

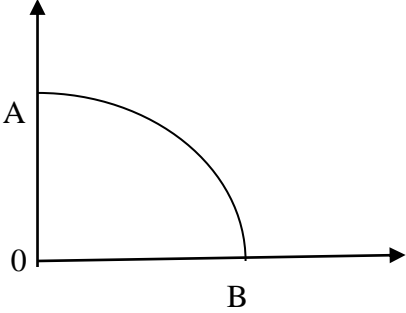
COMMON PRE-BOARD EXAMINATION 2017-2018

ECONOMICS ANSWER KEY

CLASS XII

Maximum Marks: 80

SECTION- A																				
1	c. Resources increase or technology is upgraded	1																		
2	Relation between variable input and output keeping all other inputs constant.	1																		
3	140	1																		
4	d) None of the above	1																		
5	<p>MOC/MRT can be defined as the rate of sacrifice of one good per unit increase in the production of other good.</p> $MRT = \frac{\text{Unit of one good sacrificed}}{\text{more units of the other good produced.}}$ $= \frac{\text{Change in Good Y}}{\text{Change in good X}}$ <table border="1" style="margin-left: auto; margin-right: auto;"> <thead> <tr> <th>Good 1</th> <th>Good 2</th> <th>MRT</th> </tr> </thead> <tbody> <tr> <td>0</td> <td>10</td> <td>-</td> </tr> <tr> <td>1</td> <td>9</td> <td>1</td> </tr> <tr> <td>2</td> <td>7</td> <td>2</td> </tr> <tr> <td>3</td> <td>4</td> <td>3</td> </tr> <tr> <td>4</td> <td>0</td> <td>4</td> </tr> </tbody> </table> <p>Diagram with explanation.</p> <p style="text-align: center;">OR</p> <p>The economy has to decide what goods and services are to be produced. For instance which of the consumer goods like cloth, sugar etc are to be produced and which of the capital goods like machines, tractors etc are to be produced.</p> <p>When an economy has taken a decision as to what goods or services are to be produced, then it has to decide about its quantity.</p>	Good 1	Good 2	MRT	0	10	-	1	9	1	2	7	2	3	4	3	4	0	4	3
Good 1	Good 2	MRT																		
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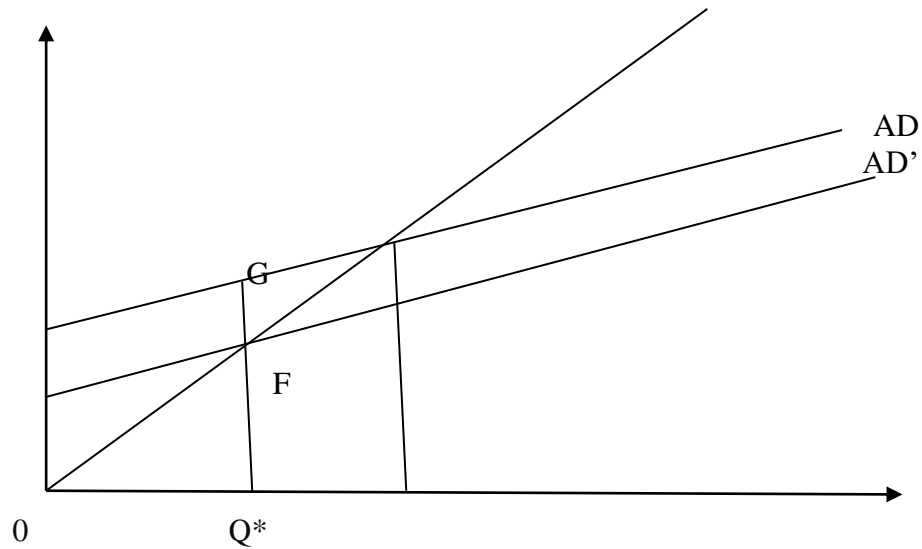
	 <p data-bbox="277 562 1347 707">If the entire resources of the economy are diverted to produce good Y, then it will produce OA level of good Y or if the entire resources are diverted to produce good X, then it will produce only good X (ie. OB level). Economy can also select any other point on PPC.</p> <p data-bbox="277 745 884 781">Explanation with Production possibility Curve.</p>	
6	<p data-bbox="325 822 1023 927">i) Demand decreases, demand curve shift to the left ii) Demand increases, demand curve shift the right iii) Demand decreases, demand curve shift to the left</p> <p data-bbox="400 967 603 1003">(Use diagrams)</p>	1 1 1
7	$E_d = \frac{\Delta Q}{\Delta P} \times \frac{P}{Q}$ $-1 = \frac{10}{-2} \times \frac{10}{Q}$ $= 2Q = 100$ $Q = 100/2 = 50$	4
8	<p data-bbox="277 1341 1062 1518">Fixing of price above equilibrium price. To protect the interest of producers, labourers etc Excess supply Unless government prepares to buy, excess supply- price fall (Implications with a diagram.)</p> <p data-bbox="794 1597 842 1632" style="text-align: center;">OR</p> <p data-bbox="277 1637 1315 1850">Chain effects of 'decrease' in demand. Diagram- decrease in demand, while supply remains unchanged leads to excess supply. Decrease in equilibrium price, contraction of supply takes place and equilibrium quantity also falls. Explanation with diagram</p>	4
9	<p data-bbox="277 1856 1315 1924">Decrease in supply: Decrease in supply means fall in supply for a product due to changes in factors other than price.</p> <p data-bbox="277 1928 392 1964">Diagram</p> <p data-bbox="277 1968 443 2004">Reasons are:</p>	2

	<ul style="list-style-type: none"> • increase in unit tax • increase in input price • Deterioration in technology • Increase in price of other products <p>Contraction of supply: A fall in supply of a product due to decrease in its price alone is called contraction of supply.</p> <p>Diagrams with explanations</p>	2
10	<p>a) Consumer will be in equilibrium by indifference curve and budget line analysis at that level at which one of the indifference curve is just tangent to the budget line.</p> <p>At this point, Slope of the indifference curve = Slope of the budget line</p> <p style="text-align: center;">MRS = Price Ratio</p> $\text{MRS} = \frac{\text{Change in } X_2}{\text{Change in } X_1}$ $\text{MRS} = -\frac{P_1}{P_2}$ <p>(Diagram)</p> <p>In the diagram, consumer is in equilibrium at point E because at this point MRS = Price ratio and indifference curve is tangent to the budget line.</p> <p>Initially when consumer starts to substitute good 2 for good 1, $\text{MRS} > \text{Price ratio}$, hence consumer gains. That is, the utility received from an extra unit of good 1 is more than the utility lost from good 2.</p> <p>At the point of tangency $\text{MRS} = \text{Price ratio}$, ie at point E.</p> <p>If consumer further substitute good 2 for good 1, price ratio will be greater than MRS. That is why utility received from an extra unit of good 1 is less than the utility lost from good 2.</p> <p>Consumer will not select any bundle on IC1 like C and D because IC1 consists of the bundles less preferred than the bundles on IC2.</p> <p>Consumer cannot select IC3 because those bundles are budget constraints.</p> <p style="text-align: center;">OR</p> <p>a). MU of good X = Price of X Table and diagram</p> <p>b). At equilibrium, If $\text{MU}_x/\text{P}_x = \text{MU}_y/\text{P}_y$, Given, $\text{MU}_x/\text{P}_x = \text{MU}_y/\text{P}_y$, $10/8 \neq 8/10$ 1.25 not equal to 0.8 So consumer is not in equilibrium.</p> <p>$\text{MU}_x/\text{P}_x > \text{MU}_y/\text{P}_y$, then it means that satisfaction of consumer, derived from spending a rupee on Good X is greater than the satisfaction derived from spending a rupee on Good Y.</p> <p>He will reallocate his income by substituting Good X for Good Y.</p> <p>As the consumption of Good X increases the marginal utility derived from it goes on diminishing and reverse proposition occurs for Good Y, this process will continue till MU_x/P_x becomes equal to MU_y/P_y.</p>	6

15	<p>When the commercial banks are in need of funds for a short period, they can borrow from the Central Bank. The rate of interest charged by the Central Bank on such lending is called Repo Rate.</p>	1																									
16	<p>a) Revenue Receipts Tax b) Capital Receipts Borrowing (or any other relevant examples)</p>	<p>1/2 1/2</p>																									
17	<table border="1" data-bbox="280 600 1094 857"> <thead> <tr> <th>Income (Y)</th> <th>MPC</th> <th>Savings (S)</th> <th>Consumption</th> <th>APC</th> </tr> </thead> <tbody> <tr> <td>0</td> <td></td> <td>(-)30</td> <td>30</td> <td>-</td> </tr> <tr> <td>100</td> <td>0.75</td> <td>(-)5</td> <td>105</td> <td>1.05</td> </tr> <tr> <td>200</td> <td>0.75</td> <td>20</td> <td>180</td> <td>0.9</td> </tr> <tr> <td>300</td> <td>0.75</td> <td>45</td> <td>255</td> <td>0.85</td> </tr> </tbody> </table>	Income (Y)	MPC	Savings (S)	Consumption	APC	0		(-)30	30	-	100	0.75	(-)5	105	1.05	200	0.75	20	180	0.9	300	0.75	45	255	0.85	3
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18	<div data-bbox="534 936 1364 1422" data-label="Figure"> </div> <p>In the diagram on the Y axis we measure planned saving and investment. Investment curve is parallel to X axis because we assume investment is autonomous and independent of its determinants. Saving curve begins from the negative segment of the Y axis because at low levels of income savings can be negative. As income increases saving also increases. Therefore it is positively sloped.</p> <p>The economy will be in equilibrium by S and I approach at that level of output at which planned saving = planned investment. In the above diagram, the economy is in equilibrium at OM level of output.</p> <p>If the planned savings exceeds planned investments (beyond OM level of output) accumulation of inventories takes place. Firms would respond to this by reducing the employment hence output. This process will continue till the equilibrium level of output where planned savings = planned investments.</p>	3																									

OR

If AD for a level of output is more than the full employment level of output, it is called excess demand.



The inflationary gap is the amount by which the actual aggregate demand exceeds the level of aggregate demand required to establish the full employment equilibrium.

In the diagram, economy will be in full employment equilibrium level of output at point F on the AD (C+I) curve and the economy will produce the full employment level of output OQ^* .

FG is the inflationary gap.

The inflationary gap is so called because it sets in motion forces that will cause inflation or arise in the price level. At point G, the aggregate demand curve (C+I) lies above the 45 degree line. As a result, the aggregate demand Q^*G is greater than the level of output OQ^* . The effect of this will be to create demand pull inflation (an aggregate demand induced rise in the price level).

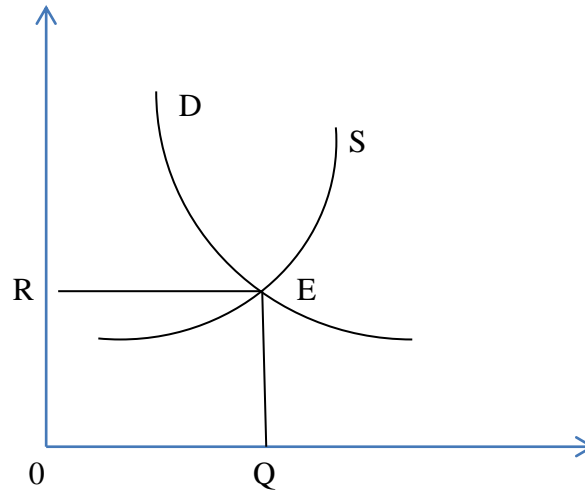
Fiscal Policy measures: Fiscal policy measures to increase aggregate demand may be done by either increasing the level of government expenditure or by reducing the amount of taxes. If the government expenditure is increased by an amount equal to the deflationary gap, it will restore the economy to the full employment equilibrium.

19

The budget is an annual statement of the estimated receipts and expenditure of the government over the fiscal year.

1

	<p>a) Allocation function: In an economy there are number of public goods required for normal functioning of government and the welfare of the people as a whole.</p> <p>Such goods cannot be provided through market mechanism. Therefore public goods must be provided by the government through budgetary allocation. This is called the allocation function.</p> <p>b) Distribution function: Through its tax and expenditure policy, the government attempts to bring about a distribution of income that is considered fair by the society. The government affects the personal disposable income of households by making transfer payments and collecting taxes. In this way government can alter the income distribution. This is called distribution function.</p> <p>c) Stabilisation function: The economy tends to be subject to substantial fluctuations and may suffer from prolonged period of deflation or inflation. During excess demand government expenditure must be reduced and tax rates must be increased to control inflation and stabilize the economy. Similarly during deficient demand government expenditure must be increased and tax rate must be reduced to control deflation and stabilize the economy. This is called stabilization function.</p> <p style="text-align: center;">OR</p> <p>It implies that government is dissaving and using up the savings of the other sectors of the economy to finance a part of government consumption expenditure.</p> <p>This means that the government will have to borrow not only to finance its investment but also for its consumption requirements.</p> <p>This will increase the borrowing liability of the government which in turn force the government to cut productive capital expenditure or welfare expenditure. Increase in borrowing also increases interest payment liabilities. This will increase revenue deficit and create inflation in the economy.</p>	3 4																
20	<p>a). Distribution of GDP</p> <p>Externalities Non-monetary exchanges (Any two points with explanation)</p> <p>b).</p> <table border="1" data-bbox="277 1675 1045 1868"> <thead> <tr> <th>Year</th> <th>Nominal GDP</th> <th>Real GDP</th> <th>GDP deflator</th> </tr> </thead> <tbody> <tr> <td>2014-15</td> <td>6.5</td> <td>6.5</td> <td><u>100</u></td> </tr> <tr> <td>2015-16</td> <td><u>8.4</u></td> <td>6</td> <td>140</td> </tr> <tr> <td>2016-17</td> <td>9</td> <td><u>7.2</u></td> <td>125</td> </tr> </tbody> </table>	Year	Nominal GDP	Real GDP	GDP deflator	2014-15	6.5	6.5	<u>100</u>	2015-16	<u>8.4</u>	6	140	2016-17	9	<u>7.2</u>	125	2 2
Year	Nominal GDP	Real GDP	GDP deflator															
2014-15	6.5	6.5	<u>100</u>															
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Demand curve for foreign exchange is negatively sloped because there is an inverse relationship between exchange rate and demand for foreign exchange, ie at high rate of exchange less foreign exchange will be demanded and vice-versa.

Supply curve for foreign exchange is positively sloped because there is a direct relation between exchange rate and supply of foreign exchange, ie at high rate of exchange more foreign exchange will be supplied and vice-versa.

2

In the above diagram, exchange rate is determined at the point E, where demand and supply of foreign exchange are equal. Therefore OR is the equilibrium exchange rate.

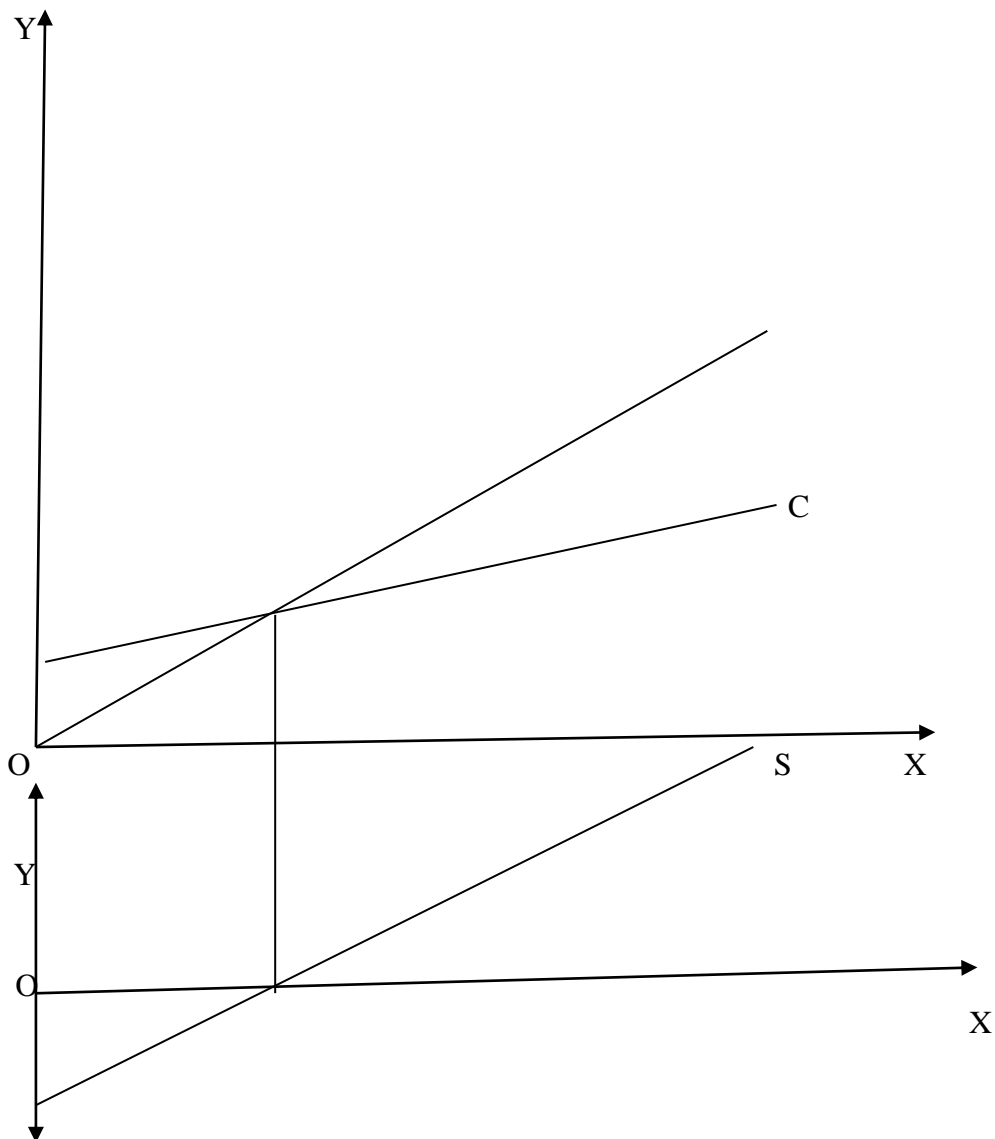
b). Foreign buyers will be able to buy more from one unit of currency as a result of currency depreciation. This makes export cheaper for the foreign buyers. As a result exports are likely to increase (To be explained)

24

Let us suppose $C=100+0.8 Y$ and MPC is constant.

6

Income (Y)	Consumption (C)	Saving (S)	ΔY	ΔC	ΔS	MPC ($\Delta S/\Delta Y$)	MPS ($\Delta S/\Delta Y$)
0	100	-100	-	-	-	-	-
100	180	-80	100	80	20	0.8	0.2
200	260	-60	100	80	20	0.8	0.2
300	340	-40	100	80	20	0.8	0.2
400	420	-20	100	80	20	0.8	0.2
500	500	0	10	80	20	0.8	0.2
600	580	20	100	80	20	0.8	0.2
700	660	40	100	80	20	0.8	0.2
800	740	60	100	80	20	0.8	0.2
900	820	80	100	80	20	0.8	0.2
1000	900	100	100	80	20	0.8	0.2



In the diagram, part A shows consumption function curve. 45° line drawn on the assumption that at any point on it $\text{Income} = \text{consumption}$. At low level of income consumption function curves lies above the 45° line, because consumption exceeds income.

When $\text{Income} = \text{Consumption}$, consumption function curve intersect 45° line, it is called break even point.

Any level of income more than it, consumption is less than income. Therefore consumption function curve lies below 45° line

Part B shows saving function curve. When consumption exceeds income dissaving takes place. Therefore saving function curve lies below the X axis. When $Y = C$, saving function curve intersect X axis. When income is more than consumption saving takes place. Therefore saving function curve lies above X axis.

In part A, saving or dissaving is measured by taking the vertical distance between 45° line and consumption function curve.

In part B, saving or dissaving is measured by taking the vertical distance between X axis and saving function curve.