult to cope politically and socially with the rapid changes wrought by post-World War II economic development. Consequently, many Muslims are seeking stability in the one constancy in their lives—the relatively rigid rules of Islamic law. In some countries the resurgence of Islam is in part a genuine religious revival against those who have neglected religious practice or compromised philosophical principles in the process of modernization. For the most part, however, the revival of Islam represents a reaction against the forces of change that threaten traditional power relationships and conservative social, economic, and political values.

Many Muslims are attracted by Islam's promise of economic independence, moderation, and equity. Among the poor less developed countries (LDCs), conversion to Islam, with its basically conservative, middle class values, is viewed as a concrete sign of modernization devoid of the colonial overtones and secularism of Western modernization, or the "mechanistic Godlessness" of Communism. Instead, Islam offers the prospect of actively constructing the world as God is presumed to have intended. For other LDCs Islam offers identification with the well-demonstrated power of the Arab oil countries. Many of the developing Muslim countries also are banking on the Arab OPEC nations for economic aid, for which an Islamic orientation is a prerequisite.

The strict adherence to fundamentalist Muslim values could result in substantial changes in the economies of the Muslim countries and in the way they deal with each other and the rest of the world. To the extent that the West fails to recognize the role of economics in the overall Islamic way of life, its economic relationships with the Muslim world will be neither comfortable nor rewarding.

**Background: Islam as a Religion**

Islam is a way of life. As such, it has overlapping aspects of religion, politics, culture, and economics. Islam the religion is a system of beliefs and practices initially revealed by God to Muhammad in the 7th century AD, enshrined in the Koran, supplemented by tradition, and modified in response to changes in time and place. Literally, "Islam" means submission to the will of God. By definition, a Muslim is one who believes that God is unique and omnipotent (a belief held by many non-Muslims) and that God's revelations to mankind culminated in the apostleship of Muhammad (which distinguishes Muslims from other monotheistic believers).

Originally the simple, humble religion of a few unsophisticated tribes in Arabia, Islam has become the dominant faith of about 720 million people of disparate ethnic and national backgrounds. Islam's followers predominate in political systems ranging from the Saudi Arabian monarchy to Marxist South Yemen; in economies ranging from the one-resource, oil-rich Middle Eastern states to desperately poor agricultural communities such as Bangladesh, Mali, and Somalia (see appendix A).

As a faith, Islam is far from monolithic. Since Muhammad's death in 632, political and theological differences have split Islam into an array of sects and subsects (see appendix B). Islam's adherents include more than 600 million Sunnis and 85-90 million Shias, the latter primarily in Iran, Pakistan, and Iraq. The Sunni-Shia split sprang from an early struggle over succession to the Caliphate, the secular and religious head of Islam. Within the two major sects, numerous subgroupings have developed during Islam's 1,350-year history.

## Islam and Economics

Economic relations between people are an important aspect of the Islamic way of life. The Prophet Muhammad, a poor orphan who overcame his background to become a successful merchant, lived, worked, and proselytized among the commercial cities of pre-Islamic Arabia. The rise of 6th-century Mecca as a thriving international commercial center was based on its monopolies over services and organized trade, and its control of vital commercial links. Mecca's growing power and prosperity and the control of political, economic, and religious life by its commercial elite, however, contributed to the creation of tremendous disparities of wealth in the city and to growing hostility of the Bedouin tribes that were linked to Mecca. Because Muhammad lived in the shadow of this conflict and the potential breakdown of traditional social, moral, intellectual, and religious values, his teachings at times were directed against the important economic abuses of his day: monopoly market control, price fixing, cheating on quality and quantity, broken contracts, hoarding, and usurious interest rates.

A Muslim economy is a vision of a just society consisting of individuals motivated by high principles rather than material self-interest; the underlying principle is the relationship binding the individual to God. The objective of the Islamic economic system is to secure the widest and most beneficent distribution of wealth through institutional arrangements and moral exhortation.

Islam calls for justice and moderation in consumption, while scorning monopoly power, inefficient use of resources, hoarding, and gambling. Since all forms of wealth are the gift of God to all mankind, each individual is required to share his wealth with the community. Islam does not, however, require or necessarily approve of absolute equality of wealth, because to do so would be tantamount to denying the favor of God. Islam recognizes differences in talents—and consequently economic rewards—among people, but it demands that each individual be responsible not only to himself but also to those less endowed and to society as a whole. Indeed, it is the duty of an Islamic state to ensure at least a subsistence level of existence for all its citizens by, if need be, redistributing wealth from the rich to the poor.

While devoid of a specific economic theory, Islam offers guidelines for many kinds of economic behavior, which must be viewed as the theoretical ideal; different juridical interpretations, secular motives, and sheer hypocrisy have resulted in practices frequently differing from orthodox Muslim teachings.

### Islamic Law

Islamic law is called the *Sharia*, which comprises several sources (see appendix C). These include the Koran (God's word revealed to Muhammad), the *sunna* (practices of the Prophet Muhammad), and *ijma* (consensus).

In addition, Shia Islam considers two other valid sources of Islamic law: *aql* (reason), and *ijtihad* (independent judgment of the *mujtahids*, the doctors of Islamic law).

The laws attempt to order the Muslim's life, of which economic relations are part. They condemn thievery, protect private property, set inheritance procedures, prescribe religion-based taxes, and in general define a Muslim's rights and obligations.

The multiplicity of sources for Islamic economic law and the grounding of law in theology present Muslims with a dilemma. On one hand is the claimed immutability of laws passed down by or in the name of God; on the other hand is the need (perceived by many Muslims) for rules to be dynamic and unambiguously applicable to changing circumstances. Nonetheless, uniquely Islamic views of some basic economic concepts can be derived through the *Sharia*. The fundamental economic tenets in Islam are two: God has absolute ownership of everything, and some minimum level of welfare must be provided to all Muslims in the community.

The Koran specifies three main mechanisms for sharing the gifts of God: prohibition of interest, compulsory tax collections earmarked for the poor, and redistribution of wealth through complicated inheritance laws.

### Interest

The taking or charging of interest (*riba*, or increase) is the most controversial and probably the most violated of Islamic economic sanctions. The Koranic prohibi-

tion of interest grew in reaction to the practice during Muhammad's time of Arab moneylenders rolling over loans when due to double or more the initial debt. After a series of such rollovers, the debtor eventually owed his whole property or even his person against an initially small loan. Condemnation of interest charges is in keeping with the Islamic prohibition of earning with neither risk nor effort. Muslim jurists cite the adverse effect of interest payments on the poor, and the divorce of the owner of capital from the production process as additional reasons for the prohibition.

Subsequent interpretations of the *Sharia* have put interest restrictions on several paths. Strict constructionists interpret the prohibition of *riba* as forbidding any loan in which repayment is in the same medium as the loan itself, even if no interest is charged. They cite Koranic prohibitions on all trade in like commodities (grain for grain, gold for gold, and by extension, money instruments for money instruments) unless the transaction is at face value, the exchange is hand to hand, and no time duration is involved. This interpretation of the Koran is meant to curb speculative loans while stimulating production and trade by permitting repayment in different goods. For example, a money loan can be repaid at some later point with goods of equal value, or a loan of goods could be repaid with an equal value of money. A more liberal interpretation of the Koran is similar to Western concepts of prohibiting only usurious interest payments while allowing reasonable rates to be charged. Individual Muslim communities may also have differing interpretations between these two extremes.

The traditionalists who aspire to restore Islam to its original orthodoxy have attempted to adapt Islamic doctrine to the economic needs of modern times by creating interest-free, Islamic banks. The banks are modeled on a successful experiment in the Egyptian town of Mit-Ghamr in the mid-1960s. The first major Islamic bank was started in Dubai in 1975, and its success led to establishing a series of banks in Saudi Arabia, Kuwait, Sudan, and Egypt; Jordan and Bahrain probably will have Islamic banks shortly.

The major difference between the Islamic banks and Western banks that now operate in Muslim countries is that the Islamic banks are not based on fixed rates of interest on loans or deposits. Instead, they invest most

of their capital in profitmaking enterprises and share profits—and losses—among depositors in proportion to the size of the depositor's account.

In this new category of financial institution is the intergovernmental Islamic Development Bank (IDB) established in 1975 with funds from 22 Muslim countries. Membership has increased and now includes 33 countries, but the bank is dominated by Saudi Arabia, Libya, the United Arab Emirates, and Kuwait, which together have contributed more than two-thirds of its \$900 million funding. The IDB is designed to promote economic cooperation among Muslim countries in compliance with the *Sharia* law. Except for its emphasis on Islamic orthodoxy and the absence of interest charges, the IDB resembles most other regional development banks in that it extends funds for economic development projects and for balance-of-payments financing and supplies technical assistance to member countries.

#### *Taxes*

The compulsory tax (*zakat*, or alms) is one of the five pillars of Islam.<sup>1</sup> *Zakat* was instituted in the early days of Islam to help provide for the welfare of the poor at a time of gross wealth dichotomies. In most Muslim countries today *zakat* is a matter of conscience, although some proponents of Muslim states call for a formal *zakat* system administered by the government. Generally, the *zakat* is a flat-rate levy amounting to 2.5 percent annually on income and property. *Zakat* also applies to commercial goods, some categories of livestock, excavated treasures, and mined wealth. *Zakat* receipts can be used only for the poor and to promote Islam.

A similar tax, *ushr*, is collected on farm production. This tax has a long history as a source of revenue for Muslim treasuries. Traditionally, it is collected from Muslim farmers at harvest time on crop output in excess of production costs. Generally, the tax rate is 10 percent on crops from rainfed land and 5 percent on land on which the farmer must pay for irrigation. Both

<sup>1</sup> The five pillars of Islam mandated by the Prophet Muhammad are (a) a verbal declaration of God's uniqueness and the primacy of the Prophet Muhammad; (b) performance of daily ritual prayer; (c) contribution of alms; (d) fasting during the month of Ramadan; and (e) making the pilgrimage (*hajj*) to Mecca.



*zakat* and *ushr* clearly fit in with Islamic concepts of both state and individual social responsibility for the basic human needs of disadvantaged Muslims, and with the Islamic goal of income redistribution.

Shia Islam specifies an additional levy, a religious tax, *khums* (literally, one-fifth), paid to the family of the Prophet. This tax was eliminated by the Sunnis after Muhammad's death. The Shias maintain it, however, with the Shia clergy receiving the tax revenues. Traditionally, the tax as its name implies is equal to one-fifth of a Muslim's yearly cash income.

Beyond either privately administered or state-administered *zakat* and *ushr* levies, the tax system of Muslim states is similar to that of most developing countries. Although the laws of Muslim countries have their origin in the *Sharia*, the laws relating to taxation have in most cases been codified into civil statutes drawing on Western legal principles. Muslim countries generally have the usual complement of taxes on income, profits, transactions, property, and trade to generate revenues for government budgets.

#### ***Inheritance***

Another major mechanism for redistributing income by preventing the creation or hoarding of family wealth is the Islamic law on inheritance. At most, a person can allocate only one-third of his estate outside his family and may not make a will that deprives one of his legal heirs or favors one over another. The remainder of the estate is distributed among relatives in specific, legally defined shares.

#### ***Property and the Individual***

Besides these three unique characteristics Islamic economic institutions are not that much different from those of non-Muslim countries. Despite God's absolute ownership of all property, legal ownership of private property is safeguarded in Islam. Islam regards possession and ownership of property as the result of a natural human instinct and that it stimulates individual initiative and thus benefits society. Muslim ownership is more of a stewardship, however, and may be circumscribed if the owner demonstrates an inability to properly administer God's property or if the public interest requires it.

In effect, the Muslim community owns all property and grants stewardship either directly or implicitly to private individuals. Some property, such as rivers, roads, and public utilities, cannot be granted to individuals; some types of property, such as forest land and minerals, can be granted but later taken away if the public good requires. The state can retain control of whatever the community defines as indispensable for the people, or which if entrusted to private ownership will cause unnecessary hardship, or which is required for national defense. Nonetheless, private ownership is the rule and public ownership the exception in most Muslim states.

Property itself, however, is less important than the use to which it is put. The *Sharia* specifically points out that property use must benefit the community, cause no one harm, must not be used to secure undue economic or political power, and must be neither prodigal nor parsimonious. Islamic law discourages hoarding by requiring that property be put to at least some productive use. Indeed, property that is not put to use during a specific time period may be declared in the public domain and can be acquired by other Muslims by what amounts to homesteading. If the new owner fails to exploit the land within three years, however, it reverts to the state.

#### ***Contracts***

Contracts are valued highly in Islamic economies. The Koran directs that almost all transactions be put into writing. If a contract is freely and fairly negotiated, and written in the presence of witnesses, it is inviolable.

Contracts are used extensively in Muslim countries to facilitate particular forms of business organization. During Muhammad's time the prevalent forms of business organization were (a) partnership; (b) joint stock company; (c) business on commission; and (d) *mudaraba*. *Mudaraba* is a contract between two parties, one of which provides capital and the other labor. Both share in the profits and losses of the enterprise; labor is not paid a wage but receives a contractual share of the profits. *Mudaraba* is approved some by Muslim jurists as ideal for an Islamic economy because it recognizes disparities in wealth, encourages use of idle capital, and gives laborers a greater incentive to work.

Islamic law is ambiguous on business arrangements between landlords and tenants, especially in the agricultural sector. Islam condemns any tenant system that limits benefits to a few while neglecting a poor majority. Muhammad disliked cultivation for hire and empowered the Muslim state to forbid tenant farming whenever it was likely to damage the interests of the farmer or lead to disputes between farmer and landlord. Muhammad, however, was more opposed to the abuses he saw in landlord-tenant relations than in the system of hire cultivation itself.

In theory, the cultivator is only obliged to pay land rent out of his crop surplus (output minus costs). The level of rent will depend on the productivity of the land, the welfare of the farmer, and the cost of cultivation. Muslim jurists disagree on the legality of share tenancy, under which the landlord receives an agreed percentage share of output. The Hanafi school, for example, regards share tenancy as equivalent to a lawful partnership between capital and labor. More rigid interpreters cite sayings of Muhammad that the actual amount of produce constituting the share is uncertain (economic uncertainty being objectionable) at the time of the contract and that payment to labor of a part of what labor produces is prohibited. Contemporary opponents of share tenancy combine practical with theological arguments by also citing the tenant's disincentive to boost output or improve land. Most Muslim critics find it more acceptable if the cultivator rents for a predetermined cash payment so long as a contract is fairly negotiated.

### ***Wages***

An Islamic economy calls for a minimum wage sufficient to cover the cost of basic necessities for the worker and his family. Beyond the minimum, a normal labor market prevails. Workers are permitted any reasonable wage that does not infringe on the rights of the employer; alternatively the employer is cautioned against unfair wages that exploit the worker. Wages in the public sector must reflect equity and justice on both sides. Muhammad allowed only a 10-to-1 differential between the lowest and highest paid public employees; differentials were based on the nature of work, seniority, education, and skills. In theory Islam also prohibits restrictions on labor mobility and choice of occupation in order to stabilize wages nationwide.

### ***Risk and Uncertainty***

Many of Muhammad's teachings and subsequent interpretations were designed to stabilize economic life by correcting abuses in markets and by eliminating economic uncertainty. Islamic economies in theory prohibit monopolies, hoarding, withholding goods from markets, and price fixing. Muslim communities usually have the traditional post of *muhtasib*, a person who checks the weights and measures used in the marketplace and investigates cases of fraud. Forward transactions and futures markets are precluded by Muhammad's command that whoever buys cereals shall not sell them until he obtains possession. Because Muhammad found gambling disruptive of family and economic life, he prohibited making money by chance. As a result, auction sales are prohibited because the final selling price is uncertain at the start. Muslim scholars are divided on the issue of insurance. Strict constructionists argue that insurance is merely a form of gambling on the future and hence violates Koranic injunctions against profiting from uncertainty. A more liberal interpretation claims that, on the contrary, insurance is valid precisely because it protects the holder from uncertainty.

### ***Prohibited Activities***

Islam prohibits trade in certain goods the production and consumption of which has been deemed immoral. For example, trade in pork and any products from pigs is banned, as is trade in alcoholic spirits. In many cases the prohibitions on specific types of economic activity, such as the use of condemned goods or the employment of women, are not so much based on scriptures as on tradition, to which centuries of silent consent have given religious validity.

### **What an Islamic Economy Is Not**

An Islamic economy is not an economic system in the sense that capitalism or socialism are economic systems. Islam does not pretend to have a scientific theory about how an economy operates, or what institutions are required for its functioning. The form of economic organization in a Muslim country is irrelevant to Islam so long as its operation does not violate Islamic

principles. Within Islam's guidelines on responsibilities toward society and the limitations of personal capabilities there is in theory much freedom for individual choice. The performance of an economy of a Muslim country in any systematic sense still depends heavily on specific national characteristics, including the resource base, economic organization, cultural heritage, colonial influences, and extent of integration into the world economy, rather than on the degree of Islamic orthodoxy.

Islam is not a no-growth philosophy. It is not intrinsically opposed to economic and social development or to modernization. Many Muslim theologians since the middle of the 19th century have generally concluded that there is no serious conflict between Islam and modernization as such. On the other hand, orthodox Islam must by definition oppose secularization and hence is opposed to the more objectionable side effects of the economic development and modernization process that undermine religious influence, such as the introduction of materialist values, moral corruption, and the spread of purely secular political philosophies. There is, therefore, a danger that opposition to the side effects may be carried over to condemnation of the development process itself. In practice, conservative Muslims have generally lacked sufficient power to prevent development and modernization in the Muslim world; nonetheless they have caused serious disruptions in, for example, Iran and Pakistan.

With the possible exception of post-Shah Iran, no government of a Muslim country—as opposed to its conservative Muslim constituents—has shown any real desire to halt economic development for purely religious reasons. When development confronts Islamic orthodoxy, most governments have chosen development even if it meant evading or ignoring Islamic precepts that would interfere. Indeed, Islamic traditions of obedience to authority make it easier for governments to implement preferred policies. Nonetheless, the revival of Islamic consciousness means that political leaders will have to take Islam into account more carefully when forming policies.<sup>2</sup>

<sup>2</sup> Nonreligious factors can be at least as important brakes on progress as religious conservatism. Indeed, an upsurge of religious extremism is frequently a reaction to these factors, which include overpopulation, illiteracy, poor infrastructure, maldistributed wealth, corruption, inertia, and nationalism.

### Islamic Economics in the Modern World

Islam creates a vision of social utopia but is of little help in describing how it is to be reached. The Islamic concept of welfare economics was implemented in early Islam in Medina under the leadership of the Prophet and was expanded by the early caliphs to include a vast empire. Islam's success at that time resulted largely from its missionary zeal, the strong central authority of the caliphs, and the personal, ecumenical nature of Islam, which made territorial boundaries irrelevant. Beginning in the 10th and 11th centuries, however, Muslim economies moved away from the ideal set by Muhammad as political upheavals, the crusades, the Mongol wars, and the rise of asceticism fragmented the Muslim world. Much later, European colonialism contributed to cultural alienation.

Despite Islam's emphasis on welfare and brotherhood, Muslim societies have not shown any more benevolent attitude toward the disadvantaged than countries in the West. Indeed, child labor and slavery have flourished in the Middle East, and wage earners were no less exploited by Muslim capitalists than they were by the 18th and 19th century factory owners of Europe and America. Even today, Muslim economic precepts are only superficially honored and rarely enforced, serving instead to merely color the fundamental economic choices made by society. For example, the Wahhabi sect of Saudi Arabia has long been distinguished by its Islamic orthodoxy and protective condemnation of innovation; yet political reality there has frequently overcome religious opposition to contemporary economic development, albeit at a high social cost.

Part of the reason for Islam's failure to create a utopian state is the continued absence of any central authority to both define and implement it. The various Muslim groups have had differing patterns of relationships between Islam and the civil government. While Islam itself transcends national boundaries—which leads many to speak of the Muslim nation as a single entity—there is no central authority which can guide and control the Muslim revival. Muslim society contains many social and ethnic strata, schools, and

sects corresponding in a way to political parties in the West. These groups expound different, often conflicting theories, all of which they claim are based on valid interpretations of the *Sharia*. Consequently, religious conformism varies to a large degree both within and between Muslim countries.

Muslim religious and government leaders have frequently adapted the *Sharia* to the needs of contemporary economic development. Critics say that while this adaptive process is effective in assuaging religious consciences, it violates the spirit of Muhammad's intent. Interest is a case in point. The prohibition of interest by Muslim law results in widespread illegal usury, particularly in agricultural or seasonal communities where the need for funds is not synchronized with the generation of revenues.

An easy way out of the difficulty has been found in many Muslim communities. A borrower buys a quantity of staple merchandise such as wheat, sugar, or cotton from the lender on extended credit and at an inflated price. A notarized document is made acknowledging the debt, and the borrower then sells the goods back to the lender at the market price; the loss amounts to the interest forbidden by Muslim law. Modern Muslims tend to attribute such practices to the influence of colonialism, foreign domination, and decadent Western practices; yet there is ample evidence that these sorts of abuses existed in earlier times when foreign factors played no part.

Circumlocutious attempts to define the end result of money investments that generate additional money as something other than interest do not eliminate the basis behind Muhammad's ban, which was the concentration of wealth in the hands of the few. Similarly, the Koran's laws on inheritance, which, by restricting testamentary freedom and imposing a division of the heritage among specifically indicated relatives in fixed shares, are supposed to have hindered the accumulation of wealth in few hands.

In reality these arrangements, inspired by a concern for justice without any clear realization of the economic consequences, were more effective in preventing the transmission than the formation of great fortunes. Since enterprises in the Middle East tend to be mainly

family affairs, division of the property did not prevent the family from continuing to accumulate capital. If worse came to worst, the harmful consequences of possible division of an inheritance could be eliminated by the strategy of gifts to prospective heirs before the donor's death.<sup>3</sup> Moreover the Islamic invention of the pious foundation (*waqf*), which ideally supports schools, orphanages, shrines, and other institutions, is often abused by impious administrators to siphon off funds or perpetuate family control.

### Looking Ahead

The interpretation given to Islamic economic structures and the extent to which Islamic economic rules are applied will vary from country to country in response to domestic needs, a country's resource base, and the extent to which the country is integrated into the world economy. In consonance with national differences in resources, politics, and Islamic orthodoxy, the greatest effect of the imposition of Islamic economic principles would be on the domestic economy. Nonetheless, a bandwagon of orthodox Islamic economies would mean substantial changes in the way they deal with each other and with the rest of the world.

Foreign investment in Muslim countries, especially by the developed West, would be curbed and banking would have to operate under new and unusual rules. International companies that deal even peripherally in condemned goods might find their operations forbidden in a Muslim country. Commodity specifications would have to be watched carefully to avoid any vestige of condemned goods as raw materials, for example. Banks and other companies would have to revise criteria for loans and investment decisions based on the prohibition of interest charges. Muslim countries may force companies to comply with embargoes against countries or companies that are perceived as enemies of Islam.

<sup>3</sup> The harmful consequences of selectively strict application of Islamic inheritance laws are evident in Iran, where farmland has over time become fragmented into small, inefficient plots. Avoidance of estate fragmentation is also achieved by the common pattern in some Muslim communities of marriages between cousins.

Insofar as Islamic orthodoxy guides economic relations, its adherents would tend to deal more among themselves than with the world at large. The bazaar would likely emerge as the dominant domestic market form. Products offered would probably show a greater concentration of necessities and simple domestic manufactured goods. Non-OPEC Muslim countries, almost all of which are less developed and exporters of primary commodities, could experience slower growth should Islamic guidelines that emphasize agricultural self-sufficiency and self-styled autarky be implemented. Consequently, a widespread upsurge in Islamic economic rules could reduce the availability of and increase the price of some primary commodities in international markets.

Substantial changes probably would take place in the labor forces in countries that turned to orthodox Islam. Women would be eliminated from most occupations, save homemaker, and fall further behind males in acquiring education and skills. The immediate impact would be greatest on labor-short countries in the Middle East, which would have to pay the economic, political, and social price of imported foreign laborers. Over the longer run, even those Muslim countries with large labor surpluses could experience slower gains in economic welfare from excluding female labor resources from participation in development.

Muslim countries would probably experience a greater degree of economic instability under a rigidly Islamic structure. Economic policy decisions could be taken out of the hands of technocrats, businessmen, and politicians and put into the hands of religious leaders who have a different vision of a country's destiny. Muslim countries would have to rely more heavily on decisions by religious-political leaders in sorting out priorities and in settling the pattern of investment, consumer demand, prices, and the distribution of income and wealth. The economies would be more insulated from international market forces. The prohibition of interest charges would eliminate or substantially weaken monetary policy as a tool for rationing investment funds and implementing government policies. Muslim countries would have to give greater weight to incomes policies to control demand and prices, and public spending would play a larger role in the economy.

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## Appendix B

### Major Sects and Schools of Islamic Law

Islam is divided into two major sects, Sunni and Shia. Nearly 80 percent of Muslims are Sunni, which is considered the orthodox sect. A major difference between Sunni and Shia Islam in a way parallels the distinction between some Protestant sects and Roman Catholic Christianity. Sunnis believe that man is capable of communicating with God independently on his own terms and that any devout Muslim can aspire to be a temporal leader of Islam. Shias, on the other hand, hold that man needs an intercessor (Imam) between the human and the divine, and that the political-religious leadership of the Islamic community rests with an unbroken chain of Imams who are descendants of the Prophet's son-in-law, Ali. Disputes over leadership succession have further split Shia Islam into several subsects. Shia predominates in Iran, Iraq and Bahrain, but there are Shia minorities in many Sunni-dominated countries.

About 3 percent of the world's Muslims are members of the mystical *Sufi* movement that probably began in Iran in the 8th century in reaction to the general worldliness that had overtaken the Muslim community. *Sufis* are ardent missionaries and are responsible for Islamic conversions in India, central Asia, and northern Africa.

The violent discussions that raged in the early history of Islam after Muhammad's death in 632 in regard to religious, legal, and political questions resulted in the evolution of different schools of interpretation of Islamic law. Of the major schools four survive: Hanafi, Maliki, Shafii, and Hanbali. Shia law was for long excluded by the Sunnis, but al-Azhar, the Sunni university in Cairo, now recognizes it as a fifth school. The first four are orthodox Sunni Islam, and a Sunni may belong to any one of them. A Muslim can transfer allegiance from one school to another, but once chosen its decisions on faith and law are binding.

The comparatively liberal Hanafi school is followed by the majority of Muslims, especially those in India, Pakistan, Afghanistan, central Asia, Turkey, and lower Egypt. In the 8th century, Abu Hanifah sought to broaden the base and reduce the rigidity of divine law by introducing analogical reasoning (*qiyas*) as a valid source of law. Believing that "necessity renders legitimate that which is, strictly speaking, forbidden," Abu Hanifah leaned more on opinion and less on tradition than other Muslim interpreters.

The Maliki school, on the other hand, is based heavily on the traditions, sayings, and deeds of the Prophet. It makes only limited use of the consensus of the community. This literalist school was founded by the theologian-jurist Malik ibn-Anas in the 8th century and today is the prevailing tradition in north and west Africa and in upper Egypt.

In the 9th century, Muhammad ibn-Idris al-Shafii tried to reconcile Hanafi and Maliki law but ended up creating a third, relatively liberal school. Shafii jurisprudence predominates in Southeast Asian Muslim communities. Shafii's main principle was that the ultimate source of legislation was the Koran, and that secondary sources (tradition and consensus) had to be linked to the Koran in an authenticated manner. Analogy was permitted only grudgingly if other sources were totally inadequate.

Ahmad ibn-Hanbal, a student of Shafii, founded the smallest and strictest school of law. Its most notable adherents are the Wahhabi movement in Saudi Arabia. The Hanbali recognize literal interpretations of the Koran and Prophetic traditions as valid sources of law. They underplay consensus, and reserve analogy only for dire necessity.

*This appendix is Unclassified.*

## Appendix C

### The *Sharia*

The entire body of Islamic law is called the *Sharia*. It covers religion, dogma, and law in the usual sense but also includes economic, social, and political behavior. It must be followed by all Muslims. The *Sharia* is composed of several sources of legal statements. For Sunni Muslims it includes the Koran (the word of God), the *sunna* (the practices of the Prophet), and *ijma* (consensus). Shia Islam, in addition, considers two other sources of law valid, *aql* (reason), and *ijtihad* (interpretation by legal authorities).

The primary source of law for the *Sharia* is the Koran, God's word revealed to the Prophet Muhammad in the early 7th century. The Koran is not a law code and Muhammad was not a lawgiver in any Western sense. His teachings and prophecies are cut to the requirements of his own environment and were generally inspired by and promulgated to fit specific cases. Instead, the Koran is an appeal to mankind and to Muslims in particular to obey the law of God.

To most Western eyes, the Koran does not contain the elaboration thought necessary for a more complicated society than existed in 7th century Arabia. Muslim purists, however, believe that true Islam can be based only on the Koran (and the *sunna*) and that in them can be found precepts valid for any time, place, or occurrence. Moreover, analogous to the believed supremacy of the Latin mass among fundamentalist Roman Catholics, the true Muslim, regardless of his nationality, considers valid only the Arabic text of the Koran.

Within the *Sharia* the Koran is augmented by the *sunna*, which is the body of commands, approvals, prohibitions, and acquiescences of the Prophet Muhammad. The individual actions (the *sunna*) are found in the *hadiths*, or the narratives of what Muhammad and his companions actually or reportedly said and did. For the Sunni, the authority of the traditions of the caliphs and the companions is less than those of the Prophet himself. According to Shia principles, an authentic tradition attributed to the Imams (the successors to Ali) is as binding as the direct word of God through Muhammad. Much

Muslim scholarship has gone into proving the validity of the traditions passed down through centuries by tracing them back through "respectable men" to their original sources.

To cope with circumstances not directly related to Koranic or *sunna* references, *ijma* evolved as a source of law. The Sunni recognize both consensus of the doctors of law and of the community. This broad communal input to *ijma* leads to a relatively more pragmatic and liberal interpretation of law than that of the Shias. The latter claim that all knowledge derived from fallible men is useless and that truth can come only from God as relayed through the Prophet Muhammad and subsequently through the infallible Imams. Hence for the Shias, *ijma* means the consensus of those who interpret in their religious arguments the commands of the Imams on a particular question—in other words the *mujtahids*.

Shia Muslims recognize as well *ijtihad*, or the interpretation of situations by the *mujtahids*, as an input to the *Sharia*. *Ijtihad* has been defined by Shia jurists as the capacity or ability to discover law through juristic speculation and reasoning. Shia scholars argue that the concept of *ijtihad* provides the means for reinterpreting law in the light of modern requirements. This contrasts with the Sunni practice that requires textual support for legal decisions.\* For the Sunni, the right to make fresh decisions based on *ijtihad* was closed after the great lawmakers finished their work in the 10th century.

Finally, Shia Islam prescribes *aql*, or human reason, as an input to the *Sharia*. *Aql* is not the private use of reason or opinion, but rather the basic human intellect by which rational man arrives at universal truths, such as that "murder is abhorrent." *Aql* permits the truth to be discovered when *Sharia* texts differ or contradict each other.

\* Sunni Islam permits a limited adaptation of law to modern circumstances through *qiyas*, or analogy between current issues and Koranic and *sunna* rules.

*This appendix is Unclassified*

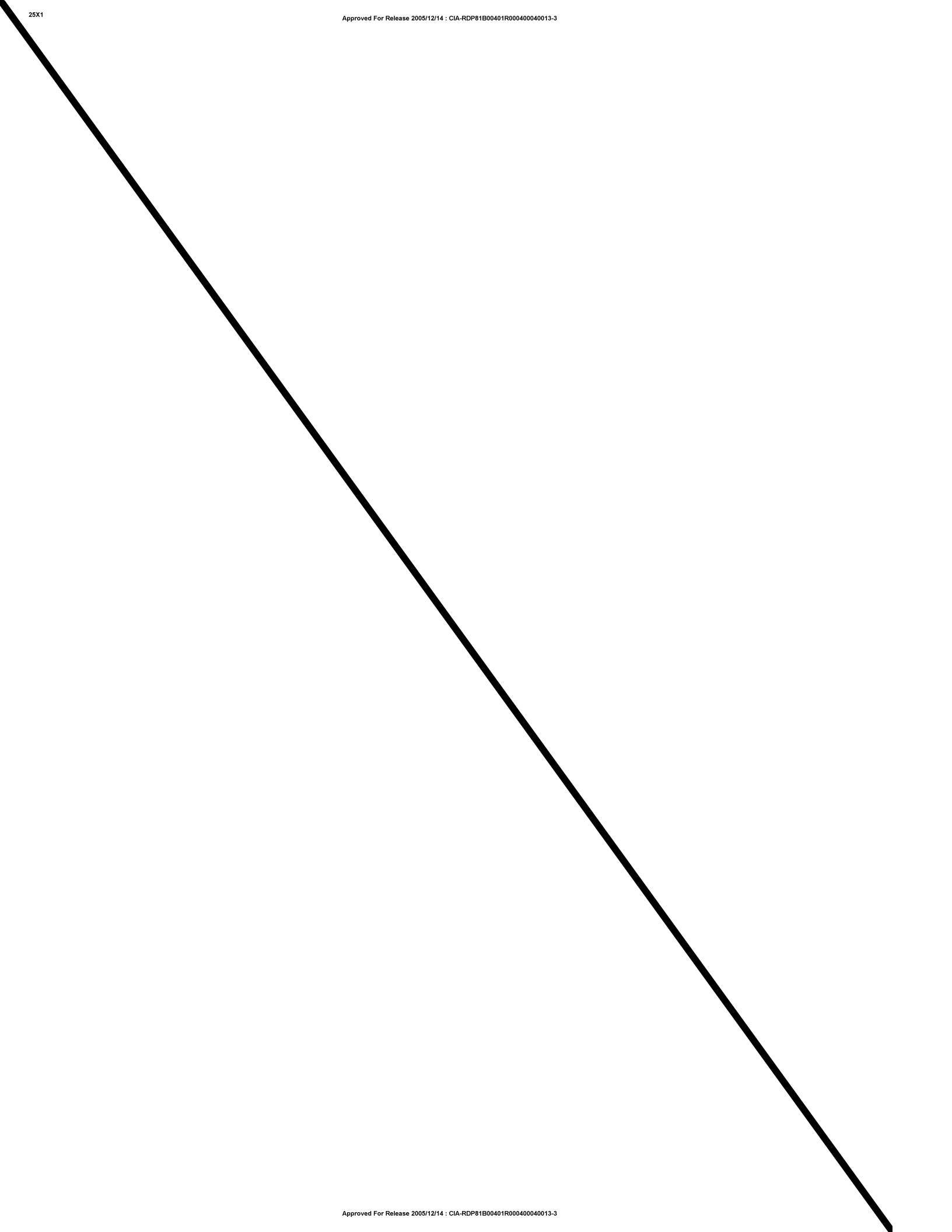


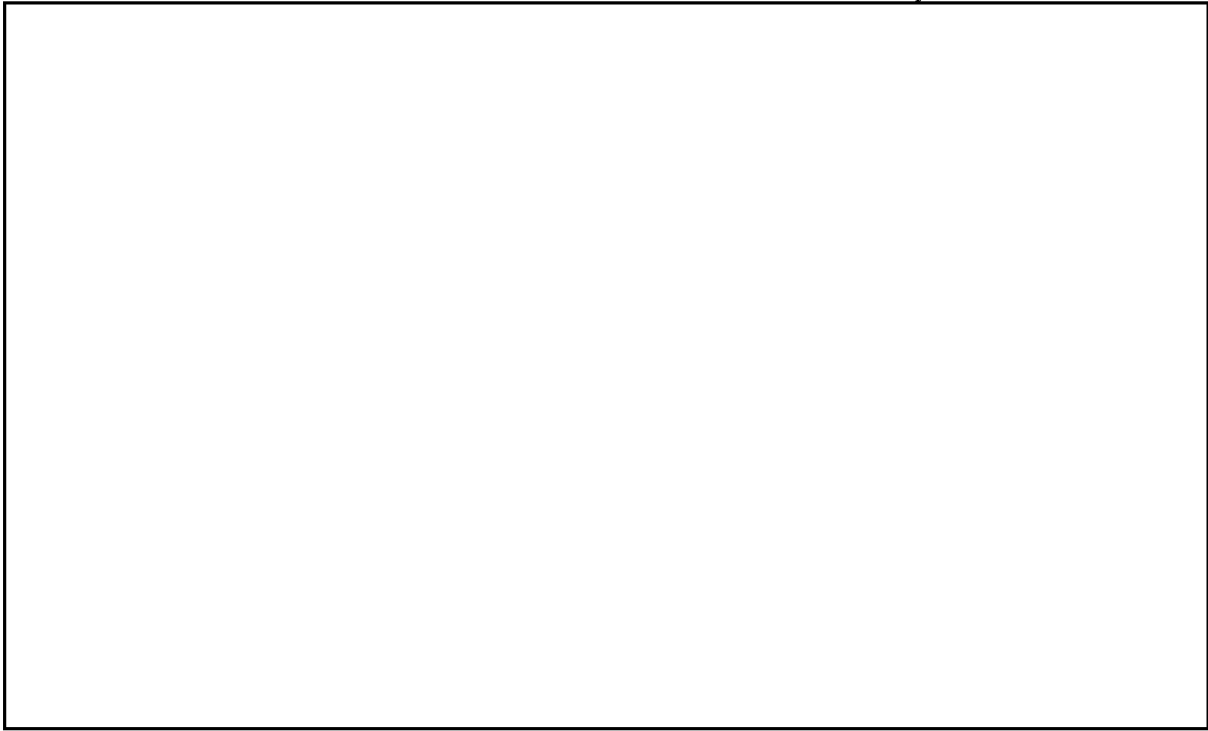
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
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
IRAN: THE BAZAARIS—FINANCIERS OF REVOLUTION



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Among the socioeconomic groups most disrupted by the Shah's reform programs were the bazaaris—the traditional traders, bankers, and businessmen of Iranian society. Conservative, religious, and nationalistic, they felt driven to renew their traditional alliance with Shiite religious leaders—the Shah's number one enemies—in order to reestablish the old order. This alliance served as the inner core from which the revolution spread. For their part, the bazaaris contributed financing and an organization and communication system that helped put thousands of demonstrators into the streets. 

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Six months after the revolution, the bazaari backing for Ayatollah Khomeini may be on the wane. Many merchants are unhappy with continuing unsettled economic conditions. More important, they are disturbed by the nationalizations of private businesses and the recent trial of shopkeepers for profiteering. Further economic deterioration could shift bazaari allegiance to other religious leaders or even to a strong secular personality should one begin to emerge. Signs of disenchantment with the revolution are already apparent—notably the support of some bazaaris for the Moslem People's Islamic Republic Party of Ayatollah Shariat-Madari instead of the Islamic Republic Party of Khomeini's. 

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### Traditional Role and Influence

The bazaar in Iran is the long-established center of financial and commercial activity. More important, it is also a symbol for the merchants, traders, and businessmen who compose the bulk of Iran's middle class. These individuals share a common heritage and deep-rooted values, even though their activities, such as manufacturing, have spread well beyond the physical boundaries of the bazaar itself. Although their once overwhelming influence over the Iranian economy was eroded by industrialization and the rapid growth of the economy and government power over the last two decades, the bazaaris have remained the commercial core of every Iranian city. On the eve of the revolution, the bazaaris still accounted for an estimated one-third of imports, most nonoil exports, and two-thirds of retail trade. Furthermore, the moneylenders of the bazaaris controlled up to one-fourth of domestic financial dealings. [REDACTED]

The influence of the bazaar extends well beyond its commercial and financial activities. The bazaaris, who number 400,000 in Tehran alone, have more daily contact with the people in every city and village of any size than the mullahs. Through extended family connections, the bazaaris have influence with professionals and intellectuals. Although often only attending lower level religious schools themselves, the merchants have been able in recent generations to send their sons to institutions of higher education. These family members have moved into places of prominence in law, medicine, the universities, and the government bureaucracy. [REDACTED]



### Organization

Within and between bazaaris, the merchants are linked by centuries-old family, ethnic, tribal, religious, and commercial ties. Since kinship is of great importance in Iranian society and friendships outside the bazaar are minimal, these ties along with personal friendships provide a powerful basis for unifying and organizing. Hence, the bazaaris by consensus recognize a head for each major business branch, who needs never be elected formally. These leaders have a network of lieutenants who in turn run their own subgroups. The pyramidal structure extends down to the *luti*—the tens of thousands of porters and laborers who work in the bazaaris. [REDACTED]

Over the course of centuries an unwritten code of behavior and honor based on

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Islamic principles has evolved. The community disburses both aid and punishment; it supports the needy until they can get back on their feet, while ensuring that those in disfavor are given no opportunities in the bazaar. No merchant can afford to disregard the hierarchy of the bazaar for fear of being blackballed. [REDACTED]

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### Connection With the Mosque

Islam is a common denominator among most bazaaris, playing an important role in their lives. Formal observance of Islam, with its emphasis on regular communal activities, provides a basis for social solidarity which in turn lays the foundation for concerted action in the self-interest of the bazaar. Religion also provides a legitimate channel for the display of wealth and prestige in the community. A pious bazaari is ascribed personal qualities beneficial to his business dealings; a show of wealth is viewed as the just reward for the fulfillment of religious duties rather than as conspicuous consumption. [REDACTED]

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The bazaaris hold a prestigious position in Islam, which was founded by a successful businessman\* and respects trade as the most noble occupation and the most lawful profession. Trade is viewed foremost as an event entailing human contact and dialogue rather than as a commercial transaction; hence, it is considered proper to trade in the bazaar but improper to shop in impersonal supermarkets. The *Makaseb* (the collection of Shiite commercial laws) governs business dealings in the bazaar though these are often not strictly observed since few of the bazaaris can read Arabic. [REDACTED]

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For their part, the bazaaris have been among the staunchest supporters of the mosque, both financially and philosophically. Traditionally, they provide the bulk of mosque funds through tithing up to one-fifth of their income; prior to the revolution, about 80 percent of the money available to Shiite leaders came from the bazaar. The bazaaris also listened sympathetically to the clergy's complaints and supported a return to Islamic fundamentalism. Besides financing, the bazaaris have aided the mullahs in times of upheaval by mobilizing their forces and using their communications network to help paralyze the economy and bring mobs into the street. Prior to the 1978 revolution, the merchants had supported the mullahs on at least two occasions in this century—the Constitutional Revolution of 1905-07 and the urban riots of June 1963. [REDACTED]

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### Opposition to the Shah

The bazaaris' antipathy for the Shah had philosophical, religious, and commercial roots. The Western-oriented industrialization drive of the Shah ran counter to the conservative, Islamic-oriented outlook of the bazaaris, while his modernistic policies stirred opposition on religious grounds. Early on, the bazaaris supported the embitt-

\* Mohammad and the first caliph are counted among the most famous merchants of Mecca. [REDACTED]

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tered clergy in their protest against the Shah's land reform, which removed much of the *waqf* (religious) lands from mosque control. Likewise, the merchants joined religious Iranians in opposing modernizing measures such as coeducation and women's divorce rights. [REDACTED]

Opposition to the Shah also had a strong commercial motivation. In the rush toward industrialization, the bazaar was being bypassed. Newcomers with palace and government connections were reaping the rewards of economic development—often through bribery rather than the time-honored bazaar tradition of bargaining. Government-sponsored banks began to take over financing and state enterprises often took near-exclusive control over much of the trade, such as in caviar, tobacco, and many agricultural commodities. [REDACTED]

Other unpopular acts affecting the bazaaris include:

- Implementation of price controls in 1975, policed by 10,000 inspectors. At least initially, the power of the bazaaris to control the minimum price of almost every commodity retailed in Iran was diminished. A reported 250,000 shopkeepers nationwide were penalized for breaking controls before the program died down; 8,000 merchants served prison sentences.
- An attempt to make the bazaaris pay social security contributions for their workers. This was unacceptable to the bazaaris who take care of their own and practice charity according to the rules of Islam. Protest was so strong that the government had to back down. Even this did not calm the angered bazaaris since taxes and government efficiency in collecting them continued to rise at the time when recession threatened their well-being.
- A decision by the Tehran city government, never implemented, to build a freeway through the center of the bazaar [REDACTED]

### Aftermath of the Revolution

While the bazaaris have demonstrated their ability to influence events in Iran, they have gained little economically from the revolution. Even though government interference in their activities has been reduced, the bazaaris have not proved able to mold government policies in their favor. They have received no special benefits and, in fact, have been hurt by the downturn in economic activity. [REDACTED]

Immediately after the revolution credit was tight and international trade severely curtailed. This situation now appears to have eased a bit. Shops are well stocked with less expensive consumer items, and there are signs of an upswing in consumer spending. The more expensive consumer durables, however, are probably moving slowly, as many of the upper middle class have left Iran, or are attempting to leave.

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Nonoil exports are still curtailed, with carpet exports totally banned. Both legal importation and smuggling of food and consumer items seems to have picked up, but imports of other categories of goods are still depressed. [REDACTED]

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### Outlook

It is not clear whether the reduction of government influence and the resurgence of Islam will be enough to ensure continued bazaari support for Khomeini. The bazaar remains a stronghold of traditional religion in Iranian society, and many bazaaris still appear to be aligned with the Ayatollah. Support could evaporate, however, if the economy deteriorates and the security situation worsens in the months ahead. While religious, the bazaaris are pragmatic in monetary matters, and they could turn to other religious leaders or to a strong secular leader who would restore stability and profits to the country. [REDACTED]

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Two postrevolutionary developments have been particularly disturbing to the bazaaris:

- The recent nationalizations of banks and other businesses are viewed as a major threat. Speaking for the bazaaris, Mahmud Manian recently demanded that the government return certain nationalized enterprises to private ownership. He stated that bazaaris should be allowed to return to their old ways of controlling business and commerce and exhorted the government to adopt a free market policy.
- Another foreboding event was the prosecution of three Tehran shopowners and a trader for profiteering by a special court of the Khomeini Guilds Committee. The Committee urged residents to report any trader or shopkeeper found "indulging in actions against the ideals of the Revolution" such as profiteering and hoarding. This development is strikingly similar to the Shah's previous price control campaign. [REDACTED]

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There have been growing signs of disenchantment with the Khomeini revolution. On occasion, a rural bazaar has shut down in protest of heavy-handed activities by revolutionary committees. Some bazaaris have been hedging their bets by paying protection money to the leftist Fedayeen organization. There are also indications of increasing bazaari support and funding of the Moslem People's Islamic Republic Party of Ayatollah Shariat-Madari. The US Embassy in Tehran reports that Shariat-Madari's picture is replacing Khomeini's in many bazaar shops—a low-key form of protest. [REDACTED]

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IRAN: UNREST AMONG PEASANTRY

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Iran's 17 million rural inhabitants—hitherto supporters of the new Islamic Republic—are becoming increasingly restive. This trend could accelerate in the coming months unless the regime can devise and implement effective agricultural policies. The policies so far suggested by the revolutionary leadership—including a rural-based Iran and a reversal of rural-urban migration—probably would depress agricultural activity and fan resentment. Rural tensions—some of which began with the Shah's land reform in the 1960s—already are being reflected in widespread land seizures as the breakdown in law and order continues.

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Rural Traits as Basis of Political Apathy

Most Iranian peasants have little knowledge or interest in life beyond the village. Over the centuries, they have acquired a deep-seated distrust for government officials, who are viewed as outsiders interested only in exploiting the villagers. The limited interest rural dwellers display in life outside the village has been the result of their membership in tribes or ethnic minorities, which for many purposes transcends class relations.

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A strong sense of individualism and the focusing of primary loyalties on the family have been major factors in the peasants' isolation and political apathy. The extended family is the basic social unit in rural areas, providing its members with identity, security, and social orientation. The traditional importance of the family is reinforced by Islamic beliefs and practices.

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Illiteracy and fragmentation of the rural sector—only one-fourth of the 65,000 villages scattered about the countryside have more than 250 inhabitants—have also bolstered the inwardness of rural life. Books and teachers have been scarce, and, in any case, educational attainment previously has had little effect on income. The Literacy Corps, formed by the Shah from urban students doing national service, managed to penetrate into some of the isolated rural areas. Nevertheless, even in the early 1970s enrollment in primary education was still only 40 percent in rural areas compared with 90 percent in the cities. About 3 million primary school age children remain out of school primarily because of parental objection.

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## Forces of Change

The pattern of rural life was jarred in the 1960s by a land reform instituted by the Shah as part of the White Revolution. Although achieving its primary goal of breaking the power of the absentee landowners, the land reform failed to coalesce new political support for the Shah and widened the gap between landed and landless peasants. Under the program, only two million peasant families (*nasaqdars*) were given the right (*nasaq*) to work a particular piece of land; the majority of agricultural workers and village laborers (*khushnishins*) were outside the program. While the *nasaqdars* for the most part remained close to the subsistence level, their social and economic standing relative to the *khushnishins* improved somewhat. [REDACTED]

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Land reform did little economically to help agriculture, which was downplayed by the Shah in his drive to modernize industry in the 1970s. In fact, land reform compounded the problem of small-scale production, contributing to the inability of agriculture to meet rapidly rising domestic demand. Iran shifted from being a net exporter of agricultural goods in the late 1960s to being a net importer of one-fourth of its food in 1978. Although the average Iranian peasant is better off in absolute terms today than a decade ago, the gap between rural and urban incomes has grown—peasant incomes in 1978 were only one-fifth of urban worker incomes, compared with an estimated one-third in 1970. As the oil bonanza pushed up urban incomes, the government kept food prices low, the increased demand for food being satisfied largely through imports. In short, the peasant failed to get the economic return normally dictated by boom conditions. [REDACTED]

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Thousands of farm workers continued to be pulled into the cities by the Shah's industrialization drive. Migration created rural labor shortages and, as workers revisited their native villages, heightened awareness of the outside world, its material goods, and its political events. [REDACTED]

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Despite increasing discontent, rural dwellers, by and large, did not participate actively in the Islamic Revolution of late 1978. At the same time, the rural population was sympathetic to the idea of a more religious Iran and was traditionally opposed to strong central governments. The thousands of demonstrators that the mullahs were able to put in the streets were made up largely of peasants who had migrated to the cities. [REDACTED]

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## Aftermath of Islamic Revolution

While the revolution originally was an urban-based phenomenon, it has had an increasing impact on the rural sector. The large commercial farms that were untouched by the Shah's land reform and that yielded one-half the value added in agriculture have suffered from the general disruptions of the economy. For example, port strikes and payment difficulties have cut imports of animal feed, forcing two-thirds of the poultry businesses to close. Cotton output has been reduced because of

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widespread shortages of fertilizer and pesticides, attributable to strikes, fuel shortages, and turmoil in the ports. Subsistence farmers, less affected by these problems, should benefit this year from favorable weather. [REDACTED]

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Widespread land usurpations, not only by *khushnishins* but also by former landlords who lost their lands to land reform, are deepening the feeling of insecurity. Losses in farm production in the richer lands of the North (including Mazandaran) and West, are particularly heavy; many districts are controlled by ethnic minorities, some of whom are seizing land and some of whom have been in open revolt. [REDACTED]

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### Policies of the Government

Khomeini's vision of an Islamic Republic in Iran does not yet include specific plans for the rural sector although he has expounded a vague goal of agricultural self-sufficiency and a society based on rural virtues. An original aim of the revolutionary leaders was to give every rural dweller a plot of land—the Koran holds that every person is entitled to own the land he works. More recently, Khomeini has alluded to some form of land reform that could (a) return to the religious establishment lands taken during the Shah's land reform program and (b) give to the poor those lands on which owners have not paid "Islamic Taxes." Khomeini's economic adviser Bani Sadr has also suggested that 1.6 million workers encouraged to migrate to the cities by the Shah be returned to the rural districts and live in the old network of villages. While Bani Sadr has admitted this might resemble a Kampuchea-style operation, he optimistically maintains it could be accomplished by the use of faith and persuasion rather than force. [REDACTED]

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The Bazargan administration has allocated funds for low-interest agricultural loans and has eased government restrictions on the importation of agricultural inputs, such as feed grains and pesticides. It has also raised the support prices for domestic cereal crops and has restricted the importation of some fruits to help local producers. The administration, however, has been too disorganized to make hard decisions on basic agricultural policy. [REDACTED]

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### Outlook

The Iranian Government needs peace in the countryside and peasant cooperation to begin restructuring the economy. The Islamic leadership may be able to use the increased prominence of Islam to maintain at least passive support among most peasants. Except for ethnic minorities struggling for autonomy, most rural dwellers simply want to get on with the business of living their own lives with a minimum of government interference. Peasant attitudes could change radically if government initiatives adversely affected rural lifestyles. [REDACTED]

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Khomeini could find, like the Shah, that land reform often causes more problems than it solves. In addition to the land fragmentation that could occur from further land

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reform, plots would become even smaller if land were divided among the inheritors as required by Islamic Law—a practice abolished under the Shah but obviously favored by religious leaders. Aware of the effects on production, some leaders may soft-pedal land reform; a few religious leaders have already conceded that the Koran does not provide a guide for the way larger enterprises, such as commercial farms, are to be handled. Regardless of the course of land reform, land usurpations are continuing. Because of the continued general instability of the countryside, friction between the landed and the landless almost certainly will mark the rural situation. [REDACTED]

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With urban economic activity severely depressed and government deemphasis of industrialization, job opportunities in the cities have dried up. Government attempts to send former rural inhabitants back to the country might be inaugurated to reduce urban unemployment and to alleviate labor shortages in some rural areas. Most former villagers are unwilling to return to the harsh conditions of the countryside. Their lack of incentive, poor attitude toward rural life, and exposure to urban politics would lead to further social and political disruptions. [REDACTED]

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IRAN: URBAN LABOR FORCE—FERTILE GROUND FOR UNREST [redacted]

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The modern labor sector, which played a pivotal role in the Shah's overthrow, represents a volatile and destabilizing force in today's Iran. While Iranian urban workers have given enthusiastic political support to Khomeini, they have been unresponsive to his calls to sacrifice for the revolution and to resume productive work. As the semiparalysis in urban commerce and industry continues and as subsistence funds rapidly dwindle, urban workers will become even more dissatisfied. Unless the economy revives, these workers, newly aware of their political clout, could become a focal point in a growing challenge to the Islamic Republic [redacted]

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Characteristics of the Modern Sector Labor Force

The urban labor force grew rapidly in the post-1973 oil boom years, as rural dwellers flocked to the cities in search of construction and factory jobs created by the Shah's industrialization drive. These migrants were almost exclusively male, very young—most often the 15 to 34 age bracket—and generally illiterate, unskilled, and religiously conservative. Many of the newcomers sought employment in Tehran, where more than half of all manufactured goods are produced. They also moved into the steel, petrochemical, refining, and ordnance plants of Isfahan; the electronics industry centered in Shiraz; in the heavy engineering industry of Tabriz; and in the oil industry center of Ahwaz. [redacted]

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Despite their lack of skills, the new entrants found themselves in a sellers market where they could command high salaries. This resulted in pampered workers, whose high rate of absenteeism, theft, job-hopping (annual turnover in many plants reached 45 to 50 percent per year), and slowdowns made them among the least productive and most expensive workers in the world. [redacted]

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Iran lacks the tradition of an independent labor union organization, and labor's political power was weak up until the revolution. Workers had been frequently used as political pawns by the Shah, first in a power play against the large landowners and then against the growing strength of the industrialists. In 1957, the Shah outlawed all unions, fearing that the extreme youth and inexperience of the industrial labor force made the workers easy prey for political subversion. By 1962, he had switched tactics, encouraging government-controlled unions, as a way to control leftist influence. Only those unions certified by SAVAK were permitted to function, usually under hand-picked leaders. [redacted]

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As Iran's financial position strengthened in the mid-1970s, the Shah's government initiated efforts to buy worker loyalty. Labor relations became increasingly paternalistic. The government passed laws granting workers automatic pay hikes, generous

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social benefits, and opportunities to buy into company ownership on favorable terms. It also sided with workers in labor disputes and enforced the 1959 labor code provision that no worker could be fired until his case was reviewed by the Labor Ministry Court, which usually found in favor of the worker. [REDACTED]

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### Labor Bloom Begins to Fade

Despite increased benefits and wages, many urban workers had become disenchanted with their lot by the beginning of 1978. Their rising expectations were being stifled by (a) the economic downturn, which increased unemployment, especially in the construction sector, and (b) the deterioration of living conditions in the cities. Workers became more active in pressing their demands for better pay, longer vacations, and improved pensions. The government's repeated assertion that it intended to reduce annual bonuses—which often amounted to several months' pay—increased wildcat strikes. [REDACTED]

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As general political turmoil took hold in Iran, unemployed and underemployed workers, living on the fringes of society in places such as south Tehran, joined the anti-Shah demonstrations. For the most part, however, participating workers were not members of identifiable worker groups. Generally they were recruited by representatives of neighborhood mosques responsible for organizing protests. [REDACTED]

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As the anti-Shah movement built up steam in the second half of 1978, workers in government ministries, factories, and in the vital oil fields walked off their jobs. The strikes in the southern oilfields were the critical expression of labor's force in the revolution and were pivotal in the Shah's overthrow. Even with the intervention of emissaries from Ayatollah Khomeini, who was still exiled in Paris, the independent-minded oil workers initially refused to return to work. Their resistance was made easier, as was that of factory workers, by their continuing to receive paychecks while on strike. [REDACTED]

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The government, hoping to defuse worker protests, granted practically all their exorbitant wage and fringe benefit demands. This sign of government weakness merely encouraged additional groups to walk off their jobs and fostered a shift from economic to political demands. [REDACTED]

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### Labor in Postrevolutionary Iran

With much of Iran's modern urban-based economy at a standstill, the lot of the average urban worker has further deteriorated since the revolution. Although the extent of unemployment is disguised by padded employment rolls, we believe that between 3 million and 4 million workers (out of a national labor force of approximately 11 million) are without jobs; several million more are underemployed. Many of the 1.2 million workers formerly employed in the construction sector, unlike idle industrial workers, are not being paid and must subsist largely on a cushion of personal savings, family assistance and help from the Mosque. [REDACTED]

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Many workers are demonstrating their dissatisfaction with current conditions through strikes and sit-ins, but most are biding their time in hope that the revolutionary leadership will eventually be able to fulfill its promises to improve their lives. Workers in the modern labor sector, having successfully flexed their muscles during the revolution, have not responded to urgings to sacrifice for the revolution. Many workers have ignored Khomeini's call to return to their jobs to help revitalize the moribund economy, and the nationalization of the nation's major industries apparently has not spurred workers to resume productive activities. [REDACTED]

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Oil workers, who many think were the proximate cause of the Shah's downfall, have returned to their jobs, but are demanding a voice in National Iranian Oil Company (NIOC) management and in government directives concerning oil. While oil production has remained at or near the 4 million b/d level between April and mid-August, the decision to produce at that rate apparently required the okay of oil workers. Since 22 August, labor unrest has caused intermittent falloffs in production though it is now reported to be back up near normal levels. In Khuzestan Province, where 90 percent of Iran's oil is produced, local Arab leaders have threatened to cut off production/exports completely if the Khomeini government refuses to meet their demands for improved conditions and a measure of local autonomy. [REDACTED]

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Worker committees that sprang up during the revolution—composed in many cases of the most radical workers in a given enterprise—have served to reinforce worker resistance to a return to normalcy and have successfully kept prerevolutionary management at bay. Committees have demanded the right to involve themselves in all aspects of management, including the formulation of wage scales, social benefits, and the selection of supervisors, and have insisted that management agree to follow all decisions voted on by the committees. Moreover, in those factories where managers tried to eliminate nonproductive workers, committees have successfully demanded severance benefits equal to as much as six months' pay for each year worked. This has effectively prevented most layoffs. [REDACTED]

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We have only spotty information about labor/political organizing among workers in Iran since the revolution. We assume that radicals and leftists of various stripes have taken advantage of continuing chaos to recruit workers to their cause. An Iranian political analyst asserts that the "chariks"—Marxist guerrillas—are courting workers with economic assistance and are sponsoring "educational" sessions at factory sites during lunch hours. [REDACTED]

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### Government Efforts and Plans

Apart from pleas from Ayatollah Khomeini for workers to cease strike activities and resume productive work, the government has done little to cope with the problems of several million unemployed and underemployed. Minister of Labor Darius Foruhar, who has conceded that there is a role for legitimate trade unions, opposes worker interference in management functions. Foruhar claims that the

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25X1 government has established a "special force" to regulate labor and to reduce worker interference. [redacted]

25X1 Foruhar claimed that the government intends to reactivate stalled rural highway and housing projects in an effort to encourage local residents to remain and to attract urban unemployed to return to the countryside. According to Admiral Madani, the Governor-General of Khuzestan Province, several public works projects have already been funded to achieve these objectives in his province. In April, the government also created a \$140-million-per-month loan fund to provide emergency aid to the unemployed. Until recent weeks, little money has been disbursed from this fund. In any case, this fund, even if fully spent, would barely put a dent in the nation's unemployment problem. [redacted]

### Outlook

The government thus far has been unable to decide on the desirable composition and level of production in postrevolutionary Iran. This indecision, coupled with intransigent labor problems, precludes any meaningful economic revival in the near term. Workers who hoped to reap substantial economic benefits from the new Islamic government find their rising expectations dashed by high unemployment, rising inflation, and shortages of goods, including textiles, plastics, vegetable oil, soaps, and detergents, certain medical supplies, auto parts, and paper products. [redacted]

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As the lot of the urban unemployed and underemployed worsens, increased political activity can be expected. The core of young illiterate, unskilled, and unemployed city workers could turn to the left. Moreover the modern middle class, many of whom lost their jobs when foreign-owned companies folded, has found its hopes dashed as well. Although Khomeini currently remains the commanding presence in Iran and clearly retains the allegiance and adoration of most of the modern labor force, the seeds for eventual demise of the Islamic Republic may be planted in his failure to revive the economy. [redacted]

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A revival can only come about if the government overcomes its provisional image and self-perception, develops confidence in itself, and comes to grips with the need to generate a comprehensive economic policy. New upper- and middle-level managers will have to be developed to replace those who have left the country, been imprisoned, or fired. In addition, the more intransigent worker committees will have to be brought under control and the policy against dismissals reversed. Recent reports indicate that the last two requisites are beginning to be met. [redacted]

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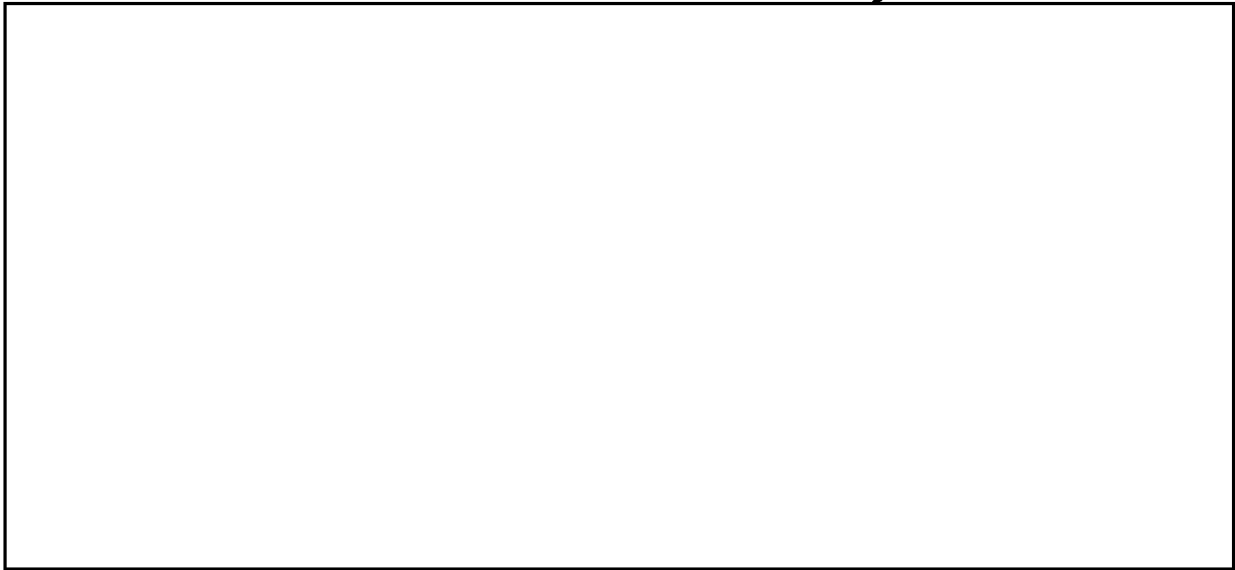


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Economic Intelligence Agency Weekly Review



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IRANIAN CIVIL SERVANTS: CHAMELEONS OF REVOLUTION

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Civil servants, the predominately middle class technocrats in the boiler room of any functioning Iranian government, participated in but were not leaders of the Islamic Revolution. Government workers joined the Shah's opposition out of a mixture of economic, political, and religious motives. While many of the senior managers felt that they could eventually capture control of the movement, they subsequently found that it was Khomeini's forces who manipulated them. Many government workers are frightened by the ongoing executions of counterrevolutionaries; few appear to be actively doing their jobs, and even fewer are risking initiatives. Their growing disillusionment with the new Islamic Republic is not likely to become focused unless a strong secular leader appears on the scene.

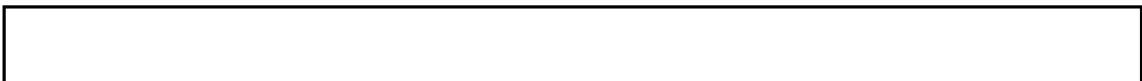
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**Characteristics of the Iranian Bureaucracy**

The Persians have one of the world's oldest bureaucratic traditions, and the civil servant class (*karmandan*) has constituted the machinery of day-to-day government. The bureaucrats in turn have been directed and controlled by the ruling class. Because of this control, the *karmandan* have been more or less the servants of the upper class. The bureaucracy has provided a unique opportunity for the most ambitious and best educated of the middle and lower class to move into the elite decisionmaking group if they demonstrate competence and/or allegiance to the right master.

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Government service has traditionally been prized as a secure job, and near the end of the Shah's reign about 350,000 persons were employed in ministries and



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government agencies under Civil Service Regulations.\* While traditionally part of the middle class, government employees have felt (and often have been) underpaid compared with workers in the private sector. Official pay has been kept low under the assumption that it would be supplemented in the form of *bakhshish* (payoffs). [redacted]

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Even the lowest ranking civil servant has considered his position a personal fiefdom, and persons wishing service from the bureaucracy have routinely paid *bakhshish* to assure that the civil servant's special knowledge and competence would be brought to bear on his case. At the higher levels of the bureaucracy, this frequently has resulted in the skimming off of large sums of government funds earmarked for development purposes. It has also bred discontent among the many conscientious workers and those unable to take advantage of the system, who have found their official earnings and benefits constantly eroded by inflation. [redacted]

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While the old bureaucracy in Iran tended to be conservative and highly religious, the Shah's extravagant economic goals created a corps of highly educated and skilled technocrats much more liberal minded and Western oriented. The new bureaucrat has received modern training instead of the traditional *maktab-madrasah* education (education under the auspices of the religious community). Many have received their training abroad; others were taught in the secular schools created by the Shah. By the mid-1970s, the Ministry of Education had grown into the largest government body, employing about half the bureaucracy, and the number of civil servants with more than a high school education had doubled since the mid-1960s, to 20 percent. [redacted]

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The religious community viewed this secularization of the educational system—and thus the bureaucracy—as a threat to its influence and to basic Islamic principles. One of the more offensive changes was the large-scale promotion of women's rights under the Shah. With the opening of education and occupational opportunities, the number of women working for the government in the mid-1970s reached about 90,000, triple the number employed a decade earlier. In comparison, the number of male workers over the same period remained constant. Employment of women by the government, however, was limited primarily to urban areas, as the government was unsuccessful in pushing its campaign for women's rights into the conservative rural areas. [redacted]

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### Molding the Bureaucracy

The Shah followed the traditional principle of divide and rule. Agencies with parallel functions were created to act as watch dogs over each other. Power was distributed to a series of individuals or agencies with overlapping responsibilities so that each became fragmented and weak. Loyalty could be found in a handful of trusted officials at the top; for most, the system generated mistrust and mutual antagonism. The resulting tension had many undesirable effects. Government officials

[redacted]

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25X1 came to expect the Shah to provide all policy guidance and avoided taking initiative. [redacted]

25X1 Concentration of authority and responsibility at the top meant that action occurred within the bureaucracy only when royal attention was focused on a particular subject. The high degree of insecurity caused many to avoid top positions in government. The result was a very thin layer of overburdened decisionmakers. High officials often were forced to make decisions on weighty matters without adequate study because they could not find enough people to whom they could delegate authority. [redacted]

### The Bureaucrats and the Revolution

25X1 The Shah was not completely successful in reforming and molding the bureaucracy to meet his needs. This was partly because friends of the regime generally were immune to reform measures. Also, traditions die hard; while the positions and loyalties of old bureaucrats were slowly weakened and undercut, they were not destroyed. Foreign educated officials, trying to impose order in unwieldy domains, found these deepest attitudes a major barrier to moving on with the job. They often lost sight of their goals and became indistinguishable, except in dress, from their predecessors of a century ago. [redacted]

25X1 The shakiness of the Shah's grip on government employees manifested itself last October when civil servants joined private sector workers in demonstrations and strikes organized by the Shah's religious and political opposition. While their demands initially were focused on salaries and benefits, they soon escalated to political opposition to the Shah. The work stoppages practically eliminated economic policy-making and shut down administrative functions. Not surprisingly, however, enough workers were found to get out the payrolls. When the fall of the Shah became imminent, senior officials struggled to maintain tranquility in their ministries and threw their weight behind Khomeini. This did not reflect so much their support of Khomeini's ideas but their belief that they could eventually capture control of the revolutionary movement because only they possessed the skills necessary to run a modern state. [redacted]

25X1 Senior government officials, however, were insufficiently organized—mainly because of the Shah's divide and conquer policies—to present a unified front and thus offered no alternative to an Islamic Republic. They subsequently found Khomeini's movement used them rather than vice versa. With establishment of the Islamic Republic many key officials were forced to flee the country, were fired, or were summarily executed because of their close association with the Shah. [redacted]

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### Aftermath of the Revolution

While rank-and-file bureaucrats supported the revolution, they have not been immediate beneficiaries. In one of its first acts, the new government reduced the

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special allowances and compensation of government bureaucrats, reducing the real income of most higher government officials by as much as 50 percent. Women in the civil service ranks were singled out for harassment. While they were allowed to return to work, the position of women in general is tenuous, as exemplified by (a) the requirement for a more conservative mode of dress; (b) exclusion from certain training, for example, in the legal field; and (c) the reduction of marriage age of females to 12 years, as part of the general return to Islamic precepts. [redacted]

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Mundane activities such as directing traffic and stamping passports somehow are being taken care of. At the same time, the *karmandan* have often ignored the Ayatollah's call to engage in productive activities, opting instead for long tea drinking sessions and political discussions. Economic planning remains in disarray and administrative offices are barely functioning. We have received numerous reports of government projects at a standstill and of delays in government welfare payments. Most rank-and-file workers still show up at work and collect their paychecks; without supervision, direction, and confidence that the revolution has ended, they do little. A purge of antirevolutionary bureaucrats has been threatened in an attempt to get government activity moving. [redacted]

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### Outlook

A return to normalcy in the bureaucracy is not likely until Khomeini establishes some form of hierarchical control. Many *karmandans* still perceive the Barzagan government as a temporary institution and choose to avoid decisions rather than do something that could be construed as counterrevolutionary. Government employees will continue to lie low until they receive explicit directions for the formulation and implementation of new policies for the post-Shah era. Installation of a permanent government, after approval of the new theocratic constitution, presumably would prompt the bureaucracy to resume a more normal level of activity. [redacted]

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While the *karmandan* continue to respect Khomeini as a revolutionary leader, he has not established control over the daily details of government, and the civil servants are becoming increasingly disillusioned with his policies and the continued chaos in Iran. Moreover, the concept of a strict Islamic republic does not fit with the modern outlook of most government workers, especially the more highly educated. Khomeini's old-fashioned view of women and the mullahs' suppression of democratic freedoms no doubt are alienating many. All this said, dissension within the bureaucracy is not likely to pose a threat to the revolutionary government unless a strong secular leader appears. [redacted]

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[redacted]

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5 October 1979

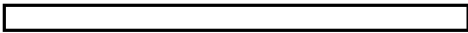
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Articles

IRAN: THE CLERGY, CREATING A THEOCRACY



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The Shia clergy of Iran, Shah Mohammad Reza Pahlavi's most persistent opponents, have a long tradition of opposition to secular rule. In the last 150 years this opposition has recurringly taken the theme of resistance to both domestic absolutism and foreign domination. The clergy are regaining the economic, judicial, and political power they have been losing for more than a century—especially under the Pahlavi dynasty—and the founding of an Islamic theocracy in Iran appears probable. However, the more secular and modern elements in the society and the ethnic minorities—all participants in the toppling of the Shah—are becoming increasingly frustrated by the rigidity of the clergy.



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Shia Tradition and Doctrine

Clergy of the Shia sect of Islam—the official religion to which about 95 percent of Iran's 36 million people belong—have been long-time opponents of secular governments and especially of the Pahlavi dynasty. According to Shia doctrine, secular and spiritual leadership should be combined in a single person as manifested by the 12 Imams, descendants of Muhammad. The separation of the two powers, which occurred about 150 years before the disappearance of the 12th Imam in 873 A.D., is viewed by the Shiites as both temporary and illegal.



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While Shia doctrine recognized other spiritual leaders as "agents" of the Hidden Imam, the direct appointment of such agents ceased in 940 A.D. when the last agent refused to name a successor. The concept of the agent of the Imam has been revived, however, and some Iranians have referred to Khomeini in this vein. Khomeini, although distancing himself from claims of being an agent or a true Imam, accepts his role as the preeminent figure among the *mujtahid*—popularly recognized religious leaders worthy of imitation. The Shia concept of *mujtahid* also encompasses the doctrine of *ijtihad*—the discovery and authoritative enunciation of fresh religious truths based on the Shariah.\*\*



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\*\* The Shariah is the sum of the laws derived from the Koran, the Traditions, the consensus of the scholars, human reason, and *ijtihad*.



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### Clerical Opposition to Westernism and Tyranny

Clerical opposition to secular rule took on the twin themes of resistance to foreign domination and domestic absolutism during the late 18th and early 19th centuries when European nations became more interested in the country, which was then ruled by the Qajar dynasty. One of the earlier instances of clerical political action took place in 1826 when the *ulama* (clergy), fearing Russian influence and expansionism, forced the Qajar shah to renew war against Russia by calling a *jihad* (holy war). Unfortunately for Persia, the war was lost and Russia gained more Persian territory as well as extraterritorial rights exempting Russian citizens from trials in Persian courts. [ ]

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Other foreign countries demanded similar treatment for their citizens, but such concessions were abolished by Reza Shah—the present Shah's father. The Iranian-American agreement of 1964, which gave the US military mission a special status based on the stipulations of the Geneva Convention, was represented by the Shah's opponents as a reestablishment of the concessions. A \$200 million loan from the United States for the purchase of military equipment was seen as a payoff to the Shah for granting the "capitulations." This was seized on by Ayatollah Khomeini to renew his attacks on the Shah. [ ]

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The clergy also played a major role in the Constitutional Revolution of 1905-06. The constitution then promulgated gave a body of five theologians the right to set aside any law that in their opinion contravened the holy principles of Islam. Since this article had been ignored by subsequent secular rulers, the full implementation of the 1906 constitution became a rallying call for some clergy in the early stages of the 1978-79 revolution [ ]

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### Clerical Opposition to the Pahlavis

The monarchy alienated the clergy by emphasizing Iran's dynastic tradition—which emphasized pre-Islamic Persian glories—rather than its Islamic heritage and by undertaking a series of measures aimed at undermining clerical power. The power of the clergy was derived from many sources. Since Islamic law—as based on the Sharia—was the only law available, the clergy maintained a judicial monopoly. Power was also derived from clerical participation in the government bureaucracy, relationships through marriage, and control of funds from *waqf* (religious) endowments, which included land, villages, and sources of irrigation water. At the same time, preaching and good works gave the clergy influence over the population in general. [ ]

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In exercising power, the clergy gathered wealth, prestige, and personal security. Under Islam, clergymen were under no special restrictions with regard to acquisition of property, and in this pursuit they were sometimes not above abusing their extensive control of courts and legal procedures. Their financial advancement in turn strengthened their political influence. [ ]

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Reza Shah undertook measures aimed at undermining the clergy's power which often resulted in the substantial reduction of *ulama* income. The severest blow came in the early 1930s when religious law was replaced by Western codes and Western style courts were established with nonreligious judges. While religious authority on matters of personal status, such as marriage and divorce, continued, it was gradually restricted over the years. Reza Shah's government also refused to exempt theological students from military service and began the removal of general education from clerical control. Clerical participation in the bureaucracy was curtailed, and the collection and use of *waaf* funds was restricted. [ ]

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During this time, Western dress was forced on the population and Western forms of entertainment, such as the cinema, were introduced. The antagonism of the *ulama* was aroused not only by these measures but also by the progressively open contempt shown them by the Shah. [ ]

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Pressure on the clergy eased after the Soviet and British invasion of Iran in 1941, when Reza Shah was forced to abdicate. Several of the Shah's antireligious measures lapsed, and the clergy was able to regain some of its old control over endowments and education. This resurgence of clerical influence lasted from 1941 until the royalist coup of 1953. [ ]

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Shah Mohammad Reza Pahlavi renewed his father's efforts to Westernize Iran and undermine the clerical opposition as soon as he had consolidated his power. Education was almost totally secularized. The Shah's land reform program of the early 1960s included the redistribution of a considerable portion of *waaf* lands. Earnings from the endowments were replaced by an annual government grant. Women's rights legislation also removed more of the *ulama's* judicial influence over marital and family affairs. [ ]

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With the rapid change and social upheaval ushered in by modernization, especially after the 1973 oil boom, many Iranians retreated in dismay to traditional religious values. Economic problems, lack of political participation, and corruption all came to be blamed on the government's modernization and Westernization policy; thus it is not surprising that many Iranians looked to Islam as the remedy. During most of his reign, the Shah's autocratic style left little scope for political criticism, and the religious establishment became the spokesman for grievances. Later, when the Shah attempted to create a more liberal atmosphere, the clergy were quick to exploit the new freedom to incite the poorly educated and unemployed urban masses. [ ]

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### The *Ulama* Today

The revolution in Iran, given form and leadership by Ayatolla Khomeini, has provided the Shia clergy an unparalleled opportunity to take over the reigns of government. Their goal is the establishment of an Islamic republic that perpetuates their role as preeminent leaders of the nation. The new constitution being written

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gives extensive powers to a *marja-i-taqlid*—a recognized religious leader of highest prominence—to oversee the government. If no single *marja* can be settled upon, a body of five theologians will sit in his place. [REDACTED]

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Currently, the revolution has permitted the clergy to assume leadership roles at all levels of government, from local councils to the powerful Revolutionary Council at the top of the government pyramid. Khomeini himself is the final authority and arbitrator of all government decisions. While there are two or three Ayatollas who could be considered to be close to the same stature as Khomeini, they do not command nearly the widespread following. Ayatolla Shariat-Madari, who is probably second in popularity, especially among the Azerbaijanis and the more Westernized middle class, is the only moderate among the well-known *ulama*. He has preferred, so far, to avoid a direct political contest with Khomeini and may be open to criticism that he was supportive of the Shah in the mid-1960s. The other well-known clergy tend to be as orthodox and conservative as Khomeini. [REDACTED]

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The specific policies for attaining a totally Islamic society are often vague and left open to interpretation. In the economic sphere, for instance, an Islamic economy appears to be nothing more than a free economy in which "just" participants follow the teachings of the Koran and Sharia. It is more of a collection of laws and attitudes than an economic system. The prohibition against interest and the system of inheritance laws are fairly well established. Islamic banks, as such, are akin to Western venture capital firms—taking deposits, investing, sharing in profits and losses, and passing on the profits and losses to their depositors. The practical aspects of working within the international monetary system have not been completely worked out, however, and in other Islamic countries rules and definitions have been bent to accommodate the prohibitions against interest. [REDACTED]

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Another established principle is the duty of sharing wealth with the poor. The *zakahat*, as the almsgiving duty is called, can be interpreted as a compulsory tax. It is largely a matter of conscience in most Moslem countries today. [REDACTED]

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Private property is protected under Islam, but, since all property ultimately belongs to God, its earthly owners have only a stewardship role. Thus, the property of the industrialists who fled Iran could be nationalized because these people demonstrated their inability to adequately administer the property. Property can also be seized for nonuse or for the public good. [REDACTED]

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As to general economic policies, Iranian leaders stress the importance of agriculture and view favorably enterprises based upon individual initiative such as farming, small-scale merchandising, services, and light manufacturing. Large-scale enterprises in every field will likely fall under the province of the state. Individuals almost certainly will not be allowed to accumulate holdings as vast as some acquired under the Shah. [REDACTED]

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### Outlook

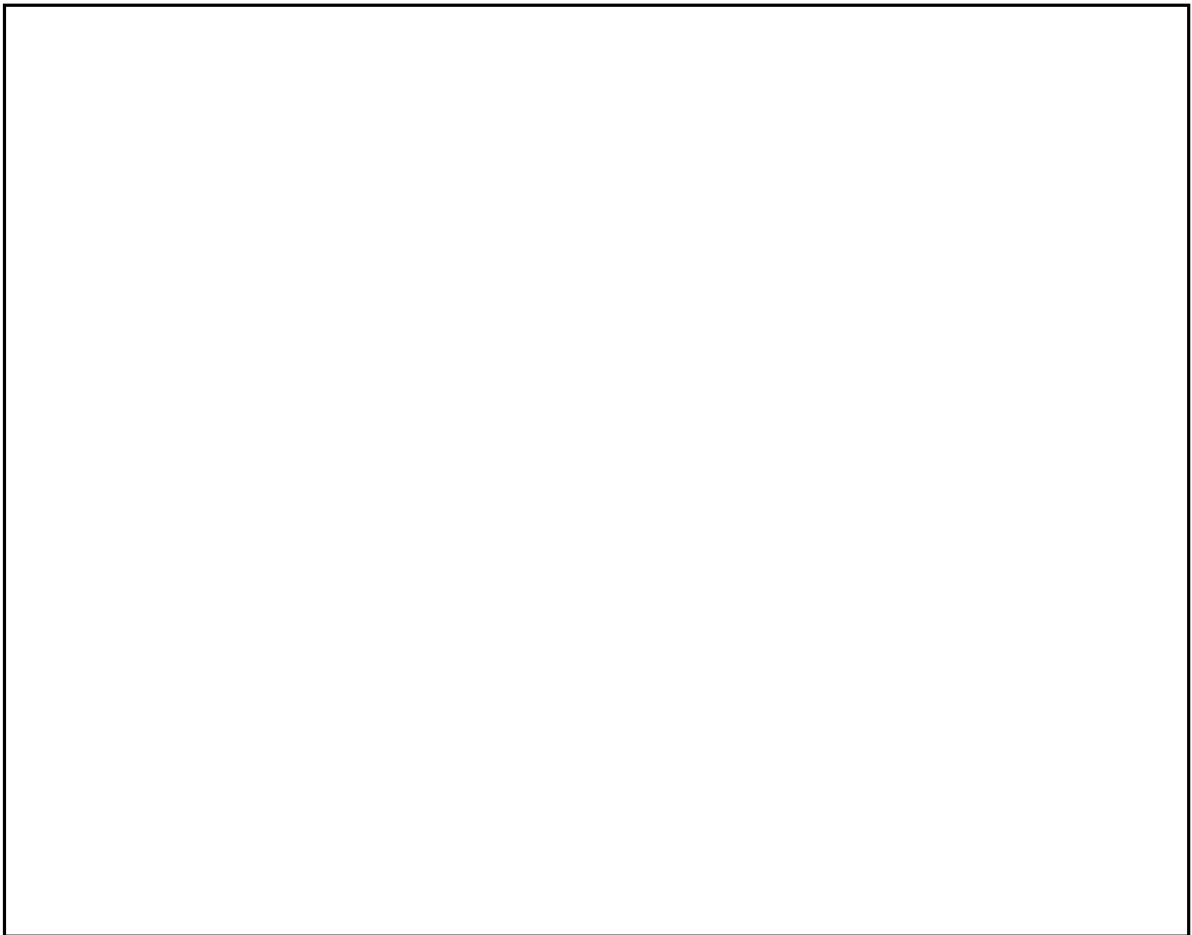
The clergy are now closer than at any other time in recent history to attaining the combination of secular and religious leadership of the early Imams. Even though his personal popularity and that of his revolution have fallen in recent months, Khomeini remains the rallying point for most Iranians and the founding of a theocratic state appears almost certain. Only the death of Khomeini or the outbreak of widescale ethnic revolt could sidetrack its development.

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While popular discontent may grow if economic conditions worsen, Khomeini has managed to insulate himself somewhat from the implementation of policy. In addition, while the ideal of an Islamic state may prove impractical in the economic sphere, the interpretation of Islamic doctrine is in theory flexible enough to allow adaptation of new policies. So far, however, the Iranian leadership has given no indication that it will be sufficiently flexible to stem the growing alienation among the middle class, the bureaucrats, and the secular forces generally who are needed to run an already modernized Iran.

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