

6.11.1 Dynamic Theory of Profit

This theory was propounded by the American economist J.B. Clark in 1900. To him, profit is the difference between price and cost of production of the commodity. Hence, profit is the reward for dynamic changes in society. Further he points out that, profit cannot arise in a static society. Static society is one where everything is stationary or stagnant and there is no change at all. Therefore, there is no role for an entrepreneur in a static society. The price of the commodities in a static society would be equal to their cost of production. So, there would be no profit for the entrepreneur. The entrepreneur only gets wages for management and interest on his capital.



At present several changes are taking place in a dynamic society. Changes are permanent. According to Clark, the following five main changes are taking place in a dynamic society.

1. Population is increasing
2. Volume of Capital is increasing.
3. Methods of production are improving.
4. Forms of industrial organization are changing.
5. The wants of consumer are multiplying.

6.11.2 Innovation Theory of Profit

Innovation theory of profit was propounded by Joseph. A. Schumpeter. To

Schumpeter, an entrepreneur is not only an undertaker of a business, but also an innovator in the process of production. To him, profit is the reward for “innovation”. Innovation means invention put into commercial practice.

According to Schumpeter, an innovation may consist of the following:

1. Introduction of a new product.
2. Introduction of a new method of production.
3. Opening up of a new market.
4. Discovery of new raw materials
5. Reorganization of an industry / firm.

When any one of these innovations is introduced by an entrepreneur, it leads to reduction in the cost of production and thereby brings profit to an entrepreneur. To obtain profit continuously, the innovator needs to innovate continuously. The real innovators do so. Imitative entrepreneurs cannot innovate.

6.11.3 Risk Bearing Theory of Profit

Risk bearing theory of profit was propounded by the American economist F.B. Hawley in 1907. According to him, profit is the reward for “risk taking” in business. Risk taking is an essential function of the entrepreneur and is the basis of profit. It is a well known fact that every business involves some risks.

Since the entrepreneur undertakes the risks, he receives profits. If the entrepreneur does not receive the reward, he will not be prepared to undertake the risks. Thus, higher the risks, the greater are the profit.