2019
ECONOMICS

Time : 3 Hours   Maximum Marks   80

Instructions for the Candidates :

- Please check that this question paper contains _____ printed pages .

- Code Number given on the right hand side of the question paper should be written on the title pages of the answer book by the candidate .

- Please check that this question paper contains 23 questions .

- Please write down the Serial Number of the question before attempting it .

- 15 Minutes time has been allotted to read this question paper .

General Instructions:

- All questions in both the sections are compulsory.

- Marks for questions are indicated against each question.

- Question Nos. 1 – 4 and 13 -16 are very short-answer question carrying 1 mark each. They are required to be answered in one sentence each.

- Question Nos. 5 – 6 and 17 – 18 are short-answer questions carrying 3 mark each. Answer to them should normally not exceed 60 words each.

- Question Nos. 10 – 12 and 22 – 24 are long-answer questions carrying 6 marks each. Answer to them should normally exceed 100 words each.

- Answers should be brief and to the point and the above word limits should be adhered to as far as possible.

SECTION – A

Q 1. In the given figure X_1Y_1 and X_2Y_2 are Production Possibility Curve in two different periods T_1 and T_2 respectively for Good X and Good Y. A_1 and A_2 represent actual outputs and P_1 and P_2 represent potential outputs respectively in the two time periods. **[1 Marks]**
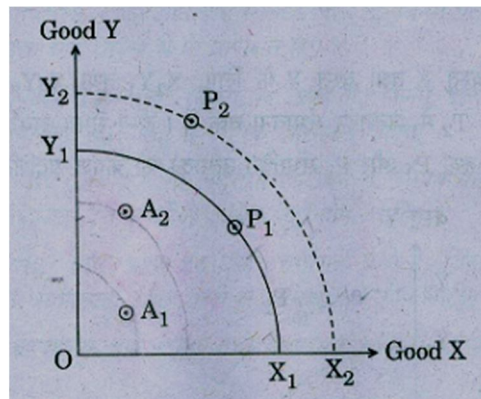
The change in actual output of Goods X and Y over the two periods would be represented by movement from _____ . (Fill up the blanks)

(a) A_2 to P_2 (b) A_1 to P_2 (c) P_1 to A_2 (d*) A_1 to A_2

OR

The Marginal Rate of Transformation (MRT) is constant. The Production Possibility Curve, so formed, would be _____ to the origin. (Fill up the blank)

Ans. Straight Line.

Q 2. If the supply curve is a straight line parallel to the vertical axis (Y-axis), supply of the good is called as_____ . (Fill up the blank) **[1 Marks]**

(a) Unitary Elastic Supply   (b) Perfectly Elastic Supply

(c) Perfectly Inelastic Supply   (d) Perfectly Elastic Demand

Ans. (c)

Q 3. Under imperfect competition, Average Revenue (AR) remains _____ Marginal Revenue (MR). (Fill up the blank) **[1 Marks]**

OR

"For a firm to be in equilibrium, Marginal Revenue (MR) and Marginal Cost (MC) must be _____ and beyond that level of output Marginal Cost must be _____". (Fill up the blank). **[1 Marks]**

Ans. Greater than   or   Equal, Rising

Q 4. The Total Revenue earned by selling 20 units is ₹ 700. Marginal Revenue earned by selling 21st Unit is ₹ 70. The value of Total Revenue earned by selling total 21 units will be _____ . (Choose the correct alternative) **[1 Marks]**

(a) ₹ 721   (b) ₹ 630   (c) ₹ 770   (d) ₹ 720

Ans. (c) Rs. 770

Q 5. Discuss briefly the concept of normative economics, with suitable example. **[3 Marks]**

Ans. Normative Economics tells us "what ought to be". Normative Economics deals with what ought to be or how the economic problems should be solved . For example, India should not be an overpopulated country or prices should not rise. Normative Economics discusses what are desirable things and should be realised and what are undesirable things and should be avoided. It gives decisions regarding value judgements .

Q 6. Explain the law of diminishing marginal utility, with the help of a hypothetical schedule. **[3 Marks]**

Ans. Law of diminishing marginal utility states that the utility of each successive unit goes on diminishing as more and more units of a commodity is consumed, when units of other commodities remains constant.

Assumptions :

– Rational behaviour of consumer.

– Cardinal measurability of utility.

– Utility can be measured by money and marginal utility of money remains constant.

– Income and mental status of consumer are assumed to be remains constant during the act of consumption .

– Price of commodity, price of other commodities, income of consumer and other factors that can affect the utility are assumed to be remain constant.

Q	MU
1	6
2	4
3	2
4	0
5	-2

Explanation of the law : Initially as the consumer increases the consumption marginal utility decreases but it is positive (as in our example from first to third unit of the commodity marginal utility decreases from 6 to 2) After certain units consumer reaches to a point where utility from additional unit becomes zero or marginal utility curve intersects the X axis (as in our example at fourth unit of the commodity marginal utility becomes 0). This represents the point of complete satisfaction. If consumer further increases the consumption of the commodity then utility derived from additional units will becomes negative means the consumer is deriving negative utility or disutility from the additional units of the commodity (as in our example at fifth unit of the commodity marginal utility further decreases and becomes negative 2).

OR

Elaborate the law of demand, with the help of a hypothetical schedule. **[3 Marks]**

Ans. **According to law of demand,** "More quantity is demanded due to fall in price and less quantity is demanded due to rise in price, when other things remains constant." Thus law of demand shows the negative relationship between price of a commodity and its quantity demanded. According to law of demand, demand of a commodity is a function of its price .

Dx = f (Px)

here, Dx = Demand of X commodity, Px = Price of X commodity

Assumptions of law of demand :

(i)   Price of other related goods remains constant.

(ii)   Income of the consumer remains unchanged.

(iii)   Psychological factors like habits, taste, preferences of the consumers remains constant.

(iv)   There is no expectation about the future price changes, etc.

Explanation of the law

P_x	D_x
10	100
20	80
30	60

According to law of demand shows the inverse relationship between price of concerned commodity and its quantity demanded. This inverse relationship can be seen in demand schedule and demand curve. The negative slope of the demand curve is due to the inverse relationship between price of the commodity and quantity demanded. When the price of commodity was OP the consumer was demanding OQ units of the commodity. As the price rises to OP_1 the demand falls to OQ_1 (which is contraction in demand) and as the price falls to OP_2 the demand rises to OQ_2 (which is expansion in demand).

Q 7.   Which of the following statement are true or false ? Give valid reasons in support of your answer.

    (a)   Average cost curve cuts Average variable cost curve, at its minimum level.

    (b)   Average product curve and Marginal product curve are 'U-shaped' curves.

    (c)   Under all market conditions, Average revenue and Marginal revenue are equal to each other.

    (d)   Total cost curve and Total variable cost curve are parallel to each other.   **[4 Marks]**

Ans.   **(a)**   **False :** AC and AVC curves are 'U' shaped curve. The vertical gap between AC and AVC curves represents AFC. As we know that with the increase in output, AFC continuously decreases, therefore with the increase in output the vertical gap between AC and AVC curves continuously decrease but never intersect.

    (b)   **False :** Average Product curve and Marginal product curve are inverse U-Shaped curves.

    (c)   **False :** In only perfect competition market average revenue and marginal revenue are equal to each other, not under all market conditions.

    (d)   **True :** The vertical gap between TC and TVC is remains constant because this vertical gap represents TFC and as we know that TFC remains the same or constant with the increase in output . Therefore the vertical gap between TC and TVC curve remains same and both curves are parallel to each other.

<center>**OR**</center>

    Explain a firm's equilibrium under perfect competition using a hypothetical schedule.

<div align="right">**[4 Marks]**</div>

Ans.   "The firm's equilibrium refers to the situation in which producer maximizes his profits (or minimizes his loss) and the producer has no intention to make any changes in his existing production or to make any changes in his existing expenditure on means of production". Profit of the firm operating in perfect competition market, is maximised where the price line (AR = MR) intersects the MC curve and MC should be rising.

Conditions for producer's equilibrium :

(a) MR = MC.

(b) MC should be rising at that level of output .

(or MC curve intersects MR curve from below).

Assumptions :

(i) Rational behaviour of producer.

(ii) The goal of producer is profit maximisation.

(iii) Price of commodity remains constant.

(iv) Price of means of production remains constant.

(v) There is perfect competition exist in market.

(vi) Technique of production and management remains constant.

Q	P/AR/MR	MC
1	20	15
2	20	10
3	20	15
4	20	20
5	20	25
6	20	30

If the producer is producing 4 units of commodity then MR is equal to MC. Which means that the cost incurred on producing additional unit is equal to the revenue received from the sale of that unit, which indicates that the producer is receiving normal profit on that unit but the total profit is maximum. So producer will maintain this level of output for maximum profit. At this level MR = MC and MC is rising at that level of output .

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Q 8. (a) The coefficient of price elasticity of demand for Good X is (—) 0.2. If there is a 5% increase in the price of the good, by what percentage will the quantity demanded for the good fall ?

(b) Arrange the following coefficient of price elasticity of demand in ascending order :

(—) 3.1, (—) 0.2, (—) 1.1 **[4 Marks]**

Ans.

(a) $e_d = \dfrac{\% \text{ change in quantity demanded}}{\% \text{ change in price}}$
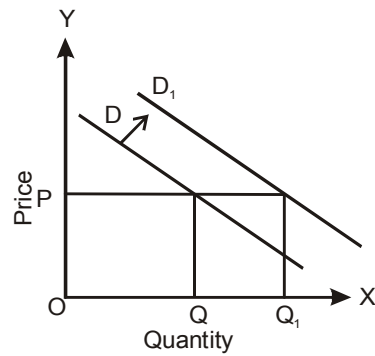
$-0.2 = \dfrac{\% \text{ change in quantity demanded}}{5\%}$

% change in quantity demanded = 1%

(b) (—) 3.1, (—) 1.1, (—) 0.2

OR

How would the demand for a commodity be affected by a change in "taste and preference" of the consumers in favour of the commodity ? Explain using a diagram. **[4 Marks]**

Ans.

Change in taste and preferences of consumer : If the taste, habit or preferences of consumer changes in favour of the commodity then demand of such commodity will increases and demand curve will shift rightwards.

Q 9. The market for a good is in equilibrium. Explain, using a diagram, how an improvement in technology for producing the good would affect the equilibrium price and equilibrium quantity, keeping other factors constant. **[4 Marks]**

Ans. As the an improvement in technology for producing the good, supply of the commodity also increases. Which results in the rightward shift of supply curve. Due to increase in supply and demand remains constant the equilibrium price will decrease and equilibrium quantity will increases.
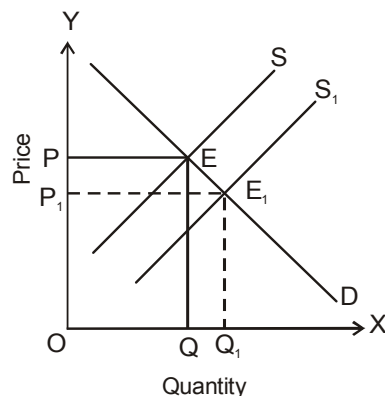
In the present diagram D and S are respectively initial demand and supply curves. 'E' is the initial equilibrium point where equilibrium price is OP and equilibrium quantity is OQ. As the input improvement in technology supply curve shifts rightwards (due to increase in supply) and becomes S_1. Due to that equilibrium point shifts to E_1 and equilibrium price falls to OP_1 and equilibrium quantity rises to OQ_1 .

Q 10. (a)   What is meant by increasing returns to a variable factor ?   **[2 + 4 Marks]**
        (b)   Discuss briefly, any two reasons for the decreasing returns to a variable factor.

Ans. (a)   In short run period, when other factors of production remains constant, if the proportionate change in TP is greater than the proportionate change in units of a variable factor, it is said to be law of increasing returns to a variable factor *or* In

short run period when other factors remains constant, if MP increases with the increase in units of a variable factor, then it is known as law of increasing returns to a variable factor.

(b) **(i)** **Decrease in level of efficiency :** If we increase the units of variable factors too much with fixed factors of production (after optimum combination), then the factor proportion becomes more and more worse. Due to that efficiency of both the factors decreases (because we are moving away from ideal combination). That's why AP and MP both decreases. Due to that AC and MC both increases.

(ii) **Imperfect substitute :** At the point of optimum combination of means of production average and marginal productivity can be increased by substituting fixed factor (because at this point fixed factor is completely utilised). But the factors of production are not perfect substitutes, therefore it is not possible to replace fixed factor with other factor and that's why, if we have to increase the output at optimum combination then we have to increase the units of variable factor with the same units of fixed factor. As a result there will be over utilisation of fixed factor, so AP and MP both decreases and AC and MC both increases. So ultimately decreasing returns will applies.

Q 11. (a) "A firm under perfect competition is a price taker, whereas a firm under monopoly is a price maker." Defend or refute the given statement with valid reasons.

(b) What is meant by "product differentiation" ? Explain with example. **[1 Marks]**

Ans. **(a)** **The statement is correct**. In the **perfect competition market,** every firm will only accept the price of the commodity which is determined by the powers of market demand and market supply in the market or industry.

The firms are adopting the dependent price policy, because they are producing a very minute fraction of the total supply of the market. They have no control over the prices. No firm can adopt its independent price policy. The firm will only adjust its production according to prices of the market. None of the firm is ready to sale the product below this price and none of the buyer is ready to pay more than this price.

Whereas, In **monopoly market** there is only one producer of the commodity, therefore that producer is supplying 100 % of that commodity, means he is controlling the entire supply of the market. Therefore that firm can effect the Price and Supply of the Market .

The firm adopts independent price policy, firm can increase or decrease the price of its commodity. Firms have full control over the price and therefore it is termed as price maker.

(b) When there is a difference between the commodities produced by different firms then it is known as product differentiation. This difference may be of colour, shape, size, weight, taste, texture, trademark, brandname, packing, etc. Goods produced by different firms are similar but not identical. There is mark of

identification on commodity so that the consumer or producer can differentiate. Therefore consumers show personal attachment with particular firms. This feature of market can be found in monopolistic competition or oligopoly market. For e.g. Toothpaste, Soap etc.

There are variety of Toothpaste available in the market which has difference in taste brandname, packing, colour, size etc.

Q 12. Explain the following conditions:

  (a) Movement along the same indifference curve.

 (b) Shift from a lower to a higher indifference curve.   **[3 + 3 Marks]**

Ans. (a) All the points along the same indifference curve represents all those combination of two commodities which provides the same level of satisfaction to the consumer. Level of satisfaction remains constant whether **we move upward or downward along the same indifference curve.** Consumer is neutral or indifferent among these combinations because he does not prefer any one combination over the other.
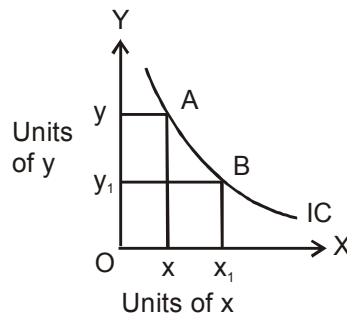
   In the present diagram, combination A (OX + OY) provides the satisfaction equal to combination B (OX_1 + OY_1).

  (b) Curves nearer to origin represents lower level of satisfaction and curves which are away from origin represent higher level of satisfaction. Means as we move away from origin, level of satisfaction continuously increases.
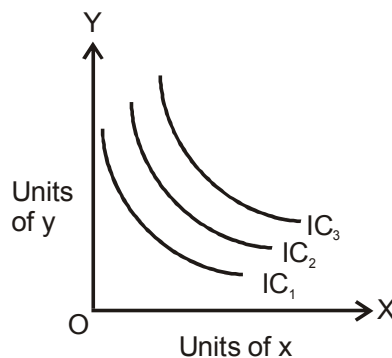
   In the present diagram IC_2 represents higher level of satisfaction in comparison to IC_1 and in the same way IC_3 represents satisfaction more than IC_1 and IC_2.

   So if there are three indifference curves in a single diagram then they will represents three different level of satisfaction.

Explain the Law of Equi-Marginal Utility. **[6 Marks]**

Ans. Consumer is said to be in the state of equilibrium when he is attaining maximum satisfaction out of his limited income and he has no tendency to make any changes in his existing consumption.

Suppose the consumer wants to purchase more than one commodity from his given monetary income. Then according to law of Equi-marginal utility the consumer will be in the state of equilibrium when the ratio between marginal utility and price of one commodity must be equal to the ratio between marginal utility and price of other commodities. In other words the law of equi-marginal utility states that the consumer should incur expenditure on different commodities in such a manner that the utility derived from last rupee spent on last unit of each commodity must be equal.

Assumptions : **Consumer's equilibrium is based on following assumptions :**
(i) The consumer is assumed to be rational. His aim is to achieve maximum satisfaction through his limited monetary income.
(ii) Utility derived from the consumption of commodity can be expressed in numbers, such as 1, 2, 3, 4 etc.
(iii) It is assumed that utility of commodity can be measured by money and marginal utility of money remains constant.
(iv) Income and mental status of consumer remains constant during the act of consumption.
(v) Price of concerned commodity and price of other commodities remains constant.
(vi) Units of concerned commodity are homogenous.
(vii) It is assumed that law of diminishing marginal utility operates for the commodities consumed.
(viii) Other factors which can affect utility are assumed to be remain constant.

Conditions for consumer's equilibrium :-
(i) The ratio between marginal utility and price of one commodity must be equal to the ratio between marginal utility and price of other commodities.

$$\frac{MU_X}{P_X} = \frac{MU_y}{P_y} = \text{.....................} = \frac{MU_n}{P_n}$$

(ii) Total expenditure should be equal to total income.

$$(P_x \times Q_x) + (P_y \times Q_y) + \text{............} + (P_n \times Q_n) = \text{Monetary Income}$$

Here, MU = Marginal utility;
P = Price of commodity;
Q = Quantity of commodity

Explaination of the law :
The law of equi-marginal utility explain the consumer's equilibrium when he is consuming many commodities. Suppose there are only two commodities X and Y, which a consumer wants to purchase with his limited monetary income.

According to **Marshall, "If a person has a thing which can be put to several uses, will distribute it among these uses in such a way that it has the same marginal utility in all."** In other words consumer is in equilibrium when marginal utility of money spent on each commodity is equal. Marginal utility of money being spent on a commodity is equal to the marginal utility of the commodity divided by the price of commodity.

Suppose the income of consumer and respective prices of X and Y commodities are as follows :-

Q	MUx	MUx/Px	MUy	MUy/Py
1	80	20	80	16
2	72	18	70	14
3	64	16	60	12
4	56	14	50	10
5	48	12	40	8
6	40	10	30	6

let $P_x = ₹ 4/Q$ $P_y = ₹ 5/Q$ Income = ₹ 35

Conditions of consumer's equilibrium :

(i)   At 5th unit of X commodity $\dfrac{MU_X}{P_X} = \dfrac{48}{4} = \dfrac{12}{1}$

   At 3rd unit of Y commodity $\dfrac{MU_y}{P_y} = \dfrac{60}{5} = \dfrac{12}{1}$

   Therefore $\dfrac{MU_X}{P_X} = \dfrac{MU_y}{P_y} = $ ....(i)

(ii)   Total expenditure   = $(P_x \times Q_x) + (P_y \times Q_y)$
                                 =   (4 X 5) + (5 X 3)   = ₹ 35

Therefore ,   Total income = Total expenditure   ....(ii)

So both the conditions of consumer's equilibrium is satisfied here. Therefore the consumer will buy 5 units of X commodity and 3 units of Y commodity to achieve maximum satisfaction from his limited monetary income. If the consumer derives greater utility from any one commodity relatively, then the consumer will shift his resources from other commodity to that commodity, in order to achieve higher level of satisfaction.

SECTION – B

(MACRO ECONOMICS)

13.   In order to encourage investments in the economy, the Central Bank may _____.   **[1 Marks]**

   (Choose the correct alternative).

   (a)   Reduce Cash Reserve Ratio   (b)   Increase Cash Reserve Ration

   (c)   Sell Government securities in open market   (d)   Increase Bank Rate

Ans.   (a)   Reduce Cash Reserve Ratio

14.   Define 'money multiplier'.   **[1 Marks]**

Ans.   When the primary cash deposits in the banking system leads to multiple expansion in the total deposits, it is called money multiplier.

$$\text{Money multiplier} = \frac{\text{Total deposits}}{\text{primary cash deposits}} \text{ or } \frac{1}{\text{Legal reserve ratio}}$$

15. Primary deficit in a government budget will be zero, when _____ . **[1 Marks]**

(Choose the correct alternative).

(a) Revenue deficit is zero   (b) Net interest payments are zero

(c) Fiscal deficit is zero   (d) Fiscal deficit is equal to interest payment

Ans. (d) Fiscal deficit is equal to interest payment

16. What do you mean by an indirect tax ? **[1 Marks]**

Ans. When the liability to pay and burden of a tax lie on same person, is treated as a Direct Tax. Ex-Income Tax, Corporation Tax etc.

OR

What do you mean by an indirect tax ?

Ans. When the liability to pay and burden of a tax lie on different person, is treated as a Indirect Tax. Ex-GST.

17. State the impact of "Excess Demand" under the Keynesian theory on employment, in an economy.

[3 Marks]

Ans. Excess Demand is not a desired situation because it does not lead to any increase in level of aggregate supply as the economy is already at full employment level. Excess demand has the following effect on output, employment and general price level:

1. **Effect on Output :** Excess demand does not affect the level of output because economy is already at full employment level and there is no ideal capacity in the economy.

2. **Effect on Employment :** There will be no change in the level of employment as the economy is already operating at full employment equilibrium and there is no involuntary unemployment.

3. **Effect on General Price Level :** Excess demand leads to rise in the general price level (known as inflation) as aggregate demand is more than aggregate supply.

OR

State the meaning of the following : **[3 Marks]**

(a) Ex-Ante Savings

(b) Full Employment

(c) Autonomous Consumption

Ans. **(a)** **Ex-ante saving :** The saving which the firms or entrepreneur desire to maker in the economy during a period is called ex-ante (planned savings).

(b) **Full employment** refers to the situation when all the workers who are willing and able to work at prevailing wage rate are actually employed.

(c) **Autonomous consumption :** When income is zero, consumption is not zero because consumption can never be zero even at zero level of income; there are some basic needs which need to be fulfilled even at zero level of income and to fulfil those basic needs we use past savings. This consumption at zero level of income is termed as "**Autonomous consumption"** and is denoted as $\bar{C}$.

18. Estimate the change in final income if Marginal Propensity to Consume (MPC) is 0.75 and change in initial investment is ₹ 2,000 crores. **[3 Marks]**

Ans.

$$K = \frac{1}{1 - MPC} \qquad\qquad K = \frac{\Delta Y}{\Delta I}$$

$$K = \frac{1}{1 - 0.75} \qquad\qquad 4 = \frac{\Delta Y}{2,000}$$

$$K = 4 \qquad\qquad\qquad \Delta Y = 8,000 \text{ crores}$$

19. "Higher Gross Domestic Product (GDP) means greater per capita availability of goods in the economy." Do you agree with the given statement ? Give valid reason in support of your answer.

[4 Marks]

Ans. As the Gross Domestic Product Increases, availability of goods and services also increases. But it is not always true to say that per capita availability of goods in the economy increases with the Increase in Gross Domestic Product. It is only possible when rest of the factors which can affect the welfare are assumed to be remains constant. Means there are some **Limitations of Real GDP as an Index of per capita availability of goods, such as :**

(i) **Growth of Population :** If the growth rate of population is more than the growth rate of GNP, then the per capita real GDP and economic welfare decreases even with the increase in output.

(ii) **Change of Composition of National Income :** If the production of War Material or Capital Goods increases in comparison to Consumer Goods , then it will Decreases the capita availability of goods.

(iii) **Distribution of National Income:** If the distribution of National income becomes unequal with the increase in National income then it will decrease economic welfare.

(iv) **Government Expenditure on Law and Order and Defence :** Expenditure on law and order and defence is termed as non–development expenditure. These expenditure does not promote economic welfare of the masses, but it will increase the National income etc.

OR

Explain the meaning of Real Gross Domestic Product and Nominal Gross Domestic Product, using a numerical example.

Ans. **Real Gross Domestic Product :** It refers to money value of final goods and services produced in a country in a year, measured at price of base year. It is a better tool for measuring the economic growth of a country . It is generally used for comparing the GDP of different years.

Real GDP.= Base year Price (P_O) × Current Quantity (Q_1) .

Nominal Gross Domestic Product : It refers to money value of final goods and services produced in a country in a year, measured at current year prices. It is not a good tool for measuring the economic

growth of a country. It is affected by change in both price and quantity. It is not a suitable tool for comparing the GDP of different years.

Nominal GDP. = Current Price (P_1) × Current Quantity (Q_1)

For example -

				Base year = 2015
Year	Bread (Units)	Price of Bread (₹)	Nominal GDP	Real GDP
2015	1,000	10,	1,000 × 10 = 10,000	1,000 × 10 = 10,000
2016	1,000	20	1,000 × 20 = 20,000	1,000 × 10 = 10,000
2017	1,200	15	1,200 × 15 = 18,000	1,200 × 10 = 12,000

From above example we learn that compared to 2015, there is no change in real GDP in 2016 and there is only 20 per cent rise in the real GDP of 2017. Because the price is held constant, real GDP varies from year to year only if the quantities produced vary and thus, real GDP provides a better measure of economic well being than nominal GDP.

20. Discuss briefly the "credit controller" function of a Central Bank. **[4 Marks]**

Ans. **Controller of Money Supply and Credit :** The Central Bank controls the money supply and credit in the best interests of the economy. By this central bank can control inflationary and deflationary situation in the economy. Central bank uses various instruments to perform this function which can be categorised in -

(a) **Qualitative instruments** such as margin requirement, moral suasion, consumer credit, rationing of credit, differentiated rate of interest and direct action.(aims to influence the use of credit and direction of credit).

(b) **Quantitative instruments** such as bank rate, open market operations, CRR and SLR.(aims at controlling cost of credit and availability of credit).

21. Classify the following statements as revenue receipts or capital receipts. Give valid reasons in support of your answer. **[4 Marks]**

(a) Financial help from a multinational corporation for victims in a flood affected area.

(b) Sale of shares of a Public sector Undertaking (PSU) to a private company, Y Ltd.

(c) Dividends paid to the Government by the State Bank of India.

(d) Borrowings from International Monetary Fund (IMF).

Ans. **(a)** **Revenue receipt,** it is a kind of transfer receipt.

(b) **Capital receipt,** It is an example of Dis-investment. It reduced the assets of the government therefore, it is a Capital Receipts.

(c) **Revenue receipt,** it neither creates liability nor reduced the assets for the government therefore it is Revenue Receipts.

(d) **Capital Receipts,** it creates liability for the government therefore it is Capital Receipts

22. Define the following : **[6 Marks]**

(a) Value Addition (b) Gross Domestic Product

(c) Flow Variables (d) Income from property and entrepreneurship

Ans. **(a)** **Value Addition** is the contribution of the enterprise to the current flow of goods and service. In other words, value added can be defined as the difference between value of output of a firm in a n accounting year and value of inputs brought from other firms (or value of intermediate consumption).

Value added = Value of Output – Value of Inputs

(b) **Gross Domestic Product (GDP) :** Gross Domestic Product (GDP) is the market value of all the final goods and services produced within the domestic territory of a country during a year.

(c) **Flow Variables :** A flow is a quantity of any economic variable which is measured during a period of time (or per unit of time) say, a week, a month or a year. For example, monthly wages of a worker, the per hour speed of a train, production of cloth during a year etc.

(d) **Income from property and entrepreneurship** in the form of rent, royalty, interest and profit is termed as operating surplus.

    (i) **Income from Property :** There are two principal forms of the income from property : (a) rent and royalty and (b) interest.

    (ii) **Income from Entrepreneurship (Profit) :** Profit is a residual factor payment to the owners of an enterprise.

OR

Given the following data, find the values of "Gross Domestic Capital Formation" and "Operating Surplus". **[6 Marks]**

S. No.	Particulars	Amount (₹ in crores)
(i)	National Income	22,100
(ii)	Wages and Salaries	12,000
(iii)	Private Final Consumption Expenditure	7,200
(iv)	Net Indirect Taxes	700
(v)	Gross Domestic Capital Formation	?
(vi)	Depreciation	500
(vii)	Government Final Consumption Expenditure	6,100
(viii)	Mixed Income of Self Employed	4,800
(ix)	Operating Surplus	?
(x)	Net Exports	3,400
(xi)	Rent	1,200
(xii)	Net Factor Income from Abroad	(—) 150

Ans. (i) $GDP_{MP} = NNP_{FC}$ + Depreciation – NFIA + NIDT

GDP_{MP} = 22100 + 500 – (- 150) + 700

GDP_{MP} = ₹ 23450

GDP_{MP} = Pvt. final consumption expenditure + Government Final consumption Expenditure + Gross Domestic Capital Formation + Net Export

23450 = 7200 + 6100 + x + 3400

X = 6750

Gross Domestic Capital Formulation = ₹ 6750

(ii) NOP_{FC} = COE + OS + MI
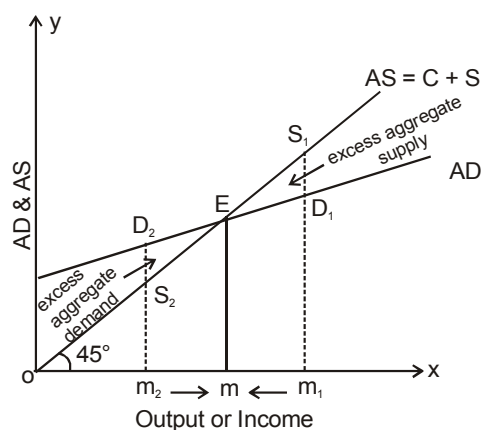
22250 = 12000 + OS + 4800

OS = ₹ 5450

NOP_{FC} = NNP_{FC} – NFIA

= 22100 – (-150)

= ₹ 22250

23. Discuss the adjustment mechanism in the following situation : **[6 Marks]**

(a) Aggregate demand is lesser than Aggregate Supply.

Ans.

When Aggregate Demand is Less than Aggregate Supply it means Consumers and Firms buying goods less than Firm's Production, it increases inventories of unsold stock so firms decrease their production level consequently employment and output will also decrease and economy is back on equilibrium level where planned spending (AD) becomes equal to planned output (AS).

(b) Ex-Ante Investment are greater than Ex-Ante Savings.

Ans. **Ex-ante Investment is more than Ex-ante savings:** Suppose the industrialists wish to invest ₹ 50,000 crores while the family units makes a saving of ₹ 45,000 crores. In such a condition, the aggregate demand is more the aggregate supply. To supply this demand, the industrialists will use more raw material and more means of production to increase their production. This will lead to an increase in the national income, the saving and investment will become equal and a state of equilibrium will be achieved.

24. (a) Distinguish between 'Trade Deficit' and 'Current Account Deficit'. **[3 + 3 Marks]**

Ans. (a)

Trade Deficit'	Current Account Deficit
The difference between exports and imports of visible items is called Trade Balance. If imports exceed exports, it is regarded as Trade deficit.	Transactions relating to trade in goods and service and transfer payments constitute the current account. When current receipts are less than payments then it is regarded as current account deficit.
Trade deficit = Imports > Exports	Current Account deficit = Autonomous Current receipts < Autonomous Current payments
It's includes only visible items.	It's include only visible items, invisible items and unilateral transfer.

(b) Discuss briefly the concept of flexible exchange rate system of foreign exchange rate determination.

Ans. A system in which there is no official intervention in the determination of foreign exchange rate. The exchange rate is determined by the interaction of demand and supply of the foreign exchange market. It is known as flexible rate because it tends to change with the change in demand and supply of different currencies in foreign exchange market.

Demand of Foreign Exchange : Demand of foreign exchange means demand of foreign currencies. The demand curve of foreign exchange is downward sloping due to negative relationship between foreign exchange rate and demand of foreign exchange. The foreign exchange is demanded due to following reasons :

(a) To purchase goods and services from other countries.

(b) To send gifts or transfers to abroad.

(c) To invest in other countries.

(d) To speculate on the value of foreign currencies.

Supply of Foreign Exchange : Supply of foreign exchange means inflow of foreign currency from rest of the world. The supply curve of foreign exchange is upward sloping due to positive relationship between foreign exchange rate and supply of foriegn exchange. The foriegn exchange is supplied due to following reasons :

(a) Foreigners purchasing home country's goods and services through exports.

(b) Gifts or transfers received from abroad .

(c) Investment by non resident inside the domestic territory (Foreign Investment) .

(d) To speculate on the value of domestic currencies.
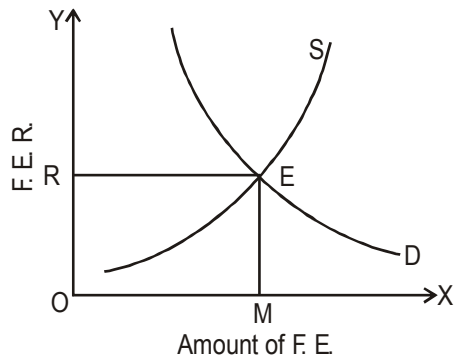
Amount of F. E.

Foreign Exchange Rate is determined at the rate where demand and supply of foreign exchange are equal. In the present graph amount of foreign exchange is shown on X axis and foreign exchange rate is shown on Y axis. D and S curve respectively represents demand and supply of foreign exchange. At 'OR' exchange rate demand and supply of foreign exchange are equal (which is shown by OM). Therefore this exchange rate will be determined in the market. If demand and supply of foreign exchange changes then this exchange rate will also changes.