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Answers Key:

Answer in Detail

1. **National Income:**
(i) Measurement of national income and its composition by sectors are the basic aspects of macro economic analysis.
(ii) It gives a long term understanding of the growth process of an economy.
Inflation:
(i) Estimating the general price level based on wholesale price, index, consumer price.
Business Cycle:
(i) Cyclical movements can be studied based on aggregate economic variables.
Poverty and Unemployment:
(i) Clear understanding about the magnitude of poverty and unemployment helps allocation of resources and adapting corrective measures.
Economic Growth:
(i) The growth and development of an economy and the factors determining them could be understood only through macro analysis.
Economic Policies:
(i) Macro Economics is used to frame economic policies.
(ii) Economic policies are used to solve the basic problems, to overcome the obstacles and to achieve growth.
2. 1. In an economy, the fundamental economic activities are production and consumption.
2. These are several other activities.
3. The ultimate aim is to achieve growth.
4. The exchange activity supports production and consumption.
5. These activities are influenced by economic and non economic activities.
6. The economic activities include transportation, banking, advertising, planning.
7. The non-economic activities are environment, education, health, entertainment.
8. The external activities are import, export, international relations, emigration, immigration, foreign investment, foreign exchange earnings.
9. All these activities influence the entire functioning of the economy.
3. **Introduction:**
(i) Whatever is produced is either used for consumption or for saving. So, national output can be computed at any of three levels, ie., production, income and expenditure.
(ii) Therefore there are three methods to measure national income.
Product Method (inventory method):
(i) This method measures the output of the country. Gross value of output from different sectors like agriculture, industry, trade, commerce is obtained by the summation of all the values added in the productive process.
(ii) In India, the gross value of the farm output is obtained as follows:
(iii) Total production of 64 agriculture commodities is estimated. The output of each crop is measured by multiplying the area sown by the average yield per hectare.
(iv) Total output of each commodity is valued at market prices.
(v) The aggregate value of total output of these 64 commodities is taken to measure the gross value of agricultural output.
(vi) The net value of the agricultural output is measured by making deductions for the cost of seed, manures and fertilizers, market charges.
(vii) Net value of each sector is measured in this way.
(viii) Double counting should be avoided.
(ix) Value of output used for self consumption should be counted but sale and purchase of second hand durable goods should be excluded.
Income Method (Factor Earning Method):
(i) National income is calculated by adding up all the incomes generated while producing national product.
(ii) Enterprises are classified into industrial groups.
(iii) Factor incomes are grouped under labour income (wages, salaries, fringe benefits), capital income (profit, interest, dividend) and mixed income (farming, sole proprietorship).
$Y = w + r + i + \pi + (R - P)$
(iv) Transfer payment, receipt from sale of second hand goods, windfall gains and corporate profit tax must not be included.
(v) Imputed value of rent for self occupied houses or offices and Imputed value of services provided by owners of production units are to be included.
Expenditure method (outlay method):
(i) The total expenditure incurred by the society in a particular year is added together.
(ii) It includes personal consumption expenditure (C), net domestic investment (I), Government expenditure on consumption (G) and net exports (X-M).
$GNP = C + I + G + (X - M)$
(iii) Expenditure on second hand goods, purchase of shares and bonds, transfer payments and expenditure on intermediate goods should not be included.
Conclusion:
Output = Income = Expenditure
(i) This is because the three methods are circular in nature. So, if the 3 methods are done correctly this equation must hold.
4. **Introduction**
According to J. B. Say "Supply creates its own demand"

Explanation

A person receives his income from production which is spent on the purchase of goods and services produced by others. For the economy as a whole, therefore, total production equals total income.

Criticisms

(i) According to Keynes, supply does not. create its demand. It is not applicable where demand does not increase as much as production increases.
(ii) Automatic adjustment process will not remove unemployment. Unemployment can be removed by increase in the rate of investment.
(iii) Money is not neutral. Individuals hold money for unforeseen contingencies, businessmen keep cash reserve for future activities.
(iv) Say's law is supply creates its own demand and there is no over production. Keynes said that over production is possible
(v) Keynes regards full employment as a special case because there is underemployment in capitalist economies.
(vi) State intervention is needed when there is over production and mass unemployment.

5. S.No Keynesian Classicism 1. Short-run equilibrium Long-run equilibrium 2. Savings is a vice Saving is a social virtue 3. Money functions as medium of exchange and store of value. Money acts as a medium of exchange. 4. Macro approch to national problems. Micro foundation to macro problems. 5. State intervention is advocated. Favoured laissez-fair policy. 6. Applicable to all situations-full employment and less than full employment. Applicable only to the full employment 7. Captialism has inherent contradictions Captialism is good. 8. Budgeting should be adjusted to the requirements of economy. Balanced budget is favored. 9. Equality between saving and investment is achieved through changes in income Equality between saving and investment is achieved through changes of rate of interest 10. Rate of interest is determined by the demand for and supply of money Rate of interest is determined by saving and investment. 11. Rate of interest is a flow. Rate of interest is a stock. 12. Demand vreates its own supply. Supply creates its own demand. 13. Rate of interest is a reward for parting with liquidity Rate of interest is a reward for savings.

6.

S. No	Marginal Efficiency of Captial (MEC)	Marginal Efficiency of Investment (MEI)
1.	It is based on given supply price for capital.	It is based on the induced change in the price due to change in the demand for capital.
2.	It represents the rate of return on all successive unit 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
3.	The capital stock is taken on the X axis of diagram.	The amount of investment is taken on the X axis of diagram.
4.	It is a 'Stock' concept.	It is a 'Flow' concept.
5.	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.

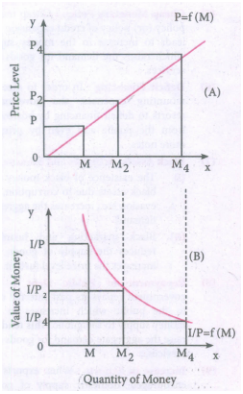
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7. **Introduction:**

(i) It was first propounded in 1588 by an Italian economist Davanzatti. It was popularised by an Americill economist, Irving Fisher is his book, "The Purchasing Power of Money" in 1911. He gave it a quantitative form in terms of "Equation of Exchange".

Equations:

MV = PT
(i) The Supply of Money = Demand for Money
M = Money Supply
V = Velocity of Money
P = Price level
T = Volume of Transaction.
(ii) The total quantity of money will be equal to the total value of all goods and services bought and sold.
$P = \frac{MV}{T}$
(iii) The quantity of money determines the price level and the price level varies directly with the quantity of money provided 'V' and 'T' remain constant.
(iv) Later Fisher extended his exchange to include bank deposits M_1 and its velocity V_1.
$PT = MV + M'V'$
$P = \frac{MV+M'V'}{T}$
- The price level is determined by
(a) quantity of money in circulation M
(b) velocity of circulation of money V
(c) volume of bank credit money M_1
(d) velocity of circulation of credit money V_1
(c) Volume of trade ('T')



(i) It show's the effect of changes in the quantity of money on the price level.
(ii) When quantity of money is OM_1, the price level is OP_1.
(iii) When the quantity of money is doubled to OM_2, the price level is also doubled to OP_2.
(iv) When quantity of money is increased four-fold to OM_4, the price level also increases by 4 times to OP_4 his relationship is shown by the curve OP = f(M) from the origin at 45°.

Quantity of money

(i) Fig B shows the inverse relation between the quantity of money and the value of money.
(ii) Value of money is taken on the vertical axis.
(iii) When the quantity of money is OM_1, the value of money is OI / P_1.
(iv) When quantity of money is doubled to OM_2, the value of money becomes one half of what it was before (OI / P_2)
(v) When quantity of money increases by the four fold to OM_4, the value of among is reduced by OI / P_4
(vi) This inverse relationship between the quantity of money and the value of money is shown by downward sloping curve $1 / OP = f(M)$.

Answer Briefly

8. (i) Automatic working without any government intervention.
(ii) Efficient use of resources.
(iii) Incentives for hard work.
(iv) Production and productivity are high, so there is economic progress.
(v) Consumers sovereignty exist.
(vi) Increased saving and investment leads to higher capital formation.
(vii) Development of new technology.

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9. (i) A country with a high national income enjoys greater economic welfare and higher standard of living.
(ii) But the per capita income as an index of economic welfare has some limitations.
(iii) Welfare depends on the composition of goods and services. If more capital goods over consumer goods are produced welfare will be lesser.
(iv) Higher GDP with greater air, water, soil pollution will affect welfare.
(v) Production of war goods will increase output but not welfare.
(vi) If more women and children are employed or workers are forced to work for long hours economic welfare is affected.
(v) Therefore the Physical Quality of Life Index is a better indicator of economic welfare than national income.

10.

S. No	Autonomous Investment	Induced Investment
2.	Independent	Planned
3.	Income inelastic	Income elastic
4.	Welfare motive	Profit motive

11. (i) Money supply means the total amount of money in an economy.
(ii) It refers to the amount of money which is in circulation in an economy at any given time.
(iii) Money supply determines the price level and interest rates.
(iv) Money supply viewed at a given point of time is a stock and over a period of time it is a flow.

12.

S. No.	Money Market	Capital Market
(1)	Short term funds are loaned and borrowed	Long term funds are loaned and borrowed
(2)	It deals with purchase, sale and transfer of short term credit instruments.	It raises capital by dealing in shares, bonds mortgages and other long term investments.
(3)	Commercial banks, acceptance houses, Non Banking Financial Institutions and the Central Bank deals with short term funds	Instruments traded in capital market comprise of equity shares, preference. shares, Debentures, bonds and other long term securities.

13. FDI has the following objectives.
(i) Sales Expansion
(ii) Acquisition of resources

(iii) Diversification
(iv) Minimization of competitive risk

14. Inclusive growth, Trade issues, Global governance, Shared Prosperity, International peace and security.

Answer Shortly

15. Economies can be classified into different types based on the Status of Development are
    1. Developed
    2. Underdeveloped
    3. Undeveloped and
    4. Developing economies
16. (i) A Model is a simplified representation of real situation.
    (ii) Economists use models to describe economic activities, their relationships and their behaviour.
17. GDP deflator is an index of price changes of goods and services included in GDP.
    GDP deflator $= \frac{Nominal\ GDP}{Real\ GDP} \times 100$
18. (i) Farmers keep a large portion of food and other goods produced on the farm for self consumption.
    (ii) This amount varies from person to person.
    (iii) The problem is whether this unsold portion should be included in NI or not.
19. (i) Invention and innovations lead to the adoption of new techniques.
    (ii) So existing workers are retrenched.
    (iii) This is called technological unemployment.
    (iv) It is due to the use of labour saving devices.
20. It is the proportion of disposable income which individuals spend on consumption.
21. (i) The Central Bank purchases and sells Government securities and proper eligible securities like bills and securities of private concerns.
    (ii) This is called Open Market operation.

Multiple Choice Question

22. (b) Income Theory
23. (d) aggregates
24. (b) America
25. (b) Karl Marx
26. (c) Economic
27. (a) Zero
28. (d) Under employment
29. (d) Rate of Interest
30. (a) Balanced budget
31. (d) ₹ 0.9
32. (c) Change in consumption / change in income
33. (a) Central Monetary authority
34. (b) Rate at which the RBI is willing to lend to commercial banks
35. (d) March 1982
36. (a) Rs.500 and Rs.1000
37. (b) Resources are not equally distributed among all trading nations
38. (a) Jacob Viner
39. (b) Atomic energy
40. (b) World Bank
41. (d) North Korea

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