CBSE Question Paper 2018

Class 12 Economics (Reconducted)

Time allowed : 3 hours

Maximum Marks : 80

General Instructions:

i. All questions in both the sections are compulsory.
ii. Marks for questions are indicated against each question.
iii. Question Nos. 1 – 4 and 13 – 16 are very short-answer questions carrying 1 mark each. They are required to be answered in one sentence each.
iv. Question Nos. 5 – 6 and 17 – 18 are short-answer questions carrying 3 marks each. Answers to them should normally not exceed 60 words each.
v. Question Nos. 7 – 9 and 19 – 21 are also short-answer questions carrying 4 marks each. Answers to them should normally not exceed 70 words each.
vi. Question Nos. 10 – 12 and 22 – 24 are long-answer questions carrying 6 marks each. Answers to them should normally not exceed 100 words each.
vii. Answers should be brief and to the point and the above word limits should be adhered to as far as possible.

1. **Define opportunity cost.**
   Ans. The value of next best alternative foregone.
2. **At what level of production is total cost equal to total fixed cost?**
   Ans. At zero level of output
3. **Which of the following does not cause shift of supply curve of a good? (Choose the correct alternative)**
   a. Price of input
   b. Price of the good
   c. Goods and services tax
   d. Subsidy
   Ans. (b) Price of the good
4. **Which of the following measures of price elasticity shows elastic supply? (Choose**

the correct alternative)

a. 0
b. 0·5
c. 1·0
d. 1·5

Ans. (d) 1.5

5. **Explain the central problem of "What is produced and in what quantities".**

OR

In what circumstances may the production possibility frontier shift away from the origin? Explain.

Ans. This problem deals with the situation where an economy must decide as to what goods or services it must produce and in what quantity. It is because the resources are scarce/limited and can be put to alternative uses. (to be marked as a whole)

OR

Production Possibility Frontier may shift away from origin, due to the following:

i. Increase in resources
ii. Improvement in technologies

6. **A consumer buys 200 units of a good at a price of ₹20 per unit. Price elasticity of demand is (–) 2. At what price will he be willing to purchase 300 units? Calculate.**

Ans. $E_d = \frac{\Delta Q}{\Delta P} \times \frac{P}{Q}$

$-2 = \frac{100}{\Delta P} \times \frac{20}{200}$

$-2(\Delta P) = 10$

$\Delta P = -5$

New Price=Orignal Price(P)+ΔP =20+(-)5=₹15

7. **Write a budget line equation of a consumer if the two goods purchased by the consumer, Good X and Good Y are priced at ₹ 10 and ₹ 5 respectively and the consumer's income is ₹ 100.**

OR

Define marginal rate of substitution. Explain its behaviour along an indifference

curve.

Ans. Budget Line equation:

$m = P_xQ_x + P_yQ_y$; where m=income

Accordingly: $100 = 10Q_x + 5Q_y$

OR

Marginal Rate of Substitution is defined as 'the rate at which a consumer is willing to sacrifice units of a good to obtain one more unit of the other good.

Marginal Rate of Substitution diminishes as the consumer moves downward along the same indifference curve. It shows that consumer is willing to sacrifice lesser units of a Good Y, in order to gain one additional unit of Good X. This happens due to the operation of law of diminishing marginal utility.

8. **Explain the conditions of producer's equilibrium under perfect competition.**

Ans. A producer is said to be in equilibrium when he produces that level of output at which :

a. MC = MR
b. MC > MR after the MC = MR output level

Explanation to the conditions:

Condition – 1 MC=MR

Suppose when a producer starts producing a good, with the given factors and finds MR > MC he goes on producing because every new unit produced adds to profits.

As he goes on producing more units of the good he may face an output level when MC = MR and this output level satisfies MC = MR condition of equilibrium.

Condition – 2 MC>MR after the MC=MR output level

After MC = MR level, if MC > MR, every new unit produced is sold at a loss. So, he would not like to produce more units thereafter. Therefore, only that output level at which MC = MR, and beyond which MC > MR, is the output at which the producer is in equilibrium

9. **Explain the implications of "freedom of entry and exit of firms" under perfect competition.**

Ans. 'Freedom of Entry', signifies that there are no barriers to the entry of new firms into industry. When the existing firms are earning supernormal profits, the new firms, attracted by the prospects of profit,enter the industry. This raises market supply which in

turn leads tofall in market price and consequently profits. The entry continuestill each firm is earning just the normal profits.

'Freedom to exit', signifies that there are no barriers which restrictthe existing firms from leaving the industry. The firms try to leavewhen they are facing losses. As the firms start leaving market supply falls leading to rise in market price and consequently reduction in losses. The firms continue to leave till the losses are wiped out and each existing firm is earning just the normal profits.

10. **A consumer consumes only two goods X and Y. Explain the conditions of consumer's equilibrium using Utility Analysis.**

Ans. Assuming that a consumer is consuming only two goods X and Y, the conditions of consumer's equilibrium (Utility Analysis) are:

a. $\frac{MU_X}{P_X} = \frac{MU_Y}{P_Y}$
b. MU of a good as more unit of good are consumed.

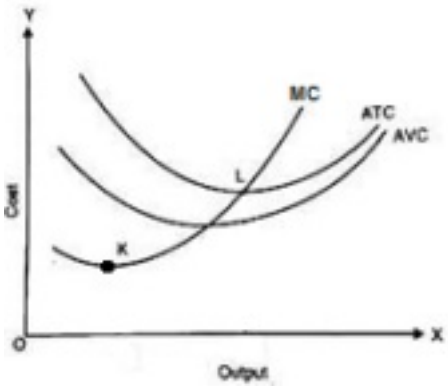
Explanation

i. Suppose $\frac{MU_X}{P_X} > \frac{MU_Y}{P_Y}$ The consumer will not be in equilibrium because per rupee MU of X is greater than per rupee MU of Y. This will induce the consumer to buy more of X by reducing expenditure on Y, leading to fall in MUx and rise in MU_y. This will continue till the consumer attains the condition of $\frac{MU_X}{P_X} = \frac{MU_Y}{P_Y}$
$\left(Explanation on \frac{MU}{P_X} < \frac{MU_Y}{P_Y} is also correct\right)$
ii. Unless MU of a good falls, as more units are consumed the consumer will not reach the equilibrium.

11. **Draw Average Variable Cost (AVC), Average Total Cost (ATC) and Marginal Cost (MC) curves in a single diagram. State the relation between MC curve and AVC & ATC curves.**

Ans. Examiners please check:

i. MC curves intersects ATC and AVC curves at their minimum points.
ii. Vertical distance between ATC curve and AVC curve goes on declining as output increases.



Relationship among MC,AVC & AC :

When MC < ATC or AVC , ATC or AVC falls

MC = ATC or AVC , ATC or AVC constant

MC > ATC or AVC , ATC or AVC rises

12. **Define price floor. Explain the implications of price floor.**

OR

Market of a good is in equilibrium. If the demand for the good 'decreases'. Explain the chain of effects of this change.

Ans. 'Price Floor' is the minimum price fixed by the government below which sellers cannot sell their product.

Since this price is normally set above the equilibrium price, there is excess supply in the market. As the seller may not be able to sell all that he wants to sell, he may illegally attempt to sell the product at a price below the floor price.

OR

Market of a good is in equilibrium. If the demand for the good decreases this creates an excess supply of the good at the existing price, in the market.

- The excess supply creates competition among sellers, resulting in fall inprice, because sellers will not be able to sell all that they want to sell at the existing price.
- Fall in price leads to rise in demand and fall in supply.
- These changes continue till the market reaches new equilibrium.

13. **Give one example of negative externalities.**

Ans. Pollution created by factories/vehicles

14. **Credit creation by commercial banks is determined by (Choose the correct**

alternative)

a. **Cash Reserve Ratio (CRR)**
b. **Statutory Liquidity Ratio (SLR)**
c. **Initial Deposits**
d. **All the above**

Ans. d) All of the above

15. **State the two components of M_1 measure of Money Supply.**

Ans. Currency held by public and demand deposits held by banks.

16. **Define aggregate supply.**

Ans. Aggregate Supply refers to the estimated money value of all the final goods and services planned to be produced in an economy.

17. **Distinguish between stock and flow variables with suitable examples.**

OR

What are capital goods? How are they different from consumption goods?

Ans. Any economic variable which is measured at a point of time is known as stock, e.g. capital,etc.

Whereas, any economic variable measured during a period of time is known as flow, e.g. income, etc. (any other relevant example)

OR

Capital goods are those durable goods which are used in production of goods and services,

Whereas consumption goods are those goods which are used for satisfaction of wants by the consumers.

18. **Define investment multiplier. How is it related to marginal propensity to consume?**

Ans. Investment Multiplier is a measure of the effect of change in initial investment on change in final national income.

There exist a direct relation between MPC and multiplier, i.e. higher the value of MPC, higher will be investment multiplier

$K = \frac{1}{1-MPC}$

19. **What is monetary policy ? State any three instruments of monetary policy.**

Ans. Policy adopted by the Central Bank of an economy in the direction of credit control

or money supply is known as Monetary Policy.
Instruments of Monetary Policy are Bank Rate, Repo Rate, Reverse Repo Rate, Cash Reserve Ratio.

20. **Define full employment in an economy. Discuss the situation when aggregate demand is more than aggregate supply at full employment income level.**

OR

What are two alternative ways of determining equilibrium level of income? How are these related?

Ans. Full Employment is a situation where those who are able and willing to work are getting work at the prevailing wage rate.
When Aggregate Demand is greater than Aggregate Supply at full employment, such a situation is known as Excess Demand or Inflationary Gap. It is called inflationary becausethis leads to a rise in general price level of the economy. (diagram not necessary)

OR

Two alternative ways of determining equilibrium level of income are:

i. Aggregate Demand – Aggregate Supply Approach (AD-AS Approach)
ii. Saving-Investment Approach (S-I Approach).
Interrelation between the two approaches:
AD=AS (AD-AS approach)
C+I = C+S
I=S (S-I approach)

21. **What is ex-Ante consumption ? Distinguish between autonomous consumption and induced consumption.**

Ans. Ex-ante consumption refers to the consumption expenditure planned to be incurred during a period.
Autonomous Consumption refers to the consumption expenditure which does not depend upon the level of income, i.e. the consumption at zero level of income.
Whereas, Induced Consumption expenditure is directly determined by the level of income.

22. **What is government budget? Explain its major components.**

OR

Explain (a) allocation of resources and (b) economic stability as objectives of government budget.

Ans. Government Budget is defined as a statement of planned receipts and planned expenditure of the government during a fiscal year. Its major components are:

i. **Revenue Receipts:** the receipts which neither create a liability nor lead to reduction in assets.
ii. **Capital Receipts:** the receipts which either create a liability or lead to reduction in assets.
iii. **Revenue Expenditures:** the expenditure which does not lead to any creation of assets or reduction in liabilities.
iv. **Capital expenditures:** the expenditure which leads to creation of assets or reduction in liabilities.

OR

OBJECTIVES OF GOVERNMENT BUDGET:

a. **Allocation of resources in the economy**
   There are many non-profitable economic activities which are not undertaken by the private sector like, water supply, sanitation, etc., but are necessarily undertaken by government in public interest. So Government can undertake these activities in order to create social welfare. In addition, government can encourage the private sector through tax concessions, subsidies, etc., to undertake certain production in public interest.
b. **Economic stability**
   Economic stability means absence of large-scale fluctuation in prices. Such fluctuations create uncertainties in the economy. Government can exercise control over these fluctuations through taxes and expenditure.
   For example, under inflationary situations, government may discourage spending by increasing taxes or reducing its own expenditure whereas, under deflationary conditions, government may encourage spending by giving tax concession, subsidies, etc

23. **Discuss briefly the meanings of :**
    i. **Fixed Exchange Rate**
    ii. **Flexible Exchange Rate**
    iii. **Managed Floating Exchange Rate**

Ans. Fixed Exchange Rate: is the exchange rate determined by the government for conversion of domestic currency into foreign currency.
Flexible Exchange Rate: is the rate of exchange which is determined by the market forces of demand and supply in the foreign exchange market.
Managed Floating Exchange Rate: Floating rate influenced by buying and selling foreign exchange by the central bank in the foreign exchange market.

24. **Calculate (a) Operating Surplus, and (b) Domestic Income:**

	(₹ in crores)
(i) Compensation of employees	**2,000**
(ii) Rent and interest	**800**
(iii) Indirect taxes	**120**
(iv) Corporation tax	**460**
(v) Consumption of fixed capital	**100**
(vi) Subsidies	**20**
(vii) Dividend	**940**
(viii) Undistributed profits	**300**
(ix) Net factor income to abroad	**150**
(x) Mixed income	**200**

Ans.

a. Operating Surplus = (ii)+ [(iv) + (vii) + (viii)]
   = 800+ 460+940+300 = ₹2500 crore
b. Domestic Income = (i)+ Operating Surplus + (x)
   = 2,000 + 2500 + 200 = ₹4,700 crores