CUET-UG Economics Sample Paper-10

Duration: 1 Hour **Maximum Marks: 250**

Instructions

- This paper contains a total of 50 Multiple Choice Questions.
- Each correct answer carries **+5 marks**.
- Each incorrect answer carries **-1 mark**.
- No negative marking for unattempted questions.

Q1. Explain the central problem of an economy and discuss how the problem of "what to produce" is resolved in a market economy with the help of demand and price mechanism.

(A) Through government planning only

(B) Through price mechanism based on demand and supply

(C) Through random allocation of resources

(D) Through fixed production quotas

Q2. Discuss the law of demand and analyze the effect of a fall in price of a normal good on consumer equilibrium using indifference curve approach.

(A) Income effect only

(B) Substitution effect only

(C) Both income and substitution effects

(D) No effect on equilibrium

Q3. A consumer consumes two goods X and Y. Explain how consumer reaches equilibrium using marginal rate of substitution (MRS) and budget constraint, and analyze what happens when price of good X decreases.

(A) MRS increases indefinitely

(B) Consumer equilibrium remains unchanged

(C) Consumer shifts to higher indifference curve

(D) Budget line shifts inward

Q4. Explain the concept of price elasticity of demand and analyze how availability of close substitutes and proportion of income spent affect elasticity of demand for a commodity.

(A) Demand becomes perfectly inelastic

(B) Demand becomes more elastic

(C) Demand becomes unitary elastic

(D) Demand becomes perfectly elastic

Q5. Using indifference curve analysis, explain the decomposition of price effect into substitution effect and income effect for a normal good and interpret the final change in quantity demanded.

(A) Only substitution effect exists

(B) Only income effect exists

(C) Both reinforce each other

(D) Both cancel each other

Q6. Explain the law of variable proportions and analyze the stages of production with respect to marginal product and total product curves in short run production.

(A) Only increasing returns stage exists

(B) Only diminishing returns stage exists

(C) Three stages of production

(D) No relationship between inputs and output

Q7. A firm increases labour while keeping capital fixed. Analyze how marginal product of labour behaves and explain the economic rationale behind diminishing returns.

(A) MPL increases continuously

(B) MPL remains constant

(C) MPL eventually decreases

(D) MPL becomes zero immediately

Q8. Explain the concept of cost in economics and distinguish between fixed cost and variable cost. Analyze their behavior in short run production.

(A) Both vary with output

(B) Fixed cost varies, variable cost constant

(C) Fixed cost constant, variable cost varies

(D) Both remain constant

Q9. Discuss the relationship between average cost (AC) and marginal cost (MC) curves and explain why MC curve cuts AC curve at its minimum point.

(A) MC always above AC

(B) MC always below AC

(C) MC intersects AC at minimum

(D) No relation between AC and MC

Q10. Analyze the long run production function and explain returns to scale. Discuss increasing, constant, and decreasing returns with suitable economic interpretation.

(A) Output decreases always

(B) Output increases proportionally only

(C) Output may increase more, equal, or less than inputs

(D) Output remains constant

Q11. Explain the concept of perfect competition and analyze how price is determined under this market structure. Discuss why firms are price takers and how equilibrium price is established through industry demand and supply.

(A) Firms determine price individually

(B) Price is fixed by government

(C) Price is determined by industry demand and supply

(D) Price is random

Q12. A perfectly competitive firm faces a horizontal demand curve. Explain why marginal revenue equals price and analyze the profit maximization condition using $MR = MC$ rule.

(A) $MR < MC$

(B) $MR = MC$

(C) $MR > MC$

(D) No relation between MR and MC

Q13. Explain the short run equilibrium of a firm under perfect competition and analyze different situations of supernormal profit, normal profit, and losses using cost curves.

(A) Firm always earns supernormal profit

(B) Firm always incurs losses

(C) Firm may earn profit, loss, or normal profit

(D) Firm never reaches equilibrium

Q14. Discuss the long run equilibrium of a perfectly competitive firm and explain why firms earn only normal profits in the long run due to free entry and exit of firms.

(A) Firms earn supernormal profit permanently

(B) Firms earn only normal profit in long run

(C) Firms incur losses in long run

(D) Firms stop production

Q15. Explain the concept of market equilibrium and analyze how equilibrium price and quantity are determined through interaction of demand and supply curves.

(A) Only demand determines price

(B) Only supply determines price

(C) Both demand and supply determine equilibrium

(D) Price is fixed externally

Q16. Analyze the effect of an increase in demand on equilibrium price and quantity, assuming supply remains constant. Explain the adjustment mechanism in the market.

(A) Price falls and quantity decreases

(B) Price rises and quantity increases

(C) Price remains constant

(D) Quantity decreases only

Q17. Explain the concept of circular flow of income in a two-sector economy and analyze how households and firms interact to determine national income.

(A) Only firms determine income

(B) Only households determine income

(C) Interaction of households and firms determines income

(D) Government determines income

Q18. Discuss the concept of Gross Domestic Product (GDP) and differentiate between GDP at market price and GDP at factor cost with suitable explanation.

(A) Both are always equal

(B) GDP at MP includes net indirect taxes

(C) GDP at FC includes taxes

(D) No difference exists

Q19. Explain the expenditure method of measuring national income and analyze the role of consumption, investment, government expenditure, and net exports.

(A) Only consumption is counted

(B) Only investment is counted

(C) Sum of all expenditures is counted

(D) Only exports are counted

Q20. Differentiate between nominal GDP and real GDP and explain how price changes affect the measurement of economic growth.

(A) Both measure same growth

(B) Nominal GDP ignores price changes

(C) Real GDP adjusts for inflation

(D) Real GDP includes only services

Q21. Explain the concept of value added method and discuss how double counting is avoided while calculating national income.

(A) By counting all outputs repeatedly

(B) By ignoring intermediate goods

(C) By adding taxes only

(D) By counting exports only

Q22. Discuss the limitations of GDP as a measure of welfare and explain why higher GDP does not necessarily imply higher economic well-being.

(A) GDP measures welfare perfectly

(B) GDP ignores income distribution and environment

(C) GDP includes only consumption

(D) GDP excludes production

Q23. Explain the functions of money and analyze its role as a medium of exchange, unit of account, and store of value in modern economies.

(A) Only medium of exchange

(B) Only store of value

(C) Performs multiple functions

(D) Has no economic role

Q24. Discuss the process of credit creation by commercial banks and explain how multiple expansion of deposits takes place.

(A) Banks destroy money

(B) Banks only store money

(C) Banks create multiple deposits

(D) No credit creation occurs

Q25. Explain the role of central bank in controlling money supply using tools like repo rate, CRR, and open market operations.

(A) Central bank cannot control money

(B) Uses monetary policy tools

(C) Controls only taxes

(D) Controls only exports

Q26. Analyze the concept of money multiplier and explain how reserve ratio affects the total money supply in the economy.

(A) Higher reserve ratio increases money supply

(B) Lower reserve ratio increases money supply

(C) No relation exists

(D) Money supply remains constant

Q27. Explain the concept of government budget and differentiate between revenue budget and capital budget with suitable examples.

(A) No difference exists

(B) Revenue budget deals with daily expenses

(C) Capital budget deals with assets only

(D) Both B and C

Q28. Discuss different types of government deficits and explain the significance of fiscal deficit in economic policy.

(A) No deficits exist

(B) Only revenue deficit matters

(C) Fiscal deficit indicates borrowing requirement

(D) Deficits have no impact

Q29. Explain the role of taxation in government budget and analyze how taxes affect income distribution and economic growth.

(A) Taxes have no effect

(B) Taxes reduce inequality

(C) Taxes only increase prices

(D) Taxes affect only imports

Q30. Discuss the concept of balanced, surplus, and deficit budgets and analyze their impact on economic stability.

(A) Budget has no impact

(B) Only deficit budget exists

(C) All types affect economy differently

(D) Surplus budget harms economy always

Q31. Explain the concept of balance of payments and analyze its components—current account and capital account.

(A) Only current account exists

(B) Only capital account exists

(C) Both accounts form BOP

(D) No accounts exist

Q32. Discuss the determination of exchange rate under flexible exchange rate system and analyze how demand and supply of foreign exchange affect it.

(A) Exchange rate is fixed always

(B) Determined by demand and supply

(C) Determined by firms only

(D) Determined randomly

Q33. Explain the concept of foreign exchange reserves and discuss their importance in maintaining economic stability.

(A) No importance

(B) Helps in managing currency value

(C) Used only for imports

(D) Has no role in economy

Q34. Analyze the difference between depreciation and devaluation of currency and their impact on exports and imports.

(A) No difference exists

(B) Both reduce exports

(C) Depreciation increases exports

(D) Both increase imports

Q35. Explain the concept of aggregate demand and its components in an economy. Analyze how it determines the level of income and employment.

(A) Only consumption matters

(B) Only investment matters

(C) All components determine demand

(D) No relation with employment

Q36. Discuss the concept of aggregate supply and explain how it interacts with aggregate demand to determine equilibrium level of income.

(A) No interaction exists

(B) Only supply determines income

(C) Both AD and AS determine equilibrium

(D) Only demand matters

Q37. Explain the concept of multiplier and analyze how a change in investment leads to a multiple change in income.

(A) Multiplier reduces income

(B) Multiplier amplifies income change

(C) No effect exists

(D) Multiplier affects only prices

Q38. Discuss the concept of full employment equilibrium and explain how underemployment equilibrium can occur in an economy.

(A) Economy always at full employment

(B) Underemployment is impossible

(C) Equilibrium can exist below full employment

(D) Employment has no relation with income

Q39. Explain the role of government in correcting unemployment using fiscal policy and analyze its impact on aggregate demand.

(A) Government has no role

(B) Uses fiscal policy to increase demand

(C) Only monetary policy works

(D) Government reduces employment

Q40. Explain the objectives of economic planning in India after independence and analyze the role of Five-Year Plans in promoting growth and self-reliance.

(A) Only industrial growth

(B) Balanced growth and self-reliance

(C) Only agricultural growth

(D) No planning required

Q41. Discuss the role of public sector in India's development during 1947–90 and explain how it contributed to industrialization and infrastructure development.

(A) No role of public sector

(B) Only private sector developed economy

(C) Public sector led industrial growth

(D) Only agriculture was developed

Q42. Explain the strategy of import substitution adopted in India during the planning period and analyze its impact on domestic industries.

(A) Encouraged imports

(B) Discouraged domestic production

(C) Promoted domestic industries by restricting imports

(D) Had no effect

Q43. Explain the need for economic reforms in India in 1991 and analyze the role of LPG (Liberalization, Privatization, Globalization) policy in economic transformation.

(A) No reforms were needed

(B) Only liberalization was adopted

(C) LPG policy transformed economy

(D) Only privatization was implemented

Q44. Discuss the impact of globalization on Indian economy and analyze its effects on trade, employment, and economic growth.

(A) Reduced trade completely

(B) Increased global integration and growth

(C) No impact on economy

(D) Only reduced employment

Q45. Explain the problem of unemployment in India and analyze different types of unemployment such as disguised and seasonal unemployment.

(A) Only one type exists

(B) No unemployment in India

(C) Multiple types including disguised and seasonal

(D) Only urban unemployment exists

Q46. Discuss the issue of poverty in India and analyze the measures taken by the government to reduce poverty levels.

(A) Poverty does not exist

(B) Only economic growth reduces poverty

(C) Government schemes help reduce poverty

(D) No measures are taken

Q47. Explain the challenges of sustainable development in India and analyze the trade-off between economic growth and environmental protection.

(A) No environmental concerns

(B) Growth and environment are unrelated

(C) Need balance between growth and environment

(D) Only growth matters

Q48. Discuss the problem of human capital formation in India and analyze the role of education and health in economic development.

(A) No role of education

(B) Only physical capital matters

(C) Education and health improve productivity

(D) Human capital has no impact

Q49. Explain the agricultural sector challenges in India and analyze issues like low productivity, dependence on monsoon, and lack of infrastructure.

(A) Agriculture has no problems

(B) Only high productivity issues

(C) Multiple structural challenges exist

(D) Only industrial sector matters

Q50. Compare the development experience of India with China and Pakistan and analyze differences in growth strategies and outcomes.

(A) All countries followed identical strategies

(B) Only India developed

(C) Different strategies led to different outcomes

(D) No comparison possible

Detailed Solutions

Q1.

Solution

Concept: The central problem of an economy arises due to scarcity of resources and unlimited wants. The key questions are: what to produce, how to produce, and for whom to produce. In a market economy, the allocation of resources is guided by the price mechanism, where demand and supply determine prices. Producers respond to price signals and consumer preferences.

Solution: In a market economy, the problem of "what to produce" is resolved through the interaction of demand and supply. Goods that have higher demand fetch higher prices, encouraging producers to allocate more resources toward their production. Conversely, goods with lower demand receive fewer resources. Thus, consumer sovereignty plays a key role, as producers aim to maximize profits by producing what consumers prefer. The price mechanism ensures efficient allocation without central planning.

Final Answer: (B) Through price mechanism based on demand and supply

Answer: (B)

Q2.

Solution

Concept: The law of demand states that, ceteris paribus, quantity demanded increases when price falls. In indifference curve analysis, a fall in price leads to both substitution effect (consumer substitutes cheaper good) and income effect (real purchasing power increases), affecting consumer equilibrium.

Solution: When the price of a normal good falls, the budget line rotates outward, allowing the consumer to reach a higher indifference curve. The substitution effect makes the cheaper good more attractive compared to other goods, increasing its consumption. The income effect further increases consumption due to increased real income. Thus, both effects work in the same direction, leading to higher quantity demanded and a new equilibrium at a higher satisfaction level.

Final Answer: (C) Both income and substitution effects

Answer: (C)

Q3.

Solution

Concept: Consumer equilibrium is achieved when the marginal rate of substitution (MRS) between two goods equals the ratio of their prices, subject to the budget constraint. MRS reflects the consumer's willingness to substitute one good for another while maintaining utility.

Solution: A consumer reaches equilibrium where the budget line is tangent to the highest attainable indifference curve, i.e., $MRS = \frac{P_X}{P_Y}$. When the price of good X decreases, the budget line rotates outward, making X relatively cheaper. This leads to both substitution and income effects, causing the consumer to purchase more of X. Consequently, the consumer moves to a higher indifference curve, indicating an increase in overall satisfaction and improved equilibrium.

Final Answer: (C) Consumer shifts to higher indifference curve

Answer: (C)

Q4.

Solution

Concept: Price elasticity of demand measures responsiveness of quantity demanded to change in price. Factors like availability of close substitutes and proportion of income spent significantly influence elasticity. Goods with many substitutes are more elastic because consumers can easily switch. Similarly, if a commodity takes a large share of income, consumers respond strongly to price changes, increasing elasticity. Thus, both factors increase sensitivity of demand to price variations.

Solution: When close substitutes are available, consumers shift consumption easily if price rises, making demand elastic. For example, tea and coffee. Similarly, if a good consumes a large portion of income (like cars), even small price changes affect demand significantly. Hence elasticity increases. On the other hand, necessities with small income share remain inelastic. Therefore, both availability of substitutes and higher income proportion make demand more elastic.

Final Answer: Demand becomes more elastic

Answer: (B)

Q5.

Solution

Concept: In indifference curve analysis, price effect is divided into substitution effect and income effect. For a normal good, both effects work in the same direction. Substitution effect occurs due to relative price change, while income effect occurs due to change in purchasing power. Both jointly determine final change in quantity demanded and movement to a higher indifference curve.

Solution: When price of a normal good falls, substitution effect increases demand as the good becomes relatively cheaper. Income effect also increases demand because real income rises. Since both effects act in the same direction, total demand increases significantly. This leads to movement along the budget line and shift to a higher indifference curve. Thus, both substitution and income effects reinforce each other in case of normal goods.

Final Answer: Both reinforce each other

Answer: (C)

Q6.

Solution

Concept: The law of variable proportions explains short-run production where one factor varies while others remain fixed. It describes relationship between input and output through three stages: increasing returns, diminishing returns, and negative returns. These stages are analyzed using total product (TP) and marginal product (MP) curves.

Solution: Initially, better utilization of fixed factors leads to increasing returns (MP rises). In the second stage, diminishing returns occur as MP starts falling but remains positive. In the third stage, excessive input causes MP to become negative, reducing total output. Rational production occurs in stage II where TP is maximum and MP is positive but decreasing. Thus, production follows three distinct stages.

Final Answer: Three stages of production

Answer: (C)

Q7.

Solution

Concept: Marginal Product of Labour (MPL) refers to the additional output produced by employing one more unit of labour while keeping other factors fixed. According to the law of variable proportions, initially MPL increases due to better utilization and specialization, but after a point, it starts declining because fixed factors become insufficient. This leads to inefficiency and overcrowding of labour, causing diminishing returns in production.

Solution: When a firm increases labour with capital fixed, initially MPL rises due to improved coordination and division of work. However, after reaching an optimal level, additional labour causes congestion and overuse of fixed capital. As a result, each extra worker contributes less output than before. Hence, MPL eventually decreases. This reflects the law of diminishing returns, which is a fundamental principle in short-run production analysis.

Final Answer: MPL eventually decreases

Answer: (C)

Q8.

Solution

Concept: In economics, cost refers to the expenditure incurred in producing goods or services. Fixed costs are those which do not change with output (e.g., rent, salaries), while variable costs vary directly with production (e.g., raw materials, wages). In the short run, at least one factor is fixed, so costs are classified accordingly to understand production behavior.

Solution: Fixed costs remain constant regardless of the level of output, even when production is zero. On the other hand, variable costs increase as output increases because more inputs are required. In short-run production, total cost is the sum of fixed and variable costs. Thus, fixed cost is constant while variable cost varies with output, helping firms analyze cost efficiency and production decisions.

Final Answer: Fixed cost constant, variable cost varies

Answer: (C)

Q9.

Solution

Concept: Average Cost (AC) is the cost per unit of output, while Marginal Cost (MC) is the additional cost of producing one more unit. The relationship between AC and MC is crucial in cost analysis. MC influences AC: when MC is less than AC, AC falls; when MC is greater than AC, AC rises.

Solution: The MC curve intersects the AC curve at its minimum point because at that point MC equals AC. Before this point, MC is below AC, pulling the average down. After this point, MC is above AC, pushing the average up. Hence, the intersection occurs exactly at the lowest point of the AC curve, representing the most efficient level of production.

Final Answer: MC intersects AC at minimum

Answer: (C)

Q10.

Solution

Concept: In the long run, all factors of production are variable, and firms can change scale. Returns to scale describe how output responds when all inputs are increased proportionately. If output increases more than inputs, it is increasing returns; if proportionately, constant returns; and if less, decreasing returns. These arise due to economies and diseconomies of scale.

Solution: When inputs are doubled, output may more than double due to specialization and efficiencies (increasing returns). If output exactly doubles, production exhibits constant returns, reflecting balanced expansion. If output rises less than proportionately, decreasing returns occur due to managerial inefficiencies and coordination problems. Hence, output behavior varies depending on scale effects and technological conditions.

Final Answer: Output may increase more, equal, or less than inputs

Answer: (C)

Q11.

Solution

Concept: Perfect competition is a market structure with many buyers and sellers, homogeneous products, and free entry and exit. No single firm can influence price; hence firms are price takers. Price is determined by the intersection of industry demand and supply, representing equilibrium in the market.

Solution: In perfect competition, individual firms accept the market price because their output is too small to affect it. The equilibrium price is determined where industry demand equals industry supply. At this point, quantity demanded equals quantity supplied. Firms adjust output based on this price, ensuring efficient allocation of resources without external intervention.

Final Answer: Price is determined by industry demand and supply

Answer: (C)

Q12.

Solution

Concept: A perfectly competitive firm faces a horizontal demand curve because it sells at the market price. Hence, marginal revenue (MR) equals price (P). Profit maximization occurs where the difference between total revenue and total cost is maximum, which happens when MR equals MC.

Solution: Since the firm is a price taker, each additional unit sold adds the same amount to revenue, so $MR = P$. The firm maximizes profit at the level of output where $MR = MC$. If $MR > MC$, increasing output raises profit, while if $MR < MC$, reducing output minimizes losses. Thus equilibrium is achieved when $MR = MC$.

Final Answer: $\boxed{MR = MC}$

Answer: (B)

Q13.

Solution

Concept: Short run equilibrium of a perfectly competitive firm occurs where marginal revenue (MR) equals marginal cost (MC). In the short run, firms may earn supernormal profit, normal profit, or incur losses depending on the relationship between price (P) and average cost (AC). Cost curves like AC and MC help determine the firm's profit position.

Solution: If price is above AC, the firm earns supernormal profit. If price equals AC, it earns normal profit (break-even). If price is below AC but above AVC, the firm incurs losses but continues production. If price falls below AVC, the firm shuts down. Thus, in the short run, firms can operate under different profit conditions depending on market price and cost structure.

Final Answer: Firm may earn profit, loss, or normal profit

Answer: (C)

Q14.

Solution

Concept: In the long run, firms can freely enter or exit the market under perfect competition. This ensures that any supernormal profit attracts new firms, increasing supply and reducing price. Similarly, losses force firms to exit, reducing supply and increasing price, leading to equilibrium.

Solution: Due to free entry and exit, firms in the long run earn only normal profit. If firms earn supernormal profits, new firms enter the market, increasing supply and lowering price until profit becomes normal. If firms incur losses, some exit, reducing supply and raising price. Eventually, equilibrium is reached where price equals minimum average cost.

Final Answer: Firms earn only normal profit in long run

Answer: (B)

Q15.

Solution

Concept: Market equilibrium refers to a situation where quantity demanded equals quantity supplied. It is determined by the interaction of demand and supply curves. The equilibrium price is the price at which there is no excess demand or excess supply in the market.

Solution: The demand curve shows the quantity consumers are willing to buy at different prices, while the supply curve shows the quantity producers are willing to sell. Their intersection determines equilibrium price and quantity. At this point, market clears, and there is no tendency for price to change. Any deviation creates surplus or shortage, pushing the market back to equilibrium.

Final Answer: Both demand and supply determine equilibrium

Answer: (C)

Q16.

Solution

Concept: An increase in demand, with supply remaining constant, leads to a shift of the demand curve to the right. Market equilibrium is determined by the intersection of demand and supply. When demand increases, excess demand occurs at the original price, causing upward pressure on price and an increase in equilibrium quantity.

Solution: Initially, at the old price, quantity demanded exceeds quantity supplied, creating a shortage. This shortage pushes prices upward. As price rises, quantity supplied increases and quantity demanded decreases until a new equilibrium is established. Thus, both equilibrium price and quantity increase. This adjustment continues until demand equals supply again, restoring market balance.

Final Answer: Price rises and quantity increases

Answer: (B)

Q17.

Solution

Concept: Circular flow of income in a two-sector economy involves households and firms. Households provide factors of production to firms and receive income (wages, rent, interest, profit). Firms produce goods and services and sell them to households, creating a continuous flow of income and expenditure.

Solution: Households supply labour and other resources to firms and receive income in return. They use this income to purchase goods and services produced by firms. Thus, income flows from firms to households, and expenditure flows from households to firms. This interaction determines national income in the economy. It highlights interdependence between production and consumption sectors.

Final Answer: Interaction of households and firms determines income

Answer: (C)

Q18.

Solution

Concept: Gross Domestic Product (GDP) measures the total value of final goods and services produced within a country. GDP at market price (MP) includes indirect taxes and excludes subsidies, while GDP at factor cost (FC) excludes indirect taxes and includes subsidies.

Solution: GDP at MP reflects the price paid by consumers, which includes taxes like GST. GDP at FC reflects income earned by factors of production. The relationship is:

$$GDP_{MP} = GDP_{FC} + \text{Net Indirect Taxes}$$

Thus, GDP at MP includes net indirect taxes, while GDP at FC excludes them. This distinction helps in analyzing production and income separately.

Final Answer: GDP at MP includes net indirect taxes

Answer: (B)

Q19.

Solution

Concept: The expenditure method measures national income by summing total spending on final goods and services in an economy. It includes consumption (C), investment (I), government expenditure (G), and net exports (X–M). This approach reflects aggregate demand and shows how different sectors contribute to economic activity.

Solution: Under this method, national income is calculated as:

$$GDP = C + I + G + (X - M)$$

Consumption represents household spending, investment includes capital formation, government expenditure covers public spending, and net exports measure external trade balance. By adding all these expenditures on final goods, we obtain total income generated in the economy. Thus, it captures overall economic activity effectively.

Final Answer: Sum of all expenditures is counted

Answer: (C)

Q20.

Solution

Concept: Nominal GDP measures output using current prices, while real GDP measures output using constant prices, adjusting for inflation. This distinction helps in understanding actual economic growth without the distortion caused by price changes.

Solution: Nominal GDP may increase due to either higher output or higher prices. Real GDP removes the effect of price changes by using base-year prices, thus reflecting true growth in output. When inflation rises, nominal GDP increases even if production remains unchanged. Therefore, real GDP is a better indicator of economic growth as it adjusts for inflationary effects.

Final Answer: Real GDP adjusts for inflation

Answer: (C)

Q21.

Solution

Concept: The value added method calculates national income by summing the value added at each stage of production. Value added is the difference between value of output and value of intermediate goods. This method ensures that each stage contributes only its net addition to output.

Solution: Double counting occurs when intermediate goods are counted multiple times. To avoid this, only value added at each stage is included. Alternatively, only final goods are counted. For example, wheat, flour, and bread are not counted separately in full; only the final product or incremental value is considered. This prevents overestimation of national income.

Final Answer: By ignoring intermediate goods

Answer: (B)

Q22.

Solution

Concept: GDP measures the total value of goods and services produced, but it is not a perfect indicator of welfare. It ignores factors like income distribution, environmental degradation, non-market activities, and quality of life. Economic well-being depends on broader social and economic conditions beyond production levels.

Solution: A rise in GDP may not improve welfare if income is unevenly distributed or if production harms the environment. GDP does not include household work, leisure, or social welfare indicators. For example, pollution may increase GDP but reduce quality of life. Thus, higher GDP does not necessarily imply higher well-being, as it overlooks important qualitative aspects of development.

Final Answer: GDP ignores income distribution and environment

Answer: (B)

Q23.

Solution

Concept: Money is a crucial component of modern economies and performs several functions: medium of exchange, unit of account, store of value, and standard of deferred payments. These functions facilitate smooth economic transactions and efficient allocation of resources.

Solution: As a medium of exchange, money eliminates the problem of barter. As a unit of account, it provides a common measure of value. As a store of value, it allows individuals to save purchasing power for future use. These multiple roles make money essential for economic stability and growth, supporting trade, investment, and financial planning.

Final Answer: Performs multiple functions

Answer: (C)

Q24.

Solution

Concept: Commercial banks create credit through the process of accepting deposits and lending a portion of them while keeping reserves. This leads to multiple expansion of deposits in the banking system, known as credit creation.

Solution: When a bank receives deposits, it keeps a fraction as reserve and lends the rest. The loaned amount is deposited again in another bank, which repeats the process. This chain continues, leading to multiple creation of deposits. The total expansion depends on the reserve ratio. Thus, banks do not just store money but actively create credit, increasing money supply in the economy.

Final Answer: Banks create multiple deposits

Answer: (C)

Q25.

Solution

Concept: The central bank controls money supply through monetary policy tools such as repo rate, Cash Reserve Ratio (CRR), and open market operations (OMO). These tools influence liquidity, credit availability, and interest rates in the economy to maintain stability and control inflation.

Solution: Repo rate is the rate at which the central bank lends to commercial banks; increasing it reduces borrowing and money supply. CRR is the proportion of deposits banks must keep with the central bank; higher CRR reduces lending capacity. Open market operations involve buying or selling government securities to inject or absorb liquidity. Through these tools, the central bank effectively regulates money supply.

Final Answer: Uses monetary policy tools

Answer: (B)

Q26.

Solution

Concept: Money multiplier refers to the ratio of total money supply to initial deposits. It shows how banks create multiple deposits through lending. The reserve ratio plays a key role, as it determines how much banks can lend from deposits.

Solution: The money multiplier is given by:

$$\text{Multiplier} = \frac{1}{\text{Reserve Ratio}}$$

If the reserve ratio is low, banks can lend more, increasing money supply significantly. Conversely, a high reserve ratio restricts lending and reduces money creation. Thus, money supply is inversely related to reserve ratio, making it a crucial tool for controlling liquidity in the economy.

Final Answer: Lower reserve ratio increases money supply

Answer: (B)

Q27.

Solution

Concept: Government budget is an annual financial statement showing estimated receipts and expenditures. It is divided into revenue budget and capital budget. Revenue budget deals with recurring income and expenses, while capital budget relates to assets, liabilities, and long-term investments.

Solution: Revenue budget includes revenue receipts (like taxes) and revenue expenditure (like salaries, subsidies). Capital budget includes capital receipts (like loans, disinvestment) and capital expenditure (like infrastructure investment). Revenue budget reflects day-to-day operations, while capital budget focuses on asset creation and financial planning. Thus, both components together give a complete picture of government finances.

Final Answer: Both B and C

Answer: (D)

Q28.

Solution

Concept: Government deficits include revenue deficit, fiscal deficit, and primary deficit. Fiscal deficit is the most comprehensive measure, showing the gap between total expenditure and total receipts excluding borrowings. It reflects the borrowing requirement of the government and is crucial for macroeconomic policy.

Solution: Revenue deficit indicates excess of revenue expenditure over revenue receipts. Fiscal deficit includes total borrowing needed to finance expenditure. A high fiscal deficit implies increased government borrowing, which may lead to inflation or debt burden. However, it can also stimulate growth during recession. Thus, fiscal deficit plays a key role in balancing growth and stability.

Final Answer: Fiscal deficit indicates borrowing requirement

Answer: (C)

Q29.

Solution

Concept: Taxation is a major source of government revenue and an important fiscal policy tool. It helps in resource mobilization, redistribution of income, and influencing economic activities such as consumption, saving, and investment.

Solution: Progressive taxation reduces income inequality by imposing higher taxes on higher income groups. Taxes also influence economic growth by affecting disposable income and investment decisions. While high taxes may discourage production, well-structured taxation promotes equity and development. Thus, taxation plays a dual role in improving income distribution and supporting economic growth.

Final Answer: Taxes reduce inequality

Answer: (B)

Q30.

Solution

Concept: Government budgets can be balanced, surplus, or deficit. A balanced budget has equal receipts and expenditure, a surplus budget has higher receipts than expenditure, and a deficit budget has higher expenditure than receipts. Each type has different economic implications.

Solution: A deficit budget can stimulate economic growth during recession by increasing spending. A surplus budget helps control inflation by reducing demand. A balanced budget maintains stability. Thus, governments use different budget types depending on economic conditions to maintain stability, control inflation, and promote growth.

Final Answer: All types affect economy differently

Answer: (C)

Q31.

Solution

Concept: Balance of Payments (BOP) is a systematic record of all economic transactions between residents of a country and the rest of the world over a period. It consists of two main components: the current account and the capital account, which together reflect a country's external economic position.

Solution: The current account records transactions related to trade in goods and services, income, and transfers. The capital account records financial transactions such as foreign investments, loans, and capital flows. A surplus or deficit in BOP indicates the country's economic interaction with the global economy. Both accounts together provide a complete picture of international transactions.

Final Answer: Both accounts form BOP

Answer: (C)

Q32.

Solution

Concept: Under a flexible exchange rate system, the value of a currency is determined by the forces of demand and supply in the foreign exchange market. Demand for foreign currency arises from imports and investments abroad, while supply comes from exports and foreign investments.

Solution: If demand for foreign exchange increases, the domestic currency depreciates. If supply increases, the domestic currency appreciates. The equilibrium exchange rate is determined where demand equals supply. This system allows automatic adjustment in external imbalances without government intervention, making exchange rates responsive to market conditions.

Final Answer: Determined by demand and supply

Answer: (B)

Q33.

Solution

Concept: Foreign exchange reserves are assets held by a country's central bank in foreign currencies. These reserves include foreign currency, gold, and international financial assets, and are used to manage exchange rates and ensure economic stability.

Solution: Foreign exchange reserves help stabilize the domestic currency by allowing the central bank to intervene in foreign exchange markets. They also ensure the country can meet international payment obligations and handle economic shocks. Adequate reserves build investor confidence and protect against external crises, making them crucial for maintaining overall economic stability.

Final Answer: Helps in managing currency value

Answer: (B)

Q34.

Solution

Concept: Depreciation and devaluation both refer to a fall in the value of domestic currency, but depreciation occurs under a flexible exchange rate due to market forces, while devaluation is a deliberate policy action under a fixed exchange rate system by the government or central bank.

Solution: When currency value falls, exports become cheaper for foreign buyers, increasing export demand, while imports become expensive, reducing import demand. Depreciation happens automatically due to excess demand for foreign currency, whereas devaluation is a policy tool. Both improve trade balance, but depreciation specifically reflects market adjustment. Hence, depreciation leads to increased exports and reduced imports.

Final Answer: Depreciation increases exports

Answer: (C)

Q35.

Solution

Concept: Aggregate demand (AD) refers to total demand for goods and services in an economy at a given price level. It consists of consumption (C), investment (I), government expenditure (G), and net exports (X–M). AD determines overall economic activity.

Solution: AD is expressed as:

$$AD = C + I + G + (X - M)$$

An increase in AD leads to higher production, income, and employment, while a decrease reduces them. Each component plays a role: consumption drives demand, investment boosts production capacity, government spending supports infrastructure, and net exports reflect external demand. Thus, all components together determine income and employment levels.

Final Answer: All components determine demand

Answer: (C)

Q36.

Solution

Concept: Aggregate supply (AS) represents total output firms are willing to produce at a given price level. Equilibrium income is determined where aggregate demand equals aggregate supply, reflecting balance between production and demand.

Solution: When AD equals AS, the economy is in equilibrium with no tendency for change. If AD exceeds AS, output and income increase. If AS exceeds AD, production falls. The interaction of AD and AS determines national income, employment, and price stability. Thus, equilibrium level of income is jointly determined by both demand and supply forces in the economy.

Final Answer: Both AD and AS determine equilibrium

Answer: (C)

Q37.

Solution

Concept: The multiplier refers to the process by which an initial change in investment leads to a larger change in national income. It depends on the marginal propensity to consume (MPC), which determines how much of additional income is spent further.

Solution: When investment increases, it raises income of producers, who in turn spend a portion of it. This spending becomes income for others, creating a chain reaction. The total increase in income is a multiple of the initial investment:

$$k = \frac{1}{1 - MPC}$$

Thus, a small rise in investment generates a larger increase in income and employment, demonstrating the amplifying effect of the multiplier.

Final Answer: Multiplier amplifies income change

Answer: (B)

Q38.

Solution

Concept: Full employment equilibrium occurs when all available resources are fully utilized. However, due to insufficient aggregate demand, an economy may settle at a lower level of output, known as underemployment equilibrium.

Solution: If aggregate demand is inadequate, firms produce less output, leading to unemployment of resources. Even though AD equals AS, the equilibrium level of income is below full employment. This situation persists because there is no automatic mechanism to increase demand. Thus, equilibrium can exist with unemployment, highlighting a key limitation of market forces.

Final Answer: Equilibrium can exist below full employment

Answer: (C)

Q39.

Solution

Concept: Government plays a crucial role in reducing unemployment through fiscal policy, which includes changes in government expenditure and taxation. These measures influence aggregate demand and help stabilize the economy.

Solution: To reduce unemployment, the government can increase public expenditure or reduce taxes, thereby boosting aggregate demand. Higher demand leads to increased production and employment. During recession, expansionary fiscal policy is used to stimulate economic activity. Thus, government intervention helps correct unemployment by influencing demand and promoting economic growth.

Final Answer: Uses fiscal policy to increase demand

Answer: (B)

Q40.

Solution

Concept: After independence, India adopted economic planning to achieve rapid development, reduce poverty, and ensure balanced growth. The Five-Year Plans were central to this strategy, focusing on industrialization, agriculture, employment, and self-reliance to build a strong economic foundation.

Solution: The objectives of planning included economic growth, social justice, modernization, and self-reliance. Five-Year Plans allocated resources to priority sectors like heavy industries and infrastructure. They aimed to reduce dependence on foreign countries and promote domestic capabilities. Through systematic planning, India sought balanced regional development and long-term economic stability.

Final Answer: Balanced growth and self-reliance

Answer: (B)

Q41.

Solution

Concept: The public sector played a dominant role in India's economic development between 1947–90. It was responsible for establishing basic and heavy industries, infrastructure, and providing essential services, which were not adequately developed by the private sector.

Solution: The government invested heavily in sectors like steel, power, transport, and communication. Public sector enterprises laid the foundation for industrial growth and ensured equitable distribution of resources. They also reduced regional disparities and supported long-term development goals. Thus, the public sector was the driving force behind India's industrialization during the planning period.

Final Answer: Public sector led industrial growth

Answer: (C)

Q42.

Solution

Concept: Import substitution is a strategy aimed at reducing dependence on foreign goods by encouraging domestic production. It involves imposing tariffs, quotas, and restrictions on imports to protect local industries.

Solution: During the planning period, India adopted import substitution to promote self-reliance. By restricting imports, domestic industries were protected from foreign competition, allowing them to grow. This policy helped in developing local manufacturing capacity and reducing foreign exchange dependence. However, it also led to inefficiencies and lack of global competitiveness in some sectors.

Final Answer: Promoted domestic industries by restricting imports

Answer: (C)

Q43.

Solution

Concept: In 1991, India faced a severe economic crisis marked by high fiscal deficit, low foreign exchange reserves, and slow growth. Economic reforms were introduced through LPG (Liberalization, Privatization, Globalization) to stabilize and modernize the economy.

Solution: Liberalization removed unnecessary government controls, privatization reduced the role of public sector, and globalization integrated India with the world economy. These reforms improved efficiency, attracted foreign investment, and boosted economic growth. The LPG policy transformed India from a closed economy to a more competitive and market-oriented system.

Final Answer: LPG policy transformed economy

Answer: (C)

Q44.

Solution

Concept: Globalization refers to the integration of an economy with the global market through trade, investment, and technology transfer. It has significant effects on growth, employment, and international trade patterns.

Solution: Globalization increased exports and imports, leading to higher economic growth. It attracted foreign investment, improved technology, and created new employment opportunities, especially in services. However, it also led to competition and job insecurity in some sectors. Overall, it enhanced global integration and contributed to India's economic expansion.

Final Answer: Increased global integration and growth

Answer: (B)

Q45.

Solution

Concept: Unemployment is a major challenge in India due to population growth and limited job opportunities. It exists in various forms, including disguised unemployment in agriculture and seasonal unemployment in rural areas.

Solution: Disguised unemployment occurs when more people are employed than required, leading to zero marginal productivity. Seasonal unemployment arises during off-season periods in agriculture. Other forms include structural and urban unemployment. These types reflect underutilization of labour resources, affecting economic growth and living standards.

Final Answer: Multiple types including disguised and seasonal

Answer: (C)

Q46.

Solution

Concept: Poverty in India refers to a condition where people are unable to meet basic needs like food, shelter, and clothing. It is influenced by unemployment, low income, and inequality. The government adopts various policies and schemes to reduce poverty and improve living standards.
Solution: Measures to reduce poverty include employment generation programs (like MGNREGA), food security schemes, rural development initiatives, and skill development programs. These policies aim to increase income, provide basic services, and create opportunities. While economic growth helps, targeted government intervention is essential to ensure inclusive development and effective poverty reduction.
Final Answer: Government schemes help reduce poverty

Answer: (C)

Q47.

Solution

Concept: Sustainable development means meeting present needs without compromising the ability of future generations to meet their needs. It involves balancing economic growth with environmental protection and resource conservation.
Solution: Rapid industrialization and urbanization often lead to environmental degradation, pollution, and resource depletion. Therefore, policies must ensure efficient resource use, renewable energy adoption, and environmental conservation. The challenge lies in achieving economic growth while maintaining ecological balance. Thus, sustainable development requires a careful balance between growth and environmental protection.
Final Answer: Need balance between growth and environment

Answer: (C)

Q48.

Solution

Concept: Human capital formation refers to the process of improving the quality of human resources through education, health, and skill development. It plays a crucial role in enhancing productivity and economic growth.
Solution: Education increases knowledge and skills, while health improves efficiency and work capacity. Investment in human capital leads to higher productivity, innovation, and better employment opportunities. In India, challenges like inadequate access to quality education and healthcare hinder development. Thus, strengthening human capital is essential for long-term economic progress.
Final Answer: Education and health improve productivity

Answer: (C)

Q49.

Solution

Concept: The agricultural sector in India faces several structural challenges that limit its productivity and growth. These include dependence on monsoon, fragmented land holdings, lack of modern technology, and inadequate infrastructure such as irrigation, storage, and transportation.
Solution: Indian agriculture is highly dependent on rainfall, making output uncertain. Low use of advanced inputs like fertilizers and machinery reduces productivity. Poor infrastructure leads to post-harvest losses and inefficient market access. These issues result in low income for farmers and slow sectoral growth. Addressing these challenges requires investment in irrigation, technology, and rural infrastructure.
Final Answer: Multiple structural challenges exist

Answer: (C)

Q50.

Solution

Concept: India, China, and Pakistan adopted different development strategies after independence, leading to varied economic outcomes. Their approaches to industrialization, population control, and policy reforms influenced their growth trajectories.
Solution: China focused on rapid industrialization, strong state control, and early economic reforms, achieving high growth rates. India adopted a mixed economy with gradual reforms, leading to moderate growth. Pakistan initially showed growth but faced instability and policy inconsistencies. Differences in governance, investment in human capital, and openness to global markets resulted in distinct development outcomes.
Final Answer: Different strategies led to different outcomes

Answer: (C)

Answer Key

Q	Ans	Q	Ans	Q	Ans	Q	Ans	Q	Ans
1	B	2	C	3	C	4	B	5	C
6	C	7	C	8	C	9	C	10	C
1	C	12	B	13	C	14	B	15	C
16	B	17	C	18	B	19	C	20	C
21	B	22	B	23	C	24	C	25	B
26	B	27	D	28	C	29	B	30	C
31	C	32	B	33	B	34	C	35	C
36	C	37	B	38	C	39	B	40	B
41	C	42	C	43	C	44	B	45	C
46	C	47	C	48	C	49	C	50	C