

# 5. Production, Specialization and Exchange

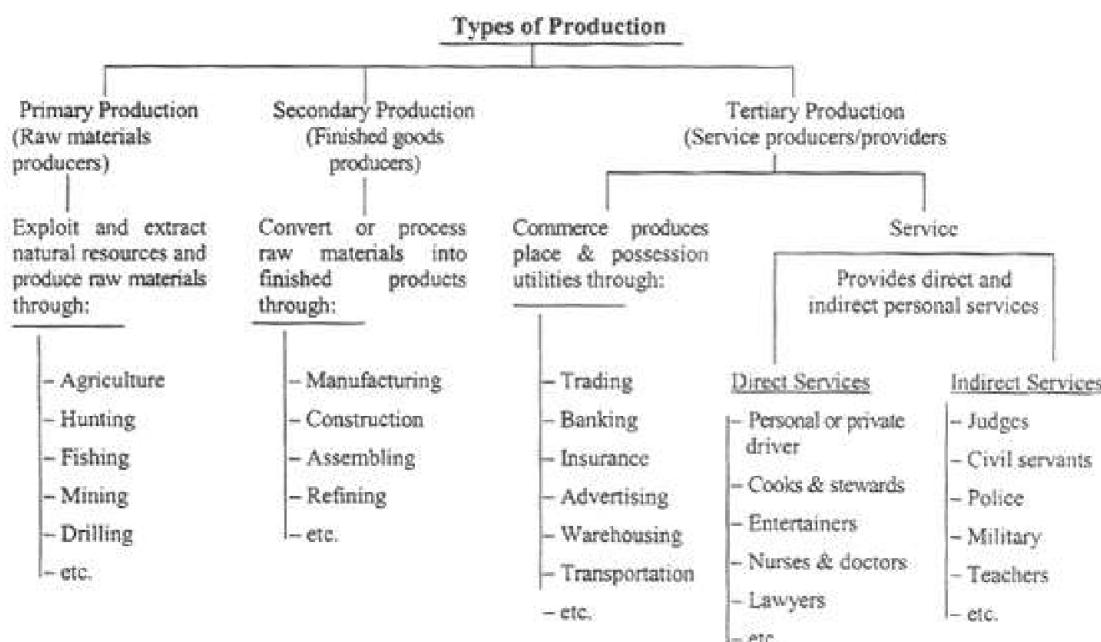
## Objectives

At the end of this chapter, students should be able to define production, specialization and exchange; list factors of production and give examples, and identify the relationships between the three.

## 5.1 Meaning of Production

Production can be defined as the making of goods and provision of services that give satisfaction to the needs or wants of others. It is the creation of utility. Production can be classified into three, namely Primary, Secondary and Tertiary.

Although we have shown what goods or services are rendered by each of the occupational groups discussed in [Chapter 4](#), we can re-examine the same outputs in terms of human efforts and the satisfaction such outputs give to wants or needs. This is presented in Table 5.1.



**Fig. 5.1: Classification of Production**

It can be observed from the table above that for the results of any human activity to be productive, it must not only have resulted from efforts, it must also have met the needs of others. This explains why such efforts are remunerated in one way or the other, and why those whose wants are satisfied by the results of such efforts have to pay for the satisfaction. We mentioned earlier on that the results of efforts of others, that is, the finished products of others, are sometimes raw materials to another group. We shall now go further to examine the component parts of these factors of production.

## 5.2 Factors of Production

The resources which are used in productive processes are known as factors of production. There are four factors of production: *labour, land, capital and entrepreneurship* or *organization*.

## 5.2.1 Labour

This is a summation of all the human beings that are available for gainful employment within a country. It is otherwise referred to as the labour force or the working population of a country. It includes both the country's nationals and the foreign nationals within the country. However, the available labour force or the working population excludes:

- (i) all children below school age;
- (ii) all students in full-time education;
- (iii) housewives otherwise engaged in unpaid domestic chores;
- (iv) old age pensioners and retired workers;
- (v) chronically sick people and the lunatics.

The list in (i) – (v) above can be referred to as the unemployable, while the rest who are capable of active employment are referred to as employables. It must be added that the workers who are able bodied, are physically and mentally sound, but who loathe being employed belong to the class of employables. They are characteristically referred to as *work-shy*. Those who are capable of work and are ready for a job, but cannot find one are referred to as *unemployed*. Although government statistics are not as refined or developed as to show the true size of the unemployed in any African country, the sight of school-leavers – primary and secondary – roaming the streets in big cities and small towns in search of jobs that are unavailable is sufficient to estimate the enormity of the problem.

In fact, labour has been defined as:

All mental and physical exertion of the body or mind undergone partly or wholly in the performance of some task, with a view to obtaining some reward other than the mere pleasure derived from the work, or all human efforts applied to production.

The reward to labour is wages (salaries, commissions and fees).

### (a) Classes of Labour

In commerce, labour can be classified as follows: (as it is not a homogenous factor of production).

- (i) **The skilled labour:** Examples are the technologists, engineers, mechanics, carpenters, tailors, teachers, doctors, nurses, lawyers, etc.
- (ii) **The semi-skilled labour:** These are technicians, ward maids and apprentices of all grades. They represent a class halfway between skilled and unskilled manual labour.
- (iii) **The unskilled labour:** Examples of these are cleaners, carriers of loads, and casual labourers. They constitute the largest sector of the labour market in West Africa and are, therefore, very lowly paid. However, in the labour market of Western countries, they are very few and, therefore, highly remunerated.

### (b) Size of Labour

**Increase in the size of labour force:** The supply of labour can be increased by any of these measures:

- (i) enlarging market;
- (ii) increasing the population by having more children per family;
- (iii) lowering of compulsory school-leaving age. For instance, if school children have been staying for full-time education up till the age of eighteen, they can be asked to leave at sixteen;
- (iv) changing the distribution in favour of the employables;
- (v) increasing the age of retirement, for instance from sixty years to sixty-five years;
- (vi) increasing the working hours per day, e.g. closing time 3.30 pm to 4.30 pm (starting from 7.30 am) or working additional hours on Saturday (8.00am – 12.00 noon);
- (vii) increasing the rate of remuneration (wages or salaries), but this may lead to a reduction in labour supply;

- (viii) encouraging the immigration of foreign workers;
- (ix) changing social habits to allow more housewives to accept employment outside their domestic duties.

### **(c) Quality of labour**

The quality of labour can be improved as follows:

- (i) giving opportunities for higher educational attainments, secondary school leavers would be more productive than the primary six, secondary or modern school ‘graduands’;
- (ii) creating opportunities for professional training for instance teaching, banking, accountancy, insurance, medicine, architecture town-planning and a host of others;
- (iii) improving the physical conditions under which employees carry out their duties. For instance, comfortable seats and desks, well-ventilated offices and good sanitary environment are all conducive to higher productivity, In a country with high temperature for most of the year, the use of air-conditioners in offices would contribute to high efficiency of workers, especially the business executives;
- (iv) operating good employment working conditions. Good incentives, reasonable salaries and tangible fringe benefits all serve to bring the best out of workers;
- (v) providing efficient equipment – where employees work with machinery and other equipment, the efficiency of labour can be enhanced by the good quality of this machinery and equipment.

### **5.2.2 Land**

This is an important factor of production. It is not limited simply to the floor space of an office, or to the soil on which we grow crops and walk. It includes all other gifts of nature which are within a man’s environment, and which are for the use of man for his own benefit. It includes the minerals, bodies of water, climate, natural vegetation, sunshine, moonlight, and air. There is hardly any earthly product which does not originate directly or indirectly from the land. Our clothes, shoes, textbooks, writing materials, the houses in which we live, and the vehicles in which we travel are all directly or indirectly acquired from the land.

The reward to land as factor of production is rent. Land is limited in supply, i.e. It is fixed.

### **5.2.3 Capital**

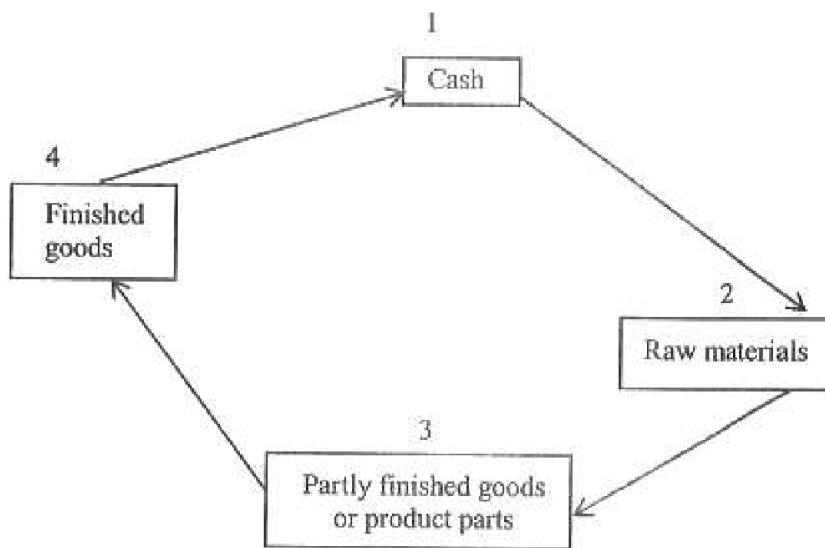
If land is nature’s gift, capital is man-made. Economists define capital as ‘man-made productive assets’. Consumer goods are goods produced for consumption purposes only such as food products or household furniture; while capital goods are produced for the sole purpose of producing further wealth – examples are machinery, the barber’s pair of scissors and razor blades. The generator for generating electricity for running a factory that produces some commodities is a capital good, while that which generates electricity for cooking meals at home is a consumer good.

Furthermore, capital must have been generated in the past but conserved (left unused for further generation of wealth or capital for the future). That is, capital results from the unspent part of our income. For instance, the unspent portions of our income are saved with the commercial banks, from where those who wish to borrow for investment purposes do so. The reward capital receives as factor of production is interest.

The accountant would normally classify capital in a business into two main categories:

- (i) **Fixed capital:** This is otherwise referred to as fixed assets. Fixed assets are the property of any business which are retained in the business, used over and over again to generate further wealth or production. Examples of these are buildings, furniture, premises, plant, machinery and vehicles.
- (ii) **Circulating capital:** This is that part of capital investment in a business which has the feature of changing form from time to time. By this, we mean that one particular type of item can change into

another type within a short time. Examples of such items are cash, raw materials, product parts or semi-finished goods and finished goods. This is demonstrated in the flow chart below.



**Fig. 5.2: Circulating of Capital**

Let us examine the flow chart above as a business of items of circulating capital. We may start from cash, though in reality we can make any one of the items a starting point.

The cycle of business goes thus: 'cash' is turned into raw materials by buying raw materials with 'cash'. The 'raw materials' bought are turned into 'partly finished goods or products parts'. These in turn are converted through production processes into 'finished goods' which are sold in the market for 'cash', thereby completing the circle. Repeating the same journey round the circle can be done many times over, depending on the rate of business turnover. It is this going through the 'circle' that is referred to as circulating.

Whether an item of capital is fixed or circulating depends on the nature of the business. To a publishing company, the fleet of vehicles with which it distributes its stock of books to the markets all over the country would represent fixed capital; but to a vehicle assembly company like the Peugeot Assembly Plant (Nigeria) Ltd. in Kaduna, its fleet or vehicles constitute circulating capital.

#### **5.2.4 The Entrepreneur**

An entrepreneur may be defined as the coordinating factor of production. It is he who organises the other factors of production, land, labour and capital for more production purposes of goods and services. He formulates policies and takes decision as to how the other factors of production should be combined. He directs the business activities and bears the risk of the business. His reward for this is profit.

### **5.3 Interrelationship between Production, Specialization and Exchange**

Production and exchange in the modern society or economy are interrelated. Specialization occurs when a workers performs one task in a production process (indirect production) or produces one type of product for which he is best suited. In this case, he does not only attempt to be self-sufficient by producing the goods and services which he needs but he also produces for others to consume. He is therefore said to be producing for the market.

Specialization which is one of the basic features of modern economy necessitates exchange. This implies that production takes place at one end and consumption takes place at the other end. In between

them there is exchange whereby the producer (worker) exchanges his products for the goods and services he needs but does not produce himself.

If the goods (products) are exchanged directly for goods, it is called barter. This was the case in the past. Nowadays, in a modern society or economy such as ours, money serves as a medium of exchange. The producer (worker) in a modern or money economy, sells his products for money which he in turn uses to buy the goods and services he needs from other producers (workers).

Without exchange, division of labour and indirect production will be impossible. Exchange thus plays an important role in modern economy.

## Summary

- For production to be meaningful it must involve human activities that make goods and provide services that give satisfaction to human wants, that is, creation of utility.
- (i) **Labour:** This is all human effort, mental and physical, applied to production. Labour can be graded as to quality and can similarly be improved upon. Reward of labour can be wages, (salaries, fees, commission).
- (ii) **Capital:** This is man-made resource for future production accumulated from the unspent income or products of man. Its reward is interest.
- (iii) **Land:** This is nature's gift: the soil, water, sea, etc. and it cannot be increased easily. It earns rent as its reward.
- (iv) **Entrepreneurship:** This is the organizer of the other factors of production for production purposes. He earns profit for his services as his own reward.

## Revision Questions

### A. *Essay Questions*

1. List the factors of production. Discuss them and state which one is most uncommon in your country today.
2. (i) Who is an entrepreneur?  
(ii) What are his primary functions?  
(iii) Would you place him in a category that is distinguishable from that of general labour? Why?
3. 'For the different categories of factors of production there are different forms of remuneration'. Do you agree with the above statement? In which forms are the different factors remunerated?
4. (a) What is production?  
(b) Explain the different activities involved in industrial, commercial, and service occupations.  
*(WASSCE 1994)*
5. (a) What is production?  
(b) Illustrate with a labelled diagram the main divisions and subdivisions of production.  
*(WASCCE 1998)*

### B. *Objective Questions*

1. The manufacture of goods and the provision of services that lead to the satisfaction of people's want is
  - A. production
  - B. labour
  - C. entrepreneur
  - D. exchange

2. Which of the following has a relatively fixed supply?
- Capital
  - Entrepreneurship
  - Current assets
  - Land

(WAEC 1999)

3. What is NOT the function of an entrepreneur?
- bearing risks
  - deciding on tax to pay
  - deciding what to produce
  - organizing other factors
  - providing initial capital

(NECO 2001)

4. The factor of production which involves both the mental and physical effort of man is called
- capital
  - entrepreneur
  - labour
  - land
5. The conversion of raw materials into finished products creates
- marginal utility
  - place utility
  - form utility
  - time utility
6. Which of the following converts raw materials into finished products?
- Extractive industry
  - Manufacturing industry
  - Commercial industry
  - Construction industry
7. The three main divisions of production include
- industrial, commercial and banking services
  - industrial, commercial and services
  - industrial, transportation and services
  - industrial, manufacturing and services
8. The primary motive of production is
- promotion
  - competition
  - employment
  - consumption
9. Which of the following is classified under extractive production?
- Shoemaking
  - Dressmaking
  - Road construction
  - Coal mining

10. Changing raw materials into finished goods is an example of
- A. primary production
  - B. secondary production
  - C. tertiary production
  - D. direct service

## Project

Compile a list of the different categories of labour available in your locality. In each category, work out the grades of remuneration.