

**The Dark Economy:
Examining the Practices and Policies of the Islamic State**

Andrew J. Williams

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I. INTRODUCTION

On June 29th 2014, Abu Bakr al-Baghdadi, leader of the Islamic State of Iraq and Syria (ISIS), declared the group a “Caliphate” from the city of Mosul, Iraq and rebranded under the name of the “Islamic State” (Collard 2015). The establishment of the new Caliphate, according to Brigitte L. Nacos (2015, 67-68), granted the leaders of ISIS a claim to “religious, political, and military authority over all Muslims around the world.” While the actions of ISIS members draw comparisons to the Islamic extremists associated with Al Qaeda, an organization responsible for the September 11th attacks in 2001, the goals, organization, and scale of the Islamic State’s operations significantly exceed the attempts of other radical Islamic groups originating in the Middle East. The leaders and militants of both Al Qaeda and ISIS share a similar vision in wanting to “purify” the religion of Islam from “the wrong teachings and practices of Muslim and non-Muslim infidels” through the use of terror and violence (Nacos 2016, 69). But while Al Qaeda relied on a decentralized network of “safe havens” and small forces to carry out missions, ISIS forces have assumed an offensive strategy designed to conquer and coerce large territories (Nacos 2016, 69).

As Audrey Kurth Cronin (2015) discusses in her article entitled “ISIS is Not a Terrorist Group”, the Islamic State is a successor to Al Qaeda in a variety of ways, ultimately improving upon the effectiveness of their “jihadist” agenda. While Al Qaeda relied on only “dozens or hundreds” of members to engage in terror attacks, the Islamic State boasts a well-trained and equipped fighting force of nearly 30,000 militants (Cronin 2015). Fighters under the Al Qaeda network relied on guerilla-styled attacks, but were

outmatched when going toe to toe with government armies. Islamic State fighters, in comparison, operate in a similar manner to state military forces, coordinating attacks and assuming control of large cities and regions. At the present, the Islamic State continues to control territory in Iraq and Syria while expanding influence in Libya and Nigeria, churning the propaganda machine in hopes of attracting more sympathy and support from Muslims around the world (Nacos 2016, 68). In order to ensure the Islamic State's continued rise and legitimacy as the new Caliphate, the leaders of ISIS have set in place political and economic structures designed to sustain military operations.

With an ever-growing concern voiced by Western media outlets in both America and Europe, especially in light of Islamic State attacks on journalists, civilians, and other resistance forces, efforts have been taken by nations including the United States to slow the advance of the organization. Outside of the military strategies being explored and implemented against ISIS forces, exploring the inner working of the Islamic State's economy provides valuable information in regards to how the organization generates funding for the radical cause. The Islamic State's economy, also derogatorily referred to as the "Daesh" economy will be examined in detail throughout the course of this paper (Garrity 2015). More specifically, the term Daesh, translated from Arabic, means "to trample and to crush" as well as "a bigot" (Garrity 2015). If the Islamic State truly intends to exercise takfiri doctrine in putting to death all persons who either reject their understanding of Islam or accept another interpretation, then determining the effectiveness of the Daesh economy from an Austrian perspective will prove helpful in assessing the group's sustainability moving forward (Wood 2015).

As will be developed through the following sections of this paper, the economic practices and policies enforced by Islamic State leaders are counterintuitive to generating prosperity or furthering their expansionist goals, thus the level of concern surrounding the organization is significantly exaggerated. First, to be considered is whether or not the Islamic State should be classified as a non-state terrorist organization or a legitimate state actor will be explored in order to set the context for the rest of the paper. Second, the religious foundations for the economic practices of Daesh will be examined through the study of Islamic Scholars and researchers. The third section of the paper will detail the Daesh economy in full, touching on the instruments used to generate funding as well as the policies and practices taken by ISIS leaders to ensure their forces effectively remain in control of financial operations. The fourth section of the paper will examine different Austrian scholars and economists to provide a theoretical analysis of why the Islamic State's economic practices are ultimately perverse for macroeconomic growth. Finally, the fifth section will detail empirical evidence to demonstrate how the Islamic State's current practices have hurt their economic potential.

II. Defining the Political Structure of the Islamic State

Before delving into the particulars of the Daesh economy and the foundational principles of an Islamic economy dictated by their interpretation of the Quran, a general confusion persists over how to define the Islamic State, whether as a terrorist organization or an expanding state (Nacos 2016, 67). Clarifying where the Islamic State falls on the spectrum of political classification will help set the context for the rest of the paper in defining the political structure of Daesh. Beyond establishing a clear definition,

the legitimacy of the group can be assessed on both a domestic and international scale. The rapid growth of ISIS since the mid-2000s needs clarification in light of the group's success, and the work of Nacos (2016) and Cronin (2015) are useful sources for exploring the matter.

As noted previously in the introduction of the paper, the Islamic State has separated itself from other terrorist organizations in terms of the large scale of its operations. While other terrorist groups including Hezbollah, Hamas, and FARC have been able to control territory under a well-organized military force, the Islamic State operates in both the Middle East and Africa with intentions of expanding even farther into Europe (Nacos 2016, 68). Where other extreme Islamic insurgencies, including Al Qaeda, are primed on opposing the authority of "secular" rule in Muslim communities, Cronin (2015) notes the intentions of the Islamic State are farther reaching. Specifically, ISIS hopes to continually legitimize a firm and "pure Sunni Islamist state", seeking to expand control over territory in the Middle East for the purpose of smashing the political borders established by Western powers in the 20th century (Cronin 2015). In short, the Islamic State's leaders seek to be the "sole" authority over all Muslims in the world, not simply the Middle East and Africa (Cronin 2015).

Beyond the large scale and scope of the Islamic State's operations, the bureaucratic organization of Daesh also makes the group remarkably similar to the political structure of a state actor. At the top of the Islamic State's structure, the group's leader, Abu Bakr al-Baghdadi, also known as the Caliph or Commander in Chief (Thompson & Shubert 2015). Baghdadi is accompanied by a Cabinet of advisors who

collaborate for the purpose of enacting and enforcing Islamic State policies over the regions of governance. Baghdadi, however, retains a position of nearly “unchecked authority” over the captured territory (Glenn 2015). In order to effectively maintain and manage the region under ISIS control, Baghdadi appoints deputies to watch over and deliver orders to the territories controlled in both Iraq and Syria. At the present, Abu Ali al-Anbari is appointed as the Islamic State’s deputy over Syrian territory while Abu Muslim al-Turkmani is appointed deputy over Iraqi territory (Thompson & Shubert 2015). Thus Baghdadi, the Cabinet, and the two deputies make up the executive branch of the Islamic State government, referred to as the “Al Imara” (Thompson & Shubert 2015).

Each deputy is assigned the responsibility of dictating the will of the Caliph to the governors within both Syria and Iraq. In total, 24 governors, evenly divided between Iraq and Syria, answer to the authority of deputies (Thompson & Shubert 2015). In order to ensure the orders of the executive branch are received and properly administered throughout the sub-states within each territory, the governors utilize local councils for the purpose of implementing policy (Thompson & Shubert 2015). The councils assigned to each governor specialize in different areas of bureaucratic management including legal matters, finances, intelligence, and so on (Glenn 2015). In an effort to guarantee obedience to the executive branch, the Shura Council acts as a religious monitor for the Daesh elite, reporting directly to the executive branch while making sure all levels of society adhere to strict sharia law (Thompson & Shubert 2015).

Through a system of strict authoritarian command, the leaders of the Islamic State strive to maintain “direct control” over both the citizens dwelling in their territory as well as their fighters (Glenn 2015). The schools, courts, financial institutions, and businesses all are required to yield to the will of the Caliph, and anyone who dares offer opposition faces the threat of extortion, torture, public humiliation, and/or a brutal death. The complex system of rule as seen under ISIS had not been established by previous jihadi groups in the region, let alone a definitive declaration of being a new Caliphate. Nacos (2016, 69) notes how the bureaucratic qualities and military endeavors of ISIS make the group very similar to other nation-states. But beyond the ability to influence local populaces under ISIS control, the Islamic State has also utilized extensive propaganda campaigns to recruit Muslims around the world to migrate to the region to join the so-called holy cause and expel the infidels (Nacos 2016, 216).

Debate over whether ISIS can really be classified as a state actor utilizing terror or as a non-state terrorist organization has garnered significant attention from political and intelligence experts. At the present, the Islamic State is not recognized by any state power as having any “international legitimacy”, thereby limiting its potential for being recognized as a state (Shany, Cohen, & Mimran 2014). The Islamic State also does not clearly meet several characteristics of statehood as defined by the 1933 Montevideo Convention on the Rights and Duties of States, including a definable territory and permanent population (Shany, Cohen, & Mimran 2014). The Islamic State, furthermore, is not a member of the United Nations, meaning the claims of statehood by ISIS have gone completely unrecognized by other nations primarily because the radical government

acquired land and resources through the use of violence (Shany, Cohen, & Mimran 2014). Despite the near complete rejection by politicians and religious leaders of the Islamic State being a legitimate state-actor, no universal or unified definition of statehood exists, meaning the standards for judging ISIS are often ambiguous and continually subject to change (Boyle 2015).

In light of this reality, writers including Tim Arango (2015) of *The New York Times*, Peter Weber (2014) of *The Week*, and Audrey Kurth Cronin (2015) all make the argument for ISIS being either a state-actor or a pseudo-state actor in light of the confusion surrounding statehood classification. The Islamic State is currently engaged in a civil war with the Iraqi government and has gained significant territory, showcasing the military might of the radical group (Cronin 2015). While the Islamic State also governs with an iron fist, the governmental institutions set up by the group have brought “relative stability” to the communities living in the Daesh region (Arango 2015). Tim Arango (2015) recognizes the ISIS government will likely not become an “accountable” state within the near future, but given time and effort, he argues the potential exists. Peter Weber (2014) argues for nations in the West to classify ISIS as a sovereign state in order for a formal declaration of war to occur against the Islamic State. While great difficulties exist in attempting to fight a terrorist organization run on radical ideology, granting ISIS statehood, a goal its leaders have been seeking intensely, would allow Western states to engage in conventional combat in order to topple the formalized government (Weber 2014).

In assessing the arguments on both sides, the Islamic State meets the criteria of statehood while falling short in terms of international relations. ISIS has developed a system of government structured around a strict religious legal system in established territory, assigning political power to a host of individuals for the purpose of maintaining the goals and stability of the Caliph. But despite such characteristics, due to the government's use of terror and violation of human rights, other states on the global political stage refuse to recognize the Islamic State with any legitimacy. The Islamic State is thereby deemed as a pseudo-state, indicating the group is trying to take the necessary steps on the path towards achieving statehood, yet such efforts are being hampered by the international community indefinitely. Regardless of how other states in the global arena classify the Islamic State, the group cannot simply be deemed as just another terrorist organization when its leaders have already set up an extensive system of government concerned with managing the economic affairs of the people under Daesh control.

III. Scriptural Interpretation and Justification for Islamic State Economic Policy

In order for one to understand the current policies and regulations dictating the actions of thousands living under the Daesh economy, exploring the history and holy books of the Islamic religion offers key insights into the justifications for such practices. Regardless of time and the presence of the ISIS, a majority of the Muslim world living in both the Middle East and Africa has been shaped by Sharia law as presented in both the Quran and the Sunnah (Facchini 2008, 3). Sharia law, also understood as “path” in Arabic, is a set of laws under Islam designed to guide the life of believers in almost all

areas from daily routines to religious obligations (Johnson & Sergie 2014). For example, Saudi Arabia still abides by Sharia law in regards to carrying administering legal affairs such as criminal punishments and familial affairs (Johnson & Sergie 2014). While Islamic countries, including Azerbaijan and Tajikistan, have opted to form secular governments, a majority of countries located in the Middle East continue to look to Islam as their foundation and source of legitimacy (Johnson & Sergie 2014). The Islamic State not only enforces Sharia law in its entirety, the ISIS government also enforces a strict interpretation of the Muslims holy books to guide the political and economic decision making.

According to the work of Francois Facchini (2008, 8), the early Islamic Caliphates and a significant amount of Muslims states, including the Islamic State, do not see any separation between political and religious affairs. In short, while countries in the West, predominantly established and ruled by Christian leaders, recognize the need to distinguish the church from the state, the religion of Islam dictates a different tradition in building states (Facchini 2008, 12). According to the writings of Muslim scholars, including Al-Mawardi, the moral values of Islam will not be effective unless observed by all citizens, and the institution of the State serves as an essential mechanism in ensuring such Islamic values are enforced (Chapra 2016). Since the state is expected to submit to the laws of “God” (Allah) under a system of government guided by Islamic teaching, there can be no separation between the spiritual and temporal orders (Facchini 2008, 12). Based on the rhetoric and propaganda churned out by the Islamic State in magazines

including *Dabiq*, the leaders and followers of ISIS hold to such an interpretation of Islam's holy books (Wood 2015).

According to the research and interviews conducted by Graeme Wood (2015) in *The Atlantic*, Islamic extremists see tremendous significance in ISIS's self-proclaimed establishment of a Caliphate. One of the Muslim extremists interviewed, Anjem Choudary, argued the establishment of a new Caliphate would require complete adherence to Sharia law as well as the migration of all Muslims to the new Islamic state (Wood 2015). All Muslims under the extremist interpretation must swear an oath of allegiance, or "bay'ah", to the Caliph or run the risk of being labeled as an infidel or "apostate" (PragerU 2016). Choudary also argued, through his interpretation of Islamic law, the problem with Muslim states only partially implementing Sharia law. He states: "when places like Saudi Arabia just implement the penal code, and don't provide the social and economic justice of the Sharia—the whole package—they simply engender hatred toward the Sharia" (Wood 2015).

Such religious claims indicate the totality found in the Islamic State's interpretation of Muslim scripture and law. Bernard Haykel, a professor at the University of Oxford, argues the Islamic State is attempting to resurrect an empire seen in the earliest days of the religion, carefully attempting to reproduce the policies enacted during and after the time of the Prophet Mohammad (Wood 2015). While few sources survive from the first Muslim society created by Mohammad during the late 6th and 7th centuries, other accounts arising from Islamic historians in the 9th and 10th centuries offer insight into what life was like (Hughes 2016). From the early sources, the leaders of the early

caliphates often followed an apocalyptic vision, believing in the idea of expansion to violently impose the good of the Islamic religion against people who refused to accept (Hughes 2016). ISIS chose to adopt a similar religious vision for their state in order to maintain authenticity with the customs of the period, claiming such practices to be true Islam. In terms of economic practices, the next section detailing the components of the Daesh economy will offer historical examples of how ISIS justifies the establishment of certain policies.

While Islamic State supporters continue to justify their actions through a strict interpretation of Sharia, one must remember such views represent an incredibly small portion of the global Muslim population. According to the estimates tallied from polls at the PEW Research Center, of the nearly 1.5 billion Muslims worldwide, only about 2 percent, or roughly 3 million Muslims, believe in the idea of taking violent action to enforce the strict interpretation of Sharia law (PragerU 2015). The Islamic texts have sparked debate within the Muslim community for centuries over the correct interpretation of certain laws and passages, and the arguments are not too different from the discussions seen in both Christianity and Judaism. But what can be said for certain is the Islamic State interprets their “Holy Scriptures” with a totalitarian mindset, looking to expansionary policy and means of extreme violence to bring about the will of Allah (PragerU 2015). The totalitarian mindset permeates every facet of life under the Islamic State, as will be explored in the economic practices of ISIS.

IV. Detailing the Islamic State’s Economic System and Policy

In order to fund the expansionary efforts of the Islamic State, ISIS supporters have developed a complex economic system within their Syrian-Iraq territory to both finance military operations and stabilize their strict Sharia society. According to a Thomas Reuters report written by Jean-Charles Brisard and Damien Martinez (2014, 3), the Islamic State controls nearly \$2 trillion in assets while generating an income of almost \$3 billion a year. Claiming a region roughly the size of the United Kingdom, the Islamic State controls a significant amount of natural resources and commodities, including oil, agriculture, and industrial activities (Brisard & Martinez 2014, 3). As mentioned previously, the Islamic State relies on strict interpretation of Sharia law to guide and justify their revenue generating actions. Discussed below are the different categories of revenue generation utilized in the Daesh economy, each understood in light of ISIS's scriptural and historic interpretations.

i. Taxation

One of the largest sources of revenue for the Islamic State, if not the largest, is generated through the implementation of an extensive tax system, established for the purpose of strengthening "administrative and civil control" over the conquered region (Brisard & Martinez 2014). According to an audit report smuggled out of Deir ez-Zor, Syria, taxation generates nearly 25 percent of the income for ISIS fighters (Smith 2015). In other reports, Sarah Almkhtar (2015) discovered taxation and extortion together generated the largest portion of ISIS revenue in 2014, totaling around \$600 million for the year. Historically, Islamic jurists and religious leaders attempted to create a system of taxation adhering to the words of the Quran as well as the words of the Prophet

(Böwering & Crone 2012, 545). Today, the leaders of the Islamic State incorporate the work of the previous religious authorities into structuring their own tax system. The Islamic State justifies the tax system through the doctrine of *siyasa shar'iyya*, “which delegates to Islamic governments a limited authority to develop man-made regulations that are consistent with” Sharia law (McCants & Revkin 2015).

According to the research of Gerhard Böwering and Patricia Crone (2012, 545), the classic tax system of Islam, as seen in the centuries during and following the first caliphates, is based on the legal status of (1) taxable land and (2) the “communal or religious status” of the taxpayer. The first of the Islamic taxes was the *zakat*, a 2.5 percent tax tied to all Muslims living under the Islamic State, imposed primarily as a religious duty for giving alms to the poor (Böwering & Crone 2012, 545). *Kharaj*, commonly accounting for the largest portion of state revenue, was a land tax imposed by the Islamic State on both Muslims and non-Muslims (Böwering & Crone 2012, 545). For the non-Muslim citizens living within an Islamic state, a poll tax called *jizya* was levied at a “fixed amount” (Böwering & Crone 2012, 545). Finally, a tax called *ushr* was imposed as an import-export tariff in trade, historically levied around 10 percent on non-Muslim foreign traders, 2.5 percent for Muslims, and 5 percent for “local” non-Muslims (McCants & Revkin 2015). While the *zakat* and *jizya* find origin in the words of the Quran, the *kharaj* and *ushr* have developed over time went on and are not explicitly described in either the Quran or Sunnah (McCants & Revkin 2015).

Today, the Islamic State continues the tradition of previous caliphates in imposing all of the previously listed taxes, while incorporating several new taxes to further increase

state revenue. According to the research of Mara Revkin (2015), the Islamic State has *zakat* offices scattered throughout both Iraq and Syria for the purpose of collecting taxes and redistributing the revenue. Beyond the taxes typically reported in previous caliphates, the Islamic State imposes taxes on resources such as water and electricity, despite the poor quality of each (Smith 2015). The report written by Jean-Charles Brisard and Damien Martinez (2015) notes the following taxes reported from regions under ISIS control: taxes on communication companies, taxes on all goods in ISIS controlled territory, taxes on cash withdrawals, border checkpoint taxes for trucks, road usage taxes, and even taxes on looted archeological sites.

Reports leaking out from cities under ISIS control often describe a level of corruption accompanying the tax collecting process. For example, in an interview conducted by Vanek Smith (2015) with Mohammed Kedderer, a Syrian citizen who escaped from ISIS, revealed how Islamic State tax collectors often generate new tax requirements for citizens, threatening the use of force if one refuses to pay. Whether demanding tax money because one's beard is too long or because one forgot to carry certain papers, ISIS tax collectors are notorious for coercing away the money of citizens (Smith 2015). Such methods of taxation forced Kedderer to invest in gold jewelry as well as hiding to protect his monetary assets (Smith 2015). Beyond the suspicious taxation methods utilized on citizens, employees for the government of Iraq see their salaries taxed at nearly 50 percent while companies based in either Iraq or Syria see their "contracts and revenue taxed up to 20 percent" (Almukhtar 2015).

In total, reports indicate the Islamic State generates between \$8 million and \$30 million a month through means of taxation and extortion, and anywhere from \$100 million to \$300 million in revenue annually (Brisard & Martinez 2014). While the primary methods of taxation, including *zakat* and *jizya*, do find partial justification in the words of the Quran, researcher Mara Revkin (2015) argues the additional taxes imposed at the provincial and local levels are utilized for the purpose of “state-building and territorial conquest.” According to an interview conducted by Kevin Sullivan (2015) for *The Washington Post*, Abu Ibrahim al-Raqqawi, an activist from the city of Raqqa, Syria, reported of the Islamic State raising taxes for the purpose of paying both fighters and foreigners. While ISIS claims to be adhering to Islamic principles, the reports of fighters mistreating the poor continue to call into question the legitimacy of the Islamic State’s tax system (Sullivan 2015).

ii. Ransom Payments

According to the research of Christine Duhaime (2015, 4), one of the most “consistent” methods utilized by the Islamic State for revenue generation is by receiving ransom payments for kidnapped individuals. Using foreign brokers as the middlemen, the Islamic State receives US cash through a conduit country in exchange for the individual (Duhaime 2015, 4). The ransom process is complex and logistically demanding, requiring the efforts of “spies, informers, kidnappers, jailers and negotiators” to arrange the deals and reap a profit (Inside the Islamic State Kidnap Machine 2015). ISIS typically targets high ranking political officials, businessmen, and foreign nationals for kidnapping, and the continual practice has reaped the Islamic State approximately \$10 million a month

(Brisard & Martinez 2014). In terms of ransom kidnappings, ISIS does not clearly provide religious justification for the action besides the fact the victims are declared as infidels. Rather, the tactic is motivated by the necessity of generating wealth versus finding root in Islamic teachings (Balogun 2013).

iii. Confiscation/Looting

While the Islamic State's tax system easily classifies as monetary coercion, the wholesale business of looting generates a sizeable portion of the government's revenue. According to the audit report from the ISIS occupied city of Deir ez-Zor, Syria, looting and confiscation comprise 44 percent of government revenue in the province (Smith 2015). The detailed Syrian records chronicled the theft of a variety of goods, including cars, houses, land, cigarettes, and even livestock (Smith 2015). Beyond the material assets of citizens, Islamic State forces focused their efforts on financial institutions as well, stealing nearly \$425 million from "the Mosul branch of the *Central Bank of Iraq*" (Brisard & Martinez 2014). The Islamic State justifies the theft of property as simply the "gathering of spoils" as conquerors of their territory in the name of Allah (Martin 2014). As a result, theft is essentially sanctioned by the state for the purpose of sustaining government operations and fighters.

According to the research of Erika Solomon and Sam Jones (2015), once ISIS fighters have confiscated stolen goods, they report their findings to "war spoils" offices in their respective provinces, calculating the monetary value of the loot and granting a fifth of the good's value to the fighter. While weaponry and equipment is transferred to the

government, all “non-military goods are sold at ‘loot markets’”, where Islamic State fighters are permitted to buy any good at half the market price (Solomon & Jones 2015). For example, an LCD television priced at \$150 for a civilian would be sold for \$75 to an ISIS militant. With loot markets defined in such a manner, the Islamic State’s fighters are more capable of purchasing goods to fulfill their needs and wants over the average citizen living in occupied territory, rapidly increasing the gap between the rich and poor.

Another area where the Islamic State profits tremendously from looting is with the market for antiquities. While ISIS has received considerable media attention for their destruction of so-called pagan archeological/historical sites, militants often raid cities and sites beforehand to collect large amounts of statues, artwork, and coins for the black market (Smith 2015). The Daesh government is closely involved in the business of artifact smuggling and trafficking, going as far as to assign a “minister of antiquities”, to oversee the looting endeavors, as well as enforcing looting regulations (Smith 2015). As per the interview between Vanek Smith (2015) and Allison Cuneo, in order for a fighter to loot a site, they must first pay and wait for an official permit for the Islamic State to do so. The value of the artifacts being snuck out of the region total in millions of US dollars.

iv. Extractive Industries

Due to the location of the Islamic State’s territory, the region is blessed with an abundance of natural resources, allowing ISIS forces to take advantage of the factories and fields previously under Iraqi/Syrian control for their radical religious cause. Oil is one of the most plentiful resources found in Islamic State territory, and as of 2014 ISIS

controls seven oil fields and two refineries in Syria, thirteen oilfields and one refinery in Iraq, and “several pumping stations in both countries” (Brisard & Martinez 2014, 6-7). According to the research of Jean-Charles Brisard and Damien Martinez (2014, 7), the Islamic State controls “more than 60 percent of Syria’s oil production capacity and less than 10 percent of Iraq’s oil production capacity”, allowing for an estimated 80,000 to 120,000 barrels of oil to be produced every day. Such production capacity would, in theory, net the Islamic State roughly \$2 to \$4 million a day or close to \$730 million or \$1.4 billion a year (Brisard & Martinez 2014, 7). One report from September 2014 estimated the Islamic State generated nearly \$150 million in one month alone from oil production (Duhaime 2015, 5).

Reports and production totals are prone to inaccuracies due to the fluctuations in territory controlled and the periodic airstrikes carried out by the United States (Brisard & Martinez 2014, 7). By October 2014, intelligence indicated the United States had destroyed nearly “half” of the Islamic State’s refining abilities, severely limiting total outputs (Swanson 2015). Despite estimates of being limited to producing only 20,000 barrels of oil a day, due to the airstrikes, ISIS militants are covert and cunning with their sales (Brisard & Martinez 2014, 7). ISIS smugglers and traders utilize social media applications on their cell phones to coordinate meetings along the Turkish border, negotiating prices below the market level for oil and even bartering in certain situations (Swanson 2015).

Besides oil, the Islamic State is heavily involved in the production of natural gas, phosphate, and cement. The research of Jean-Charles Brisard and Damien Martinez

(2014, 8) reveals ISIS controls of seven natural gas fields in Iraq and Syria and is theoretically capable of generating nearly \$979 million a year if used to full potential. With control over a phosphate mine in the Al-Anbar province of Iraq, the Islamic State has the capacity to generate almost \$50 million a year from producing and trading phosphate (Brisard & Martinez 2014, 8). Five cement factories are also under Islamic State control, capable of producing between \$300 and \$580 million a year if the facilities are utilized to their full potential (Brisard & Martinez 2014). While the potential total revenue from such industries is considerably high, opportunities are limited given the lack of required industrial assets and the threat of sabotage by outside powers (Duhaime 2015, 6).

Finally, agriculture and farmers dwelling within ISIS territory serve as yet another extractive means to generate revenue for the state. Besides paying *zakat* taxes, farmers sell their crops to the Islamic State officials who wait until the market price of the crop rises before attempting to sell (Solomon & Jones 2015). Because of the great fertility in the Iraq/Syrian region, the estimated potential revenue generated from selling crops, including wheat and barley, on the black market for a discount is near \$200 million a year (Swanson 2015). In other situations the Islamic State simply seizes crops and livestock from farmers with little warning, in some cases restricting the flow of seed and fertilizer (Fick 2014). In one case reported in *The Washington Post*, Islamic State militants took 10 percent of a family's wheat crop in Syria, suggesting the crop would be used to feed the poor (Sullivan 2015).

v. Sex Slavery Business

Besides kidnapping hostages, the Islamic State militants capture both women and girls for their lucrative human trafficking business. According to the religious claims of the Islamic State's followers, a "narrow and selective reading of the Quran" grants militants the privilege to engage in sexual activities, including rape, as worship to Allah (Callimachi 2015). The enslavement of women, furthermore, is justified by ISIS from Shariah law as the taking of war spoils from infidels, essentially a gift for their religious deeds (Abdelaziz 2014). Utilizing social media networks, the internet, and even local marketplaces, Islamic State fighters have been selling both women and children to customers both throughout ISIS territory and in countries abroad (Duhaime 2015). Human rights organizations have uncovered websites where young girls were being sold for only \$8 to \$12 each, outlining the extreme disregard for human life (Duhaime 2015).

The Yazidis, a Kurdish speaking people living in northern Iraq, and Christians have been the most impacted by the Islamic State's human trafficking. In 2014, almost 5,270 Yazidis women and girls were abducted by ISIS and pushed into the sex slave trade, and nearly 3,144 are still being held captive by the militants (Callimachi 2015). The process works as follows: after the women and girls are captured, they are sent to warehouses for inspection, marketing, and eventual transportation to provinces through Islamic State territory aboard a fleet of buses dedicated to the business (Callimachi 2015). Upon arrival to a specified province, Islamic State leaders are allowed the first opportunity to observe the slaves and purchase, with the remainder put up for sale to foreigners and ISIS fighters (Bolton 2015). Women and children under the Islamic State

thus become commodities bought and sold at will, discriminated and analyzed in a manner similar to animals. While more avenues of profit exist for the Islamic State, the methods as previously detailed above are the largest sources for economic activity.

V. Analyzing the Islamic State's Economy from an Austrian Perspective

While the economic actions of the Islamic State have prompted concern from foreign powers both in the Middle East and abroad, writers and thinkers from the Austrian School of Economics offer theories and evidence to suggest the actions of such radical militants is truly counterproductive to producing prosperity. Economic growth is a necessity for the Islamic State, allowing them to expand their operations and maintain their hold over the territory currently occupied. The methods currently utilized by the Islamic State have generated significant success already, but writers including John Tamny (2014) argue that Austrian economists including Ludwig Von Mises would not have expressed as much concern over ISIS as many bureaucrats and political scientists have. In this section, several areas of Austrian economic theory will be examined in regards to the economic policies and practices carried out by the Islamic State. The theory will provide a framework for uncovering the empirical evidence supporting the argument that the Islamic State's operations will not generate economic prosperity.

i. The Centralized and Interventionist Economy

While some businesses are allowed to continue operation in ISIS territory, the Islamic State assumes control over a majority of different industries and ensures rigorous measures on the businesses still operating. From agriculture to oil, the Islamic State

mandates certain individuals to oversee production of goods and services, managing a plethora of activities all the way up to selling the product. But the classic problem, as cited by Austrian economists, with a majority of services being provided by a centralized bureaucratic institution is the absence of profit and loss indicators. Shawn Ritenour (2010, 93), in his work *Foundations of Economics*, argues that the entrepreneur earns profit through the process of voluntary exchange in the market. Utilizing market prices and the preferences of consumers, the entrepreneur is able to allocate their resources in the most efficient manner in order to ensure the greatest profit while minimizing losses (Ritenour 2010, 93).

The state or centralized authority is incapable of utilizing economic calculation because of the fact that revenue is not generated through voluntary exchange, but rather through coercive measures including taxation. By coercing funds instead of earning revenue solely by the means of profit and loss, the central government has no way of efficiently determining the allocation of resources in light of demand since the process occurs outside the market (Rothbard 2009, 965). As a result, taxpayer money is malinvested into areas of production that would not have taken place under a pure private economy, meaning resources are also misdirected away from their optimal ends (Rothbard 2009, 965). Also, since the Islamic State has no way of determining consumer preferences outside the market, an Austrian economist would expect funds to be distributed disproportionately across different areas in favor of certain industries over others. Essentially, the Islamic State leaders are given the power to choose winners and

losers versus allowing the consumers in the market choose whatever organization best satisfies their preferences.

As Mises (2009, 713) describes in his work *Human Action*, in a society characterized by government intervention like the Islamic State's, while the bureaucratic leaders can paint the illusion that private property are "seemingly preserved" along with the presence of presence of prices and wages, there is only "shop managing" taking place instead of true entrepreneurship. On the surface, the shop managers conduct the typical actions seen under regular businesses, including the hiring and firing of employees and the purchasing and selling assets (Mises 2009, 713). But in reality, these managers are subject to the will of the government's offices, required to obey all decrees in regards to business action or face the consequences. As described by Mises (2009, 713-14), these governmental offices tell the "shop managers what and how to produce, at what prices and from whom to buy, at what prices and to whom to sell," assigning workers to different jobs and fixing wages. Such is the case with the Islamic State, where the leaders at the top of the bureaucratic structure dictate their financial and economic commands to the governors and councils overseeing various regions.

Under the description of interventionism described above, the Islamic State does not fall under the category of pure socialism, but rather under the classification of a hampered economy where market functions are maintained alongside the interference of government officials (Mises 2009, 714). By aiming at specific lines of production, the Islamic State is seeking to bring about their political and religious goals, using the threat of violence as a tool for ensuring its demands are met. Given that this is the present

economic system that the leaders of the Islamic State have decided to abide by, Austrian economic theory states that industries subsidized by government forces will redirect resources away from the efficient towards the people who are less efficient, ultimately lowering the standards of living for a population (Rothbard 2009, 942-43). Instead of looking to serve each other, members of such a society will increasingly look to develop connections with the governing authorities to personally benefit from the coercive measures utilized by the state (Rothbard 2009, 942). Such measures limit the productiveness of society, and their use by the Islamic State will hamper opportunities for prosperity and expanded operations.

ii. The Problem of Taxation, Price Controls, and Other Regulations

Examining the coercive measure of taxation more specifically, Austrian writers including Rothbard and Mises have made the case for why taxation is a form of binary intervention, where the intervening party forces another party to engaged in exchange against their will (Rothbard 2009, 878). According to Rothbard (2009, 914), when the government engages in the taxation of income, the producers begin to see their “production base” diminish while the non-producers see their incomes and resources “swell.” Furthermore, the higher the level of taxes imposed on the producers, the lower the marginal utility for work will be (Rothbard 2009, 914). Essentially, since the cost of production is significantly increased due to the government’s coercion, producers are more inclined to shift their time and energy away from work and put it towards either leisure or the pursuit of joining those who benefit from taxation (Rothbard 2009, 914). As a result, the level of saving and investment will decrease among individuals throughout

society, turning to consumption instead, as well as giving entrepreneurs less funds to work with to efficiently allocate their resources (Rothbard 2009, 914-15).

The Islamic State utilizes a variety of taxes, as noted in the previous section, to generate their income. Because of the wide-reaching and extensive tax structure put in place under the Islamic State, the Austrian perspective notes two consequences arising for the people living under the heavy taxation. First, as the income of the taxpayers grows smaller, fewer consumer goods can be purchased and thus the standard of living for the taxpayer falls (Ritenour 2010, 435). Furthermore, the tax consumers in the government spend the coerced money and distort demand within the economy towards areas that otherwise would not have received the revenue had it not been taxed (Ritenour 2010, 435-36). Second, the presence of a government budget, created through the taxation of citizens, “severs production from distribution,” essentially meaning that some parties receive the benefit of income without obtaining it through productive service (Ritenour 2010, 436-37).

Beyond the rigid tax structure, the Islamic State also enforces numerous rent and price controls on a variety of goods under their economy (Mohdin 2015). According to research conducted by Michael Weiss and Hassan Hassan (2016, 211), the Islamic State fixed the price of a liter of oil down from the going market price of \$11 to \$0.35 in an effort to decrease the profit margins on other oil producers in their territory. Fixing prices either above or below the market price will again result in the distortion of supply and demand. The case of an effective price ceiling, or a maximum legal price set below the market price for a particular good, will result in a shortage of the good in question,

resulting in rationing and a decrease quality in the good (Ritenour 2010, 413-15). On the other hand, an effective price floor, or the institution of a minimum legal price above the market price for a certain good, results in excess supply for the producers of the goods in question, leading to waste and an increased demand for cheaper substitutes (Ritenour 2010, 419-22).

The regulatory atmosphere, again, as mentioned earlier in the paper, is stifling to say the least under the Islamic State. Limits imposed by the government on business operation and personal action hamper opportunities and exchanges where citizens are able to satisfy their personal ends. The common theme of winners and losers continues as some restrictions force efficient producers out of the economy and prop-up the efforts of inefficient ones (Bylund 2016). Ultimately, it is the consumers that suffer the most under the burden of regulation, losing out on chances to obtain beneficial goods and opportunities for employment (Bylund 2016). If the leaders of the Islamic State continue to adhere to such stiff regulations to bring about their strategic ends, the population they hold authority over will face the rising threat of poverty beside the already present threat of militant violence. As a result, both citizens and businesses will make an effort to leave Islamic State territory to find better alternative areas for living, depriving ISIS of the necessary manpower and knowledge to engage in business.

As citizens migrate from the region controlled by Daesh, the division of labor progressively breaks down with the passing of time. Following the arguments of Rothbard (2008), the collapse of the division of labor serves as yet another an example of how potential economic growth is stifled under heavily regulated regimes like the Islamic

State. Under the free market, Austrian economic theory states that individuals will have a greater opportunity to develop their individual skills, engaging in a process known as specialization (Rothbard 2008). Simply put, greater specialization among individuals allows for a greater number of consumers and producers to have their preferences satisfied, thus allowing the free market to grow. But under the centralized economy of the Islamic State, Austrian theory notes that individuals are given less freedom to discover their unique potential, creating greater “uniformity” and “less diversity” among both producers and consumers (Rothbard 2008). Ultimately, such practices will result in a far smaller degree of individual specialization as well as some citizens being placed in roles where they do not have a comparative advantage, limiting the regime’s economic potential and hampering development.

iii. Poorly Defined and Enforced Property Rights

The Islamic State has also failed to create institutions which seek to properly define property rights and have instead pursued a political structure built on confiscation of property to serve the needs of the bureaucrats. This tendency to rely on public ownership over private ownership will only continue to push the young Islamic State economy down a road of economic inefficiencies and failure. As Mises (2009, 678-79) argued, the institution and protection of property rights, both for a person’s being, the previously unappropriated materials they bring into productive use, and the goods they acquire through voluntary exchange, is essential for market functionality. If individuals are unable or are unsure of their ability to bring the factors of production under their

control, then not only is the individual unable to serve their own needs, their opportunities to serve others diminish tremendously (Mises 2009, 679-80).

Since the Islamic State fails to provide the legal institutions necessary for defining and safeguarding property rights, entrepreneurs living in ISIS controlled territory are less likely to invest in expanding business operations (Hansen-Lewis and Shapiro 2015, 149). As Hayek (2005, 40-42) wrote, property rights give individuals the guarantee freedom in what they do with their belongings. But when the state instead chooses to dictate how people's property should be used, the future becomes even more uncertain for those attempting to forecast (Hansen-Lewis and Shapiro 2015, 149-50). Furthermore, corruption stemming from forces tied to the authoritarian state open more opportunities for exploitation. As a result of limited property rights in conjunction with heavy regulation, the individuals in society become more focused on attempting to gain favor among the bureaucrats in power or escaping the conditions altogether.

VI. Empirical Evidence for the Austrian Perspective

Reports and research conducted in the territory occupied by the Islamic State has already revealed numerous problems associated with the economic policies of the radical bureaucrats. Interventionist policies on the part of ISIS leaders have crippled the local economies based in both Syrian and Iraqi territory. Because the bureaucrats largely divert resources towards providing income for Islamic State forces and military equipment, the citizens living under ISIS control have experience shortages for essential goods. For example, fighters and citizens swearing allegiance to the Islamic State receive free

electricity, essential for individual life and modern businesses (Mullen 2015). With the recent bombings by foreign powers in Islamic State territory, the electric infrastructure has taken damage, resulting in decreased output for the population (Bajekal 2014).

As a result of the redistributive measures taken by the Islamic State, resources, including electricity, are diverted primarily to the elite while a majority of citizens face significant shortages. According to a report written by Kevin Sullivan (2015), some regions under Islamic State control experience electricity shortages so severe that families may only receive access during certain periods of the day for a limited amount of time. Airstrikes on extractive facilities have also limited the quantity of diesel necessary for agricultural machines, resulting in a shortage in both food for civilians (Bajekal 2014). Because Islamic State fighters receive free food through interventionist measures, as well as control the supply routes through the regions where crops are more plentiful, food prices become tremendously expensive for the citizens already losing significant income from taxation and extortion (Sullivan 2015). Regions where large numbers of Islamic State leaders and fighters dwell receive the most benefits from the redistribution while other regions receive little to no government support, demonstrating the disparity created under a centralized economy (Sullivan 2015).

The same situation of disparity can be found with respect to healthcare under the Islamic State, where members with strong ties to political leaders are granted access to the best medical resources available (Sullivan 2015). Creating a public system of healthcare has diverted resources away from many hospitals throughout Iraq and Syria, creating shortages in blood, anesthesia, and medical equipment on top of shortages in

electricity, fuel, and water (Sullivan 2015). While the best doctors are paid significantly to work for ISIS, others face diminished incomes and have resorted in many circumstances to escaping Islamic State territory to find better opportunities in other countries. The loss of medical professionals and skilled technicians due to the coercive measures implemented by the Islamic State has forced the radical leaders to adopt even more stringent policies in order to keep talented workers. One such policy requires doctors needing to travel outside Islamic State territory to provide up to five guarantees from friends and family that they will return, indicating the threat of brutal violence will be used if they do not (Sullivan 2015).

Only more problems continue to rise with centralized Islamic State control over the economic actions of its citizens. For instance, the problem of how to allocate incomes for bureaucratic officials and those loyal to the state becomes apparent given the government's inability to measure profit and loss. Because of this, the radical bureaucrats have faced tremendous difficulty in efficiently allocating resources for their supporters, leading to situations as seen in Al-Raqqa where the salaries of ISIS fighters were cut but nearly 50 percent for the purpose of increasing the salaries of foreign fighters (Hartogs 2016). Again, as Austrian theory previously noted, the centralized economy creates a system proliferated by winners and losers. As a result of some parties losing income and goods promised by the Islamic State, reports of hundreds of fighters defecting throughout ISIS controlled territory is becoming a common phenomenon (Burman 2015).

While the Islamic State has been successful in utilizing the resources and facilities abandoned in both Iraq and Syria, Jacob Shapiro (2016) argues several points for why

ISIS will not be able to sustain their economic success. One, the statistics and numbers received in reports from the region are highly suspect and often contradictory to the actual data observed. For example, luminosity data provided by the NOAA and NECI measured the intensity methane gas flares coming from oil facilities in ISIS controlled territory to determine whether or not the facilities were being utilized to their pre-ISIS occupation levels (Hansen-Lewis & Shapiro 2015, 144-45). The data revealed the Islamic State's "productive base" dropped rapidly in comparison to pre-occupation totals when Daesh took over, and as time went on from January 2014, the intensity of site flairs continued to drop, indicating the oil facilities were operating at only a fraction of normal operation (Hansen-Lewis & Shapiro 2015, 144-45). Shapiro (2015) cites three reasons for the lower output levels: (1) continued airstrikes targeting the oil and natural gas infrastructure make work dangerous as well as difficult, (2) equipment necessary for maintenance and repairs is often unattainable and/or expensive, and (3) the number of experienced/specialized technical personnel needed to efficiently run the plants are limited, continually shrinking in number despite the lucrative salaries offered to keep them (Hansen-Lewis & Shapiro, 2015, 143-44).

Because the numbers used to estimate the production totals for ISIS are often based on facilities operating at full potential with the necessary personnel, Shapiro (2016) argues the projected revenues for the Islamic State grossly overvalue the group's actual capabilities considering the deterioration of the division of labor mentioned previously. The reports coming out of the region do not take into account the productive capabilities of each oil site individually, but rather estimate the Islamic State's overall production by

observing only one or two sites (Shatz & Shapiro 2016). When the Islamic State sells oil, traders sell their product at steep discounts below the going market price in order to generate greater demand for their products (Hansen-Lewis & Shapiro 2015, 143-44). Furthermore, the Islamic State relies heavily on labor intensive activities versus capital intensive activities, including the siphoning of fuel through hoses run under territorial borders, making the process more inefficient and time consuming (Smith 2015). Shapiro (2015, 144) argues “lack of access to conventional oil production and marketing opportunities will prevent Daesh from earning substantial oil revenue over the long-run.”

Other methods of Islamic State financing, including ransom and taxation, are also seen as inefficient long-term options according to Shapiro (2015). While ransom payments can generate nearly \$20 million a year, human trafficking is typically used as “payment in kind” for ISIS fighters and does not generate substantial revenue potential in comparison to extractive industries (Hansen-Lewis & Shapiro 2015, 145). Beyond human trafficking, the Islamic State does not engage in many for-profit business ventures, limiting potential to earn revenue and develop markets (Hansen-Lewis & Shapiro 2015, 145). Instead, the Islamic State continues to look to extortion and taxation to generate large shares of revenue, but Shapiro (2015, 145) notes how such tactics reduce the incentive for citizens to save and invest as well as creating “regulatory uncertainty” given the inconsistency of taxes across different provinces. The Islamic State’s strict belief in credit and insurance markets being immoral, furthermore, hinders investment necessary to jumpstart businesses and projects, limiting development and societal growth (Hansen-Lewis & Shapiro 2015, 149).

To give a sense of how much income is directed away from citizens living under ISIS control, reports from Deir el Zour in Syria shed more light on the costs of regular goods and services. Taking the average Syrian GDP per capita of about \$1,700, in terms of healthcare, mothers looking to receive a C-section are required to pay \$80 while regular births can run as high as \$55 or \$60, not including the cost of other medical necessities (Masi 2015). In the same region, the price of foodstuffs increased nearly 1000 percent according to reports by Joanna Paraszczuk (2015), leading to even more hardships for the large numbers of citizens left unemployed due to the government crowding out private business. Fines reported out of Mosul, Iraq were as high as \$10 to \$20 for actions as petty as forgetting to put garbage out along with a required purchase of ISIS rubbish removal services by businesses and households (Masi 2015). The situation has generated increased demand for public jobs considering the private alternatives are unable to provide enough pay due to regulations, taxation, and continued extortion on the part of Islamic State militants (Paraszczuk 2015).

The Islamic State, furthermore, does not invest revenue earned into developing new military technology or production techniques, limiting opportunities to lower costs and develop more efficient means of violence to combat their enemies (Faria 2014, 285). Joao Ricardo Faria (2014, 293-94) notes how terror groups like the Islamic State more often than not fail to develop advanced “non-conventional weapons,” choosing instead to rely on existing technology while modifying the methods that have been carried down by previous fighters. Furthermore, while the Islamic State has generated a tremendous amount of revenue, the ability of ISIS leaders to expand their war machine is

significantly limited compared to surrounding nations. To illustrate the economic power of ISIS in comparison to its enemies, Shapiro (2015) estimated the Islamic State to have a GDP (2014 USD) of \$30 billion with a defense budget of \$900 million to \$3 billion. But even the smallest neighboring countries, with only comparatively better economies, all have larger defense budgets and the ability to outspend ISIS if needed. Examples include Iraq (\$9.5 billion), Turkey (\$20 billion), and Saudi Arabia (\$80 billion) (Hansen-Lewis & Shapiro 2015, 148).

Finally, in terms of foreign relations and conflicts, the Islamic State is currently engaged in fighting a costly three-front war against (1) the Syrians (supported by the Russian government) in the west, (2) the Kurds in the north, and (3) the Iraqis in the east (Shatz & Shapiro 2016). The ever-changing nature of the conflict, including the possibility of increased intervention from even larger military powers, the Islamic State is being squeezed of resources. Centralizing economic activity has only created gross misallocations of resources, and as Austrian theory previous stated, the misallocations will only continue until private enterprise is given the freedom to operate. With infrastructure being systematically targeted, a shrinking population being extracted to the point of poverty, and the costs associated with retaining both territory and fighters, the Islamic State is losing ground in terms of maintaining a consistent base for revenue (Hansen-Lewis & Shapiro 2015, 148-49).

VII. Conclusion

Despite the economic evidence indicating the unsustainability of the Islamic State, the pseudo-state should not be immediately dismissed. The economy organized under ISIS governance is significantly effective in extracting both property and money from the citizens within Daesh territory. Utilizing a radical brand of Quranic interpretation, the Islamic State is quick to justify actions seen as barbaric as commands from an all-powerful deity. Powerful propaganda and the promise of spoils have allowed ISIS to recruit fighters, develop an effective military force as well as a rigid bureaucracy, and seize large territory in both Iraq and Syria. The leaders of the Islamic State are determined to solidify the legitimacy of their new caliphate, thus the jihadist pseudo-state will continue to operate in an authoritarian manner to ensure resources are directed towards ends guaranteeing the expansion of the territory.

But while economic strategies including diversification and innovation allow the Islamic State to experience a relative degree of economic success, Austrian economic theory and the empirical research indicates ISIS will need to develop less coercive institutions if the leaders wish to experience economic prosperity in the future. Taxation and extortion create an environment of uncertainty for citizens in the region, and limited access to electricity, water, and healthcare severely limits the potential of the population to be productive well into the future (Shatz & Shapiro 2016). But unless the Islamic State decides to deviate away from their strict interpretation of the Muslim holy books, an unlikely scenario given the previous research, the government will continue to invest in the military while neglecting the essential needs of the people. Even if the Islamic State

begins receiving significant foreign financial support, the policies of the Daesh economy place ISIS on a road to economic regression and lower standards of living.

As John Tamny (2014) notes, referencing Mises' work *Socialism*, the under-developed Islamic State arose from one of the least economically productive areas on the globe and has yet to “create even one consumer good that is desired by global consumers.” The very fact that the Islamic State is financed largely by methods of theft and coercion immediately limits the potential growth of the pseudo-state, especially in comparison to mostly-free nations including the United States, which far outpaces most developed nations in terms of economic growth. While the United States can by no means be called a free market, the American government does not comparatively engage in as much business extortion and personal regulation as Daesh, and the lack of economic prosperity reveals the fruits of such labor (Tamny 2014). Just as “the more highly developed societies attain greater natural wealth than the less highly developed,” so too are these nations more capable of defending themselves against the less developed (Tamny 2014). Unless the Islamic State radically alters their economic policies to ensure greater freedom, property protection, and a focus on the satisfying the consumer, the pseudo-state will not see its capabilities expand and instead face continued regression.

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