Chapter 1: Introduction to Micro Economics

Question: 1

Fill in the blank with appropriate alternative given below.

The terms Micro and Macro Economics were first used by _______________.

Options

- Adam Smith
- Robbins
- Ragner Frisch
- Marshall

Solution

The terms Micro and Macro Economics were first used by **Ragner Frisch.** Ragner Frisch of The University of Oslo was the first person to coin the terms 'Microeconomics' and 'Macroeconomics' in the year 1993. Since then, these terms are used by economists all over the world.

Question: 2

Fill in the blank with appropriate alternative given below

Micro Economics is a study of _________.

Options

- Whole economy
- general price level
- National output
- Individual economic unit

Solution

Micro Economics is a study of **Individual economic unit.** Microeconomics is the study of behaviour of individual units in an economy such as individual consumer, producer and firm.

Question: 3

Fill in the blank with appropriate alternative given below.

Micro Economics is also called as _________________.

Options

- Income theory
- Price theory
- Growth theory
- Employment theory

Solution

Micro Economics is also called as **Price theory.** Microeconomics is also known as the price theory. We know that in Microeconomics we study the behaviour of individual economic units such as the producer and the consumer. Through the study of such behaviour the main focus is the determination of prices (commodities and factor prices) in the market.

Question: 4

Fill in the blank with appropriate alternative given below.

Micro Economic analysis adopts ___________________ method.

Options

- lumping
- aggregative
- Slicing
- inclusive

Solution

Micro Economic analysis adopts **slicing** method. Microeconomics is the study of behaviour of individual units in the economy. For this purpose, the entire economy is sliced, i.e. divided into several smaller/individual units and each unit is then analysed in detail.

Question: 5

Fill in the blank with appropriate alternative given below.

Micro Economics is a ___________________________ equilibrium approach.

Options

- partial
- general
- total
- multi-variable

Solution

Micro Economics is a **Partial** equilibrium approach.

In microeconomics each of the individual units is studied in isolation. That is, while studying one unit/variable the effect of other units or variables is taken to be constant. It ignores the interdependence of economic variables. In other words, it is based on the assumption of “other things remain constant” (ceteris paribus). Thus, because of this assumption, it is said that microeconomics has a partial equilibrium approach.

Question: 6

Match the following

Group A	Group B
1) Adam Smith	A) Aggregates
2) Micro Economics	B) Prof. Boulding
3) Macro Economics	C) Father of Economics
4) Dr. Marshall	D) Individual units
	E) Economic efficiency
	F) Principles of Economics

Solution

Group A	Group B
1) Adam Smith	C) Father of Economics
2) Micro Economics	D) Individual units
3) Macro Economics	A) Aggregates
4) Dr. Marshall	F) Principles of Economics

Explanation:

1) Adam Smith is regarded as the Father of Economics. He is the founder of Microeconomics. In his book ‘The Wealth of Nations’, published in the year 1776, he has mentioned how the prices of commodities and factors of production are fixed.

2) In microeconomics, we study the behaviour of individual economic units, basically consumers and firms.

3) In macroeconomics, we study the economy as a whole. It focuses on the aggregate measures such as aggregate demand, aggregate supply and aggregate price level.

4) The principles of economics were propounded by a well-known neo-classical economist Dr. Alfred Marshall in 1890.

Question: 7

State whether the following statement is TRUE or FALSE.

Dr. Marshall is known as the Father of Economics.

Options

- TRUE
- FALSE

Solution

False

Adam Smith is known as the Father of Economics, as he is the founder of microeconomics. On the other hand, Dr. Marshall is a neo-classical economist who developed the Principles of Economics.

Question: 8

State whether the following statement is TRUE or FALSE.

Micro Economics studies theory of firm.

Options

- TRUE
- FALSE

Solution

True

Microeconomics studies the behaviour of individual units. Accordingly, a firm being an individual unit, its behaviour is studied under microeconomics. Microeconomics studies prices of commodities and factors of production in both the consumer and factor markets.

Question: 9

State whether the following statement is TRUE or FALSE.

Micro Economics deals with allocation of resources.

Options

- TRUE
- FALSE

Solution

True

Microeconomics explains the optimum allocation of resources. It explains the distribution of resources among the competing groups in a manner that ensures their efficient usage; that is, there is minimum wastage of resources. In other words, it explains us how these scarce resources should be distributed so that they can be utilised to the fullest.

Question: 10

State whether the following statement is TRUE or FALSE.

Micro Economic theory assumes full employment.

Options

- TRUE
- FALSE

Solution

True

The microeconomic theory is based on many assumptions such as full employment, perfect competition and a laissez-faire style of working. However, these assumptions may not always exist in reality and, consequently, make the validity of microeconomics doubtful.

Question: 11

State whether the following statement is TRUE or FALSE.

Micro Economic theory suggests policies to solve problem of inflation.

Options

- TRUE
- FALSE

Solution

False

Microeconomics is the study of the behaviour of individual units in an economy. Problems such as inflation relate to the behaviour of the all the economic units simultaneously in an economy. In this regard, it is beyond the scope of microeconomics.

Question: 12

Define or Explain the following concept.

Micro Economics

Solution

Microeconomics is the study of behaviour of individual economic units, basically consumers and firms, which interact in the market of different goods and services. It analyses how consumers make their consumption choices and take decisions, given
their incomes and prices of goods and services. Similarly, it analyses how firms decide how much to produce by applying different input combinations. It also helps in determining prices, in both the commodity and factor markets, based on the demand and supply analysis. Thus, microeconomics is a study that basically focuses on the behaviour of individual economic units.

Question: 13

Define or Explain the following concept.

Partial equilibrium

Solution

Partial equilibrium is an equilibrium situation achieved taking into consideration only a part of the market condition. That is, it is the equilibrium with regard to an individual unit assuming the effect of other units and variables constant. In other words, it is based on the assumption of “other things remaining constant”. It neglects the interdependence among variables. Thus, microeconomic analysis is regarded as partial equilibrium.

Question: 14

Define or Explain the following concept.

Economic efficiency

Solution

Economic efficiency can be defined as a situation in which welfare of the society is maximised. Microeconomics focuses on utilising scarce resources in a way that the public/social welfare is maximised. Economic efficiency involves attainment of efficiency along the following three aspects.

1. Production efficiency: It refers to producing the maximum amount of output from the available resources. 2. Consumption efficiency: It refers to distributing the produced goods and services among the various consumers in such a manner that the overall social welfare is maximised.

3. Overall economic efficiency: It refers to efficiency with regard to the production mix. In other words, it refers to producing that combination of goods and services that provide maximum satisfaction to the people.

Question: 15

Define or Explain the following concept.

Individual economic unit

Solution

Individual economic unit refers to a single variable such as an individual firm, a particular household, the price of an individual commodity and wages/income of an individual. The behaviour of individual economic units is studied under microeconomics.

Question: 16

Define or Explain the following concept.

Resource allocation

Solution

Resource allocation refers to the distribution of resources among competing groups. These resources may be natural resources, money, labour, etc., which the producers use in production processes to produce goods. Resource allocation involves making decisions regarding how the resources should be allocated to each group such that they can be utilised in the best possible manner providing maximum gains to the society. The decision regarding resource allocation is particularly important because resources are scarce and also have competing uses. Thus, effort must be made to use them efficiently and optimally.

Question: 17

Give reason or explain the following statement:

Micro economics is also known as price theory.

Solution: 1

Yes, Microeconomics is also known as price theory.

Reason: Microeconomics is primarily concerned with price determination of goods and services as well as factors of production. Therefore, it is also known as price theory.

Solution: 2

We know that in microeconomics we study the behaviour of individual economic units such as the consumer and the producer. The basic aim of such a study is to determine the prices (in the commodities and factor markets). It is for this reason that microeconomics is also known as the price theory.

Question: 18

Give reason or explain the following statement.

Micro economics studies individual economic unit.

Solution: 1

Yes, I agree with this statement.

i. The term Micro Economics is derived from the Greek word "**Mikros**" which means "Small". Micro economics gives a detailed analysis of one part of the economy or society. It studies the behaviour of individual units of the economy, such as households, firms, industries and markets.

ii. Micro economics is concerned with the study of behaviour of individual element(s) of an economy, whereas, macro economies concerned with the study of behaviours of an economy as whole.

iii. Micro economics gives a microscopic picture of the economy. The activities of numerous economic units and their inter-relationship are studied and analysed minutely through this method.

Solution: 2

Micro economics is a study that focuses on the behaviour of an individual economic units such as the consumer and the producer. It analyses how consumers make their consumption choices and take decisions, given their incomes and prices of goods and services. Similarly, it analyses how firms decide how much to produce by applying different input combinations. The basic focus of such a study is the determination of prices in the factor and the commodities market.

Question: 19

Give reason or explain the following statement.

Micro Economics analyses partial equilibrium.

Solution

Microeconomics is based on partial equilibrium analysis. That is, while analysing each of the units/variables the effect of other units is assumed to be constant. In other words, it is based on the assumption of ceteris paribus. To put in simple words, it analyses each of the units is isolation while ignoring the interdependence among them. Such an analysis is known as partial equilibrium analysis.

Question: 20

Give reason or explain the following statement.

Micro Economic theories are based on certain assumptions.

Solution

Microeconomic theories are based on assumptions such as full employment, perfect competition, a laissez-faire style of working (no government intervention) and ceteris paribus. These assumptions help in understanding the relationship between any two variables. However, these assumptions may or may not exist in the real world.

Question: 21

Give reason or explain the following statement.

Marginalism principle is used as a tool of analysis in micro economics.

Solution

Marginalism principle focuses on studying the change in total amount when one additional unit is added to it. This additional unit is called the marginal unit. All microeconomic decisions are based on this concept.

Question: 22

Write short note on :
Features of Micro-Economics

Solution

Microeconomics refers to the study of individual economic units such as the consumer and the producer. The following are the features of microeconomics.

i. Individual units - Microeconomics is a study of behaviour of individual units in an economy such as an individual consumer and producer.

ii. **Price theory** - Microeconomics is also called the price theory, as it helps in determining the prices of both the commodities and factors of production in their respective markets.

iii. Slicing method - Microeconomic analysis adopts the slicing method wherein, the entire economy is divided into various smaller units and then each unit is analysed individually in detail.

iv. Partial equilibrium - Microeconomics uses a partial equilibrium approach. Herein, each of the units is studied in isolation assuming the effect of the other units as constant. It ignores the interdependence among the various units.

v. Microscopic approach - Just as a microscope enables us to see a larger view of smaller things, microeconomics shows a magnified view of an individual unit. It analyses small units in detail. It examines how these individual units perform economic activities and reach equilibrium.

Question: 23

Write short note on :
Subject matter of Micro Economics

Solution

Microeconomics is the study of the following theories:

i. Theory of product pricing - The theory of product pricing explains how the prices of goods are determined in the market. For this, it is important to study demand and supply in the market. The demand is studied by studying the consumer behaviour and the supply is studied by studying the cost and production behaviour of the firm.

ii. Theory of factor pricing - The theory explains how the prices of various factors of production, namely, land, labour, capital and entrepreneur, are determined in the factor market in the form of rent, wages, interest and profits respectively.

iii. Theory of economic welfare - This theory of microeconomics deals with the allocation of resources. It explains that resources should be used in a manner that gives maximum satisfaction to people. It involves making decisions such as what to produce, how much to produce, when to produce, for whom to produce and by what technique to produce.

Question: 24

Write short note on :
Historical review of Micro Economics

Solution

History of microeconomics can be traced to classical economists. Adam Smith is regarded as the Father of Microeconomics. In his book 'The Wealth of Nations', published in the year 1776, he discussed how the prices of goods and the factors of production are determined. However, microeconomic analysis was done by Dr. Alfred Marshall, a neo-classical economist. He was the first person to use the principle of marginalism. Some of the other popular economists who have contributed to the development of microeconomics are Prof. Pigou, J. R. Hicks, Prof. Samuelson, Mrs. Joan Robinson and Chamberlin.

Question: 25

Write short note on :
Importance of Micro Economics

Solution

The following points highlight the importance of microeconomics:

i. It helps us in understanding how free market economies work.

ii. It explains how the prices are determined in both commodity and factor markets.

iii. It helps in making policies such as the tax policy, public expenditure policy and price policy.

iv. It helps businessmen in making decisions about prices, cost of production, investment, etc., on the basis of knowledge of the price theory.

v. It helps in examining different aspects of international trade such as the effect of tariffs on the exchange rates and gains from international trade.

vi. It helps in the development of certain models that are used for understanding and solving complex economic situations.

Question: 26

Answer the following question
Explain the meaning of Micro Economics with the help of few important definitions.

Solution

Microeconomics is the study of the issues pertaining to individual economic units, basically consumers and firms, which interact in the market of different goods and services. It studies how consumers make their consumption choices and decisions, given their incomes and prices of goods and services. Similarly, it analyses how firms decide how much to produce by using different input combinations. The basic focus of this study is the determination of prices in the commodity markets and factor markets. The meaning of microeconomics can be better understood with the help of the following definitions.

According to Prof. K. E. Boulding, "Micro Economics is the study of particular firm, particular household, individual prices, wages, incomes, individual industries and particular commodities." In the words of Maurice Dob, "Micro economics is in fact a microscopic study of the economy."

Question: 27

Answer the following question
What is the scope & subject matter of Micro Economics?

Solution

Microeconomics deals with the study of the following theories:

i. Theory of product pricing - The theory of product pricing explains how the prices of goods are determined in the market. For this, it is important to study demand and supply in the market. The demand is studied by studying the consumer behaviour and the supply is studied by studying the cost and production behaviour of the firm.

ii. Theory of factor pricing - The theory explains how the prices of various factors of production, namely, land, labour, capital and entrepreneur are determined in the factor market, in the form of rent, wages, interest and profits, respectively.

iii. Theory of economic welfare - This theory of microeconomics deals with the allocation of resources. It explains that resources should be used in a manner that gives maximum satisfaction to people. It involves making decisions such as what to produce, how much to produce, when to produce, for whom to produce and by what technique to produce.

Question: 28

Answer the following question
What is the importance of Micro Economics?

Solution

The following points highlight the importance of microeconomics:

i. It helps us in understanding how free market economies work.

ii. It explains how the prices are determined in both commodity and factor markets.

iii. It helps in making policies such as the tax policy, public expenditure policy and price policy.

iv. It helps businessmen in making decisions about prices, cost of production, investment, etc., on the basis of knowledge of the price theory.

v. It helps in examining different aspects of international trade such as the effect of tariffs on the exchange rates and gains from international trade.

vi. It helps in the development of certain models that help in understanding and solving complex economic situations.

vii. It helps in allocating resources in an efficient manner so that there is no wastage.

Question: 29

Answer the following question
What are the features of Micro Economics?

Solution

i. Individual units - Microeconomics is a study that basically focuses on the behaviour of individual units such as an individual consumer and producer.

ii. Price theory - Microeconomics is also called the price theory, as it helps in determining the prices of both the commodities and factors of production in their respective markets.

iii. Slicing method - Microeconomic analysis adopts the slicing method. Under this method, the entire economy is divided into smaller units and then each unit is analysed individually in detail.

iv. Partial equilibrium - Microeconomics uses a partial equilibrium approach. The equilibrium points are identified assuming "other things remain constant" (ceteris paribus). It ignores the interdependence of economic variables.

v. Microscopic approach - Just as a microscope enables us to see a larger view of smaller things, microeconomics shows a magnified view of an individual unit. It analyses small units in detail. It examines how these individual units perform economic activities and reach equilibrium.

vi. Marginalism principle: Marginal means change in the total due to an additional unit. The additional unit is known as the marginal unit. Microeconomics is based on the principle of marginalism as important economic decisions are based on the marginal unit.

vii. Analysis of market: Microeconomic studies deals in the study of different market structure namely, perfect competition, monopoly, monopolistic competition, oligopoly. It analyses how prices and ouput are determined in the market.

Question: 30

Answer the following question
What are the basic economic questions dealt by Micro Economics?

Solution

Microeconomics deals with the following questions:

i. What goods are to be produced and in what quantities? - This question deals with the types of goods that are to be produced by the firm and the quantity in which they are to be produced.

ii. Who will produce them and how? - After taking the decision on the type of goods to be produced, the firm must decide upon the technique (labour-intensive or capital-intensive) required to produce those goods.

iii. To whom & how the wealth, so produced, shall be distributed? - This question is concerned with the distribution of income or wealth and the channel through which this wealth is to be distributed.

iv. How resources are to be allocated to ensure production and consumption in an efficient manner? - Efficient allocation of resources means distribution of resources in a manner such that they reach the individual or group who values it the most.

Question: 31

Do you agree with the following statement? Give reason.
Micro Economics studies behaviour of individual unit.

Solution

Micro Economics studies behaviour of individual unit - **True**

Yes, microeconomics is a study that basically focuses on the behaviour of an individual units in the economy such as consumer and producer.

Question: 32

Do you agree with the following statement? Give reason.
Micro Economics is known as income theory.

Solution

Micro Economics is known as income theory - **False**

No, microeconomics is not known as the income theory, rather ,it is known as the price theory, as it focuses on determining the prices of commodities and factors of production in the market.

Question: 33

Answer in detail
Explain the features of Micro Economics.

Solution

The following are the features of microeconomics.

i. Individual units - Microeconomics is a study that basically focuses on the behaviour of individual units such as an individual consumer and producer.

ii. Price theory - Microeconomics is also called the price theory, as it helps in determining the prices of both the commodities and factors of production in their respective markets.

iii. Slicing method - Microeconomic analysis adopts the slicing method. Under this method, the entire economy is divided into smaller units and then each unit is analysed individually in detail.

iv. Partial equilibrium - Microeconomics uses a partial equilibrium approach. The equilibrium points are identified assuming “other things remain constant” (ceteris paribus). It ignores the interdependence of economic variables.

v. Microscopic approach - Just as a microscope enables us to see a larger view of smaller things, microeconomics shows a magnified view of an individual unit. It analyses small units in detail. It examines how these individual units perform economic activities and reach equilibrium.

vi. Marginalism principle: Marginal means change in the total due to an additional unit. The additional unit is known as the marginal unit. Microeconomics is based on the principle of marginalism as important economic decisions are based on the marginal unit.

vii. Analysis of market: Microeconomic studies deals in the study of different market structure namely, perfect competition, monopoly, monopolistic competition, oligopoly. It analyses how prices and ouput are determined in the market.

viii. Based on assumptions: Microeconomic analysis is based on certain assumptions such as laissez faire, full employment, perfect competition, ceteris paribus, etc. Such assumptions although make the analysis simple, but may not exists in reality.

Question: 34

Answer in detail
Explain the scope and subject matter of Micro Economics.

Solution

Microeconomics is the study of the following theories:

i. Theory of product pricing - The theory of product pricing explains how the prices of goods are determined in the market. For this, it is important to study demand and supply in the market. The demand is studied by studying the consumer behaviour and the supply is studied by studying the cost and production behaviour of the firm.

ii. Theory of factor pricing - The theory explains how the prices of various factors of production, namely, land, labour, capital and entrepreneur are determined in the factor market in the form of rent, wages, interest and profits, respectively.

iii. Theory of economic welfare - This theory of microeconomics deals with the allocation of resources. It explains that resources should be used in a manner that gives maximum satisfaction to people. It involves making decisions such as what to produce, how much to produce, when to produce, for whom to produce and by what technique to produce.