Eq O/P/ Eq GDP - Reason-Based (Comp. of Sub)

Q.1. In the Keynesian theory, technology changes as the level of output changes.

Ans. False. In the Keynesian theory, technology is assumed to remain constant.

Q.2. Equilibrium GDP refers to that level of GDP where AD = AS but S > I.

Ans. False. Equilibrium GDP refers to that level of GDP where AD = AS as well as S = I.

Q.3. When AD = AS, producers suffer the burden of unwanted supplies.

Ans. False. When AD = AS, the producers do not suffer the burden of unwanted supplies or unsold stocks. Because in such a situation, actual stocks with the producers = desired stocks with the producers.

Q.4. Ex-ante saving and ex-ante investment are equal at the point of equilibrium.

Ans. True. Ex-ante investment is the investment expenditure which is intended to be made in the economy during the period of one year. Ex-ante saving is the saving which people intend to make in the economy during the period of one year. Equilibrium is struck when ex-ante saving (S) = ex-ante investment (I).

Q.5. There are no exports in a closed economy.

Ans. True. A closed economy is the one which has no economic relations with the rest of the world. Accordingly, there are no exports in this economy.

Q.6. AS is perfectly elastic owing to the excess supply in the economy.

Ans. False. AS is perfectly elastic owing to the existence of excess capacity in the economy.

Q.7. AS increases proportionate to the increase in AD so long as there is excess capacity in the economy.

Ans. True. AS increases proportionate to the increase in AD so long as there is excess capacity in the economy. Because, excess capacity arises because

of the deficiency of demand. So that, as demand increases, supply increases proportionately.

Q.8. An economy can attain the maximum equilibrium GDP level even when excess capacity is not fully exhausted.

Ans. False. An economy can attain the maximum equilibrium GDP level only when excess capacity is fully exhausted or the level when there is full employment of resources in the economy.

Q.9. When AS < AD, AS adjusts itself to AD.

Ans. True. When AS < AD, flow of goods and services in the economy tends to be less than their demand. The existing stocks of the producers would be sold out and the producers would suffer the loss of unfulfilled demand. To rebuild the desired stocks and avoid the loss of unfulfilled demand, the producers would plan greater production. AS would increase to become equal to AD. This is how AS converges with AD.

Q.10. When S > I, level of income and employment tends to shrink.

Ans. True. In case S > I, it implies a situation when a fall in expenditure through 'S' is more than the rise in expenditure through 'I'. Accordingly, aggregate expenditure in the economy would be less than what is needed to buy the planned output. Stocks of the producers would be in excess of the desired stocks. Planned output for the subsequent year will fall. Level of income and employment will tend to shrink till the point when S = I.

Q.11. In an economy, the equilibrium level of income is 800. The autonomous consumption is 70 and the investment expenditure is 250. Marginal propensity to consume in this economy will be 0.5.

Ans. False. Marginal propensity to consume in this economy will be 0.6.

Given, equilibrium level of income (Y) = 800

Autonomous consumption $(\overline{C})$ = 70

Investment expenditure (I) = 250

At the equilibrium level,

$$Y = C + I$$

Or, $$Y = \overline{C} + MPC\,(Y) + I$$

$\Rightarrow$ $$800 = 70 + MPC\,(800) + 250$$

$\Rightarrow$ $$800 = 320 + 800\,(MPC)$$

$\Rightarrow$ $$800\,(MPC) = 800 - 320$$

$\Rightarrow$ $$800\,(MPC) = 480$$

$$\Rightarrow \qquad \text{MPC} = \frac{480}{800}$$

$$\Rightarrow \qquad \text{MPC} = 0.6$$

Therefore, marginal propensity to consume in this economy will be 0.6.

Q.12. In an economy, the investment expenditure is 600 and the consumption function is: C = 90 + 0.7Y. The economy is in equilibrium at an income level 2,000.

Ans. False. The economy is in equilibrium at an income level of 2,300.

Given, $\quad C = 90 + 0.7Y$

$\qquad$ Investment expenditure (I) $= 600$

At the equilibrium level,

$$Y = C + I$$

$$\Rightarrow \qquad Y = 90 + 0.7Y + 600$$

$$\Rightarrow \qquad Y = 690 + 0.7Y$$

$$\Rightarrow \qquad Y - 0.7Y = 690$$

$$\Rightarrow \qquad 0.3Y = 690$$

$$\therefore \qquad Y = \frac{690}{0.3} = 2,300$$

Thus, the economy is not in equilibrium. Because, the equilibrium level of income is 2,300 which is greater than the given income level of 2,000.