SYJC ECONOMICS PRELIM JAN'18
SOLUTION (24.1.2018)

प्र. क्र.
Q. No. 1 (A)

Note : Five statements with four options each will be given in the question paper. Rewrite the complete statement in the answer sheet by choosing the correct alternative. Underline the selected alternative (answer). Do not change the sequence of the statements.

(1) Market demand is a total demand of <u>all</u> buyers.

(2) Perfectly inelastic demand curve is <u>vertical straight line parallel to 'OY' axis</u>.

(3) Other factors remaining constant, when price of a commodity rises, there is <u>extension</u> of supply.

(4) National income is <u>flow concept</u>.

(5) <u>Central bank</u> is the apex body of the monetary and banking system of the nation's economy.

(Marking scheme : 1 mark for each correct answer; Total 5 marks)

1 (B)

Note : Five items will be given in Group 'A' to match from the eight alternatives in Group 'B'. Rewrite each item from Group 'A' in the answer sheet and write the appropriate alternative from Group 'B' in front of it. Do not change the sequence of the items in Group 'A'.

(a) Adam Smith - (2) Father of economics

(b) Railway - (3) Public monopoly

(c) Legal tender money - (7) Fiat money

(d) D-mat account - (5) Buying and selling of shares

(e) Bank rate - (6) Quantitative tool of credit control

(Marking Scheme : 1 mark for each correct pair; Total 5 marks)

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Q. No. 1 (C)

Note : Six statements will be given in the question paper. Rewrite the complete statement in the answer sheet followed by the correct answer True or False.

(1) Total Revenue = Total quantity × Price - True.

(2) Demand for necessary goods is inelastic - True.

(3) Capital is a natural factor of production - False.

(4) Consumption expenditure is the only component of aggregate demand - False.

(5) Credit money is created by the central bank of a country - False.

(6) Budget is a monthly statement - False.

(Marking Scheme : 1 mark for each correct answer; Total 6 marks)

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Q. No. 2 (A)

Note : Six concepts will be given in the question paper. You are expected to Define or Explain any three of them. This is a very short answer type question. Therefore, write answers to-the-point. Write atleast 2 definitions or 2 points of explanations / formulas as well as draw diagrams wherever needed. Underline important points.

(1) Microeconomics :

(i) Microeconomics is the branch of economics concerned with the study of economic behaviour of individual economic units.

(ii) It studies the behaviour of individual households, firms, industries, product pricing and factor pricing as well as allocation of resources.

(2) Service utility :

(i) Utility obtained by the consumers from the services given by the professionals is called service utility.

(ii) For instance, a utility obtained by the consumers from the services of doctors, teachers, chartered accountants, lawyers, etc.

(3) Unitary elastic demand :

(i) 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.

(ii) The numerical value of unitary elastic demand is One. For instance if the price of a commodity falls by 25 per cent, its demand also rises by 25 per cent. In the case of perfectly elastic demand, the demand curve is a horizontal straight line, parallel to X-axis.

(4) Disposable income :

(i) Disposable income or Personal disposable income is that part of personal income which is left after payment of personal direct taxes like income tax, personal property tax, etc.

(ii) Disposable income is used for consumption or saving.

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Q. No. 2 (A)

(5) Autonomous consumption :

(i) Consumption is that part of income which is spent on purchasing goods and services. Autonomous consumption refers to the types of consumption which is independent of income. It is income inelastic.

(ii) Autonomous consumption can never be zero. Even at a zero income level, there is some positive autonomous consumption.

(6) Bank rate :

(i) Bank rate is the minimum rate of interest charged by the Central Bank to commercial banks while giving loans to them against eligible securities or by rediscounting bills of exchange. It is also called rediscount rate.

(ii) During inflation, the bank rate is increased. This, in turn, increases the lending rate of commercial banks which ultimately leads in contraction in credit and control over inflation. On the other hand, during deflation, the bank rate is decreased. This, in turn, decreases the lending rate of commercial banks which ultimately leads in expansion in credit and control over deflation.

(Marking Scheme : 2 marks for each correct answer; Total 6 marks.)

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Q. No. 2 (B)

Note : Six statements will be given in the question paper. You are expected to give reasons to any three of them. This is also a very short answer type question. Therefore, write only two to four points of explanation / reasons in the answer. Your answer may have question-statement either in the beginning or at the end.

(1) (i) According to the law of supply propounded by Dr. Alfred Marshall, 'Other things being constant, the higher the price of the commodity greater is the quantity supplied and lower the price of the commodity, smaller is the quantity supplied.'

(ii) Individual Supply Schedule :

Price (₹)	Supply (Units per day)
100	10
200	20
300	30

From the above individual supply schedule, it can be seen that at less price (₹100) supply tends to be less (10 units) and at more price (₹300) supply tends to be more (30 units). This shows that supply is directly related to price.

(2) (i) In a monopoly market, there is a single seller or a single producer. Therefore, the monopolist has no rivals and he faces no competition. In a monopoly market, there are large number of buyers and they do not have any other substitute for the product produced by the monopolist.

(ii) Under monopoly, the entry of other firm is strictly restricted by natural, economic, technological or legal barriers. Therefore, in monopoly, the monopolist can charge any price for his product. He can also charge different prices to different consumers for the same product. Therefore, price discrimination is possible under monopoly.

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Q. No. 2 (B)

(3) (i) Labourer and his labour (work) always go together. Hence labourer must be present himself where he is supposed to render his services.

(ii) Labour is perishable in nature. If a labourer is absent for a day, his labour for that day goes wasted. Thus, the amount of labour lost is lost forever, it cannot be used for future. Thus, labour cannot be stored and used for future.

(4) (i) Macroeconomics is the study of economic system as a whole. It studies wide aggregate (macroeconomic) variables like national income, total employment, general price level, economic growth rate, total investment, etc.

(ii) It also studies the interrelation among these various aggregates, their determination and causes of fluctuations in them. Thus, macroeconomics is the study of aggregates.

(5) (i) By the Banking Act, commercial banks have to maintain a certain per cent (3 per cent to 15 per cent) of cash with Central Bank (RBI) as reserves against their demand and time deposits. This amount cannot be used by banks for lending activities.

(ii) If the CRR is increased the amount available for lending gets reduced and vice versa. Thus, the CRR affects the lending capacity of the banks.

(6) (i) Microeconomics is concerned with the study of economic behaviour of small individual economic units of an economy. Resource allocation means utilisation of resources for the production of various goods and services. The study of microeconomics is mainly confined to resource allocation.

(ii) Microeconomics explains how relative prices of commodities and factors of production determine the allocation of resources. Allocation of resources determines what goods are to be produced,

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how the goods are to be produced and distributed, etc. Microeconomics also examines the efficiency in the allocation of resources and economic welfare of society.

(Marking Scheme : 2 marks for each correct answer; Total 6 marks.)

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Q. No. 3 (A)

Note : Six pairs will be given in the question paper. You are expected to Distinguish between any three of them. Only two points are expected in answer. Write the first point explaining the difference between meaning / definition. Write the second point explaining the difference between scope / nature / formula / interrelationship, etc. Give subtitles to each point and underline them.

(1)

Increase in demand	Decrease in demand
(i) Meaning :	
A rise in demand caused by favourable changes in other factors than price is called increase in demand.	A fall in demand caused by unfavourable changes in other factors other than price is called decrease in demand.
(ii) Causes :	
Increase in demand is caused by : (1) Rise in income (2) Increased liking for a commodity (3) Decrease in taxes	Decrease in demand is caused by : (1) Fall in income (2) Decreased liking for a commodity (3) Increase in taxes

(2)

Partial equilibirium	General equilibirium
(i) Meaning :	
Partial equilibrium is a type of equilibrium used in microeconomics, which explains the equilibrium of a particular unit of an economy.	General equilibrium is a type of equilibrium used in macroeconomics, which explains the equilibrium of the entire economy.
(ii) Nature :	
Partial equilibrium neglects the functional relationship and interdependence between the economic variables by assuming 'other things being constant.'	General equilibrium assumes the functional relationship and inter-dependence between the economic variables by assuming 'everything depends on everything else.'

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Q. No. 3 (A)

(3)	Personal income	National income
	(i) Meaning :	
	Personal income is the sum of all incomes actually received by all individuals or households from all the sources during a given year.	The national income is the aggregate monetary value of all final goods and services produced in a country during one year.
	(ii) Concept :	
	Study of personal income comes under the purview of micro-economics. It is a microeconomic concept.	Study of national income comes under the purview of macro-economics. It is a macroeconomic concept.

(4)	Standard Coins	Token Coins
	(i) Meaning :	
	Full bodied money (Standard coins) are those coins whose face value is equal to their intrinsic value.	Token coins are those coins whose face value is higher than their intrinsic value.
	(ii) Metals used :	
	Full bodied/Standard coins were made out of standard metals like gold and silver.	Token coins are made out of cheaper metals like aluminium, nickel, etc.

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Q. No. 3 (A)

(5)

Direct tax	Indirect tax
(i) Meaning :	
A tax which is paid by the person on whom it is levied is called direct tax.	A tax which is paid by a person on whom it is not actually levied is called indirect tax.
(ii) Examples :	
Income tax, wealth tax, etc. are the examples of direct tax.	Sales tax, Excise duty, etc. are the examples of indirect tax.

(6)

Extension of supply	Contraction of supply
(i) Meaning :	
A rise in supply caused by rise in the price while other factors remaining constant is called expansion (extension) of supply.	A fall in supply caused by fall in price while other factors remaining constant is called contraction supply.
(ii) Equilibrium point :	
In expansion in supply, the equilibrium point moves upwards from the left to the right on the same supply curve.	In contraction in supply, the equilibrium point moves downwards from the right to the left on the same supply curve.

(Marking Scheme : 1 mark for meaning and 1 mark for explaining the difference. 2 marks for each correct answer; Total 6 marks.)

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Q. No. 3 (B)

Note : Four short notes will be asked in the question paper. You are expected to attempt any two of them. Write precise and to-the-point answers. Draw diagrams as well as write schedules, formulas, etc. Underline and give subtitles, wherever necessary.

(1) Importance of microeconomics :

(i) Helpful to understand the working of free market economy : Microeconomics helps to understand how free market economy works and gets regulated by demand and supply principles.

(ii) Helpful in explaining price determination and allocation of resources : Microeconomics helps in explaining the price determination of goods and services as well as factors of production. It also explains the process of and efficiency in the allocation of resources.

(iii) Helps businessmen : Microeconomics helps businessmen in formulating prices of product or service, minimising the cost of production, analysing profitability of investment, attainment of maximum productivity, etc. It also helps businessmen in demand forecasting.

(iv) Useful to government : Microeconomics is useful to government in framing economic policies such as tax policy, public expenditure policy, price policy, etc. Microeconomics also guides government in attaining the goal of efficient allocation of resources and economic welfare of society.

(v) Helpful in international trade and public finance : Microeconomics is useful in studying the aspects related to international trade such as effects of tariff, determination of exchange rate, gains from international trade, etc. Microeconomics also helps in analysing the aspects related to public finance such as incidence and effect of a particular tax.

(vi) Helpful in model building : Microeconomics helps in understanding complex economic situations with its variety of models. Many terms,

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concepts, terminologies, tools of economic analysis of microeconomics have valuably contributed to the science of economics.

(2) Factors determining elasticity of demand :

(i) Nature of Commodities : Nature of commodities is one of the important factors influencing the elasticity of demand. For example, the demand tends to be elastic for luxury goods like branded watches, perfumes, etc. and inelastic for necessaries like salt, medicines, etc.

(ii) Durability : Elasticity of demand also gets influenced by the durability of a commodity. Durable commodities such as tables, fans tends to have elastic demand and the perishable commodities such as flowers, fruits tend to have inelastic demand.

(iii) Substitute Goods : A commodity having larger number of substitutes tends to have elastic demand and vice versa. For example, due to the availability of larger number of substitutes, the demand for cold drinks tends to be elastic. Similarly due to a lack of substitutes, the demand for salt is inelastic.

(iv) Uses of a Commodity : A commodity which can be put to several uses has elastic demand. When the price of such a commodity falls, it is put into various uses. Similarly when the price of such a commodity rises, it is put only for important purposes. For example, electricity has elastic demand.

(v) Price : High priced goods such as diamond as well as low priced commodities like match box tend to have inelastic demand. On the other hand, the demand for medium priced goods such as perfumes, T-shirts tend to have elastic demand.

(vi) Habits : The demand for habituated goods tends to be inelastic. For example, a smoker's demand for cigarettes is inelastic.

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(3) Features of monopoly :

(i) Single seller : In a monopoly market there is a single seller or a single producer. Under monopoly, the monopolist has no rivals and therefore he faces no competition.

(ii) No close substitute : There are no close substitutes for the commodity sold in the monopoly market. Therefore a monopolist faces no competition.

(iii) Barriers to entry : Under monopoly, the entry of other firm is strictly restricted. The monopolist has complete hold over the supply in the market. Such a provision protects monopoly powers.

(iv) No distinction between firm and the industry : Under monopoly there is only one seller. Therefore, there is no distinction between the firm and the industry. Under monopoly, the firm itself becomes the industry of a product.

(v) Control over the market supply : The monopolist has the complete hold over the market supply as he is a sole producer of the commodity. In monopoly, many entry barriers such as natural, economic, technological or legal do not allow competitors to enter the market.

(vi) Price maker : The firm under monopoly is a price maker and not a price taker. Monopolist can set any price of the commodity as he has complete control over the supply of the product.

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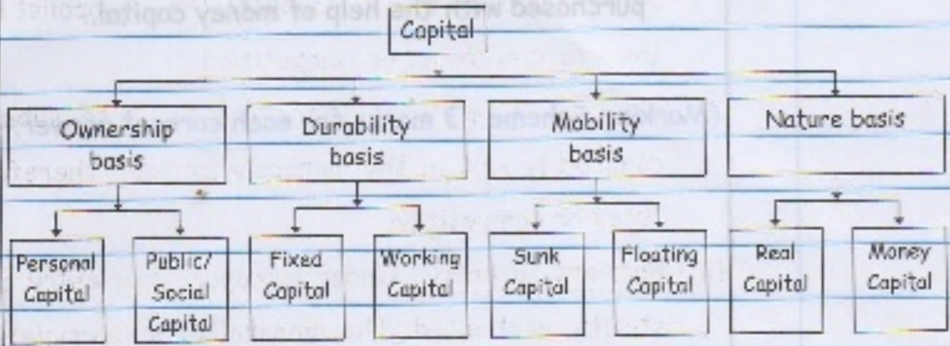
(4) Types of capital : The different types of capital are shown in the following chart :



The different types of capital are explained as follows :

(i) Private or Personal capital : Capital which is owned by individual or institute is called private or personal capital. For example, a firm owned by an individual, machinery, etc.

(ii) Public or Social capital : Capital which is owned collectively by the society or the government, is called public or social capital. For example, municipal school, municipal hospital, railways, etc.

(iii) Fixed capital : Capital which is used in a production process again and again is called fixed capital. It is durable in nature. For example, machinery, factory building, etc.

(iv) Working or Circulating capital : Capital which is used in a production process only once is called working or circulating capital. It is also known as variable capital. For example, raw material, power fuel, etc.

(v) Sunk capital : Capital which is used for a specific purpose is called sunk capital. It cannot be used easily from one business to another business. For example, xerox machine, road roller, railway lines, etc.

(vi) Floating capital : Capital which has several alternative uses is called floating capital. It can be used easily from one business to another business. For example, electricity, coal, petrol, etc.

(vii) Real capital : Physical capital used in the production process is called real capital. For example, machinery, raw material, equipment, etc. It is used to produce other goods.

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(viii) Money capital : Capital which is in the form of money is called money capital. Real capital like raw material, machinery can be purchased with the help of money capital.

(Marking Scheme : 3 marks for each correct answer; Total 6 marks)

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Q. No. 4

Note : Six short answer questions will be asked in the question paper. You are expected to write answers to any three of them. Write precise and to-the-point answers. Underline important points of the answers. Write definitions, schedules, formulas, etc. as well as draw diagrams wherever necessary. Give subtitles wherever possible.

(1) Characteristics of utility :

(i) Relative concept : Utility changes from time to time and from place to place. For example, woollen clothes possess more utility during winter and less utility during summer. Similarly they possess more utility in Kashmir and less utility in Mumbai.

(ii) Subjective concept : Utility gets influenced by person's likes, dislikes, habits, preferences, etc. Therefore utility changes from person to person. For example, a non-vegetarian finds utility in mutton, but the vegetarian does not find utility from it.

(iii) Ethically neutral : The concept of utility is morally and ethically colourless. Utility never takes into account the concepts such as good or bad, moral or immoral, etc. For example, in economics, milk as well as wine possesses utility.

(iv) Utility and usefulness are not same : Commodity possessing utility may not always possess usefulness. Utility and usefulness are totally different concepts. For example, a harmful product like poison possesses utility but it does not possess usefulness.

(v) Not same as pleasure : A commodity possessing utility may not always provide pleasure to the consumer. Thus utility and pleasure are totally different concepts. For example, injection possesses utility, but its consumption does not give pleasure to the patient.

(vi) Utility differs from satisfaction : Utility and satisfaction are totally different concepts. Utility is the starting point of consumption, whereas satisfaction is derived after consumption. For example, for a thirsty person a glass of water has utility. When he drinks that glass of water he derives satisfaction from it.

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Q. No. 4

(vii) Not easily measurable : Utility is a psychological concept. It has no physical existence. Therefore it cannot be measured in numbers.

(viii) Depends upon the intensity of want : Utility has direct relation to intensity of want. Individual finds more utility in a commodity if his want is more intense and vice versa. For example, hungry individual finds more utility in food than a person who is not so hungry.

(2) Features of pure competition :

(i) Large number of sellers : In pure competition, there is a large number of potential sellers selling their commodity in the market. Their number is so large that a single seller cannot influence the market price.

(ii) Large number of buyers : In pure competition, there is a large number of potential buyers buying commodity in the market. Their number is so large that a single buyer cannot influence the market price.

(iii) Free entry and exit : In pure competition, any firm can freely enter or can take exit from the market without any restrictions.

(iv) Homogeneous product : In pure competition, every firm produces and sells identical products, i.e. units of a commodity produced by each firm are uniform in respect of size shape, colour, quality, etc. Therefore the commodities sold in pure market are perfect substitutes to one another.

(v) Single price : In pure competition, all units of commodity have uniform and single price and it is determined by the interaction of forces of market demand and market supply.

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(3) Features of macroeconomics :

(i) Study of aggregates : Macroeconomics deals with the study of a nation's economy as a whole. It is the study of very large, economy-wide aggregates such as national output, total employment, aggregate demand, aggregate supply, total investment, total consumption, general price level, etc.

(ii) Lumping method : Macroeconomics deals with the behaviour of aggregates, i.e. total values of macroeconomic variables. Therefore, it uses lumping method.

(iii) A general equilibrium analysis : Macroeconomics studies the behaviour of a number of economic variables at a time and takes into consideration their interdependence. It assumes 'everything depends on everything else.'

(iv) Income analysis : Macroeconomics is also known as the Theory of Income and Employment or Income Analysis. It explains the determination of the level of national income and employment and what causes fluctuations in them.

(v) Policy-oriented : Macroeconomics, according to Keynes, is a policy oriented science. Macroeconomic 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.

(vi) Dynamic Science : Macroeconomics studies the changes in aggregate economic variables and analyses dynamic nature of the economy. It enables us to study the progress of an economy over a period of time.

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Q. No. 4

(4) Primary functions of commercial bank :

(1) Accepting deposits : Accepting deposits from the public is the primary or basic function of commercial bank. The bank acts as an intermediary by accepting deposits and paying interest on them and lending loans and charging higher interest to the borrowers. Commercial bank accept the following types of deposits :

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

(i) Current account deposits : It is usually opened by businessmen, corporations, industrial enterprises, public bodies, trustees, etc. The current account facilitates account holders to carry out their transactions with minimum cash at hand.

(ii) 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. They are opened mainly by salaried class, middle income group or small traders.

(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 :

(i) Recurring deposits : In order to encourage people to make regular savings, banks receive deposits in recurring accounts. A person is required to deposit a fixed sum of money for a specified period of time.

(ii) Fixed deposits : Deposits under this account are made for a fixed or a specified period. The money can be withdrawn only after the stipulated or specified time period. Rate of interest is relatively higher on these deposits.

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(2) Advancing loans : The deposits accepted by the banks from the depositors are not kept as 'idle cash balance'. After keeping certain cash reserves, the balance is used to lend to the needy borrowers in the forms of loans and advances. Generally, banks grant loans and advances to the borrowers in the following forms :

(A) Loans : Loans can be classified into the following types :

(i) Call loans / Money at call notice : Loans provided by commercial banks for a period of 7 to 15 days are known as call loans.

(ii) Short term loans : Short-term loans are provided by commercial banks for a period of not more than two years.

(iii) Medium term loans : Medium term loans are provided by commercial banks for a period from 2 years up to 5 years.

(iv) Long term loans : Long term loans are provided by commercial banks for a period of more than 5 years.

(B) Cash credit : Cash credit facilities are allowed to any customer / borrower by which the borrower is allowed to draw from that account up to a certain limit against eligible securities.

(C) Overdraft facility : Overdraft facility is generally given to current account holders by which customers are allowed to withdraw the amount from the account in excess of their balance.

(D) Discounting of bills : Discounting of bill of exchange means advancing a loan against a promise of repayment in future. The commercial bank charge a commission for discounting bills.

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Q. No. 4

(5) Types of budget :

The different types of budget are shown in the following chart :

- Budget
  - Balanced Budget
  - Surplus Budget
  - Deficit Budget

The different types of budget are explained as follows :

(i) Balanced Budget : A government budget is said to be balanced when its estimated revenue and anticipated expenditure are equal. i.e. Government Receipts = Government Expenditure.

The concept of balanced budget has been advocated by classical economists like Adam Smith. A balanced budget was considered by classical economists as neutral in its effect on the working of the economy and hence they regarded it as the best.

However, modern economists believe that the policy of balanced budget may not always be suitable for the economy.

(ii) Surplus Budget : When estimated government receipts are more than the estimated government expenditure it is termed as surplus budget. Thus, in a surplus budget, Estimated Government Receipts > Anticipated Government Expenditure.

A surplus budget is used either to reduce government public debt (its liabilities) or to increase its savings.

A surplus budget may prove useful during the period of inflation. However, it should not be used in situation other than the inflationary gap, as it may lead to unemployment and low levels of output in an economy.

(iii) Deficit Budget : When estimated government receipts are less than the estimated government expenditure, then the budget is termed as deficit budget. In deficit budget, Estimated Government Receipts < Anticipated Government Expenditure.

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A deficit budget increases the liability of the government or decreases its reserves.

A deficit budget may prove useful during the period of depression.

(6) The determinants of aggregate demand :

The determinants of the aggregate demand are expressed as $AD = C + I + G + (X - M)$. They are as follows :

(i) Consumption expenditure (C) : Consumption expenditure refers to the expenditure incurred on those goods and services which satisfy the wants of private individuals and institutions directly. Consumption expenditure is directly related to the aggregate demand.

(ii) Investment expenditure (I) : An addition to the country's physical stock of capital is called investment. Expenditure incurred on forming the capital is called investment expenditure. Investment expenditure is directly related to the aggregate demand.

(iii) Government expenditure (G) : The consumption expenditure and investment expenditure incurred by the government for the purpose of maximising welfare and promoting maximum growth and development is called government expenditure. Government expenditure is directly related to the aggregate demand.

(iv) Net earnings from foreign transactions (X – M) : The difference between the export value and the import value is known as net earnings from foreign transactions. Positive net earnings increases the aggregate demand, negative net earnings decreases the aggregate demand and zero net earnings does not affect aggregate demand.

(Marking Scheme : 4 marks for each correct answer; Total 12 marks)

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Q. No. 5

Note : Six questions will be given in the question paper. You are expected to write answers to any three questions. 1 mark is allotted for stating 'Yes' or 'No' and 3 marks are allotted for stating correct reasons. Rewrite the statement in the answer sheet followed by the correct option of 'Yes, I Agree' or 'No, I do not agree' (Disagree). Write atleast three reasons. Draw diagrams, schedules wherever necessary.

(1) There are no exceptions to the law of demand.

No, I do not agree with this statement.

Reasons : The following are some of the exceptions to the law of demand :

(i) Giffen goods : Sir Robert Giffen from England noticed that in the case of inferior quality products (Giffen goods), the Law of Demand does not hold good. When the price of Giffen goods falls, buyers' real income gets increased. As its effect, buyers demand more of superior quality goods. Thus, a fall in the prices of Giffen goods leads to fall in their demand.

(ii) Prestige goods : Diamonds, luxury cars, posh bungalows, etc. are considered as prestige goods. Such goods have a snob appeal. Therefore, prestige goods are demanded in greater quantities at higher prices and vice versa.

(iii) Price illusions or Consumers' psychological bias : Many consumers wrongly assume that high priced goods are of better quality. Due to this illusion, such buyers demand costlier goods in greater quantities.

(iv) Demonstration Effect : Many low income group people have the tendency of imitating the consumption pattern of high income group. This effect is called demonstration effect. Due to this effect, people from low income group demand more of costlier products and services.

(v) Ignorance : Many times the buyers do not have a complete knowledge of a market. Due to such ignorance, they demand costlier goods in greater quantities.

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Speculation, habitual goods, etc. are some other exceptions to the law of demand.

(2) A commercial bank can create credit on the basis of primary deposits.

Yes, I agree with this statement.

Reasons :

(i) 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.

(ii) 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.

(iii) When the borrower withdraws money from his loan account by a cheque, it is deposited by the payee in some other bank. 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.

(3) Central bank is called the bankers' bank.

Yes, I agree with this statement.

Reasons :

The central bank acts as a leader, bankaer and coordinator of commercial banks in the country. As a banker or leader to all other banks, the central bank performs the following functions :

(i) Custodian of cash reserves of commercial banks : By Banking Act, every commercial bank has to maintain a contain percentage of its total demand and time deposits with the central bank. By varying the legal minimum cash Reserve central bank controls the total volume of credit created by the commercial banks.

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(ii) Clearing house facility : All commercial banks are required to keep deposit accounts with the Central Bank. Because of this the Central bank is in a position to act as clearing house for commercial banks. Commercial banks are the members of the central bank's clearing house system which facilitates the settling of daily balances due between the member banks arising from cheque and cash transactions throughout the economy.

(iii) Advices to commercial banks : The Central bank advices the commercial banks if their activities are harmful to commercial banking. In case of financial difficulties, Central bank provides financial accommodation to commercial banks by lending funds.

(iv) Lender of the last resort : The commercial banks operate on the basis of low cash reserve system. If there is a great (sudden) demand for cash by the depositors, even a well managed commercial bank can run into difficulty. In such cases, the Central bank comes to help commercial bank. Thus, Central bank is the ultimate source of financial assistance to all commercial banks in a country. Thus, during the financial crisis, commercial banks always approach the Central bank for required financial assistance.

Thus, Central Bank acts as a banker to all Comercial banks.

(4) There is no difference between stock and supply.

No, I do not agree with this statement.

Reasons :

(i) Stock refers to the entire quantity of commodity, which exists with the seller. It is the potential supply. Supply refers to the quantity of a commodity offered for sale at a given price and at a point of time.

(ii) Stock always depends upon the quantity of products produced or purchased by the producer or businessman. Supply directly depends upon quantity of products available in the stock. Thus, stock is a source from where supply of products can be made.

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(iii) Stock is always greater than supply. However, in case of perishable goods such as fish, milk, fruits, vegetables, etc., stock and supply can be same. Supply can never exceed the stock. Therefore, there is a difference between stock and supply.

(5) General acceptability is the only quality of good money.

No, I do not agree with this statement

Reasons : Apart from general acceptability good money has many other qualities. Other qualities of good money are explained as follows :

(i) Divisibility : Good money posses the quality of divisibility. It is divisible into different denominations such ₹ 25, ₹ 10, ₹ 50, ₹ 100, ₹ 500 and so on.

(ii) Durability : Good money posses the quality of durability. Good money last for a longer period of time, e.g. metallic coins are more durable than paper currency.

(iii) Cognizability : Good money posses the quality of cognizability i.e. easily recognizable and distinguishable from other things.

(iv) Portability : Good money posses the quality of portability i.e. easy to carry from one place to another without any difficulty, expense and inconvenience, e.g. Paper currencies are easily portable.

(v) Homogeneity : Good money posses the quality of homogeneity i.e. the money of same denomination should be same in size, weight, appearance, etc.

(6) Law of Diminishing Marginal Utility is important in practice.

Yes, I agree with this statement.

Reasons :

(i) The law of DMU helps consumers in deriving the maximum satisfaction from the given income.

(ii) Similarly the law also helps the producer in determining price and sales policy and thereby maximising his profits.

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(iii) The law of DMU is helpful to the monopolist to practise price discrimination and thereby maximising his profits.

(iv) The law of DMU is helpful to the government in implementing economic policies such as public distribution system, social justice, etc.

(v) The law is helpful to the finance minister in framing the progressive tax system and thereby reducing economic inequality and to improve the welfare of society.

(vi) The law of DMU helps in explaining the paradox of value in use and value in exchange in case of water and diamond. Water has less price, though has more value in use. Diamond has high price though has less value in use.

(Marking Scheme : 1 mark for stating Agree or Disagree and 3 marks for giving reasons, 4 marks for each correct answer; Total 12 marks.)

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Note : Four long answer questions will be asked in the question paper. You are expected to write explanatory answers to any two questions. Write answers to-the-point. Underline the important points. Write definitions, schedules, and formulas as well as draw diagrams wherever necessary.

(1) (A) The law of demand : The law of demand can be stated and explained with the help of the following points :

(i) The law of demand is one of the fundamental laws of consumption. It is propounded by Dr. Alfred Marshall in his famous book, 'Principles of Economics'. The law of demand explains the inverse relationship between the price and the demand.

(ii) Statement of Law : "Other things being equal, the amount demanded rises with a fall in price and diminishes with a rise in price."

(iii) The law of demand can be explained with the help of the following individual demand schedule :

Price (₹)	Individual demand of commodity x (per day in units)
100	5
200	4
300	3
400	2
500	1

(iv) Explanation of individual demand schedule : From the above individual demand schedule it can be observed that at a lesser price (₹ 100) more units of commodity x are demanded (5 units). Similarly, at a higher price (₹ 500) less units of commodity x are demanded (1 unit). Thus there exists an inverse relationship between the price and the quantity demanded.

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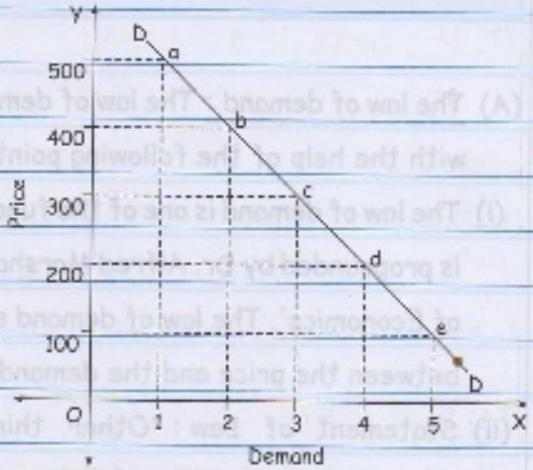
(v) The law of demand can be explained with the help of the following diagram of individual demand curve.



(vi) Explanation of individual demand curve : In the above diagram, Y-axis represents the price of the commodity x and X-axis represents demand of commodity x. From the above diagram it can be seen that the demand curve, i.e. DD slopes downwards from the left to the right. Price and demand are inversely related to each other. Therefore, the demand curve has negative slope.

(B) Assumptions :

(1) No change in population : The law assumes that the size and composition of population remains constant.

(2) No change in income : The law assumes that there is no change in consumer's income.

(3) No change in tastes and habits : The law assumes that there is no change in tastes, habits, preferences, likings, etc. of the consumer.

(4) No expectations regarding future price : The law assumes that consumers do not have any expectations regarding rise or fall in the price of a commodity in the near future.

(5) No change in prices of substitute goods : The law assumes that the prices of substitute goods of a commodity in question remain constant.

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(6) No change in prices of complementary goods : The law assumes that the prices of complementary goods of a commodity in question remain constant.

(7) No change in government policy : The law assumes that the government's taxation policy remains constant.

(Marking Scheme : 6 marks for explanation of law of demand with statement, schedule and diagram; 2 marks for assumptions; Total 8 marks.)

(2) (A) Ratio method :

(1) Ratio method of measuring elasticity of demand is developed by Dr. Alfred Marshall. This method is also known as arithmetic method or percentage method or proportional method of measuring elasticity of demand.

(2) In this method, the elasticity of demand is measured by dividing the percentage change in the quantity demanded of a commodity by the percentage change in its price.

(3) The formula used for the measurement of the elasticity of demand is as follows :

$$E_d = \frac{\text{Proportionate change in the quantity demanded}}{\text{Proportionate change in the price}}$$

Symbolically,

$$E_d = \frac{\triangle Q}{\triangle P} \times \frac{P}{Q}$$

Where, (i) $\triangle Q$ Change in the quantity demanded, i.e. $Q_1 - Q$, i.e. New Demand - Original Demand, (ii) $\triangle P$ = Change in the price, i.e. $P_1 - P$, i.e. New Price – Original Price (iii) P = Original Price and (iv) Q = Original Demand.

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(4) Ratio method can be explained with the help of the following example :

	Price (₹)	Demand (per day in units)
Original	200	1000
New	100	1500

$$E_P = \frac{(1500 - 1000)}{(100 - 200)} \times \frac{200}{1000} = \frac{500}{-100} \times \frac{200}{1000} = -1 = 1$$

(By eliminating negative sign)

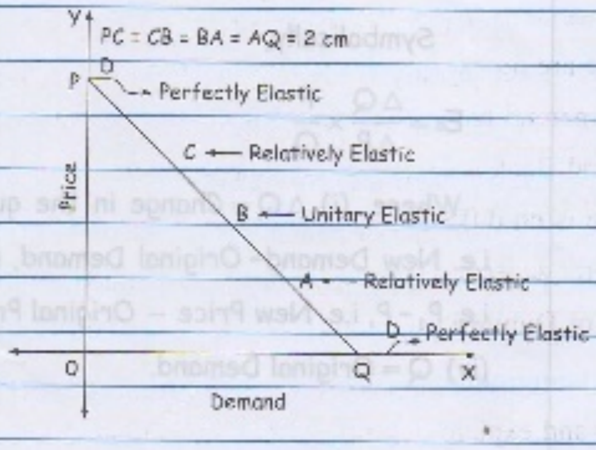
As the numerical value of the elasticity of demand is 1, the demand is unitary elastic in this example.

(B) Geometric method :

(1) Geometric method of measuring elasticity of demand is also developed by Dr. Alfred Marshall. This method is also known as point method of measuring elasticity of demand.

(2) This method is used to find out the elasticity of demand at any given point on a demand curve.

(3) For measuring the elasticity of demand at a given point on the linear demand curve, the linear demand curve can be extended to meet the Y-axis at P and X-axis at Q as follows :



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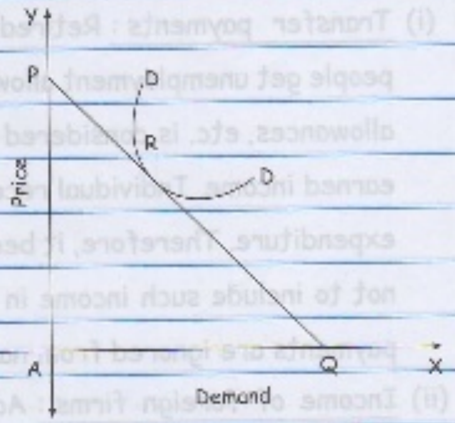
The price elasticity of demand at a point 'A' can be calculated with the help of the following formula :

$$E_d = \frac{\text{Lower segment of the demand curve below the given point}}{\text{Upper segment of the demand curve above the given point}}$$

$$E_d = \frac{AQ}{AP} = \frac{2}{6} = 0.33$$

At point 'A' the numerical value of elasticity of demand is less than one ($E_d = 0.33$). Therefore at point 'A' the demand is relatively inelastic.

(4) For measuring the elasticity of demand at a given point on the non-linear demand curve, tangent from a given point touching the Y-axis and X-axis is drawn as follows : RQ = 6 cm, RP = 2 cm



The price elasticity of demand at a point 'R' can be calculated with the help of the following formula :

$$E_d = \frac{\text{Lower segment of the tangent below the given point}}{\text{Upper segment of the tangent below the given point}}$$

$$E_d = \frac{RQ}{RP} = \frac{6}{2} = 3$$

At point 'R' the numerical value of elasticity of demand is greater than one. ($E_d = 3$). Therefore at point 'R' the demand is relatively elastic.

[Marking Scheme : 4 marks for Ratio method and 4 marks for Geometric method; Total 8 marks.]

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(3) (A) Meaning of National Income :

(i) According to Pigou, "The national income is that part of the objective income of the community, including of course income derived from abroad, which can be measured in money."

(ii) According to Fisher, "The national dividend or income consists solely of services as received by ultimate consumer, whether from their material or from their human environments."

In brief the national income is the aggregate monetary value of all final goods and services produced in the economy in a period of one year.

(B) Theoretical difficulties also known as conceptual difficulties in measuring the national income are as follows :

(i) Transfer payments : Retired people gets pension. Unemployed people get unemployment allowance. Though pension, unemployment allowances, etc. is considered as an individual's income, it is not an earned income. Individual receives this income from government's expenditure. Therefore, it becomes difficult to decide whether or not to include such income in national income. Generally, transfer payments are ignored from national income.

(ii) Income of foreign firms : According to International Monetary Fund's view point, income of a foreign firm should be included in national income of the country, where the firm actually undertakes production work. However, profits earned by foreign firms are credited to their home country. Therefore, it becomes difficult to decide whether or not to include the income of foreign firms in the national income.

(iii) Unpaid services : National income is always measured in money, but there are 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

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love, affection, mercy, sympathy and charity are not included in national income as they are not paid for. By excluding all such services, the national income is underestimated.

(iv) Incomes from illegal activities : Income earned through illegal activities such as gambling, black marketing, theft, smuggling, etc. is not included in national income. But these goods and services do have value and meet the needs of the consumers. Thus, excluding income from illegal activities leads to underestimation of national income.

(v) Treatment of government sector : Government provides a number of public services like defence, public administration, law and order, etc. Measuring the exact market value of such government services is quite difficult, as the real value of these services is not known. Therefore, these services are considered as final consumption and their approximate values are added in the national income.

(vi) Production for self consumption : Goods produced for self consumption such as food grains, vegetables and other farm produce do not enter the market. Therefore, it becomes difficult to find out their exact market value. Therefore, the value of such goods is estimated at the rate of market price that have been marketed. Thus, the approximate values of the goods produced for self consumption are added in the national income.

(vii) Changing price level : 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. Thus, it becomes difficult to estimate the exact national income due to changing price level.

(Marking Scheme : 2 marks for meaning of national income, 6 marks for explaining theoretical difficulties : Total 8 marks)

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(4) (A) Subjective factors determining consumption function :

(i) Motive of precaution : Generally, people save a large part of their income as a precaution against future unforeseen contingencies. High motive of precaution results in decrease in the consumption and increase in savings and vice versa.

(ii) Motive of foresight : Individual has to provide for the future needs. Individual has to provide for the future needs like higher education of children, maintenance of dependants, maintenance during old age, etc. High motive of foresight results in decrease in the consumption and increase in savings and vice versa.

(iii) Motive of calculation : In order to earn income, people invest in shares, debentures or other income earning assets. High motive of calculation results in decrease in the consumption and increase in savings and vice versa.

(iv) Motive of improvement : Generally, people have the desire to enjoy improved standard of living and also higher status in the future. High motive of improvement results in decrease in the consumption and increase in savings and vice versa.

(v) Motive of independence : Every individual likes to attain independence and to gain power. High motive of independence results in decrease in the consumption and increase in savings and vice versa.

(vi) Motive of enterprise : Some people plans to undertake business in future. They provide for capital investment. High motive of enterprise results in decrease in the consumption and increase in savings and vice versa.

(vii) Motive of pride : Individual takes pride in leaving substantial wealth to children, giving donations. High motive of pride results in decrease in the consumption and increase in savings and vice versa.

(viii) Motive of avarice : Some people like to satisfy pure miserliness. High motive of avarice results in decrease in the consumption and increase in savings and vice versa.

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(B) Objective factors determining consumption function :

(i) Changes in wage rate : Wage rate directly affects the consumption function. A change in income distribution also cause a change in expenditure on consumption. If income in terms of wage rate increases, consumption expenditure increases and vice versa. A change in income distribution will cause change in expenditure on consumption.

(ii) Change in disposable income : Disposable income directly affects the consumption expenditure. A rise in disposable income increases the consumption expenditure and vice a versa.

(iii) Change in the rate of interest : Rate of interest inversely affects the consumption expenditure. An increase in the rate of interest may have dampening impact on consumption. On the other hand, a fall in the rate of interest may encourage people to consume more.

(iv) Change in capital value (windfall gains of unexpected gains) : Capital gains directly affects the consumption expenditure. Capital gains are due to sudden change in money value of wealth. During the period of prosperity huge unexpected gains or windfall gains may accrue to the capitalist class and as a result their consumption may increase. Some examples of windfall gains are unexpected rise in profits due to unexpected upswing in business or unexpected rise in the rate of return on investment in some company's shares or debentures, etc.

(v) Fiscal policy : Increased taxes decrease the consumption expenditure and vice versa. Certain types of changes in fiscal policy adversely affects consumption. For example, increase in income tax, capital gain tax, estate duty, etc. decreases consumption. On the other hand, increase in government's spending in various ways (including deficit financing) increases the propensity to consume.

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(vi) Expectations about the future income : If future income is expected to increase, it results in increased consumption and decreased savings and vice versa.

(vii) Changes in depreciation allowances : Depreciation allowance inversely affects consumption expenditure. Changes in fiscal policy of the government affects consumption. Certain type of changes in fiscal policy adversely affect consumption. For example, increase in income tax, capital gain tax, estate duty, etc. On the other hand, increase in government spending in various ways (including deficit financing) would increase propensity to consume.

(viii) Demographic factors : Size of population, family size, etc. also affect consumption.

(Marking Scheme : 4 marks for subjective factors and 4 marks for objective factors determining consumption functions; Total 8 marks. In part 'A' and part 'B' 8 points each with brief explanation and suitable titles are expected.)