UNIT- 4: THEORY OF DISTRIBUTION: marginal productivity theory of distribution, **rent:** concept of differential rent, scarcity rent, economic rent, contract rent, quasi rent and pure rent. Modern theory of rent. **Wages**: money wages and real wages, factors determining real wages, **theories of wages**: wages fund theory, subsistence theory, residual claimant theory, **theories of profit**: risk theory of profit, uncertainty bearing theory of profit and innovation theory of profit.

OUTCOMES:

- Theories of distribution attempt to explain how income is divided among the various factors of production, including land, labor, and capital.
- The outcomes of theories of rent attempt to explain the existence of economic rent and how it is distributed among various factors of production.
- The outcomes of theories of profit attempt to explain the sources of profit in the economy and how it is distributed among various actors.

INTRODUCTION:

- The theory of distribution is a branch of mathematics that deals with the study of functions and their properties. It is concerned with the distribution of various mathematical objects such as functions, sequences, and measures. The theory of distribution, also known as distribution theory or generalized functions, provides a framework for dealing with objects that are not functions in the classical sense but have properties that are useful in various areas of mathematics and physics.
- The theory of distribution was introduced by the French mathematician Laurent Schwartz in the 1940s.
- In summary, the theory of distribution is an important branch of mathematics that provides a powerful tool for dealing with a wide range of mathematical and physical problems.

The Theory Of Distribution:

- This article talks about the theory of distribution which takes into account the factors of production to determine the prices of their services.
- It is also known as the theory of factor pricing.

There are two aspects of this theory:-

1. **Personal Distribution:**- Income distribution among individuals is known as personal distribution. The theory of personal distribution studies how personal income of individuals is determined and what causes the inequalities in their income.

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2. **Functional Distribution**: - This refers to how income is to be distributed among various factors of production. The theory of functional distribution studies how the relative prices of factors of production are determined. That is the reason why it has also been termed as the theory of factor prices.

Theory of Distribution:

- Theory of distribution is a specific matter of study of the theory of price. As the prices of products can be described with the help of the interaction of the demand and supply forces, likewise its distribution can also be described by the determination of prices of the factors which are also explained with interaction of their demand and supply forces
- But the important point to keep in mind is that In the theory of distribution, we depict the prices of the services rendered by the factors of production and not of the factors of production
- **For example**, in the market of the factors of production, it is not the labour which is being bought or sold, but the services of labour. Similarly, land, capital, and entrepreneur goods are not being evaluated, but the services of such land, capital, and entrepreneur goods
- Thus, rent is not the price of land but the price of services or use of land & wages is the price of the service of Labour & interest is the price of the use of capital, and profit is the reward of entrepreneur’s services
- Hence we can observe from the above mentioned points that the need for the theory of distribution (or the theory of factor pricing) arose due to the shortcomings in the theory of product pricing.

Classical Theory of Distribution:

According to the classical theory of distribution, the prices of the services of factors of production are determined by the supply and demand forces of such services.

- **Rent**:- As per the theory of rent propounded by Ricardo, rent is that portion of the produce of earth which is paid to the landlord for the original and indestructible powers of soil. He viewed rent as the differential surplus that some plots of land earn over and above the other
- **Wages**:- As per the theory of wages propounded by economist **T. R. Mealthis** and **J. S. Mill**, labour is sold in the market and its value is determined like the other

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commodities**. According to J. S. Mill**, the wage rate depends on the ratio of workforce to the amount of working capital

- **Interest**:- As per the theory of interest propounded by economist **J. S. Mill**, the interest is determined by the interaction of demand and supply forces of capital. The demand for capital is made for the purpose of investment and thus the demand for capital varies inversely with the rate of interest.
- **Profit:-** As per this theory of profit, the value of a commodity is determined on the basis of the services of labour used in it.

Marginal Productivity Theory Of Distribution:

Marginal productivity theory was given by German Economist Von Thunen in 1826. According to this theory, prices of the factors of production depend on its productivity and it is determined by the marginal productivity of the factor concerned. In other words, under perfect competition, every factor of production gets remuneration equal to its marginal productivity.

- **Marginal Productivity**:- It refers to the additional unit of product generated due to the employment of an additional unit of a factor of production.

- **Assumptions:-** Assumptions of this theory are as follows:

  1. Perfect market competition in product market
  2. Variable proportion type production function (i.e. output can be increased by changing the factor ratio)
  3. Divisible factor
  4. Full employment
  5. Constant technology
  6. Factors can be substituted
  7. One variable input and the other is fixed

Rent:

- In simple words, 'rent' is used as a part of the produce which is paid to the owner of land for the use of his goods and services.
- In economics, rent has been differently defined from time to time.
- **"Rent is the price paid for the use of land." –Prof. Carver.**
- "Economic Rent may be defined as any payment to a factor of production which is in excess of the minimum amount necessary to keep the factor in its present occupation." – **Boulding**

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- "Rent is the difference between actual payment to a factor and its supply price or transfer earnings." – **Hibdon**

Types of Rent:

In microeconomics, there are several types of rent, including:

1. **Economic Rent**: This refers to the payment made for a factor of production (such as land or labour) that is in limited supply and cannot be easily replicated. Economic rent is a surplus payment made by consumers for a particular factor of production.
2. **Transfer Rent**: Transfer rent is the payment made for the use of a factor of production that is owned by someone else. For example, if a tenant pays rent to a landlord for the use of a house, this is transfer rent.
3. **Quasi Rent**: Quasi rent refers to the surplus that is earned by a factor of production that has a fixed supply in the short term but can be increased in the long term. For example, if a company invests in a new machine that has a fixed supply in the short term, but can be replicated in the long term, the surplus it earns is quasi rent.
4. **Monopoly Rent**: Monopoly rent is the payment made for the use of a factor of production that is controlled by a monopoly. For example, a monopolist might charge a high price for a product because they have control over the supply of the product.
5. **Differential rent** is a concept in economics that refers to the difference in the rent paid for land or other natural resources that have different levels of productivity or quality. It is the extra payment made for the use of land that has higher productivity or is more advantageous in terms of location, fertility, or other factors that make it more profitable to use.

   Differential rent is a crucial concept in agricultural economics, where it is used to explain the rent paid for farmland. In this context, differential rent arises because different plots of land have different levels of productivity due to differences in soil fertility, topography, access to water, and other factors.

6. **Scarcity rent** is a type of economic rent that arises due to the scarcity of a particular resource. It is the extra payment made for the use of a resource that is in limited supply relative to the demand for it. Scarcity rent is a form of economic profit that arises when the demand for a resource exceeds its supply, creating a situation where users of the resource must compete to obtain it.

   The concept of scarcity rent is important in economics because it explains why some resources command higher prices than others, even though their production costs may be similar. Scarcity rent also has implications for

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public policy, as it highlights the importance of managing natural resources and limiting access to certain resources in order to promote their efficient use.

7. **Contract rent** is typically negotiated between the landlord and the tenant based on a number of factors, including the location and condition of the property, the length of the lease agreement, the level of demand for rental properties in the area, and the financial situation of the tenant.

8. **Pure rent** is a term used in economics to describe a type of economic rent that arises when a factor of production, such as land or natural resources, generates income without any effort or investment by the owner. Pure rent is sometimes also referred to as "unearned rent" or "economic rent.

   For example, pure rent can arise when a landowner collects rent from a tenant for the use of land that is especially fertile, giving the tenant a higher yield than would be possible on less fertile land. In this case, the landowner receives pure rent simply for owning the land, and without any effort or investment on their part to make it more productive.

Overall, rents in microeconomics are payments made for the use of a factor of production and are determined by the supply and demand for that factor.

Explain Modern Theory of Rent

The modern theory of rent is an amplified and modified form of Ricardian theory. This theory was explained by Mrs Robinson Marshall, William Stanley Jevons, etc. According to Modern Economists, rent is a surplus that is not related to land alone, it can be part of the income of labour, capital and entrepreneur also.

According to Modern Economists, “Rent is the difference between actual earning and transfer earning of a factor.”
Rent = Actual Earning – Transfer Earning

Actual Earning: It is that earning which is a factor gets in its present occupation.

Transfer Earning: Transfer earning of a factor is that part of its income which it could get in its next best alternative use. Thus, it is the earning which must be paid to a factor to keep it in its present use.

Why Does Rent Arise?

According to modern theory, the main causes of the emergence of rent are as follows:

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1. **Scarcity of Factor:** Rent arises due to the scarcity of a factor of production in relation to its demand.
2. **Specificity of a factor of production:** According to Prof. Wiser – there are two types of factors of production:

- **Specific factors –** Specific factors are those which have no alternative use. The specificity of factors is the main cause of the emergence of rent.
- **Non-specific factors –** Non-specific factors are those which have alternative use

Determination of Rent

According to the modern theory of rent, rent is determined where the demand for factor equals the supply of factor. Modern economists define rent in two ways:

1. It is a payment for the use of land only.
2. It is a surplus or difference between actual earning and transfers earning.

1. Determination of Rent of Land:

Rent is the payment for the use of land. According to the modern economist, rent arises due to scarcity of land. It is determined by the demand and the supply of land.

- Demand for Land
- Supply of Land

i. Demand for Land

The demand for land is derived from the demand. It means that demand for land depends upon agricultural products, e.g., if the population increases, the demand for food will increase, resulting in increased demand for land and vice-versa. Demand for land is influenced by its marginal productivity. That is why the demand curves DD as shown in fig. slopes downward from left to right.

ii. Supply of Land

The supply of land is fixed for an economy. It is perfectly inelastic; it means its supply is independent of what it earns. Rent is determined at an appointment where the demand curve of land and supply curve of land intersects each other

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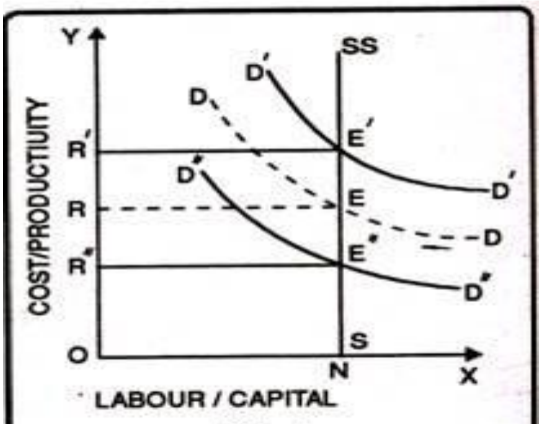

Fig. 5.

In the figure, DD is the demand curve and SS is the supply curve. E is the point of equilibrium. In this position, OR is rent. If the demand for land increases, the demand curve shifts upwards and becomes D1D1, then the new equilibrium will be E1 and therefore, rent will rise to OR1. If demand decreases DD to D2D2, then the new equilibrium point will be E2 and at this, rent will fall to OR2. Thus, rent is like the price of other goods and is determined by the equilibrium between demands for the supply of land. Rent is paid because of the scarcity of land.

2. Rent as the difference between Actual Earning and Transfer Earning:

According to modern theory, rent arises because there is a difference between actual earning and transfer earning. How much rent a factor of production will get, depending on its elasticity of supply? Supply of a factor can be of three types:

- **Perfectly elastic supply**
- **Perfectly inelastic supply**
- **Less elastic supply**

i. Rent When the Supply of a Factor is Perfectly Elastic

The supply of a factor is perfectly elastic when at the existing rate; supply of the factor can be increased up to any extent. Such a factor is not scary. The actual earning of this factor is equal to transfer earning. Thus, there is no difference between actual earning and transfer earning so rent is zero as shown in the below figure.

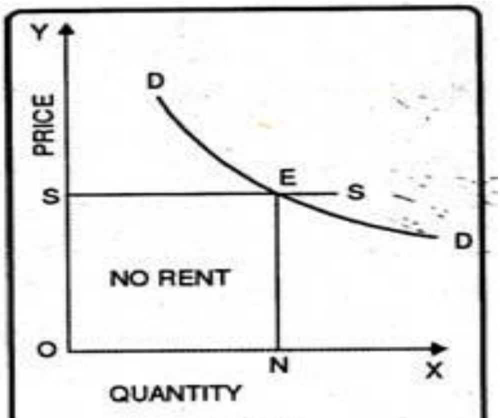

Fig. 6.

In this figure, units of factors are shown on OX-axis and price is on OY-axis. E is the point of equilibrium and therefore, at OP price, ON units of factor are employed. When demand for factor increases to D1D1, then the new equilibrium point is E1. This equilibrium point shows that when demand for factor increases, its supply also increases. Due to this, the price factor remains the same. In this case, nor rent arises.

Actual Earning = OPE1N1
Transfer Earning = OPE1N1
Actual Earning = Transfer Earning

Rent = OPE1N1 – OPE1N1 = Zero

ii. <u>Rent When the Supply of Factor is Perfectly Inelastic</u>

Supply of a factor of perfectly inelastic when increases or decreases in its demand does not affect its supply. In this case, transfer earning if the factor is zero and whatever the actual earning it gets is called rent as shown in the figure below.

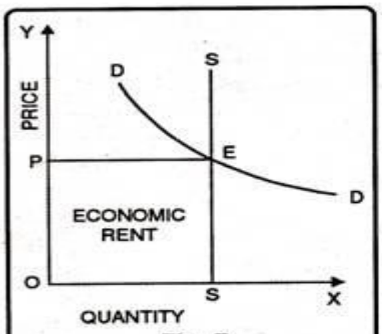

Fig. 7.

Rent = Actual Earning (Since Transfer Earning is zero)

In this figure, SS is the supply curve and DD is the demand curve of the land. E is the point of equilibrium. At this point, the actual earning of land is OP and transfer earning is zero and rent is OPES. When demand for land increases to D1D1, the actual earning also increase OP to OP1 and transfer earning zero. Thus, the entire earning of this factor is called rent.

iii. Rent When the Supply of Factor is Less Elastic

Supply of a factor is less elastic when increases in its demand id followed by less increase in its supply. Therefore, the actual earning of the factor exceeds its transfer earning which is called rent. It is shown with the help of this figure.

In this figure, SS is a less elastic supply curve and DD is the demand curve. E is the point of equilibrium. At this point, the ON factor is employed at OP price. SS supply curve of factor indicates that the minimum supply price or transfer earning is OS while its actual earning is OP. hence, rent will be PES.

WAGES

- "A wage may be defined as the sum of money paid under contract by an employer to worker for services rendered." -**Benham**
- "Wages is the payment to labour for its assistance to production." -**A.H. Hansen**
- 'Wage rate is the price paid for the use of labour." -**Mc Connell**
- "A wage is price, it is the price paid by the employer to the worker on account of labour performed." -**J.R. Turner**

Types of Wages:

In real practice, wages are of many types as follows:

1. Piece Wages*:*

Piece wages are the wages paid according to the work done by the worker. To calculate the piece wages, the number of units produced by the worker are taken into consideration.

2. Time Wages*:*

If the labourer is paid for his services according to time, it is called as time wages. For example, if the labour is paid Rs. 35 per day, it will be termed as time wage.

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3. Cash Wages*:* Cash wages refer to the wages paid to the labour in terms of money. The salary paid to a worker is an instance of cash wages.

4. Wages in Kind*:*

When the labourer is paid in terms of goods rather than cash, is called the wage in kind. These types of wages are popular in rural areas.

5. Contract Wages*:*

Under this type, the wages are fixed in the beginning for complete work. For instance, if a contractor is told that he will be paid Rs. 25,000 for the construction of building, it will be termed as contract wages.

Concepts of Wages:

The following are the two main concepts of wages:

A. Nominal Wage:
B. Real Wage:

A. Money Wages or Nominal Wages*:*

The total amount of money received by the labourer in the process of production is called the money wages or nominal wages.

B. Real Wages*:*

Real wages mean translation of money wages into real terms or in terms of commodities and services that money can buy. They refer to the advantages of worker's occupation, i.e. the amount of the necessaries, comforts and luxuries of life which the worker can command in return for his services.

An example will make the things clear. Suppose 'A' receives Rs. 500 p.m. as money wages during the year. Suppose also that midway through the year the prices of commodities and services, that the worker buys, go up, on the average, by 50%.

It means that though the money wages remain the same, the real wages (consumption basket in terms of commodities and services) are reduced by 50%. Real wages also include extra supplementary benefits along with the money wages.

Distinction between Real and Money Wages:

Adam Smith has distinguished the money wages and real wages on the following basis:

1. Relation with Price:

Keeping all other things constant, there exists inverse relation between real wages and price i.e. with the increase in price level real wages tend to decline and vice-versa.

2. Money and Real Wages:

Ceterus paribus, an increase in money wages will lead to an increase in real wages. It is due to the reason that with the increase in money wages, a labourer can purchase more goods and services than before.

3. Basic Difference:

According to Adam Smith, money wages are paid in terms of the quantity of money whereas real w ages are paid in terms of necessaries of life. Therefore money w ages are expressed in terms of money and that of real wages in terms of goods and services.

THERE ARE 7 THEORIES OF WAGES

- Wages Fund theory
- Subsistence theory
- The surplus value theory of wages
- Residual claimant theory
- Marginal productivity theory
- The bargaining theory of wages
- Behavioural theory of wages

Wages Fund Theory:

- This theory was developed by **Adam Smith (1723-1790).** His theory was based on the basic assumption that workers are paid wages out of a pre-determined fund of wealth.
- This fund, he called, wages fund created as a result of savings. According to Adam Smith, the demand for labour and rate of wages depend on the size of the wages fund.
- According to this theory, therefore, trade unions cannot raise wages for the labour class as a whole.
- The efforts of trade unions to raise wages are futile. If they succeeded in raising wages in one trade, it can only be at the expense of another, since the wage fund is fixed and the trade unions have no control over population

Subsistence Theory:

- This theory was propounded by David Ricardo (1772-1823). According to this theory, “The labourers are paid to enable them to subsist and perpetuate the race without increase or diminution”. This payment is also called as „subsistence wages‟.
- If workers are paid less than subsistence wages, the number of workers will decrease as a result of starvation death; malnutrition, disease etc. and many would not marry.
- Then, wage rates would again go up to subsistence level. Since wage rate tends to be at, subsistence level at all cases, that is why this theory is also known as „Iron Law of Wages‟.
- It assumes that when they were paid more than the subsistence level, they might indulge in enjoyment and consequently their numbers would increase, and this would result in a low rate of wages.

Residual Claimant Theory:

- This theory owes its development to Francis A. Walker (1840- 1897). According to Walker, there are four factors of production or business activity, viz., land, labour, capital and entrepreneurship.
- He views that once all other three factors are rewarded what remains left is paid as wages to workers. Thus, according to this theory, worker is the residual claimant.

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- This theory admits the possibility of increase in wages through greater efficiency of employees. In this sense, it is an optimistic theory; the subsistence theory and wages fund theory were pessimistic theories.
- **According to Walker**, wages are the residue left over, after the other factors of production have been paid.

Theories of Profit:

1. Risk-Bearing Theory of Profit
2. **Uncertainty-Bearing Theory of Profit**
3. Rent Theory of Profit
4. Innovation Theory of Profit
5. Dynamic Theory of Profit
6. Monopoly Power Theory of Profit
7. Labour Exploitation Theory of Profit
8. Marginal Productivity Theory of Profit

1. Risk-Bearing Theory of Profit:

The main proponent of this theory is Prof. Hawley. According to Hawley, one of the major functions of an entrepreneur is to bear risk that is associated first with the setting up of the business and then with the management of the business.

The risks in a business are of two types:

(i) Risk involved in the selection of the field of business; and
(ii) Risk associated with the management of the business.

After investing capital in a particular business, the entrepreneur has to wait for a long time before he can know if his selection of the field of business has been appropriate—this long wait is a form of risk-bearing.
Again, while managing the business, the entrepreneur has to bear all the risks arising out of unexpected changes in the demand and supply for the product.

There may be sudden changes in the demand for a good owing to changes in the tastes, habits and incomes of the buyers, changes in the availability and prices of the substitute products, etc.

Also, there may be unexpected changes in the supply of the good owing to changes in the availability of the factors of production and changes in production techniques, etc.

Therefore, that the entrepreneur has to bear the risks associated with the unexpected changes in demand and supply of the product and also the risks associated with the consequent changes in the price of the product, total revenue and profit of the firm. The greater the ability of the entrepreneur to bear all these risks, the higher would be his level of profit. This is the main contention of the risk-bearing theory.

Critical Evaluation of the Theory:

The arguments that may be advanced in favour of the theory:

(i) The theory attracts our attention to the fact that one of the main functions of the entrepreneurs is to bear the risks.
(ii) The theory focuses also on the fact that a very few persons come forward to play the role of entrepreneurs because here they would have to bear the risks. That is why the supply of entrepreneurial services is very limited.

Arguments Against the Theory:

Let us now come to the arguments against the theory. These are:

(i) Risk-bearing is not the only function of an entrepreneur who has to perform many vital functions. For example, the entrepreneur has to innovate at regular intervals new products, new markets and improved methods of production and business.

He may augment his revenue and reduce his expenditures through such innovations and, consequently, his profit level would go up. Therefore, profit may also be considered as a reward for effecting innovations. Again, the entrepreneurs, all of them, have not the same ability to face risks and to perform other activities.

Therefore, owing to differences in such ability, some entrepreneurs may earn rent of ability. Similarly, if the entrepreneur is able to establish a monopolistic dominance in the market, then also his income, i.e., profit, would include the added income acquired through monopoly power. Therefore, profit cannot be explained only as a reward for risk-bearing.

(ii) The entrepreneur has surely to bear risks and his profit, at least some part of it, may be considered to be a reward for risk-bearing. However, risk is a subjective concept. We cannot measure risk in an objective, cardinal manner. That is why it is not possible to establish a functional relationship between risk and profit.

(iii) The exponents of the risk-bearing theory of profit did not distinguish between insurable risk and non-insurable risk. But if we are to obtain a good estimate of the amount of risk- bearing, it is essential to remember this distinction. For, the entrepreneurs actually do not bear the burden of insurable risks—it is borne by the insurance companies.

Therefore, they cannot be considered as risks. According to Prof. Knight, the entrepreneurs bear the burden of non-insurable risks and he has called these non-insurable risks by the name of uncertainty. The entrepreneur should obtain profit as a reward for bearing this uncertainity.

2. Uncertainty-Bearing Theory of Profit:

Prof. F. H. Knight (1885-1973) has developed the uncertainty-bearing theory of profit. He says that we may distinguish between insurable risks and non-insurable risks. This distinction is important. For, the entrepreneurs actually do not bear the burden of insurable risks—it is borne by the insurance companies. Therefore, they cannot be considered as risks for the entrepreneurs.

For example, we know from experience that factory premises are exposed to the risk of fire. We also know why there may be fire in a factory premise, and so, we may adopt necessary measures for prevention of fire.

In spite of all this, there remains the risk of fire, and, once the insurance companies agree to bear this risk, it no longer remains a risk. In other words, according to Knight, insurable risks should not be considered as risks and there is no question of the entrepreneurs bearing this risk.

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However, the entrepreneurs bear the burden of non-insurable risks for there is no insurance company to bear these risks on their behalf. Prof. Knight has called these risks the uncertainties.

He tells us that the entrepreneur should get profit as a reward for bearing the uncertainties of the business world. The more prudently an entrepreneur bears the uncertainties, the more should be the amount of profit to reward him with.

Critical Evaluation of the Theory:

The following arguments are advanced in favour of the uncertainty-bearing theory of profit:

(i) The theory attracts our attention to the fact that not all types of risk are to be borne by the entrepreneur. He actually bears the non-insurable risks. The insurable risks are taken care of by the insurance agencies.

(ii) The theory tells us that, like all other productive services, uncertainty-bearing is also a productive service. The entrepreneur supplies this productive service and profit is the price of this service.

(iii) Since, in general, people are averse to uncertainty-bearing, the supply of entrepreneurs in the real world is very small. This impression is also obtained from the theory.

Arguments Against the Theory:

The following arguments are advanced against the theory:

(i) Uncertainty-bearing is not the only function of an entrepreneur. The innovation of new products, new markets or new production and business techniques are also among the main tasks of an entrepreneur.

Therefore, along with the function of uncertainty-bearing, that of innovation may also be the source of profit. Again, the rent of ability and monopolistic dominance may also be the sources of profit. Similarly, a firm may earn profit owing to its goodwill in the market. Therefore, we cannot say that profit arises only as a reward for uncertainty-bearing.

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(ii) Uncertainty is something subjective—it has no objective, cardinal measure. In the case of organisation and management of a particular business, different entrepreneurs may have different perceptions of the degree of uncertainty involved. Therefore, it is almost impossible to build up a functional relation between uncertainty and profit.

3. Innovation Theory of Profit:

The innovation theory of profit was developed by **Prof. Joseph A. Schumpeter (1883-1950).** According to **Schumpeter**, the main function of an entrepreneur is to innovate. Here we have to remember first the distinction which Schumpeter had made between invention and innovation.

Invention is the discovery of a law of nature by a scientist. On the other hand, if an entrepreneur manufactures a new product or introduces a new production technique by using the newly discovered law of nature, and thereby makes the commercial use of the invention possible, then this is called innovation.

For example, the scientists have discovered or invented the laws of science that are behind the manufacture of the goods like electric lights or fans, radio sets, television sets, refrigerators and such other goods. But the entrepreneurs have innovated these goods. Innovation is the commercial use of the laws of science that have been discovered by the scientists.

Schumpeter has said that if the entrepreneur can innovate new techniques of production and sale, if he can innovate a new product or a new model of an old product and if he can find new markets for selling the product, then Only, he will be able to play the role of a pioneer in the business world and increase the amount of profit. We may call this increase in profit the innovation-induced profit.

Criticisms of the Theory:

Schumpeter's innovation theory of profit has explained nicely how an entrepreneur may increase the amount of profit by means of innovations. But this theory cannot fully explain why profit arises or why the entrepreneurs should earn profit.

For example, we know that an entrepreneur should obtain profit as a reward for bearing risk or uncertainty, for his ability to establish monopolistic dominance, and for many other reasons. But Schumpeter did not consider these factors that might work behind the emergence of profit.

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1. According to the marginal productivity theory of distribution, how are factors of production rewarded?
a) Based on their total productivity
b) Based on their average productivity
c) Based on their marginal productivity
d) Equally regardless of productivity

Answer: c) Based on their marginal productivity

2. Which of the following statements best describes the marginal productivity theory of distribution?
a) Factors of production are paid according to their total productivity
b) Factors of production are paid according to their average productivity
c) Factors of production are paid according to the price level in the market
d) Factors of production are paid according to their contribution to the last unit of output

Answer: d) Factors of production are paid according to their contribution to the last unit of output

3. n the marginal productivity theory of distribution, what happens to factor payments as the marginal product of a factor increases?
a) Factor payments decrease
b) Factor payments remain constant
c) Factor payments increase
d) Factor payments fluctuate unpredictably

Answer: c) Factor payments increase

4. According to the marginal productivity theory, what happens to factor payments when there is excess supply of a factor?
a) Factor payments increase
b) Factor payments decrease
c) Factor payments remain constant
d) Factor payments become unpredictable

Answer: b) Factor payments decrease

5.In the marginal productivity theory, what is the relationship between the price of a product and the marginal productivity of the factors used in its production?
a) Inverse relationship

b) Direct relationship
c) No relationship
d) Indirect relationship

Answer: b) Direct relationship

6. Differential rent refers to:
a) The difference between economic rent and contract rent
b) The difference in rent paid for different grades of land
c) The rent paid for scarce resources
d) The rent paid based on a contractual agreement

Answer: b) The difference in rent paid for different grades of land

7. Scarcity rent arises when:
a) Resources are abundant
b) Resources are evenly distributed
c) Resources are scarce
d) Resources are not utilized efficiently

Answer: c) Resources are scarce

8. Economic rent is defined as:
a) Rent paid for the use of land and other natural resources
b) Rent paid for the use of capital equipment
c) Rent paid for the use of labor
d) Rent paid for the use of buildings and infrastructure

Answer: a) Rent paid for the use of land and other natural resources

9. Contract rent is determined by:
a) Supply and demand in the market
b) Legal contracts between parties
c) Government regulations
d) Negotiation between landlord and tenant

Answer: d) Negotiation between landlord and tenant

10. Quasi rent refers to:
a) Rent paid for the use of land
b) Temporary surplus earnings of a factor of production
c) Rent paid for the use of capital
d) Rent paid for the use of labor

Answer: b) Temporary surplus earnings of a factor of production

11. Pure rent is:
a) The same as economic rent
b) The same as contract rent
c) Rent paid for the use of buildings and infrastructure
d) Rent earned solely due to ownership of land or other natural resources

Answer: d) Rent earned solely due to ownership of land or other natural resources

12. Which of the following statements best describes the modern theory of rent?
a) Rent is determined solely by the marginal productivity of land
b) Rent is determined by the interaction of supply and demand in the market
c) Rent is determined by government regulations
d) Rent is determined by historical factors

Answer: b) Rent is determined by the interaction of supply and demand in the market

13. The modern theory of rent suggests that rent arises due to:
a) Land scarcity only
b) Capital scarcity only
c) Both land and capital scarcity
d) Labor scarcity

Answer: c) Both land and capital scarcity

14. According to the modern theory of rent, what happens to rent when demand for land increases?
a) Rent increases
b) Rent decreases
c) Rent remains constant
d) Rent becomes unpredictable

Answer: a) Rent increases

15. Which of the following factors influences the determination of rent in the modern theory?
a) Market demand only
b) Market supply only
c) Both market demand and supply
d) Government regulations only

Answer: c) Both market demand and supply

16. What is the primary focus of the modern theory of rent?
a) Marginal productivity of land
b) Interaction of supply and demand in the market
c) Historical factors determining rent
d) Government regulations on rent

Answer: b) Interaction of supply and demand in the market

17. In the modern theory of rent, rent is determined by:
a) Marginal productivity of land only
b) Marginal productivity of capital only
c) Interaction of supply and demand in the market
d) Historical factors

Answer: c) Interaction of supply and demand in the market

18. According to the modern theory of rent, what role does competition play in rent determination?
a) Competition has no effect on rent
b) Competition increases rent
c) Competition decreases rent
d) Competition stabilizes rent

Answer: c) Competition decreases rent

19. Which of the following factors can lead to a decrease in rent according to the modern theory?
a) Increase in demand and decrease in supply
b) Decrease in demand and increase in supply
c) Increase in both demand and supply
d) Decrease in both demand and supply

Answer: b) Decrease in demand and increase in supply

20. How does technological advancement influence rent according to the modern theory?
a) Technological advancement decreases rent
b) Technological advancement increases rent
c) Technological advancement has no effect on rent
d) Technological advancement stabilizes rent

Answer: a) Technological advancement decreases rent

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21. What happens to rent when there is excess supply of land in the market according to the modern theory?
a) Rent increases
b) Rent decreases
c) Rent remains constant
d) Rent becomes unpredictable

Answer: b) Rent decreases

22. In the modern theory of rent, what happens to rent when there is excess demand for land?
a) Rent increases
b) Rent decreases
c) Rent remains constant
d) Rent becomes unpredictable

Answer: a) Rent increases

23. According to the modern theory, what happens to rent when there is technological regression?
a) Rent increases
b) Rent decreases
c) Rent remains constant
d) Rent becomes unpredictable

Answer: b) Rent decreases

24. What role does the elasticity of demand play in determining rent according to the modern theory?
a) Elastic demand increases rent
b) Inelastic demand increases rent
c) Elastic demand decreases rent
d) Inelastic demand decreases rent

Answer: c) Elastic demand decreases rent

25. Which of the following factors does NOT influence rent according to the modern theory?
a) Market demand
b) Technological advancement
c) Government regulations
d) Historical factors

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Answer: d) Historical factors

26. How does population growth affect rent according to the modern theory?
a) Population growth increases rent
b) Population growth decreases rent
c) Population growth has no effect on rent
d) Population growth stabilizes rent

Answer: a) Population growth increases rent

27. According to the modern theory, what happens to rent when there is a decrease in the fertility of land?
a) Rent increases
b) Rent decreases
c) Rent remains constant
d) Rent becomes unpredictable

Answer: a) Rent increases

28. How does the level of infrastructure development influence rent according to the modern theory?
a) Higher infrastructure development decreases rent
b) Higher infrastructure development increases rent
c) Infrastructure development has no effect on rent
d) Infrastructure development stabilizes rent

Answer: b) Higher infrastructure development increases rent

29. What role does the elasticity of supply play in determining rent according to the modern theory?
a) Elastic supply decreases rent
b) Inelastic supply decreases rent
c) Elastic supply increases rent
d) Inelastic supply increases rent

Answer: a) Elastic supply decreases rent

30. According to the modern theory, what happens to rent when there is a decrease in the cost of production?
a) Rent increases
b) Rent decreases
c) Rent remains constant
d) Rent becomes unpredictable

Answer: b) Rent decreases

31. What are money wages?
a) Wages paid in kind rather than money
b) Wages adjusted for inflation
c) Wages paid in the form of currency
d) Wages paid in the form of goods and services

Answer: c) Wages paid in the form of currency

32. Real wages are:
a) Nominal wages adjusted for inflation
b) Wages paid in real terms without adjustment
c) Wages paid in kind
d) Wages paid in foreign currency

Answer: a) Nominal wages adjusted for inflation

33. Factors determining real wages include:
a) Labor productivity and labor supply only
b) Labor productivity, labor supply, and demand for labor
c) Labor productivity and demand for goods only
d) Labor supply and demand for goods only

Answer: b) Labor productivity, labor supply, and demand for labor

34. According to the theory of wages, what determines real wages?
a) The subsistence level of wages
b) The wages fund available in the economy
c) The interaction of supply and demand in the labor market
d) The surplus value extracted from labor

Answer: c) The interaction of supply and demand in the labor market

35. The subsistence theory of wages suggests that wages:
a) Are determined by the level of labor productivity
b) Are determined by the cost of living necessary for workers to survive
c) Are determined by the amount of capital available for wages
d) Are determined by the bargaining power of workers

Answer: b) Are determined by the cost of living necessary for workers to survive

36. According to the wages fund theory, wages are determined by:
a) The subsistence level of wages

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b) The total amount of capital available for wages
c) The bargaining power of workers and employers
d) The level of labor productivity

Answer: b) The total amount of capital available for wages

37. The subsistence theory of wages suggests that:
a) Wages tend to equal the amount necessary for workers to survive
b) Wages are determined by the level of labor productivity
c) Wages are determined by the bargaining power of workers
d) Wages are determined by the level of capital investment

Answer: a) Wages tend to equal the amount necessary for workers to survive

38. According to the residual claimant theory of wages:
a) Wages are determined by the surplus value extracted from labor
b) Wages are determined by the bargaining power of workers and employers
c) Wages are determined by the level of capital investment
d) Wages are determined by the level of labor productivity

Answer: a) Wages are determined by the surplus value extracted from labor

39. The residual claimant theory of wages suggests that:
a) Employers receive the surplus value generated by workers
b) Workers receive the surplus value generated by employers
c) Wages are determined by the bargaining power of workers
d) Wages are determined by the level of capital investment

Answer: a) Employers receive the surplus value generated by workers

40. According to the subsistence theory of wages, what happens when wages fall below the subsistence level?
a) Workers accept lower wages to maintain employment
b) Workers demand higher wages through collective bargaining
c) Workers resort to strikes and protests
d) Workers seek alternative employment opportunities

Answer: c) Workers resort to strikes and protests

41. The wages fund theory suggests that:
a) Wages are determined by the total amount of capital available for wages
b) Wages are determined by the level of labor productivity
c) Wages are determined by the bargaining power of workers
d) Wages are determined by the surplus value extracted from labor

Answer: a) Wages are determined by the total amount of capital available for wages

42. The subsistence theory of wages is associated with which economist?
a) David Ricardo
b) John Stuart Mill
c) Adam Smith
d) Karl Marx

Answer: a) David Ricardo

43. According to the residual claimant theory of wages, who receives the surplus value generated by labor?
a) Employers
b) Workers
c) Government
d) Consumers

Answer: a) Employers

44. The wages fund theory implies that:
a) There is a fixed amount of capital available for wages
b) Wages are determined by the level of labor productivity
c) Wages are determined by the bargaining power of workers
d) Wages tend to equal the amount necessary for workers to survive

Answer: a) There is a fixed amount of capital available for wages

45. According to the residual claimant theory, what determines the distribution of surplus value between labor and capital?
a) Bargaining power of workers
b) Level of government intervention
c) Technological advancements
d) Relative scarcity of labor and capital

Answer: a) Bargaining power of workers

46. The risk theory of profit suggests that:
a) Profit is the reward for innovation and entrepreneurship
b) Profit is the reward for bearing uncertainty and risk
c) Profit is the result of exploiting workers' surplus value
d) Profit is the result of government intervention in the economy

Answer: b) Profit is the reward for bearing uncertainty and risk

47. According to the risk theory of profit, what role do entrepreneurs play in the economy?
a) They exploit workers' surplus value
b) They bear uncertainty and risk in pursuit of profit
c) They determine wages and prices in the market
d) They redistribute wealth in society

Answer: b) They bear uncertainty and risk in pursuit of profit

48. The uncertainty bearing theory of profit suggests that:
a) Profit is the reward for bearing uncertainty and risk
b) Profit is the result of exploiting workers' surplus value
c) Profit is the result of government intervention in the economy
d) Profit is the reward for innovation and entrepreneurship

Answer: a) Profit is the reward for bearing uncertainty and risk

49. According to the uncertainty bearing theory of profit, what role do entrepreneurs play in the economy?
a) They exploit workers' surplus value
b) They bear uncertainty and risk in pursuit of profit
c) They determine wages and prices in the market
d) They redistribute wealth in society

Answer: b) They bear uncertainty and risk in pursuit of profit

50. The innovation theory of profit suggests that:
a) Profit is the reward for bearing uncertainty and risk
b) Profit is the result of exploiting workers' surplus value
c) Profit is the result of government intervention in the economy
d) Profit is the reward for innovation and entrepreneurship

Answer: d) Profit is the reward for innovation and entrepreneurship

51. According to the innovation theory of profit, what role do entrepreneurs play in the economy?
a) They exploit workers' surplus value
b) They bear uncertainty and risk in pursuit of profit
c) They determine wages and prices in the market
d) They redistribute wealth in society

Answer: d) They redistribute wealth in society

52. The risk theory of profit is associated with which economist?
a) David Ricardo
b) John Stuart Mill
c) Joseph Schumpeter
d) Frank Knight

Answer: d) Frank Knight

53. The uncertainty bearing theory of profit is associated with which economist?
a) David Ricardo
b) John Stuart Mill
c) Joseph Schumpeter
d) Frank Knight

Answer: c) Joseph Schumpeter

54. The innovation theory of profit is associated with which economist?
a) David Ricardo
b) John Stuart Mill
c) Joseph Schumpeter
d) Frank Knight

Answer: c) Joseph Schumpeter

55. According to the risk theory of profit, what happens to profit when entrepreneurs bear higher levels of risk?
a) Profit increases
b) Profit decreases
c) Profit remains constant
d) Profit becomes unpredictable

Answer: a) Profit increases

56. According to the uncertainty bearing theory of profit, what role does uncertainty play in determining profit?
a) Uncertainty has no effect on profit
b) Higher uncertainty leads to higher profit
c) Higher uncertainty leads to lower profit
d) Uncertainty stabilizes profit

Answer: b) Higher uncertainty leads to higher profit

57. According to the innovation theory of profit, what role does innovation play in determining profit?

a) Innovation has no effect on profit
b) Higher innovation leads to higher profit
c) Higher innovation leads to lower profit
d) Innovation stabilizes profit

Answer: b) Higher innovation leads to higher profit

58. Which of the following factors influences profit according to the risk theory of profit?
a) Government regulations
b) Technological advancements
c) Uncertainty and risk
d) Bargaining power of workers

Answer: c) Uncertainty and risk

59. Which of the following factors influences profit according to the uncertainty bearing theory of profit?
a) Government regulations
b) Technological advancements
c) Uncertainty and risk
d) Bargaining power of workers

Answer: c) Uncertainty and risk

60. Which of the following factors influences profit according to the innovation theory of profit?
a) Government regulations
b) Technological advancements
c) Uncertainty and risk
d) Bargaining power of workers

Answer: b) Technological advancements

61. What is the primary difference between money wages and real wages?
a) Money wages are adjusted for inflation, while real wages are not.
b) Money wages represent nominal earnings, while real wages represent purchasing power.
c) Money wages are paid in cash, while real wages are paid in kind.
d) Money wages are paid weekly, while real wages are paid monthly.

Answer: b) Money wages represent nominal earnings, while real wages represent purchasing power.

62. Factors determining real wages include all of the following EXCEPT:
a) Labor productivity
b) Demand for goods and services
c) Inflation rate
d) Labor supply

Answer: c) Inflation rate

63.According to the subsistence theory of wages, what determines the level of wages?
a) Bargaining power of workers
b) Supply and demand in the labor market
c) Cost of living necessary for workers' survival
d) Level of capital investment

Answer: c) Cost of living necessary for workers' survival

64. The wages fund theory suggests that:
a) There is a fixed amount of capital available for wages.
b) Wages are determined by the level of labor productivity.
c) Wages tend to equal the amount necessary for workers to survive.
d) Wages are determined by the bargaining power of workers and employers.

Answer: a) There is a fixed amount of capital available for wages.

65. According to the residual claimant theory of wages, who receives the surplus value generated by labor?
a) Employers
b) Workers
c) Government
d) Consumers

Answer: a) Employers

66. The risk theory of profit posits that profit is the reward for:
a) Bearing uncertainty and risk.
b) Exploiting workers' surplus value.
c) Government intervention in the economy.
d) Technological advancements.

Answer: a) Bearing uncertainty and risk.

67. The uncertainty bearing theory of profit suggests that:
a) Profit is the result of exploiting workers' surplus value.

b) Profit is the reward for bearing uncertainty and risk.
c) Profit is the result of government intervention in the economy.
d) Profit is the reward for innovation and entrepreneurship.

Answer: b) Profit is the reward for bearing uncertainty and risk.

68. According to the innovation theory of profit, profit is the reward for:
a) Bearing uncertainty and risk.
b) Exploiting workers' surplus value.
c) Government intervention in the economy.
d) Innovation and entrepreneurship.

Answer: d) Innovation and entrepreneurship.

69. The risk theory of profit is associated with which economist?
a) Adam Smith
b) Karl Marx
c) Frank Knight
d) John Maynard Keynes

Answer: c) Frank Knight

70. The uncertainty bearing theory of profit is associated with which economist?
a) Joseph Schumpeter
b) John Stuart Mill
c) David Ricardo
d) John Maynard Keynes

Answer: a) Joseph Schumpeter

71. The innovation theory of profit is associated with which economist?
a) Adam Smith
b) John Maynard Keynes
c) David Ricardo
d) Joseph Schumpeter

Answer: d) Joseph Schumpeter

72. According to the risk theory of profit, what happens to profit when entrepreneurs bear higher levels of risk?
a) Profit increases
b) Profit decreases
c) Profit remains constant
d) Profit becomes unpredictable

Answer: a) Profit increases

According to the uncertainty bearing theory of profit, what role does uncertainty play in determining profit?
a) Uncertainty has no effect on profit
b) Higher uncertainty leads to higher profit
c) Higher uncertainty leads to lower profit
d) Uncertainty stabilizes profit

Answer: b) Higher uncertainty leads to higher profit

According to the innovation theory of profit, what role does innovation play in determining profit?
a) Innovation has no effect on profit
b) Higher innovation leads to higher profit
c) Higher innovation leads to lower profit
d) Innovation stabilizes profit

Answer: b) Higher innovation leads to higher profit

According to the risk theory of profit, what role do entrepreneurs play in the economy?
a) They exploit workers' surplus value
b) They bear uncertainty and risk in pursuit of profit
c) They determine wages and prices in the market
d) They redistribute wealth in society

Answer: b) They bear uncertainty and risk in pursuit of profit

The uncertainty bearing theory of profit suggests that profit is the reward for:
a) Bearing uncertainty and risk.
b) Exploiting workers' surplus value.
c) Government intervention in the economy.
d) Technological advancements.

Answer: a) Bearing uncertainty and risk.

The innovation theory of profit is associated with which economist?
a) David Ricardo
b) John Stuart Mill
c) Joseph Schumpeter
d) Frank Knight

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Answer: c) Joseph Schumpeter

According to the innovation theory of profit, what happens to profit when entrepreneurs introduce new products or production methods?
a) Profit decreases
b) Profit increases
c) Profit remains constant
d) Profit becomes unpredictable

Answer: b) Profit increases

Which of the following factors influences profit according to the risk theory of profit?
a) Government regulations
b) Technological advancements
c) Uncertainty and risk
d) Bargaining power of workers

Answer: c) Uncertainty and risk

Which of the following factors influences profit according to the uncertainty bearing theory of profit?
a) Government regulations
b) Technological advancements
c) Uncertainty and risk
d) Bargaining power of workers

Answer: c) Uncertainty and risk

According to the innovation theory of profit, what role does innovation play in determining profit?
a) Innovation has no effect on profit
b) Higher innovation leads to higher profit
c) Higher innovation leads to lower profit
d) Innovation stabilizes profit

Answer: b) Higher innovation leads to higher profit

According to the risk theory of profit, what happens to profit when entrepreneurs bear higher levels of risk?
a) Profit increases
b) Profit decreases
c) Profit remains constant
d) Profit becomes unpredictable

Answer: a) Profit increases

According to the uncertainty bearing theory of profit, what role does uncertainty play in determining profit?
a) Uncertainty has no effect on profit
b) Higher uncertainty leads to higher profit
c) Higher uncertainty leads to lower profit
d) Uncertainty stabilizes profit

Answer: b) Higher uncertainty leads to higher profit

According to the innovation theory of profit, what role do entrepreneurs play in the economy?
a) They exploit workers' surplus value
b) They bear uncertainty and risk in pursuit of profit
c) They determine wages and prices in the market
d) They redistribute wealth in society

Answer: d) They redistribute wealth in society

The risk theory of profit is associated with which economist?
a) David Ricardo
b) John Stuart Mill
c) Joseph Schumpeter
d) Frank Knight

Answer: d) Frank Knight

The uncertainty bearing theory of profit is associated with which economist?
a) David Ricardo
b) John Stuart Mill
c) Joseph Schumpeter
d) Frank Knight

Answer: c) Joseph Schumpeter

The innovation theory of profit is associated with which economist?
a) David Ricardo
b) John Stuart Mill
c) Joseph Schumpeter
d) Frank Knight

Answer: c) Joseph Schumpeter

According to the risk theory of profit, what happens to profit when entrepreneurs bear higher levels of risk?
a) Profit increases
b) Profit decreases
c) Profit remains constant
d) Profit becomes unpredictable

Answer: a) Profit increases

According to the uncertainty bearing theory of profit, what role does uncertainty play in determining profit?
a) Uncertainty has no effect on profit
b) Higher uncertainty leads to higher profit
c) Higher uncertainty leads to lower profit
d) Uncertainty stabilizes profit

Answer: b) Higher uncertainty leads to higher profit

According to the innovation theory of profit, what role does innovation play in determining profit?
a) Innovation has no effect on profit
b) Higher innovation leads to higher profit
c) Higher innovation leads to lower profit
d) Innovation stabilizes profit

Answer: b) Higher innovation leads to higher profit

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