

2019

ECONOMICS — HONOURS

Paper : CC - 3

Full Marks : 65

The figures in the margin indicate full marks.

*Candidates are required to give their answers in their own words
as far as practicable.*

SECTION - A

1. Answer **any ten** questions :

2×10

- (a) What will be the impact on GDP if a consumer decides to buy a refrigerator made in South Korea rather than one made in India?
- (b) Explain why Balanced Budget Multiplier is unity.
- (c) What is meant by 'liquidity trap'?
- (d) What is the full-employment budget surplus?
- (e) State whether the following statement is true or false and give reasons for your answer :

“For a country where GNP exceeds GDP, we find that the residents of that country are earning less abroad than the foreigners are earning in that country.”

(f) In the following hypothetical economy :

GDP	₹ 7,000
Gross Investment	₹ 800
Net Investment	₹ 550
Consumption	₹ 4,500
Government purchase of goods	₹ 1,100
Budget surplus	₹ 30

Find disposable income.

- (g) What is GDP deflator?
- (h) What components of GDP (if any) would each of the following transactions affect? Explain.
- (i) The Central Government of India repaves NH31.
- (ii) Your parents buy a car from Volkswagon, a German company.

Please Turn Over

- (i) Why is imputed rental income of owner occupied housing included in GDP and not the market value of the house itself?
- (j) Differentiate between stock variables and flow variables citing examples.
- (k) State and explain what will happen if $MPC > 1$ in SKM.
- (l) Suppose the economy is operating at equilibrium with $y_0 = 1000$. If the government undertakes a fiscal change so that the tax rate 't' increases by 0.05 and government spending increases by 50, will the budget surplus increase or decrease? Why?
- (m) What effect does an increase in money supply produce in the classical model?
- (n) What is the difference between MEC and MEI?
- (o) What will be the impact on rental price of capital, cost of capital and investment if anti-inflationary monetary policy raises the interest rate?

SECTION - B

2. Answer *any three* questions :

- (a) Why do we call mechanisms such as proportional income taxes "automatic stabilizer"? Explain how and why it affects fluctuations in output. 2+3
- (b) When the present value of future return stream (discounted at the market rate of interest) of a certain investment project is just equal to the present cost, how is the "marginal efficiency of capital" related to the rate of interest? Explain. 5
- (c) Explain saving-investment gap and its relation with budget deficit. 5
- (d) Explain paradox of thrift. 5
- (e) Is Say's law consistent with Quantity Theory of Money? Explain with arguments. 5

SECTION - C

Answer *any three* questions.

3. Suppose we have an economy described by the following equations :

$$C = 100 + 5 Y_d$$

$$I = 50 + 0.1 Y$$

$$G = 100$$

$$T = 0.2 Y$$

where C = Consumption, Y_d = Disposable Income, I = Investment, G = Government Expenditure, T = Tax, Y = National Income.

Find out equilibrium values of Y , I , C and government budget deficit. How will an increase in the tax rate from 0.2 to 0.3 affect aggregate domestic savings? Can you call this result 'Paradox of thrift'?

6+3+1

4. Explain the impact of real interest rate on housing demand, housing price and residential investment. 2+2+6

5. Suppose there are two groups of people in an economy, with their respective consumption function as

$$C_A = 100 + 0.5 Y_A$$

$$C_B = 150 + 0.75 Y_B$$

Planned investment 200. Where C_i and Y_i are respectively consumption and income levels for the i th group (for all $i = A, B$). Suppose each group gets 50% of total GDP in the economy. Determine the equilibrium level of income. Considering the equilibrium income as the initial income, a lumpsum tax T is imposed on Group A and the same amount is given as a transfer to Group B. Now determine planned consumption, planned savings, planned aggregate demand and actual investment at the initial level of equilibrium. 2+2+2+2+2

6. (a) Consider the police force of a country. Its job is to maintain law and order of the country. Suppose that in a given year it spent ₹ 10 lakh interest on its outstanding loan, ₹ 20 lakh in wages and salaries, ₹ 10 lakh on stationery, fuel, power and acquired buildings, equipment and cars worth ₹ 30 crore. What is its GVA in a given year? Did it contribute anything to G and transfer payments of government administration and defence? Explain.

- (b) Suppose that in a given year in a closed economy with government, private and public sector enterprises produced goods and services worth ₹ 10 lakhs i.e., their aggregate GVA in the given year was ₹ 10 lakhs. They sold in the same year goods and services of ₹ 8 lakhs to households and ₹ 5 lakhs to government administration and defence. Besides, government administration and defence paid ₹ 10 lakhs in wages and salaries and ₹ 1 lakh in interest to households. What is the aggregate gross investment of the firms in the given year? Calculate GDP of the economy by the expenditure method. (2+3) + (2+3)

7. (a) Explain the impact of

(i) shift in the supply schedule of labour

(ii) shift of the production function upwards on the equilibrium values in the classical model.

- (b) How will the equilibrium values be affected if the wages are rigid?

6+4