

Chapter 5

Theory of Production

5

CHAPTER

INTRODUCTION

Production to an economist means any activity that results in the creation of goods and services to satisfy human wants. This chapter discusses the various aspects of production under the following headings:

- ◆ Meaning of production
- ◆ Aim of production
- ◆ Types of production
- ◆ Stages of production
- ◆ Factors of production
- ◆ Characteristics of factors of production
- ◆ Process of production

OBJECTIVES

At the end of this chapter, students should be able to:

- ◆ Explain the concept of production;
- ◆ State and explain the characteristics of each factor of production;
- ◆ State and explain the different types of production.

5.1 Meaning of Production

Production is the transformation of raw materials into finished goods. It also includes the distribution and provision of goods and services in order to satisfy human wants. Production is said to be complete when the goods and services produced reach the final users or consumers.

Production is also the creation of utility, while utility is the ability of any commodity or service to satisfy human wants (Fig. 5.1).



FIG. 5.1 Process of production

5.2 Aim of Production

The aim of all production is to satisfy human wants. It is a waste of time, effort and resources to produce things which people do not want. All production therefore must aim towards the satisfaction of human wants. Man's basic wants are food, clothing and shelter. The aim of production is to improve the economic welfare of the people. Economic well-being depends on the volume of production. As the volume of production increases, there is a corresponding increase in

the material well-being of the people. The primary aim of all production activities is to make available goods and services which can be used to satisfy human wants. This explains the statement that consumption is the final aim of production. The goods or commodities that satisfy human wants directly are called consumer goods (Fig. 5.2).



FIG. 5.2 Consumer goods

5.3 Capital Goods

These are goods meant for the production of further goods; for example, machines, cars and lorries used in carrying out productive activities (Fig. 5.3).



FIG. 5.3 Capital goods

5.4 Stages of Production

- Primary production:** This is the type of production that involves the tapping or extraction of natural resources, agricultural products, mining, quarrying, fishing, hunting, and so on.
- Secondary production:** This type of production involves the processing or conversion of primary products or raw materials into finished, semi-finished or intermediate products; for example, furniture making, clothes, processing of foods, and so on. The manufacturing and constructive industries are involved in this stage of production.

FIG. 5.3 Capital goods

iii. Tertiary production: This is the stage of production where the goods and services produced at the above two stages are taken to those who need them. This stage completes the production processes since production is not complete until the goods and services produced reach the final consumers. Examples are distribution, communication, banking, insurance, teaching, legal service, and so on.

5.5 Types of Production

i. Direct production: This is the type of production that is carried out on a small scale usually by a family or household whose aim is to meet the family's requirement.

ii. Indirect production: This means the production of goods and services for exchange in order to use the money realised to satisfy the other needs of the producer. This type of production takes place because it is not possible in the modern society for anybody to satisfy all his needs directly with his own goods and services.

5.6 The Production Process

Production is made up of complex set of activities which contribute directly or indirectly towards satisfying human wants. The production process has the four basic stages as shown in Fig. 5.4.

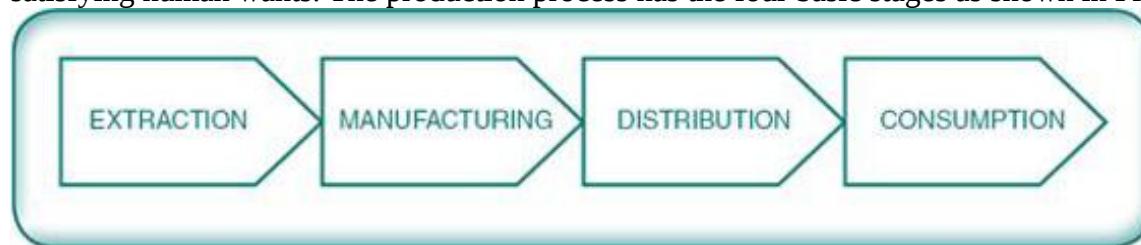


FIG. 5.4 Production process

It is necessary to note that while some commodities like crude oil pass through the four stages, the provision of most services does not pass through these stages. Instead, services are usually provided directly to the consumers. Thus, the services of the doctor, the lawyer, or the teacher do not undergo further processing stages before reaching the consumers.

5.7 Factors of Production

Factors of production are the resources used to produce goods and services. There are four factors of production. They are land, capital, labour and entrepreneur. These four factors must be combined before production can take place.

5.7.1 Land

Land as a factor of production is a free gift of nature and is fixed. It is the oldest factor of production. Land in economics does not include only land surface of the earth but all other free gifts of nature like water, forest, mineral resources, sun, mountains, rocks, lakes, and so on.

Features of Land

- (a) It is a free gift of nature and has no cost of production.
- (b) It is fixed in supply. For example, the natural resources like crude oil, diamonds, and gold cannot be increased in volume by man.
- (c) It costs human being nothing to bring it into existence.
- (d) It is geographically immobile. It cannot be moved.
- (e) Land is subject to the law of diminishing returns.
- (f) The quality and value of land vary from one place to another. Some lands are located in good business environment that attract high value. Some lands are more fertile than others.
- (g) The reward of land is called rent.

5.7.2 Labour

Labour means all human efforts, which can be physical, mental, skilled or semi-skilled and unskilled, used in production of goods and services. The reward of labour is called wages or salaries. Labour is an active factor of production.

Characteristics of labour

- (a) Labour cannot be stored like capital.
- (b) Labour is unpredictable.
- (c) It is unique because it is provided by man.
- (d) Labour is mobile.
- (e) Labour is not fixed. Its quality and quantity can be increased.

Types of labour

- (a) Skilled labour:** This involves the use of mental ability in carrying out productive activities. It

includes workers who are highly educated up to the university level and other professionals who hold administrative and managerial positions like engineers, lawyers and economists.

(b) Semi-skilled labour: This type of labour involves the combination of both physical and mental efforts in carrying out productive activities. It includes workers with little education and training up to senior secondary school level. Workers here include clerks, typists and other middle-level workers.

(c) Unskilled labour: Labour is unskilled if the work requires little or no training; for example, cleaners, labourers and porters.

5.7.3 Capital

Capital means wealth set aside for the production of further wealth. It means different things to different people. A farmer's hoes, matchets, seedlings, and other farming implements are his capital. To a hunter, his arrows, bow, traps and spear constitute his capital. The trader's money and his wares mean his capital.

Features of capital

- (a) Capital is man-made.
- (b) It can be accumulated.
- (c) It takes different forms like machinery, money, building, etc.
- (d) The reward for capital is interest.
- (e) Capital can depreciate in value.

Types of capital

(a) Fixed capital: Fixed capitals are the durable assets of a business that can last for a very long time. These forms of capitals do not change their form in the process of production. For example, furniture, buildings, machinery and vehicles.

(b) Circulating or working capital: This refers to those materials that change their form in the process of production into finished products; examples include raw materials, fuel and money set aside for the payment of wages and salaries.

(c) Social capital: This includes those forms of capital provided by the government that help in production. They include electricity, roads, railways, airports and sea ports.

5.7.4 The Entrepreneur

This is defined as the factor of production that organises and co-ordinates other factors of production for more productive purposes. The entrepreneur is the person who risks his capital in establishing a business whose profitability can never be determined at that time. An entrepreneur is the person who co-ordinates, controls and organizes the production process to obtain maximum production at minimum costs, with a view to making profit. The reward for entrepreneur is profit.

Characteristics of the Entrepreneur

- (a) The entrepreneur employs all other factors of production.
- (b) The risks he bears are not transferable.
- (c) His functions regarding what and how to produce are unique.
- (d) His reward is his profit.

Functions of the Entrepreneur

(a) Provision of capital: He provides the initial capital used in the formation of the business. It is from this capital provided by the entrepreneur that other factors of production are hired.

(b) Decision taking: He takes decisions as to the type of business to embark on, what to produce and the quantity to be supplied to the market.

(c) Risk bearing: He bears all types of risks that occur in the business. If the business fails, he will bear the loss all alone.

(d) Co-ordination of other factors of production: The entrepreneur combines and co-ordinates other factors of production in order to achieve meaningful production. He determines the quality and quantity of other factors of production to be used.

Summary

Definition of production

- Production is the creation of goods and services to satisfy human wants.
- Transformation in production process means
- Changing the form of a commodity from raw materials to finished goods
- Changing the location of a commodity from one place to another
- Provision of services that facilitate the exchange of goods and services

- The aim of production: The aim of production is the satisfaction of human wants directly or indirectly.
- Consumer goods: Goods that directly satisfy human wants, for example, bread, milk, and so on.

Revision Questions

Objective Questions

1. In economics, production is complete when:
 - (a) Goods are produced in factories
 - (b) Goods are sold to wholesaler
 - (c) Prices are fixed for goods and services
 - (d) Goods and services reach the consumers
 - (e) Goods are sold to retailers
2. Land is often different from other factors of production because:
 - (a) It is a free gift of nature
 - (b) It constitutes one-third of the entire world
 - (c) It has different grades
 - (d) It is owned by individuals
 - (e) It is owned by government (**SSCE 1992**)
3. In economics the reward for labour is in the form of:
 - (a) Wages
 - (b) Profit
 - (c) Rent
 - (d) Dividends
 - (e) Interest (**SSCE 1993**)
4. Capital as a factor of production is important because:
 - (a) It enables us to carry out tasks which cannot be done by human efforts only
 - (b) Most tasks can be done with save hands
 - (c) People can work without capital
 - (d) Without capital all other factors are useless
 - (e) It provides money which is essential for the growth of business
- Capital goods: Goods that indirectly satisfy human wants through aiding the production of final consumer goods, e.g., television and furniture.

Stages of production

- (a) Primary stage: This is the first stage of production; for example, the extraction of raw materials from the land.
- (b) Secondary stage: This involves the processing of raw materials into finished products or consumer goods.
- (c) Tertiary stage: This includes distribution, transportation and sales of goods.

Factors of production

These are the instruments of production and the different types are as enumerated below.

- Land: This includes all the gifts of nature.
- Labour: This is human effort, manually or mentally engaged in production.
- Capital: These are wealth set aside for the production of further wealth.
- Entrepreneurship: This involves the organisation and direction of other factors of production.
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Class Activities

- (a) Students should be taken out to the nearest farms and factories to observe and compare the production processes on the farms with those in the factories.
- (b) On a map of Nigeria locate the main mineral resources.
- (c) Draw a chart showing the types of production in your country.
- (d) Draw the map of Nigeria and mark on it the main cash crops that are grown in each area.
5. The term ‘production’ in economics means:

- (a) The manufacturing of goods
- (b) The creation of utilities
- (c) Giving birth to children
- (d) The distribution of goods and services
- (e) Using labour in creating something (**SSCE 1995**)

Essay Questions

1. (a) What is meant by production?
(b) Explain, with the aid of examples the following types of production:
 - (i) Primary
 - (ii) Secondary and
 - (iii) Tertiary. (**SSCE 1998**)
2. (a) Define labour as a factor of production.
(b) Explain five characteristics of labour. (**SSCE 2001**)
3. (a) What are capital goods?
(b) Explain the problems associated with the distribution of goods in your country. (**SSCE 2005**)
4. (a) Explain with examples the following types of production:
 - (i) Primary
 - (ii) Secondary and
 - (iii) Tertiary production.
(b) Give two reasons why primary production predominates in developing countries.

Glossary

Production: Transformation of raw materials to finished goods.

Capital Goods: Goods meant for the production of other goods.

Land: Free gift of nature and is fixed.

Labour: All human efforts.

Capital: Wealth set aside for the production of further wealth.

Entrepreneur: An organizer and coordinator of other factors of production.

Primary production: Production involving extraction.

Secondary production: Production involving conversion

Tertiary production: Production stage of taken the products to the consumers.

Direct production: Small scale production by household.

Indirect production: Production to realize money to satisfy other needs of the producer.