

## Timur Kuran

Why are some societies relatively rich and others relatively poor? This is perhaps the most fundamental question in all of economics. Although aspects of the issue remain unresolved, there is a consensus among economists that well-defined property rights, low and stable inflation, and reasonable regulatory and taxation regimes are conducive to growth. In short, markets do produce the goods.

But what produces the institutions that are necessary for the development of a well-functioning market system? That is the question that economist Timur Kuran of Duke University has been asking recently. In particular, his work has led him to wonder why the Middle East, probably the most prosperous region of the world in the Middle Ages, failed to grow in the way that Western Europe has during the last several centuries. The product of that research will appear in 2010 with the publication of his book *Islam and Economic Underdevelopment: Legal Roots of Organizational Stagnation in the Middle East*.

Kuran has been interested in the economics of religion for many years, but much of his early work was on a very different topic: What are the incentives that lead people often to express a certain preference privately but another publicly — and what are the public policy implications of such “preference falsification”?

Before coming to Duke in 2007, Kuran taught at the University of Southern California for 25 years. He also has held visiting positions at the University of Chicago and Stanford University.

Aaron Steelman interviewed Kuran in his office at Duke on Sept. 16, 2009.



**RF:** Could you briefly discuss what you mean by the phrase “preference falsification”?

**Kuran:** Preference falsification is the act of wanting one thing and saying that you want another, or having one ranking among options but conveying another publicly. It happens frequently in every society. Just to be polite, for instance, we may express admiration for something we don't really admire. Preference falsification also occurs in response to perceived social pressures. We perceive that if we don't express admiration for something or, alternatively, we don't condemn something, we ourselves will be condemned or else miss out on a particular reward. The motivating perception need not correspond to reality. Finding ourselves in a group of people looking at a painting, we may sense that the group considers it beautiful, perhaps because the painting is famous, when actually everyone thinks it is pretty mediocre. So we wind up praising the painting because this appears to be a safe course of action. In such contexts preference falsification does not do much harm. If we always said what popped into our minds, there would be more frictions, and more hurt. White lies serve a useful purpose.

However, preference falsification is common also in situations where it does measurable harm. When a community is trying to decide how to govern itself or which economic policies to pursue, untruthfulness distorts the political system. It sends signals that make others reluctant to express themselves truthfully.

**RF: Do you believe that preference falsification is, on net, harmful?**

**Kuran:** As I said, I think that the impact is negative when it comes to politics. On personal matters, the effects are relatively benign. Still, I can think of examples where it is harmful in social life. As individuals, sometimes we need to hear the truth. A person can benefit from being urged to get his life in order. By expressing ourselves candidly, we might avoid big problems down the road.

**RF: Perhaps there are instances, though, where preference falsification is beneficial for public policy. For example, if you live in a relatively market-oriented system that is improving people's standards of living, you might be better off having people who harbor highly interventionist sympathies falsify their preferences.**

**Kuran:** Preference falsification on the part of mad and crazy people is a good thing, of course. Your example does not go to an extreme; it involves ambiguity. But, yes, having a system that induces people with bad ideas to refrain from expressing them is probably beneficial on the whole. There are also drawbacks, though.

Most people living in a liberal, market-oriented regime, such as the one you describe, are going to be content. The regime will have few opponents. It would be better to allow the few crackpots to express themselves than to make life so miserable for them that they are driven underground, and into militant movements. On balance, liberal regimes do not have to worry about crazy ideas, from the left or the right. Today, at New York's Grand Central Station there are people who sell Trotskyite newspapers, as they have for 50 years. I have always wondered how these newspaper sellers make a living. Who buys their newspapers? Yet, I am glad that they sell the papers in public, and that they are not being forced underground.

**RF: Can preference falsification be modeled?**

**Kuran:** Yes, it can be modeled because the individual deciding whether to falsify his preferences or express them truthfully faces trade-offs. He will earn benefits or incur punishments depending on the choice he makes. In falsifying their preferences, individuals do what is in their own best interest, given the social pressures that they perceive. So they are maximizing something, which is the essence of economic modeling. Whether the social consequences are optimal is something else; often they are not. This is not the only context where individually optimal choices harm society. A wide range of individually rational choices generate negative externalities. The point is that preference falsification does lend itself to modeling.

If the phenomenon poses any analytic challenge, it concerns not formalization but predictability. Most economists build models to predict the future. But in models involving

preference falsification, information under the surface, in other words private information, makes it difficult to predict.

Consider a society that is on the verge of exploding, on the verge of a huge shift in public opinion amounting to a revolution, such as the East European Revolution of the late 1980s or the Iranian Revolution of 1978-79. We can model this society without having an inkling of what is about to unfold. After the revolution has taken place, the same model will make it seem too obvious to miss. Preference falsification was present prior to the revolution (there was often a large penalty associated with being seen as a dissident) and, in the opposite form, after the revolution (no one wanted to admit that they liked, or benefited from, the previous regime). The former manifestation of preference falsification limited predictability. The latter manifestation makes it hard, after the fact, to understand why prediction is subject to error.

**RF: Still, it seems perplexing that most social scientists had very little idea what was going on in the Soviet Bloc in, say, 1988.**

**Kuran:** I agree. In retrospect it does indeed seem odd that most analysts of the Soviet Bloc totally missed what was going on. At the time the Soviet Bloc seemed essentially static in a political sense. Now we can identify what happened. Here is the apparent sequence of events. In 1985 Gorbachev, the leader of the Soviet Bloc, acknowledged publicly that the regime was facing serious problems and that the Soviet system needed rethinking. The ensuing reforms, known as perestroika, legitimized the expression of new ideas, including ideas that had been bubbling under the surface but expressed only in clandestine publications. The second major initiative, glasnost or openness, formally opened up the system to public criticism.

In the 1985-89 period the secret police organizations of the Soviet Bloc kept a pretty close eye on public opinion. The records show that confidence in the system had fallen sharply. Gorbachev and the other Soviet leaders thought they could control the apparent decline in confidence, but events overtook them. The general lesson, I think, is that in an inefficient, authoritarian regime legitimizing dissent may lead to its demise. There are obvious implications for the future of Saudi Arabia, Iran, and other oppressive regimes that generate considerable discontent.

**RF: Some economists have argued that in, say, the case of China, economic liberalization will ultimately lead to political liberalization. What are your thoughts?**

**Kuran:** I certainly agree. Chinese economic liberalization is producing a prosperous middle class. At present this middle class is putting up with social controls because it is getting richer at a very rapid pace. Sooner or later it will want to share political power.

**RF: The secret ballot should make it relatively easy for people to vote their private preferences. If that is the case, do the politicians we elect (and the policies they enact) accurately reflect what we want as a polity? Or does the fact that we sometimes censor our private beliefs lead to a more constrained debate, where views outside the perceived mainstream are not widely voiced and, hence, candidates who represent those views are not afforded a place alongside more conventional candidates?**

**Kuran:** In a modern democracy, we elect candidates by a secret ballot. This is partly because we recognize that preference falsification distorts the choices we make collectively. The secret ballot allows voters to express choices without risking retaliation. Yet, the voters who go to the polls do not face a full menu of options.

Typically, their options have been truncated by a political struggle that ran its course well before the polls opened. Candidates have been selected in an environment in which money matters enormously, and those able to raise sufficient money are the candidates who have said nothing offensive to key constituencies. The upshot is that on most issues candidates take positions fairly close to the middle of the ideological spectrum. This is not to deny that political parties can differ on particular issues. However, the process that I have described does weed out individuals with ideas that are perhaps premature or perceived as risky. Such individuals never come before us as serious candidates. Consequently, on almost any issue one can identify positions that ought to receive political consideration but do not.

Let me illustrate this claim through an example. As everyone knows, a large share of our health care resources goes to terminally ill people. Meanwhile, millions of young and middle-aged people lack health insurance. Obviously, many of the people in the latter group would benefit from insurance. Hence, society should be discussing the merits of rationing health care subsidies to the very old in the interest of providing better health care to the young and middle-aged. Yet, few individual leaders are willing to do so openly and honestly. It is extremely risky even to mention the existence of a trade-off.

Judge Richard Posner might be mentioned as an exception. I do not know whether he has written specifically about the trade-off in question. However, on a number of other issues he has taken quite radical positions that other circuit court judges are not willing to take. Perhaps the reason is that he is unlikely to be nominated to the Supreme

## Timur Kuran

### ► Present Position

Professor of Economics and Political Science, and Gorter Family Professor of Islamic Studies, Duke University

### ► Previous Faculty Appointment

University of Southern California (1982-2007)

### ► Education

A.B. (1977), Princeton University; Ph.D. (1982), Stanford University

### ► Selected Publications

*Islam and Economic Underdevelopment: Legal Roots of Organizational Stagnation in the Middle East* (forthcoming); *Islam and Mammon: The Economic Predicaments of Islamism* (2004); *Private Truths, Public Lies: The Social Consequences of Preference Falsification* (1995); author or co-author of numerous papers in such journals as the *American Economic Review*, *Quarterly Journal of Economics*, *Journal of Economic History*, and *American Journal of Sociology*

Court. If so, he has little to lose by stating his preferences truthfully and much to gain from solidifying his reputation within the legal profession as someone prepared to voice his opinions fervently. A younger circuit court judge, or a law professor eyeing a Supreme Court nomination, has everything to lose from taking positions perceived as radical.

**RF: How did you become interested in the economics of religion?**

**Kuran:** I grew up in Turkey, which is a predominantly Muslim country with a secular constitution. At the time, educated Turks were overwhelmingly supportive of secularism. They agreed that the abrogation of Islamic law was justified and approved of making westernization an official policy. Yet no one talked about the disad-

vantages of the discarded Islamic institutions. Implicit in all discussions was the idea that these institutions were harmful; they resulted in backwardness, they delayed Turkey's industrialization, they kept the literacy rate low, and so on. I never understood the mechanisms involved because the claims were not publicly debated.

I came to the United States for college and got interested in economics. At the time, economists showed no interest in religion. Religion was one thing and economics another; neither had anything to contribute to the other. As a Ph.D. student in economics, I did not do any work that touched on religion. However, I thought that one day I would explore this topic.

When I completed my dissertation in March 1982, I already had a job lined up for September. I decided to give myself one month to read works I would probably not read as an assistant professor trying to publish in conventional subfields of the discipline. This was my reward for graduating early. Wandering through Stanford's Green Library in search of interesting books, I came across such titles as *Islam and Economics* and *Islam and Development*. These were books written by "Islamic economists." They claimed that the world's economic problems could be solved by returning to Islam. The arguments appeared interesting yet superficial. I shared my criticisms with some friends, who encouraged me to turn them into an article.

Before my move to the University of Southern California that fall, I had drafted a critique of this literature. The *Journal of Economic Behavior & Organization* published the piece in 1983, following two rounds of revisions. Soon after publication I started getting calls. Islamist movements were

making waves and people wanted to know the implications for economics. On account of one journal article, I wound up being invited to conferences and seminars as an expert. I denied being an expert; all I had done was to read some books and write a critique. But apparently I belonged to a tiny group of formally trained economists who had studied Islamic economics with an open mind and objectively. Before I knew it, I was writing other articles on the subject. My research began to encompass Islamic economic reforms that were taking place in countries like Pakistan and Malaysia. The book *Islam and Mammon* collects some of my major findings and arguments.

**RF: Is there such a thing as “Islamic economics,” or is it, as some have claimed, an invented tradition?**

**Kuran:** Although the concept of “Islamic economics” dates from the 1940s, it is promoted as a very old doctrine that gave rise to many practical successes. In that sense it is indeed an invented tradition. Today, Islamic economics constitutes a vibrant school of thought. It is the subject of international conferences at which various issues are debated. In terms of analytic sophistication it does not rise to the level of neoclassical economics or even Marxist economics. The rather repetitive literature that falls under the rubric of Islamic economics promotes certain principles, and it revolves around certain pet issues. Over the years, I should add, its sophistication has grown. There now exist quarterly journals of Islamic economics that have the feel of the *American Economic Review*, at least in the sense that they are filled with models and statistical tests.

If you are asking whether Islam offers a distinct form of economics, my answer is no. The economic principles spelled out in the Koran closely resemble ones found in the Bible. The Koran encourages transparency in economic relations. It promotes honesty. It requires people to be charitable toward others. Such prescriptions are not unique to Islam, or, for that matter, to religion.

**RF: What, then, are the principles of “Islamic economics,” according to its proponents?**

**Kuran:** The Islamists have latched onto three specific principles to distinguish their version of economics from neoclassical economics, Keynesian economics, and Marxist economics. The first is the ban on interest. If implemented, such a ban would have huge consequences. The second principle involves redistribution from rich to poor, according to an Islamic template. The Koran prescribes a form of redistribution called *zakat*. Islamic economists want *zakat* to be the foundation of redistribution. The third principle is that economic relations should be built on the norms I mentioned before: honesty, transparency, and justice. As I have already said, these can be extracted from the Bible as easily as from the Koran.

These three principles are compatible with a wide

array of economic systems. This is evident from the diversity of the economic agendas characterized as Islamic. Some Islamic economists have inferred that they lead to Islamic socialism. Others have used the same principles to rationalize free markets.

**RF: How commonly do we observe those three principles actually being practiced in Islamic countries?**

**Kuran:** Certain societies have made interest illegal. But there is no example of either a Muslim or non-Muslim society, past or present, that has done away with interest in practice. There is always a demand to borrow money at interest. That demand induces people to find ways to circumvent the ban.

As a redistribution system that emerged in seventh-century Arabia, *zakat* reflects seventh-century Arabian conditions. It requires wealth holders to transfer shares of their precious metals, camels, and crops to the poor. The requirements are highly specific; for that reason they lost relevance as the early Arab empires conquered Syria, Iraq, and Egypt, all relatively urbanized societies with a different resource base than largely nomadic Arabia. Islamic economists have tried to restore the significance of *zakat*. Some have argued that rates set centuries ago should be implemented today, and that the taxable commodities should remain the same.

Where these traditionalists have had their way, there have been perverse consequences. In Malaysia, for instance, *zakat* has been collected from peasants but not from urban workers or civil servants. As a result, inequality has actually increased. The majority of Islamic economists are now trying to reinterpret *zakat* to suit modern conditions. Some have called for a radical reinterpretation: Wealth should be shared not only within Muslim countries but also among them. If the radicals get their way — unlikely anytime soon — the richer Muslim countries would redistribute wealth to the poorer ones.

**RF: The Islamic world was relatively prosperous during the Middle Ages but then suffered through a long period of near stagnation. What accounts for that?**

**Kuran:** The Middle East and Europe started out with similar commercial institutions around the year 1000. The institutions used to pool labor and capital were not different in any essential respect. But the European variants adapted much more quickly to changing circumstances than those of the Middle East. Evidently there were greater incentives to innovate in Europe than in the Middle East. Why? One important difference involved inheritance practices. The Koran prescribes a highly egalitarian inheritance system. All children, including daughters, get a share of the estate. There was a downside to this egalitarianism. The estates of successful businessmen tended to get fragmented, making it difficult for successful businesses to



carry over from one generation to the next.

The problem was exacerbated by another Islamic institution: polygamy. The wealthiest members of a Muslim community tended to have multiple wives and, hence, many more children than the norm. Precisely because they were wealthy, their children tended to survive in greater numbers. So when a wealthy businessman died, there tended to be many inheritors. In principle, the inheritors could have banded together to keep the family business going. In practice, such cooperation was uncommon. We know of great entrepreneurs in premodern Egypt and Turkey who built a massive business network, amassed a great deal of capital, and developed a stellar reputation. Their business empires did not survive them.

In Europe, there existed a wide variety of inheritance systems. The one that contributed most to economic growth and modernization, especially in Great Britain, Holland, Belgium, Switzerland, and parts of France, was primogeniture. Under primogeniture the entire estate goes to the eldest son. It is not by chance that these countries developed more rapidly than other parts of the world. In contrast to the Islamic inheritance system this form of inheritance enables business continuity across generations. Ironically, the Islamic system is relatively more egalitarian, and it conforms more closely to modern sensibilities. Nevertheless, it had the effect of retarding economic modernization and, ultimately, industrialization.

Because of the prevailing inheritance system in the Middle East, people tended to keep their partnerships small and ephemeral. In Western Europe, where the fragmentation of estates could be prevented, people were willing to form large and durable partnerships. Larger and longer-lasting partnerships created problems of coordination, communication, and risk-sharing. Efforts to alleviate these problems led to organizational advances. By the 16th and 17th centuries, business corporations were being formed in Western Europe. Nothing resembling this dynamic unfolded in the Middle East.

As these corporations became larger, their shareholders started looking for a way to withdraw capital without endangering the entire enterprise. The emergence of the early stock markets in Amsterdam and London provided this convenience. Large publicly traded companies stood to benefit from standardized accounting; it would facilitate the valuation of their shares. In the Middle East, these developments were absent because they were not needed.

What made Great Britain an industrial power was not only the invention of technologies such as the steam engine. In the 19th century one could easily ship a steam engine to Cairo. However, Cairo lacked the institutions of modern capitalism, so it could not have used a steam engine efficiently. Institutions are critical to economic performance, and in the course of the second millennium they became increasingly sophisticated in Western Europe but essentially stagnated in the Middle East. This is the basic argument of my book to be published in 2010 by Princeton University

Press, tentatively titled *Islam and Economic Underdevelopment: Legal Roots of Organizational Stagnation in the Middle East*.

In researching this book, I looked at about 10,000 commercial cases from the 17th century, all recorded in the court archives of Istanbul. Why Istanbul and why the 17th century? Until modern times Istanbul was the most advanced commercial center of the Eastern Mediterranean, and it was during the 17th century that organizational forms in Western Europe registered the advances essential to modern economic life. My goal was to see whether parallels existed in Istanbul.

I plan to continue mining the resulting data set in forthcoming papers. Because the original documents may prove useful to other researchers working on related questions, I will also be publishing the data set itself. A 10-volume collection of 17th-century court cases will appear in 2010. It will contain summaries in English and modern Turkish, along with transliterations of the Ottoman-Turkish transcripts.

**RF: I have noticed that you typically use the word “underdeveloped” rather than “developing,” which seems to be the preferred term among economists in this field. Is your choice of words meant to represent an important distinction?**

**Kuran:** “Developing” is a euphemism that emerged in the 1970s to describe what used to be called “backwardness” or “underdevelopment.” It was considered a more gentle, and thus more acceptable, alternative to the term I prefer to use, “underdeveloped.” Yet some of the countries lumped together under the rubric “developing” have not been developing in any meaningful sense; they have become poorer, not richer. To call them “developing” does not do their people any good; on the contrary, it does harm by obscuring the need for fundamental reforms. Terms ought to illuminate phenomena, not obfuscate them.

“Underdeveloped” is a more satisfactory term for my purposes because it signals my concern with *relative* economic performance. During the second millennium, the Middle East continued to grow, though more slowly than Western Europe. My central question is whether Islam contributed to turning the Middle East into a region that is poorer than Europe.

**RF: What is your next project?**

**Kuran:** I have now turned my attention to political underdevelopment in the Middle East. Where the book about to be published focuses on commerce and finance, the next one will focus on democratization, political liberties, and the evolution of governance patterns. The Islamic world’s political underdevelopment has to do with failures to develop political checks and balances; and those failures are related to the very institutions that led to economic underdevelopment. Economic and political liberalization are mutually supportive processes. **RF**