Roll Number		

Code Number:30/1

ANSWER KEY

INDIAN SCHOOL MUSCAT
THIRD PRELIMINARY EXAMINATION
ECONOMICS

CLASS: XII Sub. Code: 030 Time Allotted: 3 Hrs

04.02.2018 Max. Marks: 80

SECTION A (MICRO ECONOMICS)

1 a) Distribution Of national product should be equal or unequal (Ans) 1

2 Ans: cardinal utility – can be measured Ordinal – Utility can be ranked 1

3 a) Marginal utility curve (Ans) 1

4 Ans: A consumer prefer a bundle which has more of one good and no less of the other good , compared to all bundles then preferences are monotonic. 1

5 Ans: Use of modern technology reduces the cost and increases the supply. 3

Or

Reduction of the GST will reduce the cost of production and increases the supply

6 Ans: What type of goods to be produced and what quantities,- limited resources have alternative uses. 3

7 Ed = (-) Percentage change in Quantity demanded/percentage change in price 4

Percentage change in price = 6-5/5 x 100 = 1/5 x 100 = 20%

Percentage change in demand = -10%

Ed = (-) -10%/20% = 0.5

8 When MPP is greater than average product, APP increases 4

When APP is at its maximum and constant both the MPP and APP are equal.

When MPP is less than APP, APP falls

When MPP falls & is negative, APP falls but remains positive

Or

(i)<u>Initially</u> when output increases **<u>MC decreases reaches its minimum</u>** point &**<u>then increases</u>** throughout these output levels <u>MC is less than AC</u>,

so MC pulls AC downwards &<u>AC decreases</u>

When MC<AC, AC FALLS

***(ii)** When MC is equal to AC, AC is at its minimum point

MC=AC, AC =Minimum

9 Ans: In this market there are <u>few large sellers</u> selling <u>homogenous or differentiated</u> good. <u>Firms are mutually interdependent for deciding prices</u> either competitively or through 4

competition. There is restricted entry into and exit from the market.
Collusive oligopoly – In this type of oligopoly firms decide price of goods through mutual cooperation with each other by forming groups or cartels.

10 Ans: 6

- If Market price (e.g.: OP_1)is less than equilibrium price
  Then quantity demanded (P_1M) is more than quantity supplied (P_1N) , so Excess Demand equal to NM occurs.
  Buyers will compete with each other and some buyers will be willing to pay higher prices to get the good.

Sellers will increase prices, hence quantity demanded falls and quantity supplied rises. Price is again raised. This process continues till the excess demand gets wiped out and equilibrium price is reached where, quantity demanded = quantity supplied = OQ_2.

11 ***The Marginal Cost (MC) of the firm must be equal to its Marginal Revenue (MR).*** 6

The firm attains equilibrium at point E & output OQ_3 *earns maximum profit (maximum profit = area* E_1 *TE) when its MC is equal to MR.*
It is an essential condition b'cozwhen MC<MR below OQ_1 *level of output, the firm still expects to get moreprofits;*
& when MC>MR before OQ_1 & after OQ_3 *level of output , the firm gets loss as it spends more than what it earns from the extra unit.*
2. ***The Marginal Cost (MC) must be greater than MR after the equilibrium point, i.ebeyond*** *equilibriumlevel of output maximum profits decline****.***
MC must intersect MR from below but not from above. If the MC intersects from above of the MC curve i.e. MC>MR, then it implies that the firm was already facing loss & further production will accrue profits to the firm. Moreover, the question of maximizing profits does not arise as the firm was getting losses on the production of previous units of the good.
MC &MR

12 1. **Budget set**:- It refers to **attainable combinations** of a set of two goods, given prices of goods and income of the consumer. 6
   Budget line(price line):- It is a line showing different possible combinations of good-1 and good-2, which a consumer can buy, given his budget and the prices of good-1 and good-2. Anywhere, on the budget line, a consumer is spending his entire income either on good-1 or on good-2 or on both

SECTION B (MACRO ECONOMICS)

13 Deposit can withdraw at any time 1

14 a) Average propensity to Consume. (Ans) 1

15 Actual AD is more than full employment output. 1

16 a) Both A and C (Ans) 1

17 **Reallocation of resources –** The government seeks to reallocate with a view to balance the goals of profit maximization and social welfare. A production of goods which are injurious to health like wine is discouraged through heavy taxation. On the other hand production of socially useful goods like Khadi is encouraged through subsidies. 3

18 3

- **Foreign Dependence:** Government also borrows from the rest of the world, which results in economic interdependence on them & economic interference by the lending countries. It causes economic slavery, if the lending county dictates its terms on the borrowing country.
- **Causes Inflation:** The government resort to borrowing from the Reserve Bank of India (RBI) to meet its fiscal deficit. It is done by '**Deficit Financing'** Or ' **Monetisation of Debt**' , Which means RBI prints currency 7 gives it to Govt. to finance debt. This increases the circulation of money in the economy and creates inflationary pressure, if there is excess supply of money.
- **Restricts Economic Development:** When Govt. has to borrow to finance deficits, to repay loans and interest on loans, less money is left with the Govt. for economic development.

19 Ans: Bank rate is the rate at which Central Bank lends funds to commercial banks. 4

If bank rate increases:

* Cost of borrowing from RBI increases.
* So banks borrow less
* Their credit giving ability decreases.
* Banks also increase lending rates i.e. rate at which they lend to public.
* This discourages businessmen from taking loans. This reduces volume of credit and money supply.

A decrease in bank rates on the other hand will increase credit and money supply.

Or

- Central Bank has monopoly over issue of notes (currency). Coins and one rupee note are issued by Government of India but Central Bank puts currency notes &coins into circulation and withdraws it from circulation. Issue of notes is monetary liability of Central Bank as it backs currency by assets of equal value gold coins, gold bullions, foreign securities & domestic government's local currency securities.

20 i) Investment multiplier Ans: 5 4

ii) Change in income Ans: 2000

21 Calculate Gross National Product at Factor cost: 4

ITEMS Rs. (Arab)

No. Of units produced	120
Price per unit	Rs. 80
Changes in stock	1200
Purchase of raw material	1860
Subsidy	100
Consumption of fixed capital	40
Net Factor Income to Abroad	(- 75)
Import of raw material	150

22 Ans: GDP deflator 6

Real GDP or GDP at constant prices or GDP at base year prices	Nominal GDP or GDP at market prices or GDP at current year prices
1. It is the monetary value of all goods and services produced in an economy during a financial year, estimated using base year prices.	1. It is the monetary value of all goods and services produced in an economy during a financial year, estimated using current market prices.
2. Base year price is taken as constant.	2. Market prices do not remain constant.
3. This GDP changes only due to change in output of the economy. So it is a reliable measure of economic growth.	3. It changes due to change in both price and output of the economy. So it is not a reliable measure of economic growth.

23 Ans In **accounting terms** BOP **always balances** because it is based on double-entry book keeping system and the sum of credit side is always equal to sum of debit side items. 6
The individual items in BoP may not balance but the total credits of the country must be equal to total debits.
A deficit or surplus in current account is balanced by surplus or deficit in capital account.
If there is difference between the autonomous items, it would be settled by accommodating items which are intended to balance the BoP. Hence Balance of payment always balances.
Disequilibrium occurs in BOP in **economic terms.**

When sum of credit side of autonomous items is more than sum of debit side then there is

surplus in BOP

Correction of surplus in BOP in done by monetary authority by increasing reserves of gold,

foreign exchange with RBI and increasing SDRS held with the IMF (International monetary fund)

24 Ans: Income starts from zero but Consumption never starts from zero because minimum consumption equal to **Autonomous consumption** is necessary for survival 6

(1) When income =0 {Y=0},
When income is zero negative saving occurs,
Because minimum consumption for Survival is done,by reducing assets or savings
Consumption =c^ (autonomous consumption), &S=-c^(negative autonomous consumption)
(2) When (income)< (Consumption),{Y<C}
S is negative
(3) When (income)= (Consumption), Y= C
S is zero
(4)When (income) > (Consumption), Y>C
S is positive

Or

(1) Equilibrium occurs at income, employment and output level
Where, AD=AS=200 =OY2At point E

Planned spending = Planned Output

Adjustment mechanism when AD & AS are not equal
(2) At income, employment and output level **below equilibrium level** of income
AD >AS For eg. $Y_1M>Y_1R$

If planned spending > Planned output

Consumer & firms together are buying more than what firms are producing

So undesired or unplanned decrease in inventories occurs

i.e inventories reduce
Producer will **increase production**.
Employment& income also **rise**, till equilibrium is reached. Where, AD=AS=200
(3) At income, employment and output level **above equilibrium level** of income
AD <AS, $Y_3T<Y_3N$

If Exante i.e. Planned spending < Planned output

Consumers & Firms are buying less than what firms are producing
Unplanned increase inventories of unsold good occurs
inventories rise
Producer will **decrease production**.
Employment& income also **fall**, till equilibrium is reached. Where, AD=AS