

XII-ECONOMICS – I MID TERM ANSWER KEY

I. CHOOSE THE BEST ANSWER (10×1=10)

Q.NO	OPTION CODE	ANSWER
1	b	Income theory
2	a	Adam Smith
3	b	Three
4	d	Capital Sector
5	b	Classical
6	d	Saving
7	b	$\Delta c/\Delta y$
8	b	J.M.Keynes
9	a	Balanced budget
10	a	1

II. 2MARKS (15 IS COMPULSORY) (4×2=8)

11. Economic model

It is an explanation of how the economy, or part of the economy, works.

(or)

A model is a simplified representation of real situation.

12. Full Employment

Full employment refers to a situation in which every able bodied person who is willing to work at the prevailing wage rate, is employed.

(or)

Keynes defines full employment as the absence of involuntary unemployment.

13. Propensity to consume

Proportion of total income or of an increase in income that consumers tend to spend on goods and services rather than to save.

14. Economy

A. J. Brown as, "A system by which people earn their living."

(or)

J. R. Hicks defined as, "An economy is a cooperation of producers and workers to make goods and services that satisfy the wants of the consumers."

(or)

In short, an economy is referred to any system or area where economic activities are carried out.

15. Formula for calculating GDP

GDP by expenditure method at market prices
 $= C + I + G + (X - M)$

III. 3 Marks (20 is compulsory) (4×3=12)

16. Two Sector Model

It is for a simple economy with households and firms.

(i) Household Sector: The household sector is the sole buyer of goods and services, and the sole supplier of factors of production

(ii) Firms: The firm sector generates its revenue by selling goods and services to the household sector.



17. Per Capita Income

- The average income of a person of a country in a particular year
- Per Capita income = $\frac{\text{National Income}}{\text{Population}}$

18. Aggregate demand :

The aggregate demand is the amount of money which entrepreneurs expect to get by selling the output produced by the number of labourers employed. Aggregate demand has the following four components:

- Consumption demand
- Investment demand
- Government expenditure and
- Net Export (export – import)

19. Uses of National income

- The national income of a country describes the economic performance or production performance of a country.
- National income data help in measuring changes in the standard of living over time
- Enable us to compare standard of living of different countries.
- Level of development of a country is also measured by using national income figures.

20. Propositions of Keynes Law of consumption:

- When income increases, consumption expenditure also increases but by a smaller amount.
- The increased income will be divided in some proportion between consumption expenditure and saving.
- Increase in income always leads to an increase in both consumption and saving.

IV. 5 Marks

(3×5=15)

21.

Features	Capitalism	Socialism	Mixedism
Ownership (Means of Production)	Private Ownership	Public Ownership	Private and Public Ownership
Economic motive	Profit	Social Welfare	Social Welfare and Profit Motive
Government Role	Internal Regulation only	Complete Involvement	Limited Role
Income Distribution	Unequal	Equal	Less unequal
Nature of Enterprise	Private Enterprise	Government Enterprise	Both Private and State Enterprises
Major Problem	Inequality	Inefficiency	Inequality and Inefficiency

(or)

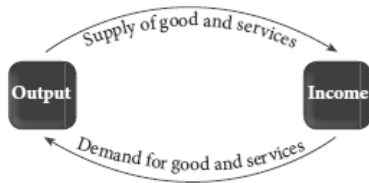
importance of national income(any 5 points)

1. To know the relative importance of the various sectors of the economy and their contribution.
2. To formulate the national policies
3. To formulate planning and evaluate plan progress
4. To build economic models both in short - run and long - run.
5. To make international comparison, inter - regional comparison
6. To know a country's per capita income.
7. To know the distribution of income for various factors of production

22.

Say's law of market:

J.B. Say enunciated the proposition that "Supply creates its own demand".



Assumptions of the Say's law of market

1. No single buyer or seller of commodity or an input can affect price.
2. Full employment.
3. The laissez faire policy .
4. There will be a perfect competition in labour and product market.
5. There is wage-price flexibility.
6. Money acts only as a medium of exchange.
7. Long - run analysis.
8. There is no possibility for over production or unemployment.

Implications of Say's Law

1. There is no possibility for over production or unemployment.
2. As automatic price mechanism operates in the economy
3. Interest flexibility brings about equality between saving and investment.
4. Money performs only the medium of exchange.

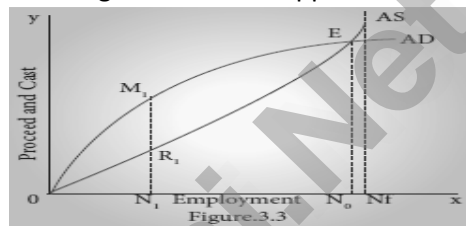
(or)

Marginal Efficiency of Capital(MEC)	Marginal Efficiency of Investment(MEI)
It represents the rate of return on all successive units of capital without regard to existing capital.	It shows the rate of return on just those units of capital over and above the existing capital stock.
It is a "stock" concept.	It is a "flow" concept.
It is based on a given supply price for capital.	It is based on the induced change in the price due to change in the demand for capital.
The capital stock is taken on the X axis of diagram.	The amount of investment is taken on the X - axis of diagram.
It determines the optimum capital stock in an economy at each level of interest rate.	It determines the net investment of the economy at each interest rate given the capital stock

23.

There are two approaches to determination of the equilibrium level of income in Keynesian theory. These are

1. Aggregate demand – Aggregate supply approach
2. Saving – Investment approach



- In the figure, the aggregate demand and aggregate supply reach equilibrium at point E.
- The employment level is No at that point. They expected level of profit is M1 R1.
- To attain this level of profit, entrepreneurs will employ more labourers.
- The tendency to employ more labour will stop once they reach point E.
- It is important to note that the equilibrium level of employment need not be the full employment level (N1)
- it is understood that the difference between No – Nf is the level of unemployment.
- Thus the concept of effective demand becomes significant in explaining the under employment equilibrium.

(or)

Operation of the Acceleration Principle

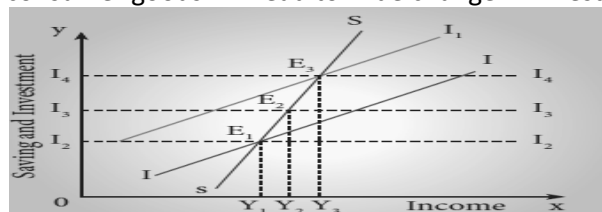
Let us suppose that in order to produce 1000 consumer goods, 100 machines are required.

Every year 10 machines have to be replaced

Suppose that demand for consumer goods rises by 10 percent (ie from 1000 to 1100).

This results in increase in demand for 10 more machines. So that total demand for machines is 20.

we can conclude even a mild change in demand for consumer goods will lead to wide change in investment.



At point E1, the economy is in equilibrium with OY1

income.

Saving and investment are equal
at OI2.

Now, investment is increased from OI2 to OI4. This
increases income from OY1 to OY3, the equilibrium point
being E3

Therefore, increase in income by Y1 Y2 is due to the
multiplier effect and the increase in income by Y2 Y3 is
due to the accelerator effect.

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