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MCQs With Explanatory Notes
For
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For

Economy

Corporate
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Micro-Macro Economics

Demand & Supply/Price/Revenue & Cost

1. Devaluation usually causes the internal price to
 (a) Fall (b) Rise
 (c) Remain unchanged (d) None of these

Ans. (c) Devaluation is a deliberate downward adjustment to the value of a country's currency, relative to another currency, group of currencies. Since it is relative to other currency so internal price remains unchanged. It causes a country's exports to become less expensive and imports more expensive. Devaluation is monetary policy tool used by countries that have a fixed exchange rate or semi fixed exchange rate. It is often confused with Depreciation and is the opposite of revaluation.

2. The supply-side economics lays greater emphasis on the point of view of
 (a) producer (b) global economy
 (c) consumer (d) middle-man

Ans. (a) Supply side economics lays greater emphasis on the point of view of the producer whereas the demand side economics lays emphasis on the interest of the consumer.

3. The price at which the Government purchase foodgrains for maintaining the public distribution system and for building up buffer stocks are known as
 (a) Minimum support prices (b) Procurement prices
 (c) Issue prices (d) Coiling prices

Ans. (b) The price at which the Government purchases foodgrains for maintaining the public distribution system and for building up buffer stocks are known as procurement prices. Minimum support price: It is a form of market Intervention by Govt. of India to insure agricultural producers against any sharp fall in farm price. M.S.P. are announced by Govt of India. Issue price : It is the price at which shares are offered to retail investors in IPO issue.

4. Which one of the following agencies of Indian Government implements the Price Support Scheme (PSS)?
 (a) FCI
 (b) NAFED
 (c) Agriculture pricing agency of India
 (d) None of the above

Ans. (b) In Order to help the farmers in getting remunerative prices for their produce with a view to encourage higher investment and as also to increase production and productivity of a commodity, the government declares Minimum Support Price (MSPs) for 23 notified agricultural commodities for each Kharif & Rabi crop season. National Agricultural cooperative Marketing Federation of India Ltd (NAFED) is one of the Central Nodal Agencies which implements PSS.

5. Who recommends the MSP and issue prices?
 (a) Ministry of agriculture
 (b) Planning commission
 (c) Commission for Agricultural Costs and Prices
 (d) NABARD

Ans. (c) CACP was set up in 1985 and recommends for MSP, issue prices as well as procurement prices.

6. The base of Consumer Price Index for Industrial Workers has been shifted from 1982 to—
 (a) 1995 (b) 1998
 (c) 2000 (d) 2001

Ans. (d) The base of CPI for industrial worker is being shifted from 1982 to 2001.

7. With reference to India, consider the following statements:
[CDS-2010]

- The Wholesale Price Index (WPI) in India is available on a monthly basis only.
 - As compared to Consumer Price Index for Industrial Workers (CPIIW), the WPI gives less weight to food articles.
- Which of the statements given above is/are correct?
 (a) 1 only (b) 2 only
 (c) Both 1 and 2 (d) Neither 1 nor 2

Ans. (b) After the Abhijit Sen committee's proposals in 2004-05, the government had approved the proposal to release wholesale price based inflation data on a monthly basis, instead of every week. The base year was changed to 2004-05 from 1993-94. However data on primary and fuel items was continued to release on a weekly basis. Consumer Price Index food group has a weight of close to 50 percent as compared to the combined weight of 39.06 percent (food articles and Manufactured food products) in wholesale Price Index food basket.

8. Which of the following would cause the aggregate demand curve to shift to the right?
 (a) an increase in purchases by the federal government
 (b) an increase in real interest rates
 (c) an appreciation of the American dollar
 (d) a decrease in the money supply

Ans. (a) An increase in purchase by the federal Gov. causes the aggregate demand curve to shift to the right.

9. Which of the following statements is true about supply-side economics?
 (a) The main change made by the tax laws of 1981 and 1986 was to increase marginal tax rates in order to balance the budget
 (b) The Laffer Curve says that, if marginal tax rates fall, tax revenues will rise, and the budget deficit will decrease
 (c) If the tax laws of 1981 and 1986 had had their intended effect, consumption would have risen, causing an increase in both real GDP and in the price level
 (d) All of these

Ans. (b) The Laffer Curve says that, if marginal tax rates fall, tax revenues will rise, and the budget deficit will decrease. Supply side economics is a macro economic theory that gives economic growth can be most effectively created by investing in capital and by lowering barriers on the production of goods and services.

10. Which of the following is not a 'Public Good'?

[CDS-2016-I]

- (a) Electricity (b) National Defence
(c) Light House (d) Public Parks

Ans. (a) Electricity is not public good but it is club good including roads, bridges, gas, sewage, wires, telecom.

11. What is meant by price discrimination? [CDS-2015-II]

- (a) Increase in price of a commodity over time
(b) A situation where the same product is sold to different consumers for different prices
(c) Subsidization of a product by the Government to sell it at a lower price
(d) General decrease in price of a commodity over time

Ans. (b) When different consumers pay different prices for the same product, this situation is known as price discrimination.

12. What is meant by 'Public Good'? [CDS-2015-II]

- (a) A commodity produced by the Government
(b) A commodity whose benefits are indivisibly spread among the entire community
(c) A Government scheme that benefits the poor households
(d) Any commodity that is very popular among general public

Ans. (b) Public good means a commodity or service which is given without profit to everyone in a society by government or any organisation.

13. In view of the fact that kerosene is an inferior good in India, what is/are its implication(s)?

1. As households get richer, they consume less kerosene.
2. Over time there is a decline in quality of kerosene.
3. Government needs to stop subsidies on kerosene.

Select the correct answer using the code given below.

[CDS-2015-II]

- (a) 1 only (b) 1 and 2 only
(c) 2 and 3 only (d) 1, 2 and 3

Ans. (a) Generally Kerosene is used as fuel by the poor, as they get prosperity, they use little of this fuel.

14. Brent index is associated with [CDS-2011-II]

- (a) crude oil prices (b) copper future prices
(c) gold future prices (d) shipping rate index

Ans. (a) Brent Crude is a major trading classification of sweet light crude oil that serves as a major benchmark price for purchases of oil worldwide. Brent Crude is extracted from the North Sea and comprises Brent Blend, Forties Blend, Oseberg and Ekofisk crudes. The Brent Crude oil marker is also known as Brent Blend, London Brent and Brent petroleum. The index represents the average price of trading in the 25 day Brent Blend, Forties, Oseberg, Ekofisk (BFOE) market in the relevant delivery month as reported and confirmed by the industry media.

15. Which one among the following is a fixed cost to a manufacturing firm in the short run? [CDS-2013-I]

- (a) Insurance on buildings
(b) Overtime payment to worker
(c) Cost of energy
(d) Cost of raw materials

Ans. (a) In the short run insurance premium are fixed costs because they are independent of the level of production.

16. The income elasticity of demand for inferior goods is [CDS-2013-II]

- (a) less than one (b) less than zero
(c) equal to one (d) greater than one

Ans. (b) Inferior goods have a negative (less than 0) income elasticity of demand meaning that demand falls as income rises.

17. The average fixed cost curve will always be [CDS-2013-II]

- (a) a rectangular hyperbola
(b) a downward sloping convex to the origin curve
(c) a downward sloping straight line
(d) a U-shaped curve

Ans. (a) Total fixed costs are constant, so the average fixed cost curve diminishes with the output. Thus, the average fixed cost curve is a rectangular hyperbola.

18. If the average total cost is declining then [CDS-2013-II]

- (a) the marginal cost must be less than the average total cost
(b) total cost must be constant
(c) the average fixed cost curve must be above the average variable cost curve
(d) the marginal cost must be greater than the average total cost

Ans. (a) When marginal cost is less than average cost, average cost must be falling. When marginal cost exceeds average cost must be rising. The marginal cost and average cost curves are related to each other.

19. Which of the following statements is/are true? [CDS-2014-II]

1. If increase in demand and supply are of equal magnitude, the price will remain unchanged, but the equilibrium quantity will increase.
2. If increase in demand is of greater magnitude than increase in supply, both equilibrium price and equilibrium quantity will increase.
3. If increase in supply is of greater magnitude than increase in demand, equilibrium price will fall but equilibrium quantity will increase.

Select the correct answer using the code given below :

- (a) 1 only I (b) 1 and 2 only
(c) 2 and 3 only (d) 1, 2 and 3

Ans. (d)

20. Which of the following statements are correct? [CDS-2014-II]

1. When marginal revenue is positive, total revenue increases with increase in output.
2. When marginal revenue is zero, total revenue is maximum.
3. When marginal revenue becomes negative, total revenue falls with increase in output.

Select the correct answer using the code given below:

- (a) 1 and 2 only (b) 2 and 3 only
(c) 1 and 3 only (d) 1, 2 and 3

Ans. (d)

21. Demand for a commodity refers to [CDS-2015-I]
 (a) Desire for that commodity
 (b) Need for that commodity
 (c) Quantity demanded of that commodity
 (d) Quantity demanded at certain price during any particular period of time

Ans. (d) The demand for a commodity at a given price is the quantity that will be purchased at a unit of time and at a unit price. Demand has the following features; Demand refers to the quantity at a given price, Demand must be defined per unit time.

22. An exceptional demand curve is one that slopes [CDS-2015-I]
 (a) downward to the right (b) upward to the right
 (c) horizontally (d) upward to the left

Ans. (b) When the curve slopes downwards from left to right; higher prices reduce the quantity demanded.

23. Rise in the price of a commodity means [CDS-2015-I]
 (a) rise in the value of currency only
 (b) fall in the value of currency only
 (c) rise in the value of commodity only
 (d) fall in the value of currency and rise in the value of commodity

Ans. (b) When the price level rises, each unit of currency buys fewer goods and services. So rise in the price of a commodity means fall in the value of currency only.

24. A closed economy is an economy in which [MPPSC 2017-I]
 (a) the money supply is fully controlled
 (b) deficit financing takes place
 (c) only exports take place
 (d) neither exports nor imports takes place

Ans. (d) A closed economy has no trade activity with outside economies. A closed economy is self-sufficient, which means no imports come into the country and no exports leave the country. The purpose of a closed economy is to provide domestic consumers with everything they need from within the country's borders.

25. Despite being a high saving economy, capital formation may not result in significant increase in output due to [IAS Prelims-2017]
 (a) weak administrative machinery
 (b) illiteracy
 (c) high population density
 (d) high capital-output ratio

Ans. (d) Capital Output Ratio (ICOR) measures the percentage increase in capital formation required obtaining a percentage increase in GDP. Entrepreneurs, by investing their own savings and informally mobilizing the savings of their friends and relatives contribute to the process of capital formation. These informal funding supplements the funds made available by the formal means of raising resources from banks, financial institutions and capital markets. So, "D" is the fitting option- if capital to output ratio is high then capital formation may not result in significant increase in the output.

26. Surge pricing takes place when a service provider
 (a) raises the price of its product or service as demand outstrips supply

- (b) follows preset prices immune to demand and supply dynamics
 (c) fixes a minimum price for its services
 (d) fixes an average price on the basis of transactions carried over a day

Ans. (a) Surge pricing occurs when a company raises the price of its product or service if there is an increase in demand and lowers prices when demand is weak.

27. Which one of the following is not an assumption in the law of demand? [CDS 2019-I]
 (a) There are no changes in the taste and preferences of consumers.
 (b) Income of consumers remains constant.
 (c) Consumers are affected by demonstration effect.
 (d) There are no changes in the price of substitute goods.

Ans. (c) The law of demand is applicable with the following assumptions. (1) No change in price of related commodities. (2) No change in income of the consumer. (3) No change in taste and preferences, customs, habit and fashion of the consumer. (4) No change in size of population. (5) No expectation regarding future change in price.

28. Which one of the following statements is not correct. [CDS 2019-I]
 (a) When total utility is maximum, marginal utility is zero.
 (b) When total utility is decreasing marginal utility is negative
 (c) When total utility is increasing, marginal utility is positive.
 (d) When total utility is maximum, marginal and average utility are equal to each other.

Ans. (d) When total utility is maximum, marginal utility is zero and it is not equal to average utility.

29. When some goods or productive factors are completely fixed in amount, regardless of price, the supply curve is [CDS 2019-I]
 (a) horizontal
 (b) downward sloping to the right
 (c) vertical
 (d) upward sloping to the right

Ans. (a) Some goods or productive factors are completely fixed in amount, regardless of price. There is only one Mona Lisa by da Vinci. Nature's original endowment of land can be taken as fixed in amount. In this case, the supply curve is always horizontal.

30. Consider the following statements
 1. The weightage of food in Consumer Price Index (CPI) is higher than that in Wholesale Price Index (WPI).
 2. The WPI does not capture changes in the prices of services, which CPI does.
 3. Reserve Bank of India has now adopted WPI as its key measure of inflation and to decide on changing the key policy rates. [IAS Prelims 2020]

Which of the statements given- above is/are correct ?

- (a) 1 and 2 only (b) 2 only
 (c) 3 only 4, (d) 1, 2 and 3

Ans. (a)

Under the new monetary policy Framework effective since 2016, RBI tries to control inflation at 2-6% of CPI (All India). So, #3 is wrong. Option c and d eliminated. In both (a & b) the options, statement#2 is common so we have to accept #2 as correct. Even without checking. Everything boils down to whether statement#1 is correct or not?

Both WPI and CPI are based on Laspeyres formula wherein weightage is assigned to multiple commodities and their prices are tracked. The weight of an individual commodity depends on how frequently it is bought by the consumer. So obviously consumer price index would be giving more weightage to the food products compared to WPI which is aimed at the manufacturers. So, #1 should be correct.

31. In economics, if a diagram has a line passing through the origin and has 45° angle with either axis and it is asserted that along the line $X = Y$, what is tacitly assumed?

[CDS 2020-I]

- (a) Both variables are pure numbers.
- (b) Both variables are in the same unit.
- (c) Both variables are in different units.
- (d) At least one variable is a pure number.

Ans. (b) Because the function is increasing, the slope must be positive. An angle of 45 degrees means that the values of x equal the values of y. To find the slope of a straight line use this equation $M(\text{slope}) = (Y_2 - Y_1)/(X_2 - X_1)$, and as before $X_1 = Y_1$ and $X_2 = Y_2$. Depending on the previous information, the slope is 1.

Profit & Loss/Recession & Depression

1. Who among the following has suggested migration to accrual accounting system from cash based accounting system in India?
- (a) I.V. Reddy
 - (b) D.N. Ghosh
 - (c) R.H. Patil
 - (d) C. Rangarajan

Ans. (d)

2. Consider the following actions by the Government:
1. Cutting the tax rates.
 2. Increasing the government spending.
 3. Abolishing the subsidies.
- In the context of economic recession, which of the above actions can be considered a part of the 'fiscal stimulus' package?
- (a) 1 and 2 only
 - (b) 2 only
 - (c) 1 and 3 only
 - (d) 1, 2 and 3

Ans. (a) Fiscal stimulus : Government measures, normally involving increased public spending and lower taxation are aimed at giving a positive jolt to economic activity.

3. Which one of the following terms is used in Economics to denote a technique for avoiding a risk by making a counteracting transaction?
- [CDS-2016-I]
- (a) Dumping
 - (b) Hedging
 - (c) Discounting
 - (d) Deflating

Ans. (b) Hedging is used in limiting or offsetting probability of loss from fluctuations in the prices of commodities, currencies or securities.

4. Which of the following is measured by the Lorenz curve?
- [UPPSC 2018]
- (a) Illiteracy
 - (b) Unemployment
 - (c) Population growth rate
 - (d) Inequality of Income

Ans. (d) Inequality of Income is measured by the Lorenz curve. In economics, the Lorenz curve is a graphical representation of the distribution of income or of wealth. It was developed by Max O. Lorenz in 1905 for representing inequality of the wealth distribution.

DIRECTIONS : The following item consists of two statements, Statement I and Statement II. Examine these two statements carefully and select the correct answer using the code given below.

5. **Statement I :** There has been a sharp decline in savings rate in Indian economy between 2007-2008 to 2015-2016.
Statement II : There has been a fall in household and public savings.

[CDS 2018-II]

Code:

- (a) Both the statements are individually true and Statement II is the correct explanation of Statement I
- (b) Both the statements are individually true but Statement II is not the correct explanation of Statement I
- (c) Statement I is true but statement II is false
- (d) Statement I is false but Statement II is true

Ans. (a) There has been a sharp decline in savings rate in Indian economy between 2007-2008 to 2015-2016. The household savings rate could remain stagnant or even decline as financial liabilities increase with greater retail credit penetration.

Market, Factors of Production & Inflation

1. Inflation is caused by
- (a) Increase in supply of goods
 - (b) Increase in cash with the government
 - (c) Decrease in money supply
 - (d) Increase in money supply

Ans. (d) Inflation is increased in the prices of commodities. It is caused due to decrease in supply and increase in demand of commodities. So when money supply in the economy increases it means people have more purchasing capacity and thus demand increases which results in inflation.

Some factors affecting inflationary pressure.

(i) Rising Property prices	→	Increased consumer wealth	→	Demand pull inflation risk
(ii) Increasing world oil price	→	High cost for Business	→	Cost pull inflation risk
(iii) Depreciatry exchange rate	→	Increased import price+rising export	→	Cost push and Demand pull inflation risk

2. The process of curing inflation by reducing money supply is called
- (a) Cost-push inflation
 - (b) Down-pull inflation/Demand pull inflation
 - (c) Disinflation
 - (d) Reflation

Ans. (c) The process of curing inflation by reducing money supply is called disinflation. Disinflation is a decrease in the rate of inflation – a slowdown in the rate of increase of the price level of goods and services in GDP.

Cost pull inflation - It is caused by an increase in prices of inputs like Labour, raw material etc. The increased price of the factors of production leads to the decreased supply of Goods.

Demand pull inflation - It is asserted to rise when Aggregate demand in an economy outpaces aggregate supply. It involves inflation rising as real GDP rises and unemployment falls.

3. The term stagflation refers to a situation where
- growth has no relation with the change in price
 - rate of growth and prices both are decreasing
 - rate of growth is faster than the rate of price increase
 - rate of growth is slower than the rate of price increase

Ans. (d) Stagflation occurs when the economy isn't growing but prices are increasing, which is not a good situation for a country to be in.

Stagflation - Persistent high inflation combined with high unemployment and stagnant demand in a country's economy.

4. During period of inflation, interest, rates should
- Increase
 - Decrease
 - Remain constant
 - Fluctuate

Ans. (a) During inflation interest rates should increase so that the investor invests more in lieu of higher interest earning thus money supply reduce which can reduce inflation. Similarly higher interest rates means credit becomes costly so that again supply of money reduces which helps in curbing inflation.

5. In the parlance of economy / commerce, what is 'Gilt-edged market'?
- Gold and Silver market
 - Industrial securities market
 - Market of safe securities
 - Market of software technology products

Ans. (c) In the parlance of economy, Gilt-edged market is called market of safe securities. "Gilt-edged" denotes high-grade securities, consequently carrying low yields.

6. Inflation in India is measured on which of the following indexes / indicators?
- Cost of Living Index (CLI)
 - Consumer Price Index (CPI)
 - Gross Domestic Product (GDP)
 - Wholesale Price Index (WPI)

Ans. (b) Cost of Living Index - It is a theoretical price index that measures relative cost of living over time or regions.

Consumer Price Index - It is a measure that examines the weightest average of prices of a basket of consumer goods & services such as transportation food and medical care.

7. When the prices of commodities, goods and services start declining consistently, the phenomenon is known as
- Discount field
 - Deflation
 - Negative growth
 - Market capitalism

Ans. (b) When the prices of commodities, goods and services start declining consistently, the phenomenon is known as deflation. Deflation is because of fall in the aggregate level of demand. That is, there is a fall in how much the whole economy is willing to buy and the price for goods.

Negative Growth - It refers to a contraction in business sales or earning. It is also used to refer to a contraction in country's economy as evidenced by a decrease in its GDP during any quarter of a given year.

Market Capitalism - An economic system which supports private enterprise within a free market, the means of production being privately owned.

8. The basis of determining dearness allowance (D.A.) to government employees in India is
- National income
 - Consumer Price Index
 - Standard of living
 - Per capita income

Ans. (b) The basis of determining dearness allowance (D.A.) to government employees in India is consumer price index. Dearness Allowance (DA) is an allowance paid to employees to compensate them for erosion of real income / wage due to inflation. The increase in the cost of living and the consequent erosion of income is measured in terms of a consumer price index number and, DA to be sanctioned to employees is determined on the basis of the percentage increase in that index.

Dearness Allowance - D.A. is calculated as a percentage of an Indian citizen's basic salary to mitigate the impact of inflation on people.

9. Economic growth is usually coupled with
- Deflation
 - Inflation
 - Hyper inflation
 - Stagflation

Ans. (b) With increase in GDP, aggregate demand increases, because more production means people have more disposable income, which means more consumer spending. As a result, prices rise in response, and in conclusion because aggregate demand grows faster than long-term aggregate supply, economic growth will be coupled with inflation.

Hyper inflation - In economic, hyper inflation occurs when a country experience very high and usually actuarially rates of inflation. Economic growth is usually coupled with inflation.

10. Consider the following statements in regard to money market in India:

- It is a market for short-term funds with maturity ranging from overnight to one year.
- It acts as an instrument of liquidity adjustment for the Central Bank.

Which of the statements given above is/are correct?

- 1 only
- 2 only
- Both 1 and 2
- Neither 1 nor 2

Ans. (c) The money market consists of financial institutions and dealers in money or credit who wish to either borrow or lend. Participants borrow and lend for short periods of time, typically up to twelve months. Money market trades in short-term financial instruments commonly called "paper."

11. Which of the following can be the outcome(s) of very high inflation in the economy?
- Reduction in economic growth
 - Increase in savings
 - Reduction in exports
- Select the correct answer using the codes below :
- 1 and 2 only
 - 3 only
 - 2 and 3 only
 - 1 and 3 only