**ANSWERS**

**Q1.) Fill in the blanks: -**

1) Partial

2) Savings

3) Product Pricing

4) Income

5) Effective demand

**Q.2) Match the following: -**

1) A – 3

2) B – 4

3) C – 2

4) D – 5

5) E – 1

6) F – 6

**Q3.) True or False: -**

1) Aggregate supply depends on Natural Resource. **Ans – True**

2) Macro – economics is Slicing Method. **Ans – False**

3) Cheque is a Near Money. **Ans – False**

4) Micro – economics talks about total demand & supply. **Ans – False**

5) Govt investment is autonomous in nature. **Ans – True**

**Q4.) Explain the Term :- (Any 2)**

**1)** Aggregate Demand.

**Ans –**  Aggregate demand refers to the total quantity of goods and services demanded in an economy, over a period of time. It includes

1) Consumption expenditure made by the households.

2) Investment spending by business house.

3) Government expenditure on purchase of various goods and services.

4) Net Income from foreign trade i.e. difference between exports and imports.

Symbolically,

ADF = C + I + G + (X – M)

Where, ADF = Aggregate Demand Function

C = Consumption Expenditure

I = Investment Expenditure

G = Government Expenditure

(X – M)= Exports – Imports

**Determinants of / Factors determining Aggregate Demand**:

**1) Consumption/ Expenditure:** Consumption expenditure of the household is a major item in the aggregate demand. It includes the purchases of food and other consumer durables. Consumption expenditure is determined by the disposable income of the consumer. Disposable income is equivalent to the personal income minus tax expenditure. Consumption Expenditure is inversely related to price level.

**2) Investment Expenditure:** It is the second component of aggregate demand. Investment expenditure refers to the addition made to the capital stock, it does not include the repurchase of shares, bonds, debentures, etc. because it is only a transfer of investment expenditure. Investment expenditure consists of new investments made in the construction of buildings, machinery, overhead, facilities etc. investment expenditure depends on the economic policy of the Government.

**3) Government Expenditure:** It consists of the payment made by the Government on purchase of consumer goods and capital goods Government purchases consumer goods for Defence purposes and for public distribution system. Similarly, Government spends money on Investment in Defence and other public utility services.

**4) Net Foreign Trade Balance:** It is the difference between exports and imports in a country. In a closed economy, Net Foreign Trade is not a component of national income, whereas in an open economy there is exchange of goods and services between different countries. When Net Foreign Trade Balance is positive it increases national income and when it is negative it decreases national income. Increase in exports over imports shown increased demand for the domestic product in the foreign market accordingly. Aggregate Demand increases when exports are more.

**2)** Partial equilibrium.

**Ans –** Micro Economic analysis is a partial equilibrium analysis. Partial equilibrium analyses equilibrium analysis. Partial equilibrium analyses equilibrium position of individual consumer individual firm, individual industry etc. Partial equilibrium analysis isolates an individual unit from other forces and proceeds with the assumption. “Other things remaining the same” (Ceteris paribus). This approach neglects the interdependence between economic variables **.**

**3)** Autonomous Consumption expenditure.

**Ans –** J.M. Keynes introduced the concept of consumption function in his book. “The General Theory of Employment, Interest and Money”. Keynes developed the “Psychological Law of Consumption”. This law indicates

❖ When Income increases, the consumption expenditure also increases. But consumption expenditure increases at a lower rate as compared to increase in Income.

Consumption function refers to the functional relationship between consumption and level of income.

C = f (y)

Where, C = Consumption Expenditure.

f = functional relation and

y = level of income

**Classification of Consumption Expenditure:**

**1. Autonomous Consumption Expenditure**: Consumption Expenditure that is not dependent on the level of income is known as Autonomous Consumption Expenditure. For e.g. religious expenditure, government taxes, etc.

**2. Induced Consumption Expenditure**: Consumption expenditure depending on the level of income is known as Induced Consumption Expenditure. It increases as the level of Income increases.

In simple words, consumption function shows that as income increases, consumption expenditure also increases but less than proportionately.

**Schedule:**

|  |  |
| --- | --- |
| **Income** | **Consumption** |
| 100  200  300  400  500 | 150  200  250  300  350 |

**Q5.) Answer the following: - (Any 3)**

**1)** Features of Micro economics.

**Ans – 1. Study of individual units**

Micro Economics is the study of behaviour of small individual economic units, like particular households, individual firms, individual prices etc.

**2. Price Theory**

Micro Economics is called price theory because it is primarily concerned with determination of prices of goods and factors of production.

**3. Slicing method**

Micro Economics splits the economy into small individual unit and then studies each unit separately in detail. Thus it is said that Micro Economics uses Slicing method.

**4. Partial equilibrium**

Micro Economic analysis is a partial equilibrium analysis. Partial equilibrium analyses equilibrium analysis. Partial equilibrium analyses equilibrium position of individual consumer individual firm, individual industry etc. Partial equilibrium analysis isolates an individual unit from other forces and proceeds with the assumption. “Other things remaining the same” (Ceteris paribus). This approach neglects the interdependence between economic variables.

**5. Microscopic approach**

Micro Economics is the microscopic study of the economy. The individuals or households as consumers, and individuals or firms as producers play their part in the working of whole economic organism”.

In Micro Economic theory, we discuss how the various cells of economic organism, such as thousands of consumers, thousands of producers or firms, thousands of workers and resource suppliers in the economy, do their economic activities and reach their equilibrium state. In other words in Micro Economics, we attempt only a microscopic study of the national economy in its totality.

**6. Analysis of resource allocation and economic efficiency**

Micro Economics deals with the allocation of resources among competing groups, Micro Economics explains how relative prices of commodities and factors of production determine

(a) What goods will be produced & in what quantities? (b) How they will be distributed?

It means Micro Economics also deals with the problem of income distribution.

**7. Based on certain assumptions**

Micro Economics assume laissez fair policy, pure capitalism, full employment, perfect competition etc. which do not exist in reality. Also most of the theories are based on the ‘ceteris paribus’ assumption i.e. other things being constant. The assumption makes the analysis simple, but at the same time, it neglects the interdependence between economic variables. The assumption makes the theories static and neglects changing economic world.

**8. Limited Scope**

Micro Economics studies individual economic units & not the whole economy. It does not deal with the nation-wide problems like unemployment, inflation, deflation, poverty, balance of payment situation, economic growth etc. So its scope is limited.

**2)** Primary function of Money.

**Ans** – **I. PRIMARY FUNCTIONS:** These are the basic functions of money which help in smooth functioning of any modern and monetary economy.

**1) Medium of Exchange:** The most important function of Money is to make buying and selling of goods and services possible in the market. He value of all goods and services and expressed in terms of money. Money is generally accepted as a means of payment. Any commodity as well as service can be exchanged for money. In Money economy, everything can be purchased and sold for money. As a medium of exchange, money removes the problem of double coincidence of wants faced in barter system. Mr. A can sell his goods to Mr. B for money and can use this money to buy goods he wants, from others who have them.

**2) Measure of Value:** Under Barter System, It was difficult to find out the value of different goods, there was a problem of common measure of value. Money has solved this problem. Money now acts as measure of value. Value of any commodity can be expressed in terms of money. Since the value of all goods and services is measured in a standard unit of money, it becomes easy to find out the value of various commodities purchased by the people. If a pen is costing Rs.10 and a Note books is costing Rs. 20, then we can say that one note book is worth two pens.

**3)** Qualities of Money.

**Ans** –

**4)** Explain subjective factor affecting consumption

**Ans** – **a) Subjective Factors:** Subjective factors are internal to the economic system. They are fairly stable in the Short-run. They include psychological characteristics of human nature, social practices, social institutions and social arrangements. These factors determine the form and slope of consumption function.

**1. Precaution:** The precautionary motive to build up reserves against unforeseen contingencies like accidents etc. reduces consumption and increases savings.

**2. Foresight:** People provide for expected needs in future by way of interest, appreciation of stock, people reduce their consumption at present.

**3. Calculation:** To enjoy a higher consumption in future by way of interest, appreciation of stock, people reduce their consumption at present.

**4. Improvement:** The desire to enjoy a better standard of living and social status in future, people spend less and save more.

**5. Pride:** The desire to leave fortune for their heirs affects Consumption Function.

**Q6.) Long answers : - ( Any 1)**

**1)** Explain with Diagram Effective demand.

**Ans** –

**2)** Limitation of Barter system

**Ans** – In olden days, people were self-sufficient. They had very few basic need of food, clothing and shelter. Hence, the economic activities were limited to production and consumption. As civilization progressed, human wants multiplied. It became difficult for a person to satisfy all his increasing wants by producing all the desired things himself. As a result, People exchanged goods and services produced by them with goods and services produced by others. This system was called Barter System and the economy was called Barter Economy.

**Limitations of Barter Systems:** As human wants were going on increasing due to development, barter system of exchange became outdated. It had various limitations, they were as follows.

**1. Lack of Double coincidence of wants:** Under Barter System, Peoples wants may not always match. For Example: Raghu a farmer is producing Sugarcane and he required cloth. But Ramu a weaver ay not require Sugarcane. So, there can be no exchange. Raghu will have to go without cloth. It is always not necessary that two people’s wants may coincide or match.

**2. Lack of Common measure of value:** Under Barter system, there was no common measure that could be used for measuring the value of all products. It was very difficult to determine the value of different products and then to exchange them for each other. Due absence of measure of value there were frequent misunderstandings, quarrels and confusion in the market. The trade was limited due to lack of common measure in the society.

**3. Difficulty in Storage:** There was also the problem of storage of wealth. As the barter trade consisted entirely of commodities, storing of wealth under barter system would mean storing of commodities themselves. Most of the products were perishable in nature and so they cannot be stored for a longer period of time.

**4. Difficulty in exchange of Indivisible Commodities:** Under Barter System every commodity was treated as money and was exchanged for another commodity. Sometimes it was not possible to divide certain commodity Into small pieces or parts for the purpose of exchange. For example: Rehan wants a chocolate, he insists his father Rahim to get it. Rahim has a cow, if he directly exchanges the cow for a single of chocolate he is at huge loss. The value of cow is much greater than that of a chocolate. At the same time, it is not possible to divide the cow into small number of pieces. Under such situations exchange may not take place.

**5. Difficulty of Deferred Payment:** Sometimes contracts involving future payments have to be made in an exchange economy. People have to enter into agreements regarding salaries, wages, rents, interests etc for over a period of time. But in barter system, these future payments are to be stated in terms of specific goods. There was a lack of any satisfactory unit in terms of which contracts requiring future payments can be made.

Conclusion: Barter system was inconvenient and time consuming system of trade.

**3)** Explain keeper physiological law of consumption [With table & diagram].