I. Choose the correct answer

CHAPTER-1	
1. The author of wealth definition is : (a) Alfred Marshall b) Lionel Robbinsc) Adam Smith d) Samuelson	Adam Smith
2. The author of scarcity definition is (a) Adam Smith (b) Samuelson (c) Alfred Marshall (d) Lionel Robbins	Lionel Robbins
3. The concept of Net Economic Welfare has been given by (a) Samuelson (b) Marshall (c) Adam Smith (d) Lionel Robbins	Samuelson
4. Economics is a a) positive science b) normative science c) Both d) none	Both
5. In economics, we make use of a) deductive method b) inductive methodc) both d) none	Both
CHAPTER-2	
1. The basic economic problems are common to a) Capitalism b) Socialism c) Mixed economy d) All the above	All the above
2. Traditional economy is a a) Subsistence economy b) Market economy c) Command economy d) Monetary economy	Subsistence economy
3. The basic force that drives the capitalist economy is a) Planning b) Technology c) Government d) Profit – motive	Profit – motive
4. In a socialist economy, all decisions regarding production and distribution are taken by : a) Market forces b) Central planning authority c) Customs and traditions d) Private sector.	Central planning authority
5. Redtapism and corruption lead to a) Inefficiency of production b) Inequality of income and wealth c) Absence of technology d) Efficient use of resources	Inefficiency of production
CHAPTER-3	
1. Necessaries, comforts and luxuries are a) Classification of goods and services b) Classification of wants c) Classification of utility d) None of the above	Classification of goods and services
2. The Indifference curve approach was introduced by a) Alfred Marshall b) Lionel Robbins c) J.R. Hicks and R.G.D. Allen d) Adam Smith	J.R. Hicks and R.G.D. Allen
3. Utility is a a) Social concept b) Subjective / psychological concept c) Political concept d) Scientific concept	Subjective / psychological concept
4. Single commodity consumption mode is a) Production possibility curve b) Law of Equi-marginal utility c) Law of supply d) Law of Diminishing Marginal Utility	Law of Diminishing Marginal Utility
5. Consumer surplus is a) Potential Price – Actual Price b) MUn = TUn –TUn-1	Potential Price – Actual Price

c) Demand = supply d) None	
CHAPTER-4	
1. Demand for a commodity depends on a) Price of that commodity b) Price of related goods c) Income d) All the above	All the above
2. Law of Demand establishes a) inverse relationship between price and quantity b) Positive relationship between price and quantity c) Both d) None	inverse relationship between price and quantity
3. Increase in demand is shown by a) Movement along the same demand curve b) Shifts of the demand curve c) The highest point on the demand curve d) Lowest point on the demand curve	Shifts of the demand
4. The degree of response of demand to change in price is a) Income elasticity of demand b) Cross – elasticity of demand c) Price elasticity of demand d) All the above.	Price elasticity of demand
5. Factors determining supply are : a) Production technology b) Prices of factors of production c) Taxes and subsidies d) All the above	All the above
CHAPTER-5	
1. At the point of equilibrium a) Only one price prevails b) Quantity demanded = quantity supplied c) The demand curve intersects the supply curve d) All the above	All the above
2. Above the equilibrium price a. S < D b. S > D c. S = D d. none	S > D
3. Changes in quantity demanded occur a. Only when price changes b. Due to change of taste c. both d. None	Only when price changes
4. The time element in price analysis was introduced by a. J.R. Hicks b. J.M. Keynes c. Alfred Marshall d. J.S. Mill	Alfred Marshall
5. In the long period a. All factors change b. Only variable factor changes c. Only fixed factor changes d. Variable and fixed factors remain constant.	All factors change
CHAPTER-6	
1. Production refers to a. destruction of utility b. creation of utilities c. exchange value d. None	creation of utilities
2. The initial supply price of land is a. Zero b. Greater than one C. Less than one d. Equal to one	Zero
3. Labour cannot be separated from a. Capital b. labourer c. profit d. organization	labourer
4. reward paid to capital is a. interest b. profit c. wages d. rent	interest
5. A successful entrepreneur is one who is ready to accept	Risks

a. Innovations b. Risks c. deciding the location of the production unit d. none.	
CHAPTER-7	
1. real cost is a) pain and sacrifice b) subjective concept c) efforts and foregoing leisure d) All the above	All the above
2. Economic cost includes explicit cost and a) implicit cost b) social cost c) fixed cost d) money cost	implicit cost
3. social costs are those costs a) not borne by the firms b) incurred by the society c) health hazards d) all of these	all of these
4. Average fixed cost is obtained by dividing a) TC/Q b) TFC/Q c) TVC/Q d) None	TFC/Q
5. Marginal revenue is the least addition made to the a) average revenue b) Total production c) Total revenue d) none	Total revenue
CHAPTER-8	
1. Perfect competition is a market situation where we have a single seller a. a single seller b. two sellers c. large number of sellers d. few sellers	large number of sellers
2. A firm can achieve equilibrium when its a. MC = MR b. MC = AC c. MR = AR d. MR = AC	MC = MR
3. The firm and industry are one and the same under a. perfect competition b. duopoly c. oligopoly d. monopoly	monopoly
4. Under perfect competition, the demand curve is a. Upward sloping b. horizontal c. downward sloping d. vertical	horizontal
5. Most important form of selling cost is a. Advertisement b. Sales c. Homogeneous product d. None	Advertisement
CHAPTER-9	
1. Rent is the price paid for the use of a) Capital b) Organisation c) Labour d) Land	Land
2. Profits are the reward for a) land b) capital c) labour d) organisation	organisation
3. The demand for labour is a) effective demand b) direct demand c) derived demand d) elastic demand.	derived demand
4. The author of the concept of quasi – rent is a) Adam Smith b) Marshall c) Ricardo d) Samuelson	Marshall
5. The author of liquidity preference theory is a) J.M. Keynes b) Marshall c) Samuelson d) Knight	J.M. Keynes

CHAPTER-10	
1. The macro economic thinking was revolutionized by a) David Ricardo b) J.M. Keynes c) Adam Smith d) Malthus	J.M. Keynes
2. The Classical Theory assumed the existence of a) Unemployment b) Disguised unemployment c) Full employment d) Under-employment	Full employment
3. The central problem in Macro Economics is a) Income and employment b) Price and Output c) Interest and Money d) None	Income and employment
4. To explain the simple theory of income determination, Keynes used a) Consumption and Investment b) Aggregate demand and aggregate supply c) Production and Expenditure d) All the above	Aggregate demand and aggregate supply
5. The marginal propensity to consume a) $\Delta S/\Delta Y$ b) C/y . c) $\Delta P/\Delta Q$ d) $\Delta C/\Delta Y$	$\Delta C/\Delta Y$

CHAPTER-11	
1. Monetary policy is controlled by a) central government b) state government c) central bank d) private sector.	central bank
2. Currency with the public is known as a) M1 b) M2 c) M3 d) M4	M1
3. Bank rate is raised during a) deflation b) inflation c) stable prices d) unemployment	inflation
4. During inflation a) businessmen gain b) wage earners gain c) salaried people gain d) Rentiers gain	businessmen gain
5. A situation marked by rising prices and stagnation in demand is known as a) cost-push inflation b) demand – pull inflation c) stagflation d) wage – push inflation.	stagflation

CHAPTER-12	
1. Public finance is concerned with the income and expenditure of a) Private sector b) Agricultural sector c) Public authorities d) Industrial sector	Public authorities
2. Tax revenue deals with the a) Fees b) Kinds of taxes c) Revenue d) Non tax revenue	Kinds of taxes
3. The federal form of government consists of a) central, state and local government b) central and state government c) state and local government d) above all	central, state and local government
4. The compulsory charge levied by the government is a) Licence b) Gifts and grants c) Loan d) Tax	Tax
5. In ZBB every year is considered as a a) base year b) financial year c) new year d) academic year	new year

Fill in the blanks

CHAPTER-1

1. The term “micro” means_________	small
2. Strictly speaking production refers to the creation of_________	utilities
3. Exchange of goods for goods is known as _________	barter
4. Economics is a _________ science	social
5. An example of cosmopolitan wealth is _____________	ocea

CHAPTER-2

1) In a traditional economy, basic problems are solved by____ and _____.	Customs and Traditions
2) Most of the economic activities of capitalism are centered on__________	Price Mechanism
3) Production possibility curve is also known as _____________	Transformation / producton possibility frontier
4) The prime motive of socialist economy is _______________	Social /COLLECTIVE WELFARE
5) Under mixed economy, the economic control is exercised by _________ and ____________ sectors.	Private and public.

CHAPTER-3

1. ____________ means using up of goods and services	Consumption
2. wants may be both ________ and _________	Competitive and complementary
3. Marshallian utility approach is ________ analysis	Cardinal utility analysis
4. Marginal utility falls to zero, when the total utility is __________	Total utility
5. An indifference curves is __________ to the origin	“Principles of Economics"

CHAPTER-4

1. The demand curve slopes downwards due to __________	Law of diminishing marginal utility
2. Adding up of individual consumers schedule is __________	Market demand schedule
3. Goods that are demanded for their social prestige come under _____ effect.	Veblen effect
4. The concept of elasticity of demand was introduced by __________	Alfred Marshall
5. The rate of change of supply to a change is price is ___________	Elasticity of supply.

CHAPTER-5

1. ____________ is the major determinant of supply	Price
2. Agriculture, industry, growth and distribution are the _______ of the economy.	Sub-systems
3. At ___________ price, there is no tendency to change the price or quantity.	Equilibrium
4. Modern economists divide time periods into ______ and ________	Short period and long period
5. The supply curve in the market period is a _________ line.	Vertical

CHAPTER-6

1. Land and labour are called ____________ factors	primary
2. An enquiry into the nature and causes of wealth of nations was written by _________	Adam Smith
3. ___________ is limited by the extent of market.	Division of labour
4. ____________ is man-made physical goods used to produce other goods.	capital

CHAPTER-7	
1. Money cost is also called ________	Nominal cost
2. Economic profit is the difference between total revenue and_________	Economic cost
3. the distinction between the fixed and variable factors is possible only in _____________	Short run
4. Total cost is the sum ____________	total fixed cost and total variable cost
5. The marginal cost curve is _________ shaped	'U' shaped

CHAPTER-8	
1. Under perfect competition, the firms are producing ____________product.	homogeneous
2. When the Average revenue of the firm is greater than its average cost, the firm is earning __________	Super normal profit
3. The perfect competitive firms are ___________	price-take
4. Monopoly power achieved through patent right is called _________	legal monopoly
5. Firms realize the importance of ___________ under oligopoly.	mutual co-operation

CHAPTER-9	
1. Marginal productivity theory is the _____________theory ofdistribution.	general
2. Marginal productivity theory is based on the assumption of ____________ competition.	perfect
3. Transfer earnings refer to _____________ cost	opportunity
4. Money wages are also known as ____________ wages	nominal
5. Organization is done by the _____________	entrepreneur

CHAPTER-10	
1. The term consumption function explains the relationship between________ and ________	Income and Consumption
2. _________ is the ratio of charge in saving to a change in income.	Marginal Propensity to save
3 The worldwide depression of 1930s was also caused by a ________	Fall in investment
4. __________ refers to the cash holdings of the people.	Liquidity Preference
5. The magnified effect of initial investment on income is called______ effect.	Multiplier

CHAPTER-11	
1. The direct exchange of goods for goods is known as ___________	barter
2. Deflation is a period marked by __________ prices	falling
3. The equation of exchange (MV = PT) was given by	Irving Fisher
4. Galloping inflation is also known as _____________	hyper-inflation or run-away inflation
5. Monetary policy is usually effective in controlling _____________	inflation

CHAPTER-12	
1. _______ means different sources of government income	public revenue
2. the absence of direct and proportional benefit is ________	quid pro – quo
3. __________ are considered as fundamental principles of taxation	canons of taxation
4. The classification of direct and indirect taxes is based on criterion of _________ tax	shifting of the incidence
5. tax is a blend of progressive tax and proportional tax.	digressive

Match the following:

CHAPTER-	
1. “Principles of Economics”	Marshall
2. First Nobel prize	Tinbergen and Frisch
3. Dynamic approach	Time Element
4. Wealth	Stock
5. Income	Flow
CHAPTER-2	
1. Minimum cost	Maximum benefit
2. opportunity cost	next alternative forgone
3. private property	Laissez faire economy
4. Bureaucratic expansion	socialism
5. Market forces	supply, demand and price
CHAPTER-3	
1. Wants	Advertisements
2. “Principles of economics”	Marshall
3. Maximum social advantage	Hicks and Dalton
4. Indifference curve	Ordinal Ranking
5. Luxuries	Diamond, Jewels
CHAPTER-4	
1. Positive relationship of	Veblen effect
2. Tea and coffee	substitutes price and demand
3. Segment between two points	Arc
4. Ed>	elastic demand
5. Cross-elasticity is zero	X and Y are not related
CHAPTER-5	
1. Equilibrium	Pair of price and quantity
2. Excess demand	D > S
3. Price discount	Annual stock clearance
4. Long period supply curve	More elastic
5. Short period price	Demand and supply.
CHAPTER-6	
1. Entrepreneur, an innovator	Schumpeter
2. Division of labour	Adam Smit
3. Production function	Cobb – Douglas
4. bundle of risks	Hawley
5. Exertion of body or mind	Marshall
CHAPTER-7	
1. Average cost	cost per unit
2. TC	TFC + TVC
3. The long run average cost curve	planning curve

4. MCn	TCn – TCn-
5. Profit	TR – TC

CHAPTER-8	
1. Global market	Gold and silver
2. Consumer sovereignty	perfect competition
3. South Africa	diamond
4. Technical monopoly	Coco Cola
5. monopolistic competition	E.H. Chamberlin
CHAPTER-9	
1. Residual claimant theory	Walker
2. Waiting theory of Interest	Marshall
3. Loanable Funds Theory	Neo-classical theory
4. Dynamic Theory of profit	Clark
5. Risk-bearing theory of profit	Hawley
CHAPTER-10	
1. Aggregate Demand	C + I + G +(X-M)
2. Slope	Vertical Change/Horizontal Change
3. K	1/1-MPC
4. Y	C + S
5. Keynes	Liquidity Preference
CHAPTER-11	
1. Quantitative credit control	Bank rate
2. Selective credit control	Moral Suasion
3. cheap money policy	Low rate of interest
4. wages and prices push	Creeping inflation.
5. Value of money	Purchasing power of money one another
CHAPTER-12	
1. Conons of taxation	Adam Smith
2. Progressive tax	Best tax system
3. Fiscal policy	rebate and subsidies
4. Regressive tax d. Revenue and expenditure are equal	Tax rate decreases
5. Balanced budget	Tax rate decreases

IV. Answer each one of the questions in a word or two :

CHAPTER-1	
1. What is the other name for Economics ?	political economy
2. What are the subjects that econometrics make use of ?	Statistics, mathematics, economics
3. What is the method that Ricardo made use of ?	Inductive method
4. Give one or two examples of free goods.	air, sunshine
5. What is the other name for money income ?	nominal income
CHAPTER-2	
1. Is traditional economy a subsistence economy ?	Yes
2. What is the basic force that drives a capitalist economy ?	Profit Motive
3. What is the result of over-production ?	Depression
4. Name any two successful socialist economies.	China and Cuba
5. Is there planning under mixed economy ?	Yes
CHAPTER-3	
1. Define Utility	Want satisfying power
2. What is the other name for the law of Equi-Marginal Utility	Gossen's second law
3. What is Indifference curve ?	Locus of different combinations of two commodities
4. What is Indifference Map ?	It is a group of indifference curves for two commodities
5. What is the other name for budget line ?	Price – ratio line
CHAPTER-4	
1. What is the basic assumption of economic theory ?	Other things being equal / ceteris paribus condition
2. How does the demand change during boom and depression ?	During boom demand increases and during depression demand
3. Give the formula for point method	ep = lower segment of the demand curve / upper segment of the demand curve
4. What is income elasticity of demand ?	The degree of responsiveness of demand to change in income.
5. When the demand for labour is inelastic, can a trade union raise wages ?	Yes
CHAPTER-5	
1. What is equilibrium in general ?	State of rest / balance
2. What are the determinants of shift in demand curve ?	Income, taste, price of substitutes
3. Who has introduced the time element ?	Alfred Marshall
4. Give an example for fixed input ?	Heavy machinery / building
5. Is supply fixed in the market period ?	Yes
CHAPTER-6	
1. Who is the changing agent of the society ?	Entrepreneur
2. How do internal economies arise ?	From within the firm
3. What is other name for isoquant ?	Iso-Product curve
4. Give the condition for producer's equilibrium ?	MRTS xy = Px / Py
5. State the Cobb-Douglas production function.	Q = b La Cb

CHAPTER-7	
1. When average revenue remains constant what will be M.R. ?	M.R. remains constant / coincide with A.R.
2. What is Marginal Revenue ?	Addition made to the total revenue.
3. What is break-even point ?	No - profit no-loss point
4. What is an envelope curve ?	It is a group of short run cost curves / planning curve
5. How will you calculate AC ?	TC/q

CHAPTER-8	
1. What is an industry?	Group of firms
2. Who undertakes the public utilities?	state
3. How does the government control monopoly?	taxation / legislative method
4. What is the essential feature of monopolistic competition?	product differentiation
5. In which year the MRTP Act was passed?	1969

CHAPTER-9	
1. According to Ricardio, do all lands get rent ?	No
2. Even if all lands are equally fertile, can rent arise ?	Yes
3. Who is the author of Agio theory of interest ?	Bohm-Bawerk
4. Who is the author of the rent theory of profits ?	Walker
5. What is the name of Schumpeter's theory of profits ?	Innovation theory

CHAPTER-10	
1. What crippled the free enterprise economies of US and UK?	Great Depression
2. State J.B. Say's Law of Market.	Supply creates its own demand
3. Who is the author of the "General Theory of Employment, Interest and Money"?	Keynes
4. Name the point of intersection of Aggregate Demand and Aggregate Supply	Keynesian cross
5. Give the formula for Multiplier	K = 1 / 1-MPC

CHAPTER-11	
1. Name the bank which controls money supply in a country.	central bank
2. When is dear money policy followed ?	during inflation
3. What is the name of inflation without a rise in price level ?	suppressed inflation
4. Is wage cut a remedy for depression?	No
5. Give the example of a country that experienced hyperinflation.	Germany

CHAPTER-12	
1. What is a tax ?	Compulsory contribution
2. Give the expansion for VAT	value added tax
3. What is the meaning of proportional tax ?	uniform tax rate
4. What are the kinds of budget ?	balanced and unbalanced budget
5. What is public debt ?	borrowing from the public

1.What are the basic issues of any society?

The basic issues of any society are:

1.What to produce and in what quantities?

2.How shall goods be produced?

3.For Whom shall the goods be produced?

2.Name the important general economic systems?

The important general economic systems are:

1.Traditional Economy.

2.Capitalist Economy.

3.Socialist Economy and

4.Mixed Economy

3.List the basic features of socialism

The basic features of socialism are:

1.In socialist economies, social or collective welfare will be the prime motive.

2.The right to private property is limited.

3.Most of economic policy decisions will be taken by a centralized planning, and

4.Market forces have only a limited role to play.

4.Is India a mixed economy?

Yes, India is a mixed economy, because it possess all the following features of the mixed economy.

1.In a mixed economy both public and private instutions exercise economic control.

2.The public sector functions as a socialistic economy and the private sector as a free enterprise economy.

3.All decisions recording, what, how, and for whom to produce are taten by the state.

5.What is opportunity cost?

The opportunity cost of an action is the value of next best alternative forgone. For example, if you choose to watch cricket in TV., you must give up an extra hour study. Thus by watching TV., you have forgone the opportunity of scoring an extra five or ten marks in examination.

6.What is equilibrium price?

There is only one price at which the preferences of sellers and buyers meet together. At the point the quantity demanded of a commodity by the buyer is equivalent to the quantity the seller is willing to sell. This price is called as the equilibrium price and it occurs at the point of intersection of the supply curve and the demand curve.

7.Distinguish between change in demand and shift in demand.

Changes in quantity demanded occur only when there is change in the price. The change in the the price quantity schedule brings movements on the demand curve. Any change in the other determinants like income and tastes will shift the demand curve as a whole.

8. What are the determinants in shift in supply?

Price is the major determinant of supply. The determinants which will shift the entire supply curve is the price of factors of production, i.e. land and labour.

9.Differentiate the short period from the long period.

The short period for a firm is the time period during which at least one of the inputs is fixed input.

The long period is the time period during which all the inputs are variable inputs.

The specific duration of the short period and long period will vary from the firm to firm.

10.Write a short note on market period.

Market period is the period during which the ability of the firms to affect any changes in supply in response to any change in demand is extremely limited or almost nil. Thus supply is more or less fixed in the market period without any change.

11.Name the types of utility.

Production means the creation of utilities. These utilities are in the nature of

1) form utility

2) place utility

3) time utility and

4) possession utility.

12.Define labour.

Alfred Marshall defines labour as " the use or exertion of body or mind, partly or wholly, with a view to secure an income apart from the pleasure derived from the work".

13. What is meant by division of labour?

The concept of "division of labour " was introduced by Adam smith. Division of labour means dividing the process of production into distinct and several component processes and assigning each component in the hands of a labour or a set of labourers, who are specialists in that particular process. (eg. Readymade shirts)

14.What are the forms of capital?

The forms of capital are

1) Physical capital or Material Resources.

2)Money Capital or monetary Resources and

3) Human Capital or Human Resources.

15.What is Production function? What are its classification?

The functional relationship between inputs and outputs is known as production function. Inputs refers to the factor services which are used in production i.e land, labour, capital and enterprise. Output refers to the volume of goods produced.

Production function may be classified into two.

1)Short-run production function which is studied through Law of Variable Proportions.

2)Long-run production function which is explained by Constant Returns to scale.

16.Bring out the distinction between short run and long run.

Short-run is a period of time over which certain factors of production cannot be changed, and such factors are called fixed factors. The factors whose quantity can be changed in the short run are variable factors.

Long run is a period of time over which all factors of production can be changed, to meet the changes in demand.

17. Define opportunity cost.

The opportunity cost of any good is the next best alternative that is sacrificed. For example, a farmer who produces wheat can produce potatoes with the same factors. Therefore, the opportunity cost of a quintal of wheat is the amount of output of potatoes given up.

18.What are economic cost?

Economic costs include explicit costs and implicit costs. Explicit costs(accounting cost) are the payments made by the producers to the supplies of various productive factors. The money reward to the entrepreneur for his own services may be given as an example of implicit costs.

19. Define Marginal cost.

Marginal cost is defined as the addition made to the total cost by the production of one additional unit of output.

$$\boxed{MC_n = TC_n - TC_{n-1}}$$

Where,

MC_n = Marginal cost

TC_n = Total cost of production n- units

TC_{n-1} = Total cost of production $n-1$ units.

20. Mention the relationship between MC and AC

1) When MC is less than AC, AC is falling.

2) When MC is greaterthan AC, AC is rising.

3) At the minimum point of AC, MC cuts and equal to AC.

PART - C

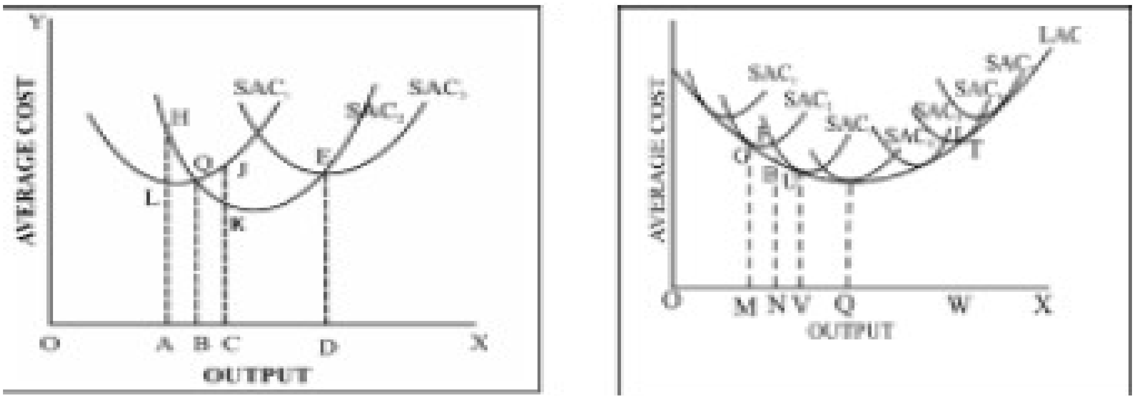
Answer the following questions in about a page

1. Give a note on long run average cost curve.

Long run Average Cost Curve (LAC)

In the long-run all factors are variable. Therefore the firm can change the size of the plant (capital equipment, machinery etc) to meet the changes in demand. A long-run average cost curve depicts the functional relationship between output and the long-run cost of production.

Long-run average cost curve



The Long run Average Cost (LAC) Curve is based on the assumption that in the long run a firm has a number of alternatives with regard to the scale of operations. For each scale of production or plant

size, the firm has an appropriate short-run average cost (SAC) curve. The pattern of these short-run average cost curves is shown in the above diagram.

We have assumed that technologically there are only three sizes of plants – small, medium and large. SAC_1 is relevant for a small size plant, SAC_2 for a medium size plant and SAC_3 for a large size plant. In the short period, when the output demanded is OA, the firm will choose the smallest size plant. But for an output beyond OB, the firm will choose medium size plant as the average cost of small size plant is higher for the same output (JC>KC). For output beyond OD, the firm will choose large size plant (SAC_3).

In the short-run, the firm is tied with a given plant but in the long-run, the firm moves from one plant to another. As the scale of production is changed, a new plant is added. The long-run cost of production is the least possible cost of production of any given level of output, when all inputs become variable, including the size of the plant.

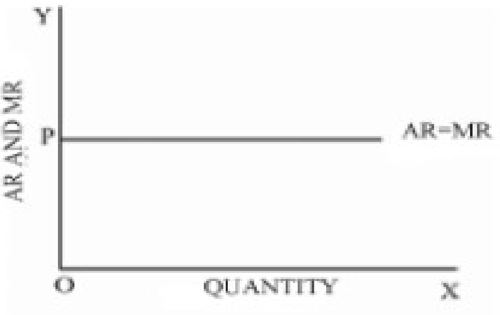
The long run average cost curve is called 'planning curve' of a firm as it helps in choosing a plant on the decided level of output. The long run average cost curve is also called envelope curve as it supports or envelops a group of short-run cost curves. From the figure we can understand that the long run average cost curve initially falls with increase in output and after a certain point it rises making a boat shape.

2. Explain the relationship between AR and MR curve

Relationship between AR and MR curves

When the average revenue (price) remains constant, the marginal revenue will also remain constant and will coincide with the average revenue.

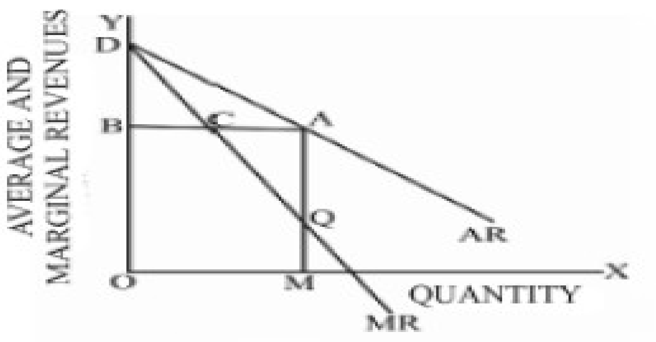
No.of units Sold	Price or AR (Rs)	TR (Rs)	MR Rs)
1	10	10	10
2	10	20	10
3	10	30	10
4	10	40	10
5	10	50	10
6	10	60	10



A firm can sell large quantities only at lower prices. In that case, the average revenue (price) of the product falls. When AR falls MR will also fall. But fall in MR will be more than the fall in the AR. Hence the marginal revenue curve will lie below the average revenue curve

Downward sloping AR and MR

No.of units Sold	Price or AR (Rs)	TR (Rs)	MR Rs)
1	10	10	10
2	9	18	8
3	8	24	6
4	7	28	4
5	6	30	2
6	5	30	0



3. Explain the short run average cost curves

Short run average cost curves

Average Fixed Cost (AFC)

The average fixed cost is the fixed cost per unit of output. It is obtained by dividing the total fixed cost by the number of units of the commodity produced.

Average Variable cost (AVC):

Average variable cost is the variable cost per unit of output. It is the total variable cost divided by the number of units of output produced.

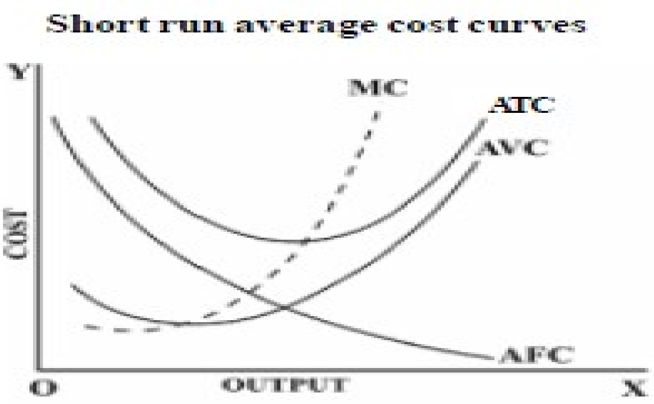
Average Total Cost or Average Cost :

Average total cost is simply called average cost which is the total cost divided by the numberof units of output produced.

Table:

Units of output	Total fixed cast	Total variable cost	Total cost	Average fixed cost	Average variable cost	Average cost
0	120	0	120	--	--	--
1	120	100	220	120	100	220
2	120	160	280	60	80	140
3	120	210	330	40	70	110
4	120	240	360	30	60	90
5	120	400	520	24	80	104

6	120	880	1000	15	110	125



Average variable cost curve is 'U' Shaped. As the output increases, the AVC will fall upto normal capacity output due to the operation of increasing returns. But beyond the normal capacity output, the AVC will rise due to the operation of diminishing returns.

4. Explain the marginal cost with suitable illustration.

Marginal Cost

Marginal cost is defined as the addition made to the total cost by the production of one additional unit of output.

$$\boxed{MC_n = TC_n - TC_{n-1}}$$

Where,

MC_n = Marginal cost

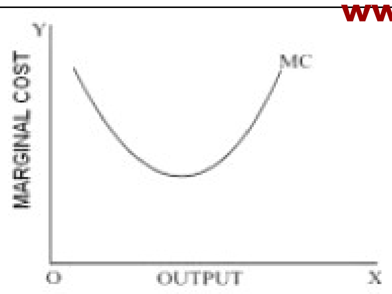
TC_n = Total cost of production n- units

TC_{n-1} = Total cost of production $n-1$ units.

For example, when a firm produces 100 units of output, the marginal cost would be equal to the total cost of producing 100 units minus the total cost of producing 99 units. Suppose the total cost of producing 99 units is Rs 9000 and the total cost of producing 100 units is Rs 10,000 then the marginal cost will be Rs10, 000 – Rs 9,000 = Rs 1,000. The firm has incurred a sum of Rs 1,000 in the production of one more unit of the commodity.

Table **Diagram**

Units of output	Total cost	**Marginal Cost**
0	20	--
1	40	20
2	50	10
3	55	5
4	65	10
5	85	20



The marginal cost curve is 'U' shaped. The shape of the cost curve is determined by the law of variable proportions. If increasing returns (economies of scale)is in operation, the marginal cost curve will be declining, as the cost will be decreasing with the increase in output. When the diminishing returns (diseconomies of scale) are in operation, the MC curve will be increasing as it is the situation of increasing cost.

5. Explain the relationship between SAC and SMC.

Relationship between short-run average and short-run marginal cost curves

The relationship between the marginal and the average cost is more a mathematical one rather than economic.

Average Total Cost or Average Cost :

Average total cost is simply called average cost which is the total cost divided by the number of units of output produced.

Marginal Cost

Marginal cost is defined as the addition made to the total cost by the production of one additional unit of output.

Units of output	Total cost	**Average Cost**	**Marginal Cost**
1	50	50	----
2	80	40	30
3	90	30	10
4	108	27	18
5	150	30	42
6	240	40	90
7	350	50	110

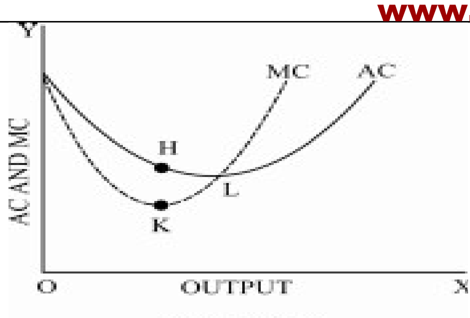


FIGURE 7.4

The relationship can be given as follows:

1) When marginal cost is less than average cost, average cost is falling

2) When marginal cost is greater than the average cost, average cost is rising

3) The marginal cost curve must cut the average cost curve at AC's minimum point from below. Thus at the minimum point of AC, MC is equal to AC.

6. What are the criticisms of Say's Law?

Criticism of Say's Law

1. Great Depression made Say's law unpopular

2. All incomes earned are not always spent on consumption

3. Similarly whatever is saved is not automatically invested

4. The Law was based on wrong analysis of market

5. It suffers from the fallacy of aggregation

6. Aggregate supply and aggregate demand are not always equal

7. Rate of interest is not the equilibrating factor

8. Capitalist system is not self-adjusting always

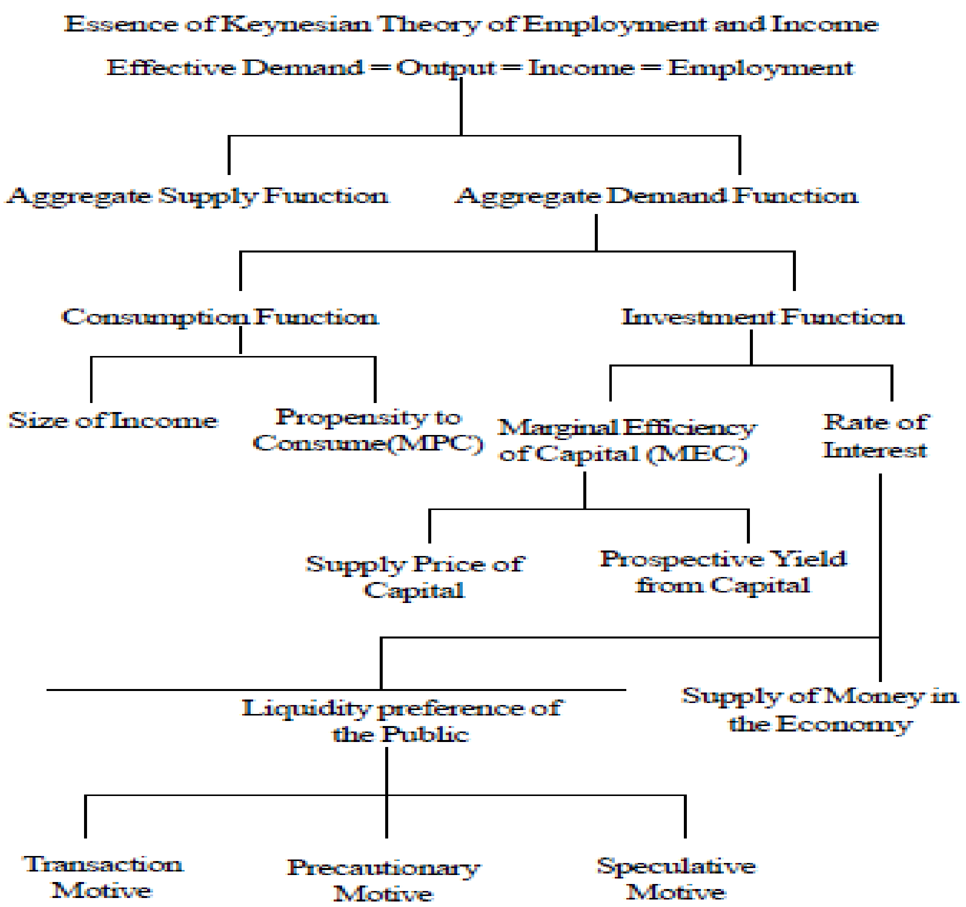
9. Perfect competition is an unrealistic assumption

10. Money is a dominant force in the economy

11. The law is applicable only for long period

12. Say's law holds goods only in a barter economy

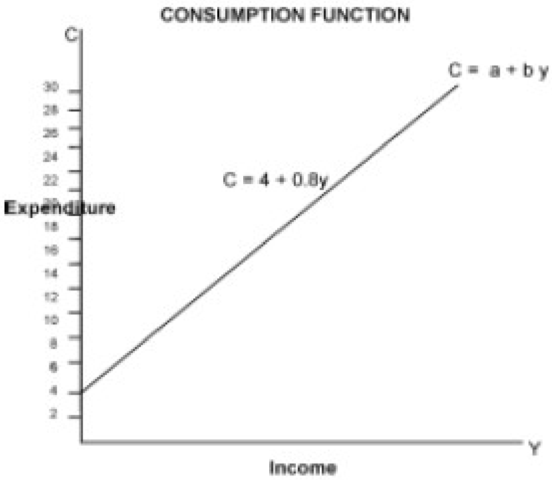
7. Draw the flow chart to depict the essence of Keynes theory.



8. Describe the consumption function with a diagram

Consumption Function

People spend most of their income on commodities. Some spend their income fully and some others spend a portion and keep the rest for saving. How much the community as a whole spends and saves? It is about the relationship between income and consumption. The term 'consumption function' explains the relationship between income and consumption. A function is the link between two or more variables. The proportion of income spent on actual consumption at different levels of income is called propensity to consume.



Keynes made it clear that there is a direct relation between income and consumption. Consumption function or propensity to consume is the ratio that measures the functional relationship between income and consumption. In mathematical form the relation can be expressed as,

C = a + b y .... (2)

C = 4 + .8Y

Thus a consumption function is generally described in terms of the linear equation Y = a + bY where the constant 'a' is the amount of autonomous consumption and slope (b) is MPC. The rate of change in consumption due to change in income depends on the MPC. Equation (2) simply says that consumption (C) depends on income (Y). The + sign indicates that as income increases, obviously consumption will also increase. But the rate of increase in consumption will be little less than that of the rate of increase in income. It is because some unspent portion of the income will be saved. This aspect is made clear in the Keynes law of consumption. He points out, "the psychology of the community is such that when real income is increased, aggregate consumption is increased, but not so much as income" . Keynes also made it clear that in the short run, the consumption function is stable because consumption habits of the people are more or less stable in short period.

All these points or the income-consumption relationship can also be expressed in the above Figure The vertical axis shows the spending on consumption indicated by C and the horizontal axis shows income or output indicated by Y. The straight line consumption function CC is defined in terms of equation $C = 4 + .8Y$.

The consumption curve CC is a short run curve. In this case consumption takes place even when income is zero. In equation (2) 4 is the level of initial consumption when income is zero and it is not affected by income. Even when income is zero, people spend some minimum level either by gift or borrowing. This consumption which is not related to income is called as autonomous consumption. That is the reason why curve C starts from 4 on the vertical axis.

9. What are the determinants of consumption other than income?

<u>Determinants of Consumption</u>

Though income is the most important factor that has greater influence on consumption, there are other factors which influence the propensity to consume. They are:

1. Income distribution

2. Size and nature of wealth distribution

3. Age distribution of population

4. Inflation or price level

5. Government policies

6. Rate of interest

7. Expectations about price, income, etc.

8. Advertisements

9. Improvement in the living standard

10. Changes in cultural values

As discussed earlier, aggregate demand consists of two parts (if you ignore government and external trade) namely consumption function and investment function. However, consumption function or MPC remains constant in the short run. Hence, Keynes placed greater emphasis on investment function.

10. What are the assumptions of Keynes' Simple Income Determination?

Assumptions

Keynes made the following assumption to explain income determination in a simple way.

1. There are only two sectors viz. consumers (C) and firms (I).

2. Government influence on the economy is nil. In other words government expenditure (G) is zero.

As there is no taxation, all personal income will become disposable income.

3. The economy is a closed one without any influence of foreign trade (X-M) that is, X-M is zero.

4. Wages and prices remain constant.

5. There are unemployed resources and hence less than full employment equilibrium prevails.

6. There is no variation in the rate of interest.

7. Investment is autonomous and it has no effect on price level or rate of interest.

8. The consumption expenditure is stable.

Due to the first three assumptions the basic equation

$Y = C + I + G + X-M$

has been reduced to $Y = C + I$

11. Explain the canons of taxation

Canons of Taxation

Canons of taxation are considered as fundamental principles of taxation. Adam Smith laid down the following canons of taxation:

a) Canon of equity

b) Canon of certainty

c) Canon of convenience

d) Canon of economy

1. Canon of equity

This canon is also called the 'ability to pay' principle of taxation. It means that taxes should be imposed according to the capacity of the tax payer. Poor should be taxed less and rich should be taxed more. This canon involves the principle of justice. All persons contribute according to their ability. As the cost of running the government should be equally borne by all, this canon is justified.

2. Canon of certainty

Every tax payer should know the amount of tax to be paid, when to be paid, and where to be paid and also should be certain about the rate of tax to make investment decisions.

3. Canon of convenience

Tax payment should be convenient and less burdensome to the tax payer. e.g. income tax collected at source, sales tax collected at the time of sales and land tax collected after harvest.

4. Canon of economy

This canon signifies that the cost of collecting the revenue should be kept at the minimum possible level. The tax laws and procedures should be made simple, so as to reduce the expenses in maintaining people's income tax accounts. ie. administrative expenditure to be kept at a minimum.

12. What are main sources of tax and non-tax revenue of the state government ?

Taxes of the State Governments

Under the Constitution of India, only the State governments are provided with separate powers to raise revenue, while the Unionterritories are financed by the Central government directly. The main sources of tax and non-tax revenue are

1. Land revenue,

2. Taxes on the sale and purchase of goods except newspaper,

3. Taxes on agricultural income,

4. Taxes on land and building,

5. Succession and estate duties in respect of agricultural land,

6. Excise duty on alcoholic liquors and narcotics,

7. Taxes on the entry of goods into a local area,

8. Taxes on mineral rights,

9. Taxes on the consumption of electricity

10. Taxes on vehicles, animals and boats,

11. Taxes on goods and passengers carried by road and inland water ways,

12. Stamp duties, court fees and registration,

13. Entertainment tax,

14. Taxes on advertisements other than those in newspaper,

15. Taxes on trade, profession and employment,

16. Income from irrigation and forests,

17. Grants from the central government and

18. Other incomes such as income from registration and share in the income-tax, excise and estate duties and debt services, loans and overdrafts.

13. Define Budget. Explain the balanced and unbalanced budget.

Definition:

Prof. Dimock says, "A budget is a balanced estimate of expenditures and receipts for a given period of time. In the hands of the administration, the budget is record of past performance, a method of current control and a projection of future plans".

Kinds of Budget

Balanced budget and unbalanced budget

1) **Balanced Budget :**

A balanced budget is that, over a period of time, revenue does not fall short of expenditure. In other words government budget is said to be balanced when its tax revenue and expenditure are equal.

2) **Unbalanced Budget (Surplus or deficit) :**

An unbalanced budget is that, over a period of time, revenue exceeds expenditure or expenditure exceeds revenue. In other words, the government's income or tax revenue and expenditure are not equal.

When there is an excess of income over expenditure, it is called a surplus budget. On the other hand, when there is an excess of expenditure over income, it is a case of deficit budget.

Classical economists advocated balanced budget. But it is not always helpful in achieving and sustaining economic growth. Modern economists argue that an unbalanced budget is very useful for achieving and maintaining economic stability

14. What are the limitations of fiscal policy ?

Limitations to fiscal policy

1) Size of fiscal measures

The budget is not a mere statement of receipts and revenues of the government. It explains and shapes the economic structure of a country. When the budget forms a small part of the national income in developing economies, fiscal policy cannot have the desired impact on the economic development. Direct taxation at times become an instrument of limited applicability, as the vast majority of the people are not covered by it. Further, when the total tax revenue forms a smaller portion of the national income, fiscal measures will not step up the sagging economy requiring massive help.

2. Fiscal policy as ineffective anti-cyclical measure

Fiscal measures- both loosening fiscal policy and tightening fiscal policy- will not stimulate speedy economic growth of a country, when the different sectors of the economy are not closely integrated with one another. Action taken by the government may not always have the same effect on all the sectors. Thus we may have for instance the recession in some sectors followed by a rise in prices in other sectors. An increasing purchasing power through deficit financing, a policy advocated by J.M. Keynes in 1930s may not have the effect of reviving the recession hit economies, but merely result in a spiraling rise in prices.

3. Administrative delay

Fiscal measures may introduce delay, uncertainties and arbitrariness arising from administrative bottlenecks. As a result, fiscal policy fails to be a powerful and therefore a useful stabilization policy.

Other Limitations

Large scale underemployment, lack of coordination from the public, tax evasion, low tax base are the other limitations of fiscal policy.

15. Differentiate between the direct and indirect taxes ?

1. Direct and Indirect taxes

According to Dalton, "A direct tax is one which is really paid by aperson on whom it is imposed whereas an indirect tax, though imposed on a person, is partly or wholly paid by another".

In the case of a direct tax, the tax payer who pays a direct tax is also the tax bearer. In the case of indirect taxes, the taxpayer and the tax bearer are different persons.

Direct taxes

Direct taxes are collected from the public directly. That it is to say, these taxes are imposed on and collected from the same person. One cannot evade paying the tax if it is imposed on him. Income tax, wealth tax, corporate tax, gift tax, estate duty, expenditure tax are good examples of direct taxes.

Indirect taxes

Taxes imposed on commodities and services are termed as indirect taxes. There is a chance for shifting the burden of indirect taxes. The incidence is upon the person who ultimately pays it. Examples of indirect taxes are excise duties, customs duties and sales taxes (commodity taxes).

Burden and shifting:

The burden of a direct tax is borne by the person on whom it is levied. For example, income tax is a direct tax. Its burden falls on the person who is liable to pay it to the Government. He cannot transfer the burden to some other person.

An indirect tax is initially paid by one person but ultimately the burden of the tax is fully or partially borne by another person. Because there is a possibility of transfer of burden of an indirect tax. For example, the excise duty on a motor-bike is initially paid by the manufacturer. But he subsequently shifts this burden to the consumer by including the tax in the price of the bike. Roughly, we may say that the direct taxes are paid by the rich and the indirect taxes are paid by the poor.

PART D

Answer for each question should be about three pages

31. Discuss the law of demand.

Law of Demand

The law of demand states that there is a negative or inverse relationship between the price and quantity demanded of a commodity over a period of time.

Definition:

Alfred Marshall stated that " *the greater the amount sold, the smaller must be the price at which it is offered, in order that it may find purchasers; or in other words, the amount demanded increases with a fall in price and diminishes with rise in price*".

According to Ferguson, the law of demand is that the quantity demanded varies inversely with price.

Thus the law of demand states that people will buy more at lower prices and buy less at higher prices, other things remaining the same. By other things remaining the same, we mean the following assumptions.

Assumptions of the Law

1. No change in the consumer's income
2. No change in consumer's tastes and preferences
3. No changes in the prices of other goods
4. No new substitutes for the goods have been discovered
5. People do not feel that the present fall in price is a prelude to a further decline in price.

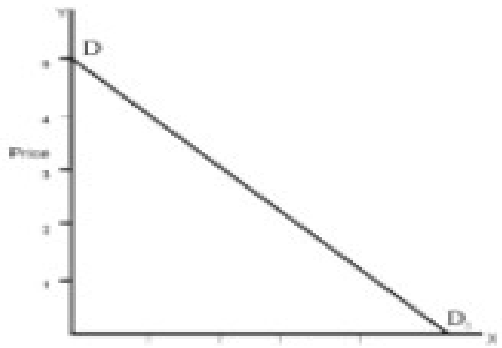
Demand Schedule and individual demand schedule

Demand schedule is a tabular statement showing how much of a commodity is demanded at different prices. It shows a list of prices and corresponding quantities demanded by an individual consumer. This is an individual demand

schedule.

Price	Demand (Orange)
5	1
4	2
3	3
2	4
1	5

Demand Curve and individual demand curve



1 2 3 4 5

Demand

The demand schedule can be converted into a demand curve by measuring price on vertical axis and quantity on horizontal axis as shown in the above figure the demand curve. The curve slopes downwards from left to right showing that, when price rises, less is demanded and vice versa. Thus the demand curve represents the inverse relationship between the price and quantity demanded, other things remaining constant.

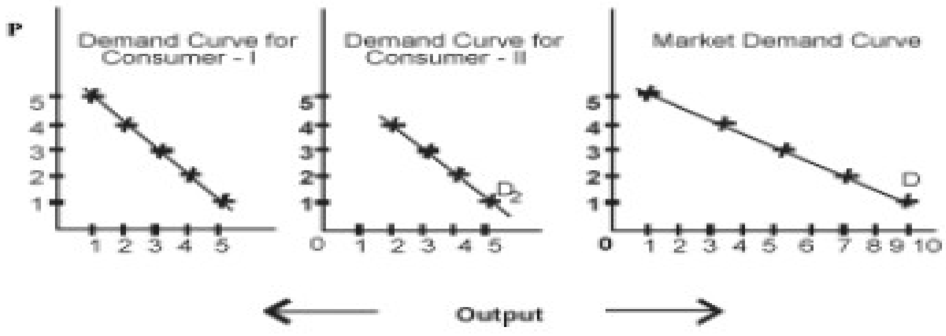
Why does the demand curve slope downwards?

The demand curve slopes downwards mainly due to the law of diminishing marginal utility. The law of diminishing marginal utility states that an additional unit of a commodity gives a lesser satisfaction. Therefore, the consumer will buy more only at a lower price. The demand curve slopes downwards because the marginal utility curve also slopes downwards.

Market demand schedule

A demand schedule for a market can be constructed by adding up demand schedules of the individual consumers in the market. Suppose that the market for oranges consists of 2 consumers. The market demand is calculated as follows.

Price of Oranges (in Rs)	Quantity demanded		
	Consumer I	Consumer II	Market Demand
5	1	-	1
4	2	1	3
3	3	2	5
2	4	3	7
1	5	4	9



Market demand curve

The market demand also increases with a fall in price and vice versa.

In the above Figure, the quantity demanded by consumer I and consumer II are measured on the horizontal axis and the market price is measured on the vertical axis. The total demand of these two consumers i.e. $D_1 + D_2 = DD_M$.- DD_M– the market demand curve - also slopes downwards just like the individual demand curve. Like normal demand curvs, it is convex to the origin. This reveals the inverse relationship.

32. Explain the methods of measurement of price elasticity of demand in detail.

Elasticity of Demand

The law of demand explains that demand will change due to achange in the price of the commodity. But it does not explain the rate at which demand changes to a change in price. The concept of elasticity of demand measures the rate of change in demand.

The concept of elasticity of demand was introduced by Alfred Marshall. According to him "the elasticity (or responsiveness) of demand in a market is great or small according as the amount demanded increases much or little for a given fall in price, and diminishes much or little for a given rise in price".

Types of Elasticity of Demand

There are three types of elasticity of demand;

1. Price elasticity of demand;
2. Income elasticity of demand; and
3. Cross-elasticity of demand

1. Price elasticity of demand

"The degree of responsiveness of quantity demanded to a change in price is called price elasticity of demand"

$$\text{Price elasticity of demand} = \frac{\text{Percentage change in quantity demanded}}{\text{Percentage change in price}}$$

Measurement of price elasticity of demand

Important methods for calculating price elasticity of demand are

1) Percentage method
2) Point method or slope method
3) Total outlay method
4) Arc method

1. Percentage method

This is measured as the relative change in demand divided by relative change in price (or) percentage change in demand divided by percentage change in price.

$$\text{Formula is} \quad e_p = \frac{\%\Delta q}{\%\Delta p}$$

Thus there are five measures of elasticity.

a) Elastic demand, if the value of elasticity is greater than 1

b) Inelastic demand, if the value of elasticity is less than 1

c) Unitary elastic demand, if the value of elasticity is equal to 1.

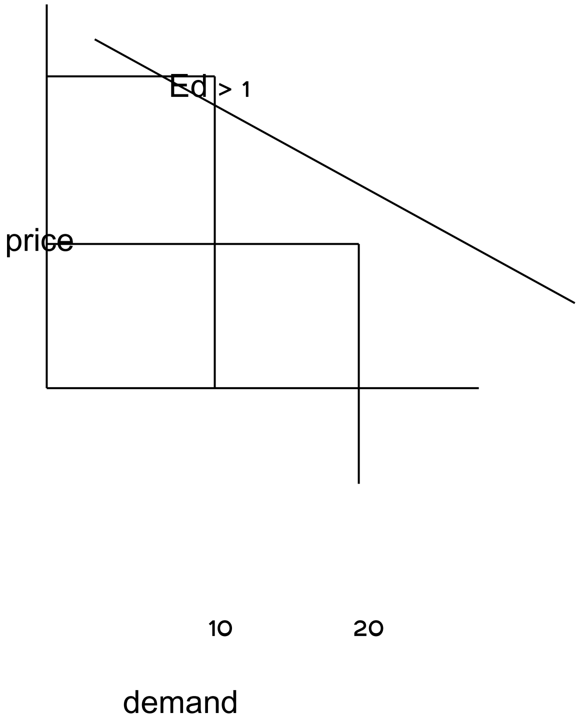
d) Perfectly inelastic demand, if the value of elasticity is zero.

e) Perfectly elastic demand, if the value of elasticity is infinity.

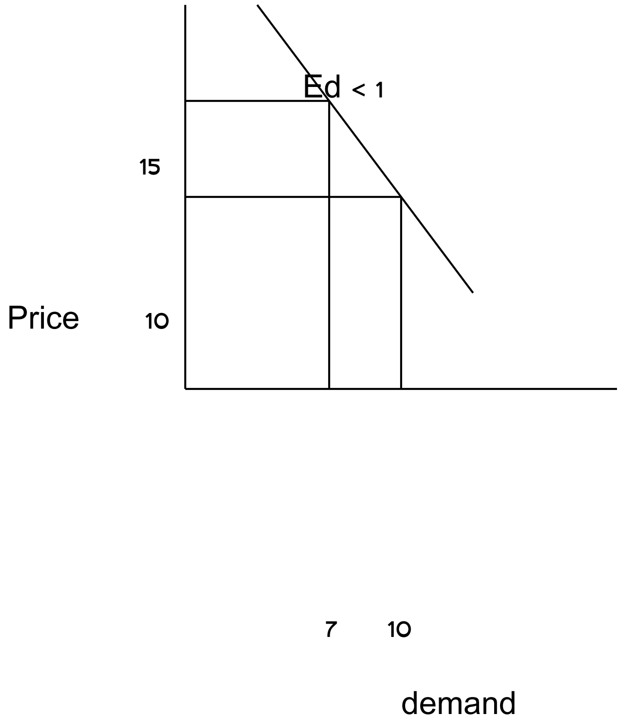
Graphical illustration

All the five measures are illustrated in the following figures

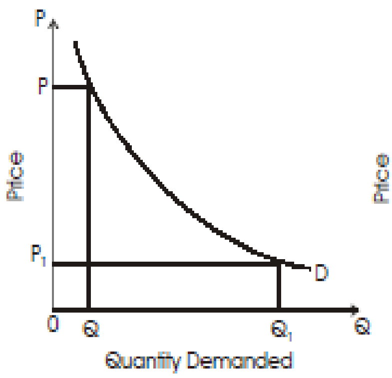
Elastic demand



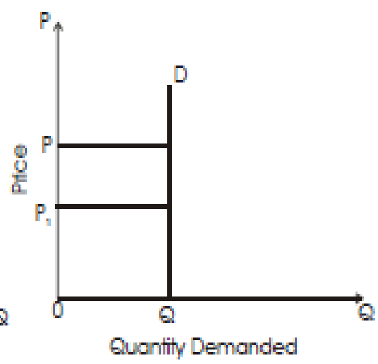
Inelastic demand



Unitary elastic demand



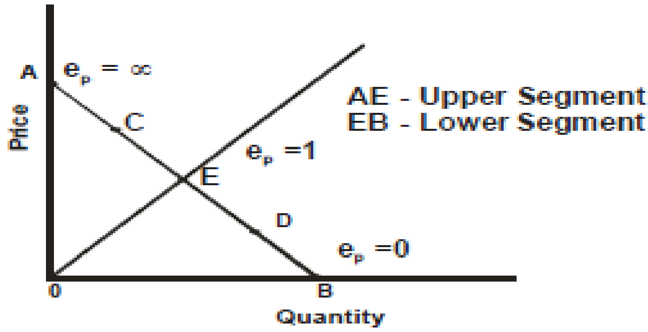
perfectly inelastic demand



perfectly elastic demand

2. Point method

We can calculate the price elasticity of demand at a point on the linear demand curve. Formula to find out e_p through point method is,



$$e_p = \frac{\text{Lower segment of the demand curve}}{\text{Upper segment of the demand curve}}$$

For example, in the above figure, the length of the demand curve AB is 4 cm

Exactly at middle point of AB demand curve,

1) e_p at point e $e_p = \frac{EB}{EA} = \frac{2}{2} = 1 \quad \therefore \; ep = 1$

2) e_p at point D = (middle point of EB portion of demand curve)

$$\frac{DB}{DA} = \frac{1}{3} = 0.3 \quad ep < 1$$

3) e_p at point c (middle point of EA portion of demand curve)

$$\therefore \; ep = \frac{CB}{CA} = \frac{3}{1} = 3 \quad ep > 1$$

4) e_p at point B $= \frac{0}{AB} = \frac{0}{4} = 0$

(o by anything is zero, a mathematical principle) $\therefore ep = 0$

5) e_p at point A $= \frac{AB}{0} = \frac{4}{0} = \infty$

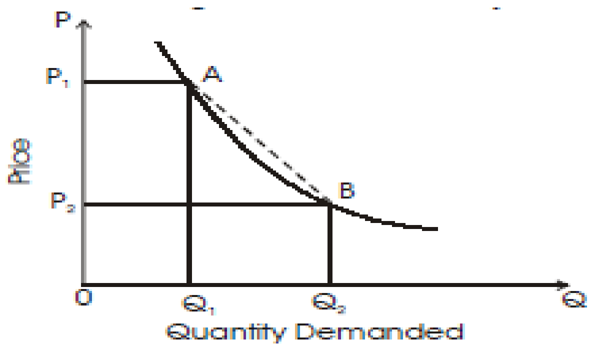
3. Total outlay method:

We can measure elasticity through a change in expenditure on commodities due to a change in price.

Changes in price	Types of elasticity of demand		
	$e_p = 1$	$e_p < 1$	$e_p > 1$
fall in price	Total outlay remains constant	Total outlay falls	Total outlay rises
rise in price	Total outlay remains constant	Total outlay rises	Total outlay falls

4) Arc method

Segment of a demand curve between two points is called an Arc.



In the above figure we can measure arc elasticity between points A and B on the demand curve; we will have to take the average prices of OP_1 and OP_2 and average of the two quantities demanded (original and the new).