ISC SEMESTER 2 EXAMINATION
SAMPLE PAPER - 5
ECONOMICS

Maximum Marks: 40

Time allowed: One and a half hour

Candidates are allowed an additional ***10 minutes*** *for* **only** *reading the paper.*

They must ***NOT*** *start writing during this time.*

Answer ***all*** *questions in* ***Section A, Section B and Section C.***

Section-A

Question 1.

(i) If gross value added is ₹40 and intermediate cost is ₹70, find the value of output of a firm.

(a) ₹30 (b) ₹40 (c) ₹110 (d) ₹70

(ii) To increase the flow of credit, RBI will:

Choose the correct alternative:

(a) Increase the bank rate
(c) Increase the CRR
(b) Decrease the bank rate
(d) Increase the SLR

(iii) The impact of "Excess Demand" under Keynesian theory of income and employment, in an economy are:

(a) decrease in income, output, employment and general price level.
(b) decrease in nominal income, but no change in real output.
(c) increase in income, output, employment and general price level.
(d) no change in output/employment but increase in general price level.

(iv) Which one of the following is transfer earning?

(a) Rent from building in Singapore
(b) Income after selling goods
(c) Pocket money received by students
(d) All of the above

(v) Decrease in SLR will lead to ____________ in aggregate demand.

(vi) ____________ deficit represents borrowing requirement of the government.

(vii) $GDP_{mp} = NDP_{fc}$ ___________.

(viii) Give one difference between revenue deficit and fiscal deficit.

Section-B

Answer the following questions briefly.

Question 2.

Differentiate between quantitative and qualitative tools of RBI to control flow of credit.

Question 3.

Balance of payment is always balanced in the accounting sense. Defend or refute the statement with the help of valid reasons.

Question 4.

'Real Gross Domestic Product is a better indicator of economic growth than Nominal Gross Domestic Product'.

Do you agree with the given statement? Support your answer with a suitable numerical example.

Question 5.

Calculate the value of Marginal Propensity to Consume (MPC), if in an economy, autonomous consumption is ₹500 crore ex-ante investments are ₹4,000 crore and equilibrium level of income of the economy is ₹18,000 crore.

Question 6.

(i) If Central Bank reduce reverse Repo Rate then explain how fall in reserve repo rate will reduce the money supply?

OR

(ii) "Trade Deficit must exist if a country is facing a situation of Current Account Deficit"

Defend or refute the statement, with valid argument.

Question 7.

Discuss two contingent functions of money.

Section-C

Question 8.

(i) What changes will take place if AD is less than AS. Explain the steps to achieve equilibrium level of output.

OR

(ii) What is investment multiplier? How is it related to MPC?

Question 9.

How does the rise in the flow of foreign exchange in the country affects the foreign exchange rate?

Question 10.

Calculate compensation of employees from the following data:

S. No.	Particulars	Amount (in ₹ Crore)
(i)	Profits after tax	20
(ii)	Interest	45
(iii)	Gross Domestic Product at Market Price	200
(iv)	Goods and Services Tax	10
(v)	Consumption of Fixed Capital	50
(vi)	Rent	25
(vii)	Corporate Tax	5

Question 11.

What are the revenue items in the government budget? Classify them with the help of a flow chart.

Question 12.

Read the given extract carefully and answer the following questions:

The Reserve Bank of India (RBI), cut Repo Rate to 4.4%, the lowest in at least 15 years. Also, it reduced the Cash Reserve Ratio (CRR) maintained by the banks for the first time in over seven years. CRR for all banks was cut by 100 basis points to release ₹ 1.37 lakh crore across the banking system. RBI governor Dr. Shaktikanta Das predicted a big global recession and said India will not be immune. It all depends how India responds to the situation. Aggregate demand may weaken and ease core inflation.

The Economic Times; March 27th, 2020

(i) Enlist any two instruments of RBI that is the part of the same category to which CRR belongs.

(ii) What was the expectation of RBI by reducing CRR and Repo rate?

(iii) Define demand deposits.

Answers

Section-A

Answer 1.

(i) (a) ₹110

Explanation:

Gross value is the total value of goods and services produced in an economy. In the above case, the total value is ₹110.

(ii) (b) Decrease the bank rate

Explanation:

At time of credit crunch, RBI decreases the bank rate and this encourages commercial banks and people to take more loans due to low interest payments. This enhances the flow of credit in the economy.

(iii) (d) no change in output/employment but increase in general price level.

Explanation:

Excess demand does not affect the level of output because economy is already at full employment level and there is no ideal capacity in the economy.

(iv) (c) Pocket money received by students

Explanation:

Payment received without any good or service provided in return is called transfer payment. So pocket money received by students is not a transfer earning.

(v) fall / decrease

Explanation:

Decrease in SLR will lead to decrease in aggregate demand. When SLR is reduced, banks have more money to lend which may lead to a decrease in lending rates.

(vi) Fiscal

Explanation:

Fiscal deficit represents the borrowing requirement of the government.

(vii) + Depreciation + NIT

Explanation:

$GDP_{mp} = NDP_{fc} + \text{Depreciation} + \text{NIT}$

(viii) Revenue deficit is the deficit arise due to the excess of revenue expenditure over revenue receipts, while fiscal deficit is the excess of total expenditure of the government over revenue and capital receipts except borrowings.

Section-B

Answer 2.

S.No.	Quantitative tools	Qualitative tools
1.	These are used to influence the quantity of credit in the economy.	These instruments are used for discriminating between various uses of credit.
2.	These are general in nature.	These are selective instruments

Answer 3.

I defend the statement.

Balance of payment is always balanced in accounting sense due to the concept of double entry book keeping. Against every credit entry, there is always an offsetting debit entry. Hence the receipts and payments on these two sides of BOP account must gets balanced (Debit side and credit side).

But, in functional sense, there can be deficit or surplus in BOP.

Answer 4.

I agree with the statement.

Real GDP is the money value of all the final goods and services calculated at base year prices in a given period of time.

Nominal GDP is the money value of all the final goods and services calculated at current year prices in a given period of time.

For example:

Commodities	Quantity produced in 2021	Price in 2015	Real GDP
A	10	10	100
B	15	5	75
C	5	8	40
Total			215

Real GDP calculated can be compared with the real GDP of different years due to constant prices adopted (For the year 2015)

Commodities	Quantity produced in 2021	Price in 2021	Nominal GDP
A	10	15	150
B	15	15	225
C	5	10	50
Total			425

Nominal GDP calculated above cannot be compared as it has no common base to compare with the gap of different years. The increase or decrease in nominal GDP can be the result of both change in production and prices. Hence it is not the true indicator of economic growth.

Answer 5.

Autonomous consumption = ₹500 Cr.

Investment = ₹4000 Cr.

Equilibrium level of income = ₹18000 Cr.

At equilibrium,

$$AD = AS$$

$$AD = C + I$$

$$C + I = Y$$

$$C = C_0 + bY$$

$$C_0 + bY + I = Y$$

C_0 = Autonomous consumption

b = MPC

$$500 + b\,(18000) + 4000 = 18000$$

$$b\,(18000) = 13500$$

$$b = 18000/13500 = 0.75$$

$$MPC = 0.75$$

Answer 6.

(i) In order to boost up the money supply in the economy, Central Bank recently reduced Reverse Repo Rate.

It is the rate at which the Central Bank of the country borrows money from the commercial banks in the country. Central Bank has taken this decision in order to increase the money supply in the economy. Reducing the reverse repo rate will make it less attractive for commercial banks to lend money to Central Bank and hence it will approach the general public for lending activities. This will boost up the flow of money.

OR

(ii) I refute the statement

Trade deficit is a situation which indicates the value of exports of goods is less than the import of goods. Whereas, current account deficit is a broader term which indicates excess of autonomous payments over the autonomous receipts in the current account of BOP.

If a country is facing a situation of current account deficit, there is a possibility that trade account deficit may not appear. Current Account Deficit (CAD) can be due to deficit in balance of invisible items or deficit in balance of unilateral transfers or both.

Answer 7.

1. **Facilitates credit:** Money facilitates the functioning of credit instruments such as cheques, promissory notes, bills of exchange etc. Such credit instruments facilitate transfer of value from one person to another.
2. **Liquidity:** Money is the most liquid form of all the assets and wealth. Gold, silver, land, cheques are not as liquid as money. If the need arises, these assets can be converted into immediate cash or money, but money need not to be converted into any other form as it is readily acceptable. Apart from liquidity, money also provides guarantee of liquidity/solvency to other form of wealth and assets.

Section-C

Answer 8.

(i) The above statement means that economy is facing a situation of less aggregate demand. It means, actual aggregate demand falls short of aggregate supply to achieve equilibrium. . Due to less demand in the economy, there exists the piling of stock. As the stock levels increases, firms reduce the production and income levels also falls. This will continue till the equilibrium output is achieved.

OR

(ii) Investment multiplier is the number of times income increases due to an increase in investment in an economy. It is represented as 'K'.

K = Change in income / Change in investment.

K = 1/1 – MPC

Investment multiplier and MPC are directly related to each other.

Higher is the MPC, more proportion of income is spent on consumption. As the income increases due to change in investment, it increases the consumption level which further generates the income in the economy based on the assumption, one man's expenditure is another man's income.

Hence, rise in MPC will raise the value of investment multiplier.

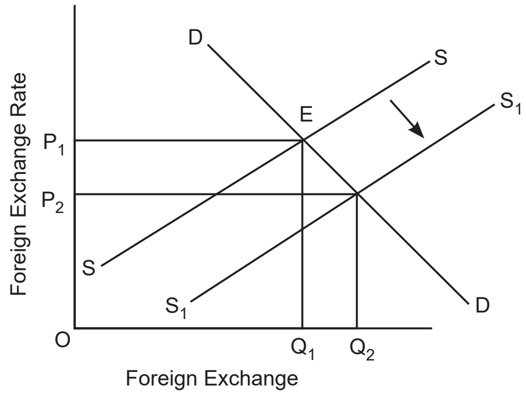
Answer 9.

When, more and more foreign exchange in terms of Dollars, Euros and Pounds will flow in our economy, it will raise the supply of foreign currency.

Due to rise in foreign capital, the supply of foreign exchange increased, leading to rightward shift in the supply curve. Due to excess supply of foreign exchange, the foreign exchange rate begins to fall.

This is known as "Appreciation of domestic currency".

In the diagram, The supply curve shifts from SS to S_1S_1, that led to resultant change in the prices from OP_1 to OP_2. This fall in price is Appreciation of domestic currency.



Answer 10.

NDP at FC = GDP at MP – Depreciation – NIT

NDP at FC = 200 – 50 – (10 – 0)

= ₹140 Cr.

NDP at FC = Compensation of employees + Operating surplus + Mixed income of self-employed.

140 = Compensation of employees + (20 + 45 + 25 + 5) + 0

140 – 95 = Compensation of employees = ₹45 Cr.

Answer 11.

Revenue items are those items which does not increase or decrease the asset or liability status of the government. They are of recurring nature. They can be classified into:

1. Revenue receipts
2. Revenue expenditures.

Revenue receipts and revenue expenditures can be shown as :

Revenue Receipts

Tax Revenue

Direct Tax
- Income Tax
- Wealth Tax
- Corporation Tax
- Interest Tax

Indirect Tax
- Custom Duty
- Sales Tax
- Service Tax
- Excise Duty

Non-Tax Revenue
- Interest
- Profits
- Escheat
- Grants-in-aid
- Fees
- Fines and Penalties
- Special Assessment

Revenue Expenditure

Planned
- Central Five Year Plan
- Assistance to State

Non-Planned
- Salaries
- Defence
- Subsidies
- Interest

Answer 12.

(i) SLR and Open market operations.

(ii) The expectation of RBI was to increase the flow of money and demand levels in the economy which is facing the problem of recession.

By reducing these rates, RBI will boost up the lending capacity of commercial banks. This will increase the flow of money and demand levels.

(iii) Demand deposits are the deposits with the bank by the general public which can be withdrawn on demand.