UNIT 2: ECONOMIC THEORY

REMEMBER

1. What is the primary focus of macroeconomics?
   A. Individual incomes
   B. National or global economy as a whole
   C. Micro-level market dynamics
   D. Individual market demand and supply

2. According to John Maynard Keynes, macroeconomics deals primarily with:
   A. Individual incomes
   B. National income and expenditure
   C. Microeconomic variables
   D. Market structures

3. What is the formula for calculating National Income using the Output Method (Production Approach)?
   A. Gross Output + Intermediate Consumption
   B. Gross Output - Intermediate Consumption
   C. Gross Output x Intermediate Consumption
   D. Gross Output / Intermediate Consumption

4. Which of the following measures the total economic output produced by a country's residents, whether they are located within the country's borders or abroad?
   A. GDP
   B. GNP
   C. NNP
   D. NDP

5. Microeconomics primarily focuses on the behaviour of:
   A. National economies
   B. Individual economic units
   C. Global markets
   D. Government policies

6. What does the law of demand state?
   A. Higher prices lead to higher quantity demanded
   B. Lower prices lead to lower quantity demanded
   C. Higher prices lead to lower quantity demanded
   D. Prices have no effect on quantity demanded

7. What is the primary assumption of the theory of demand?
   A. Ceteris Paribus

B. Rationality
C. Diminishing Marginal Utility
D. Income elasticity

8. Which scenario is an exception to the law of demand?
A. Giffen Goods
B. Normal goods
C. Luxury goods
D. Inferior goods

9. When is demand considered to be elastic?
A. When the elasticity is greater than 1
B. When the elasticity is less than 1
C. When the elasticity is exactly 1
D. When the elasticity is zero

10. What does perfectly inelastic demand imply?
A. Quantity demanded changes with any price change
B. Quantity demanded remains constant regardless of price changes
C. Quantity demanded is infinitely responsive to price changes
D. Quantity demanded is not influenced by income changes

11. What does the law of supply state?
A. As the price of a good increases, the quantity demanded increases.
B. As the price of a good increases, the quantity supplied decreases.
C. As the price of a good increases, the quantity supplied also increases.
D. As the price of a good decreases, the quantity demanded increases.

12. What does the term "ceteris paribus" imply in the theory of supply?
A. All factors are in constant flux.
B. Factors other than price remain constant.
C. Price is the only factor considered.
D. Producers have complete control over all variables.

13. Which market classification involves trade between different countries?
A. National Market
B. Local Market
C. International Market
D. Global Market

14. In perfect competition, what type of products do firms sell?
A. Homogeneous products
B. Differentiated products

C. Unique products
D. Rare products

15. According to the law of diminishing marginal utility, what happens as a person consumes more units of a good?
A. Additional satisfaction from each unit increases.
B. Additional satisfaction from each unit remains constant.
C. Additional satisfaction from each unit tends to decrease.
D. Additional satisfaction becomes unpredictable.

16. What market structure involves a single seller dominating the entire market?
A. Monopoly
B. Perfect Competition
C. Oligopoly
D. Monopolistic Competition

17. What is the elasticity of supply if a relatively small change in price leads to a proportionally larger change in the quantity supplied?
A. Perfectly Elastic Supply
B. Unitary Elastic Supply
C. Elastic Supply
D. Inelastic Supply

18. How do producers respond to changes in market conditions according to the theory of supply?
A. Irrationally
B. Emotionally
C. Logically and rationally
D. Indifferently

19. What is the fundamental concept that measures how responsive the quantity supplied is to changes in price?
A. Law of Supply
B. Market Equilibrium
C. Elasticity of Supply
D. Marginal Utility

20. What type of market structure serves as a benchmark for evaluating other market structures?
A. Monopoly
B. Perfect Competition
C. Oligopoly

D. Monopolistic Competition

UNDERSTAND

1. What distinguishes the law of supply from the law of demand?
   A. Their impact on market equilibrium
   B. Direction of the relationship between price and quantity
   C. Their reliance on ceteris paribus
   D. Their influence on producer behavior

2. Which factor does the theory of supply assume to be constant, similar to the assumption in the theory of demand?
   A. Production technology
   B. Market demand
   C. Government policies
   D. Consumer preferences

3. How does a very short period differ from a short period in market analysis?
   A. Flexibility of prices
   B. Ability to adjust production levels
   C. The extent of the fixed factors of production
   D. Consumer preferences

4. In which market structure do firms have no control over the market price and accept the prevailing market price?
   A. Monopoly
   B. Perfect Competition
   C. Oligopoly
   D. Monopolistic Competition

5. What does the law of diminishing marginal utility explain about consumption?
   A. The total satisfaction derived from consuming a good
   B. The change in consumer preferences over time
   C. The diminishing satisfaction from consuming additional units of a good
   D. The indifference in consumer choices

6. Which market classification involves trade between different countries but does not specify whether goods are being imported or exported?
   A. International Market
   B. National Market
   C. Global Market
   D. Local Market

7. What situation leads to perfectly inelastic supply in a market?

A. When supply is highly responsive to price changes
B. When producers can supply any quantity at a given price
C. When the supply curve is horizontal
D. When supply remains constant regardless of price changes

8. What does the principle of equal marginal utility per rupee represent?
A. Consumers buy goods with the highest utility
B. Consumers allocate their spending to maximize total utility
C. Consumers spend equally on all goods and services
D. Consumers derive equal satisfaction from each unit of a good

9. What market structure involves non-price competition and strategic interactions among a small number of firms?
A. Monopoly
B. Perfect Competition
C. Oligopoly
D. Monopolistic Competition

10. What does the elasticity of supply measure?
A. Responsiveness of quantity demanded to changes in price
B. Responsiveness of quantity supplied to changes in price
C. Responsiveness of price to changes in quantity supplied
D. Responsiveness of demand to changes in quantity

11. What term is used to describe the situation when producers expect future prices to rise and reduce current supply?
A. Demand shift
B. Price expectation
C. Supply curve shift
D. Speculative production

12. In perfect competition, why do firms earn zero economic profits in the long run?
A. Due to government regulations
B. Because of constant changes in market prices
C. Competition erodes above-average profits
D. Consumer preferences change rapidly

13. Which market classification involves a market that serves a specific geographic area like a neighbourhood or town?
A. Global Market
B. National Market
C. International Market

D. Local Market

14. How does the law of supply differ from the law of demand regarding price and quantity relationship?
A. They both have an inverse relationship between price and quantity
B. The law of supply has a direct relationship, while the law of demand has an inverse relationship
C. Both laws show a direct relationship between price and quantity
D. They both remain constant regardless of price changes

15. What is the primary factor influencing a market to be categorized as perfectly competitive?
A. Product differentiation
B. Price control by the dominant firm
C. A large number of buyers and sellers
D. Government intervention

16. What role does the concept of marginal utility play in consumer behavior?
A. Determines the total utility derived from consumption
B. Identifies the price of goods in the market
C. Influences the choice and quantity of goods consumed
D. Represents the average utility of goods

17. Which factor leads to an increase in the quantity supplied at all price levels, shifting the supply curve to the right?
A. Government intervention
B. Input prices decrease
C. Technological advancements
D. Consumer preferences change

18. How do rational consumers make consumption decisions based on marginal utility theory?
A. By allocating income equally to all goods
B. By spending all income on a single good
C. By maximizing total utility per rupee spent
D. By focusing on reducing costs

19. What distinguishes a very short period from a short period in market analysis?
A. Flexibility in adjusting production levels
B. Changes in consumer preferences
C. The extent of fixed production factors
D. Market price fluctuations

20. What factor influences the elasticity of supply in a market?
A. Government regulations
B. Changes in consumer preferences
C. Price fluctuations
D. Capacity to adjust production quickly

APPLY

1. How might a government intervention disrupt the typical relationship between price and quantity supplied in a market?

20 MCQs

1
M

A. By reducing production costs
B. By imposing taxes or subsidies
C. By encouraging technological advancements
D. By promoting competition

2. Suppose a technological advancement reduces the cost of production for a specific good. What impact would this likely have on the supply curve?
A. Shift to the left
B. No impact on the supply curve
C. Shift to the right
D. Cause a vertical supply curve

3. In what scenario would the price elasticity of supply be relatively high?
A. A situation of perfectly inelastic supply
B. A situation of perfectly elastic supply
C. A situation of unitary elastic supply
D. A situation of perfectly competitive supply

4. How might a natural disaster impact the supply of goods in a market?
A. Increase the quantity supplied at higher prices
B. Decrease the quantity supplied at higher prices
C. Cause a shift in the demand curve
D. Result in a perfectly elastic supply

5. Imagine a scenario where a monopolistic competitive market expands due to new firms entering. What would this most likely result in?
A. An increase in market equilibrium price
B. A decrease in market equilibrium price
C. No change in market equilibrium price
D. A shift in the demand curve

6. How might a sudden increase in raw material prices impact the supply curve?
A. Shift to the left
B. Shift to the right
C. No impact on the supply curve

D. Cause a vertical supply curve

7. In a perfectly competitive market, if a firm is earning economic profits in the short run, what would be the most likely response of other firms in the market?

A. Increase production to match the profits
B. Exit the market due to losses
C. Cut prices to attract more customers
D. Invest in research and development

8. Suppose a firm anticipates future increases in input prices. How might this affect its current supply behavior?

A. Increase current supply to offset future costs
B. Decrease current supply to manage costs
C. Keep supply constant to match future prices
D. Exit the market temporarily

9. What strategic move might a duopoly adopt to maintain market dominance?

A. Lower prices to attract more consumers
B. Collaborate to set uniform prices
C. Increase production to flood the market
D. Adopt aggressive marketing strategies

10. How might a monopolistic competitive market respond to an increase in consumer preferences for a specific product?

A. Decrease product differentiation
B. Increase the number of substitute products
C. Increase advertising to gain market share
D. Reduce market competition

11. If a local market experiences a sudden influx of new buyers, what would be the expected impact on market equilibrium?

A. Equilibrium price decreases, quantity increases
B. Equilibrium price increases, quantity decreases
C. Equilibrium price and quantity both increase
D. Equilibrium price and quantity both decrease

12. How might an increase in international trade barriers affect the market for a specific good?

A. Shift the supply curve to the right
B. Increase consumer demand for the good
C. Limit the quantity supplied in the market
D. Encourage technological advancements

13. In a perfectly competitive market, what would a sudden increase in consumer income most likely result in?
   A. An increase in market equilibrium price
   B. A decrease in market equilibrium price
   C. No change in market equilibrium price
   D. A shift in the supply curve

14. How might an increase in the number of sellers in an oligopolistic market affect market equilibrium?
   A. Increase equilibrium price and quantity
   B. Decrease equilibrium price and quantity
   C. No impact on equilibrium price but increase in quantity
   D. No impact on equilibrium price or quantity

15. If a market experiences a surge in demand due to a sudden trend, what strategy might firms adopt to maintain supply?
   A. Invest in market research
   B. Reduce production to meet demand
   C. Increase prices to limit demand
   D. Invest in expanding production capacity

16. How might a sudden increase in consumer preferences for organic products impact the supply curve for organic goods?
   A. Shift to the left
   B. Shift to the right
   C. No impact on the supply curve
   D. Cause a vertical supply curve

17. In a perfectly competitive market, if demand suddenly decreases due to changing preferences, what is the likely response of firms?
   A. Increase advertising efforts
   B. Exit the market due to losses
   C. Lower prices to stimulate demand
   D. Invest in product diversification

18. How might a sudden increase in export opportunities impact the supply curve in a national market?
   A. Shift to the left
   B. Shift to the right
   C. No impact on the supply curve
   D. Cause a vertical supply curve

19. If a market experiences a sudden decrease in production technology efficiency, what would be the likely impact on the supply curve?
  A. Shift to the left
  B. Shift to the right
  C. No impact on the supply curve
  D. Cause a vertical supply curve

20. How might a sudden increase in consumer preferences for electric cars impact the supply curve for traditional gasoline-powered cars?
  A. Shift to the left
  B. Shift to the right
  C. No impact on the supply curve
  D. Cause a vertical supply curve

ANALYZE

1. How do subsidies affect supply relationships? 1
   Answer: Alter M

2. What's the impact of technological advancements on supply curves?
   Answer: Shift

3. How do changes in input prices influence supply behaviour's?
   Answer: Adjust

4. What's the strategic approach for maintaining duopoly dominance?
   Answer: Collaboration

5. What's the consequence of a sudden rise in consumer preferences in monopolistic competition?
   Answer: Advertisement

6. How does an increase in international trade barriers affect market supply?
   Answer: Limitation

7. What's the likely result of a surge in demand for a product in a market?
   Answer: Capacity

8. How do changes in consumer preferences impact organic goods' supply?
   Answer: Increase

9. What's the expected response of firms to decreasing demand in a competitive market?
   Answer: Withdrawal

10. How do sudden export opportunities affect national market supply?
    Answer: Expansion

11. What's the outcome of a decrease in production technology efficiency?
    Answer: Contraction

12. How do changes in preferences for electric cars affect gasoline-powered cars' supply?
    Answer: Decrease

13. What's the likely result of government intervention in supply dynamics?
    Answer: Disturbance

14. How do fluctuations in raw material prices affect supply behavior?
    Answer: Altered

15. What's the impact of increased sellers in an oligopolistic market on equilibrium?
    Answer: Stability

16. How does a sudden trend affect supply management strategies?
    Answer: Adaptation

17. What's the consequence of a sudden decrease in demand in a competitive market?
    Answer: Exit

18. How do sudden disruptions in production technology influence the supply curve?
    Answer: Shrinkage

19. What's the likely outcome of an increase in consumer income in a competitive market?
    Answer: Expansion

20. How does a sudden increase in consumer preferences for specific goods affect market equilibrium?
    Answer: Adjustment

EVALUATE

Set 1

1. Local Market	a) Zero Economic Profits in the Long Run
2. International Market	b) Non-price

	Competition and Strategic Interactions
3. Perfect Competition	c) Quantities Supplied and Demanded are Essentially Fixed
4. Oligopoly	d) Immediate Market
5. Very Short Period	e) Long Run

Answers: 1. d, 2. e, 3. a , 4. b, 5.c

Set 2

1. Many buyers and sellers	A. Monopolistic Competition
2. Firms have some control over pricing due to differentiation	B. Perfect Competition
3. Dominated by a single seller or producer	C. Perfect Competition
4. Market structure with a large number of buyers and sellers	D. Oligopoly
5. Characterized by a small number of large firms	E. Monopoly

Answers: 1. C, 2. A, 3. E , 4. B, 5.D

Set-3

1. Perfectly Elastic Supply	A) Quantity can be supplied at any given price
2 .Perfectly Inelastic Supply	B) Proportionally smaller change in quantity supplied
3. Unitary Elastic Supply	C) Very responsive to changes in price
4. Elastic Supply	D) Percentage change in quantity supplied equals

	price change
5. Inelastic Supply	E) Quantity supplied remains constant regardless of price

Answers: 1. B, 2. C, 3. D , 4. E, 5.A

Set-4

Question	Options
1. Theory of Demand is based on which principle?	A. Rationality
2. What is the Law of Demand?	B. Diminishing Marginal Utility
3. What concept explains consumers' choices?	C. Ceteris Paribus
4. What law explains diminishing satisfaction?	D. Inverse relationship between price & demand
5. What is assumed constant in the theory of demand?	E. All factors except price remain constant

Answers: 1. C, 2. D, 3. A , 4. B, 5. E

Set-5

Question	Options
1. According to Adam Smith market means	A. Intersection of supply & demand curves
2. perfect competition	B. Place for exchanging goods & services
3. equilibrium price results from	C. Many buyers and sellers, no market power
4. Utility according to consumers	D. Additional satisfaction from consuming one more unit
5. marginal utility refers to	E. Maximizing satisfaction within budget

Answers: 1. B, 2. C, 3. A , 4. E, 5. D

Set-6

Limitations	**Options**
1. Deals with simplified assumptions and static analysis.	A. Simplified assumptions and ceteris paribus

2. Addresses challenges of aggregation and heterogeneity.	B. Aggregation and heterogeneity
3. Focuses on individual economic units and markets.	C. Microeconomics limitations
4. Relies on ceteris paribus assumption and incomplete info.	D. Macro and Micro limitations
5. Concerned with realistic market scenarios and behavior.	E. Realistic market scenarios and behavior

Answers: 1. D, 2. B, 3. C , 4. A, 5. E

Set 7: Measurement of National Income

Measurement Methods	**Options**
1. Method focusing on production and total value of goods.	A. Expenditure Method
2. Approach involving income earned by individuals.	B. Income Components
3. Method considering total expenditures within an economy.	C. GDP and GNP

4. Examines production, intermediate consumption, and net value.	D. Output Method
5. Consider wages, interest, profits, and taxes.	E. Income Method

Answers: 1. D, 2. E, 3. A , 4. C, 5. B

Set 8: Concepts of National Income

Concepts	Options
1. Measures economic output within a country's borders.	A. GNP
2. Total value of output produced by a country's residents.	B.NDP
3. GDP plus net income earned abroad.	C. GDP
4. GDP minus depreciation on capital assets.	D. National Income at Market Prices
5. Measures income before accounting for taxes and subsidies.	E. NNP

Answers: 1. C, 2. A, 3. B , 4. E, 5. D

EVALUATE

1. Demand curve slopes downward because as price increases, quantity demanded decreases due to the law of diminishing marginal utility.
Answer: True

2. Elasticity of demand does not measure the responsiveness of quantity demanded to changes in price.
Answer: False

3. Perfectly elastic demand means that any increase in price will result in zero quantity demanded.
Answer: True

4. In a perfectly competitive market, individual firms have control over the market price.
Answer: False

5.Equilibrium price occurs when quantity demanded equals quantity supplied in the market.
Answer: True

6.A decrease in the price of a substitute good will lead to an increase in the demand for the original good.
Answer: True

7.: When demand is perfectly inelastic, consumers are unresponsive to changes in price.
Answer: True

8. If the price elasticity of supply is greater than 1, supply is considered to be inelastic.
Answer: False

9. An increase in income leads to a decrease in demand for inferior goods.
Answer: False

10. : Market equilibrium is achieved when both consumers and producers achieve maximum satisfaction and profit, respectively.
Answer: True

11. : Gross Domestic Product (GDP) does not measure the total market value of all final goods and services produced within a country in a given period.

Answer: False

12. Inflation refers to a sustained increase in the general price level of goods and services in an economy.
Answer: True

13. The Consumer Price Index (CPI) measures the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services.
Answer: True

14. If nominal GDP is $500 billion and the GDP deflator is 125, real GDP is $625 billion.
Answer: True

15. Unemployment rate is calculated by dividing the number of unemployed individuals by the total labour force.
Answer: True

16. : Deflation refers to a sustained increase in the general price level of goods and services in an economy.
Answer: False

17. Fiscal policy refers to the use of government spending and taxation to influence the economy.
Answer: True

18. Crowding out effect occurs when increased government spending leads to a decrease in private investment.
Answer: True

19. Aggregate demand do not represent the total quantity of goods and services demanded by households, firms, and the government at various price levels.
Answer:False

20. The Phillips curve illustrates an inverse relationship between inflation and unemployment.
Answer: True

CREATE

1. The _______ curve shows the various quantities of a good that consumers are willing and able to purchase at different prices.
Answer: Demand

2. The concept of _______ measures the sensitivity of quantity demanded to changes in price.
Answer: elasticity

3. In a perfectly competitive market, each firm is a _______ taker, meaning it cannot influence the market price.
Answer: price

4. Equilibrium in a market occurs when the quantity demanded equals the _______ supplied.
Answer: quantity

5. The law of diminishing _______ states that as a consumer consumes more units of a good, the additional satisfaction from each additional unit decreases.
Answer: marginal utility

6. A perfectly elastic demand curve is represented as a _______ line on a graph.
Answer: horizontal

7. The measure of responsiveness of quantity supplied to changes in price is known as _______ of supply.
Answer: elasticity

8. In a perfectly competitive market, firms can enter or exit the market without _______ the market price.
Answer: affecting

9. The point of _______ maximization occurs where marginal cost equals marginal revenue in a perfectly competitive market.
Answer: profit

10. The _______ of a good indicates the proportionate change in quantity demanded relative to a change in income.
Answer: income elasticity

11. Gross Domestic Product (GDP) measures the total _______ value of all final goods and services produced within a country in a given time period.
Answer: market

12. Inflation is a sustained increase in the general _______ level of goods and services in an economy over time.
Answer: price

13. The Consumer Price Index (CPI) measures changes in the average prices paid by _______ for a basket of goods and services.
Answer: consumers

14. Real GDP adjusts nominal GDP for changes in _______ levels, providing a more accurate measure of an economy's performance.
Answer: price

15. The unemployment rate is the percentage of the _______ force that is unemployed and actively seeking employment.
Answer: labour

16. Deflation refers to a sustained decrease in the _______ level of goods and services in an economy.
Answer: price

17. Fiscal policy uses changes in government spending and taxation to influence the _______.
Answer: economy

18. The aggregate _______ curve shows the relationship between the price level and the quantity of real GDP demanded by households, firms, and the government.
Answer: demand

19. The Phillips curve illustrates the trade-off between _______ and unemployment in an economy.
Answer: inflation

20. The GDP _______ is a measure used to convert nominal GDP into real GDP, adjusting for price changes.
Answer: deflator
