Price Determination - Reason-Based Questions

Q.1. At market equilibrium, there is no excess demand and no excess supply.

Ans. True. Because, market equilibrium is defined as a state of the market when demand for a commodity is equal to its supply, corresponding to a particular price. Therefore, there is neither excess demand nor excess supply.

Q.2. In a situation of excess supply, market price of the commodity falls.

Ans. True. In a situation of excess supply, demand < supply. At a given price, producers are willing to sell more than what the buyers are willing to buy. Pressure of excess supply leads to reduction in market price.

Q.3. An increase in demand imply an increase in price but no change in quantity supplied.

Ans. True. With increase in demand, price increases. If quantity supplied remains unchanged, it must be a situation of perfectly inelastic supply curve. In this case, supply is perfectly inelastic.

Q.4. Due to a decrease in input price equilibrium quantity falls.

Ans. False. Owing to decrease in input price, cost of production reduces. It causes a forward shift in supply curve. Accordingly, equilibrium quantity increases.

Q.5. A decrease in the price of a complementary good causes a fall in equilibrium price of the commodity.

Ans. False. A decrease in the price of a complementary good causes a rise in equilibrium price of the commodity. Because decrease in the price of a complementary good means increase in the demand for a commodity. Increase in demand implies a shift in demand curve to the right. Diagrammatically, demand curve D, as shown in **Fig. 4** shifts rightward, *i.e.*, from D to D_1 . The new equilibrium is struck at point E_1 . The equilibrium price increases from OP to OP_1 .

FIGURE 4