

Review literature: The effect of prices and income on consumer choice and consumption in Islam

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Abstract

The change in the quantity demanded caused by a change in price occurs through two effects that are complementary to each other, which are called the substitution effect *and* the income effect, these effects also affect theory. behavior consumer in islam and based on law Islam on basically different with theory conventional. Difference this concerns score core in lower theory, motive and destination consumption, technique choice and allocation budget consumption. The method used in this study is literature review, with various sources of journal literature in the last five years. Based on the results of the reviewed articles that can explain how changes in relative prices affect consumer choices. And when choosing a product, consumers will consider its price as well as the price of alternative products from the cross-price elasticity of demand. And in Islam, the level of consumption of these goods is usually termed goods that are daruriyat, tahsiniyat, and hajiyat.

Keywords: *income, substitution effect, consumer choice*

- No more than five keywords (10 fonts)

1. Introduction

When price something goods down, effect on choice consumer could shared Becomes two type, effect income and compensation. Effect income reflected in shift from curve indifference which more low to which more tall, whereas effect substitution reflected in shift throughout curve indifference which given to something point with tilt which different. Effect substitution is change consumption food which related with change price food, with level utility permanent no changed. Effect substitution covers change consumption food consequence change which make food relatively more inexpensive than clothes.

Effect income is change consumption food on price which relatively permanent which caused by enhancement power buy. If income no influence change, increase price will Keep going lower income real. The importance of this research is to find out more clearly about the law Request state that when price go on, all Thing other considered same, amount goods which requested by consumer down and on the contrary. Change quantity which requested consequence change price occur through two effect complementary which called effect substitution and effect income. Effect substitution appear from change price relatively goods substitution from change price

goods which requested, whereas effect income appear from change income real (power buy) consumer.

Problem economy in economy micro Islam there is two that is conventional and Islam, here writer try make analysis Among income and effect compensation from change price and behavior consumer in economy Islam with approach comparative, because both of them have needs which same, so that important for analyze for differentiate Among both of them. So that result rated for kind world and hereafter. So the authors are interested in researching Effects of prices and income on consumer choice and consumption in Islam

1.1 Objectives

The effect of changes in the price of a good on consumption can be broken down into two effects, namely the income effect and the substitution effect. The substitution effect explains how objective consumption patterns can change when there is a change in the price of one good relative to the price of another good. Consumers can look for cheaper alternatives when the price of certain goods or services increases, so they can maintain their lifestyle. Conversely, when the price of an item falls, the quantity demanded for that item will increase. (Nasrudin, 2019)

Then the second objective is the change in consumption caused by the move to a higher indifference curve. Because the consumer is a saver not a borrower (as shown by the fact that first-period consumption is less than first-period income), an increase in the interest rate makes him feel better. If consumption in period one and consumption in period two are normal goods, consumers will spread this improvement in welfare over period two. This income effect tends to make consumers want more consumption in both periods. (Wati & Awaluddin, 2019)

The third objective is related to consumption. Islamic economic logic has explained that if Muslim consumers are faced with two choices, namely halal goods and haram goods, then what is the optimal solution, which is the corner solution, namely *allocating* all of their income to consume halal goods. *Corner solution* is also an optimal solution because consuming illicit goods will eliminate dis-maslahah, while consuming a number of halal goods will increase maslahah. (Ridwan, 2019)

2. Literature Review

Substitution effect

The substitution effect is a change in the quantity demanded at the same level of utility. Thus, even if the individual remains on the same satisfaction curve, his consumption pattern will be reallocated to equalize the MRS (*Marginal Rate of Substitution*) with the new price ratio. (Anggrasari Herdiana, 2018) The substitution effect explains how consumption patterns change when the price of one good changes relative to the price of another good. Consumers can look for cheaper alternatives when the price of certain goods or services increases, so they can maintain their lifestyle. Conversely, when the price of a good falls, the quantity demanded for that good will increase. (Nasrudin, 2019)

The substitution effect is the impact that occurs when there is a change in the relative price of good X to good Y so that an attempt is made to replace one item with another. With a change in the price of an item, say X, the relative price of item X to item Y also changes. (Suprayitno,

2018) From some of the meanings of the substitution effect above, it can be concluded that it can explain how changes in relative prices affect consumer choices. When choosing a product, consumers will consider its price and the price of alternative products. This concept derives from the cross-price elasticity of demand. From some of the meanings of the substitution effect above, it can be concluded that it can explain how changes in relative prices affect consumer choices. When choosing a product, consumers will consider its price and the price of alternative products. This concept derives from the cross-price elasticity of demand.

Income Effect

The income effect is the change in consumption caused by a move to a higher indifference curve. Because consumers are savers not borrowers (as shown by the fact that first-period consumption is less than first-period income), an increase in the interest rate makes them feel better. If consumption in period one and consumption in period two are normal goods, consumers will spread this improvement in welfare over period two. This income effect tends to make consumers want more consumption in both periods. (Wati & Awaluddin, 2019)

The income effect states that when the wage rate increases, a person earns more. If leisure time is considered a normal good, an increase in a person's income will cause that person to spend more time relaxing. Because the total hours in a day are constant 24 hours, an increase in free time means that the time to work or the hours offered will decrease. (Syahputri, 2019)

If an individual's purchasing power increases, it is natural to expect that the quantity of each item that will be purchased will increase. Thus the increase in income responded positively by consumers. In this case the income expansion path *has* a positive slope for normal goods. As for inferior goods, the demand for *inferior goods* decreases with increasing consumer income. (Hutagaol & Sinaga, 2022)

The income effect is the change in consumption that occurs when a price moves the consumer to a higher or lower indifference curve or a movement from one indifference curve to another resulting from a change in real income caused by a change in price. (Karim, 2017)

The income effect is a change in the quantity demanded with a changing level of utility but the relative price of good X does not change. Thus the income effect arises because a change in price inevitably changes a person's real income, so that the individual will not remain in the same satisfaction curve, but can certainly move to another curve. (Anggrasari Herdiana 2018)

From some of the explanations above, income can be understood as income referring to changes in commodity demand caused by changes in consumer real income because there are price changes that can result in changes in curve shifts.

From the two theories there is a connection where when the price of an item falls, the impact on consumer choice can be divided into two types, namely the income effect and the substitution effect. The income effect is reflected in moving from a lower to a higher indifference curve, whereas the substitution effect is reflected in moving along a given indifference curve towards a sound point with a different slope.

Consumption in Islam

The theory of consumer behavior that is built based on Islamic law has fundamental differences from conventional theory. This difference concerns the basic values that form the foundation of

the theory, the motives and purposes of consumption, to the technique of choice and budget allocation for consumption.

There are three basic values which are the foundation for the consumption behavior of Muslim society, namely: (Amelia Rezky Kiki, 2021)

1. Belief in the existence of the afterlife and the afterlife. This principle directs a consumer to prioritize consumption for the hereafter rather than the world.
2. The concept of success in the life of a Muslim is measured by the morals of the Islamic religion, and not by the amount of wealth one has.
3. The position of wealth is a gift from Allah SWT and not something that is bad in itself (so it must be avoided excessively) .

Wealth is a tool to achieve life goals, if it is cultivated and used properly. This is in accordance with the word of Allah SWT in QS Al-Baqarah verse 262.

الَّذِينَ يُنْفِقُونَ أَمْوَالَهُمْ فِي سَبِيلِ اللَّهِ ثُمَّ لَا يُتْبِعُونَ مَا أَنْفَقُوا مَنًّا وَلَا أَذًى لَهُمْ أَجْرُهُمْ عِنْدَ رَبِّهِمْ وَلَا خَوْفٌ عَلَيْهِمْ وَلَا هُمْ يَحْزَنُونَ

Meaning: *"Those who spend their wealth in the way of Allah, then do not accompany what he has spent by mentioning it and hurting (the recipient's feelings), they will get a reward from their Lord. There is no fear of them and they do not grieve." .*

According to Manan, apart from the three basic foundations above, there are also five consumption principles in Islam, namely: (Amelia Rezky Kiki, 2021)

1. The principle of justice. This principle contains a double meaning regarding seeking halal sustenance and is not prohibited by law. Allah SWT said in QS Al-Baqarah verse 173.

إِنَّمَا حَرَّمَ عَلَيْكُمُ الْمَيْتَةَ وَالدَّمَ وَلَحْمَ الْخَنزِيرِ وَمَا أُهْلَ بِهِ لِغَيْرِ اللَّهِ فَمَنْ اضْطُرَّ غَيْرَ بَاغٍ وَلَا عَادٍ فَلَا إِثْمَ عَلَيْهِ إِنَّ اللَّهَ غَفُورٌ رَحِيمٌ

Meaning: *"Indeed, He only has forbidden for you carrion, blood, pork and (meat) animals slaughtered by (mentioning the name of) other than Allah. But whoever is forced to (eat it), not because he wants it and does not (also) exceed the limit, then there is no sin for him. Indeed, Allah is Forgiving, Most Merciful." .*

2. Hygiene principles. The point is that the food must be good and fit to eat, not dirty or disgusting so as to spoil the taste buds.
3. The principle of simplicity. This principle governs human behavior regarding eating and drinking in moderation. Allah SWT said in QS Al-A'raf verse 31.

يَبْنَیْ اَدَمَ خُذُوا زِينَتَكُمْ عِنْدَ كُلِّ مَسْجِدٍ وَكُلُوا وَشَرِبُوا

Meaning: *"O son of Adam! Wear your nice clothes every (entering) the mosque, eat and drink, but don't overdo it. Indeed, Allah does not like excessive people." .*

4. The principle of generosity. By obeying Islamic commands there is no harm or sin when we eat and drink halal food provided by God. Allah SWT said in QS Al-Maidah verse 96.

اُجَلَّ لَكُمْ صَيْدُ الْبَحْرِ وَطَعَامُهُ مَتَاعًا لَّكُمْ وَلِلْغَايَةِ وَحَرَّمَ عَلَيْكُمْ صَيْدَ الْبَرِّ مَا دُمْتُمْ حُرُمًا وَاتَّقُوا اللَّهَ الَّذِي إِلَيْهِ تُحْشَرُونَ

Meaning: "It is lawful for you to hunt sea animals and food (which comes) from the sea as delicious food for you, and for those who are on their way; and it is forbidden for you (to catch) land animals while you are in ihram. And fear Allah to Him you will be gathered (back)."

5. The principle of morality. Muslims are taught to recite the name of Allah SWT before eating and expressing gratitude after eating.

3. Methods

The method used in writing this article is a literature review. That is a search of both international and national literature related to the influence of prices and income on consumer choices and consumption in Islam .

4. Results and Discussion

The effect of the substitution effect on price changes

Normal goods In economics, normal goods are all goods whose demand will increase when people's income increases which also means that these goods have a positive demand elasticity. The term normal does not refer to the quality of the item. According to the indifference curve, the amount demanded for a good can increase, decrease, or stay the same when people's income increases.

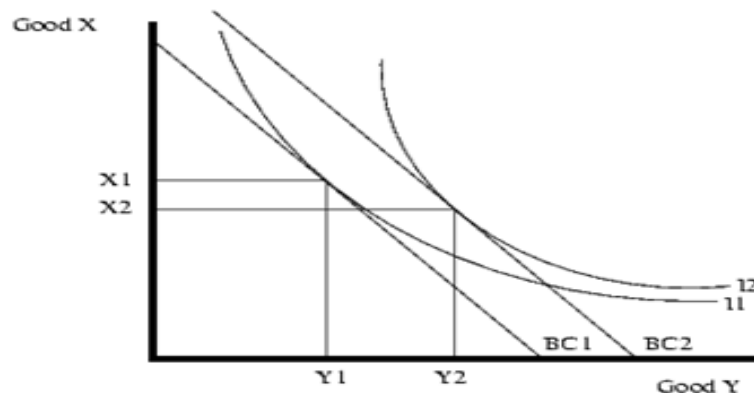


Figure 1 (Method & Pathway, 2021)

Described in the diagram above: good Y is a normal good because the quantity of the good demanded increases from Y1 to Y2 as income increases (BC1 to BC2). Good X is an inferior good because the quantity of the good demanded falls from X1 to X2 when people's income increases.

Inferior goods are goods for which demand decreases as people's income increases. One example of an inferior good is flip flops. When people's income levels are low, the level of demand for these goods will be high. However, when the level of public opinion increases, the demand for these goods will decrease because people leave them and choose to buy other, higher quality

sandals even at a higher price. According to the indifference curve, the quantity demanded of a good can increase, decrease, or stay the same when people's income increases.

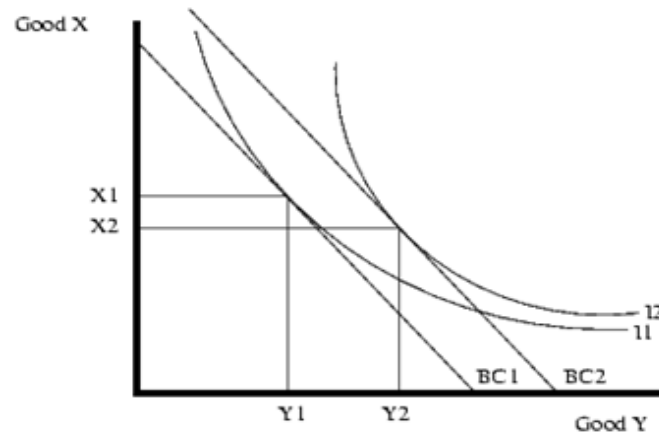


Figure 2 (Method & Pathways, 2021)

Described in the diagram below: good Y is a normal good because the quantity of the good demanded increases from Y1 to Y2 as income increases (BC1 to BC2). Good X is an inferior good because the quantity of the good demanded falls from X1 to X2 when people's income increases.

Giffen goods are goods for which when the price goes down the demand also goes down and an increase in the price of a giffen good actually increases the quantity demanded of the good. One of the goods that violates the law of demand, the higher the price of a giffen good, the higher the quantity demanded. Conversely, if the price of a giffen good is low, the demand for it will fall. Examples of this type of goods are low-quality staple foods *such* as cassava, cassava, and so on. The demand for these giffen goods is driven by poverty which keeps consumers from being able to afford higher quality goods .

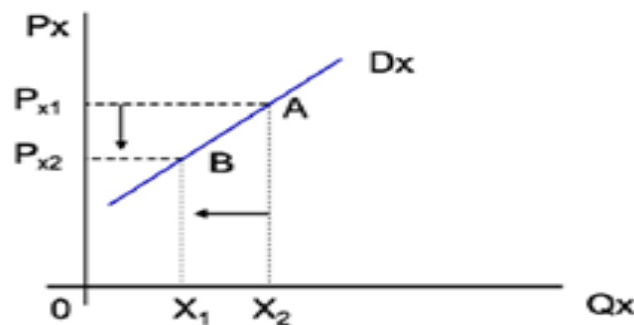


Figure 3 (Method & Pathway, 2021)

An example of a giffen item is clothing sold by second-hand clothing sellers, if the price of used clothing is low/down, the demand for these items also goes down because of the assumption in society that low prices mean the quality of the clothes is also low and vice versa, if the price goes up/high, it means quality. of used clothes is also high / good so that demand from consumers is also high.

Named after Robert Giffen (1837-1910), both for which demand increased as price increased. But these items may not exist in the real world. Giffen is the name of the economist who found evidence that there are consumers who increase their demand even though the price of the good rises.

In essence, giffen goods are classified as inferior goods (= goods for which, if our income increases, the demand for these goods will decrease. For example, before eating cassava, because income increased, cassava consumption decreased and people preferred rice consumption).

What is special, in giffen goods, the price of the goods plays a role. Nowadays, there are very few giffen goods because there are several conditions such as there must be few substitutes, and the percentage of one's income for the consumption of giffen goods is large (but there is still normal consumption of goods).

The Effect of Income on Consumer Choice

The effect of changes in the price of a good on consumption can be broken down into two effects, namely the income effect and the substitution effect. the income effect is the change in consumption that occurs when a price moves consumers to a higher/lower indifference curve or a movement from one indifference curve to another caused by a change in real income caused by a price change, whereas the substitution effect is a change in consumption that occurs when a price moves consumers along an indifference curve to a point with a new marginal point of substitution or a movement along an indifference curve results from a change in the relative prices of goods, with constant actual income.

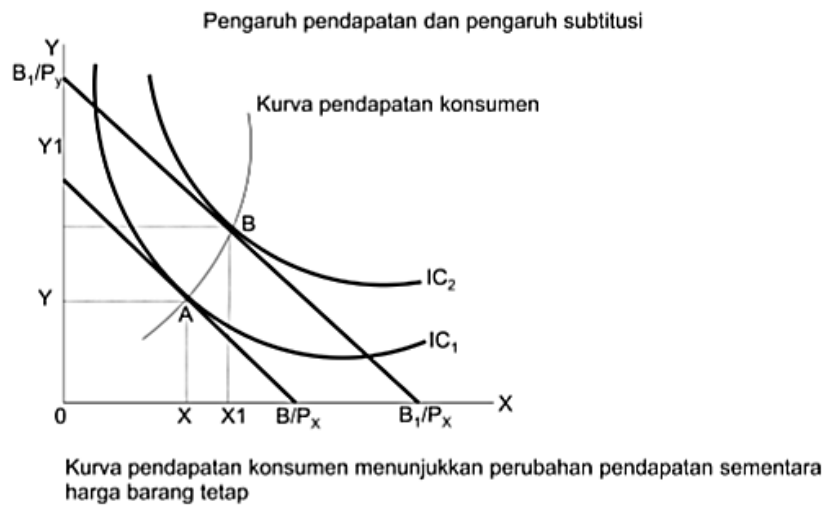


Figure 4

The substitution effect, the movement along the indifference curve to a point with a different marginal rate of substitution, is shown here by the change from point A to point B along the indifference curve. The income effect, the movement to higher indifference curves, is shown here by the change from point A to B on the indifference curve.

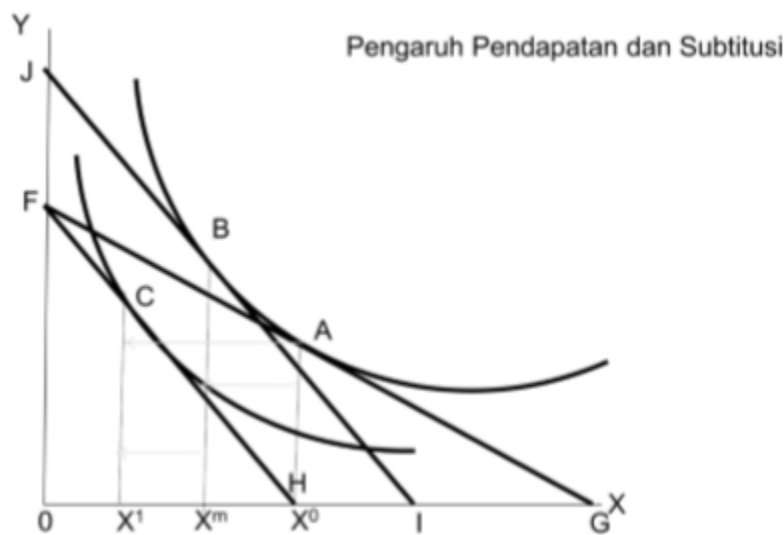


Figure 5

Suppose the consumer is initially in equilibrium at point A in the figure above, along the budget line connecting points F and G. Suppose the price of good X rises so that the budget line rotates clockwise and becomes the budget line connecting points F and H. Two things. One of the things that can be noticed about this change, first, is that an increase in the price of good X causes the budget line to slope steeper, reflecting a higher rate of market substitution between the two goods. Both of these factors cause the consumer to move from the initial consumer equilibrium (point A) to the new equilibrium (point C) in the figure above.

It is useful to isolate the two effects of a change in price to see how each effect individually changes consumer choice. In particular, ignore for a moment the fact that rising prices lead to lower indifference curves. Suppose that after the price increase, the consumer is provided with enough income to reach the budget line connecting points J and I. This budget line has the same slope as line FH, but implies higher income than budget line FH. Given this budget line, the consumer will reach equilibrium at point B, which is when less good X is consumed than at the initial situation, point A. The movement from A to B is called the substitution effect, reflecting how consumers will react to different levels of market substitution. different.

The substitution effect is the difference $X_0 - X_m$ in the figure. Importantly, the move from A to B leaves the consumer on the same indifference curve, so that the reduction in consumption of good A that the movement implies reflects a higher market substitution rate, not a decrease in the consumer's "real income."

The consumer doesn't actually face the JI budget line when prices rise, but faces the FH budget line. Now, let's take back the revenue we provide to consumers to compensate for the price increases. When these revenues are taken, the budget line shifts from JI to FH. This shift, in the budget line, reflects only a reduction in revenues; the slopes of the budget lines JI and FH are identical. Therefore, the movement from B to C is called the income effect. The income effect is the $X_m - X_1$ difference in the figure above; reflects the fact that when prices rise, the consumer's real income falls. Because good X is a normal good in the figure. A reduction in income leads to a further reduction in X's consumption.

The total effect of a price increase, therefore, consists of substitution and income effects. The substitution effect reflects movement along an indifference curve, thus isolating the effect of changes in relative prices on consumption. The income effect is produced by parallel shifts in the budget line, thus isolating the effect of reduced income on consumption and is represented by the movement from B to C. The total effect of the price increase, which we observe in the market, is the movement from A to C. The total effect of the change in consumer behavior becomes not only from the effect of increasing the relative price of item X (movement from A to B) but also from the reduced real income of consumers (movement from B to C) (Karim, 2017)

How consumption in Islam

One of the consumption behaviors is the tax in the tax itself there is an income effect and a substitution effect. The income effect results from a reduction in the income available due to the tax, while the substitution effect refers to the impact of the tax on the relative prices of the commodities subject to the tax.

So in dealing with efficiency issues from an economic perspective there are four reasons why taxes are not economically efficient according to four, namely:

Smith (1776) tackled the issue of efficiency from the perspective of the economy of collection. He gave four reasons why a tax can be economically inefficient, namely, (i) a too burdensome and

costly administrative apparatus, (ii) the disincentive effect of tax on doing business, (iii) an ill-designed tax that creates the "temptation" to evade it and imposes heavy penalties on those who attempt to evade it, and (iv) too frequent and too burdensome tax examinations. (Gueydi, 2021)

The purpose of the four reasons according to Smith why taxes can be economically inefficient, namely, administration that is too burdensome and expensive apparatus, the disincentive effect of taxes on doing business, poorly designed taxes that create "temptations" to avoid them and impose heavy penalties on them who try to avoid it, and too frequent and too burdensome tax audits. So that the reduced income due to the relatively taxable price produces a substitution effect. In the 5th zakat conference it was concluded that the income effect exceeds the substitution effect. Zakat will have income and substitution effects which have the opposite effect. The impact of taxes on capital and analysis of income and substitution effects can be addressed from two angles, namely determining the portion between consumption and saving for the future and the tax treatment of various types of savings. (Gueydi, 2021) The two things above result in a different substitution effect. This approach is also the same as zakat.

Zakat and Savings (Present and Future Consumption) Tax on interest will have an income effect and a substitution effect, because individuals will reduce available income and reduce consumption in the present and future, while saving will become less attractive due to taxes that will encourage individuals to increase their consumption and reduce it in the future. Therefore these two effects do not work in the same direction. Zakat applies not to the return of savings as in the case of interest above but to the savings themselves. The income effect results in a reduction in saving and consumption. In addition, zakat saving creates incentives or preferences for current consumption compared to the future (thrifty) because now is less attractive or a substitution effect.

Thus both the income effect and the substitution effect result in a reduction in savings. The result of income and the substitution effect on saving is predictable and is a reduction. The reduction in savings caused by zakat can be divided into two components: The reduction is caused by the income effect and Reduction caused by substitution effects

In contrast to Kahfn, zakat results in a lower consumption tendency and ultimately increases savings in aggregate. There are a number of assumptions related to the impact of zakat on savings, namely; 1) Current and future consumption (savings) are treated as superior goods for increasing income 2) Individuals can choose how much they consume and how much they save 3) All forms of savings are subject to tax or zakat. (Gueydi, 2021)

Zakat and Savings (The impact is different) Savings tax can be favorable and unfavorable depending on the different tax treatment on each savings. This produces a substitution effect or replaces higher tax savings with lower taxes.

In relation to zakat, if individuals decide to save at the bank without expecting interest or returns, the amount of their savings is reduced annually by the amount of zakat until it falls below the nisab. Therefore individuals have incentives to invest savings and to ensure that the amount of savings does not decrease due to zakat Zakat generally behaves similarly to taxes, in the sense that it has a substitution effect behavior, but there are arguments that: 1) The behavioral effects

of zakat will be significant compared to taxes because it is relative to personal choice and self-obedience embedded desire to correctly determine and pay zakat 2) Zakat losses will be lower due to the application of equal rates 3) zakat will be more beneficial and affect savings than taxes. (Gueydi, 2021)

Principles of Emergency and Maslahah in Consumption

In Islam, things that are lawful and things that are unlawful are clearly defined. Economically, it has been explained that if Muslim consumers are faced with two choices, namely halal goods and unlawful goods, then the optimal solution is what is the *corner solution*, namely allocating all of their income to consume halal goods. *Corner solution* is also an optimal solution because consuming illicit goods will eliminate dis-maslahah, while consuming a number of halal goods will increase maslahah. (Ridwan 2017)

Islamic Sharia wants humans to achieve and maintain their welfare. Imam Shatibi uses the term 'maslahah', which has a broader meaning than mere utility or satisfaction in conventional economic terminology. Maslahah is the most important goal of syara' law sufficient needs - and not fulfilling satisfaction / desire is the goal of Islamic economic activity, and efforts to achieve this goal are one of the obligations in religion.

At a certain level of income, Islamic consumers, because they have an allocation for matters relating to the hereafter, will consume less goods than non-Muslims. The thing that limits it is the concept of maslahah mentioned above. Not all goods/services that provide satisfaction/utility contain maslahah in them, so not all goods/services can and are suitable for consumption by Muslims. In comparing the concept of 'satisfaction' with 'fulfillment of needs' (which is contained in maslahah), it is necessary to compare the levels of objectives of syara' law, namely between *daruriyyah*, *tahsiniyyah* and *hajiyyah*. (Arjun 2020)

6. Conclusion

The thing that causes a change in the quantity demanded when there is a change in price is the *substitution effect (SE)* and *income effect (IE)*. With a price change, there will be two impacts that occur. Thus a change in price will cause the quantity of goods demanded to increase or decrease depending on the resultant of these two impacts.

In the language of Islamic economics, the level of consumption of these goods is usually termed goods that are *daruriyat*, *tahsiniyat*, and *hajiyyat* in nature. Consumption of *daruriyat* goods refers to goods whose scarcity will cause a person to get into trouble and can even eliminate the safety of life, religion, mind, lineage and property.

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