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INTRODUCTION TO MICROECONOMICS

Q1.) What is economy?

A1.) An economy is a system that provides people, the means to work and to earn a living. In other words, it is an organisation that provides living to people by making use of available resources, goods and services that people want.

Q2.) What is scarcity?

A2.) It refers to limitation of supply of resources in relation to their demand. This problem is universal which is why we ^{have} ~~have~~ economize resources to make ^{best} optimum use of available resources.

Q3.) What are economic problems?

A3.) Economic problem is a problem of choice involving satisfaction of unlimited wants out of limited resources having alternative uses. The reason for economic problems are as follows:

1.) Scarcity of resources:

The resources like land, labour, capital, etc., are limited in relation to their demand in economy. It is the basic reason for economic problems.

2.) ~~Unlimited~~

2.) Unlimited Wants:

Human wants are never-ending, i.e., they can never be fully satisfied as soon as a want is satisfied, another new want emerges, and due to limited resources. Thus all wants cannot be satisfied.

3.) Alternative uses:

Every resource is not only scarce but has alternative uses as well.

For eg → land can be used for agriculture, school, hospital, etc. So, economy has to make choice between alternative uses of given resources.

Q4.) Differentiate between positive and normative economics.

Ans.) BASIS.	POSITIVE ECONOMICS	NORMATIVE ECONOMICS
1.) Meaning	It deals with what is or how the economic problems are actually solved.	It deals with how economic problems should be solved.
2.) Verification	It can be verified with actual data.	It cannot be verified with actual data.

Positive eco $\rightarrow$ tells what the problem is
Normative eco $\rightarrow$ tells the problem as well as the solution.

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1.) Purpose	Its purpose is to make a real description of an economic activity.	Its purpose is to determine the ideals.
2.) Suggested	It is based on facts so it is not suggestive.	It is based on opinions so, it is suggestive in nature.
3.) Value judgements	It does not give any value judgement.	It gives value judgements.
4.) Example	Prices in India are constantly rising.	India should take steps to control prices.

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Q5.) What are the central problems of an economy?

Ans.) Due to scarcity of resources, economy faces central problems which include :-

- 1.) What to produce?
- 2.) How to produce?
- 3.) For whom to produce?

WHAT TO PRODUCE?

This problem involves selection of goods and services to be produced and the quantity to be produced. Due to limited resources, economy cannot produce all goods and services. Therefore, it has to make choice among the goods.

For eg $\rightarrow$ On a ~~piece~~ piece of land, there is a possibility of producing 100 kg of rice or 200 kg of wheat. Economy has to choose one of

them because both cannot be produced.

How to Produce ?

This problem involves selection of technique to be used for production. There are mainly 2 techniques; one is labour-intensive technique that includes more of labour and less of technology and another is capital-intensive which includes more of technology and less of labour.

In developed countries like America, more of capital intensive technique is used but, in case of developing countries like India, where more of labour is ~~used~~ available, labour-intensive technique is used.

For whom to Produce ?

This problem relates to distribution of produced goods and services among individuals and economy.

In other words, it involves selection of category of people who will ultimately consume the goods so, it is a selection of section of people for whom goods to be produced, i.e., whether for richer section or poorer section, whether for producer section or consumer section, and so on.

aggregate $\rightarrow$ total.

Q6.) What do you mean by opportunity cost?

A6.) It is the cost of next best alternative foregone. As we know that, resources are scarce so we need to make choice between goods to be produced. If we have to produce more of one good, we have to reduce the quantity of another.

The quantity so sacrificed is the opportunity cost of producing extra of a given commodity.
For eg $\rightarrow$ On a piece of land, either 100kg of wheat or 200 kg of rice can be produced. The opportunity cost of producing 100kg of wheat is 200 kg of rice which is foregone.

Q7.) Differentiate between micro economics and macro economics.

Q7.) BASIS	MICROECONOMICS	MACROECONOMICS
1) Meaning	It is that part of economics which studies the behaviour of individual units.	It is that part of economics which studies the behaviour of aggregates of economy.
2) Tools	Demand and supply	Aggregate demand and aggregate supply.

1) Basic objective	To determine price of a commodity or factors.	To determine level of income and employment in economy.	(or
2) Assumptions	It assumes all macro variables to be constant like national income, national wealth, etc.	It assumes all micro variables like individual prices, decisions of household, etc, to be constant.	
3) Alternative Name	It is also known as price theory.	It is also known as income and employment theory.	
4) Examples	Individual income, output, etc.	National income, national output, etc.	✓

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Q8.) What do you mean by production possibility curve or production possibility frontier?

A2.) It refers to graphical representation of possible combinations of two goods that can be produced using given resources and technology. In other words it is a locus of points that show the possible combinations of two goods which can be produced using given resource and technology. It can further be explained with the help of following schedule and diagram.

Q9)

To increase P
For eg $\rightarrow$ One unit of P , five units of Q are sacrificed so here, MOC is five.

Q9.) What are marginal rate of Transformation?

A9.) It is the ratio of no. of units of a commodity sacrificed to gain an additional unit of another commodity. So MRT is equal to $\frac{\text{no. of units sacrificed}}{\text{no. of units gained}}$

For eg $\rightarrow$ To gain one unit of P , five units of Q are sacrificed. So, $MRT = 5:1$

Q10.) What are the characteristics or properties of PPC?

A10.) Following are the basic features or properties of PPC:

1.) PPC slopes downward:

A PPC always slopes downward from left to right since, it shows the possible quantities that can be produced of two goods within limited resources. So, to produce more of one, we have to sacrifice units of another. So, there is an inverse relationship between quantities of two goods. Hence, it slopes downward from left to right.

2) PPC is concave to the point of origin:
PPC is always concave shaped because of application of law of increasing marginal ~~opportunities~~ opportunity cost. That means to produce one more unit of a commodity, the sacrifice of another commodity keeps on increasing as, the resources are transferred from one good to another less efficient resources have to be employed. This raises the marginal opportunity cost and the curve becomes concave to point of origin.

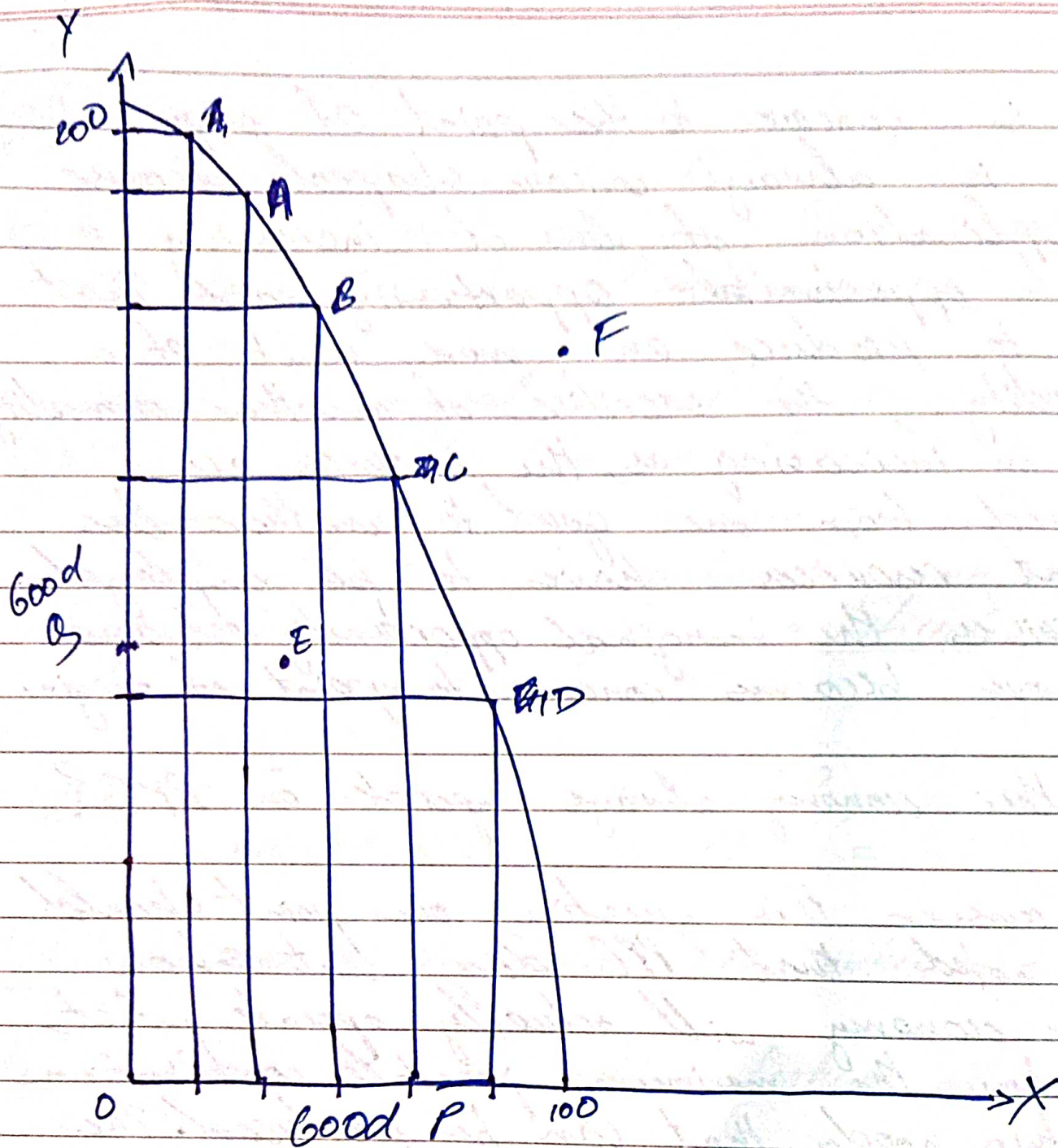
Q11.) Whether economy always operate on PPC?

Ans.) To answer this question, one point should be noted that PPC does not show where economy will actually operate in fact, it shows the maximum possible combinations of two goods that can be produced. The exact point of operation will depend on how well the resources in economy are used.

1) If resources are fully and efficiently used economy will operate at any point on PPC like A, B, C, D, shown in the diagram.

2) If resources are not fully and efficiently used, economy will operate at any point inside the PPC.

3) Economy can never operate outside PPC because they are unattainable points like pt. F in the diagram.



Q12.) Can PPC be a straight line?

A12.) A PPC can be a straight line only when we assume that MRT is constant, i.e., unit sacrificed are always equal to units gained. It is possible when we assume that all resources are equally efficient.

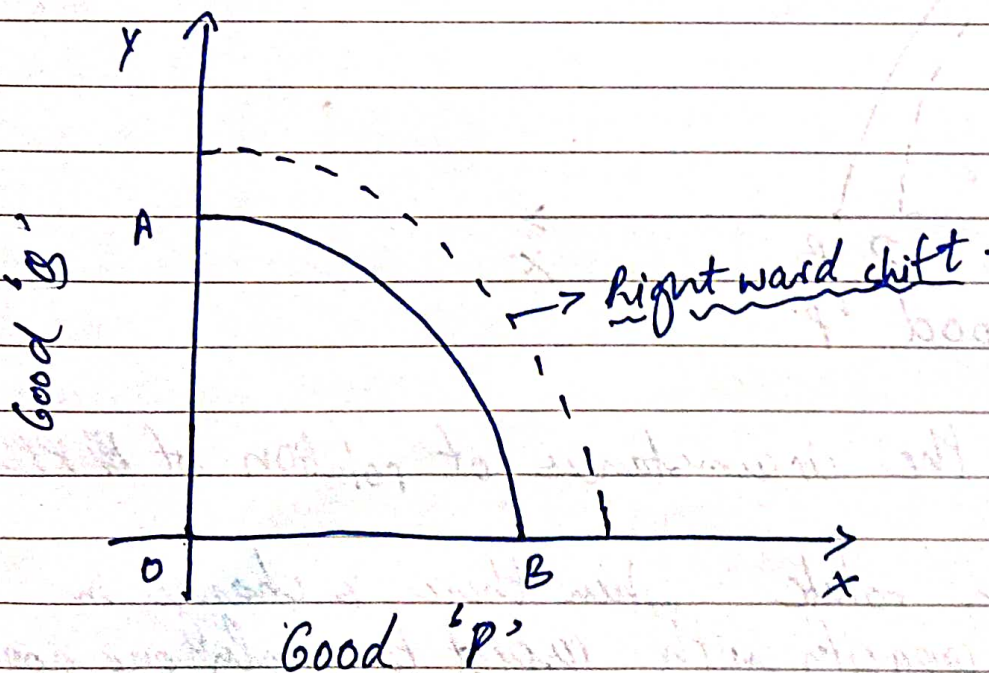
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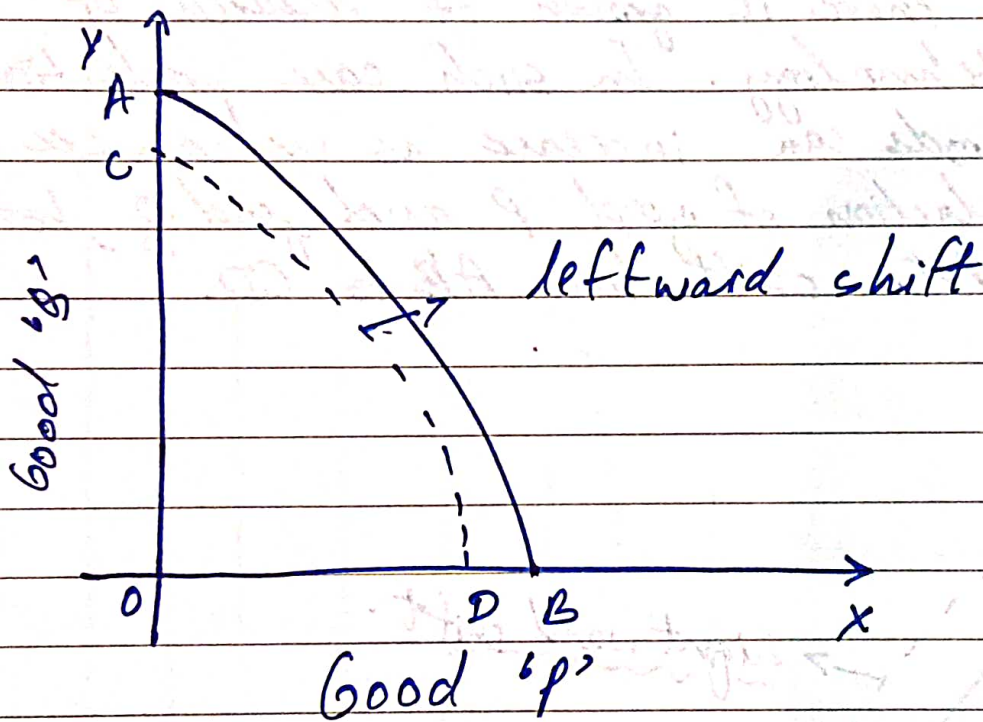
Q1.) In what circumstances a PPC can shift?

Ans.) A PPC can shift when there is change in resources or technology, wrt, both of the goods. This shift can be rightward or leftward.

1.) Rightward shift: A rightward shift is possible when there is growth of resources or advancement of technology. In such case production of both the goods can increase as we can see in the diagram. Production of good P and good Q, both increase and PPC shift from AB to CD.



ii) leftward shift: A PPC can shift towards left when there is decrease in resources or degradation of technology and that has affected production of both the goods and the production has reduced as shown in following diagram. Where PPC has shift leftward from AB to CD.



Q2.) What are the circumstances of rotation of PPC?

Ans.) A PPC can rotate when there is change in productive capacity with respect to only one good. The rotation can be on x axis or on y axis as shown in diagram below:

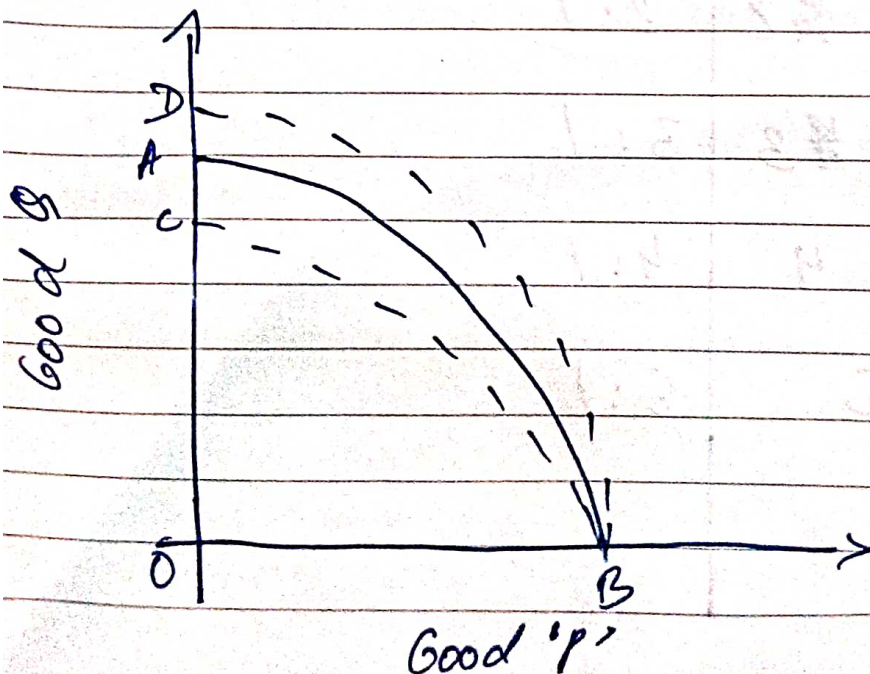


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In this diagram AB was initial PPC where there is growth of resource with respect to good P and the PPC will rotate to AD.

Similarly, when there is decline in resources with respect to Good P, PPC will rotate to AC.

Similarly, kind of rotation will take place on Y axis if there is change in resources with respect to Good Q as, shown in the diagram below.



Q3.) What do you mean by economizing of resources?

A3.) It refers to making optimum use of available resources, i.e., getting the best possible production out of limited resources.

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1) $MOC = \frac{\text{Units sacrificed}}{\text{Units gained}}$

2) $MRT = \frac{\text{Units sacrificed}}{\text{Units gained}}$

Good X	Good Y	MOC $\frac{\text{Units sacrificed}}{\text{Units gained}}$	MRT $\frac{\text{Units sacrificed}}{\text{Units gained}}$
0	15	1/0 -	-
1	14	$\frac{1}{1} = 1$	1:1
2	12	$\frac{2}{1} = 2$	2:1
3	9	$\frac{3}{1} = 3$	3:1
4	5	$\frac{4}{1} = 4$	4:1
5	0	$\frac{5}{1} = 5$	5:1

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Good A	Good B	MOC	MRT
20	0	—	—
14	1	$\frac{6}{1} = 6$	6 : 1
9	2	$\frac{5}{1} = 5$	5 : 1
5	3	$\frac{4}{1} = 4$	4 : 1
2	4	$\frac{3}{1} = 3$	3 : 1
0	5	$\frac{2}{1} = 2$	2 : 1 2 : 1