

NIOS Class 12 Economics Sample Paper-5

Duration: 180 Minutes

Maximum Marks: 100

Instructions

- This paper contains **50 Questions** divided into **Section A** (50 marks) and **Section B** (50 marks).
- **Section A** consists of:
 - **Q.1 to Q.20** – Multiple Choice type questions (MCQs) carrying 1 mark each.
 - **Q.21 to Q.35** – Objective type questions carrying 2 marks each (fill in blanks, yes/no, definitions, etc.).
- **Section B** consists of:
 - **Q.36 to Q.42** – Short answer type questions carrying 2 marks each.
 - **Q.43 to Q.48** – Answer type questions carrying 4 marks each with internal choice.
 - **Q.49 to Q.50** – Long answer type questions carrying 6 marks each with internal choice.
- There is **No Negative marking**.
- Internal choices have been provided in some questions. Attempt only one choice.
- Use of mobile phones, calculators, or any electronic gadgets is strictly prohibited.

Section: A

Q1. Which of the following best describes the concept of scarcity in economics? (1)

- (A) Resources are available in unlimited quantities
- (B) Human wants exceed the available resources
- (C) All goods are available free of cost



(D) There is no need to make choices

Q2. The branch of economics that deals with the economy as a whole is called: **(1)**

(A) Microeconomics

(B) Macroeconomics

(C) Econometrics

(D) Welfare Economics

Q3. In the utility analysis of consumer behaviour, the point of satiety is reached when: **(1)**

(A) Total Utility is zero

(B) Marginal Utility is zero

(C) Marginal Utility is negative

(D) Average Utility is zero

Q4. Which of the following will cause a shift in the demand curve? **(1)**

(A) Change in the commodity's own price

(B) Change in the price of a substitute good

(C) Movement along the same demand curve

(D) None of the above

Q5. When the percentage change in quantity demanded is less than the percentage change in price, the demand is: **(1)**

(A) Elastic

(B) Inelastic

(C) Unitary elastic

(D) Perfectly elastic

Q6. In the short run, a firm can change: **(1)**



- (A) All factors of production
- (B) Only variable factors of production
- (C) Only fixed factors of production
- (D) Neither fixed nor variable factors

Q7. Which cost remains constant at all levels of output? **(1)**

- (A) Total Variable Cost
- (B) Average Cost
- (C) Total Fixed Cost
- (D) Marginal Cost

Q8. The supply curve of a firm slopes: **(1)**

- (A) Downward from left to right
- (B) Upward from left to right
- (C) Parallel to the quantity axis
- (D) Parallel to the price axis

Q9. Price elasticity of supply for a perfectly inelastic commodity is: **(1)**

- (A) Infinity
- (B) Greater than one
- (C) Equal to one
- (D) Zero

Q10. Under which market structure does a firm face a perfectly elastic demand curve? **(1)**

- (A) Monopoly
- (B) Oligopoly
- (C) Perfect Competition



(D) Monopolistic Competition

Q11. In a perfectly competitive market, the profit-maximizing condition for a firm is: (1)

(A) $MR > MC$

(B) $MR < MC$

(C) $MR = MC$

(D) $AR = AC$

Q12. Which of the following is included in the estimation of National Income? (1)

(A) Transfer payments

(B) Sale of second-hand goods

(C) Services of a housewife

(D) Value of final goods and services produced

Q13. Net National Product at factor cost is also known as: (1)

(A) Gross Domestic Product

(B) National Income

(C) Personal Income

(D) Disposable Income

Q14. If the Marginal Propensity to Consume (MPC) is 0.75, the value of the multiplier is: (1)

(A) 2

(B) 3

(C) 4

(D) 5

Q15. The Keynesian theory of income determination assumes that in the short run: (1)



- (A) Price level is flexible
- (B) Price level is constant
- (C) Output level is fixed
- (D) Employment is always full

Q16. Which of the following is NOT a function of money? **(1)**

- (A) Medium of exchange
- (B) Store of value
- (C) Measure of poverty
- (D) Standard of deferred payment

Q17. The Reserve Bank of India uses which instrument to control the credit creation capacity of commercial banks? **(1)**

- (A) Fiscal Policy
- (B) Open Market Operations
- (C) Trade Policy
- (D) Industrial Policy

Q18. Revenue expenditure of the government includes: **(1)**

- (A) Construction of highways
- (B) Purchase of machinery
- (C) Payment of salaries to government employees
- (D) Loans given to public enterprises

Q19. The trade between two countries is referred to as: **(1)**

- (A) Internal trade
- (B) International trade
- (C) Regional trade



(D) Local trade

Q20. A deficit in the Balance of Payments indicates that: (1)

(A) Foreign exchange receipts exceed foreign exchange payments

(B) Foreign exchange payments exceed foreign exchange receipts

(C) Exports are equal to imports

(D) The country has no foreign debt

Q21. Fill in the blanks: The concept of . refers to the additional satisfaction derived from consuming one more unit of a commodity. (2)

Q22. Fill in the blanks: A demand curve indicates that quantity demanded changes infinitely with a small change in price. (2)

Q23. Write the formula for calculating the value of the investment multiplier: (2)

Q24. Write Yes or No: Does an increase in the price of a complementary good lead to an increase in the demand for the related commodity? (2)

Q25. Identify any two false statements from the following: (2)

1. Average Cost always falls as output increases

2. Total Revenue = Price $\times$ Quantity

3. Fixed costs change with the level of output

4. Marginal Cost intersects Average Cost at its minimum point

Q26. Fill in the blanks: In the long run, all factors of production are . in nature, and there are no costs. (2)

Q27. Write Yes or No: Does the GDP of a country include income earned by foreign nationals working within the domestic territory? (2)



- Q28.** Fill in the blanks: The difference between Gross National Product and Depreciation is called
(2)
- Q29.** Fill in the blanks: The average propensity to consume is calculated as $\frac{\text{Consumption}}{\text{.....}}$.
(2)
- Q30.** Define the term ‘Opportunity Cost’ in economics.
(2)
- Q31.** Fill in the blanks: The payment made to labour for rendering productive services is called
(2)
- Q32.** Define ‘Marginal Cost’ and state its relationship with Average Cost when Average Cost is at its minimum.
(2)
- Q33.** Correct the following sentence: “The supply curve slopes downward from left to right because producers supply more at lower prices.”
(2)
- Q34.** State the full form of the following:
(i) CRR (ii) SLR
(2)
- Q35.** Write Yes or No: Is the balance of trade the same as the balance of payments?
(2)

Section: B

- Q36.** Distinguish between an increase in demand and an increase in quantity demanded.
(2)
- Q37.** From the following data, calculate the Total Revenue of the firm:
(2)



Output (Units)	Price (Rs.)	Total Revenue (Rs.)
1	20	.....
2	18	.....
3	16	.....
4	14	.....

Q38. Draw a diagram showing the equilibrium of a consumer using the Indifference Curve and Budget Line approach. (2)

Q39. (i) Define the term 'Elasticity of Supply' and state any one factor that affects it.

OR

(ii) Explain the concept of 'Market Period' and 'Long Period' in supply analysis. (2)

Q40. (i) Distinguish between Revenue Expenditure and Capital Expenditure with one example of each.

OR

(ii) Explain the concept of Fiscal Deficit and its significance in government budgeting. (2)

Q41. (i) State two differences between Autonomous transactions and Accommodating transactions in the Balance of Payments.

OR

(ii) What are the components of the Current Account in the Balance of Payments? (2)

Q42. Explain the law of diminishing marginal utility with the help of a schedule and state its assumptions. (2)



- Q43.** (i) Explain the concept of Marginal Rate of Substitution (MRS) with the help of an Indifference Curve. Why does it diminish?

OR

- (ii) A consumer consumes two goods X and Y. The price of X is Rs. 4 and the price of Y is Rs. 5. The consumer's income is Rs. 200. Write the budget equation and find the maximum quantity of good X that can be purchased. (4)

- Q44.** (i) Explain the concept of price determination under perfect competition using the interaction of market demand and supply. Use a diagram.

OR

- (ii) What happens to market equilibrium when there is an increase in demand with no change in supply? Explain with a diagram. (4)

- Q45.** (i) Explain the Income Method of measuring National Income. List the components that are included and the precautions to be taken.

OR

- (ii) Differentiate between Real GDP and Nominal GDP. Which is a better indicator of economic welfare and why? (4)

- Q46.** (i) Explain the concept of credit creation by commercial banks. What is the role of the Cash Reserve Ratio (CRR) in this process?

OR

- (ii) What are the various instruments of monetary policy used by the Central Bank to control money supply? (4)



- Q47.** (i) Explain the working of the investment multiplier with a numerical example. How does it affect the level of national income?

OR

- (ii) Explain the Keynesian consumption function. Distinguish between Average Propensity to Consume (APC) and Marginal Propensity to Consume (MPC). (4)

- Q48.** Complete the following table showing the relationship between Total Product, Marginal Product, and Average Product: (4)

Units of Labour	Total Product	Marginal Product	Average Product
0	0	.....	.....
1	12	.....	.....
2	30	.....	.....
3	45	.....	.....
4	52	.....	.....
5	52	.....	.....

- Q49.** Describe the various types of budget receipts of the government. Explain the difference between Revenue Receipts and Capital Receipts with suitable examples. (6)

- Q50.** (i) Explain the meaning and components of Aggregate Demand in a two-sector economy. Derive the equilibrium level of income using the Consumption Function and the Saving-Investment approach.

OR

- (ii) Explain the concept of Excess Demand and Deficient Demand in the Keynesian framework. What are the consequences of each on the economy? How can the government use fiscal policy to correct these situations? (6)



Detailed Solutions

Q1.

Solution

Concept:

The concept of scarcity is the most fundamental idea in economics. It arises because human beings have unlimited desires but the resources available to satisfy those desires are limited in quantity. Scarcity forces every individual, firm, and government to make choices about how to allocate their limited resources among competing uses. If resources were unlimited, there would be no need for economics as a discipline because no choices or trade-offs would be required. Scarcity is not about the absolute absence of a resource but about the insufficiency relative to unlimited wants. This concept directly leads to the problem of choice, which is at the heart of all economic decision-making.

Solution:

- (a) Option A states that resources are unlimited, which contradicts the basic economic reality. Resources such as land, labour, capital, and entrepreneurship are finite and limited in supply.
- (b) Option B correctly identifies that human wants exceed available resources. This excess of desires over available means is the very definition of scarcity in economics.
- (c) Option C suggests that all goods are free, which is not true because most goods require resources for production and therefore carry a cost.
- (d) Option D implies that no choices are necessary, but scarcity inherently necessitates the making of choices because all wants cannot be satisfied simultaneously.

Final Answer: Human wants exceed the available resources

Answer: (B)

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Q2.

Solution

Concept:

Economics is broadly divided into two branches: Microeconomics and Macroeconomics. Microeconomics studies the behaviour and decision-making of individual economic units such as consumers, firms, and industries. It focuses on price determination in individual markets, consumer utility maximization, and firm profit maximization. Macroeconomics, on the other hand, examines the economy as a whole. It deals with aggregate variables such as national income, aggregate demand, aggregate supply, total employment, general price level, inflation, and economic growth. The distinction was formally established by the Norwegian economist Ragnar Frisch in 1933. Macroeconomic analysis helps governments design fiscal and monetary policies to achieve macroeconomic stability and growth.

Solution:

- (a) Microeconomics deals with individual units and specific market outcomes rather than the entire economy.
- (b) Macroeconomics studies aggregate phenomena like national income, total output, unemployment, inflation, and the general price level, making it the branch that deals with the economy as a whole.
- (c) Econometrics is a separate methodological branch that applies statistical and mathematical techniques to economic data for testing hypotheses.
- (d) Welfare Economics is a normative branch that evaluates economic outcomes based on social desirability and efficiency criteria.

Final Answer: Macroeconomics

Answer: (B)

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Q3.

Solution

Concept:

In the utility approach to consumer equilibrium, a consumer reaches the point of satiety when they have consumed a quantity of a good at which they derive maximum total satisfaction. At this specific point, the additional or marginal utility obtained from consuming the very next unit of the commodity becomes exactly zero. Total utility continues to increase as long as marginal utility remains positive, but it stops growing once marginal utility hits zero. Beyond this point, if the consumer continues to consume more, marginal utility becomes negative and total utility starts to decline, indicating dissatisfaction or disutility.

Solution:

- (a) Total utility is zero only when no units have been consumed or if consumption has gone so far into the negative marginal utility range that the entire utility is offset, which is not the definition of satiety.
- (b) Marginal utility being zero is the correct condition for the point of satiety. At this exact point, total utility is at its maximum because consuming one more unit adds nothing to total satisfaction.
- (c) Marginal utility being negative means the consumer has gone beyond the satiety point, experiencing disutility from additional consumption.
- (d) Average utility is a derived measure and does not directly determine the point of satiety in the classical utility framework.

Final Answer: Marginal Utility is zero

Answer: (B)

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Q4.

Solution

Concept:

The demand curve shows the relationship between the price of a commodity and the quantity demanded, holding all other factors constant (*ceteris paribus*). A movement along the demand curve occurs when there is a change in the commodity's own price, resulting in a change in quantity demanded. A shift of the entire demand curve, on the other hand, occurs when a factor other than the commodity's own price changes. These shift factors include changes in consumer income, tastes and preferences, prices of related goods (substitutes and complements), population size, and expectations about future prices.

Solution:

- (a) A change in the commodity's own price causes a movement along the same demand curve, not a shift.
- (b) A change in the price of a substitute good is a non-price determinant of demand. When the price of a substitute rises, consumers shift to the relatively cheaper good, increasing its demand at every price level and shifting the demand curve to the right.
- (c) Movement along the same demand curve describes a change in quantity demanded due to the good's own price change, not a shift.
- (d) Since option B correctly describes a shift factor, this option is incorrect.

Final Answer: Change in the price of a substitute good

Answer: (B)

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Q5.

Solution

Concept:

Price elasticity of demand measures the degree of responsiveness of quantity demanded to a change in the price of a commodity. It is calculated as the ratio of the percentage change in quantity demanded to the percentage change in price. When this ratio is greater than one, demand is elastic, meaning consumers are highly responsive to price changes. When the ratio is less than one, demand is inelastic, meaning quantity demanded changes by a smaller proportion than the price change. When it equals one, demand is unitary elastic. When the elasticity coefficient is zero, demand is perfectly inelastic, and when it is infinite, demand is perfectly elastic.

Solution:

- (a) Elastic demand exists when the elasticity coefficient is greater than one, meaning the percentage change in quantity demanded exceeds the percentage change in price.
- (b) Inelastic demand is correctly identified when the percentage change in quantity demanded is less than the percentage change in price, yielding a coefficient less than one.
- (c) Unitary elastic demand means both percentage changes are equal, giving a coefficient of exactly one.
- (d) Perfectly elastic demand means any price increase leads to zero quantity demanded, represented by an infinite coefficient.

Final Answer: Inelastic

Answer: (B)

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Q6.**Solution****Concept:**

In production theory, the short run is defined as a time period during which at least one factor of production is fixed and cannot be altered. Typically, capital inputs such as factory buildings, heavy machinery, and land are considered fixed in the short run because it takes considerable time to expand or reduce them. However, variable factors of production such as raw materials, casual labour, and energy can be adjusted quickly in response to changes in the desired level of output. The long run, by contrast, is a period sufficient enough for a firm to change all of its production inputs, including capital.

Solution:

- (a) Changing all factors of production is only possible in the long run, not the short run.
- (b) In the short run, only variable factors such as labour, raw materials, and energy can be changed. Fixed factors like plant size remain constant.
- (c) Fixed factors cannot be changed in the short run; that is precisely what makes them fixed in that time frame.
- (d) It is impossible to produce any output without varying at least some inputs when output changes.

Final Answer: Only variable factors of production

Answer: (B)

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Q7.

Solution

Concept:

Total cost is the sum of total fixed cost and total variable cost. Fixed costs are those expenses that do not change with the level of output. They are incurred even when output is zero. Examples include rent of the factory, insurance premiums, salaries of permanent staff, and depreciation on machinery. These costs remain constant whether the firm produces one unit or a thousand units. Variable costs, on the other hand, change directly with the level of output. Average cost and marginal cost are derived measures that fluctuate as output changes.

Solution:

- (a) Total Variable Cost increases as output increases because more raw materials and labour are needed.
- (b) Average Cost changes with output as it is total cost divided by quantity, and this ratio varies at different output levels.
- (c) Total Fixed Cost remains constant at all levels of output. Even when output is zero, the firm must bear fixed expenses like rent and insurance.
- (d) Marginal Cost, which is the additional cost of producing one more unit, varies with each successive unit of output.

Final Answer: Total Fixed Cost

Answer: (C)

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Q8.

Solution

Concept:

The supply curve represents the relationship between the price of a commodity and the quantity that producers are willing to supply, holding all other factors constant. According to the law of supply, there is a direct or positive relationship between price and quantity supplied. When the price of a commodity increases, it becomes more profitable for producers to supply larger quantities, because the higher price covers the rising marginal cost of production. This positive relationship is graphically represented by an upward-sloping supply curve from left to right.

Solution:

- (a) A downward-sloping curve from left to right represents a demand curve, not a supply curve.
- (b) The supply curve slopes upward from left to right, reflecting the positive relationship between price and quantity supplied as described by the law of supply.
- (c) A curve parallel to the quantity axis would represent perfectly elastic supply, not the general supply curve.
- (d) A curve parallel to the price axis would represent perfectly inelastic supply, which is an exceptional case and not the general shape.

Final Answer: Upward from left to right

Answer: (B)

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Q9.

Solution

Concept:

Price elasticity of supply measures the degree of responsiveness of quantity supplied to a change in the price of a commodity. When supply is perfectly inelastic, it means that the quantity supplied does not change at all regardless of changes in price. This situation is graphically represented by a vertical supply curve. Examples include goods with fixed supply such as land, rare artwork, or goods whose production cannot be increased in the short run. The elasticity coefficient for perfectly inelastic supply is zero because the percentage change in quantity supplied is zero, no matter how much the price changes.

Solution:

- (a) An elasticity of infinity represents perfectly elastic supply, where even a tiny price change causes an infinite change in quantity supplied.
- (b) An elasticity greater than one represents elastic supply, where quantity supplied is highly responsive to price changes.
- (c) An elasticity equal to one represents unitary elastic supply, where the percentage change in quantity supplied equals the percentage change in price.
- (d) A price elasticity of supply of zero correctly represents perfectly inelastic supply, where quantity supplied remains unchanged regardless of price fluctuations.

Final Answer: Zero

Answer: (D)

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Q10.

Solution

Concept:

A perfectly competitive market is characterized by a very large number of buyers and sellers, each dealing in a homogeneous product. Because each firm is a price taker and has no control over the market price, it can sell any quantity at the prevailing market price but nothing at a price even slightly higher. As a result, the demand curve facing an individual firm under perfect competition is a horizontal straight line parallel to the quantity axis. This indicates perfectly elastic demand at the ruling market price. In contrast, a monopolist faces a downward-sloping demand curve, and firms in oligopoly and monopolistic competition face different elasticity patterns.

Solution:

- (a) A monopolist faces a downward-sloping demand curve because it is the sole seller and must lower the price to sell more.
- (b) Oligopoly firms face kinked or uncertain demand curves due to interdependence among the few sellers.
- (c) Under perfect competition, each firm is a price taker, and the demand curve it faces is perfectly elastic, represented by a horizontal line at the market price.
- (d) In monopolistic competition, firms have some degree of market power due to product differentiation, resulting in a downward-sloping demand curve.

Final Answer: Perfect Competition

Answer: (C)

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Q11.

Solution

Concept:

Profit maximization is one of the primary objectives of a firm. In economic theory, a firm maximizes profit at the level of output where marginal revenue equals marginal cost. This is known as the $MR = MC$ rule. If marginal revenue exceeds marginal cost, the firm can increase profit by producing more. If marginal cost exceeds marginal revenue, the firm should reduce output. Under perfect competition, since the price is constant and equal to both AR and MR, the profit-maximizing condition can also be stated as $P = MR = MC$. The condition $AR = AC$ refers to the break-even point where the firm earns only normal profits.

Solution:

- (a) When $MR > MC$, the firm can increase profit by producing additional units, so it has not yet reached the profit-maximizing output.
- (b) When $MR < MC$, the firm is incurring losses on additional units and should reduce output to maximize profit.
- (c) When $MR = MC$, the firm has reached the optimal level of output where profit is maximized. Producing more or less would reduce total profit.
- (d) $AR = AC$ is the break-even condition where the firm earns normal profit, but it is not the profit-maximizing condition per se.

Final Answer: $MR = MC$

Answer: (C)

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Q12.

Solution

Concept:

National Income measures the total value of all final goods and services produced within an economy during a given accounting period. To avoid the problem of double counting, economists count only the value of final goods and exclude intermediate goods, transfer payments, and second-hand transactions. Transfer payments such as pensions, scholarships, and unemployment benefits are excluded because they are not made in exchange for any current productive service. The sale of second-hand goods is excluded because their value was already counted in the year they were originally produced.

Solution:

- (a) Transfer payments are excluded from national income estimation because they do not correspond to any current production of goods or services.
- (b) The sale of second-hand goods is excluded because these goods were counted in national income during the year of their original production.
- (c) Services of a housewife are excluded because they are not traded in the market and no monetary transaction takes place.
- (d) The value of final goods and services produced is correctly included in national income as it represents current productive output of the economy.

Final Answer: Value of final goods and services produced

Answer: (D)

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Q13.

Solution

Concept:

National Income is defined as the Net National Product at factor cost. This aggregate measures the total income earned by all factors of production belonging to the normal residents of a country during a year, after deducting depreciation and indirect taxes and adding subsidies. NNP at factor cost is derived by starting from GDP at market price, adding net factor income from abroad, subtracting depreciation, and adjusting for net indirect taxes. This aggregate is considered the most accurate measure of the economy's productive performance and the income earned by its residents.

Solution:

- (a) Gross Domestic Product measures the total value of goods and services produced within the domestic territory, without accounting for depreciation or net factor income from abroad.
- (b) National Income is the standard term used for Net National Product at Factor Cost, which correctly accounts for depreciation and international income flows.
- (c) Personal Income is the income actually received by individuals before the payment of personal direct taxes.
- (d) Disposable Income is the income remaining after personal direct taxes have been paid, available for consumption and saving.

Final Answer: National Income

Answer: (B)

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Q14.

Solution

Concept:

The investment multiplier is a key concept in Keynesian economics. It shows the ratio of the change in national income to the initial change in investment that caused it. The multiplier is inversely related to the Marginal Propensity to Save (MPS). The formula for the multiplier is $k = \frac{1}{1-MPC} = \frac{1}{MPS}$. When MPC is 0.75, it means that for every additional rupee of income, households spend 75 paise and save 25 paise. The resulting multiplier effect amplifies the initial change in investment into a much larger change in national income through successive rounds of spending.

Solution:

- (a) Given that $MPC = 0.75$, we can calculate $MPS = 1 - MPC = 1 - 0.75 = 0.25$.
- (b) The multiplier formula is $k = \frac{1}{MPS} = \frac{1}{0.25}$.
- (c) Dividing 1 by 0.25 gives us a multiplier value of 4.
- (d) This means that every rupee of new investment generates four rupees of additional national income through the multiplier process.

Final Answer: 4

Answer: (C)

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Q15.

Solution

Concept:

The Keynesian theory of income and employment determination was developed by John Maynard Keynes in his seminal work “The General Theory of Employment, Interest, and Money” published in 1936. A fundamental assumption of the Keynesian model in the short run is that the price level remains constant or sticky. This assumption allows Keynes to focus on the role of aggregate demand in determining output and employment. Since prices are assumed to be rigid, any change in aggregate demand directly affects the real output and employment level rather than being absorbed by price adjustments. This assumption is particularly relevant during recessions when there is significant unemployment and idle capacity.

Solution:

- (a) If the price level were flexible, the economy would self-adjust through price and wage adjustments, which contradicts Keynes’s argument for the need of government intervention.
- (b) The assumption of a constant price level in the short run is the cornerstone of Keynesian analysis. It implies that output responds to changes in aggregate demand without inflationary pressure.
- (c) The output level is not fixed; rather, it is determined by aggregate demand. The economy can operate below full employment equilibrium.
- (d) Full employment is not always achieved in the Keynesian framework; in fact, Keynes argued that the economy can be in equilibrium at less than full employment.

Final Answer: Price level is constant

Answer: (B)

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Q16.

Solution

Concept:

Money serves four primary functions in an economy. It acts as a medium of exchange, facilitating the buying and selling of goods and services without the need for barter. It serves as a unit of account, providing a common measure of the value of goods and services. Money functions as a store of value, allowing individuals to save purchasing power for future use. Finally, money serves as a standard of deferred payment, enabling transactions that involve future payments such as loans and credit. The function “measure of poverty” is not a recognized function of money in economics. Poverty is measured using income thresholds, consumption levels, or multidimensional indices.

Solution:

- (a) Medium of exchange is a primary function of money, replacing the inefficiency of the barter system.
- (b) Store of value is a function of money that allows wealth to be held in monetary form for future use.
- (c) Measure of poverty is not a function of money. Poverty measurement uses indicators like the poverty line, head count ratio, or multidimensional poverty indices, none of which are functions of money itself.
- (d) Standard of deferred payment is a function of money that facilitates credit transactions and the settlement of debts over time.

Final Answer: Output level is fixed

Answer: (C)

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Q17.**Solution****Concept:**

The Central Bank, such as the Reserve Bank of India, uses various instruments of monetary policy to regulate the money supply and credit availability in the economy. These instruments are broadly classified into quantitative and qualitative tools. Open Market Operations (OMO) are a key quantitative tool where the central bank buys or sells government securities in the open market. When the central bank sells securities, it absorbs liquidity from the banking system, reducing the reserves of commercial banks and thereby their capacity to create credit. This contractionary measure is used to control inflation and excess demand in the economy.

Solution:

- (a) Fiscal policy is the domain of the government and involves taxation and public expenditure, not the central bank's monetary tools.
- (b) Open Market Operations involve the buying and selling of government securities by the central bank to control the reserves of commercial banks and thus their credit creation capacity.
- (c) Trade policy relates to international commerce, tariffs, and exchange rates, and is not a direct tool of the central bank for controlling credit.
- (d) Industrial policy pertains to the government's strategy for promoting industrial growth and is not a monetary policy instrument.

Final Answer: Open Market Operations**Answer: (B)**[Go Back to Question 17](#)

Q18.

Solution

Concept:

The government budget classifies expenditure into revenue expenditure and capital expenditure. Revenue expenditure is the spending that does not result in the creation of assets or reduction of liabilities. It is recurring in nature and includes items like salaries of government employees, pensions, interest payments, subsidies, and grants to states. Capital expenditure, on the other hand, leads to the creation of assets (like construction of roads, bridges, and schools) or reduction of liabilities (like repayment of loans). Capital expenditure is non-recurring and contributes to the productive capacity of the economy.

Solution:

- (a) Construction of highways is a capital expenditure because it creates a durable physical asset for the government.
- (b) Purchase of machinery is a capital expenditure as it adds to the productive capacity of government enterprises.
- (c) Payment of salaries to government employees is a revenue expenditure because it is a recurring expense that does not create any asset or reduce any liability.
- (d) Loans given to public enterprises are capital expenditure as they represent the creation of financial assets for the government.

Final Answer: Payment of salaries to government employees

Answer: (C)

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Q19.**Solution****Concept:**

Trade between countries is classified based on the geographical boundaries of the trading nations. International trade, also known as external trade or foreign trade, refers to the exchange of goods, services, and capital across national boundaries. It involves exports and imports between two or more countries. Internal trade, also known as domestic trade or home trade, refers to trade that takes place within the geographical boundaries of a single country. Regional trade refers to trade agreements among a group of neighbouring countries, while local trade occurs within a small geographical area such as a city or district.

Solution:

- (a) Internal trade occurs within the borders of a single country and does not involve cross-border transactions.
- (b) International trade is the correct term for trade that takes place between two countries, involving the exchange of goods and services across national boundaries.
- (c) Regional trade is a subset of international trade that takes place among countries in a specific geographical region under trade agreements.
- (d) Local trade refers to commerce within a small locality and is a component of domestic trade.

Final Answer: International trade**Answer: (B)**[Go Back to Question 19](#)

Q20.**Solution****Concept:**

The Balance of Payments is a systematic record of all economic transactions between the residents of a country and the rest of the world during a given period. It consists of the current account and the capital account. When the total foreign exchange payments made by a country exceed the total foreign exchange receipts, the Balance of Payments is said to be in deficit. This means the country is spending more on imports, foreign aid, and overseas investments than it earns from exports and foreign investments. A BOP deficit leads to a depletion of foreign exchange reserves and may require borrowing from international institutions.

Solution:

- (a) When foreign exchange receipts exceed payments, the Balance of Payments is in surplus, not deficit.
- (b) A deficit in the Balance of Payments occurs when foreign exchange payments exceed foreign exchange receipts. The country needs to finance this deficit by drawing down reserves or borrowing from abroad.
- (c) When exports equal imports in value, the trade balance is balanced, but the overall BOP includes capital flows as well.
- (d) Having no foreign debt is unrelated to the BOP deficit, which concerns the overall flow of foreign exchange.

Final Answer: Foreign exchange payments exceed foreign exchange receipts

Answer: (B)

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Q21.

Solution

Concept:

In consumer theory, utility refers to the want-satisfying power of a commodity. As a consumer consumes successive units of a commodity, the total utility increases but at a diminishing rate. The additional satisfaction obtained from consuming one more unit of a commodity is specifically called Marginal Utility. It is calculated as the change in total utility divided by the change in the number of units consumed. Marginal utility plays a crucial role in determining consumer equilibrium, as a rational consumer continues to consume a commodity until the marginal utility equals the price paid.

Solution:

- (a) The blank in the question refers to the concept of additional satisfaction from consuming one more unit.
- (b) This additional satisfaction is technically known as Marginal Utility in economic theory.
- (c) Marginal Utility is calculated as the difference in total utility when one more unit is consumed, i.e., $MU_n = TU_n - TU_{n-1}$.
- (d) The law of diminishing marginal utility states that as more units are consumed, marginal utility tends to decline, though total utility may still increase.

Final Answer: Marginal Utility

Answer: (See Above)

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Q22.

Solution

Concept:

The elasticity of demand measures the responsiveness of quantity demanded to changes in the determinants of demand. When demand is perfectly elastic, even an infinitesimally small change in price leads to an infinitely large change in quantity demanded. The demand curve for a perfectly elastic demand is a horizontal straight line parallel to the quantity axis. This means the firm can sell any quantity at the given market price but cannot sell even a single unit at a price higher than the market price. Perfectly elastic demand is a theoretical extreme that is approximated in perfectly competitive markets where products are homogeneous.

Solution:

- (a) The question asks about a demand curve where quantity demanded changes infinitely with a small change in price.
- (b) This scenario describes perfectly elastic demand, where the elasticity coefficient is infinite.
- (c) A perfectly elastic demand curve is a horizontal line, indicating that consumers are willing to buy any quantity at the prevailing price but none at a slightly higher price.
- (d) The term that fills the blank is “perfectly elastic.”

Final Answer: perfectly elastic

Answer: (See Above)

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Q23.

Solution

Concept:

The investment multiplier is a central concept in Keynesian macroeconomics. It quantifies the effect of an initial change in autonomous spending, particularly investment, on the overall level of national income. The multiplier operates through successive rounds of spending: when investment increases, it creates income for factor owners, who then spend a portion of that income based on their Marginal Propensity to Consume, creating further income for others. The multiplier value depends on the Marginal Propensity to Save (MPS). The greater the MPS, the smaller the multiplier, because more income leaks out of the spending stream in each round.

Solution:

- (a) The investment multiplier formula relates the change in national income to the initial change in investment.
- (b) It is expressed as the reciprocal of the Marginal Propensity to Save, or equivalently, the reciprocal of one minus the Marginal Propensity to Consume.
- (c) The formula is: $k = \frac{\Delta Y}{\Delta I} = \frac{1}{1-MPC} = \frac{1}{MPS}$.
- (d) Where k is the multiplier, ΔY is the change in national income, ΔI is the change in investment, MPC is the marginal propensity to consume, and MPS is the marginal propensity to save.

Final Answer: $k = \frac{1}{1-MPC} = \frac{1}{MPS}$

Answer: (See Above)

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Q24.

Solution**Concept:**

Complementary goods are those goods that are consumed together, such as a car and petrol, a printer and ink cartridges, or bread and butter. When the price of one complementary good increases, the demand for the related complementary good decreases because the combined cost of using both goods together rises. This is because consumers perceive the joint consumption as more expensive and reduce their demand for both goods. The cross elasticity of demand for complementary goods is negative, indicating an inverse relationship between the price of one good and the demand for the other.

Solution:

- (a) The question asks whether an increase in the price of a complementary good leads to an increase in the demand for the related commodity.
- (b) For complementary goods, the relationship between the price of one and the demand for the other is inverse, not direct.
- (c) When the price of a complementary good rises, the combined cost of using both goods together increases, leading consumers to reduce their demand for the related commodity.
- (d) Therefore, the answer is No. An increase in the price of a complementary good leads to a decrease, not an increase, in the demand for the related commodity.

Final Answer: No**Answer: (See Above)**[Go Back to Question 24](#)

Q25.

Solution**Concept:**

In cost theory, various cost concepts behave differently as output changes. Total Revenue is the total income earned from selling a given quantity of output at a given price. The shape of the Average Cost curve is typically U-shaped because of the law of variable proportions. Initially, as fixed costs are spread over more units, average cost falls. Eventually, rising variable costs cause average cost to rise. Marginal Cost also has a U-shape and intersects the Average Cost curve at its minimum point, which is a fundamental relationship in microeconomic cost analysis.

Solution:

- (a) Statement 1 is false. Average Cost does not always fall as output increases. After a certain point, it starts rising due to increasing variable costs, giving it a U-shape.
- (b) Statement 2 is true. Total Revenue is correctly calculated as Price multiplied by Quantity sold.
- (c) Statement 3 is false. Fixed costs remain constant regardless of the level of output; they do not change with production levels.
- (d) Statement 4 is true. Marginal Cost indeed intersects Average Cost at its minimum point, below which AC is falling and above which AC is rising.
- (e) Therefore, the two false statements are Statement 1 and Statement 3.

Final Answer: Statements 1 and 3 are false

Answer: (See Above)

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Q26.

Solution

Concept:

In production theory, the long run is defined as a period of time long enough for a firm to change all of its factors of production. Unlike the short run where at least one factor is fixed, in the long run, there are no fixed factors. A firm can adjust its plant size, machinery, technology, and workforce entirely. Because all factors are variable, there are no fixed costs in the long run. All costs become variable, and the firm can choose the optimal combination of inputs to minimize costs. The long-run average cost curve is the envelope of all short-run average cost curves.

Solution:

- (a) The first blank should be filled with “variable” because in the long run, all factors of production can be changed and adjusted by the firm.
- (b) The second blank should be filled with “fixed” because since all factors are variable, there are no fixed costs in the long run.
- (c) This distinction is crucial because it determines the shape of the cost curves and the ability of firms to optimize their production processes.
- (d) In the long run, a firm can expand or contract its entire production capacity, making all costs variable in nature.

Final Answer: variable, fixed

Answer: (See Above)

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Q27.

Solution

Concept:

Gross Domestic Product is the total market value of all final goods and services produced within the domestic geographical territory of a country during a specified accounting period, usually one year. GDP is calculated based on the territorial principle, meaning it includes all production that takes place within the country's borders regardless of whether the producers are citizens or foreign nationals. The income earned by foreign nationals working within the domestic territory is included in the GDP because their productive activity contributes to the domestic output. However, this income would not be included in the Gross National Product, which is based on the residency principle.

Solution:

- (a) GDP measures total output produced within the domestic territory, irrespective of the nationality of the workers.
- (b) Foreign nationals working within the country contribute to domestic production through their labour and services.
- (c) Since GDP follows the territorial or domestic principle, all productive activity within the borders is counted, including that by foreign workers.
- (d) Therefore, the answer is Yes. The GDP includes income earned by foreign nationals working within the domestic territory.

Final Answer: Yes

Answer: (See Above)

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Q28.**Solution****Concept:**

National income accounting distinguishes between gross and net aggregates by accounting for the wear and tear of capital goods, known as depreciation or consumption of fixed capital. Gross National Product includes the total value of goods and services produced without deducting depreciation. When we subtract depreciation from GNP, we arrive at a net measure that accurately reflects the true increase in the nation's productive capacity. This net aggregate is known as Net National Product. The relationship is fundamental to understanding the difference between gross and net measures in macroeconomics.

Solution:

- (a) GNP measures the total value of final goods and services produced by the normal residents of a country, including capital consumption.
- (b) Depreciation represents the reduction in value of capital goods due to wear and tear, obsolescence, or passage of time during the production process.
- (c) Subtracting depreciation from GNP yields the Net National Product, which represents the net value of output after accounting for capital consumption.
- (d) Therefore, the blank should be filled with Net National Product or NNP.

Final Answer: Net National Product

Answer: (See Above)

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Q29.

Solution**Concept:**

The Average Propensity to Consume is one of the key concepts in Keynesian consumption theory. It measures the proportion of total income that a household spends on consumption. APC is calculated by dividing total consumption expenditure by total income. As income increases, APC tends to decline because a smaller proportion of income is spent on consumption and a larger proportion is saved. The APC can be greater than, equal to, or less than one. When consumption exceeds income (dissaving), APC is greater than one. The APC and Average Propensity to Save always sum to one.

Solution:

- (a) The formula for APC is the ratio of consumption expenditure to total income.
- (b) In the given question, the blank in the denominator of the APC formula needs to be filled.
- (c) Since $APC = \text{Consumption} / \text{Income}$, the blank should be filled with “Income.”
- (d) This formula indicates that out of every rupee of income earned, what fraction is spent on consumption goods and services.

Final Answer: Income**Answer: (See Above)**[Go Back to Question 29](#)

Q30.

Solution

Concept:

Opportunity cost is one of the most fundamental concepts in economics, first formalized by Friedrich Wieser. It represents the value of the next best alternative that must be foregone when a choice is made. Since resources are scarce and have alternative uses, choosing one option means giving up the benefits that could have been derived from the next best alternative. The concept of opportunity cost helps economists and individuals make rational decisions by comparing the relative costs and benefits of different options. It is not limited to monetary costs but also includes the implicit cost of time, effort, and resources that could have been employed elsewhere.

Solution:

- (a) When a decision-maker faces multiple alternatives, selecting one option means sacrificing the benefits of the other available options.
- (b) Opportunity cost is specifically the value or benefit of the single best alternative that is given up when a particular choice is made.
- (c) For example, if a student chooses to study economics instead of going to a movie, the opportunity cost of studying is the enjoyment that would have been derived from watching the movie.
- (d) This concept highlights that every choice has a cost, even if no money is directly spent, because the alternative use of time and resources is sacrificed.

Final Answer: Opportunity cost is the value of the next best alternative foregone when making a choice.

Answer: (See Above)

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Q31.**Solution****Concept:**

In the theory of production, the factors of production are compensated for their productive services. Labour is one of the four primary factors of production, along with land, capital, and entrepreneurship. Each factor receives a specific form of payment for its contribution to the production process. Land receives rent, capital earns interest, and entrepreneurship earns profit. Labour, which refers to all physical and mental human effort used in production, receives its payment in the form of wages. Wages can be paid on an hourly, daily, weekly, or monthly basis and represent the reward for the physical and intellectual effort of workers.

Solution:

- (a) In production theory, factors of production are rewarded for their contribution to the creation of goods and services.
- (b) Labour is the human input in production that involves both physical exertion and mental effort.
- (c) The payment made to labour for rendering its productive services is called wages.
- (d) Wages constitute a significant component of the cost of production and are determined by the forces of demand and supply in the labour market.

Final Answer: Wages**Answer: (See Above)**[Go Back to Question 31](#)

Q32.

Solution

Concept:

Marginal Cost is the additional cost incurred in producing one more unit of a commodity. It is calculated as the change in total cost divided by the change in output, or $MC = \frac{\Delta TC}{\Delta Q}$. The relationship between Marginal Cost and Average Cost is one of the most important relationships in cost theory. When MC is below AC, it pulls the AC downward. When MC is above AC, it pushes AC upward. The critical relationship is that the MC curve intersects the AC curve at the minimum point of AC. At this point, MC equals AC, and the Average Cost is at its lowest possible level for that production process.

Solution:

- (a) Marginal Cost is defined as the change in total cost resulting from producing one additional unit of output, calculated as $MC = \frac{\Delta TC}{\Delta Q}$.
- (b) As long as Marginal Cost remains below Average Cost, each additional unit produced costs less than the average, pulling the average down.
- (c) When Marginal Cost exceeds Average Cost, each additional unit costs more than the average, pushing the average up.
- (d) When Average Cost is at its minimum, Marginal Cost is exactly equal to Average Cost. The MC curve cuts the AC curve at its lowest point from below.

Final Answer: Marginal Cost is the additional cost of producing one more unit; at minimum AC, MC equals AC.

Answer: (See Above)

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Q33.

Solution

Concept:

The supply curve represents the positive or direct relationship between the price of a commodity and the quantity supplied by producers. According to the law of supply, all other things being equal, when the price of a commodity rises, it becomes more profitable for producers to supply larger quantities, as the higher price covers the increasing marginal cost of production. This positive relationship between price and quantity supplied causes the supply curve to slope upward from left to right, not downward. A downward-sloping supply curve would violate the basic economic logic of producer behaviour under normal market conditions.

Solution:

- (a) The original statement incorrectly states that the supply curve slopes downward and that producers supply more at lower prices.
- (b) This is the opposite of the law of supply. Producers supply more at higher prices, not lower prices, because higher prices generate greater revenue and profit.
- (c) The corrected sentence should state: “The supply curve slopes upward from left to right because producers supply more at higher prices.”
- (d) The upward slope reflects the direct positive relationship between price and quantity supplied that is the foundation of the law of supply.

Final Answer: The supply curve slopes upward from left to right because producers supply more at higher prices.

Answer: (See Above)

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Q34.**Solution****Concept:**

The Reserve Bank of India, as the central bank of the country, uses various quantitative instruments to regulate the money supply and credit creation in the economy. Two of the most important instruments are the Cash Reserve Ratio (CRR) and the Statutory Liquidity Ratio (SLR). The CRR is the minimum percentage of total deposits that commercial banks must maintain as cash reserves with the central bank. The SLR is the minimum percentage of total deposits that commercial banks must maintain in the form of liquid assets such as cash, gold, and government securities. Both instruments reduce the lendable resources of commercial banks and thus control credit creation.

Solution:

- (a) CRR stands for Cash Reserve Ratio. It is the proportion of total deposits that commercial banks must keep as reserves with the Reserve Bank of India.
- (b) SLR stands for Statutory Liquidity Ratio. It is the proportion of total deposits that commercial banks must maintain in the form of liquid assets.
- (c) Both CRR and SLR are mandatory reserve requirements set by the central bank to ensure the safety of deposits and to control the money supply in the economy.
- (d) By adjusting these ratios, the RBI can expand or contract the credit creation capacity of commercial banks.

Final Answer: (i) Cash Reserve Ratio, (ii) Statutory Liquidity Ratio

Answer: (See Above)

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Q35.

Solution

Concept:

The Balance of Trade and the Balance of Payments are two distinct concepts in international economics, though they are often confused. The Balance of Trade refers specifically to the difference between the monetary value of a country's exports and imports of visible goods only, also known as merchandise trade. It covers only tangible goods and does not include services, capital flows, or financial transfers. The Balance of Payments, on the other hand, is a comprehensive record of all economic transactions between a country and the rest of the world. It includes the current account (covering goods, services, income, and transfers) and the capital account (covering financial flows and investments).

Solution:

- (a) The Balance of Trade is a narrow concept that records only the export and import of visible or tangible goods.
- (b) The Balance of Payments is a much broader concept that includes not only visible trade but also trade in services, income flows, transfer payments, and capital flows.
- (c) While the Balance of Trade can be in surplus or deficit independently, the Balance of Payments always balances in an accounting sense because deficits are financed by borrowing or reserve depletion.
- (d) Therefore, the answer is No. The Balance of Trade and the Balance of Payments are not the same; the former is a component of the latter.

Final Answer: No

Answer: (See Above)

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Q36.

Solution

Concept:

In demand analysis, it is important to distinguish between a change in demand and a change in quantity demanded, as these two concepts describe fundamentally different market phenomena. An increase in demand refers to a rightward shift of the entire demand curve, caused by changes in factors other than the commodity's own price. An increase in quantity demanded refers to a movement along the same demand curve from one point to another, caused solely by a decrease in the commodity's own price. Understanding this distinction is crucial for correctly analyzing market behaviour and the effects of various economic policies.

Solution:

- (a) An increase in demand is a shift of the entire demand curve to the right. This occurs when non-price factors such as consumer income, tastes, price of related goods, or population change. For instance, if consumer income rises, the demand for normal goods increases at every price level.
- (b) An increase in quantity demanded is a movement along the same demand curve from a higher price point to a lower price point. It is caused solely by a reduction in the commodity's own price while all other factors remain constant.
- (c) The key difference is that an increase in demand involves a shift of the curve itself, whereas an increase in quantity demanded involves a movement along the existing curve.
- (d) For example, if the price of tea falls from Rs. 20 to Rs. 15 per cup, the quantity demanded may increase from 100 to 150 cups per day. This is an increase in quantity demanded. If, however, the income of consumers increases, the demand curve shifts right, representing an increase in demand.

Final Answer: An increase in demand shifts the curve; an increase in quantity demanded is a movement along the curve.

Answer: (See Above)

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Q37.

Solution

Concept:

Total Revenue is the total income earned by a firm from the sale of its output. It is calculated by multiplying the price per unit by the number of units sold at that price. In a monopoly or monopolistic competition, the firm faces a downward-sloping demand curve, meaning it must lower the price to sell additional units. As a result, Total Revenue initially increases but at a diminishing rate and may eventually decrease. The concept of Total Revenue is fundamental to understanding revenue concepts such as Average Revenue and Marginal Revenue.

Solution:

- (a) At 1 unit of output, Price = Rs. 20. Total Revenue = $20 \times 1 = 20$ Rs.
- (b) At 2 units, Price = Rs. 18. Total Revenue = $18 \times 2 = 36$ Rs.
- (c) At 3 units, Price = Rs. 16. Total Revenue = $16 \times 3 = 48$ Rs.
- (d) At 4 units, Price = Rs. 14. Total Revenue = $14 \times 4 = 56$ Rs.
- (e) The completed table shows that Total Revenue increases as more units are sold, but the rate of increase slows due to the falling price.

Output (Units)	Price (Rs.)	Total Revenue (Rs.)
1	20	20
2	18	36
3	16	48
4	14	56

Final Answer: Total Revenue values are Rs. 20, 36, 48, and 56.

Answer: (See Above)

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Q38.

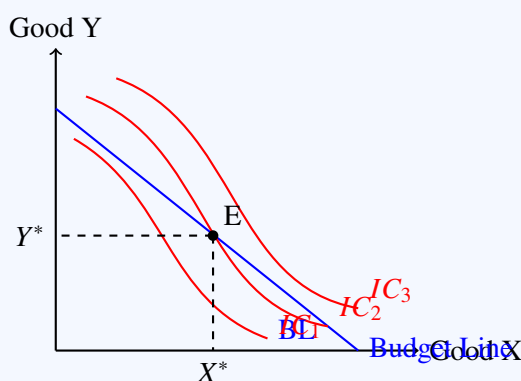
Solution

Concept:

Consumer equilibrium in the indifference curve analysis is attained at the point where the budget line is tangent to the highest attainable indifference curve. The budget line represents all combinations of two goods that a consumer can afford given their income and the prices of the goods. An indifference curve represents all combinations of two goods that give the consumer the same level of satisfaction. At the point of tangency, the slope of the budget line (which equals the price ratio) is equal to the slope of the indifference curve (which equals the Marginal Rate of Substitution). This tangency condition ensures that the consumer maximizes satisfaction within their budget constraint.

Solution:

- The horizontal axis represents the quantity of Good X, and the vertical axis represents the quantity of Good Y.
- The budget line is a straight line connecting the intercepts on both axes, representing the maximum affordable quantities of each good.
- Multiple indifference curves are drawn, with higher curves representing higher levels of satisfaction.
- Consumer equilibrium is at the point where the budget line touches (is tangent to) the highest attainable indifference curve. At this point, $MRS_{XY} = \frac{P_X}{P_Y}$.



Final Answer: Consumer equilibrium is at the tangency point E where the budget line touches the highest indifference curve.

Answer: (See Above)

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Q39.

Solution

Concept:

Supply analysis involves understanding how producers respond to price changes under different time horizons. The elasticity of supply and the shape of the supply curve depend critically on the time period under consideration. In the market period (very short run), the supply is fixed because producers have no time to adjust production. In the long run, all factors of production are variable, and firms can fully adjust their output in response to price changes, resulting in a more elastic supply curve.

Alternative (i): Elasticity of Supply

Solution:

- (a) Elasticity of supply measures the degree of responsiveness of quantity supplied to a change in the price of a commodity.
- (b) It is calculated as the ratio of the percentage change in quantity supplied to the percentage change in price.
- (c) One important factor affecting elasticity of supply is the time period. In the short run, supply tends to be inelastic because producers cannot quickly change their production capacity. In the long run, supply becomes more elastic as firms can adjust all inputs.
- (d) Other factors include the nature of the commodity, availability of inputs, and the state of technology.

Alternative (ii): Market Period and Long Period

Solution:

- (a) The market period is an extremely short time period during which the quantity of a commodity supplied is completely fixed. Producers cannot alter production levels at all, resulting in a perfectly inelastic (vertical) supply curve. Perishable goods like fresh fish or vegetables exemplify the market period.
- (b) The long period is a sufficient time frame during which firms can change all factors of production, including plant size, machinery, and workforce. Supply becomes highly elastic in the long run as firms can fully respond to price changes by expanding or contracting production capacity.

Final Answer: See above for selected alternative solution

Answer: (See Above)

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Q40.

Solution

Concept:

The government budget is a comprehensive financial statement that details the estimated receipts and expenditures of the government for a given fiscal year. Understanding the distinction between revenue and capital items is essential for analysing the fiscal health of a government. Revenue items relate to the regular income and recurring expenses, while capital items relate to asset creation, liability management, and one-time financial transactions. Similarly, fiscal deficit is an important indicator of the government's borrowing requirements.

Alternative (i): Revenue vs Capital Expenditure

Solution:

- (a) Revenue expenditure is government spending that does not create any asset or reduce any liability. It is recurring in nature. An example is the payment of interest on government borrowings or salaries of government employees.
- (b) Capital expenditure is government spending that results in the creation of physical or financial assets or reduction of existing liabilities. An example is the construction of a new national highway or repayment of government loans.
- (c) Revenue expenditure is met from current revenues and does not add to the productive capacity of the economy, whereas capital expenditure contributes to future economic growth.

Alternative (ii): Fiscal Deficit

Solution:

- (a) Fiscal deficit is the difference between the total expenditure of the government and its total receipts excluding borrowings. It is calculated as: $\text{Fiscal Deficit} = \text{Total Expenditure} - \text{Total Receipts (excluding borrowings)}$.
- (b) The fiscal deficit indicates the total borrowing requirements of the government during the fiscal year. A high fiscal deficit means the government must borrow heavily, which can lead to higher interest rates and inflationary pressures in the economy.
- (c) Managing the fiscal deficit is crucial for macroeconomic stability, as excessive government borrowing can crowd out private investment and increase the debt burden on future generations.

Final Answer: See above for selected alternative solution

Answer: (See Above)

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Q41.

Solution

Concept:

The Balance of Payments account classifies all international economic transactions into different categories. Autonomous transactions are those that are undertaken for profit or business motives and are independent of the state of the Balance of Payments. Accommodating transactions, on the other hand, are undertaken specifically to cover deficits or surpluses in the autonomous transactions. The distinction is important because the Balance of Payments is said to be in equilibrium when only autonomous transactions balance. The current account records all transactions related to trade in goods and services, income flows, and unilateral transfers.

Alternative (i): Autonomous vs Accommodating Transactions

Solution:

- (a) Autonomous transactions are independent economic transactions undertaken purely for profit or business motives, such as export and import of goods, remittances for investment, and foreign loans for commercial purposes. They are not influenced by the state of the Balance of Payments.
- (b) Accommodating transactions are those that take place to cover the deficit or surplus in the Balance of Payments resulting from autonomous transactions. Examples include borrowing from the International Monetary Fund or drawing down foreign exchange reserves.

Alternative (ii): Current Account Components

Solution:

- (a) The current account of the Balance of Payments includes the trade balance (exports and imports of visible goods), the services balance (trade in invisible services such as banking, tourism, and IT services), income receipts and payments (investment income, wages), and unilateral transfers (remittances, foreign aid, gifts).
- (b) A surplus in the current account means the country earns more from exports and income receipts than it pays for imports and income payments. A deficit indicates the opposite.

Final Answer: See above for selected alternative solution

Answer: (See Above)

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Q42.

Solution

Concept:

The Law of Diminishing Marginal Utility is one of the fundamental laws of consumer behaviour, first systematically explained by Alfred Marshall. It states that as a consumer consumes successive units of a commodity, the marginal utility derived from each additional unit tends to diminish, other things remaining constant. This law is based on the psychological reality that the intensity of a want decreases as it is progressively satisfied. The law forms the basis of the downward-sloping demand curve, as a consumer is willing to pay less for additional units of a commodity because they derive less satisfaction from each successive unit.

Solution:

- (a) Consider the following utility schedule for a consumer consuming units of a commodity:

Units	Total Utility	Marginal Utility
1	10	10
2	18	8
3	24	6
4	28	4
5	28	0
6	26	-2

- (b) As the consumer consumes more units, marginal utility falls from 10 to 8, 6, 4, 0, and eventually becomes negative.
- (c) Assumptions of the law include: the consumer is rational, consumption is continuous, the units of the commodity are homogeneous, there is no change in the consumer's income or tastes, and the prices of other goods remain constant.

Final Answer: Marginal utility decreases with each additional unit consumed, assuming all other factors remain constant.

Answer: (See Above)

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Q43.

Solution

Concept:

Consumer equilibrium involves understanding how a consumer allocates their limited income between two goods to maximize satisfaction. The Marginal Rate of Substitution (MRS) and the budget constraint are central to this analysis. MRS represents the rate at which a consumer is willing to give up one good to obtain an additional unit of another while maintaining the same level of satisfaction. The budget constraint represents the combinations of goods a consumer can afford.

Alternative (i): MRS and Indifference Curves

Solution:

- The Marginal Rate of Substitution is the rate at which a consumer is willing to substitute one good for another along an indifference curve. Mathematically, $MRS_{XY} = \frac{MU_X}{MU_Y} = -\frac{\Delta Y}{\Delta X}$.
- The MRS diminishes because of the law of diminishing marginal utility. As a consumer acquires more units of Good X, the marginal utility of X falls relative to the marginal utility of Y. Therefore, the consumer is willing to give up fewer and fewer units of Y for each additional unit of X.
- This diminishing MRS gives the indifference curve its characteristic convex shape to the origin.
- At the equilibrium point, $MRS_{XY} = \frac{P_X}{P_Y}$, meaning the consumer's subjective rate of substitution equals the market rate of exchange.

Alternative (ii): Budget Equation and Maximum Quantity

Solution:

- Given: Price of X (P_X) = Rs. 4, Price of Y (P_Y) = Rs. 5, Income (M) = Rs. 200.
- The budget equation is: $P_X \times Q_X + P_Y \times Q_Y = M$, which gives $4Q_X + 5Q_Y = 200$.
- To find the maximum quantity of X, set $Q_Y = 0$: $4Q_X = 200$, so $Q_X = 50$.
- The consumer can purchase a maximum of 50 units of Good X if they do not buy any of Good Y.

Final Answer: (i) MRS diminishes due to diminishing marginal utility; (ii) Budget equation: $4Q_X + 5Q_Y = 200$, maximum X = 50 units.

Answer: (See Above)

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Q44.

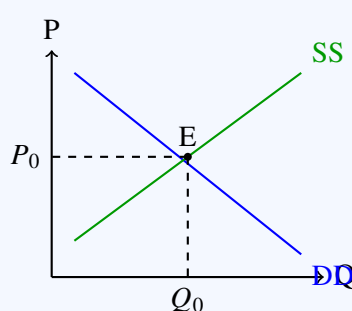
Solution

Concept: Downward-sloping market demand (DD) and upward-sloping market supply (SS), where quantity demanded equals quantity supplied ($QD = QS$).

Alternative (i): Price Determination

Solution:

- Market demand (DD) and market supply (SS) represent aggregate consumer and producer behaviors.
- If price is above P_0 , $QS > QD$ (surplus), driving price down. If price is below P_0 , $QD > QS$ (shortage), pushing price up.

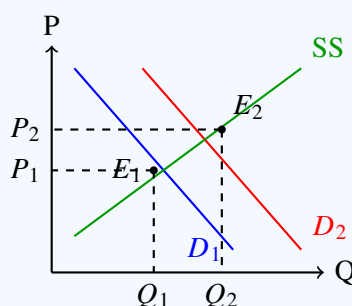


—OR—

Alternative (ii): Increase in Demand

Solution:

- An increase in demand shifts the demand curve rightward from D_1 to D_2 , leaving supply (SS) unchanged.
- At the original price, a shortage (excess demand) emerges, exerting upward pressure on price.
- As price rises, expansion of supply and contraction of new demand lead to a new equilibrium E_2 with both higher price (P_2) and quantity (Q_2).



Final Answer: See diagrams above for the selected alternative solution.

Answer: (See Above)

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Q45.

Solution

Concept:

National income can be measured using three methods: the Income Method, the Expenditure Method, and the Product (Output) Method. Each method provides the same aggregate figure when calculated correctly. The distinction between Real and Nominal GDP is crucial for understanding economic welfare because it addresses whether changes in GDP reflect actual changes in output or merely changes in prices.

Alternative (i): Income Method

Solution:

- (a) The Income Method measures national income by summing all factor incomes earned by the residents of a country for their contribution to production. The components include: Compensation of Employees (wages, salaries, bonuses), Rent and Royalties, Interest, Profit (corporate profits and proprietors' income), and Mixed Income of self-employed individuals.
- (b) From the sum of these factor incomes, we get Net Domestic Product at Factor Cost. Adding Net Factor Income from Abroad gives Net National Product at Factor Cost, which is National Income.
- (c) Precautions to avoid double counting: Only factor incomes earned from productive activities should be included. Transfer payments such as pensions, scholarships, and gifts must be excluded because they are not payments for current production. Income from the sale of second-hand goods should also be excluded.

Alternative (ii): Real GDP vs Nominal GDP

Solution:

- (a) Nominal GDP is measured at current market prices and can increase due to either an increase in output or an increase in the general price level (inflation). It does not reflect true changes in economic welfare.
- (b) Real GDP is measured at constant (base year) prices and adjusts for inflation. It reflects the actual volume of goods and services produced, making it a more accurate indicator of economic performance.
- (c) Real GDP is a better indicator of economic welfare because it isolates the effect of price changes and measures only the real increase in output and productive capacity. An increase in Real GDP means that the economy is genuinely producing more goods and services for its population.

Final Answer: See above for selected alternative solution

Answer: (See Above)

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Q46.

Solution

Concept:

Commercial banks play a vital role in the economy by accepting deposits and creating credit through the process of lending. The central bank regulates this credit creation capacity through various monetary policy instruments. Credit creation is the process by which banks expand the total money supply in the economy by lending out a portion of the deposits they receive, while maintaining a fraction as reserves.

Alternative (i): Credit Creation by Commercial Banks

Solution:

- (a) When a commercial bank receives a deposit, it does not keep the entire amount as reserves. It retains a fraction as cash reserves (determined by the CRR) and lends out the remainder.
- (b) The borrower spends the loan amount, which eventually gets deposited into another bank. This second bank also retains a fraction and lends out the rest. This process continues through multiple rounds, creating deposits that are multiples of the original deposit.
- (c) The total credit creation is calculated as: $\text{Total Deposits} = \text{Initial Deposit} \times \text{Credit Multiplier}$, where $\text{Credit Multiplier} = \frac{1}{\text{CRR}}$.
- (d) The Cash Reserve Ratio plays a critical role: a higher CRR means banks must keep more reserves and can lend less, reducing credit creation. A lower CRR has the opposite effect.

Alternative (ii): Monetary Policy Instruments

Solution:

- (a) **Open Market Operations:** The buying and selling of government securities by the central bank. Buying securities injects money into the economy, while selling absorbs liquidity.
- (b) **Bank Rate:** The rate at which the central bank lends to commercial banks. An increase in the bank rate makes borrowing expensive, reducing credit creation.
- (c) **Cash Reserve Ratio (CRR):** The minimum fraction of deposits banks must keep with the central bank. Increasing CRR reduces lendable funds.
- (d) **Statutory Liquidity Ratio (SLR):** The minimum fraction of deposits banks must maintain as liquid assets. Increasing SLR restricts credit expansion.
- (e) **Margin Requirements and Moral Suasion:** Qualitative tools that guide the lending behaviour of commercial banks.

Final Answer: See above for selected alternative solution

Answer: (See Above)

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Q47.

Solution

Concept:

The Keynesian framework provides foundational concepts for understanding how national income, consumption, and investment interact to determine the level of economic activity. The investment multiplier and the consumption function are two central pillars of this framework.

Alternative (i): Investment Multiplier

Solution:

- The investment multiplier shows how an initial change in investment leads to a magnified change in national income. Consider an initial investment of Rs. 100 crore with an MPC of 0.8.
- In Round 1, investment of Rs. 100 crore creates Rs. 100 crore of income. Recipients spend 80% (Rs. 80 crore) and save 20% (Rs. 20 crore).
- In Round 2, Rs. 80 crore becomes new income, of which Rs. 64 crore is spent and Rs. 16 crore is saved.
- This process continues until the total increase in income = $100 + 80 + 64 + 51.2 + \dots = 100 \times \frac{1}{1-0.8} = 100 \times 5 = 500$ crore.
- The multiplier value is 5, meaning the national income increases by 5 times the initial investment.

Alternative (ii): Consumption Function, APC, and MPC

Solution:

- The Keynesian Consumption Function states that consumption expenditure is a function of national income: $C = \bar{C} + cY$, where $\bar{C}$ is autonomous consumption (consumption at zero income) and c is the MPC.
- Average Propensity to Consume (APC) is the ratio of total consumption to total income: $APC = \frac{C}{Y}$. As income increases, APC tends to decline.
- Marginal Propensity to Consume (MPC) is the ratio of change in consumption to change in income: $MPC = \frac{\Delta C}{\Delta Y}$. It remains constant in the linear consumption function and lies between 0 and 1.
- The key difference: APC measures the proportion of total income spent on consumption, while MPC measures the fraction of each additional rupee of income that is spent. APC can be greater than 1 (when consumption exceeds income), but MPC always lies between 0 and 1.

Final Answer: See above for selected alternative solution

Answer: (See Above)

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Q48.

Solution

Concept:

The production function describes the relationship between inputs (factors of production) and output. When one input is varied while others are kept fixed, the resulting output patterns are described by Total Product (TP), Marginal Product (MP), and Average Product (AP). TP is the total output produced, MP is the additional output from using one more unit of the variable input, and AP is the output per unit of the variable input. These three concepts are interrelated and follow specific patterns that reflect the law of variable proportions.

Solution:

- (a) At 0 units of labour, TP = 0. MP and AP are undefined (denoted as –).
- (b) At 1 unit, TP = 12. MP = $12 - 0 = 12$. AP = $\frac{12}{1} = 12$.
- (c) At 2 units, TP = 30. MP = $30 - 12 = 18$. AP = $\frac{30}{2} = 15$.
- (d) At 3 units, TP = 45. MP = $45 - 30 = 15$. AP = $\frac{45}{3} = 15$.
- (e) At 4 units, TP = 52. MP = $52 - 45 = 7$. AP = $\frac{52}{4} = 13$.
- (f) At 5 units, TP = 52. MP = $52 - 52 = 0$. AP = $\frac{52}{5} = 10.4$.
- (g) We observe that MP rises initially (12 to 18), then starts declining (15, 7, 0), demonstrating the law of diminishing marginal returns. AP rises to a maximum of 15 and then falls.

Units of Labour	Total Product (TP)	Marginal Product (MP)	Average Product (AP)
0	0	–	–
1	12	12	12
2	30	18	15
3	45	15	15
4	52	7	13
5	52	0	10.4

Final Answer: Completed table as shown above.

Answer: (See Above)

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Q49.

Solution

Concept: A government budget estimates annual receipts and expenditures. Receipts are categorized into Revenue Receipts (do not alter asset-liability status) and Capital Receipts (alter asset-liability status).

Solution:

- (a) **Revenue Receipts:** Neither create liabilities nor reduce assets.
- **Tax Revenue:** Compulsory payments like income tax, corporate tax, and GST.
 - **Non-Tax Revenue:** Profits from public enterprises, interest receipts, fees, fines, and dividends.
- (b) **Capital Receipts:** Either create a liability or reduce a government asset.
- **Borrowings:** Loans raised from domestic or international market sources (creates liability).
 - **Recovery of Loans:** Return of funds loaned to states or public entities (reduces asset).
 - **Disinvestment:** Sale of government equity stakes in public enterprises (reduces asset).
- (c) **Key Distinction:** Revenue receipts are recurring and do not change the asset-liability position, whereas capital receipts are non-recurring and structurally alter liabilities or assets.

Final Answer: Revenue receipts neither create liabilities nor reduce assets (e.g., taxes, dividends); capital receipts either create liabilities or reduce assets (e.g., borrowings, disinvestment).

Answer: (See Above)

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Q50.

Solution

Concept: In the Keynesian framework, equilibrium national income is achieved where aggregate demand equals aggregate supply ($AD = AS$). Deviations create inflationary or deflationary gaps, which are managed via fiscal policy.

Alternative (i): Aggregate Demand and Equilibrium

Solution:

(a) **AD-AS Approach:** In a two-sector economy, $AD = C + I$. Given $C = \bar{C} + cY$ and autonomous investment $I = \bar{I}$, the aggregate demand identity is $AD = (\bar{C} + \bar{I}) + cY$.

(b) Equilibrium occurs when $Y = AD \rightarrow Y = (\bar{C} + \bar{I}) + cY$. Rearranging yields:

$$Y = \frac{\bar{C} + \bar{I}}{1 - c}$$

(c) **Saving-Investment Approach:** Alternatively, equilibrium requires planned saving to equal planned investment ($S = I$). Given $S = -\bar{C} + (1 - c)Y$, setting $S = \bar{I}$ yields identical equilibrium income: $Y = \frac{\bar{C} + \bar{I}}{1 - c}$.

—OR—

Alternative (ii): Excess and Deficient Demand

Solution:

(a) **Excess Demand (Inflationary Gap):** AD exceeds full-employment output. It leads to demand-pull inflation, rising price levels, and resource over-utilization without increasing real output.

(b) **Deficient Demand (Deflationary Gap):** AD falls below full-employment output. It results in involuntary unemployment, under-utilization of resources, and economic recession.

(c) **Fiscal Policy Corrections:**

- **For Excess Demand (Contractionary):** Reduce government spending (G) and increase direct taxes (T) to curb disposable income and aggregate purchasing power.
- **For Deficient Demand (Expansionary):** Increase government spending (G) on public works and reduce taxes (T) to stimulate consumption and investment.

Final Answer: See structural text above for the selected alternative solution.

Answer: (See Above)

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Answer Key

Q	Ans	Q	Ans	Q	Ans	Q	Ans	Q	Ans
1	B	2	B	3	B	4	B	5	B
6	B	7	C	8	B	9	D	10	C
11	C	12	D	13	B	14	C	15	B
16	C	17	B	18	C	19	B	20	B

