Sample Paper-03 (2016-17)
Economics
Class – XII

Time allowed: 3 hours **Maximum Marks: 100**

General Instructions:

(i) All questions in both sections are compulsory. However, there is internal choice in some questions.
(ii) Marks for questions are indicated against each question.
(iii) Question No.**1-5** and **16-20** are very short answer questions carrying **1 mark** each. They are required to be answered in one sentence.
(iv) Question No.**6-8** and **21-23** are short answer questions carrying **3 marks** each. Answers to them should not normally exceed 60 words each.
(v) Question No.**9-11** and **24-26** are also short answer questions carrying **4 marks** each. Answers to them should not normally exceed 70 words each.
(vi) Question No.**12-15** and **27-30** are long answer questions carrying **6 marks** each. Answers to them should not normally exceed 100 words each.
(vii) Answers should be brief and to the point and the above word limit be adhered to as far as possible.

Section A

1. Budget line is:
   (a) Parallel to X – axis
   (b) Parallel to Y-axis
   (c) Downward sloping line
   (d) None of the above.
2. If price of goods-X rises and this leads to decrease in demand for goods-Y, how are the two goods related?
3. Total utility is maximum when MU is:
   (a) positive
   (b) Zero
   (c) Negative
   (d) None of the above.
4. How is the equilibrium price of a commodity affected when demand increases more than the supply?
5. When MU is negative, TU:
   (a) Remains constant
   (b) Increases
   (c) Falls
   (d) None of the above.
6. Define and draw production possibility curve. What does the movement along this curve show?
7. Total Fixed costs of a firm are Rs 100. Its average variable cost at different levels of output is given. Calculate total cost and marginal cost.

Output (units)	1	2	3	4
TVC (Rs.)	20	38	60	86

8. Explain change in quantity supplied.
9. What is meant by consumer equilibrium? State its condition in case of a single commodity.
10. Which cost, fixed or variable, determines marginal cost? Give reasons.
11. If the local pizzeria raises the price of medium pizza from Rs 60 to Rs 100 and quantity demanded falls from 700 to 100 pizzas a night, what is the price elasticity of demand for pizzas?
12. Explain the three features of a monopoly market.
13. How does a cost saving technological progress affect market price and the quantity exchanged of a commodity? Use diagram.
14. At the market price of Rs 40, a firm supplies 400 units of output. When its price falls by 10 percent, the quantity supplied falls by 36 units. Calculate its elasticity of supply. Is its ssupply elastic.
15. Define the price elasticity of demand. Discuss the factors affecting price elasticity of demand.

Section B

16. Which of the following is a micro-economic study?
    (a) Level of employment
    (b) Aggregate demand
    (c) Study of a cotton textile industry
    (d) All of the above.
17. Which of the following is equal to National Income?
    (a) GDP_{FC}
    (b) NNP_{FC}
    (c) NNP_{MP}
    (d) GNP
18. If inflation is higher in country A than in country B and the exchange rate between the two countries is fixed, what is likely to happen to trade balance of Country A?
    (a) Trade balance of country A will be favourable
    (b) trade balance of country A will be Unfavourable
    (c) Trade balance of country A will be unaffected
    (d) None of the above.
19. Which of the following is a capital receipt?
    (a) Loan from the World Bank
    (b) Recovery of loans
    (c) Both are capital receipts
    (d) Only (a) is capital receipts
20. Why can the value of marginal propensity to consume be not greater than one?
21. When will there be a situation of deficit demand in an economy? State two measures to correct it.
22. Explain why Public goods must be provided by the government?
23. From the following data about firm X, calculate gross value added at factor cost by it:

	(Rs. in thousands)
Sales	500
Opening stock	30
Closing stock	20
Purchase of intermediate products	300
Purchase of machinery	150
Subsidy	40

24. State various general utility services provided by the commercial banks.
25. If you were the finance minister of India, which taxes would you prefer: direct or indirect taxes and why?
26. Define (i) Currency Deposit Ratio (Cdr) (ii) Reserve Deposit Ratio (rdr) (iii) High Powered Money.
27. Explain the steps involved in estimating national income by Income method. Also, explain some of the precautions taken in the income method.
28. What is foreign exchange rate? Distinguish between fixed and flexible exchange rate. State two merits each of fixed and flexible exchange rate.
29. Compare Excess Demand and Deficient Demand under following heads:
    (i) Meaning (ii) Equilibrium level
    (iii) Reason (iv) Impact on output and employment
    (v) Impact on price.
30. Given MPC = 0.8 and investment at all levels of income is Rs 40 crores, complete the following table:

Income	consumption	Savings	Investment	AD	AS = Y
0	60				
100					
200					
300					
400					
500					
600					

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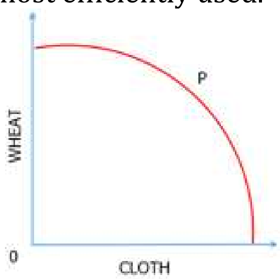
ANSWERS

1. (c) downward sloping line.
2. X and Y are complementary goods.
3. (b) Zero.
4. When demand increases more than the supply, equilibrium, price of the commodity must rise other things remaining constant.

5. (c) Falls.

6. PPC curve graphically represents the various combination of two goods which can be produced with a given amount of resources assuming that resources are fully employed and most efficiently used.

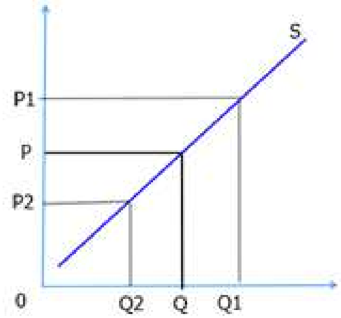


In the figure, a production possibility curve PP between wheat and cloth has been drawn. It slopes downward from left to right and is generally concave to the origin.
movement along PPC: The movement from one point on PPC to another signifies the process of the resource allocation. In other words it means shifting resources from production of one combination of two goods to the other.

7.

Output	1	2	3	4
TVC	20	38	60	86
TFC	30	30	30	30
TC	50	68	90	116
AC	50	34	30	29
MC	-	18	22	26

8. **Movement along the supply curve or change in quantity supplied.** When the supply of a good rises due to rise in the price of a good alone, it is termed as expansion of supply. When supply of a good falls due to fall in its price, it is called contraction of supply. Graphically it means movement along the supply curve.



In the given diagram, at price OP, the supply is OQ. When the price rises to OP_1, the supply rises to OQ_1. In this case, the producer moves from A to B upwards but remains on the same supply curve. When price falls to OP_2, supply falls to OQ_2. The producer moves from A to C but remains on the same supply curve.

9. A consumer is said to be in equilibrium if he is spending his given income on various goods ans=d services in such a way that maximizes his satisfaction.
   Condition for consumer equilibrium in case of a single commodity: it is attained when marginal utility of the commodity measured in terms of money is equal to its price. That is, $MU_X = P_X$.

10. Variable cost determines marginal cost. The reason is that the fixed cost do not change with change in level of output. It is the variable cost only which changes with the level of output. MC by defining is the addition made to total cost due to an additional unit of commodity produced. And this addition in TC is due to variable cost only as fixed cost remains constant. Therefore, MC depends on variable cost.

11.

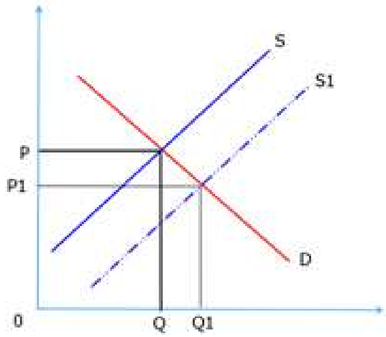
Price (Rs)	Quantity (units)
60	700
100	100

By percentage method, e_D = (change in Q/change in p)*(p/q) =(-600 / 40) * (60 / 700) = -0.8.

12. **<u>Features of monopoly market</u>:**
   (i) **<u>A single seller:</u>** The first main feature of a monopoly is that there is only one seller (or firm) of a commodity in the market with the reason that there is no distinction between industry and firm. The firm itself is the industry and has full control over the supply of a commodity. The monopolists may be an individual, affirm or a group of firms or a government corporation or even a government itself. Against a single seller, there can be any number of buyers for the commodity under monopoly.
   (ii) **<u>No close substitutes of the product</u>:** The second feature of a monopoly is that the product sold by the monopolists has no close substitutes. The goods sold by the monopolists does not face any competition. Though substitutes of the product are available, yet they are not close substitutes. The consumer will have to buy the commodity from the monopolists or go without it altogether.
   (iii) **<u>No freedom of entry of new firms</u>:** The third feature of monopoly is that there is no freedom for the new firms to enter the industry. It may be done to government order. For example, producing of some public good like electricity, water supply, etc. is the

monopoly of the government. Another reason behind the denial of freedom is patent laws. Those who develop new products are granted patent rights. An author may have a copyright of his book; a firm may patent a particular design etc., which results in monopoly.

13. A cost saving technological progress reduces unit cost of production of a commodity. This will cause an increase in supply of a commodity and leads to a rightward shift of a supply curve as shown in the given diagram. The demand curve of a commodity remaining the same, this will cause the market price of a commodity to fall and the quantity to rise.



It is clear from the diagram that as a result of increase in supply, the supply curve shifts rightwards. As a result the price falls from OP to OP_1 and the quantity rises from OQ to OQ_1.

14. Given:

Price (RS)	Supply (units)
40	400
40 – 4 = 36	400 – 36 = 364

e_s = (change in q_s/ change in p) * p/q_s
= (-36 / 4) * (40/400) = 9/10 = 0.9 < 1
As e_s < 1, the supply is inelastic.

15. Price elasticity of demand refers to the degree of responsiveness of quantity demanded of a good to a change in its price. Following are the factors affecting it:
   (i) **Availability of close substitutes for the commodity:** A commodity will have elastic demand if there are good substitutes available, eg. , Pepsi, Coco Cola, Frooti. A commodity having no substitutes, eg., salt will have inelastic demand.
   (ii) **Nature of good:** Generally, the demand of necessaries is inelastic and that for luxuries elastic. This is so because certain goods which are essential to life will be demanded at any price, whereas goods meant of luxuries can be dispersed easily if they appear to be costly.
   (iii) **Uses of the commodity:** If a commodity has only few uses such as butter, its demand is likely to be inelastic. If on the other hand, a commodity has many uses, its demand is likely to be elastic such as milk, electricity.
   (iv) **Share in total expenditure on the commodity:** The demand for such commodities where a part of income spent is generally inelastic such as commodities like needle, match box, etc. on the other hand, the demand for such commodities where a significant part of income spent, is very elastic, such as demand for woollen suit, luxuries, etc.

(v) **<u>Tastes and preferences/habits:</u>** If the consumers are habitual of some commodities, the demand for such commodities will be usually inelastic, because they will use them even their prices go up. A smoker generally does not smoke less when the prices of cigarette goes up.

(vi) **<u>Postponement of use:</u>** Usually the demand for such commodities whose use can be postponed for some time is elastic. For example, the demand for DVD player is elastic because its use can be postponed for some time if its price goes up, but the demand of wheat and rice is inelastic, because their use cannot be postponed when their prices go up.

(vii) **<u>Level of income:</u>** At a higher level of income, demand is less elastic and at lower levels of income, demand is more elastic.

Section B

16. (c) Study of cotton textile industry
17. (b) NNP_{FC}
18. (b) Trade balance of country A will be Unfavourable.
19. (c) Both are capital receipts.
20. It is because change in consumption cannot be greater than change in income.

21. Deficit demand exists when aggregate demand for a level of output is less than full employment. In other words, when aggregate demand falls short of aggregate supply at full employment level of output, then the situation is called deficient demand.
    Following fiscal measures can be used to correct deficient demand:
    (a) **Decrease in taxes**: a reduction in the amount of taxes increases the purchasing power of the people. It will increase the disposable income which will further increase 'C' component of aggregate demand and thus the problem of aggregate demand can be solved.
    (b) **Increase in government expenditure**: The government should increase its expenditure on public works program, public health, defence and education etc and should make large investments. This will increase the 'G' component of aggregate demand and thus the problem of deficient demand can be solved.
22. Public goods such as parks, roads, water, bridges, national defence, etc. are the goods which people need for their day-to-day living but they cannot produce on their own. So, it is the duty of the government, being the representative of the public, to provide public goods. Such goods can only be produced by the government.
23. Gross value added at Factor Cost = sales + change in stock (closing stock – opening stock) – purchase of intermediate products + subsidy
    = 500 + (20 – 30) – 300 + 40
    = 500 – 10 – 300 + 40 = Rs. 230 thousands.
24. The various utility services provided by commercial banks are as follows:-
    (i) **<u>Locker facility</u>:** Banks provide locker facility to their customers. The customers can keep their valuable goods and important documents in these lockers for safe custody. The bank charges a very nominal amount for the same.
    (ii) **<u>Travellers cheques</u>:** Banks issues travellers cheque to help their customers to travel without the fear of theft or loss of money. With this facility, the customers need not take the risk of carrying cash with them during their travels.
    (iii) **<u>Gift cheques</u>**: Some banks issue cheques of various denominations (say Rs 11, 21, 31, 51, 101, etc) to be used on auspicious occasions.

(iv) **<u>Underwriting securities</u>:** Banks underwrite the securities issued by the government, public or private bodies. Because of its full faith in banks, the public will not hesitate in buying securities carrying the signature of a bank.

25. Both direct and indirect taxes are not substitutes of each other. They are complementary to each other. Objectives of taxation are common to both. These are (i) to raise resources of the government (ii) to raise the rate of investment in the country (iii) to raise the incremental saving ratio. Similarly, they differ from each other in following ways:
(a) Indirect taxes reach all the sections of the society while direct taxes cannot reach all the sections;
(b) Direct taxes can be highly progressive; indirect taxes are generally proportional. Therefore, it is necessary to strike the right balance between direct and indirect taxes as a source of tax revenue.

26. (i) **<u>Currency deposit ratio</u>** is the ratio of money held by the public in currency to their holdings in bank deposits. It shows people's preference for liquidity.
Cdr = CU/DD
If a person gets Re 1, then
Amount he will put in bank account = **1/1+Cdr**
Amount he will keep in cash = **Cdr/ 1+Cdr**
Cdr increases during festive seasons as people convert deposits into cash balance for meeting extra expenditure during such periods.
(ii) **<u>Reserve deposit ratio</u>** is the proportion of total deposits that commercial banks keep as reserves. Banks hold a part of money which people keep in their bank deposits as reserve money and loan out the rest to various investment projects. Reserve money consists of:
(a) vault cash in banks.
(b) deposits of commercial banks with RBI.
(iii) **<u>High powered money</u>** (or monetary base) refers to the total liability of the monetary authority of the country, RBI. It consists of currency (notes and coins in circulation with the public and vault cash of commercial banks) and deposits held by the Government of India and commercial banks with RBI. These items are considered to be liability of RBI as these are claims which the general public, governments or banks have on RBI.

27. Under Income method, National Income is measured at the stages when factor incomes are paid out by the production units to the owners of the factors of production. The main steps involved in this method are as follows:
(i) First of all production units which uses factor services are identified.
(ii) Estimate the following factor incomes: (a) compensation of employees (b) rent (c) interest (d) profits (e) mixed incomes.
The sum total of the above factor incomes gives us domestic factor income (i.e. NDP_{FC})
(iii) Add net factor income from abroad to NDP_{FC} to arrive at national income (NNP_{FC})
NI OR NNP_{FC} = NDP_{FC} + Net factor income from abroad.
Precautions to be taken while measuring national income by income method are:
(a) Only factor incomes are included, but transfers are not included. Gifts, donations, charities, old age are not factor incomes but transfer income. These should not be included in the estimation of national income by income method.
(b) The imputed rent of owners, self-occupied houses and value of production for self consumption are included.
(c) Wealth tax, taxes on capital gains are not included in national income.

(d) Direct taxes like income tax should be included.

28. Foreign exchange rate refers to the rate at which one country's currency is exchanged with the currency of other country. There are mainly two types of exchange rate:

(a) **<u>Fixed exchange rate</u>**: is the rate which is officially fixed in terms of gold or any other currency by the government. Such a rate does not vary with changes in demand and supply of foreign currency. Only the government has the power to change it.

<u>Merits</u>:

(i) It ensures the stability in the exchange rate.

(ii) Stable exchange rate prevents capital outflow.

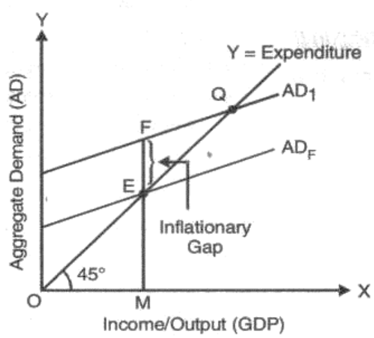
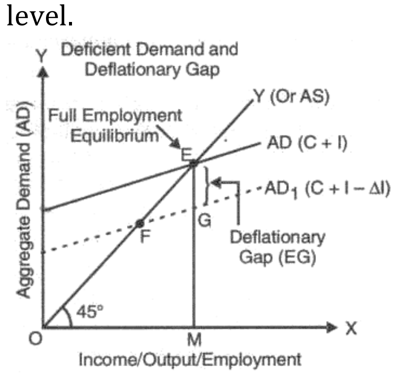
(b) **<u>Flexible exchange rate</u>:** is that rate which is determined by the forces of demand and supply of foreign exchange. There is an official intervention. It is free to fluctuate according to changes in demand and supply of foreign currency.

<u>Merits:</u>

(i) It eliminates the problem of over valuation or undervaluation of currencies.

(ii) It frees the government from the problem of balance of payment.

29.

Basis	Excess Demand	Deficient Demand
Meaning	It refers to the situation when AD is more than corresponding to full employment level in the economy.	It refers to the situation when AD is less than AS corresponding to full employment level in the economy.
Equilibrium level	It indicates over full employment equilibrium.	It indicates underemployment equilibrium.
Reason	It occurs due to excess of anticipated expenditure, i.e., due to rise in consumption expenditure, investment expenditure, etc.	It occurs due to shortage of anticipated expenditure, i.e., due to fall in consumption expenditure, investment expenditure, etc.
Impact on output and employment	It does not affect the output and employment as economy is already operating at full employment level.	It leads to fall in output and employment due to shortage of aggregate demand.
Impact on price	It lead to inflation, i.e., it result in rise in general price level.  	It leads to deflation, i.e., it results in fall in general price level. 

30. C = 60 + 0.8 Y, I = 40

Income	consumption	Savings	Investment	AD	AS = Y
0	60	-60	40	100	0
100	140	-40	40	180	100
200	220	-20	40	260	200
300	300	0	40	340	300
400	380	20	40	420	400
500	460	40	40	500	500
600	540	60	40	580	600