UNIT I

THEORY OF DEMAND AND UTILITY

Syllabus: Demand utility and Indifference curves, Approach to analysis of Demand. Elasticity of Demand, Measures of Demand elasticity. Factors of Production, Advertising Elasticity

Weightage: **2 Questions**
26 Marks

Question1: Define economics and describe basic concepts of Economics. **S-09 6 Marks**

S-15
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Answer:

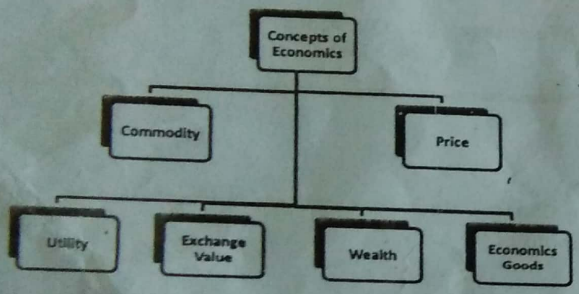
1. Economics is defined as social science that analyzes production, distribution and consumption of goods and services.
2. Economic goods definitely have monetary value associated with it.
3. Various concepts related to Economics are as follows:

   A. Commodity:

   1. Commodity refers to an object which can be possessed by a person.
   2. Commodity has an exchange value.
   3. Thus commodity is anything that satisfies human wants and has exchange value.

B. Utility:

1. Utility of commodity is its usage value or its capacity to satisfy human wants.
2. Utility and usefulness are not the same. Use of brandy as medicine is good but its excess intake is bad use. But its utility is same in both cases as it satisfies human wants.
3. Utility of commodity may vary with respect to place, time and person.



C. Price:

1. Value of commodity in terms of money is price.
2. Price helps to compare values of different commodities.
3. All transactions are made in terms of money and hence Price is very important economic concept.

D. Exchange Value:

1. Value of any commodity can be expressed in two terms; one is its value when used and other is in terms of exchange.
2. Value of commodity when it is used is referred as utility.

3. While exchange value refers to value associate commodity when it is exchanged.
4. Value of exchange depends on how scarce commodity is and what is the utility of the commodity.

E. Wealth:

1. Every commodity in economics will be associated with wealth.
2. Wealth here refers to three qualities viz. utility, scarcity and exchange value.
3. More the utility of product, more the scarcity of product, more the exchange value of the product, more will be the wealth associated with the product.
4. Thus II economic goods will have more or less wealth associated with it.

F. Economic Goods:

1. Any good having monetary value is called as economic good.
2. Human efforts are required for obtaining economic goods.
3. House, clothes, food, etc are example of economic goods.

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Concept of Demand:

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Question2: What is meant by Demand? Everyone desires a Maruti-800 Car. Does this mean that demand for Maruti 800 car is large? W-08 5 Marks

Answer:

1. In economics demand simply does not mean the desire. E.g. A middle class man will have desire to have air conditioned bungalow, but this is not demand.
2. Demand also does not mean need. E.g.: Beggar on street needs food, clothing and shelter, but then this is also not demand.
3. Thus we can define Demand as "Demand means desire backed by adequate purchasing power".
4. Thus desire or need will become demand, only if buyer has means to buy it.
5. ** Everyone desires Maruti-800 car. But everyone may not have sufficient money to buy Maruti car. Thus demand for Maruti-800 car will not be large.
6. In fact, demand means specific quantity of goods purchased.
7. Now quantity purchased will depend on price of goods.
8. Thus ultimately demand will depend on specific price of good.
9. Thus if price is not stated, we cannot determine demand of good.
10. Also it is necessary to mention demand for a time period to have complete meaning. E.g. Demand for milk is 150000 liters at a price of Rs. 30 per liter for 1 year.
11. It is logical to mention, specific market or place to define demand completely. E.g. thus we can write above example as "Demand for milk in Nagpur for 1 year is 15000 liters at a price of Rs. 30 per liter.

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Determinants of Demand:

Question3: Explain or list factors influencing individual demand?

Answer:

Individual Demand is affected due to following factors

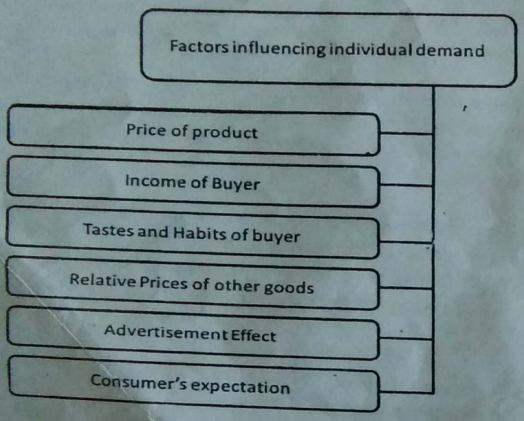
1. **Price of Product:** If price of a product is less, then demand will be more. Conversely if price of product is more than demand will be less. E.g. If price of dry fruits is more, demand is less. But if price of dry fruits fall down, more people will buy it and hence demand will be more.

2. **Income of Buyer:** If income of buyer is more he can buy more goods and thus demand for that good will be more. Conversely, if buyer has low income, he cannot buy goods and thus demand for that good will be less.

3. **Tastes and Habits of Buyer:** If person is habituated to have more tea or coffee, than demand for tea and coffee will be more. With fear of bird flu, people stopped eating eggs and chicken, thus demand for eggs and chicken will be reduced.

4. **Relative Prices of other goods – Substitutes and Complementary products:**
   i. When want or desire can be satisfied by alternative goods then, they are called as substitutes. E.g. Groundnut oil and sunflower oil are substitutes of each other.
   ii. If price of substitute increases, then demand of goods in question will increases.
   iii. If price of substitute decreases, then demand of goods in question will decrease.
   iv. Complementary goods are always in joint demand. One commodity cannot be used without other. E.g. Car and petrol

are complementary goods. If price of complementary good increases, then demand of goods in question will decrease. If price of complementary good decreases then demand of goods in question will increases.



5. **Advertisement Effect:** Demand for goods may increase due to effect of advertisements.

6. **Consumer's Expectation:**
   i. If consumer expects fall in price of goods in future, demand for that good will fall in present.
   ii. If consumer expects hike in price of good in future, demand will increase in present.

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Question4: Explain factors influencing Market Demand.

Answer:

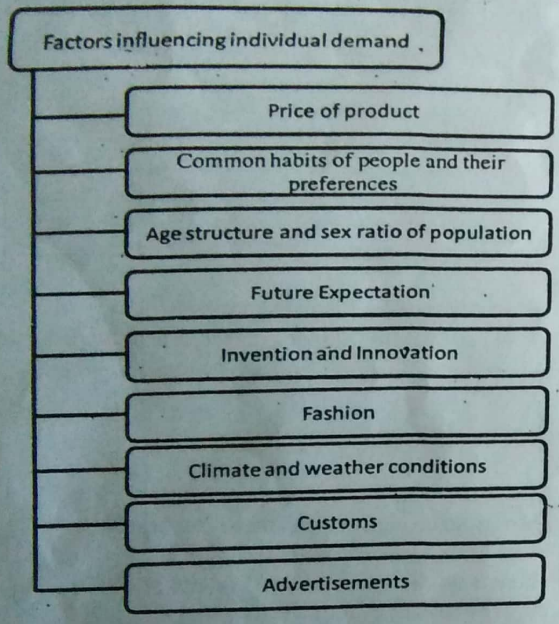
1. **Price of the Product:** At low price of product, market demand will be more. Conversely for high price of product, market demand will be less.

2. **Common habits of people and their preferences:** Common habits of people and their preferences affect market demand. E.g. In today's era, people have become more aware of health and fitness. Thus demand for traditional sweets would decrease and demand for low-fat food items would increase.

3. **Age structure and sex ratio of population:** Market demand depends on age structure and sex ratio of population. E.g. If age structure of population has more old aged people, demand for walking sticks, hearings aids, spectacles will increase. Similarly if age structure of population has more babies, demand for toys, diapers will increase.

4. **Future Expectation:** If buyer expects that price of product will rise in future, present market demand will increase. Conversely, if buyer expects that price of product will fall in future, present market demand will decrease.

5. **Invention and Innovation:** Invention and innovation of new goods reduce demand for existing goods. E.g. Invention of CDs and DVDs reduced demand for existing audio cassettes.



6. **Fashion:** Market demand for many products is affected by change in fashion. E.g. Demand for square framed spectacles will increase if it is in fashion.

7. **Climate and weather conditions:** Market demand for products also depends on climate and weather conditions. E.g. In summer, demand for cold drinks and ice-creams will be more, whereas in winter demand for same products is less.

8. **Customs:** Demand for certain products depends on customs, festivals etc. E.g. demand for kites will be high during Makar Sankranti.

9. **Advertisements:** Market demand for certain products gets affected due to advertisements.

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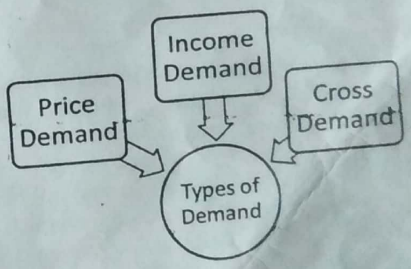
Classification of Demand:

Question5: What are different types of demand?

Answer:



Demand can be classified as follows:

A. **Price Demand:** Price demand is different quantities of product demanded in given time in given market if price of product varies.

B. **Income Demand:** Income demand is different quantities of product demanded in given time in given market if income of customer varies.

C. Cross Demand: Cross demand is different quantities of product demanded in given time in given market if price of complementary goods and substitute goods varies.

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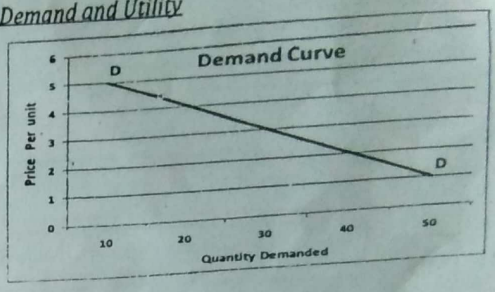
Law of Demand:

Question6: State law of demand.
Question6: State law of demand with its exceptions. **S-08 7 Marks**
Question6: What is Giffen's Paradox **W-03 3 Marks**

Answer:

1. Law of demand is stated as "Other things being equal, if price of commodity is high, smaller quantity is demanded and if price of commodity is low, larger quantity is demanded".
2. In other words, we can say that demand for product rises, if price of product falls. And demand for product falls if price of product rises, provided other things remains constant.
3. We can also conclude that, other things remaining constant demand varies inversely with price.
4. Diagrammatic representation of law of demand can be drawn as

Price of Product A	Quantity Demanded
5	10
4	20
3	30
2	40
1	50



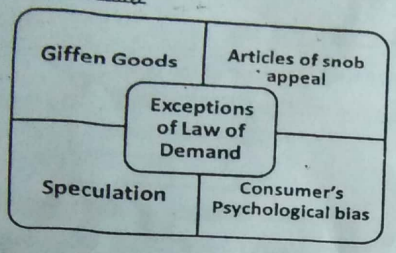
5. In above figure DD is demand curve.
6. DD is downward sloping curve, thus it indicates inverse relationship of quantity demanded and price per unit.

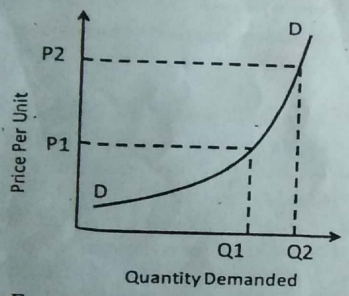
Assumptions of Law of Demand:

1. There is no change in consumer's income.
2. There is no change in consumer's preference.
3. There is no change in fashion.
4. There is no change in prices of related goods.
5. No expectations of future price change.
6. No change in age structure and sex ratio of population.
7. No change in climate and weather conditions.

Exceptions of Law of Demand OR Limitations of Law of Demand:

1. In some cases, with fall in price demand also falls and with rise in price demand also rises.
2. Such situations are exception to law of demand.
3. Demand curve for such situation can be drawn as





Exceptional Demand Curve Figure

Exceptional cases for law of Demand

A. Giffen Goods or Giffen's Paradox:

1. For certain inferior quality of goods, even if price falls demand for the goods will not increase.
2. These inferior quality goods are called as Giffen Goods.
3. Since quality of Giffen good is low, even when price is low, people do not want to buy them.

4. Hence demand will decrease instead of increasing. Thus this is an exception to law of demand.
5. Example- Rotten onions or bad quality potatoes have low price but their demand is not more. Thus this is Giffen good.
6. Giffen good is named on name of economist "Robert Giffen" who introduced this concept.

B. Articles of snob appeal:

1. Some goods are demanded for their snob appeal or status symbol.
2. Even if price of good is high demand for those goods are high because of status symbol associated with it.
3. Example- Rolls Royce Cars and Diamonds.

C. Speculation:

1. If consumer feels, price of product may change in future, then law of demand will not be followed.
2. Thus there will be an exception for law of demand. E.g. If consumer finds price of sugar is rising, then he will buy more sugar for hoarding it. Thus even with rise in price, demand for sugar does not fall.

D. Consumer's Psychological Bias:

1. Some consumers have special liking for some special brands.
2. Thus for this type of consumers; law of demand is not followed.
3. Example- Someone may like "Red Label" tea. So even if price of Red Label increases, its demand will not fall as person likes that particular brand of tea.

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Question7: Explain contraction and decrease in demand, expansion and increase in demand. W-09 7 Marks

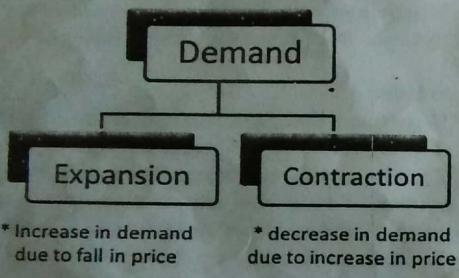
Question7: Write short note on extension and increase in demand. S-06 5 Marks

Question7: Distinguish between

1. **Extension and increase in demand**
2. **Contraction and decrease in demand S-04 4 Marks**

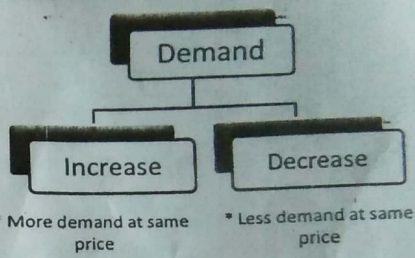
Answer:

A. Expansion and Contraction in Demand:



1. If price of product falls, then there will be more demand for the product. This is called as Expansion of demand.
2. Thus expansion of demand is; more demand of product due to fall in price of product.
3. If price of product rises than there will be less demand for the product. This is called as Contraction of demand.
4. Thus contraction of demand is; less demand of product due to rise in price of product.

B. Increase and Decrease in Demand:



1. If more quantity of product is bought than before at the same price, than we say there is increase in demand.
2. Thus at constant price, if demand is more due to other factors than it is said as increase in demand.
3. If lesser quantity of product is bought than before at the same price, than we say there is decrease in demand.
4. Thus at constant price, if demand is less due to other factors, than it is said as decrease in demand.
5. Example- Price of sugar is fixed as Rs 30/-Kg. Now there is more demand of sugar due to festive season; this is called as increase in demand.
6. Similarly if people in area become more health conscious, there will be fall in demand of sugar, even though he price of sugar is same. This is called as decrease in demand. diabetic

Factors that causes increase and decrease in demand:

(Note: Increase and Decrease in demand occurs when other factors change, but price is constant)

1. Change in income of consumer.

2. Change in taste, habits and preference of consumer.
3. Change in fashion and custom.
4. Change in price of substitutes and complementary goods.
5. Change in supply of substitutes and complementary goods.
6. Change in population structure.

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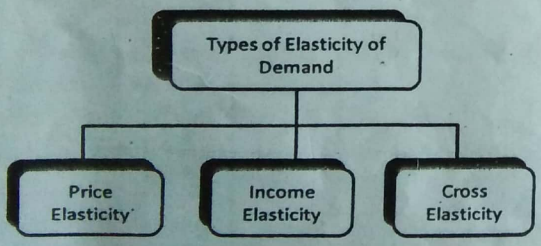
Question8: Explain the term Price elasticity, Income elasticity and Cross elasticity of demand. **S-08 6 Marks**

Answer:

1. Demand for goods varies with price. In some cases with change in price, demand varies widely.
2. While in some other cases even if price changes considerably, demand does not change considerably.
3. Thus extent of variation of demand for price changes is called as **elasticity of demand.**
4. Thus we can define elasticity of demand as "Elasticity of demand is a measure of relative change in amount purchased in response to relative change in price"



A. Price Elasticity:

1. Price elasticity refers to degree of responsiveness of demand for a product to given change in price.
2. Price elasticity is defined as ratio of percentage change in quantity demanded to percentage change in price.

$$\text{Price elasticity} = \frac{\text{Percentage change in Quantity demanded}}{\text{Percentage change in Price}}$$

B. Income Elasticity:

1. Income elasticity refers to degree of responsiveness of demand for a product to given change in income.
2. Income elasticity is defined as ratio of percentage change in quantity demanded to percentage change in income.

$$\text{Income elasticity} = \frac{\text{Percentage change in Quantity demanded}}{\text{Percentage change in Income}}$$

C. Cross Elasticity:

1. Cross elasticity refers to responsiveness of demand for a product to given change in price of commodity which can be substitute or complementary goods.
2. Cross elasticity is defined as ratio of percentage change in quantity demanded to percentage change in price of complementary or substitute goods.

$$\text{Cross elasticity} = \frac{\text{Percentage change in Quantity demanded}}{\text{Percentage change in price of substitute goods.}}$$

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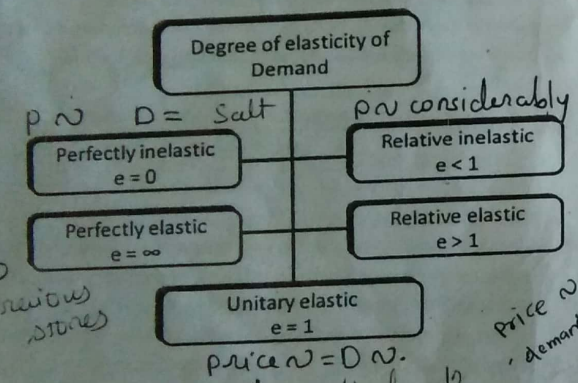
Degree of Elasticity of Demand:

Question9: Define elasticity of demand and illustrate its cases.
S-09 7 Marks

~~Question9: Explain different types of elasticity of demand.~~

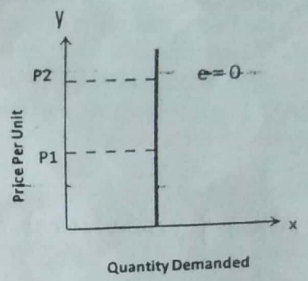
Answer:

Elasticity of demand can be defined as "Elasticity of demand is a measure of relative change in amount purchased in response to relative change in price"



A. Perfectly Inelastic:

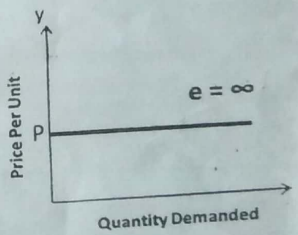
1. If there is no change in quantity demanded even if price changes drastically, demand is said to be perfectly inelastic demand.
2. If "e" is the elasticity of demand, then for perfectly inelastic demand e = 0.
3. Diagrammatically we can represent as,



Example: - SALT. Even if the price rises, we need salt for our daily use; hence demand for salt is perfectly inelastic.

B. Perfectly Elastic:

1. If with slight increase in price demand for the product reduces to 0 (zero), demand is said to be perfectly elastic.
2. If "e" is elasticity of demand, then for perfectly elastic demand $e = \infty$.
3. Diagrammatically we can represent as,

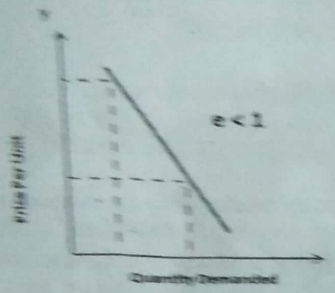


Example: - Precious Stones. If price of these valuable stones increases; their demand will fall to zero.

price ↓ consider ↑ demand ↑

C. **Relatively Inelastic demand:**

1. If there is considerable change in price but demand does not get affected in that proportion, demand is said to be relatively inelastic.



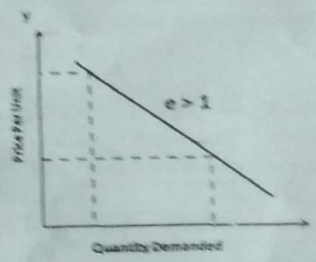
2. If "e" is elasticity of demand, then for relatively inelastic demand, e < 1.
3. Diagrammatically we can represent as.

Example: Milk. Price of milk has increased from Rs 15/- liter to Rs 30/- liter. But its demand is not reduced in that proportion.

D. **Relatively Elastic Demand:**

1. If there is small change in price, but demand gets affected considerably then demand is said to be relatively elastic demand.
2. If "e" is elasticity of demand, then for relatively elastic demand, e > 1.
3. Diagrammatically we can represent as.

Price ↓ Small ↑ demand ↑

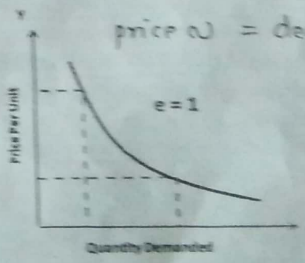


Example: Onions, Potatoes. If price of Onions increases from Rs 15/- Kg to Rs 50/- Kg, then less people will buy Onions. Instead they will prefer other less costly vegetables.

E. **Unitary Elastic Demand:**

1. If proportionate change in demand is exactly same as proportionate change in price then demand is said as Unitary elastic demand.
2. If "e" is elasticity of demand then for unitary elastic demand we have e = 1.
3. Diagrammatically we can represent as.

price ↓ = demand ↓



4. This is only theoretical condition.

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Question10: Define advertising elasticity. Discuss factors affecting it. W-02 6 Marks

Question10: Write short note on Advertising Elasticity. W-07, W-09 5 Marks

Question10: Explain Advertising elasticity of Demand. W-02, W-03 5 Marks.

Answer:

1. Advertising elasticity refers to degree of responsiveness of demand for product to given change in level of advertising.
2. Thus Advertising elasticity gives an idea as how demand will vary if expenditure on level of advertisement is varied.
3. We can also define Advertising elasticity as ratio of percentage change in quantity demanded to percentage change in Advertising expenditure.
4. Advertising elasticity may have values as e >1 or e < 1.

$$\text{Advertising elasticity of Demand} = \frac{\text{Percentage change in quantity demanded}}{\text{Percentage change in avertising expenditure}}$$

5. For e > 1, demand is relatively elastic demand. This means if we increase expenditure on advertising there will be proportionately increase in demand. A·E ↑ ∝ demand ↑
6. For e < 1, demand is relatively inelastic demand. This means if we increase expenditure on advertising there will be proportionately less increase in demand. A·E ↑ demand ↓
7. Advertising elasticity of demand is very important for company's marketing department.

8. It makes clear, amount of expenditure one should do on advertising.
9. Thus marketing department can take important strategic decisions with help of Advertising elasticity.

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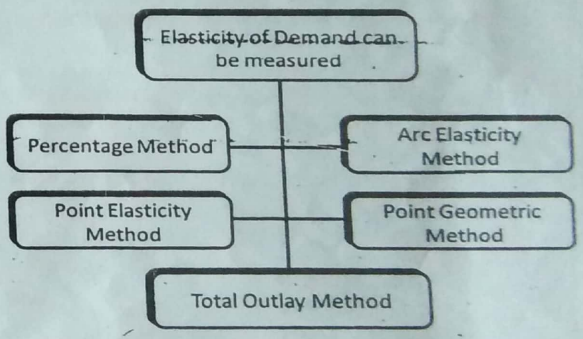
Measurement Methods for elasticity of Demand:

Question11: Explain total outlay method of measurement of elasticity of demand. W-09 6 Marks

Question11: Explain Arc elasticity method of measurement of price elasticity. S-04 6 Marks.

Answer:



1. Percentage Method:

percentage method :-

a. Elasticity of demand by percentage method can be calculated using below formula:

$$e = \frac{\text{percentage change in quantity demanded}}{\text{percentage change in price}}$$

$$\text{percentage change in quantity demanded} = \frac{\text{Net quantity demanded- old quantity demanded}}{\text{average quantity demanded}} * 100$$

$$\text{percentage change in price} = \frac{\text{New price-Old price}}{\text{Average price}} * 100.$$

2. Point elasticity Method:

a. Elasticity of demand by point elasticity method can be calculated as follows:

$$e = \frac{\Delta Q}{Q} \div \frac{\Delta P}{P}$$

$$= \frac{\Delta Q}{Q} \times \frac{P}{\Delta P}$$

$$e = \frac{\Delta Q \cdot Q}{\Delta P \cdot P} = \frac{\Delta Q}{\Delta P} \times \frac{P}{Q}$$

3. Total Outlay Method:

a. Alfred Marshall suggested this method of determining elasticity of demand.

b. He suggested determining total outlay or total money expended by consumer can be used to determine elasticity of demand.

c. Total outlay for consumer is calculated as follows.
Total outlay = Price per unit × Quantity demanded

d. Consider table below:

	Price/ Unit	Qty Demanded	Total Outlay	Elasticity of demand
Original	5	13	65	
Change 1	8	10	80	e < 1
Change 2	2	14	28	inelastic

e. As we can see increase in price causes increase in total outlay and decrease in price causes decrease in total outlay.

f. Thus for this case demand is relatively inelastic e < 1.

g. To summarize total outlay method, we can tabulate results as follows:

	Price (per Unit)	Total Outlay	Types of Elasticity
1.	Increases Decreases	Constant Constant	e = 1 (Unitary)
2.	Increases Decreases	Decreases Increases	e > 1 (relatively elastic)
3.	Increases Decreases	Increases Decreases	e < 1 (relatively inelastic)

h. Now this method is not very accurate.

i. It gives idea about type of elasticity but not its numerical value.

j. Economic significance: It tells what happens to total outlay or total revenue and thus helps in determining price policy of the company.

people may cut their current expenditure on fruits and buy medicines in case of epidemics.

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Marginal Utility:

Question15: State and explain law of diminishing marginal utility.

S-03, W-03, W-09, S-07 7 Marks

Question15: Write short note on principle of diminishing marginal utility.

W-02 5 Marks

Answer:

1. Utility refers to capacity of a good to satisfy a want.
2. As it refers to mental state, it can't be measured.
3. It may be compared with utility of another good or for convenience may be measured in terms of money.
4. Total utility is amount of satisfaction derived from consumption of a good.
5. Marginal utility is addition to total utility caused by an increase of one unit of consumption (or stock purchased).
6. For Example: If a child consumes 2 apples; his hunger is satisfied. But he does not stop and eats third apple too. Two apples is the total utility and third one is marginal utility.

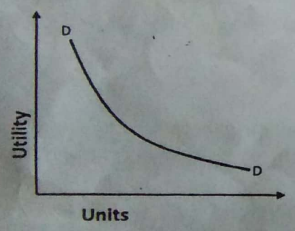
Law of Diminishing Marginal Utility:

1. It states that," The additional benefit which a person derives from a given increase of his stock diminishes with every increase in stock that he already has."

2. In simple words, law means the more and more of a thing we have the less and less I want it. (It is also called as law of satiable wants)
3. For example: If child has many chocolates and he eats one, he will derive great satisfaction. But sooner he eats another chocolate, he won't get that pleasure. Thus marginal utility of good diminishes.
4. Take the case of starving man. If he finds one slice of bread, it will have great utility for him.
5. If he finds second slice it will be welcomed by him.
6. With every addition of bread, he will have less utility.
7. He will go on consuming; up to a point where he will be on margin of doubt whether to consume any more or not.
8. If he consumes after the margin of doubt it is called as marginal unit.

Assumptions:

1. It refers only to given period of time. There should not be any long interval between consumption of goods. We also assume there is no change in consumption habits of people.



2. If we take very small units, marginal utility may decrease. Hence size of units must be reasonable. If for instance, thirsty man is given water in teaspoon marginal utility of water may increase for him.
3. All units of good must be identical. If we consider fruits, they must be of same variety, type and size.

Limitations:

1. The law does not apply to those abnormal persons who have a mad desire for something.
   E.g.1 For a drunkard, intoxication may increase with every additional dose.
   E.g.2 For a miser greed increases with more and more money.
2. In some cases with an increase in additional unit, instead of decreasing marginal utility increases.
   For example, one who has hobby of collecting old coins, his marginal utility instead of decreasing will increase.
3. Economists argue, law does not apply to money and no doubt there is some truth in it.
4. After earning sufficient amount, a stage may reach when he would prefer leisure to money. Thus with increase in money marginal utility decreases.

Importance of Law:

1. If law is not there, person will spend all his money on single commodity. But on account of operation of Law (as the law exists), consumer distributes his expenditure over number of commodities.
2. It tells us relationship between price and marginal utility. Concept of consumer's surplus is based on this law.
3. It is used in field of taxation too. Progressive taxation is based on this law.

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Question16: Explain consumer's equilibrium with help of indifference curve.

Answer:

S-15

Question18: Explain meaning of 1) Land, 2) capital, 3) Labour, 4) Entrepreneur as factors of production. W-08 8 Marks

Question18: What do you mean by factors of production? Explain the factors that determine efficiency of labour. S-09 8 Marks

Question18: What are the various factors of production? Explain peculiarities of labour. S-07 6 Marks.

Question18: What is division of labour? Explain advantages of division of labour. W-07 6 Marks

Question18: Write a short note on features of land. S-08 5 Marks

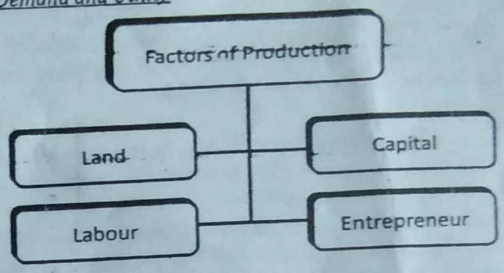
Question18: Explain importance of capital and entrepreneur in modern system of production. W-02 6 Marks

Answer:

Production means putting all utilities together to obtain output. But in sense of economics, production is not creation of utility but creation or addition of value.

Factors of Production:

1. Resources required to produce a given product are called factors of production. These may be raw materials, services, labour, capital etc.
2. These productive resources may be termed as inputs of production.
3. Traditionally factors of production are Land, Capital, Labour and Organization.



A. Land:

1. It has got special meaning in economics. It is not merely soil but has a wider sense.
2. It comprises of all the natural resources which yield income or has got an exchange value.
3. All the resources which nature gives us in form of air, light and water comes under land.
4. Peculiarities :
   a) Land is nature's Gift to men.
   b) It is a fixed quantity, i.e. changes in market price can't change supply of land. It is going to be constant.
   c) It is permanent hence original and indestructible.
   d) It lacks mobility in geographical sense.
   e) It provides infinite variation in terms of degrees of fertility. Hence no two pieces of land are alike.

B. Labour:

1. Labour is mass of unskilled men.
2. But in sense of economics, any work either mental or manual, undertaken for monetary consideration is called labour.

3. Thus according to Marshall, "Any exertion of mind or body undergone with a view to obtain or produce some commodity rather than pleasure is called labour".
4. Peculiarities:
   a) Labour being living things, is not only means of production but also the end of production.
   b) Inseparable from labourer himself.
   c) He has to sell his labour in person.
   d) Labour is perishable and has no reserve price. Thus he has to accept wage offered to him.
   e) It has weak bargaining power.
   f) Changes in price of labour re-act curiously on its supply. Thus in case of labour; fall in price may not increase the supply.
   g) There can be no rapid adjustment in supply of labour against its demand.

Factors determining efficiency of labour:

1. **Racial quality:**
   i. Heredity and racial stock to which labour belongs will determine his efficiency.
   ii. For example, labour from one particular racial stock can perform better physical work but is poor in technical knowhow.
   iii. On the other hand labour from other racial stock is well versed in technical aspects but can't do labourious work.

2. **Climatic factors:**
   i. Climatic conditions affect the efficiency of labour to great extent.

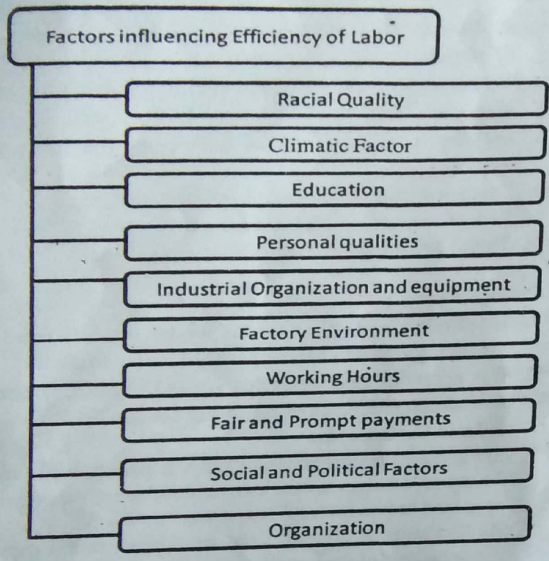
   ii. Cool bracing climate is favorable and conducive, on the other hand tropical climate is unfavorable.

3. **Education:**
   i. Education has deep impact on efficiency of labour.
   ii. Technically educated labour will have more efficiency then a person who does not know technical aspects.
   iii. Also general level of education helps in improving efficiency of labour.
   iv. A non educated labour will not have desired level of efficiency.

4. **Personal qualities:**
   i. Personal qualities like mental alertness, intelligence, resourcefulness, taking initiative add up to efficiency of labour.
   ii. While qualities like laziness, carelessness, non seriousness towards work, lethargic attitude hinders efficiency.

5. **Industrial organization and equipment:**
   i. Better work environment, well maintained tools and equipments adds to labour's efficiency.

6. **Factory environment:**
   i. Environment of factory should be conducive for labour to increase their efficiency.
   ii. Environment which is not properly ventilated, insanitary surrounding, non-airy, damped surrounding is non conductive and hence reduce efficiency.



7. Working hours:

i. Working hours should not be too long as long working hours impair efficiency.

ii. Also short intervals between works should be allowed to labour. This will increase their efficiency.

8. Fair and prompt payment:

i. Wages paid to the labour should be fair and prompt.

ii. This gives contentment to labour and he can work with more efficiency.

9. Social and political factors:

i. If the labour has sense of social security he is able to concentrate on his work and can put more efforts to achieve his goal.

ii. This ultimately will increase his efficiency.

10. Organization:

i. Organization itself plays an important role in improving efficiency of labour.

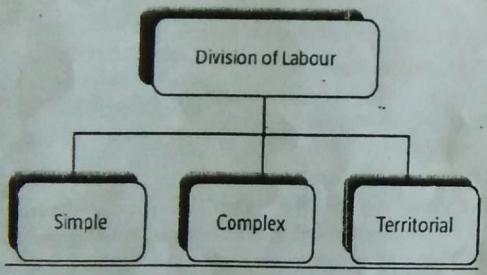
Division of labour:

1. When any article/ good are produced, entire manufacturing process is divided into number of small processes.
2. These small processes are then entrusted to separate group of labour.
3. This is called as division of labour.
4. Division of labour can be classified as follows:

a) Simple division of labour: It is also called as functional division of labour. Division of societies into major occupation as farmer, mason, cobbler, etc. is example of simple division of labour.

b) Complex division of labour: In single manufacturing cycle, work is divided into many processes. These processes are then executed by different group of workers. This is called as complex division of labour. Cutting, drilling, finishing, packing, etc. is an example of complex division of labour.

c) Territorial division of labour: It refers to certain localities, cities or towns which are specialized in production of some commodities. Banaras is famous for weaving silk, while Orissa is famous for handicrafts. This is an example of territorial division of labour.



Merits of Division of labour:

1. It increases productivity.
2. There is increase in dexterity and skill.
3. New inventions are facilitated.
4. There is great saving in time.
5. For large scale productions, quality of work is improved as there is specialized group of people working on each process.
6. There is diversity in employment. Variety of jobs is created.
7. It serves the purpose of right man in right place. Thus it helps in reduction of defects or abnormalities.

Demerits of Division of labour:

1. Employees find it as monotonous jobs.
2. This retards human development, as mind is set to work same thing every day.
3. Industry is dehumanized as each employee starts working as machine.
4. There is loss of multi skill due to repetition.
5. Risk of unemployment increases.
6. This is considered as evils of factory system.

C. Capital:

1. It refers to man's that part of wealth which is used in further producing wealth or which yields more income.
2. It is generally used for capital goods like plant, machinery, tools and accessories, stock of raw materials and fuel.
3. Is Land Capital – No
   a) Land is free gift of nature and it is not manmade or produced.
   b) Land is indestructible and permanent; capital is perishable
   c) Land has no mobility; capital is mobile
   d) Quantity of land is fixed or limited, while capital can be increased or decreased.
4. Capital plays vital role in modern production; as goods can't be furnished and materials can't be made useful, till they are processed by tools and machinery, which requires Capital.
5. It occupies central position in process of economic development. In fact capital formation is core of economic development.
6. Capital creates employment opportunities
   a) When capital is produced, some employment opportunities are created.
   b) Secondly more men are employed when capital produced is used for furnishing goods.

D. Organization enterprise / Entrepreneur:

1. Entrepreneur co-ordinates and correlates factors of production.
2. He starts, organizes and supervises the work.
3. He takes care of paying rent to landlord, paying interest on capital borrowed, wages to labour etc and residue left if any is his.
4. If nothing is left after venture, venture is miscarried.
5. It is also possible that handsome profit is made by him. Thus he takes final responsibility of business.
6. Organizing and risk taking (or uncertainty bearing) are chief functions of entrepreneur.
7. Entrepreneur also have to be innovator, it may mean the introduction of a new production method or an improvement in old methods.
8. Innovation may also be new techniques in way of an administrator, finance, marketing or human relations inside and outside firm.
9. Thus entrepreneur has to bear highest risk and so also the profit.

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