Economics Class 12 Important Question Chapter 3 Production and Costs

Q1. A central bank is a/an _______.

Apex bank
Rural bank
Regional bank
Commercial bank

Ans: a. Apex bank

Q2. What is meant by "production"?

Ans: "Production" refers to the specific process in which inputs are converted into output(s).

Q3. What will be the MP when TP is maximum?

Ans: When the Total Product (TP) is at its maximum, the Marginal Product (MP) will be zero.

Q4. State true or false: When there are diminishing returns to a factor, the total product always decreases.

Ans: False, because TPP grows at a lower rate when a factor's returns diminish.

Q5. State true or false: TPP increases only when MPP increases.

Ans: True, TPP rises as MPP falls, but it remains positive.

Q6. State true or false: An increase in TPP always indicates that there are increasing returns to a factor.

Ans: True, TPP grows even while the returns to a factor are diminishing.

Q7. State true or false: When there are diminishing returns to a factor, marginal and total products always fall.

Ans: False; only the MPP is in jeopardy, not the TPP. TPP increases at a decreasing pace when there are diminishing returns to a factor.

Q8. Why does the AFC curve never touch the "x" axis, though it lies very close to it?

Ans: The AFC curve does not touch the “x‟ axis, though it lies very close to the x-axis because TFC can never be equal to zero.

Q9. Why are AVC and AFC usually lower than AC?

Ans: Since AC is the sum of AVC and AFC, it is always greater than AVC and AFC.

Q10. Why does the TVC curve start from the origin?

Ans: At zero output level, TVC is zero.

Q11. When TVC is zero at zero level of output, what happens to TFC, Or why is TFC not zero at zero level of output?

Ans: Even if the output is zero, fixed costs are incurred.

Q12. How is TPP derived from MPP?

1) Cumulative addition

2) Cumulative subtraction

3) Cumulative product

4) Cumulative division

Ans: (1) Cumulative addition

Q13. In the short run, TPP changes with a change in which of the following factors?

1) Economic cost

2) Fixed factors

3) All the factors

4) Variable factors

Ans: (4) Variable factors

Q14. The general shape of TPP in the short run is:

1) Inverse U shaped

2) U shaped

3) Hyperbola

4) V-shaped

Ans: (1) Inverse U shaped

Q15. A production function shows the technical relationship between physical inputs and output of a commodity, i.e.,

- **Technological relationship between inputs and cost**
- **Economic relationship between inputs and output**
- **Technological relationship between inputs and output**
- **Technological relationship between inputs and price**

Ans: Technological relationship between inputs and output

Short Answer Question – 3 or 4 Marks

Q1. What is the change in demand?

Ans: When the quantity of a commodity changes as a result of a change in a factor other than price. It is also known as Demand Variation. It is of two types:

a) Increase in demand
b) Decrease in demand

Q2. What are Returns to a Factor? What do you mean by the Law of Diminishing Returns?

Ans: Returns to a component are used to explain physical output behaviour by allowing only one factor to change while holding all other factors constant. This is a short-term solution. According to the rule of diminishing returns to a factor, as the variable factor is allowed to vary (grow) while all other factors remain constant, the marginal product initially climbs, then drops, and even becomes negative.

Q3. What is the change in quantity demanded?

Ans: It is also known as movement along a demand curve. A commodity's quantity fluctuates due to a change in its own price caused by a shift in the supply curve. Changes in demand quantity can be classified into two types:

(a) expansion in demand

(b) contraction in demand.

Q4. Define the cost concept. What are the different types of costs?

Ans: The cost of production refers to the money spent on various inputs. The different types of costs are explained below:

Money Cost: The total amount of money spent by a company to manufacture a commodity.
Explicit Cost and Implicit Cost: The explicit cost is the money paid to outsiders. The implicit cost includes the cost of self-supplied factors.
Real Cost: All of the pain, sacrifice, and discomfort associated with producing factor services to manufacture commodities.

Opportunity Expense: This is the cost of passing up the next best option.

Short Run Cost:

Fixed Cost: – Cost of fixed factors.
Variable Cost: – Cost of variables.

Relationship between AC, MC, and AVC:

If MC is less than AC, AC tends to fall.

- When MC equals AC, AC is the smallest.
- When MC is greater than AC, AC tends to rise.

Long Answer Questions – 6 Marks

Q1. Explain the determinants of supply.

Ans: Supply is the quantity of a good available for sale at a given price and time. Supply is the desired flow. It evaluates how much a company is willing to sell rather than how much it sells. Supply may outnumber demand or fall short of it. In a given year, supply equals total output plus or minus commodity inventories.

The supply function is written as follows:

Sx = f(Px, Pa… Pc, PL… PO, T, Cr, St, O, G)

Here, Px is the price of the good x, Pa… Pc is equal to the prices of related items, PL… PO is the price of inputs, T is time, St is the state of technology,O is the firm's goals, and G is the taxes, subsidies, and regulations.

The determinants of the supply are shown below:

- Price of the product
- Price of related goods

Consumer income

1. Consumers' tastes and preferences
2. Advertisement expenditure
3. Consumer's expectations

Demonstration effect

Population of the country

Distribution of national income

Some of the determinants are discussed below:

- **Production costs –**are significant because the goal of most private companies is to maximise profits. Increased production costs reduce profit, thereby limiting supply. Input prices, wage rates, government regulations, taxes, and so on are all factors that influence manufacturing costs.
- **Technology –** Technological advances help to reduce production costs while increasing profit, resulting in increased supply.

Number of sellers – The number of sellers in the market increases market supply.

Expected future price increases – If producers anticipate that future price increases will be higher, they will want to hold onto their stocks and offer the items to consumers in the future, allowing them to collect the higher price.

Q2. Explain the relation between Marginal Cost and Average Variable Cost

Ans: The relationship between marginal cost and average variable cost is one of the various cost relationships. The average variable cost decreases when the marginal cost is less than the average variable cost. When the marginal cost exceeds the average variable cost, the average variable cost rises. This may also imply that in some cases, average variable cost takes on a U-shape, though this is not guaranteed because neither average variable cost nor marginal cost has a fixed cost component. Fixed and variable expenses are used in business to calculate production costs. The difference in production costs for each additional item is measured by marginal costs. Variable costs reflect the materials required to manufacture each product. As a result, variable expenses have a direct impact on the marginal cost.

For example, Mary owns a bakery and is considering expanding her current offering beyond cakes. Sandwiches will be added as well. To determine whether it is worthwhile, she will need to consider both the variable and marginal expenses. She should figure out the average cost of the extra ingredients and labour required to make the sandwiches. The variable and constant costs will then be used to calculate the marginal cost. She may find it convenient to include sandwiches if the marginal cost is too high to generate a profit.