

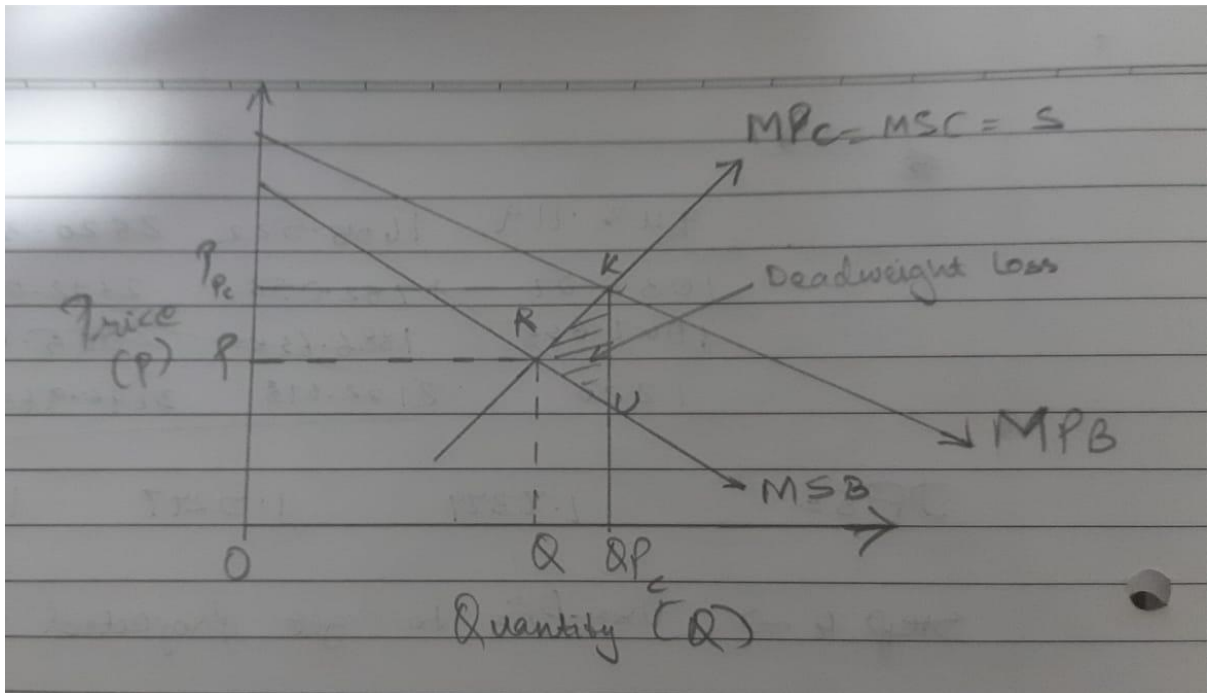
Assignment 1: Business Economics-2

1. C – If the Government raises output above the free market level, consumers will get no benefit from the extra units of output.
2. C – The gap between $S + \text{tax}$ and S will be Rs. 5 at each quantity.
3. C – Marginal revenue = marginal cost.
4. D – Cannot be supplied by the market.
5. A – Rising trade ratios for countries.
6. C – Rise and real GDP will rise.
7. B – Provide consistency with regards to taxation and subsidies.
8. C – To impose trade sanctions on countries with which it disagrees politically.
9. D – Petrol consumption involves external social costs.
10. D – Nominal GDP uses current prices; real GDP uses constant prices.
11. C – the periodic fluctuations of output around the long run trend.
12. C – Net income from abroad.
13. C – This could lead to 'black' market where the cylinders are sold at more than ceiling price.
14. C – 120 Cr.
15. D – 800 Cr.
16. C – Country X has a comparative advantage in the production of mobiles.
17. D – 280 million.
18. a. Net Domestic Income = Mixed income of the self-employed + Operating surplus + Compensation of employees = $28,000 + 10,000 + 24,000 = \text{Rs. } 62,000$ crores
b. Gross Domestic Income = Net domestic income + depreciation = $62,000 + 1,700 = \text{Rs. } 63,700$ crores
c. Net National Income = Net domestic income + net factor income from abroad = $62,000 - 300 = \text{Rs. } 61,700$ crores
19.
Usage of plastic results in wastes which is detrimental to society. Therefore usage of plastic entails social costs. For example – the transfer of plastic debris into water bodies may lead to the death of marine life. To prevent water bodies from polluting and keeping them safe for marine life, external

costs will have to be borne. Therefore, we can conclude that usage of plastic has external costs and the marginal social cost (MSC) of using plastic is greater than the marginal private cost (MPC) incurred.

However, the benefit of using plastic is greater to the user/consumer than the society. Therefore, the marginal private benefit (MPB) is greater than the marginal social benefit (MSB).

If we do not consider externalities, the market will be in an equilibrium at point K (where P_{pc} is equal to Q_{pc}). However, if we consider the socially optimum level of output, the market equilibrium will be at point R (where P equal Q). Since $MPB > MSB$ and $MSC > MPC$, there is overproduction and overconsumption of plastic. This results in deadweight welfare loss caused by overconsumption and represented by the triangle KRU in the diagram.



20.

The short-run aggregate supply curve is an upward-sloping curve that shows the quantity of total output that will be produced at each price level in the short run.

In the short run, the equilibrium price level and the equilibrium level of total output are determined by the intersection of the aggregate demand and the short-run aggregate supply curves.

In the short run, the output can be either below or above potential output. The short-run aggregate supply curve is upward sloping because the quantity supplied increases when the price rises. there is a positive correlation between the price level and output, which is shown on the short-run aggregate supply curve.

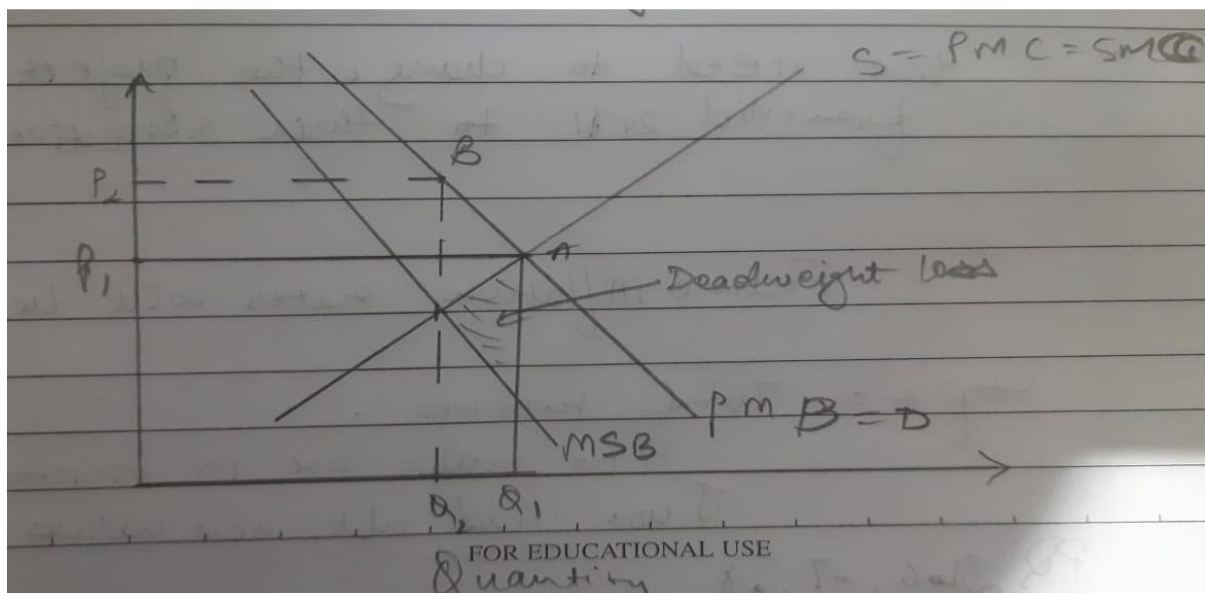
21.

i. A negative externality is a phenomenon where a third party suffers costs/losses because of an economic transaction between two other unrelated parties. A negative externality is also referred to

as external costs. Consumption of cigarettes will lead to passive smoking by the people surrounding the smoker. This may in turn lead to respiratory diseases causing ill health. Due to this more people will start demanding quality healthcare, thereby driving up the prices of healthcare services. This will result in reduced healthcare access by the marginal sections of the society. The consumption of cigarettes may also lead to reduced productivity. Thus, we can see how society at large is adversely affected by the consumption of cigarettes.

ii. Price intervention: the government may impose higher indirect taxes on tobacco consumption to deter people from smoking. This method was implemented by the Australian government and they have witnessed a lower proportion of the population indulging in smoking cigarettes. Non-price intervention: the government should carry out campaigns making people aware of the ill effects of smoking and tobacco consumption.

iii.



22. Actual economic growth is measured by the annual percentage change in a country's real national output (GDP). On the other hand, Potential economic growth is also known as trend growth and is measured by the estimated annual change in a country's potential level of national output.

23. The three methods of measuring national income are as follows:

a. Product (Output) method = Under this methodology of calculating national income, the value of all goods and services produced during the year is added up. This is the most direct method of calculating the national income of a country. It is sometimes also referred to as a value-added method to GDP or GDP at factor cost by industry of origin. It is the sum of gross value added. When one uses this method to calculate the national income, the problem of double counting arises. This is because the output of one industry is the input of another. Thus, when we calculate the national income using the product method, we might be summing the same output multiple times. To avoid

this issue, one must use the concept of 'value-added', which is the difference between output value and input at each stage of production.

b. Income method = National income calculated using this approach is the summation of all factor incomes, i.e., wages, salaries, rent, interest, and profit that one earns during the production of goods and services in the nation. Double counting in this method arises when we use the same factor income twice in the calculation process. For example – a labourer earns wages by working. He in turn uses his income to purchase goods and services which give rise to profit for a firm. Thus, during the calculation process, in essence, we have used the same income twice.

c. Expenditure method = Calculating the national income using this approach would be to add up the flows of expenditure needed to purchase the nation's output. If we had to formulate it, it would look like this: $GDP = C + I + G + (X - M)$, where;

C – consumer expenditure

I – investment expenditure

G – government expenditure

X – income from exports

M – import expenditure

The answer produced by each of these three methods will differ because all three methods consider different aspects. The output method considers the value of produced goods, the income method considers the factor payments, whereas the expenditure method uses the amount spent on expenditure. Thus, the answers we will arrive at will be different.