3. Theory of Distribution.

Point P3. Theory of distribution refers to the distribution of national income among the various factors of production. National income means the agregate value of all goods & services produced by a co. during a particular period of time. Since the national income is the joint efforts of all factors of production It is the outcome of the fore factors of production. Therefore national income must be properly distributed among the factors. Income of factors may be inform of rate, interest, wages and profit.

Types of distribution

A) Personal distribution :-

It refers to the study of individual income. It study that how much is earned by individuals.

B) Functional distribution :-

Fuctional distribution refers to the study of national income of factors. It study that how much is earned by factors of production.

Marginal Productive Theory of Distribution

It determine the income of the factors of production. It determines the share of the owners of factors of production in the national income. The theory deals with the pricing of the productive resources. It was developed by J.B. Clark and Wicksteed.

According to this theory, the income of factors of production is determined by its marginal production. Marginal production means the addition made to the total product by employing one more unit of a labour.

Assumptions:

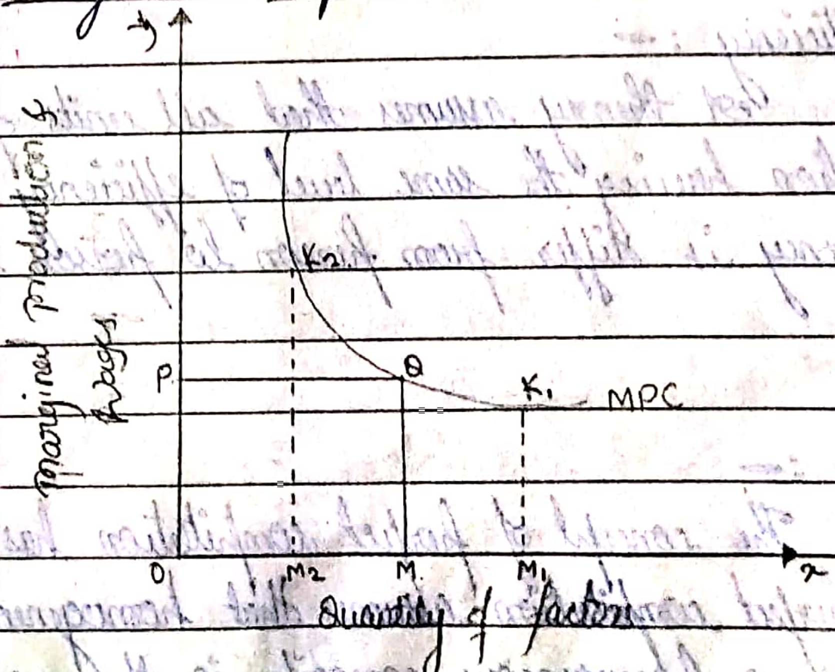
The theory is based on certain assumptions these are:

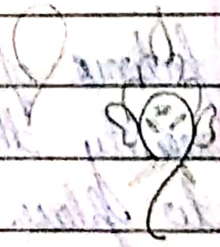
1) There must be perfect competition in goods market and factors market.
2) All units of factors of production having the same efficiency.
3) The producer is interested in getting maximum profit.
4) There must be full employment in economy.
5) The theory is based on the law of diminishing marginal productivity.
6) There must be free mobility of factors of production.

The theory distribution can be explained with the help of following diagram.

→ A producer can employ more and more units of labour up to their marginal product must be equal to marginal wage. In this case usually a firm will gets its equilibrium position.

Diagramatic representation :-





In the above diagram MPC is the marginal production curve. OY curve shows MP and Price of factors of production. OX horizontal curve denotes units of factors of production. At point K_1 a firm will get marginal profit. Because its marginal production is higher than the wage. At point K_2 a firm will get less profit with higher expenses. So therefore it is better to produce @ point Q where marginal product equals to wage.

Critisism :-

marginal productivity theory of distribution has been critisised on following terms:

1) Perfect competition :-

The theory assumes that there is a full employment in the economy. It is full utilization of available natural resources and human resources, but there is no employment in the modern economies. Even though there is under utilization of human resources as well as natural resources.

2) Same level of efficiency :-

A theory assumes that all units of the factors of production having the same level of efficiency but in reality the efficiency is differ from person to person and place to place.

3) Perfect competition :-

The concept of perfect competition has been critisized because perfect competition assumes that homogeneous commodity. But there is no homogeneous comodity in the market.

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Therefore it is wrong assumption.

4) Free mobility of factors :-
According to this theory there is free mobility of factors in the market, But there is no free mobility of factors in the economy.

5) Law of diminishing returns :-
The theory is based on the law of diminishing returns in actual. There are 3 types of behaviours of production like, increasing, decreasing and constant returns to scale.

6) method of production is constant :-
Theory assumes that no change in the methods of production. It means method of production is constant. But the production is subject to various methods

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