**Sample Paper-04 (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. How is the market demand curve derived from individual demand curve?
2. If the demand for good Y increases as the price of good X rises, how are the two goods related?
   (a) Substitute goods
   (b) complementary goods
   (c) giffen goods
   (d) None of the above
3. The demand for a good falls with an increase in income of the consumer. What type of good is it?
   (a) Inferior good
   (b) giffen good
   (c) Normal good
   (d) Both a and b.
4. When the demand is perfectly elastic, the demand curve is:
   (a) parallel to X – axis
   (b) parallel to Y-axis
   (c) downward sloping curve
   (d) upward sloping curve
5. What will be the effect on equilibrium price and production of an increase in equal proportion of demand and supply of a commodity?
6. Explain the problem of "what to produce" with the help of PPC.
7. Complete the following table:

| Output (units) | 1 | 2 | 3 | 4 |
|---|---|---|---|---|
| TR (Rs.) | 4 | 6 | 6 | 4 |
| MR (Rs.) | | | | |
| AR (Rs. ) | | | | |

8. Explain three causes of the rightward shift of the supply curve.
9. Explain the causes behind the law of demand.
10. Distinguish between AFC and AVC. How are these calculated?
11. Suppose that the demand curve for XYZ Co. slopes downwards to the right. Would you conclude that the firm is a price maker or a price taker? Give reason.
12. Explain briefly the features of perfect competition.
13. Market for a good is in equilibrium. What is the effect on equilibrium price and quantity if increase in market demand is less than the increase in market supply? Use diagram.
14. Explain the law of supply. Use diagram.
15. Explain the effect of following changes on the demand for the commodity with the help of diagram:
    (a) a fall in price of substitute goods
    (b) a favourable change in the taste of buyer.

## Section B

16. During the Great depression, there was a __________:
    (a) Increase in aggregate demand
    (b) Fall in aggregate demand
    (c) No change in aggregate demand
    (d) None of the above.
17. When will $NDP_{MP}$ be less than $NDP_{FC}$?
    (a) Subsidies are less than indirect taxes.
    (b) Subsidies are more than indirect taxes.
    (c) Subsidies are equal to indirect taxes.
    (d) None of the above.
18. Currency depreciation takes place when:
    (a) There is an increase in domestic currency price of the foreign currency.
    (b) There is a decrease in domestic currency price of the foreign currency.
    (c) There is an increase in foreign currency price of domestic currency.
    (d) None of the above.
19. Which of the following is a correct formula to calculate Net Indirect tax?
    (a) Net Indirect tax = Direct tax – Subsidies
    (b) Net Indirect tax = Indirect tax – Subsidies
    (c) Net Indirect tax = Corporate tax – Subsidies
    (d) Net Indirect tax = Corporate tax + Subsidies
20. Define NDP at market price.
21. What is effective demand? How will you derive the autonomous expenditure multiplier when price of final goods and rate of investment are given?
22. What is budget? Distinguish between balanced, surplus and deficit budget.
23. From the following, calculate gross value added at factor cost by it:

| | (Rs. In lakhs) |
|---|---|
| Net indirect taxes | 20 |
| Purchase of intermediate products | 120 |
| Purchase of machines | 300 |
| Sales | 250 |
| Consumption of fixed capital | 20 |
| Change in stock | 30 |

24. What are open market operations? How do these effect availability of credit?.

25. Suppose BOP of current account of India in a year was – 2579 million US$, whereas BOP on its capital account was 8409 million $, how will this effect the foreign exchange reserve of India?
26. Briefly explain the agency functions performed by commercial banks.
27. What are the uses of national income accounting?
28. Explain the relation between foreign exchange rate and supply of foreign exchange.
29. Show with help of saving and investment curves, the determination of equilibrium level of income.
30. Define revenue receipts in a government budget. Explain how government budget can used to bring in price stability in the economy.

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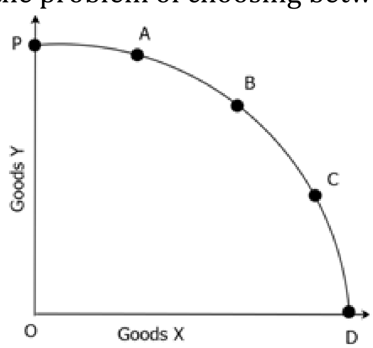
## Answers

1. Market demand curve is derived as a horizontal summation of individual demand curves.
2. (a) substitute goods.
3. (a) Inferior goods.
4. (a) Parallel to X-axis.
5. Other things remaining constant, when demand and supply increase in equal proportion there will be no change in equilibrium price. However the equilibrium quantity will increase.
6. **Problem of 'what to produce':** The problem of what to produce means which goods and services are to be produced and in what quantity. For example: the choice can be between consumer goods and capital goods. Within consumer goods, it is necessary to decide whether to produce luxuries or necessities. More of one commodity can be produced only at the cost of producing less of other commodity. On the PPC shown, the problem of what to produce is the problem of choosing between the points on the curve like A, B, C or D.




7.

| Output (units) | 1 | 2 | 3 | 4 |
|---|---|---|---|---|
| TR (Rs.) | 4 | 6 | 6 | 4 |
| MR (Rs.) | 4 | 2 | 0 | -2 |
| AR (Rs. ) | 4 | 3 | 2 | 1 |

8. Main causes of the rightward shift of the supply curve are:
   (a) **An improvement in technology** leads to a decline in the cost of production by the firm and as a result firms supply more than before at the same price. This is because the profit margin of the firms increases. Thus, supply would increase implying a rightward shift of the supply curve.
   (b) **A fall in price of inputs**: This has the same effect as improvement in technology. A fall in price of inputs like wages, raw materials etc, reduces the unit cost of production and therefore firms would like to supply more than before at the given price. As a result, supply curve shift to the right.
   (c) **A fall in price of other goods**: Suppose wheat and sunflower are the two goods that a farmer can produce. If the price of sunflower falls, then it would be more profitable for

the farmer to produce and sell more wheat. Therefore, the supply of wheat would increase even though the price of wheat remained the same. Thus, the supply curve for wheat would shift to the right.

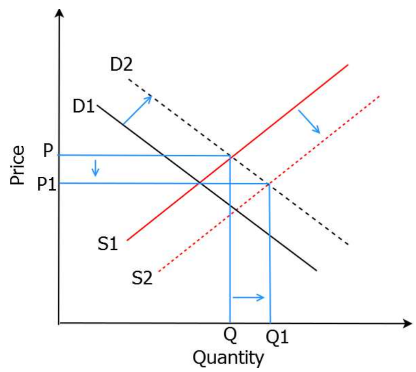
9. When the price of a good falls , it has the following two effects that lead a consumer to buy more of that commodity:
   (a) **Income effect**: when the price of a commodity falls, the real income of the consumer i.e. his purchasing power increases. As a result, he can now buy more of a commodity. This is called income effect. This causes increase in quantity demanded of the good whose price falls.
   (b) **Substitution effect**: when the price of a good falls, it becomes relatively cheaper than other goods. This induces the consumer to substitute the cheaper commodity for the other commodity which is now relatively expensive. This is called substitution effect. It causes increase in demand for the commodity whose price falls.

10. AFC: It is the per unit fixed cost of producing a commodity. It is obtained by dividing the total fixed cost by quantity of output.
    AFC = TFC/Q
    AFC decreases with an increase in the level of output.
    AVC: It is the per unit variable cost of producing a commodity. It is obtained by dividing the total variable cost by the quantity of output.
    AVC = TVC/Q
    AVC decreases but after reaching the stage of minimum cost, it starts increasing.

11. Since the demand curve of XYZ co. is downward sloping, it has to lower its price to sell additional units of output, whereas in perfect competition, the demand curve is parallel to x-axis as the firm can sell any additional amount of output at the same price. Hence, XYZ Co. is not a price taker but a price maker.

12. Following are the features of perfect competition:
    (a) **Large number of buyers and sellers**: there are large number of buyers and sellers in perfect competition. The number of sellers is so large that an individual seller produces a small portion of the total output of the market i.e. each seller is too small to influence the price in the market. Similarly, the number of buyers is so large that an individual buyer purchases an insignificant portion of the total output in the market. Therefore, no buyer can influence the price. Thus, both sellers and buyers are price takers.
    (b) **Homogenous product**: the goods sold by different sellers under perfect competition are homogenous or identical in every respect like quality, size, design etc. the products are perfect substitutes of one another. As a result, no seller can charge a higher price for the product it sells otherwise he will lose his customers.
    (c) **Freedom of entry and exit**: This mean that new firms are free to enter and existing firms can leave the market at any time. This ensures that there are neither abnormal profits nor losses by any firm in the long – run. If firms are making abnormal profits, new firms enter and raise total supply of the market. This reduces the market price and wipes out profit. In case the firms are incurring losses, some existing inefficient firms will leave the industry and reduce total supply. This raises the price till the losses are wiped out.

13. When proportionate increase in demand is less than the increase in supply, then equilibrium price will fall but the equilibrium quantity will rise. The diagram below illustrates this point.



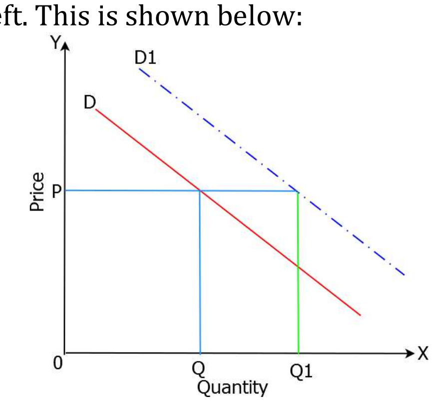

In the diagram, when the supply curve shifts to the right from $S_1S_1$ to $S_2S_2$ and demand curve shifts to the right from $D_1D_1$ to $D_2D_2$, the equilibrium price falls from OP to $OP_1$ but the equilibrium quantity rises from OQ to $OQ_1$.

14. The law of supply states that there is a direct relationship between quantity supplied of the commodity and price of the commodity. It implies that higher the price, greater the quantity supplied and lower the price, smaller the quantity supplied.
Assumptions:
(a) No change in technology.
(b) Prices of inputs remain constant.
(c) Prices of other goods do not change.
Law of supply can also be explained with the help of the following supply schedule and supply curve:

| Price | Supply (units) |
|---|---|
| 1 | 100 |
| 2 | 200 |
| 3 | 300 |

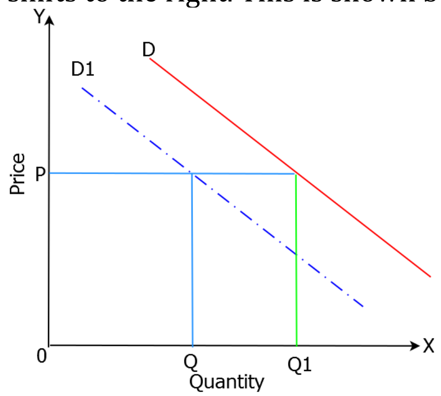
The above schedule and curve shows that with the rise in the price from Re 1 to Rs 2 and Rs 3, the quantity supplied of the commodity rises from 100 units to 200 and 300 units.

15. (a) The demand of a commodity and price of its substitute goods are directly related to each other. When the price of the substitute good (say coffee) falls, its demand rises and the demand for the commodity (say tea) falls and as a result the demand curve for tea shift to the left. This is shown below:




In the diagram, demand curve of X (say tea) is shown by the DD curve. With the fall in the price of the substitute good (say coffee), the quantity demanded of good X falls from OQ to $OQ_1$ at the same price OP1. The demand curve shifts leftwards to $D_1D_1$.

(b) The demand of a commodity and favourable changes in the taste of the buyers are directly related to each other. When there is a favourable change in the taste of the buyer, the demand of the commodity rises and as a result the demand curve of the commodity shifts to the right. This is shown below:




In the diagram, demand curve of X is shown by DD curve. With a favourable change in taste and preferences of the buyer, the demand of the commodity rises from OQ to $OQ_1$ at the given price OP. the demand curve shift rightwards to $D_1D_1$.

**SECTION B**

16. (b) Fall in aggregate demand
17. (b) Subsidies are more than indirect taxes.
18. (a) There is an increase in domestic currency price of the foreign currency.
19. (a) Net Indirect tax = Direct tax – Subsidies

20. It refers to market value of final goods and services produced within the domestic territory of the country within one year inclusive of depreciation.

21. The level of aggregate demand required to achieve full employment equilibrium is called effective demand. In other words, aggregate demand at the point of equilibrium is called effective demand. Under short – run analysis (i.e. when supply is infinitely elastic at constant price), it is the level of effective demand or aggregate demand which determines the level of income and employment.

22. A government budget is a detailed statement of the estimates of government receipts and expenditure during a financial year.
    **Surplus budget:** A surplus budget is one where the estimated revenue is greater than the estimated expenditure.
    **Balanced budget:** A surplus budget is one where the estimated revenue equals estimated expenditure.
    **Deficit budget:** A surplus budget is one where the estimated revenue is less than the estimated expenditure.
23. Gross value added at factor cost = sales + change in stock – purchase of intermediate products + net indirect taxes
    = 180 + 15 – 100 + 10
    = 105 lakhs
24. Open market operations refer to the purchase and sale of government securities in the open market by the central bank. By selling the government securities, the central bank loses equivalent amount of cash reserves thereby restricting their capacity to lend. By buying

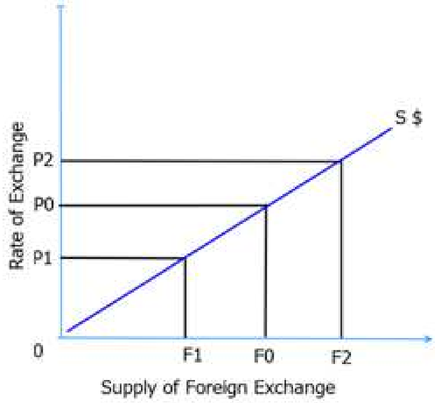
government securities, the central bank injects additional purchasing power into the system which results in the expansion of credit. Thus, depending on the situation of excess demand (or deficient demand), the central bank may resort to sale (or purchase) of government securities resulting in fall (or a rise) in the availability of credit.

25. Since surplus of balance of capital account (8409 million $) exceeds the deficit 2579 million $, there will be addition of 5830 million $ to the foreign exchange reserve of India (8409 – 2579 = 5830 million $)

26. The commercial bank performs the following agency functions for their customers in return for a commission:
    (a) **Transfer of funds:** The commercial bank provided facility of cheap and easy remittance of funds from one place to another through demand drafts, mail transfers etc.
    (b) **Collection of funds:** The banks undertake to collect funds on behalf of its customers for cheques, demand drafts, bills, hundis etc.
    (c) **Sale and purchase of securities:** The banks help the customers to buy and sell stocks and shares of the private companies as well as government securities.
    (d) **Income tax consultant:** Banks may also employ income tax experts to prepare income tax returns for their customers and to help them to get refund of income tax.

27. National income accounting is a set of rules and definitions for measuring economic activity in the economy. The followings are the various uses of national income accounting:
    (i) It shows as to how the national income is shared among the various factors of production.
    (ii) It serves as a record of economic function, viz., production, consumption, savings and capital formation.
    (iii) It indicates the specific contribution of individual sectors to aggregate performance as well as growth of these sectors.
    (iv) It indicates the changes in the sectoral composition of national output, thus giving knowledge of the structural changes in the economy.
    (v) These accounts are helpful in analysing the functioning, growth and structure of the economy's strength and failures.

28. There is a direct relation between foreign exchange rate and supply of foreign exchange. Higher the exchange rate, higher the supply of foreign exchange and vice versa. Suppose the price of US dollar in India falls from Rs. 50 to Rs. 40. It means that earlier, USA could by Rs. 50 worth of goods from India by parting one US dollar. Now it can buy only Rs. 40 worth of goods from India. Indian goods becomes costlier for USA. Therefore, USA buy less of Indian goods. This reduces the supply of US dollars to India. So lower the foreign exchange (i.e. price of US dollar) lower the supply and vice versa. Graphically the supply curve of foreign exchange is upward sloping signifying the direct relation between foreign exchange rate and supply of foreign exchange.

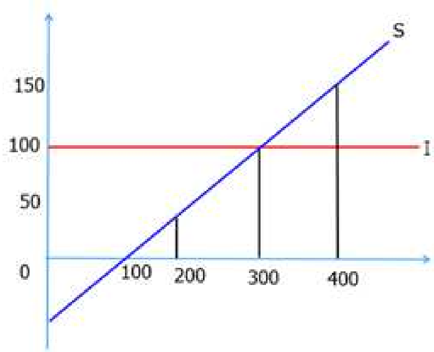



In the figure, at price $P_0$, the supply of foreign exchange is $F_0$. At a lower price $P_1$, the supply is $F_1$, i.e., lower. At a higher price $P_2$, the supply is $F_2$, i.e., higher.

29. The equilibrium level of income is determined at a point where saving and investment are equal i.e. S = I.

The following table and diagram illustrates the idea:

| Income (Y) | Consumption (c) | Saving (Y - C) | Investment (I) |
|---|---|---|---|
| 0 | 50 | - 50 | 100 |
| 100 | 10 | 0 | 100 |
| 200 | 150 | 50 | 100 |
| **300** | **200** | **100** | **100** |
| 400 | 250 | 150 | 100 |




The table and diagram shows that the equilibrium level of income is Rs 300 crores and at this point S = I = 100.

30. **Revenue Receipts** are those receipts of the government which neither creates any liability nor it creates any reduction in the assets of the government. These comprises of tax and non-tax receipts, duties and fines, interest and dividends receipts on government investments and assets. These are further classified into:

Tax Receipts

Non-tax Receipts

(a) **Tax Receipts:** A tax is a legally compulsory monetary contribution to the government by different economic units such as household, firms and other economic units. Taxes are imposed by the government on different activities, income, property, production, occupation, etc. The main motive of imposing taxes is to raise revenue and to incur various expenditures for enhancing welfare of the country. The following are the various types of taxes.

1. Direct and indirect taxes
2. Progressive and regressive taxes
3. Ad valorem and specific taxes

(b) **Non-Tax Receipts:** Non-tax receipts refer to those budget receipts of the government from sources other than taxes such as interest receipts, dividends, fines, duty fees, etc. Various non-tax receipts of the government can be classified as:

1. Fees and License- The government receives fees in return of various services provided by it to the people. Example- college fees, passport fees, registration fees, etc.
2. License Fees- These refer to the fees that are received by the government in return of the allowances granted to the people to perform certain activities. Example- Fees received from issue of import licenses.
3. Escheat- Escheat refers to the income from a property of a person who dies without having any legal heirs. In other words, the government acquires legal right over a property which has no claimant.
4. Fines and Penalties- Fines and penalties are imposed by the government on those who boycott law.

The government aims at insulating the economy from major fluctuations (like inflation, unemployment) and business cycles such as boom, recession, depression and recovery. The government through its budgetary policy tries to combat such situations. The major concern of government is to achieve higher economic growth rates while maintaining price and employment stability. This state of economic growth with stability ensures a smooth and efficient functioning of an economy.