

Q.1. (A) Fill in the blanks using proper alternative given in the brackets. (5)

1. Micro Economics is also called as Price theory.
(Income theory / Price theory / Growth theory / Employment theory)
2. Income elasticity of demand for inferior goods of Negative.
(Positive / Negative / zero/ Greater than one)
3. Autonomous consumption cannot be zero.
(Induced / Autonomous / Government / Private)
4. Deposit from current account can be withdrawn without any notice.
(Saving / current / fixed / recurring)
5. Wealth tax is an example of direct tax.
(Excise duty / Wealth tax / sales tax / gift tax)

(B) Match the following (5)

	'A'	'B'
1	Car & Petrol	Complementary goods
2	Supply	Cannot exceed stock
3	Capital	Interest
4	National Income	Final value of goods and service
5	Issue of currency notes	Central Bank

C. State whether the following statement are true or false. (6)

1. Perfectly elastic demand curve is parallel to 'Y' axis.
Ans. False
2. Geometric method is also known as point method.
Ans. True
3. In a monopoly, firm and industry are the same.
Ans. True
4. A cheque is a fiat money.
Ans. False
5. There is no difference between primary deposit and secondary deposit of a commercial Bank.
Ans. False
6. Credit rating in the quantitative credit control measure of the central bank.
Ans. False

Q.2. (A) Define or explain the following concept: (Any 3)

(6)

1. Partial equilibrium

- Ans.** (1) Partial equilibrium is the technique used by microeconomics to study the equilibrium position of an individual economic unit.
- (2) Partial equilibrium analysis assumes the condition of 'Ceteris Paribus', i.e. 'other things being constant'

2. Total cost

- Ans.** Total cost is the total expenditure incurred by a firm on the factors of production required for the production of goods and services. Total cost is the sum of total fixed cost and total variable cost. For example, if a producer incurred ₹ 50 in the form of fixed cost and ₹ 150 in the form of variable cost for producing 10 units of a good, the total cost can be calculated as follows: $TC = TFC + TVC = ₹ 50 + ₹ 150 = ₹ 200$

3. Equilibrium price

- Ans.** (1) The price at which the quantity demanded is equal to the quantity supplied is known as the equilibrium price.
- (2) In perfect competition, the equilibrium price gets determined by the interaction of both market demand and market supply and it is accepted by the large number of buyers as well as sellers.

4. Variable Capital

- Ans.** (1) Capital which is used in a production process only once is called variable capital. It is also called as working or circulating capital.
- (2) The amount of this capital varies from time to time as per the level of production. It is comparatively less durable in nature.

5. Macro variables

- Ans.** (1) The economic variables of macro quantities are called macro/macroeconomic variables. National output, national income, aggregate demand, aggregate supply, total consumption, total investments, general price level, etc. are some macro/macroeconomic variables.
- (2) Macroeconomics studies the interrelation among the various macro/macroeconomic variables, their determination and causes of fluctuation in them. It also suggests policies to solve the problems related to macro/macroeconomic variables.

6. Cash reserve ratio.

- Ans.** (1) By the Banking Act, commercial banks have to maintain a certain amount of cash with Central Bank (RBI) as reserves against their demand and time deposits. Central Bank can vary CRR between 3 per cent to 15 per cent of total time and demand deposits.
- (2) During inflation, the CRR is increased. This decreases the credit creation capacity of commercial banks. This ultimately reduces the money supply and inflation is controlled. During deflation, the CRR is decreased. This increases the credit creation capacity of commercial banks. This ultimately increases the money supply and deflation is controlled.

(B) Give reasons or explain the following: (Any 3)

(6)

1. Micro Economics is also called Slicing Method

Ans. Microeconomics splits the economy into small individual units. Then it studies the economic behaviour of each individual unit separately in detail. Thus, microeconomics uses slicing method for its analysis.

2. Utility is a subjective concept.

Ans. (1) Utility changes from person to person. Utility is influenced by personal likes, dislikes, preferences, habits, etc.

(2) For example, a non-vegetarian finds utility in mutton, but a vegetarian will not. Therefore, utility is a subjective concept.

3. Demand for habitual goods is inelastic.

Ans. (1) The demand for a habitual commodity does not change even if other factors such as price, income, taxes, etc. gets changed.

(2) For example, due to habit, a smoker's demand for cigarette remains almost fixed. Therefore, the demand for habitual/habitually used goods is (normally) inelastic.

4. National income at factor cost includes subsidy.

Ans. (1) The amount of subsidy given by government gets distributed in the incomes of factors of production.

(2) National income at factor cost is the sum of all incomes of factors of production.

Therefore, national income at factor cost includes subsidy

5. There are many subjective factors determining consumption function.

Ans. (1) The subjective motives such as motive of precaution, motive of foresight, motive of calculation, motive of improvement, motive of independence, motive of enterprise, motive of pride, motive of avarice, etc. affects consumption function.

(2) For example, high motive of enterprise and high motive of independence results in decrease in the consumption and increase in savings and vice versa.

Thus, there are many subjective factors determining consumption function.

6. As a banker to the government, the central bank transfer government funds.

Ans. (1) The Central Bank transfers government funds from one place to another place and from one account to another account.

(2) In India, the Reserve Bank of India has branches in Mumbai, Delhi, Kolkata, Chennai, Kanpur, etc. it has five zonal offices and 19 regional offices in most state capitals. At other places, the branches of the State Bank of India act as agents of the Reserve Bank of India. This helps in the transfer of the government funds.

Thus, as a banker to the government, the Central Bank transfers government funds

Q.3. (A) Distinguish between. (Any 3)**(6)**

1. Desire and demand.

Ans.

Desire	Demand
(a) Desire is a mere wish for something. For example desire for a Chartered Plane.	(a) Demand refers to desire backed by ability and willingness to pay for a particular commodity.
(b) Desire has no limits.	(b) Demand is limited by ability to pay and willingness to pay.
(c) Desire is not related or depends on price.	(c) Demand is inversely related to price.
(d) Desire is wider in scope as it includes demand.	(d) Demand is narrow in scope as it is a part of desire.
(e) Desire of a beggar to own a car.	(e) Demand for a BMW Car by business man who has ability and willingness to pay.

2. Average revenue and average cost.

Ans.

Average revenue	Average cost
(a) Average revenue refers to revenue (income) per unit of Output sold.	(a) Average cost refers to per unit cost of production.
(b) Average revenue (AR) is calculated by dividing Total Revenue (TR) by number of units sold.	(b) Average cost (AC) is calculated by dividing TC by total output.
$AR = \frac{TR}{\text{Quantity Sold}}$	$AC = \frac{TC}{\text{Total Output Produced}}$

3. Slicing method and lumping method.

Ans.

Slicing method	lumping method
(a) In slicing method the entire economy is cut into individual slices and each unit is studied in depth.	(a) In Lumping Method, we study the economy as a whole without slicing it.
(b) Micro Economics uses the slicing method.	(b) Macro Economics uses the Lumping Method.
(c) In slicing method in depth study of the behaviour of an individual unit like a household, a firm, a product, a factor is done.	(c) In Lumping Method, it deals with the behaviour of large aggregates like National Income, aggregate demand, aggregate supply, employment and their functional relationship is studied.
(d) It relates to the in-depth study of a tree and not the study of forest as a whole.	(d) It relates to the study of the forest as a whole and not a particular tree.
(e) Here we achieve a worm's eye view.	(e) It gives a bird's eye view of the whole economy.

4. Income method and expenditure method.

Ans.

Income method	Expenditure method
(a) According to Income Method, National Income is calculated by adding the factor incomes of the residents of a country earned during one year. It includes the net income from abroad.	(a) According to expenditure method national income is equal to the sum of expenditure incurred on final goods and services in the country during a year.
(b) National Income = Rent + Wages + Interest + Profit + Mixed Income + Net exports and net Income from abroad - depreciation - transfer income i.e. $NI = R + W + I + P + M.I. + (X - M) + (R - P) - dep - \text{Transfer income.}$	(b) National Income = Consumption Expenditure + Investment Expenditure + Government Expenditure + Net Exports + Net Income from abroad - depreciation - indirect tax and + subsidies.
(c) Income method shows how incomes are earned from various ways.	(c) The Expenditure Method shows how National Income is spent on various heads.
(d) Income method is more popular method and it is used in India in the service sector.	(d) This method of computing National Income is not very popular.

5. Paper money and metallic money.

Ans.

Paper money	Metallic money
(a) It refers to that money which is form of paper currency notes issued by Government.	(a) It refers to money which is made of metals like gold, silver and copper etc.
(b) They are less durable	(b) They are durable.
(c) Paper money is more convenient and they are light and so it is portable.	(c) Metallic money are not easily portable.
(d) They are suitable for larger transactions.	(d) They are suitable for small transactions.
(e) Paper money were subsequently issued after metallic money.	(e) Metallic money was introduced earlier to paper money.
(f) Paper money are easier and cheaper to print.	(f) Metallic money are not economical to produce.

6. Revenue budget and capital budget.

Ans.

Revenue budget	Capital budget
a) Revenue Budget consists of (1) Revenue Receipts (2) Revenue Expenditure	(a) Capital Budget consists of (1) Capital Receipts (2) Capital Expenditure
(b) It explains how revenue is generated by government and how it is allocated among various expenditure heads.	(b) It deals with the capital aspect.
(c) Revenue receipts consists of (1) Tax Revenue (2) Non-Tax Revenue	(c) Capital receipts consists of (1) Borrowing (2) Recovery of loans (3) Disinvestment, small savings
(d) Revenue expenditure includes developmental and non-developmental expenditure of Central Government.	(d) Capital expenditure includes expenditure on land and building machinery, investment in shares, loans granted by Central Government to State.
(e) Revenue Receipts do not create any liability of the government.	(e) Capital receipt create a liability of the government.
(f) Revenue expenditure does not lead to the creation of assets.	(f) Capital expenditure leads to the creation of assets.

(B) Write short notes. (Any 2)

(6)

1. Subject matter of micro economics.

Ans. Micro Economics basically deals with

- i) Theory of Product pricing
- ii) Theory of factor pricing (Micro theory of distribution)
- iii) Theory of economic welfare

(1) Product pricing: Microeconomics explains how the prices of variety of goods and services are determined. The prices of commodities such as cloth, rice, car, etc. and many other services get determined by the equilibrium of their demand and supply forces. Thus, theories of demand, production and cost are within the scope of microeconomics.

(2) Factor pricing: Microeconomics also explains how the prices of factors of production, viz. land, labour, capital and entrepreneur are determined. The prices of factors of production also get determined by equilibrium of their demand and supply forces. Thus, theories of rent, wages, interest and profit lies within the scope of microeconomics.

(3) Theory of Welfare: Theory of welfare also lies within the scope of microeconomics. Theory of welfare basically deals with efficiency in the allocation of resources. Efficiency in allocation of resources is attained when it results in the maximum satisfaction of people in an economy.

Therefore, microeconomics studies the following three efficiencies:

- (i) **Efficiency in production:** Efficiency in production means to produce the maximum possible amount of goods from the given amount of resources. Microeconomics analyses how efficiency in production can be obtained.
- (ii) **Efficiency in consumption:** Efficiency in consumption means distribution of produced goods and services among the people for consumption in such a way as to maximise total satisfaction of society. Microeconomics analyses how efficiency in consumption can be obtained.
- (iii) **Efficiency in the direction of production, i.e. overall economic efficiency:** Efficiency in the direction of production, i.e. overall economic efficiency means producing those goods which are most desired by people in society. Microeconomics analyses how overall economic efficiency can be obtained.

From the above points it can be noticed that the study of microeconomics is mainly concerned only with price theory and resource allocation. It does not study the aggregates relating to whole economy. It does not study national economic problems such as unemployment, poverty, inequality in income, etc. It does not include study of theory of growth, monetary policy, fiscal policy, etc. Therefore the scope and subject matter of microeconomics is comparatively limited and narrower.

2. Factors determining elasticity of demand.

Ans. Following are the factors which influence Elasticity of Demand.

1. **Nature of Commodities:** Commodities may be either necessities or luxuries. Normally, elasticity of demand for necessities is inelastic and for luxuries demand is elastic.
2. **Durability:** The demand for durable goods is elastic, whereas the demand for perishable goods is inelastic.
3. **Substitute Goods:** Availability of substitutes also determine Elasticity of Demand. The Larger the number of substitutes for a commodity in the market, greater will be the elasticity of demand.
4. **Uses of a Commodity:** When commodity can be put to several uses, its demand is elastic. The demand for electricity is elastic.
5. **Price:** Goods, which have very highly price or very low price have inelastic demand.
6. **Habits:** Habits influence Elasticity of Demand. The demand for goods which satisfy the habits is normally inelastic. For instance, the demand for cigarettes is inelastic. Also consumption of essential goods cannot be postponed therefore demand for them is inelastic.
7. **Income of Consumer:** When income level is high demand is normally inelastic, and demand is elastic at a very low level of income.
8. **Proportion of Expenditure:** Generally when proportion of income spent on a commodity is large, demand for goods tend to be inelastic. For instance for food grains is inelastic.
9. **Complementary Goods:** By and large, demand for complementary goods is inelastic. Because complementary goods such as motor car and petrol are demanded jointly.

3. Features of perfect competition.

Ans. The features of perfect competition are as follows:

- (1) **Large number of sellers:** In perfect competition, there is a large number of potential sellers selling their commodity in the market. Their number is so large that the single seller cannot influence the market price. The price of the product is determined by the interaction of market demand and market supply of a commodity. Thus, in perfect competition, a seller is a price taker.
- (2) **Large number of buyers:** In perfect competition, there is large number of potential buyers buying commodity in the market. Their number is so large that the single buyer cannot influence the market price. Thus, in perfect competition, a buyer is a price taker.
- (3) **Free entry and exit:** In perfect competition, any firm can freely enter or can take exit from the market without any restrictions.
- (4) **Homogeneous product:** In perfect competition, every firm produces and sells identical products, i.e. units of a commodity produced by each firm are uniform in respect of their size shape, colour, quality, etc. Therefore, the commodities sold in perfect market are perfect substitutes to one another.
- (5) **Perfect knowledge:** In perfect competition, the buyers as well as sellers have perfect knowledge of the market conditions. Such knowledge prevents the buyers from paying a higher price and sellers from charging a different price than what is prevailing in the market.
- (6) **Single price:** In perfect competition, all units of a commodity have uniform price and it is determined by the equilibrium of the market demand and market supply.
- (7) **Perfect mobility of factors of production:** Under perfect competition, the factors of production, i.e. land, labour, capital and enterprise enjoy complete freedom to move from one place to another and from one occupation to another. This implies the optimum use of each factor input and they are made available easily and producers do not face any problem in production of any commodity.
- (8) **No transport cost:** There is no transport cost under perfect competition. It is assumed that all the firms are close to one another. This keeps the difference in transport cost off and price remains uniform in perfect competition.
- (9) **No Government intervention:** Laissez-faire prevails under perfect competition. It means that there is no government intervention in respect of production, transportation and price determination of goods.

Perfect competition is the ideal form of market but it is very difficult to realize the above conditions practically. Thus, perfect competition is an imaginary concept

4. Functions of an entrepreneur.

Ans. (A) Organizing function: An entrepreneur has to perform following functions to organize business:

- (1) **Factor co-ordination:** An entrepreneur has to co-ordinate the other factors of production, i.e. land, labour and capital in the most optimum manner. Effective co-ordination of factors helps in minimizing the cost of production and maximizing the total output.
- (2) **Decision making:** An entrepreneur has to take several decisions, regarding how to produce, at what cost to produce, how much to produce, where to sell, etc. Thus, entrepreneur is a decision making factor in a production process.
- (3) **Planning:** Planning is an important function of an entrepreneur. Entrepreneur has to plan before, during as well as after the production process. Thus, planning is a continuous process.
- (4) **Supervision:** An entrepreneur is also a supervisor of his business. He should supervise the entire functioning of the business. He should keep on monitoring the working of factor inputs, viz. land, labour and capital.
- (5) **Making factor payments:** Entrepreneur pays fixed contractual rewards to all factors of production, i.e. land, labour and capital in the forms of rent, wages and interest respectively. Entrepreneur should distribute the rewards according to the contribution of factors of production in the production process.

(B) Risk and uncertainty bearing function: It is the unique and the most important function performed by an entrepreneur. It is the responsibility of entrepreneur to undertake the risk and uncertainties in the business. Entrepreneur bears the following two types of risks:

- (1) **Insurable risk:** The risk which is insured by the insurance company is called insurable risk. The loss due to such risk can be avoided. For example, risk due to fire, risk due to flood, risk due to accident, etc.
- (2) **Non-Insurable risk or Uncertainties:** The risk which cannot be insured by the insurance company is called non-insurable risk. The loss due to such risk cannot be avoided. For example, risk due to change in demand for the product, availability of close substitute for the product, change in government policy, war-like condition, etc.

(C) Innovative function: According to Schumpeter, the introduction of innovation is the soul of entrepreneurial function. It is the duty of entrepreneur to do innovations. An entrepreneur's innovative function includes to discover new technology of production, finding of new market, finding of new place of getting raw material, bringing out new changes in shapes and packing of the product, finding out new sales promotion techniques, etc.

Thus, entrepreneur performs a variety of functions. Therefore he is rightly described as the captain of industry.

Q.4. Write short answer for the following questions: (Any 3)

(12)

1. What are the limitations to law of DMU?

- Ans. 1. Unrealistic assumptions** - The law of Diminishing Marginal Utility is based on various assumptions like homogeneity, continuity, constancy, rationality, etc. But in reality, it is difficult to fulfil all these conditions at a time.
- 2. Cardinal measurement** -The law assumes that utility can be expressed cardinally, i.e., in numbers, so it can be added, compared and presented through schedule. In fact, cardinal measurement of utility is not possible because it is a psychological concept, but it can be measured ordinally in form of degree of comparison, i.e., higher or lower level of satisfaction.
- 3. Indivisible goods** -The law is not applicable to bulky or indivisible goods like T. V., car, house, etc. It is because; normally they are not purchased more than one at a time. So it is impossible to compare the marginal utility derived from various units of such commodities.
- 4. Constant marginal utility of money** -The law assumes that marginal utility of each unit of money remains constant, however, critics argue that marginal utility of money differs from person to person. It is influenced by changes in prices, stock of money, etc.
- 5. A single want** - The law is restricted to the satisfaction of a single want only. However, in practice, a man satisfies many wants at a time.

2. Explain the features of monopoly.

- Ans. 1) Single seller** - In a monopoly market there is a single seller or a single producer. Under monopoly he has no rivals and he faces no competition.
- 2) No close substitute** - There are no close substitutes for the commodity sold in the market. Likewise other firms may not produce the same product. Hence, monopolists do not face any competition.
- 3) Barriers to entry** - Under monopoly the entry of other firm is strictly restricted. The seller has complete hold over the supply in the market. Such provision protects the monopoly powers.
- 4) No distinction between firm and the industry** - Under monopoly there is only one seller, there is no distinction between the firm and the industry. Thus, under monopoly the firm is an industry.
- 5) Control over the market supply**- The monopolist has complete hold over the market supply. He is a sole producer of the commodity. Therefore entry barriers such as natural, economic, technological or legal do not allow competitors to enter the market.
- 6) Price maker** - The firm under monopoly is price maker and not the price taker. He can charge any price for the commodity as he has complete control over the supply of die product.
- 7) Profit maximization** - The monopolist always wants to cam supernormal profit. His decision regarding the price and the level of output are guided by the profit maximization motive. Thus, sometimes at high price, he supplies the product as per the demand and sometimes he controls the supply of the product and sells the product at high prices.
- 8) Price discrimination** - This implies charging different prices for the same product to different buyers. The monopolist succeeds in increasing his profit by adopting the technique of price discrimination.

3. What are the features of Macro Economics?

- Ans. 1) Study of aggregates** - Macro-Economics deals with the study of nations economy as a whole. It is a study of very large, economy wide aggregates such as national output or income, total employment, aggregate demand, aggregate supply, total investment, total consumption, general price level etc.
- 2) Lumping method** - Macro analysis deals with the behaviour of aggregates i.e. total values of economic variables related to whole economy. It uses method of lumping to deal with macro variables, such as aggregate demand, aggregate supply, national output etc.
- 3) A General equilibrium analysis** - Macro-Economics analysis is based on General Equilibrium Analysis. This analysis deals with entire economy in the context of equilibrium. It studies the behaviour of number of economic variables at a time and takes into consideration their functional relationship and interdependence in doing so. This approach assumes "Everything depends on everything else."

Since this approach deals with whole economy, it has to explain how aggregate supply and aggregate demand are brought into equality, and how equilibrium between these forces determine, not only price level, but also level of income and employment. This whole analysis involves the study of number of variables and their interactions.

- 4) Income analysis** - Macro-Economics is also known as the theory of income and employment or simply income analysis. Because, basic subject matter of Macro-Economic analysis is to explain what determines the level of national income and employment and what causes fluctuations in them. Further, it explains the growth of national income over a long period of time.
- 5) Policy-oriented** - Macro-Economics, according to Keynes' is a policy-oriented science. Macro-Economics analysis helps in formulating suitable economic policies to promote economic growth, to generate employment, to control inflation, to pull the economy out of depression etc.
- 6) Dynamic science** - Macro-Economics studies the changes in aggregate economic variables and analyses dynamic nature of the economy. It enables us to study progress of an economy over a period of time.
- 7) Based on interdependence** - Macro analysis takes accounts of interdependence between aggregate economic variables, such as income, output, employment, investment, price level etc. E.g., it explains how change in level of investment will finally change the level of national income, output and employment, and eventually the level of economic growth.

4. What are the determinants of aggregate supply?

- Ans. (A) Meaning:** Aggregate supply refers to the minimum amount of sales proceeds which entrepreneurs expect to receive from the sale of output at any given level of employment in a year. It essentially refers to the total national producer national income.

(B) Determinants: The determinants of aggregate supply can be shown in the following formula:

$Q = f(\bar{N}, L, \bar{K}, \bar{T})$ The bar indicates that the factor supply is held constant for the short run. The determinants of aggregate supply can be explained as follows:

- (1) Natural Resources (\bar{N}):** Natural resources include all those natural gifts which are on the surface, below the surface and above the surface of the earth. These are called land in economics. A country with a plentiful supply of natural resources like fertile soil, moderate climate, perennial rivers, satisfactory rains, essential minerals, etc. produces more number of goods and services. The aggregate supply of such a country is found to be more. For example, due to the abundant availability of natural resources, the United States annually produces nearly one-fourth of the total output of the world. On the other hand, the scarcity of natural resources results in a decrease in aggregate supply.
- (2) Human Resources (L):** Aggregate supply also gets influenced by the amount of and the quality of available labour force in a country. A country with an abundant, highly skilled, industrious and devoted labour force is able to produce more number of goods and services. This increases the aggregate supply of a country. Japan, China and Korea are the best examples of the countries having a great positive influence of labour force on aggregate supply. On the other hand, the scarcity and low quality of human resource decreases the aggregate supply of a country.
- (3) Stock of Capital (\bar{K}):** The aggregate supply and employment in the economy depends upon the stock of capital, its quality and use. The use of capital helps to increase the productivity and efficiency of other factors of production. Capital formation and accumulation of capital depends upon the savings made by people in the country. Savings depend upon the level of income. Savings are converted into investment of capital goods. A rise in the investment increases the availability of capital for production. This, in turn, increases the aggregate supply of a country. On the other hand a fall in the investment decreases the availability of capital for production. This, in turn, decreases the aggregate supply of a country.
- (4) State of Technology (\bar{T}):** Aggregate supply also gets influenced by the state of technical knowledge, at any particular point of time. With the use of modern technology, it is possible to explore new resources and new use of available resources. The use of modern technology helps in large scale production with the minimum cost. It also helps in improving the quality of production. For example, the use of computer and internet in business and industries has facilitated the expansion of business transactions. Thus, modern technology increases the aggregate supply. on the other hand, backward and outdated technology decreases the aggregate supply.

5. Explain in details the various deposits (type of accounts) of the commercial bank.

Ans. The various types of deposits are as follows:

(A) Demand Deposits: Deposits which are withdrawable on demand are known as demand deposits. They are of the following two types:

(1) Current Account Deposits: It is usually opened by businessmen, corporations, industrial enterprises, public bodies, trustees, etc. Current account facilitates customers to carry out their transactions with minimum cash at hand. Usually there are no restrictions on the amount of deposits as well as withdrawal of deposits from the current account. Commercial banks also provide overdraft facilities and agency services to the current account holders. Very low interest or no interest is paid on the current account deposits.

(2) Savings Account Deposits: Savings bank deposits are generally opened by people who wish to save a small portion of their income and deposit the same with the bank. Savings account are opened mainly by salaried class, middle income group or small traders. Normally, a small rate of interest is paid on this account. Money can be withdrawn subject to some restrictions.

(B) Time Deposits: Deposits which are repayable after a certain period of time are known as time deposits. The types of time deposits are as follows:

(1) Recurring Deposits: Banks receive deposits in recurring accounts to encourage customers to make regular savings. In recurring deposit account, a customer is required to deposit a fixed sum of money for a specified period of time.

(2) Fixed Deposits: Deposits under this account are made for a fixed or a specified period. The money deposited under this account can be withdrawn only after the stipulated or specified time period. Rate of interest" is relatively higher on these deposits. The rate of interest on fixed deposits varies with the period of time for which money is deposited. If a person wishes to withdraw before the expiry of the specified time, he receives a lower rate of interest.

6. What are the revenues of the government? Explain non-tax revenues.

Ans. Revenue Receipts

Revenue receipts of the government refer to those~ money receipts which neither create any liability nor cause any reduction, in the assets of the government. They are regular and recurring in nature.

Revenue receipts of the government are generally classified under two heads.

i) Tax Revenue

ii) Non-Tax Revenue

i) Tax Revenue

a) Direct Tax

b) Indirect Taxes

ii) Non-Tax Revenue

Non-tax revenue refers to receipts of the government from all sources other than those of tax receipts. The main sources of non-tax revenue are:

a) Interest and dividend on investments:

Government receives interest on loans given to state governments, union territories, private enterprises, which is an important source of non-tax revenue. Dividends are received by the government from its investment in other companies.

b) Fees, License Fee:

Fees refer to charges imposed by the government to cover the cost of recurring services provided by it. It is also a compulsory contribution. For example, registration fees, court fee etc.

c) Gifts and grants:

Government receives gifts and grants from international organizations and foreign governments. Sometimes individuals and companies voluntarily gift money to the government during natural calamities, such as earthquake, flood, famine, tsunami, war etc.

d) Fines and penalties:

Fines and penalties are levied on defaulters to maintain law and order. This generates revenue for example fine for jumping a signal etc.

e) Escheats:

It refers to claim of the government on the property of a person who dies without leaving behind any legal heir or a will.

Q.5. Explain with reasons whether you agree or disagree with the following statements (Any 3) (12)

1. When MU is zero, TU is maximum.

Ans. Yes, I agree with this statement.

Reasons:

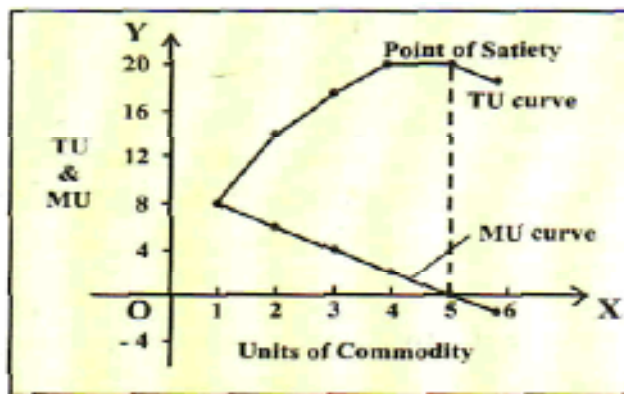
Relationship between total utility and marginal utility can be explained with the help of the following schedule and diagram:-

Total Utility and Marginal Utility Schedule

Units of Commodity	TU Units	MU Units
1	8	8
2	14	6
3	18	4
4	20	2
5	20	0
6	18	-2

The above given schedule indicates MU and TU derived from each unit of a commodity.

Graphical representation of TU and MU



The above given schedule and diagram explain that:-

1. Initially, total utility and marginal utility are equal. (TU=MU)
2. From the consumption of second unit, total utility increases at a diminishing rate and marginal utility goes on decreasing. So TU curve slopes upward and MU curve slopes downward. (TU↑, MU↓)
3. When total utility is maximum, marginal utility is zero. It indicates point of satiation (i.e. maximum satisfaction). At this point, TU curve reaches the highest level and MU curve touches the x-axis. (TU maximum, MU zero)
4. When total utility declines, marginal utility intersects the *X' axis and becomes negative. It shows dissatisfaction of a consumer. In this case. TU curve starts falling and MU curve enters into the negative quadrant. (TU↓, MU negative)

It is observed that total utility is always positive but marginal utility may be positive, zero or even negative.

2. There are no exceptions to the law of demand.

Ans. No, I do not agree with this statement

Reasons:

1. **Giffen goods:** Certain inferior goods are called Giffen goods, when the price falls, quite often less quantity will be purchased than before because of the negative income effect and people's increasing preference for a superior commodity with the rise in their real income. Sir Robert Giffen observed the situation related to demand for bread & meat in England. When price of bread was decreasing, less bread was purchased. Here surplus money was transferred to purchase meat, as a result demand for meat increased.
This behaviour is known as Giffen's paradox. Thus Giffen goods are inferior goods which have a direct relationship between price and quantity demanded. In this case the demand curve slopes upwards from left to right as shown in the above diagram.
2. **Prestige goods:** Diamonds, high priced motor cars, luxurious bungalows are prestige goods. Such goods have a "snob appeal". Rich people consume such goods as status symbol. Therefore, when the price of such goods rises their demand also rises.
3. **Price illusions or Consumers Psychological bias:** Consumers have illusion that high priced goods are of a better quality. Therefore the demand for such goods tends to increase with a rise in their price, e.g. Branded products which are expensive are demanded at a high price.
4. **Demonstration effect:** The tendency of low income group to imitate the consumption pattern of high income groups is known as Demonstration effect. For example demand for consumer durables such as washing machine, latest mobile etc.

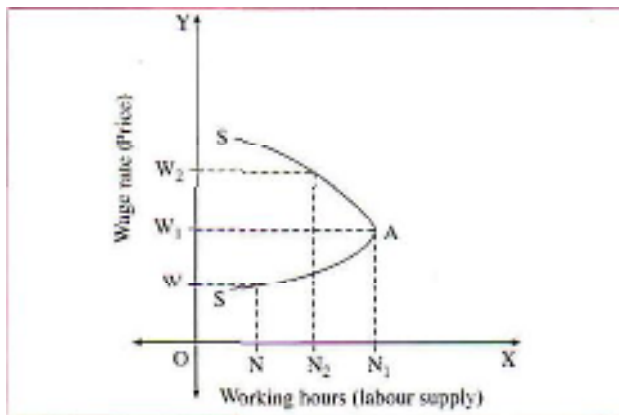
5. **Ignorance:** Sometimes people do not have proper market knowledge. They may not be aware of the fall in price of a commodity and thus they tend to purchase more at a higher price.
6. **Speculation:** When people speculate a change in price of a commodity in the future, they may not act according to the Law of demand. People may tend to buy more at rising price, when they anticipate further price rise. For example, in the stock market people tend to buy more shares at rising prices. Even if prices of some goods like sugar, oil etc. are rising before Diwali, people go on purchasing more of these things at rising prices, because they think that prices of these goods may increase further during Diwali.
7. **Habitual Goods:** Due to habit of consumption certain goods like tobacco, cigarettes etc. are purchased even if prices are rising. Thus it is an exception.

3. Supply curve of labour bends backwards.

Ans. Yes, I agree with this statement.

Reasons:

- (1) In the initial stages, labour supply increases as wage rate increases. However, at a later stage, workers would prefer leisure to work. They prefer to earn same amount of income by working for less hours.
- (2) Therefore, in the initial stages, the labour supply curve slopes upwards from the left to the right. However, in the later stage, the labour supply curve bends backward.



- (3) From the above diagram it can be seen that in the initial stages as wage rate rises from OW to OW_1 the supply of labours also rises from ON to ON_1 . However, when the wage rate rises from OW_1 to OW_2 the supply of labours do not rise further; rather it is reduced from ON_1 to ON_2 .
- (4) Thus, after the wage level OW_1 , the supply curve slopes backwards from the point A towards Y -axis indicating that at higher prices fewer labour hours are supplied.

Therefore, the backward sloping supply curve shows the inverse relationship between supply of labour and wage rate.

4. Barter system did not have any difficulties.

Ans. No, I do not agree with this statement

Reasons:

- (1) **Lack of double coincidence of wants:** Double coincidence of wants indicates the need of each other's goods and willingness to accept it. Lack of double coincidence of wants was one of the important limitations of barter system.
- (2) **Lack of common measure of value:** In the absence of a common measure of value or a unit of account, it was difficult to calculate the values of the goods exchanged.
- (3) **Difficulty of storage of goods:** Under barter exchange, it was necessary to store goods for future consumption. Storage of highly perishable goods was difficult.
- (4) **Problem of indivisibility:** Under barter system, it was difficult to make fractional payments, especially when things to be exchanged were indivisible.
- (5) **Problem of making deferred payments:** In barter system it was difficult to make deferred payments. Thus, barter system had many difficulties.

5. A commercial bank can create credit on basis of primary deposit.

Ans. Yes, I agree with this statement.

Reasons:

- (1) Primary deposits refer to money deposited by the people in the form of cash with the banks. By keeping some part of primary deposits in the form of cash reserve, the rest of the primary deposits are used for lending loans.
- (2) When a bank grants loan to a borrower, the bank opens a deposit account in the name of the borrower and the money transferred on the account of the borrower creates secondary deposits.
- (3) When the borrower withdraws money from his loan account by a cheque, it is deposited by the payee in some other bank.
- (4) Other banks again create credit on the basis of fresh deposits received after keeping the required reserves.
Thus, a commercial bank can create credit on the basis of primary deposits.

6. Central bank is a profit making institution.

Ans. No, I disagree with this statement.

Reasons:

- (1) Central Bank has the monopoly in issuing currency notes which are legal tender.
- (2) In India, Reserve Bank of India (RBI) has the sole right to issue currency notes of all denominations except one-rupee note.
- (3) The one-rupee note and coins of all denominations are issued by the Ministry of Finance of Government of India, but their distribution is undertaken by the RBI.
- (4) By having the sole power of issuing notes, the Central bank can bring uniformity in the currency, develop confidence of people in currency, regulate money supply and maintain price stability.
Therefore, central bank is the bank of issue.

Q.6. Write explanatory answers: (Any Two)

(16)

1. Explain variation in demand and change in demand.

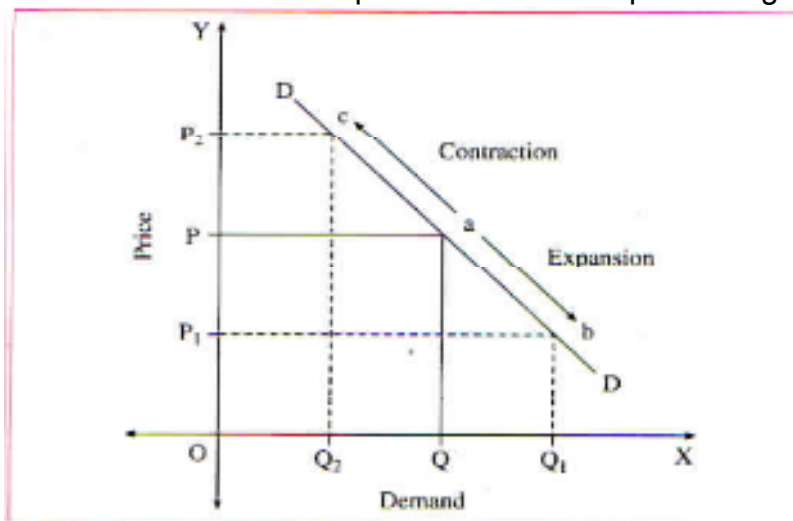
Ans. variation in demand: There are many factors that determine demand. One of the important factor is price. When demand changes due to changes in price, it is known as variation in demand. It is of two types.

- 1) Extension of demand
- 2) Contraction of demand

Extension of demand - With a fall in price when more of a commodity is bought there is 'Extension' (or Expansion) of demand." other things remaining constant.

Contraction of demand - With a rise in price when less of a commodity is bought there is contraction of demand, other things remaining constant.

Extension and contraction of demand is shown by the movement along the same demand curve. This can be explained with the help of a diagram.

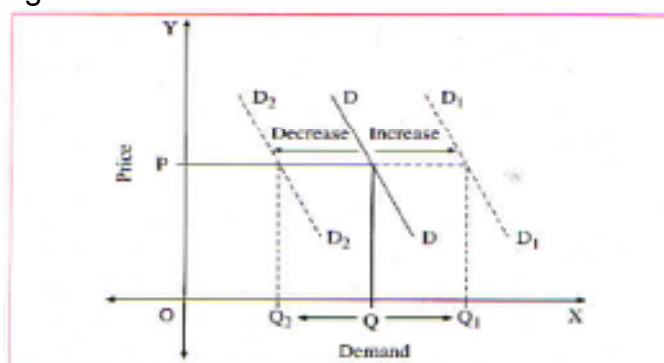


As shown above "DD' is the demand curve. A downward movement on the demand curve from point a to b shows "extension of demand" and the upward movement from point a to c shows "contraction of demand".

Change in Demand: Change in demand implies an increase or decrease in demand. There are many other factors that affect demand other than price such as population, income, tastes and habits, etc.

Increase in demand: When more quantity of a commodity is demanded because of change in the factors determining demand other than price it is an increase in demand.

Decrease in demand: When demand falls due to the changes in factors other than price, it is known as decrease in demand. For example, if income of a consumer decreases, he will demand less of the commodity at constant price, and if income of the consumer increases, he will demand more of a commodity at constant price. Changes in demand can be well explained with the help of the following diagram.



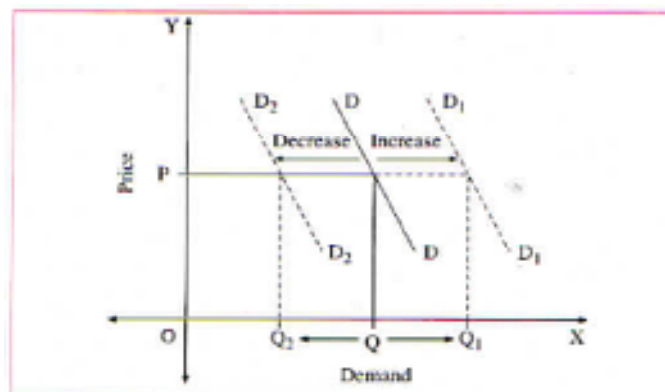
In this diagram, DD is original demand curve, which shows OQ quantity demanded at price P. If we assume that the income of a consumer increases he will demand OQ₁ quantity at the price P, which is greater than original demand. This is an increase in demand. Similarly, if income of a consumer is reduced, he will demand OQ₂ quantity of the product, which is less than OQ. This is decrease in demand. An increase and decrease in demand cannot be shown on one demand curve. When demand increases, demand curve shifts to the right side of original demand curve, i.e. D₁D₁. When demand decreases the demand curve is shifts to the left of the original demand curve, i.e. D₂D₂

2. Explain types of price elasticity of demand.

Ans. The following are the types of price elasticity of demand:

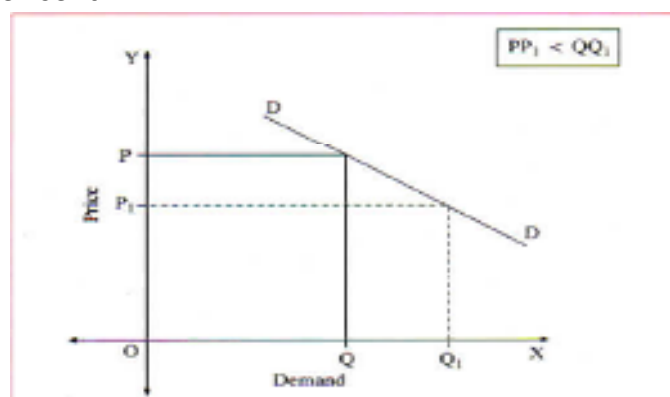
(1) **Unitary Elastic Demand:** When the proportionate change in the price of a commodity brings about exactly equal proportionate change in its quantity demanded, the demand is said to be unitary elastic. The numerical value of unitary elastic demand is one.

For example, if the price of a commodity falls by 25 per cent, its demand also rises by 25 per cent.



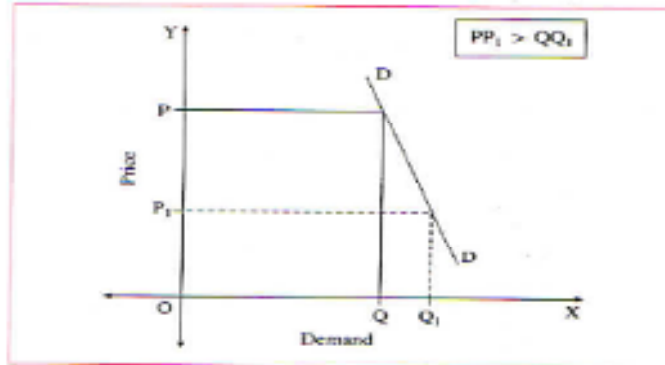
In the case of unitary elastic demand, the demand curve is rectangular hyperbola.

(2) **Relatively Elastic Demand:** When the proportionate change in the price of a commodity brings about greater than proportionate change in its quantity demanded, the demand is said to be relatively elastic. The numerical value of relatively elastic demand is greater than one. For example, if the price of a commodity falls by 25 per cent, its demand rises by 50 per cent.



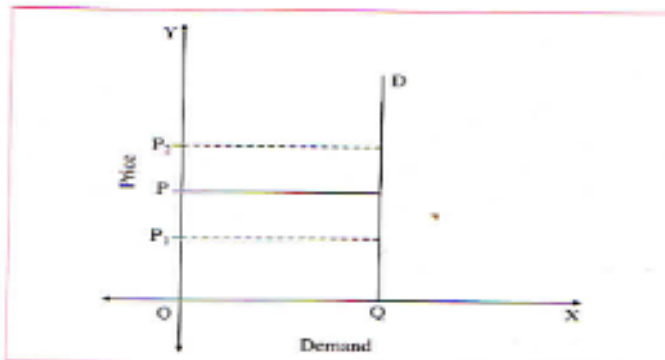
In the case of relatively elastic demand, the demand curve is a flatter line.

- (3) **Relatively Inelastic Demand** : When the proportionate change in the price of a commodity brings about less than proportionate change in its quantity demanded, the demand is said to be relatively inelastic. The numerical value of relatively inelastic demand is less than one. For example, if the price of a commodity falls by 50 per cent, its demand rises only by 25 per cent.



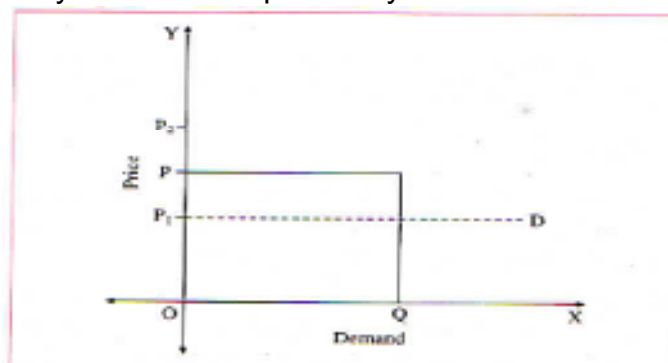
In the case of relatively inelastic demand, the demand curve is a steeper line.

- (4) **Perfectly Inelastic Demand**: When the proportionate change in price of a commodity brings no (zero) proportionate change in its quantity demanded, the demand is said to be perfectly inelastic. The numerical value of perfectly inelastic demand is zero. For example, if the price of a commodity falls by 50 per cent, its demand rises by zero per cent. In practice, such a situation occurs occasionally in the case of necessities such as salt or medicines.



In the case of perfectly inelastic demand, the demand curve is a vertical straight line, parallel to Y-axis.

- (5) **Perfectly/Infinite Elastic Demand**: When a proportionate change in the price of a commodity brings infinite (unlimited) proportionate change in the quantity demanded, the demand is said to be perfectly elastic. The numerical value of perfectly elastic demand is ∞ . perfectly elastic demand is only a theoretical possibility.



In the case of perfectly elastic demand, the demand curve is a horizontal straight line, parallel to X-axis.

3. Explain the conceptual difficulties in measurement of national income.

Ans. Theoretical difficulties:

This is also known as conceptual difficulties.

1) **Transfer payments:**

Individuals get pension, unemployment allowance. but whether these should be included in national income is difficult problem. On one hand, these earnings are a part of individual income and. on the other, they are government expenditure. Therefore, these transfer payments are ignored from national income.

2) **Income of foreign firms:**

According to IMF view-point, income of a foreign firm, should be included in the national income of the country, where the firm actually undertakes production work. However, profits earned by foreign firms are credited to the parent concern.

3) **Unpaid services:**

National income is always measured in money. but there are a number of goods and services which are difficult to be assessed in terms of money. For example, painting as a hobby by an individual, the bringing up of children by the mother, these services are not included in national income as remuneration is not given to them.

Also services of housewives and the services provided out of love, affection, mercy, sympathy and charity are not included in national income, as they are not paid for. By excluding all such services from it, the national income will work out to be less than what it actually is.

4) **Incomes from illegal activities:**

Income earned through illegal activities such as gambling, black marketing, theft, smuggling etc.. is not included in national income. Such goods and services do have value and meet the needs of the consumers. Thus to that extent national income is underestimated.

5) **Treatment of government sector:**

Government provides a number of public services like defence, public administration, law and order etc. Measuring the market value of such government services is difficult, as the real value of these services is not known, therefore it has become a convention to treat all such services as final consumption. Hence, it is included in national income.

6) **Production for self-consumption:**

Goods produced for self-consumption such as food grains, vegetables and other farm products do not enter in the market. But the value of such goods should be estimated at the rate of market price that have been marketed and should be included in national income.

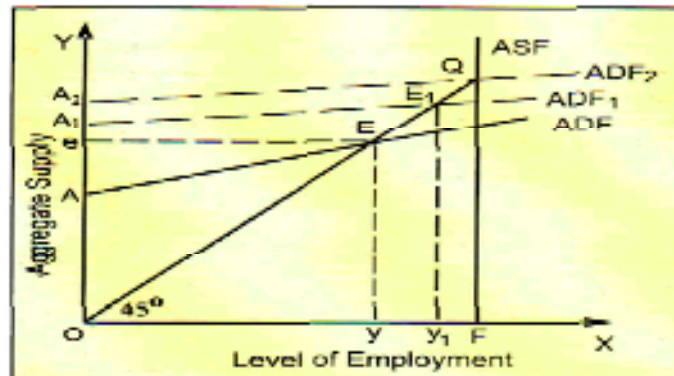
7) **Changing price levels:**

The difficulty of price changes arise in the national income estimate, when the price level in the country rises, the national income also shows an increase even though the production might have fallen and when price level falls. National Income may show a decrease even though production may have increased.

4. What do you mean by effective demand? Explain the concept of “aggregate demand function” and “aggregate supply function”

Ans. Effective Demand is also called macro-economic equilibrium. According to Keynes effective demand is determined with the intersection of aggregate demand and aggregate supply in the economy. The aggregate demand consists of consumption demand, investment demand, government demand, and foreign demand. Similarly aggregate supply depends on natural resources, labour, capital and technology. The equilibrium point of effective demand is that point, where aggregate demand function equals to aggregate supply function. Effective Demand can be shown in the following diagram.

Equilibrium between Aggregate Demand & Aggregate Supply.



The diagram indicates.

ASF = Aggregate Supply Function Curve

ADF = Aggregate Demand Function Curve

e = Point of effective demand (Equilibrium point) is a point at which total expenditure is equal to total income i.e. ADF intersects ASF at this point 'E'. Here level of employment is oy , the economy therefore has reached less than full employment level i.e. equilibrium.

When ADF shifts upwards from ADF to ADF₁ employment will increase from oy to oy_1 if a further upward shift in ADF₁ to ADF₂ the economy will reach full employment level of i.e. at point Q.

Aggregate Demand Function (A.D.F.)

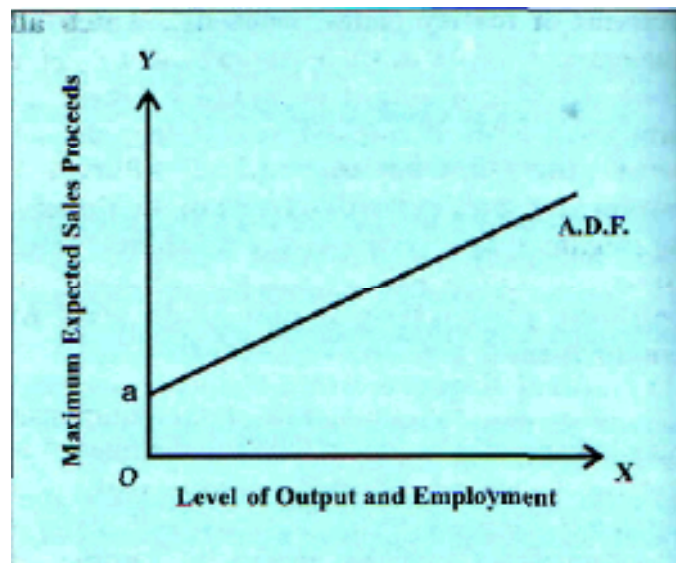
Aggregate Demand Function or Aggregate Demand is measured with the help of aggregate demand price. Here, price means expected maximum sales proceeds. Thus, aggregate demand price refers to what the households and firms are expected to spend on the purchase of different goods and services in the economy. It is this expenditure which becomes the actual sales proceeds or the revenue which producers expect to earn at a given level of employment from the sale of output.

With the increase in the level of employment, aggregate demand price also increases and there is a positive relationship between the level of employment and aggregate demand price, (i.e. expected-sales proceeds)

The Aggregate Demand curve or the Aggregate Demand Function (A.D.F.) as given in the following figure No. 9.1 shows various maximum amounts of sales proceeds, which all the entrepreneurs taken together expect to receive, from the sale of the output produced at different alternative levels of employment, in the economy as a whole.

ADF = f (N). Here ADF = Maximum expected sale proceeds
N = employment and output, f = function of.

Aggregate Demand Function



The ADF is a positive function of the level of employment and output. In the figure 9.1, Y axis shows the aggregate demand price or the maximum expected sales proceeds. The X axis shows the volume or levels of output and employment. The ADF Curve slopes upwards from left to right because, as the level of output and employment increases, income and expenditure of workers also increases. This, in turn increases the aggregate expected sale proceeds. The ADF curve begins from above the origin on vertical axis (Y) at point 'a' indicating that, even at zero level of income (Output and employment), there is some positive consumption, (i.e.. to meet the basic minimum needs), for which Keynes uses the word "autonomous consumption expenditure/"

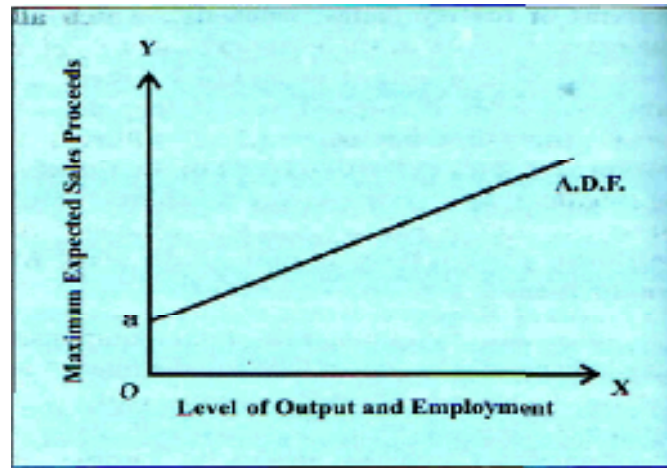
AGGREGATE SUPPLY FUNCTION (A.S.F.)

Aggregate Supply Function or Aggregate Supply is measured with the help of aggregate supply price. Here price implies minimum sales proceeds. In order to produce goods and services, the producers employ different factors of production and pay them in the form of wages, rent, interest, etc. This cost of production including the normal profits must be recovered through sale proceeds.

Aggregate supply price is the minimum amount of money (sales proceeds), which all the entrepreneurs in the economy must receive from the sale of output produced by them, at any given level of employment. If they do not receive this minimum amount, they will reduce output and employment. According to Keynes, aggregate supply price is the minimum sales proceeds which the producers must get to continue production at any given level of employment.

Aggregate Supply Curve or the Aggregate Supply Function (A.S.F.), as shown in the figure 9.2, indicates various minimum amounts of sales proceeds, which must be received by all entrepreneurs, by selling different quantities of output, at various levels of output and employment, in the economy as a whole.

Aggregate Supply Function



In the figure 9.2, ASF curve starts from the origin, showing that the cost of production is zero when there is no employment. The curve slopes upwards to the right as employment increases. In the beginning, it rises slowly and then rapidly. This is because cost of production increases as more and more people are employed. Hence, the minimum sales proceeds required also rise. Once all the persons willing to work get employed, then we have full employment (point F on X axis). The ASF Curve becomes a vertical line, parallel to Y axis (that is. perfectly inelastic), after the full employment level (F), has been achieved in the economy. This indicates that even if aggregate supply price increases. employment cannot increase. Above point Q in the figure, the Aggregate Supply Function (A.S.F.) or curve becomes vertical.