

12th Economics Lesson 3 Questions in English**3] Theories of Employment and Income**

1. Who among the following defines full employment as the absence of involuntary unemployment?

- a) **Keynes**
- b) Ricardo
- c) Adam Smith
- d) Hayek

Explanation

Keynes defines full employment as the absence of involuntary unemployment. J. M. Keynes is one of the greatest and most influential economists of the mid-20th century.

2. Every able-bodied person who is willing to work at the prevailing wage rate is employed called ---

- a) Under employment
- b) Unemployment
- c) **Full employment**
- d) Employment opportunity

Explanation

Full employment refers to a situation in which every able-bodied person who is willing to work at the prevailing wage rate, is employed.

3. Which among the following statement is correct

- 1) The economic history has shown many countries facing economic problems. Out of these problems, unemployment is the most vexing. Both classical economists and Keynes have explained the relationship between employment and income.
 - 2) Full employment refers to a situation in which every able-bodied person who is willing to work at the prevailing wage rate, is employed. In other words, full employment means that persons who are willing to work and able to work must have employment or a job.
 - 3) Friedrich Hayek defines full employment as "that level of employment at which any further increase in spending would result in an inflationary spiral of wages and prices". Not every economy in the world aims at attaining the level of full employment equilibrium where all its available resources are not fully and efficiently employed to achieve maximum level of output.
- a) **Both 1 and 2**
 - b) Both 1 and 3
 - c) Both 2 and 3

d) All 1, 2 and 3

Explanation

Lerner defines full employment as “that level of employment at which any further increase in spending would result in an inflationary spiral of wages and prices”. Every economy in the world aims at attaining the level of full employment equilibrium where all its available resources are fully and efficiently employed to achieve maximum level of output.

4. Which among the following statement is correct

- 1) India's rural economy has both more underemployment and less unemployment. The major feature of rural underemployment is the existence of underemployment in the form of disguised underemployment and seasonal underemployment.
- 2) In India, frictional, structural and open unemployment exist in urban areas. Due to urbanization, a large number of people move from rural areas to urban areas. This migration from rural to urban areas increases the size of labour force in urban areas and adds to the already unemployed labour force.
 - a) Only 1
 - b) Only 2**
 - c) Both 1 and 2
 - d) None

Explanation

India's rural economy has both unemployment and underemployment. The major feature of rural unemployment is the existence of unemployment in the form of disguised unemployment and seasonal unemployment.

5. In reality, the concept of full employment generally refers to full employment of what?

- a) Capital force
- b) Machinery force
- c) Consumer force
- d) Labour force**

Explanation

Every economy in the world aims at attaining the level of full employment equilibrium where all its available resources are fully and efficiently employed to achieve maximum level of output. But in reality, the concept of full employment generally refers to full employment of labour force of a country.

6. Which among the following is not the type of unemployment?

- a) Cyclical Unemployment

- b) Frictional Unemployment
- c) **Filtered Unemployment**
- d) Structural Unemployment

Explanation

The following are the types of unemployment 1. Cyclical Unemployment 2. Seasonal Unemployment 3. Frictional Unemployment 4. Educated Unemployment 5. Technical Unemployment 6. Structural Unemployment and 7. Disguised Unemployment.

7. Which unemployment arises due to imbalance between supply of labour and demand for labour?

- a) Structural Unemployment
- b) **Frictional Unemployment**
- c) Disguised Unemployment
- d) Cyclic Unemployment

Explanation

Frictional unemployment arises due to imbalance between supply of labour and demand for labour. This is because of immobility of labour, lack of necessary skills, breakdown of machinery, shortage of raw materials etc.

8. The lack of employable skills, mass student turnout and preference for white collar jobs are highly responsible for which unemployment in India?

- a) Cyclic Unemployment
- b) Seasonal Unemployment
- c) Structural Unemployment
- d) **Educated Unemployment**

Explanation

Sometimes educated people are underemployed or unemployed when qualification does not match the job. Faulty education system, lack of employable skills, mass student turnout and preference for white collar jobs are highly responsible for educated unemployment in India.

9. Modern technology being capital intensive requires less labourers and contributes to which unemployment?

- a) **Technical Unemployment**
- b) Seasonal Unemployment
- c) Disguised Unemployment
- d) Cyclic Unemployment

Explanation

Modern technology being capital intensive requires less labourers and contributes to technological unemployment. Now a days, invention and innovations lead to the adoption of new techniques there by the existing workers are retrenched. Labour saving devices are responsible for technological unemployment.

10. The Lack of demand for the product or shift in demand to other products cause which type of unemployment?

- a) Cyclical Unemployment
- b) Seasonal Unemployment
- c) **Structural Unemployment**
- d) Disguised Unemployment

Explanation

Structural unemployment is due to drastic change in the structure of the society. Lack of demand for the product or shift in demand to other products cause this type of unemployment. For example, rise in demand for mobile phones has adversely affected the demand for cameras, tape recorders etc. So, this kind of unemployment results from massive and deep-rooted changes in economic structure.

11. Which among the following unemployment occurs when more people are there than what is actually required?

- a) Cyclical Unemployment
- b) Seasonal Unemployment
- c) Temporary Unemployment
- d) **Disguised Unemployment**

Explanation

Disguised unemployment occurs when more people are there than what is actually required. Even if some workers are withdrawn, production does not suffer. This type of unemployment is found in agriculture. A person is said to be disguisedly by unemployed if his contribution to output is less than what he can produce by working for normal hours per day.

12. Which unemployment is also known as Temporary unemployment?

- a) Educated Unemployment
- b) **Frictional Unemployment**
- c) Seasonal Unemployment
- d) Cyclical Unemployment

Explanation

Frictional Unemployment is also known as Temporary Unemployment. The persons who lose jobs and in search of jobs are also included under frictional unemployment.

13. Which among the following statement is correct

- 1) Cyclic unemployment exists during the downturn phase of trade cycle in the economy. In a business cycle during the period of recession and depression, income and output fall leading to widespread unemployment. It is caused by deficiency of effective demand. Cyclical unemployment can be cured by public investment or expansionary monetary policy.
- 2) Seasonal Unemployment occurs during certain seasons of the year. In agriculture and agro based industries like sugar, production activities are carried out only in some seasons. These industries offer employment only during that season in a year. Therefore, people may remain unemployed during the off season. Seasonal unemployment happens from demand side also; for example, ice cream industry, holiday resorts etc.
 - a) Only 1
 - b) Only 2
 - c) **Both 1 and 2**
 - d) None

14. Who among the following wrote the book "An Enquiry into the Nature and Causes of the Wealth of Nations"?

- a) David Ricardo
- b) Karl Marx
- c) **Adam Smith**
- d) John Stuart Mill

Explanation

The classical theory of employment is composed of different views of classical economists on the issue of income and employment in the economy. Adam Smith wrote the book "An Enquiry into the Nature and Causes of the Wealth of Nations" in 1776. Since the publication of this book, classical theory was developed by David Ricardo, J.S. Mill, J.B. Say and A.C. Pigou.

15. Which among the following is the core of the classical theory of employment?

- a) Smith's law of markets
- b) Ricardo's law of markets
- c) **Say's law of markets**
- d) Pigou's law of markets

Explanation

Say's law of markets is the core of the classical theory of employment. J.B. Say (1776 – 1832) was a French Economist and an industrialist. He was influenced by the writings of Adam Smith and David Ricardo.

16. J.B. Say enunciated the proposition that which creates its own demand?

- a) **Supply**
- b) Capital
- c) Market
- d) Tax

Explanation

J.B. Say enunciated the proposition that "Supply creates its own demand". Hence there cannot be general over production or the problem of unemployment in the economy. In short, this classical theory explains that "A person receives his income from production which is spent on the purchase of goods and services produced by For the economy as a whole, therefore, total production equals total income".

17. Which among the following is the assumption of the Say's law of market?

- 1) A single buyer or seller of commodity or an input can affect price. People are not motivated by self-interest and self – interest can't determines economic decisions. There will be a perfect competition in labour and product market.
 - 2) The laissez faire policy is essential for an automatic and self-adjusting process of full employment equilibrium. Market forces determine everything right. There is wage-price flexibility. Money acts only as a medium of exchange.
 - 3) Unutilized resources used until reaches full employment. No Government intervention automatic Price adjustment mechanism operated. There is no possibility for over production or unemployment. Interest rate flexibility leads is saving – Investment equality.
- a) Both 1 and 2
 - b) Both 1 and 3
 - c) **Both 2 and 3**
 - d) All 1, 2 and 3

Explanation

No single buyer or seller of commodity or an input can affect price. People are motivated by self-interest and self – interest determines economic decisions. There will be a perfect competition in labour and product market.

18. The statement that supply creates own demand or equivalently that the aggregate investment equals the aggregate saving always holds good in which sense?

- a) Ex post
- b) Ex ante
- c) Ex sale
- d) Ex consumes

Explanation

The statement that supply creates own demand or equivalently that the aggregate investment equals the aggregate saving always holds good in the ex post sense since it is simply an accounting identity. Say's law of markets, however, states that these two are equal in ex ante sense, i.e., the total quantity which people produce i.e., aggregate supply must be equal to the total quantity which they plan to buy i.e., aggregate demand.

19. Which among the following is not the Implication of say's law?

- 1) There is more possibility for over production or unemployment. If there exist fully utilized resources in the economy, it is profitable to employ them up to the point of full employment. This is true under the condition that factors are willing to accept rewards on a par with their productivity.
 - 2) As automatic price mechanism operates in the economy, there is no need for government intervention. (However, J.M. Keynes emphasized the role of the State). Interest flexibility brings about equality between saving and investment. Money performs only the medium of exchange function in the economy, as people will not hold idle money.
- a) Only 1
 - b) Only 2
 - c) Both 1 and 2
 - d) None

Explanation

There is no possibility for over production or unemployment. If there exist unutilized resources in the economy, it is profitable to employ them up to the point of full employment. This is true under the condition that factors are willing to accept rewards on a par with their productivity.

20. Who among the following wrote the book "The General Theory of Employment, Interest and Money"?

- a) Adam Smith
- b) Friedrich Hayek
- c) **John Maynard Keynes**
- d) John Stuart Mill

Explanation

John Maynard Keynes book, "The General Theory of Employment, Interest and Money" published in 1936 is a highly significant work that marked a turning point in the development of modern economic theory.

21. Which among the following is the Criticisms of Say's Law?

- 1) According to Hayek, supply does not create its demand. It is not applicable where demand does not increase as much as production increases. Hayek regards full employment as a special case because there is over - employment in capitalist economies.
- 2) Automatic adjustment process will not remove unemployment. Unemployment can be removed by increase in the rate of investment. Money is not neutral. Individuals hold money for unforeseen contingencies while businessmen keep cash reserve for future activities.
- 3) Say's law is based on the proposition that supply creates its own demand and there is no over production. Keynes said that over production is possible. The need for state intervention arises in the case of general over production and mass unemployment.
 - a) Only 2
 - b) Both 1 and 2
 - c) Both 1 and 3
 - d) Both 2 and 3

Explanation

According to Keynes, supply does not create its demand. It is not applicable where demand does not increase as much as production increases. Keynes regards full employment as a special case because there is under - employment in capitalist economies.

22. The classical economist believes that the market forces in which economy adjust themselves to attain equilibrium?

- a) Socialist Economy
- b) **Capitalist Economy**
- c) Both Socialist and Capitalist
- d) Liberal Economy

Explanation

The theory of Keynes was against the belief of classical economists that the market forces in capitalist economy adjust themselves to attain equilibrium. Keynes not only criticized classical economists but also advocated his own theory of employment.

23. Which among the following statement is correct

- 1) Keynes' theory was a general theory as it tried to explain all types of situations, i.e. not only equilibrium level of employment but also the concept of full employment as well as the possibility of underemployment.
- 2) Keynes theory of employment was based on the view of the long run. According to him, the factors of production such as capital goods, supply of labour, technology and efficiency of labour remains changing while determining the level of employment.
 - a) Only 1
 - b) Only 2
 - c) Both 1 and 2
 - d) None

Explanation

Keynes theory of employment was based on the view of the short run. According to him, the factors of production such as capital goods, supply of labour, technology and efficiency of labour remain unchanged while determining the level of employment.

24. The starting point of Keynes theory of employment and income is the principle of what?

- a) **Effective demand**
- b) Capital demand
- c) Production demand
- d) Supply demand

Explanation

The starting point of Keynes theory of employment and income is the principle of effective demand. Effective demand denotes money actually spent by the people on products of industry. The money which entrepreneurs receive is paid in the form of rent, wages, interest and profit. Therefore, effective demand equals national income.

25. Which among the following statement is correct reading Effective demand

- 1) An increase in the aggregate effective demand would increase the level of employment. A decline in total effective demand would lead to unemployment. Therefore, total employment of a country can be determined with the help of total demand of a country.
- 2) According to the Keynes theory of employment, "Effective demand signifies the money spent on consumption of goods and services and on investment. The total expenditure is equal to the national income, which is equivalent to the national output".
- 3) The relationship between employment and output of an economy depends upon the level of effective demand which is determined by the forces of aggregate supply and aggregate demand.
 - a) Both 1 and 2
 - b) Both 1 and 3
 - c) Both 2 and 3

d) All 1, 2 and 3

26. Which among the following is the correct equation of Effective Demand (ED)?

- a) $ED = Y = C + I + OUTPUT = \text{Employment}$
- b) $ED = Y = C - I + OUTPUT = \text{Employment}$
- c) **$ED = Y = C + I = OUTPUT = \text{Employment}$**
- d) $ED = Y = C + I = OUTPUT + \text{Employment}$

Explanation

$ED = Y = C + I = \text{Output} = \text{Employment}$

27. Which among the following statement is correct regarding Effective demand

- 1) Effective demand determines the level of employment in the economy. When effective demand increases, employment will increase. When effective demand decreases, the level employment will decline.
- 2) The effective demand will be completely determined by consumption. The consumption function depends upon income of the people and marginal propensity to consume. According to Keynes, if income increases, consumption will decrease but by less than the increase in income.
- 3) The rate of interest and marginal efficiency of capital determine the investment levels. Rate of interest depends on money supply and liquidity preference. Keynes has given importance to the concept of liquidity preference.
 - a) Both 1 and 2
 - b) **Both 1 and 3**
 - c) Both 2 and 3
 - d) All 1, 2 and 3

Explanation

The effective demand will be determined by two determinants namely consumption and investment expenditures. The consumption function depends upon income of the people and marginal propensity to consume. According to Keynes, if income increases, consumption will also increase but by less than the increase in income.

28. Which among the following is not the motives of Liquidity preference?

- a) Transaction motive
- b) Precautionary motive
- c) **Adoptive motive**
- d) Speculative motive

Explanation

Liquidity preference is based on three motives namely transaction motive, precautionary motive and speculative motive. MEC depends on two factors namely Prospective yield of capital asset and supply price of capital.

29. Which is the amount of money which entrepreneurs expect to get by selling the output produced by the number of labourers employed?

- a) Aggregate supply
- b) Aggregate demand**
- c) Aggregate capital
- d) Aggregate product

Explanation

In the Keynesian model, output is determined mainly by aggregate demand. The aggregate demand is the amount of money which entrepreneurs expect to get by selling the output produced by the number of labourers employed. Therefore, it is the expected income or revenue from the sale of output at different levels of employment.

30. Which among the following is not the components of Aggregated demand?

- a) Consumption demand
- b) Investment demand
- c) Government expenditure
- d) Private expenditure**

Explanation

Aggregate demand has the following four components: 1. Consumption demand 2. Investment demand 3. Government expenditure and 4. Net Export (export – import)

31. Which is the amount that households, firms, the governments and the foreign purchasers would like to spend on domestic output?

- a) Planned demand**
- b) Consumer demand
- c) Intension demand
- d) Supply demand

Explanation

The desired or planned demand (spending) is the amount that households, firms, the governments and the foreign purchasers would like to spend on domestic output. In other words, desired demand in the economy is the sum total of desired private consumption expenditure, desired investment expenditure, desired government spending and desired net exports (difference between exports and imports). Thus, the desired spending is called aggregate spending (demand).

32. Which among the following express the Aggregate demand?

- a) $AD = C + I - G + (X - M)$
- b) $AD = C + I + G + (X + M)$
- c) **$AD = C + I + G + (X - M)$**
- d) $AD = C + I - G - (X - M)$

Explanation

The Aggregate demand can be expressed as $AD = C + I + G + (X - M)$. aggregate demand price increases or decreases with an increase or decrease in the volume of employment. Aggregate demand curve increases at an increasing rate in the beginning and then increases at a decreasing rate.

33. Which among the following refers to the value of total output of goods and services produced in an economy in a year?

- a) **Aggregate supply**
- b) Aggregate demand
- c) Aggregate capital
- d) Aggregate product

Explanation

Aggregate supply function is an increasing function of the level of employment. Aggregate supply refers to the value of total output of goods and services produced in an economy in a year. In other words, aggregate supply is equal to the value of national product, i.e., national income.

34. Which among the following statement is correct regarding Aggregate Supply Function (ASF)

- 1) The aggregate supply refers to the required number of labourers and materials to produce the necessary output. Employers hire labourers, purchase various inputs and raw materials to produce goods. Thus, production involves cost.
 - 2) If the revenue from the sale of output produced is less than the cost of production at a given level of employment and output, the entrepreneur would be encouraged to employ more labour and other inputs to produce more.
 - 3) Aggregate supply price is the total amount of money that all entrepreneurs in an economy expect to receive from the sale of output produced by given number of labourers employed. The term 'price' refers to the amount of money received from the sale of output .
- a) Both 1 and 2
 - b) **Both 1 and 3**
 - c) Both 2 and 3
 - d) All 1, 2 and 3

Explanation

If revenue from the sale of output produced exceeds the cost of production at a given level of employment and output, the entrepreneur would be encouraged to employ more labour and other inputs to produce more.

35. Which among the following is not the components of aggregate supply?

- a) Aggregate (desired) consumption expenditure (C)
- b) Aggregate (desired) government savings (S)**
- c) Net tax payments (T)
- d) Personal (desired) transfer payments to the foreigners (Rf)

Explanation

The components of aggregate supply are: 1. Aggregate (desired) consumption expenditure (C) 2. Aggregate (desired) private savings (S) 3. Net tax payments (T) (Total tax payment to be received by the government minus transfer payments, subsidy and interest payments to be incurred by the government) and 4. Personal (desired) transfer payments to the foreigners (Rf)(eg. Donations to international relief efforts).

36. Which among the following express the Aggregate supply?

- a) $\text{Aggregate Supply} = C + S + (T - Rf) = \text{Aggregate income generated in the economy}$
- b) $\text{Aggregate Supply} = C + S - (T + Rf) = \text{Aggregate income generated in the economy}$
- c) $\text{Aggregate Supply} = C + S + T - Rf = \text{Aggregate income generated in the economy}$
- d) $\text{Aggregate Supply} = C + S + T + Rf = \text{Aggregate income generated in the economy}$**

Explanation

$\text{Aggregate Supply} = C + S + T + Rf = \text{Aggregate income generated in the economy}$

37. Which among the following statement is correct regarding aggregated supply

- 1) The slope of the aggregate supply curve depends on the relation between the employment and productivity. The capital stock is often fixed and hence the law of diminishing marginal returns takes place as more workers are employed.
 - 2) If prices are high and wages low, the producers will try to employ labourers. If prices are low and wages high, investment will be curtailed, output will fall and there will be a reduction in the productive capacity. Thus, aggregate supply is an important factor in determining the level of economic activity.
- a) Only 1
 - b) Only 2
 - c) Both 1 and 2**
 - d) None

38. The basic concept used in Keynes Theory of Employment and Income is ____

- a) Aggregate demand
- b) Aggregate supply
- c) **Effective demand**
- d) Marginal Propensity Consume

Explanation

The starting point of Keynes theory of employment and income is the principle of effective demand.

39. In disguised unemployment, the marginal productivity of labour is ____

- a) **Zero**
- b) One
- c) Two
- d) Four

Explanation

In disguised unemployment, marginal productivity of labour is zero or less or negative.

40. Keynes theory pursues to replace laissez faire by _____

- a) No government intervention
- b) Maximum intervention
- c) Private sector intervention
- d) **State intervention in certain situation**

Explanation

Keynes theory pursues to replace laissez faire by State intervention in certain situation.

41. Which two sectors is taken to understand the equilibrium between ADF and ASF under the Keynes theory of employment?

- a) Transport sector and Business sector
- b) **Household sector and Business sector**
- c) Transport sector and Household sector
- d) Transport sector and Industrial sector

Explanation

Under the Keynes theory of employment, a simple two sector economy consisting of the household sector and the business sector is taken to understand the equilibrium between ADF and ASF. All the decisions concerning consumption expenditure are taken by the individual households, while the business firms take decisions concerning investment.

42. How many approaches are there to determination of the equilibrium level of income in Keynesian theory?

- a) Two
- b) Three
- c) Five
- d) Six

Explanation

There are two approaches to determination of the equilibrium level of income in Keynesian theory. These are: 1. Aggregate demand – Aggregate supply approach 2. Saving – Investment approach.

43. According to classical theory, rate of interest is a reward for ____

- a) Capital
- b) Demand
- c) **Saving**
- d) Investment

Explanation

According to classical theory, rate of interest is a reward for Saving.

44. Which among the following point does not come under Keynesianism theory?

- a) State intervention is advocated
- b) Capitalism has inherent contradictions
- c) **The function of money is to act as a medium of exchange**
- d) Rate of interest is a reward for parting with liquidity

Explanation

In Keynesianism theory the function of money is a medium of exchange on the one side and a store of value on the other side. In Classicism theory the function of money is to act as a medium of exchange.

45. According to Classical theory, Rate of interest is determined by what?

- a) Demand and Supply
- b) Sale and Supply
- c) **Saving and Investment**
- d) Demand and Saving

Explanation

According to Classical theory Rate of interest is determined by Saving and Investment.

46. According to Keynes' Theory the equality between saving and investment is advanced through what?

- a) **Change in income**
- b) Change of rate of Interest
- c) Change in demand
- d) Change in Supply

Explanation

According to Keynes' Theory the equality between saving and investment is advanced through changes in income. According to Classical theory the equality between saving and investment is achieved through changes of rate of interest.

47. According to Classical theory, rate of interest is what?

- a) **Stock**
- b) Flow
- c) Demand
- d) Income

Explanation

According to Classical theory, the rate of interest is a stock. In Keynes theory, the rate of interest is flow.

48. The expected rate of return over costs of a new capital good is called _____

- a) Marginal demand of Capital
- b) Marginal Propensity to Capital
- c) **Marginal efficiency of Capital**
- d) Marginal productivity to Capital

Explanation

The expected rate of return over costs of a new capital good is called Marginal Efficiency of Capital.

49. The additional consumption due to an additional unit of income is known as _____

- a) Marginal demand of Consume
- b) **Marginal Propensity to Consume**
- c) Marginal efficiency of Consume
- d) Marginal productivity to Consume

Explanation

The additional consumption due to an additional unit of income is known as Marginal Propensity to Consume.

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