

**CANARA VIKAS PU COLLEGE**  
**ECONOMICS KEY ANSWERS-2024**

**Part A**

I Choose the correct answer:

1. b) Consumer behavior
2. a) Marginal Revenue
3. c) Price floor
4. b) Depreciation
5. b) Autonomous consumption

II Fill in the blanks:

6. Choice
7. Perfect competition
8. Export
9. RBI
10. 1<sup>st</sup> April to 31<sup>st</sup> March

III Match the following:

11. SMC                       $\Delta TC / \Delta Q$
12. Normal Profit              Zero Profit
13. Domestic service              Non monetary Exchange
14. Money                      Medium of exchange
15. Balance of payment              Trade in goods and services

IV. Answer the following questions in one words:

16. Marginal Rate of substitution.
17. An equilibrium can be defined as a situation in which the plans of all consumers and firms in the market match and market clears.

18. If we deduct the value of depreciation from gross value added we will get the net value added.

19.  $MPC = \Delta C / \Delta y = c$

20. If some users do not pay and it is difficult and sometimes impossible to collect fees for the public goods, such non paying users are known as free riders.

#### Part B

V Answer the questions in four sentences :

21. Inferior goods are the goods for which the demand decreases with the increase in the income of the consumer.

Eg: Low quality of goods, unbranded products.

22. a. Cardinal utility Analysis- Law of Diminishing marginal utility

b. Ordinal Utility Analysis- Law of indifference curve analysis

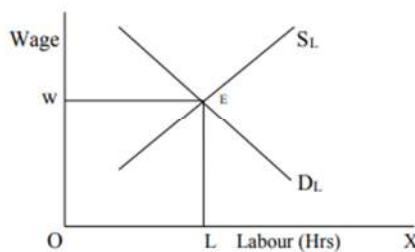
23. a. Technological progress

b. Price of inputs

24. The price at which equilibrium is reached is called Equilibrium price.

The quantity which is bought and sold at equilibrium price is called equilibrium quantity.

25. : The wage rate is determined at the point where the labour demand and supply curves intersect. This is shown in the following diagram:



In the above diagram, hours of labour is measured in X axis and Wage is measured in Y

axis. SL is labour supply curve and DL Labour demand curve. With an upward sloping

supply curve and downward sloping demand curve, the equilibrium wage rate is determined

at the point where these two curves intersect (point E). That means, the wage rate is

determined at that point where the labour that the households wish to supply is equal to the

labour that the firms wish to hire.

26. The four factors of production and their rewards are:

Land - Rent

Labour – Wages

Capital- Interest

Organisation – Profit

27. Nominal GDP

Real GDP

1. GDP is calculated for the current year's price.

1. GDP is calculated for the base years price.

2. It is denoted by GDP.

2. It is denoted by gdp.

3. Nominal GDP= Total product \* current years price

3. Real GDP= Total product\* base years price

28. The ratio of the total increment in equilibrium value of final goods output to the initial increment in autonomous expenditure is called investment multiplier.

Investment multiplier=  $\Delta Y / \Delta A = 1/1-c=1/s$

29. The distinction between surplus budget and deficit budget is as follows:

Surplus Budget

Deficit Budget

1. Here, the tax collection of Government exceeds its required expenditure.

Here, the Government's expenditure exceeds its revenue.

2. It is generally made by developed countries.

It is generally made by developing countries.

30. People demand foreign exchange rate because of the following reasons:

- To purchase goods and services from other countries.
- To send gifts abroad
- To purchase financial assets abroad.

### Part C

VI Answer the questions in 12 sentences:

31. : A market economy also known as capitalistic economy is that economy in which the economic decisions are undertaken on the basis of market mechanism by the private entrepreneurs. It functions on demand and supply conditions. In USA, Japan, Australia, UK and other countries we can see Market Economic systems.

In market economy, private individuals own the factors of production. Here, the profit is the main goal of business. There is least intervention of Government.

Price mechanism plays a major role in market economy. It is a balancing wheel of the market mechanism. Prices coordinate decisions of the producers and consumers. The price is determined by demand and supply in the market. No individual organization or Government is responsible for the production and distribution or pricing of goods. All depend on market mechanism.

Regarding basic problems of an economy, the problem of what to produce is solved on the basis of demand and profit. The producers produce those products which bring more income.

The problem - how the goods are to be produced is determined by the competition among different entrepreneurs. The select least cost combination of technology so that they can get more returns with less cost.

In market economy, the problem of whom to produce is decided on the basis of purchasing power of consumers. The producers produce commodities to the rich as they can afford to pay more but poorer sections of the society are neglected.

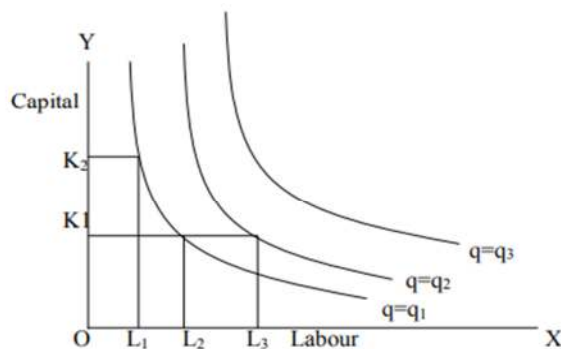
In Market economy, profits and losses play a predominant role in growth and development of every producer.

32.

<b>Substitute goods</b>	<b>Complementary goods</b>
<ul style="list-style-type: none"> <li>• These are alternative goods available to satisfy our wants.</li> <li>• If the price of a product increases, the demand for its substitute also increases.</li> <li>• Example for substitute goods are Tea and Coffee, Colgate and Pepsodant, etc.</li> <li>• Here the demand curve shifts to the right in case of price rise.</li> <li>• Price and demand move in same direction.</li> </ul>	<ul style="list-style-type: none"> <li>• These are the goods which are consumed together.</li> <li>• If the price of a product increases, the demand for its complementary good decreases.</li> <li>• Example for complementary goods are Pen and Ink, Shoes and socks etc</li> <li>• Here the demand curve shifts to left in case of price rise.</li> <li>• Price and demand move in opposite directions.</li> </ul>

33. An isoquant is the set of all possible combinations of the two inputs that yield the same maximum possible level of output. Each isoquant represents a particular level of output and is labelled with that amount of output. It is just an alternative way of representing the production function.

The concept of isoquant can be explained with the help of following diagram:



The above diagram generalizes the concept of isoquant. In the above diagram, labour is measured in OX axis and Capital is measured in OY axis. There are 3 isoquants for the three output levels viz.,  $q=q_1$ ,  $q=q_2$  and  $q=q_3$ . Two input combinations ( $L_1, K_2$ ) and ( $L_2, K_1$ ) give us the same level of output  $q_1$ . If we fix capital at  $K_1$  and increase labour to  $L_3$ , output increases and we reach a higher isoquant  $q=q_2$ . When Marginal products are positive, with greater amount of one input, the same level of output can be produced only using lesser amount of the other. Therefore, isoquants curves slope downwards from left to right (negatively sloped).

34. Price Ceiling: The Government imposed upper limit on the price of a good or service is called price ceiling. Price ceiling is generally imposed on necessary items like wheat, rice, kerosene, sugar and it is fixed below the market determined price. It is fixed below the market price because, at market determined price some sections of the population will not be able to afford these goods.

Here, though the intention of the Government is to help the consumers, it could end up creating shortage of products. In order to solve the scarcity of products, the Government may issue ration coupons to the consumers so that no individual can buy more than a certain amount of a product. This stipulated amount of a product sold through ration shops are

called Fair Price Shops.

35. 1. Micro Economics study in individual units so its scope is narrow.

Macro Economics study in aggregates, so its scope is wider.

2. The Micro Economics follows slicing method as it studies individual unit.

The Macro Economics follows lumping method as it studies in Aggregates

3. Example for micro economics are; Consumer behaviour.

Example for macro economics are: National income, unemployment

36. An externality is a cost or benefit conferred upon second or third parties as a result of acts of individual production and consumption. But the cost or benefit of an externality cannot be measured in money terms because it is not included in market activities.

In other words, Externalities refer to the benefits or harms a firm or an individual causes to another for which they are not paid or penalized. They do not have any market in which they can be bought and sold.

There are two types of externalities viz.,

- Positive Externalities and
- Negative Externalities.

For example, let us imagine that there is chemical fertilizer industry. It produces the chemical fertilizers required for agriculture. The output of the industry is taken for counting GDP of an economy. This is positive externality.

While carrying out the production the chemical fertilizer industry may also be polluting the nearby river. This may cause harm to the people who use the water of the river. Hence their health will be affected. Pollution also may kill fish and other organisms of the river. As a result, the fishermen of the river may lose their livelihood. Such harmful effects that the industry is

inflicting on others, for which it will not bear any cost are called negative externalities.

37. Money acts as a convenient unit of account. The value of all goods and services can be expressed in monetary units. This monetary unit is called price.

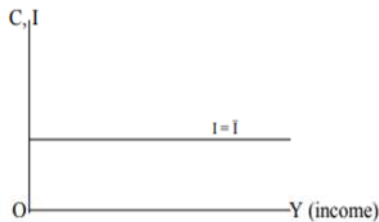
When we say the value of a certain wrist watch is rs. 500 we mean that the wrist watch can be exchanged for 500 units of money., where a unit of money is rupee in this case. If the price of the pencil is rs. 2 and that of a pen is rs 10 we can calculate the relative price of a pen with respect to a pencil. The same notion can be used to calculate the money itself with respect to other commodities.

Thus if prices of all commodities increase in terms of money the value in terms of any commodity must have decreased. We call it a deterioration in purchasing power of money.

38 The functional relationship between investment and autonomous investment is called autonomous investment.

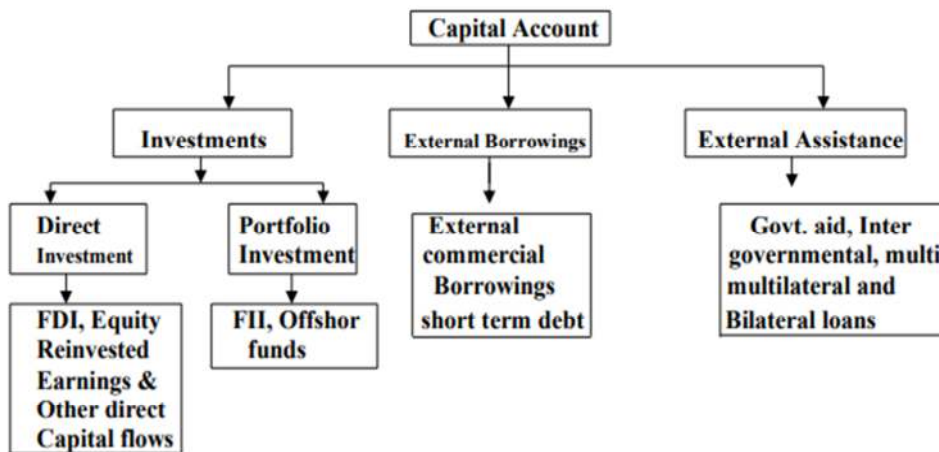
$$I = I_0$$

Where  $I_0$  = investment  $I_0$  is a positive constant which represents the autonomous investment in the economy in a given year.



In this model,  $I_0$  is autonomous which means, it is the same no matter whatever is the level of income.

39.



#### Part D

Vii Answer the following questions in 20 sentences each

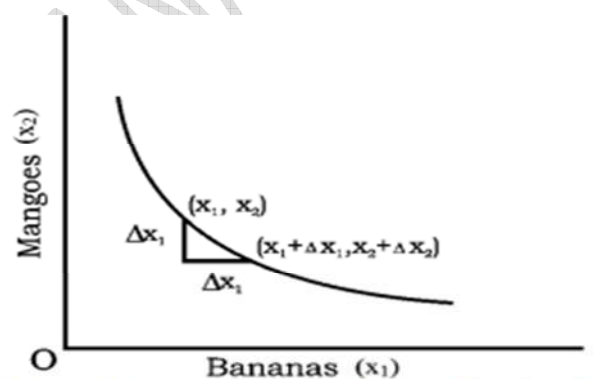
40. Features of Indifference Curve:

The main features of the indifference curve are as follows:

1. Indifference curve slopes downwards from left to right.
2. Higher indifference curve gives greater level of utility.
3. Two indifference curves never intersect each other.

1. Indifference curve slopes downwards from left to right:

An indifference curve slopes downwards from left to right because, the consumer in order to have more of one product, he has to forego some units of other product. This can be explained with the help of diagram



The indifference curve slopes downwards



The indifference curve slopes downward. An increase in the amount of bananas along the indifference curve is associated with a decrease in the amount of mangoes. If  $\Delta x_1 > 0$  then  $\Delta x_2 < 0$ .

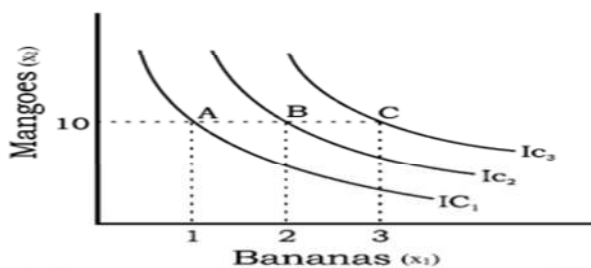
2. Higher indifference curve gives greater level of utility:

Combinations A, B and C consist of same quantity of mangoes but different quantities of bananas. Since combination B has more bananas than A, B will provide the individual a higher level of satisfaction than A.

Therefore, B will lie on a higher indifference curve than A, depicting higher satisfaction.

Likewise, C has more bananas than B (quantity of mangoes is the same in both B and C).

Therefore, C will provide higher level of satisfaction than B, and also lie on a higher indifference curve than B.



As long as marginal utility of a commodity is positive, an individual will always prefer more of that commodity, as more of the commodity will increase the level of satisfaction i.e.,  $IC_1 < IC_2 < IC_3$ .

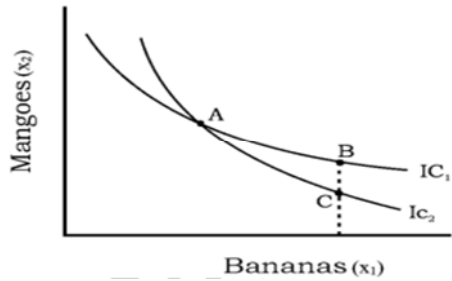
3. Two indifference curves never intersect each other:

Two indifference curves intersecting each other will lead to conflicting results.

☐ To explain this, let us allow two indifference curves to intersect each other as shown in the figure. As points A and B lie on the same indifference curve  $IC_1$ , utilities derived from combination A and combination B will give the same level of

satisfaction.

Similarly, as points A and C lie on the same indifference curve IC<sub>2</sub>, utility derived from combination A and from combination C will give the same level of satisfaction.



From this, it follows that utility from point B and from point C will also be the same. But this is clearly an absurd result, as on point B, the consumer gets a greater number of mangoes with the same quantity of bananas.

So, consumer is better off at point B than at point C. Therefore, it is clear that intersecting indifference curves will lead to conflicting results. Thus, two indifference curves cannot intersect each other

41. Total revenue is the revenue earned from the sale of all units of a product. A firm gets revenue by the sale of good that it produces in the market. Total revenue of a firm can be defined as the market price of a good by the quantity of output it sold.

$$TR = p \cdot q$$

Where, TR= Total revenue p=price q= firms output.

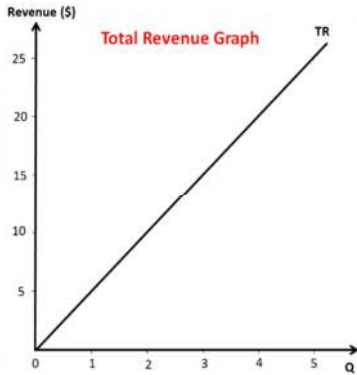
Average Revenue of a firm can be defined as total revenue per unit of output.

$$AAR = TR/Q = p \cdot q / q = p$$

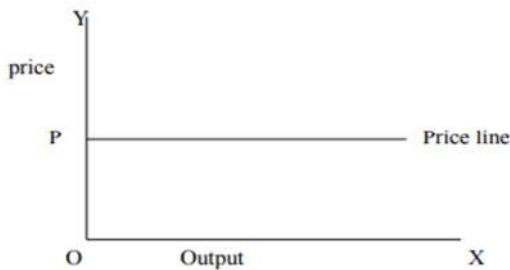
Where AR= Average Revenue TR= Total Revenue q= firms output.

Quantity sold	TR	MR	AR
0	0	-	-
1	10	10	10
2	20	10	10
3	30	10	10
4	40	10	10
5	50	10	10
6	60	10	10

Total revenue curve of a firm shows the relationship between the total revenue that the firm earns and the output level of a firm. The slope of the curve,  $Aq_1/Oq_1$  is the market price. Therefore, the slope of the straight line is  $Aq_1/Oq_1=p$



Here, we plot the average revenue for the different values of a firm's output. Since the market price is fixed at  $p$ , we obtain a horizontal straight line that cuts the  $y$  axis at a height equal to  $p$ . This horizontal straight line is called price line.



42. The macroeconomic identities are as follows:

a) Gross Domestic Product (GDP): Gross Domestic Product measures the aggregate production of final goods and services taking place within the domestic economy during a year. But the whole of it may not accrue to the citizens of the country. It includes GDP at Market prices and GDP at Factor cost.

GDP at market price is the market value of all final goods and services produced within a domestic territory of a country measured in a year. Here everything is valued at market prices. It is obtained as follows:

$$\text{GDPMP} = C + I + G + X - M$$

GDP at factor cost is gross domestic product at market prices minus net indirect taxes. It measures money value of output produced by the firms within the domestic boundaries of a country in a year.

$$\text{GDPFC} = \text{GDPMP} - \text{NIT}$$

b) Gross National Product: It refers to all the economic output produced by a nation's normal residents, whether they are located within the national boundary or abroad. It is defined as GDP plus factor income earned by the domestic factors of production employed in the rest of the world minus factor income earned by the factors of production of the rest of the world employed in the domestic economy. Therefore,

$$\text{GNP} = \text{GDP} + \text{Net factor income from abroad}$$

c) Net National Product (NNP): A part of the capital gets consumed during the year due to wear and tear. This wear and tear is called depreciation. If we deduct depreciation from GNP the measure of aggregate income that we obtain is called Net National Product. We get the value of NNP evaluated at market prices. So,

$$\text{NNP} = \text{GNP} - \text{Depreciation}$$

d) Net National Product (NNP) at factor cost: The NNP at factor is the sum of income earned by all factors in the production in the form of wages, profits, rent and interest etc., belong to a country during a year. It is also known as National income. We need to add subsidies to NNP and deduct indirect taxes from NNP to obtain NNP at factor cost.

$$\text{NNPFC} = \text{NNP at market prices} - \text{indirect taxes} + \text{subsidies}$$

e) Personal Income (PI): It refers to the part of National income (NI) which is received by

households. It is obtained as follows:

$PI = NI - \text{Undistributed Profits} - \text{Net interest payments made by the households} - \text{Corporate tax} + \text{Transfer payments to the households from the Government and firms.}$

f) Personal Disposable Income (PDI): If we deduct the personal tax payments (income tax) and Non-tax payments (fines, fees) from Personal Income, we get PDI. Therefore,

$PDI = PI - \text{Personal tax payments} - \text{Non-tax payments}$

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$PDI = PI - \text{Personal tax payments} - \text{Non-tax payments.}$

43. The open market operations as one of the tools of RBI to control money supply, refers to buying and selling of bonds issued by the Government in the open market. This purchase and sale is entrusted to the RBI on behalf of the Government.

When RBI buys a Government bond in the open market, it pays for it by giving a cheque. This cheque increases the total amount of reserves in the economy and thus increases the money supply. Similarly, selling of a bond by RBI to private individuals or institutions leads to reduction in quantity of reserves and money supply.

There are two types of open market operations. They are as follows:

a) Outright: Outright open market operations are permanent in nature. When the RBI buys the securities, it is without any promise to sell them later. Similarly, when the RBI sells these securities, it is without any promise to buy them later. As a result, the injection/absorption of the money is of permanent nature.

b) Repo: This is another type of operation in which the RBI buys the security with agreement of purchase on particular date and price. This is called repo. The interest rate at which the money is lent in this way is called repo rate.

Similarly, instead of outright sale of securities the RBI may sell the securities through an agreement which as a specification about the date and price at which it will be repurchased. This type of agreement is called reverse repo. The rate at which the money is withdrawn in this manner is called the reverse repo rate.

The RBI conducts repo and reverse repo operations at various maturities like overnight, 7 days, 14 days etc. These types of operations have now become the main tool of monetary policy of the RBI

44. The public expenditure can be classified as follows:

- Revenue Expenditure
- Capital Expenditure

Revenue Expenditure: It is the expenditure of government spent on the purposes other than the creation of physical or financial assets. It is incurred for the normal functioning of the government departments and various services, interest payments, grants given to state governments and other parties. The revenue expenditure consists of the following:

- Plan Revenue expenditure; and
- Non-plan revenue expenditure.

The plan revenue expenditure is related to central plans and central assistance for state

and union territory plans.

The non plan revenue expenditure is the more important component of revenue expenditure. It covers a vast range of general, economic and social services of the government.

The main items of non-plan expenditure are interest payments, defence services, subsidies, salaries and pensions.

Capital Expenditure: The capital expenditure of the government includes the expenditures which result in creation of physical or financial assets or reduction in financial liabilities. This includes expenditure on the acquisition of land, building, machinery, equipment, investment in shares, and loans and advances by the central government to state and union territory governments, public sector undertakings (PSUs) and other parties.

The capital expenditure is categorized as follows:

- Plan capital expenditure and
- Non-plan capital expenditure

The plan capital expenditure is related to central plan and central assistance for state and union territory plans.

The non-plan capital expenditure covers various general, social and economic services provided by the government.

#### Part E

VIII Answer the project oriented questions;

45. Consumer income  $M = \text{Rs. } 20$

Price of Bananas  $P_1 = \text{Rs. } 5$

Price of Mangoes  $P_2 = \text{Rs. } 10$

(a) No. of Bananas  $= 20/5 = 4$

(b) No. of Mangoes  $= 20/10 = 2$

(c) Slope of budget line is downward.

(d) Yes, the bundles on the budget line are equal to the consumer's income.

(e) True. If we want to have more of banana we have to give up mangoes.

46.

<b>Labour</b>	<b>TP</b>	<b>MP1</b>	<b>AP1</b>
0	0	-	-
1	10	10	10
2	24	14	12
3	40	16	13.33
4	50	10	12.5
5	56	6	11.2
6	57	1	9.5

47. USA - U.S. Dollars

UK - Pound sterling

Germany - Euro

Japan – Japanese Yen

China - Renminbi

Argentina – Argentina Peso

UAE - UAE Dirham

Bangladesh - Bangladeshi Taka

Russia - Russian Ruble.