NDA - Economics - final Mock

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Question 2

write title of every question in the beginning

you have used 8 lines but answer hasn't started yet

poor impression

1. Introduction

Own price elasticity, cross-price elasticity and income elasticity are various measures to see how consumers change their spending pattern with a change in various factors. They help assess the change in government policies impact on the consumers. Firms are also able to decide how a change in policy will impact the consumers and affecting their total revenue.

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dont use interogative words like elaborate

just start headings

2. Elaborate the own-price, cross-price and income elasticity theoretically and empirically.

1 Own price elasticity

refers to the percentage change in ~~price~~ quantity demanded of a good ~~and~~ ~~its~~ ~~impact~~ ~~or~~ due to the percentage change in price

Formula

$$PED = -\frac{\%\ \text{change in Quantity de}}{\%\ \text{change in price}}$$

e.g if price increase by 2 percent and quantity demand decreases by 1% then

PED = 0.5 - inelastic

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This means a change in pric... creates a l... ~~decrease~~ impact quantity demande...

2. Income ela...

This refer... change in... demanded... ~~impact~~ due... in ... ines...

$IED = + \frac{\%}{\%}$ ...

e.g a les... in...

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This means a %
change in price
creates a lesser
~~decrease~~ impact on
quantity demanded.

avoid cutting

2. Income elasticity demand

This refers to the
change in quantity
demanded ~~and~~ ~~its~~
~~impact~~ due to a change
in income

$$IED = + \frac{\%\text{ change in quantity demanded}}{\%\text{ change in income}}$$

e.g a 2% increase income
leads to a 4% increase
in quantity demanded

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the demand is income elasticity of dem
of this good is elastic
- a % change in income leads to a greater change in quantity demanded

→ This good is also a normal good as positive relationship between income and ~~demand~~ quantity demanded.

→ Negative relationship when good inferior an increase leads to decrease ind demand.

3. Cross-elasticity of demand

Cross elasticity of demand refers to the change in quantity demanded of a good ~~with~~

due to a change in price of another good

$$CED = \frac{\% \text{ in quantity demanded of good A}}{\% \text{ in price of good B}}$$

if CED + good are complements

that means goods are purchased together
e.g Tires and Cars

if CED − goods are Substitutes

that means goods are competing with each other

e.g Coca Cola and Pepsi

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2. Relationship of own price elasticity with total revenue

A. $\boxed{PED < 1}$ - Inelastic

Price	quantity PED<1	Marginal revenue M.R	Total revenue T.R
5	25	—	125
10	20	50	200
15	15	25	225

B. $\boxed{PED > 1}$ - Elastic

Price	Quantity demanded	Marginal revenue	Total revenue
5	25		125
10	10	-25	100
15	5	-25	75

Comparing both cases it is easy for any business to see if their product has ~~ela~~ inelastic demand

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they gain more total revenue from increasing prices - case 1 revenue keeps increasing with increase in price e.g from to t.R is 200 and 15 total revenue 225 increase of 25.

In the case 2 elastic demand if ~~consumer~~ business decreased price from 15 to 10 gains in marginal revenue of 25 as total revenue increases from 75 to 100.

Conclusion

Price elasticity, income elasticity and cross elasticity are important measures to allow business and government to determine the far-reaching impact of various factors.

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Question 3

Title ?
question is about?

1. Introduction

IS-LM model is a useful tool for macro-economic stabilization it allows the policy makers to see the impact of policy changes on goods -IS- and money market LM. it addresses some of the things left in the typical keynesian model of aggregate demand and aggregate supply.

you are leaving 9 to 10 lines without any reason

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2. Critically evaluate the IS-LM model as a tool for macroeconomic stabilization in developing countries

IS - good market

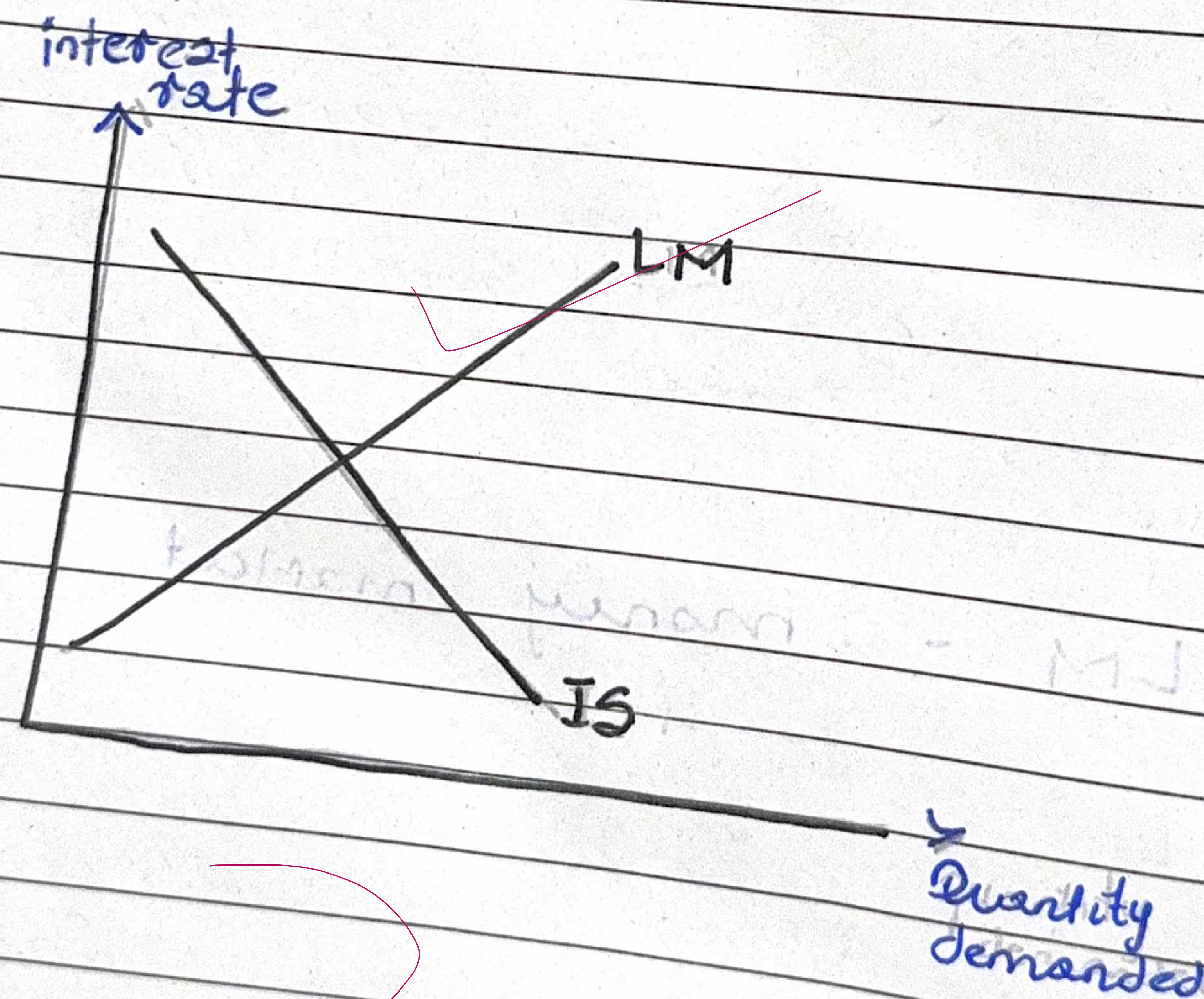
IS - I for investment and S for savings shows how both these react to changes

LM - money market

LM - liquidity for L and M for money illustrates how the financial - money market reacts to changes in interest rate

ISLM framework

together they represent the ISLM which shows how changes in interest rate & monetary policy impacts the goods and money markets



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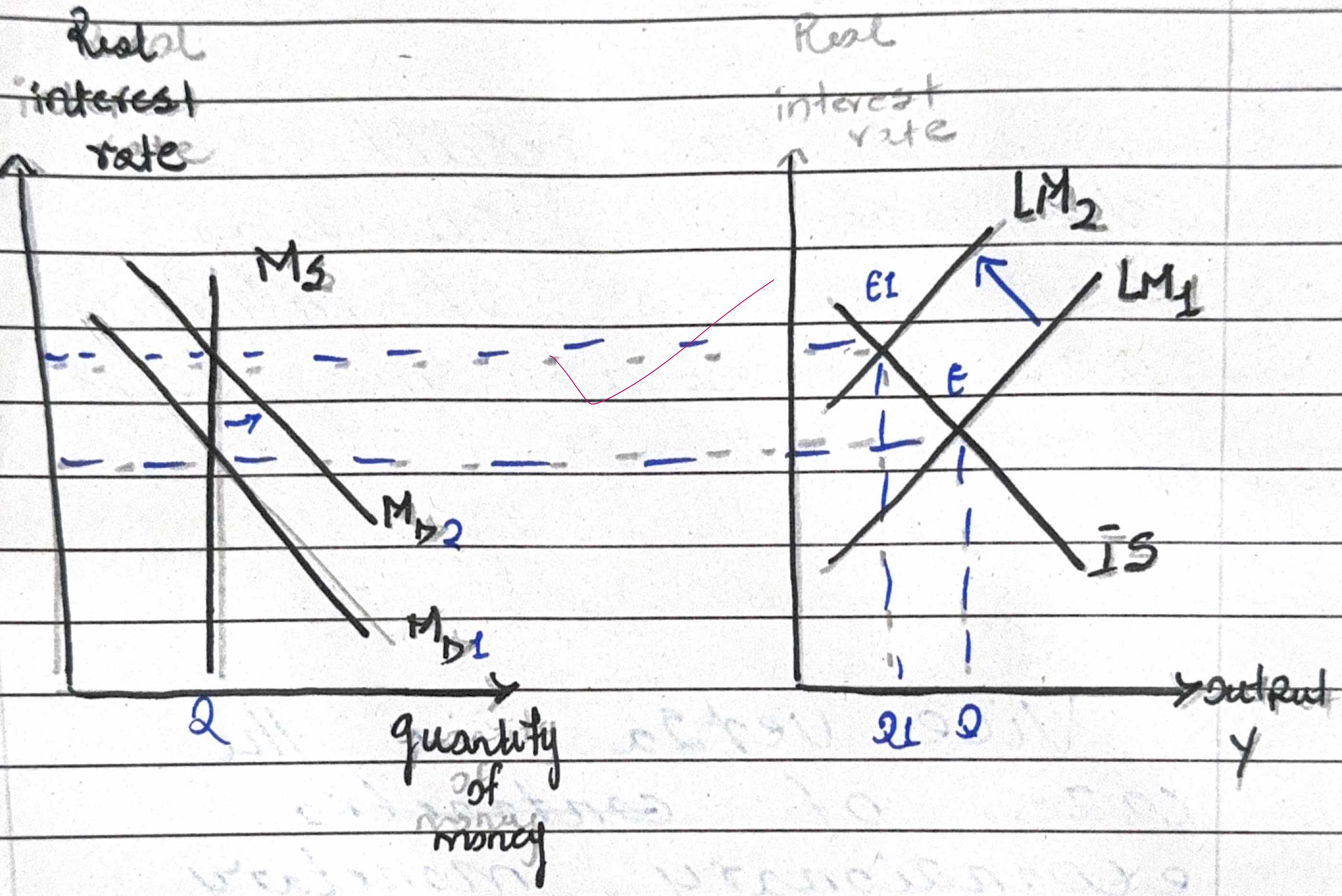
Developing countries cases

1 Contractionary monetary policy



As the graph above illustrate, the government to decrease inflation in the developing country will try to follow a contractionary monetary policy. This will lead to an increase in policy rate from r_1 to r_2.

As a result,

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people in the economy will be encouraged to save more and spend less as saving becom attractive.

The end result, a decrease in spending and easing of inflation as shown in IS/LM graph

Vice versa in the case of ~~contractio~~ expansionary monetary policy if the developing country is experiencing a recession and low inflation.

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3. Conpare its usefulness with AD-AS analysis, highlighting strengths and limitations.

Aggregate demand and aggregate supply analysis shows the impact of shifts in either demand or supply side and their impact of output.

Strengths & limitations

weakness?
or limitation?

only 3 strengths?

1. Strengths

→ the role of central Bank highlighted

→ interest rate impact comprehensively illustrated

→ joins goods and money markets

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1. Combines goods and money market — comprehensive

The goods and money markets role is explained and highlighted how each responds when changes in the economy takes place. Unlike AD-AS approach that fails to explain both these markets

2. impact of interest rate highlighted

the impact of interest rate is explained in depth, which is touched upon at the surface level in AD-AS model.

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3. Investment and Savings decision profoundly explained

How investment and saving decision changes when their is a change in government policy is explained in-depth and the rational of how these changes ensue. Unlike the AD-AS model.

4. The desire to hold liquidity and money comprehensively showcased

Why people hold money and when they prefer liquidity is explained in the model. The typical AD-AS model lacks this.

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limitations

1. Supply side factors ignored by?

The supply side factors ignored, such as what happens when their is rise in the cost of raw materials

e.g OPEC crisis

2. Overemphasis on role of central bank -

The central bank at times cannot influence decisions of people.

e.g Volcker disinflation

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3. role of expectations not explained

The role of expectations ignored in the model that people take into account future uncertainity as well when making decisions.

4. Rigidity in the economy not highlighted

Sticky wages - firms are in contract cannot change prices immediately.

sticky prices
menu costs
the business have cost and cannot instantly change their cost of items.

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write self explanatory catch headings

?

Delay to internalize changes

it takes a while for consumers and business to internalize changes.

Conclusion

The IS-LM model comprehensively explains how changes in the economy take place given certain factors and the role of central banks monetary policy. It is more comprehensive with the comparision to AD/AS model but ignores some important factors like all economic models.

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Question 4

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1. Introduction

Keynesian framework and the classical school are both pivotal in seeing how economy reacts as a whole to various factors and different approaches that can be taken. whereas the keynesian approach is about taking an active role in running of the economy, the classical approach is a more passive approach in dealing with the economy as a whole.

2. Critical evaluation of Keynsian framework and classical school in addressing inflation, unemployment.

A. Keynsian approach

The keynsian approach sees that economy is free by less constraints in the long-run than in the short-run.

-> The aggregate supply according to keynsian theory is vertical in the ~~short-run~~ long-run

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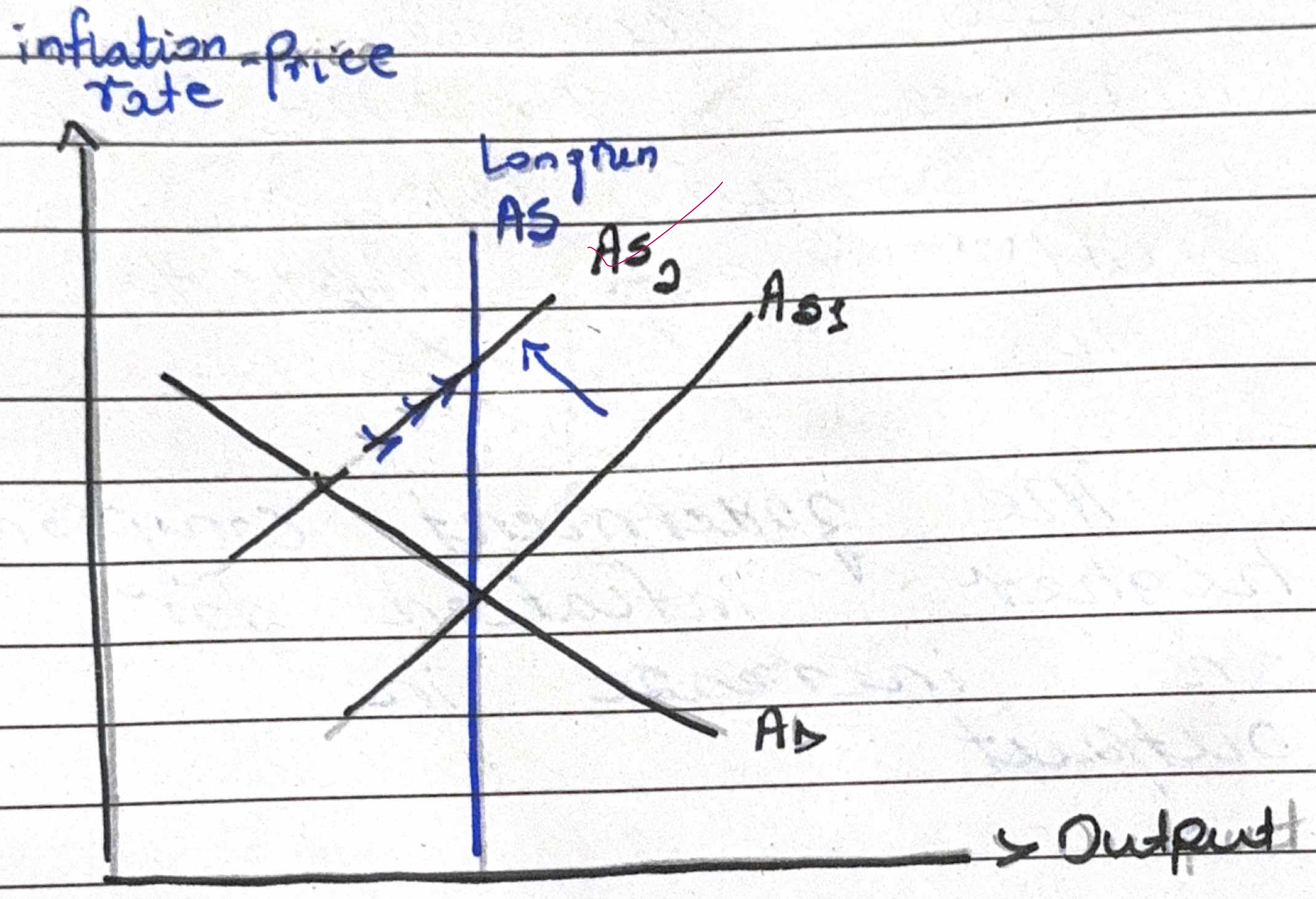
unemployment = natural rate + 2 (current - expected inflation)



As the graph above illustrates, A shift in short-run aggregate supply from AS1 to AS2 will increase ~~inflatio~~ unemployment as less demand for workers - (raw materials price increases). due to rising costs.

keynesian approach states that the

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the government should intervene and increase output by ~~selling~~ an expansionary fiscal policy increase Aggregate demand this is shown by a shift from AD_1 to AD_2

The government compromises higher inflation for an increase in output

~~Classical view~~

The unemployment will decrease as a result due to an increase in output. This expansionary policy ensures that government does not stay complacent. In the longrun government has compromized higher inflation for higher output

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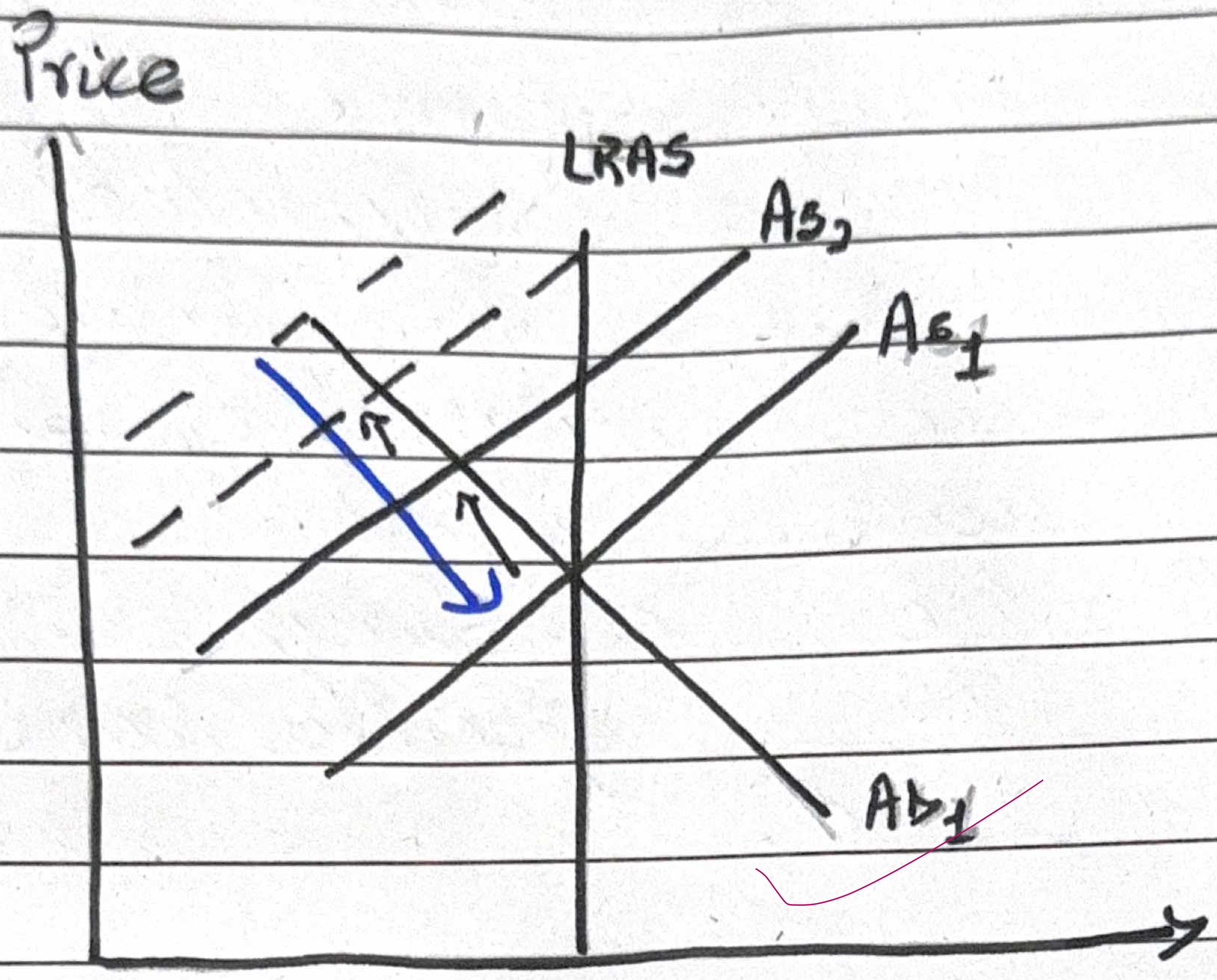
Classical view



According to classical view the government shouldnot intervene. The economy will comeback to its natural level of output.

Rational is that as firms fire workers in the economy in the shortrun workers will refuse to work at lower wages ~~but~~ ~~in the lon~~ as higher inflation but as

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firms close down or keep firing workers - AS_1 to AS_4 their will come a point when workers will begin to work at low wages (AS_4 ~~and~~ AS_1) and this will bring back the economy back to equilibrium level E.

The government without intervention achieved low inflation and unemployment.

Critical evaluation

The classical view was misguided. in the 1930s great depression as markets failed to self correct due to unions - wage stickyness. A period of stagflation high unemployment and inflation. Keynes suggested governments need to follow

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expansionary ~~monetary~~ fiscal policy. This is why Keynes called Saviour of capitalism.

Conclusion

As shown above, keynes called the Saviour of capitalism as the keynsian theory gives government an active role. Markets do not always correct themselves and governments need to intervene to bring economy to an optimal equilibrium.

what is purpose of drawing margin line?

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Question 5

1. Introduction

Monetarists, such as Milton freidman, have highlighted the importance of central bank in a economy. How it is a lender of last resort and ensures commercial banks do not practice predatory practices that jeopradize the effective functioning of the economy.

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2. Theoretical and practical arguments to assess the role of central bank as a regulator of commercial ~~Lender~~ banks and Lender of last resort

1. Printing of currency

Central bank plays a pivotal role of issuing currency. It ensures that there is adequate available cash in the economy through which people can maintain a sufficient level of liquidity.

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2. Reserve ratio

The reserve ratio is the amount of lending that banks can do. A higher reserve ratio means less lending. if banks given reserve ratio of 10% can lend 90% of deposits - credit creation

3. Prevents bankruptcy

Central bank ensure that major State owned enterprise, commercial banks and government itself does not go bankrupt and actively monitors the credit risk in the economy.

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4. Issues bonds

Central bank issues bond for the government that allow it to borrow from the people

5. Decides interest rates - Policy rate

A. impact on investment - borrowing

Central bank sets the interest rate on which basis people can borrow from each other. The private sector borrows when interests low & vice versa.

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B. impact on saving- lending

The savings reduce when central bank ~~bor~~ decides a ~~higher~~ lower interest rate when people are discouraged to save more and the spending increases in the economy.

→ This gives boost to the economy.

→ On the other hand when interest rate increased people save to get higher return on savings.

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3. How effective are these functions in preventing financial crisis in weak institutional settings?

1. Stabilize currency
- exchange rate

The central bank stabilizes currency when there is excessive depreciation. by increasing the interest rate people prefer the domestic currency to foreign currency this increases the value of currency and stabilizes it.

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2. Prevents bankruns

The central bank by ensuring banks stay liquid and guaranteeing people their deposits ensures that people do not go for depositing out all their cash in crisis.

3. Eases inflation - Store of value of currency maintained

Fisher equation = $MV = PQ$

If prices are increasing the central bank increases the policy rate and issues securities in the market to suppress spending.

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4. Government liquidity maintained can borrow

Government can borrow from the central bank if it has low liquidity and this ensures effective working of the governments projects.

5. Line of credits - LCs for business

The central bank gives Line of credits through which businesses can import from the foreign countries and import goods and capital. The central bank guarantees to payback in dollars on behalf of local business.

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6. Reserves of government maintained with central bank

The foreign reserves of the country are held with the central bank and it ensures that the country is maintaining sufficient reserves to pay creditors.

Conclusion

The central bank ensures that the country's financial system works effectively and their is trust in the financial system of the country. It ensures that the economy that does not go of at complete chaos.