

अर्थशास्त्र
ECONOMICS

कक्षा/Class: XII
2024-25

विद्यार्थी अध्ययन सामग्री
Student Support Material



केन्द्रीय विद्यालय संगठन
Kendriya Vidyalaya Sangathan



संदेश

विद्यालयी शिक्षा में शैक्षिक उत्कृष्टता प्राप्त करना केन्द्रीय विद्यालय संगठन की सर्वोच्च वरीयता है। हमारे विद्यार्थी, शिक्षक एवं शैक्षिक नेतृत्व कर्ता निरंतर उन्नति हेतु प्रयासरत रहते हैं। राष्ट्रीय शिक्षा नीति 2020 के संदर्भ में योग्यता आधारित अधिगम एवं मूल्यांकन संबन्धित उद्देश्यों को प्राप्त करना तथा सीबीएसई के दिशा निर्देशों का पालन, वर्तमान में इस प्रयास को और भी चुनौतीपूर्ण बनाता है।

केन्द्रीय विद्यालय संगठन के पांचों **आंचलिक शिक्षा एवं प्रशिक्षण संस्थान** द्वारा संकलित यह 'विद्यार्थी सहायक सामग्री' इसी दिशा में एक आवश्यक कदम है। यह सहायक सामग्री कक्षा 9 से 12 के विद्यार्थियों के लिए सभी महत्वपूर्ण विषयों पर तैयार की गयी है। केन्द्रीय विद्यालय संगठन की 'विद्यार्थी सहायक सामग्री' अपनी गुणवत्ता एवं परीक्षा संबंधी सामग्री-संकलन की विशेषज्ञता के लिए जानी जाती है और अन्य शिक्षण संस्थान भी इसका उपयोग परीक्षा संबंधी पठन सामग्री की तरह करते रहे हैं। शुभ-आशा एवं विश्वास है कि यह सहायक सामग्री विद्यार्थियों की सहयोगी बनकर सतत मार्गदर्शन करते हुए उन्हें सफलता के लक्ष्य तक पहुंचाएगी।

शुभाकांक्षा सहित।

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ECONOMICS
CLASS - XII (2024-25)

Theory: 80 Marks

3 Hours

Project: 20 Marks

Units		Marks	Periods
Part A	Introductory Macroeconomics		
	National Income and Related Aggregates	10	30
	Money and Banking	06	15
	Determination of Income and Employment	12	30
	Government Budget and the Economy	06	17
	Balance of Payments	06	18
		40	
Part B	Indian Economic Development		
	Development Experience (1947-90) and Economic Reforms since 1991	12	28
	Current Challenges facing Indian Economy	20	50
	Development Experience of India – A Comparison with Neighbours	08	12
	Theory Paper (40+40 = 80 Marks)	40	
			200
Part C	Project Work	20	20

Part A: Introductory Macroeconomics

Unit 1: National Income and Related Aggregates

30 Periods

What is Macroeconomics?

Basic concepts in macroeconomics: consumption goods, capital goods, final goods, intermediate goods; stocks and flows; gross investment and depreciation.

Circular flow of income (two sector model); Methods of calculating National Income - Value Added or Product method, Expenditure method, Income method.

Aggregates related to National Income:

Gross National Product (GNP), Net National Product (NNP), Gross Domestic Product (GDP) and Net Domestic Product (NDP) - at market price, at factor cost; Real and Nominal GDP

GDP Deflator, GDP and Welfare

Unit 2: Money and Banking**15 Periods**

Money – meaning and functions, supply of money - Currency held by the public and net demand deposits held by commercial banks.

Money creation by the commercial banking system.

Central bank and its functions (example of the Reserve Bank of India): Bank of issue, Govt. Bank, Banker's Bank, Control of Credit through Bank Rate, Cash Reserve Ratio (CRR), Statutory Liquidity Ratio (SLR), Repo Rate and Reverse Repo Rate, Open Market Operations, Margin requirement.

Unit 3: Determination of Income and Employment**30 Periods**

Aggregate demand and its components.

Propensity to consume and propensity to save (average and marginal).

Short-run equilibrium output; investment multiplier and its mechanism.

Meaning of full employment and involuntary unemployment.

Problems of excess demand and deficient demand; measures to correct them - changes in government spending, taxes and money supply.

Unit 4: Government Budget and the Economy**17 Periods**

Government budget - meaning, objectives and components.

Classification of receipts - revenue receipts and capital receipts;

Classification of expenditure – revenue expenditure and capital expenditure.

Balanced, Surplus and Deficit Budget – measures of government deficit.

Unit 5: Balance of Payments**18 Periods**

Balance of payments account - meaning and components;

Balance of payments – Surplus and Deficit

Foreign exchange rate - meaning of fixed and flexible rates and managed floating.

Determination of exchange rate in a free market, Merits and demerits of flexible and fixed exchange rate.

Managed Floating exchange rate system

Part B: Indian Economic Development

Unit 6: Development Experience (1947-90) and Economic Reforms since 1991:

28 Periods

A brief introduction of the state of Indian economy on the eve of independence.

Indian economic system and common goals of Five Year Plans.

Main features, problems and policies of agriculture (institutional aspects and new agricultural strategy), industry (IPR 1956; SSI – role & importance) and foreign trade.

Economic Reforms since 1991:

Features and appraisals of liberalisation, globalisation and privatisation (LPG policy);

Concepts of demonetization and GST

Unit 7: Current challenges facing Indian Economy

60 Periods

Human Capital Formation: How people become resource; Role of human capital in economic development; Growth of Education Sector in India

Rural development: Key issues - credit and marketing - role of cooperatives; agricultural diversification; alternative farming - organic farming

Employment: Growth and changes in work force participation rate in formal and informal sectors; problems and policies

Sustainable Economic Development: Meaning, Effects of Economic Development on Resources and Environment, including global warming

Unit 8: Development Experience of India:

12 Periods

A comparison with neighbours

India and Pakistan

India and China

Issues: economic growth, population, sectoral development and other Human Development Indicators

Part C: Project in Economics

20 Periods

Prescribed Books:

1. Statistics for Economics, NCERT
2. Indian Economic Development, NCERT
3. Introductory Microeconomics, NCERT
4. Macroeconomics, NCERT
5. Supplementary Reading Material in Economics, CBSE

Note: The above publications are also available in Hindi Medium.

Suggested Question Paper Design
Economics (Code No. 030)
Class XII (2024-25)
March 2025 Examination

Marks: 80

Duration: 3 hrs.

SN	Typology of Questions	Marks	Percentage
1	Remembering and Understanding: Exhibit memory of previously learned material by recalling facts, terms, basic concepts, and answers. Demonstrate understanding of facts and ideas by organizing, comparing, translating, interpreting, giving descriptions, and stating main ideas	44	55%
2	Applying: Solve problems to new situations by applying acquired knowledge, facts, techniques and rules in a different way.	18	22.5%
3	Analysing, Evaluating and Creating: Examine and break information into parts by identifying motives or causes. Make inferences and find evidence to support generalizations. Present and defend opinions by making judgments about information, validity of ideas, or quality of work based on a set of criteria. Compile information together in a different way by combining elements in a new pattern or proposing alternative solutions.	18	22.5%
	Total	80	100%

BLUE PRINT

Unit	Name of the unit	Allotted marks	Very short answer (Mcqs) (1mark)	Short answer type 1 (3 marks)	Short answer type 2 (4 marks)	Long answers (6 marks)	Total
	PART-A Macro Economics						
Unit 1	National Income and related aggregate	10 Marks	(1) 1	(1) 3	Nil	(1) 6	10 (3)
Unit 2	Money and Banking	6 Marks	(2) 1	Nil	(1) 4	Nil	6(3)
Unit 3	Determination of Income and Employment	12 Marks	(3) 1	(1) 3	Nil	(1) 6	12 (5)
Unit 4	Government Budget and The Economy	6 Marks	(2) 1	Nil	(1) 4	Nil	6(3)
Unit 5	Balance of payments and Its Components	6 Marks	(2) 1	Nil	(1) 4	Nil	6(3)
	PART-B Indian Economic Development						
Unit 6	Development Experience (1947-1990) And Economic Reforms Since 1991	12 Marks	(2) 1	Nil	(1) 4	(1) 6	12(4)
Unit 7	Current challenges Facing the Indian Economy	20 Marks	(4) 1	(2) 3	(1) 4	(1) 6	20(8)
Unit 8	Development Experience of India- A comparison with neighbours	8 Marks	(4) 1	Nil	(1) 4	Nil	8(5)
	Sub-Total	80 Marks	1(20) Marks	3(4) Marks	4(6) Marks	6(4) Marks	80(34)

Note: - Figures in Brackets Indicate the Number of questions and Figures outside the brackets indicate the marks for each question

INTRODUCTORY MACRO ECONOMICS

(PART A)

UNIT 1: NATIONAL INCOME AND RELATED AGGREGATES

What is Macroeconomics?

Basic concepts in macroeconomics: consumption goods, capital goods, final goods, intermediate goods; stocks and flows; gross investment and depreciation.

Circular flow of income (two sector model); Methods of calculating National Income--Value Added or Product method, Expenditure method, Income method.

Aggregates related to National Income:

Gross National Product (GNP), Net National Product (NNP), Gross Domestic Product (GDP) and Net Domestic Product (NDP) –

MACRO ECONOMICS: - Macro Economics is a branch of economics which studies economic problems relating to economy as whole, aggregate economic variables like level of income, output and employment.

List the differences between micro economics and macro economics.

Micro economics		Macro economics	
1.	Micro economics studies individual units of the economy. Ex: a firm, a consumer etc.	1.	Macro economics studies aggregates of the country. Ex. National income, inflation, unemployment.
2.	The main objective of micro economics is study of optimum allocation of resources.	2.	The important objective of macro economics is study of economic growth, determination of income and employment.
3.	Its important elements are demand and supply.	3.	It's key elements are aggregate demand and aggregate supply.
4.	It is also known as price theory	4.	It is also known as Income and employment theory.

Goods: In economics a good is defined as any physical object, manmade, that could command a price in the market and these are the materials that satisfy human wants and provide utility

Make differences between Consumer goods and Capital goods

CONSUMER GOODS	CAPITAL GOODS
1. These goods satisfy human wants directly	1. These goods satisfy human wants indirectly
2. These are used as final goods for consumption purpose	2. These are used for further production
3. These are relatively low value in comparison to capital goods	3. These goods are relatively of high value
4. These include durable, semi-durable, non-durable goods and services	4. These include durable and non-durable.

Q. Make differences between Intermediate goods and Final goods

INTERMEDIATE GOODS	FINAL GOODS
1. These goods used for further Production or for re-sale. SS	1. These are used for final consumption.
2. These are demanded by producers.	2. These are demanded by consumers.
3. These are within the production boundary.	3. These are outside the production boundary.
4. These goods will not be taken while calculating National Income.	4. These goods only will be considered while calculating National Income.

Q. Classify the following goods into intermediate goods and final goods:

(i) Milk purchased by a household. (ii) Purchase of rice by a grocery shop.

(iii) Purchase of an air conditioner for use in shop.

(iv) Cloth used for making a sofa-set by the carpenter.

(i) final good because milk directly satisfies the wants of the household(s) or the consumer(s).

(ii) intermediate good because rice is purchased for resale to its final users.

(iii) final good because air conditioner is investment expenditure as it adds to the capital stock

(iv) Cloth used for making a sofa-set by the carpenter is an intermediate good as it is used as a raw material.

Q Distinguish between Factor income and Transfer Income

Factor Income	Transfer Income
1. It is earned by factor of production like rent, interest, wages and profit	1. It is received by normal people, organization or country like gifts, grants and donations
2. It is earned due to some production process	2. It is received without any production process
3. It is included in national income	3. It is not included in national income
4. Eg. Rent, interest, profit, wages	Eg. Scholarship, gifts, grants, donations, aid

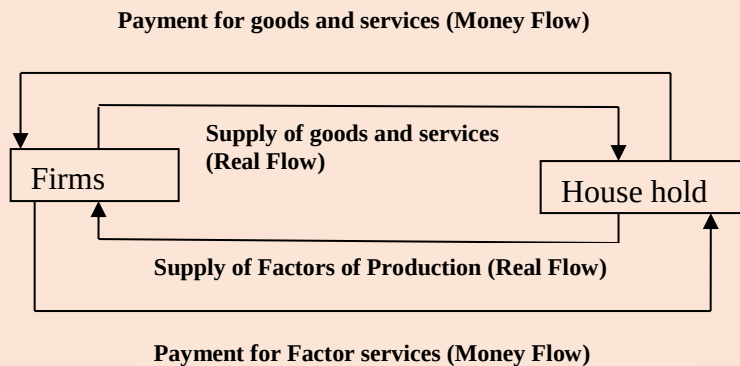
STOCK: - Quantity of an economic variable which is measured at a particular point of time. Stock has no time dimension. Stock is static concept.

FLOW: Flow is that quantity of an economic variable, which is measured during the period of time.

Stock Variable	Flow Variable
1. Stock is measured at point of time.	1.Flow is measured during a period of time. Like per hour, per day, per year.
2.Stock is static concept.	2.It is dynamic concept.
3. It does not have a time dimension	3. It has time dimension
4. Example: Wealth, capital. Money Supply	4. Example: Investment, income

CIRCULAR FLOW OF INCOME: It refers to the continuous circular movement of money and goods and services in an economy.

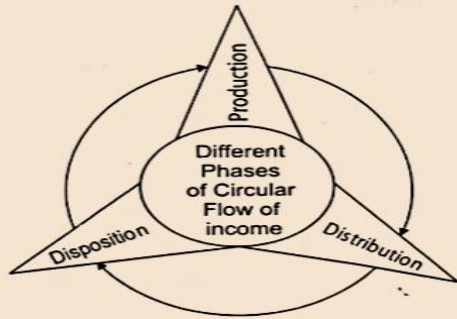
Circular flow in a two-sector economy.



Real flow: Under real flow, households render factor services to the firms and the firms produce goods and services to pay for the services.

Money flow: It includes all monetary payments by firms to households for their factor services and by households to the firm for the purchase of goods and services.

Base	Real flow	Money Flow
Meaning	It is the flow of goods and services between firms and households	It is the flow of money between firms and households
Exchange	It involves exchanges of goods and services	It involves exchange of money
Difficulty in Exchange	There may be difficulties of barter system in exchange of goods and services	There is no such difficulty in case of money flow



Production Phase: - Production unit assemble human factor of production and produce goods and services and payment to factors of production is made for their contribution in the production Example - Rent, wages.

2. Income Phase: - They get rewarded in the form of Rent, Wages, Interest, Profit.

3. Expenditure phase: - We have got unlimited wants. In order to satisfy these wants we spend our factor income and purchase goods and services.

LEAKAGES:

- Leakages in the circular flow of income are the economic activities that remove money from the circulation within an economy, causing a reduction in the overall flow of income. The primary types of leakages include savings (S), taxes (T), and imports (M).

INJECTIONS: Injections in the circular flow of income are the external economic activities that introduce money into the economy, thereby increasing the total income circulating within the system. Injections are classified into three main categories: government spending (G), investments (I), and exports (X).

INVESTMENT: - Investment is the net addition made to the existing stock of capital.

NET INVESTMENT: - Gross investment – depreciation.

DEPRECIATION: - It refers to fall in the value of fixed assets due to normal wear and tear, on passage of time and expected obsolescence. Also known as Consumption of Fixed Capital and Current Replacement Cost

INVENTORIES: -The unsold goods, unused raw materials or semi-finished goods which a firm carries from a year to the next.

There are two types of stock

1. **FIXED INVESTMENT:** - Stock of Assets in end of year – Stock of Assets in beginning of year.

2. **INVENTORY INVESTMENT:** - Stock of goods in end of year – stock of goods in beginning of year.

NET INDIRECT TAX (NIT) = Indirect Tax – Subsidies.

INDIRECT TAXES – Taxes impose by the government on production units., e.g. GST & Excise

Subsidies – Financial assistance given by the government to production units, e.g, LPG to house hold /

Fertilizer to farmer

GROSS DOMESTIC PRODUCT AT MARKET PRICE: -

It is the money value of all final goods and services produced during an accounting year with in the domestic territory of a country.

GROSS NATIONAL PRODUCT AT MARKET PRICE: -

It is a money value of all final goods and services produced by a country by normal residents during an accounting year including net factor income from abroad.

NET FACTOR INCOME FROM ABROAD (NFIA)

Net factor income from abroad is the difference between

(1) **Factor income earned by our residents from rest of world**, and

(2) Factor income earned by non-residents in our domestic territory

(3) NFIA =(Factor **income earned by our residents from rest of world** - Factor income earned by non residents in our domestic territory)
(NDP at FC +NFIA = NATIONAL INCOME)

COMPONENTS OF NET FACTOR INCOME FROM ABROAD: -

- ✓ Net compensation of employees: - (e.g Wage income of Indian workers working abroad)
- ✓ Net income from property and entrepreneurship: - (other than retained earnings of resident companies of abroad) Rent earned by Indian national for the property owned by them abroad and Profit earned by Indian from there, ventures established
- ✓ Net retained earnings of resident companies abroad (Dividend earned)

FORMULAE

- $NNP_{MP} = GNP_{MP} - \text{Depreciation}$
- $NDP_{MP} = GDP_{MP} - \text{Depreciation}$
- $NDP_{FC} = NDP_{MP} - \text{Net indirect taxes (Indirect Tax – Subsidies)}$
- $GDP_{FC} = NDP_{FC} + \text{Depreciation}$
- $GDP_{MP} = NDP_{FC} + \text{Depreciation} + \text{Net Indirect Tax}$
- $GNP_{MP} = NDP_{FC} + \text{Depreciation} + \text{Net Indirect Tax} + \text{NFIA}$
- $GNP_{FC} = NDP_{FC} + \text{Depreciation} + \text{NFIA}$
- $NNP_{FC} = GDP_{MP} - \text{Depreciation} + \text{Net factor income from abroad} - \text{Net indirect taxes}$
- (NNP_{FC} is the sum total of factor income earned by normal residents of a country during the accounting year)

$NNP_{FC} = NDP_{FC} + \text{Net factor income from abroad.}$

Concept of domestic (economic) territory

Domestic territory is a geographical territory administered by a government within which persons, goods and capital circulate freely. (Areas of operation generating domestic income, freedom of circulation of persons, goods and capital)

Political frontiers including territorial waters and air space.

Embassies, consulates, military bases etc. located abroad but including those located within the political frontiers.

Ships, aircrafts etc., operated by the residents between two or more countries.

Fishing vessels, oil and natural gas rigs etc. operated by the residents in the international waters or other areas over which the country enjoys the exclusive rights or jurisdiction.

Resident (normal resident): -

Normal resident is a person or an institution who ordinarily resides in that country and whose center of economic interest lies in that country.

The Centre of economic interest implies: -

- (1) the resident lives or is located within the economic territory.
- (2) The resident carries out the basic economic activities of earnings, spending and accumulation from that location
3. His centre of interest lies in that country.

Relation between national product and Domestic product.

Domestic product concept is based on the production units located within domestic (economic) territory, operated both by residents and non-residents.

National product concept based on resident and includes their contribution to production both within and outside the economic territory.

National product = Domestic product + Residents contribution to production outside the economic territory (Factor income from abroad) - Non- resident contribution to production inside the economic territory (Factor income to abroad)

Methods of calculation of national income**I - PRODUCT METHOD (Value added method):**

- Sales + change in stock = Value of output
- Change in stock = Closing Stock – Opening Stock
- Value of output - Intermediate consumption = Gross value added (GDP_{MP})
- $NNP_{FC} (N.I) = GDP_{MP} (-) \text{ consumption of fixed capital (depreciation)}$

(+) Net factor income from abroad

(-) Net indirect tax.

1. Sale = Price x Quantity or Sale = Domestic sale + Exports

2. Value of output = Sales + Change in stock (Change in stock = Closing stock – opening stock)

3. Gross value added (GDP_{MP}) = Value of output – Intermediate cost

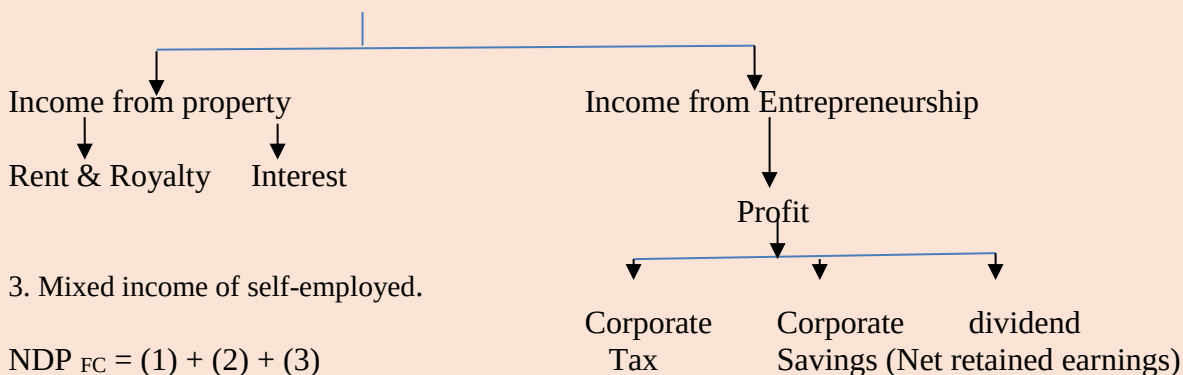
4. NNP_{FC} or NI = GDP_{MP} – Consumption of fixed capital (Depreciation) + Net Factor Income from Abroad – Net indirect Taxes

Distinction between value of output, value added and value of income generated

Basis	Value of Output (Sale)	Value added (Profit)	Value of income generated
Meaning	It is the monetary value of all the goods and services produced during the accounting year in the economy	It is addition to the total value of goods at different stages	It is the value of income earned the factors of product in the form of wages, rent, interest and profit during the accounting year
Calculation	It is calculated by multiplying the units of goods produced with their respective price	It is excess of sale price of goods over the cost of the goods	It is calculated by totaling the factor income earned by wages, interest, rent & profit.
Concept	It is broader concepts which include both the value of intermediate as well as final goods	It is a narrow concept, it is value of output fewer intermediate goods	In other words, it is value added less(net) indirect tax

INCOME METHOD/FACTOR PAYMENT METHOD

1. Compensation of employees. + 2. Operating surplus.



3. Mixed income of self-employed.

$$\text{NDP}_{\text{FC}} = (1) + (2) + (3)$$

$$\text{NNP}_{\text{FC}} = \text{NDP}_{\text{FC}} (+) \text{Net factor income from abroad}$$

$$\text{GNP}_{\text{MP}} = \text{NNP}_{\text{FC}} + \text{Consumption of Fixed Capital (CFC)} + \text{Net indirect tax (NIT)} \\ (\text{Indirect tax} - \text{subsidy})$$

1. COMPENSATION OF EMPLOYEES (COE) = Wages and salaries in cash + Wages and salaries in kind + Employer's contribution in social security scheme + Retirement pension

Cash: - Basic pay Rent, Dearness allowance, Interim relief Family allowance 3 House rent allowance, City compensatory allowance, Bonus /commission, Leave travel commission, Sick leave allowance

Kind: - free accommodation, Medical facilities, Educational facilities, Free food & lodging, Free supply of water & electricity, Conveyance facilities

Employer's contributions: - Contributory provident fund, Private pension, Contribution towards life

insurance, Contribution towards other social security schemes

2. OPERATING SURPLUS (OS)= Income from Property + income from entrepreneurship

➤ (Income from property = Rent + Royalty + Interest)

➤ (Income from entrepreneurship = Profit)

➤ (Profit = Corporate tax + Corporate savings / Net retained earnings / Undistributed profit + Dividend

3. MIXED INCOME OF SELF-EMPLOYED: - Income of self-employed is known as mixed income. In other words, mixed income is the total of wage and non-wage income. Non-wage income means income from property. In certain case it is very difficult to distinguish between income from work and income from property. For ex: a sole trader is both an employee of this firm and also the owner of the firm. As an employee he should get wages and as an owner he will receive profit. It is quite difficult to separate his wage income from the non-wage income. This is why it is mixed income.

EXPENDITURE METHOD:

1. Government final consumption expenditure.

2. Private final consumption expenditure.

3. Net Export.

4. Gross domestic capital formation.

$$\begin{array}{ccc} \text{Gross Domestic fixed} & + & \text{Change in stock} \\ \text{Capital formation} & & \text{(Closing Stock – Opening Stock)} \\ \text{GDP}_{MP} = (1) + (2) + (3) + (4) \end{array}$$

$$\text{NNP}_{FC} = \text{GDP}_{MP} - \text{consumption of Fixed Capital} + \text{NFIA} - \text{Net Indirect Taxes}$$

Note: If capital formation is given as Net domestic capital formation we arrive at NDP_{MP} .

Capital formation = Investment

IMPLICATIONS OF THE CONCEPTS OF ECONOMIC TERRITORY AND RESIDENTL-

National income and related aggregates: are basically measures of production activity. There are two categories of national income aggregates: domestic income and national income, or domestic product and national product. DOMESTIC PRODUCT: - Domestic product Includes production activity of the production units located in the economic territory Irrespective of whether owned by the residents or non-residents.

Gross Domestic Product (GDP). Net Domestic Product (NDP) are some examples.

Illustrative example: How Will you treat the following while estimating domestic product (or domestic factor income) of India?

- (i) Rent received by an Indian resident from his property in Singapore
- (ii) Salaries received by Indian residents working in Russian embassy in India
- (iii) Profits earned by a foreign company or a foreign bank in India
- (iv) Salaries paid to Koreans working in Indian embassy in Korea
- (v) Compensation of employees to the resident of Japan working in Indian embassy in Japan
- (vi) Profits made by a branch of State Bank of India in Japan

Answer:

(i) No, it will not be included in domestic factor income of India because this income is earned outside domestic territory (economic territory) of India. It is factor income earned abroad.

(ii) No, it will not be included in domestic factor income of India because Russian embassy in India is not a part

of domestic territory of India. So, this income is not earned within the domestic territory of India. It is factor income from abroad

(iii) Yes, it will be included in domestic factor income of India because the foreign company or the foreign bank is located within the domestic territory of India. So, it is an income earned within the domestic territory of India

(iv) Yes, it will be included in domestic factor income of India because this income is earned within the domestic territory of India. Indian embassy in Korea is a part of the domestic territory of India.

(v) Yes, it will be Included as It is part at factor income earned in domestic territory of India, though earned by non-resident.

(vi) No, as profits are not earned within the domestic territory of India. It is factor income from abroad

NATIONAL PRODUCT - National product Includes production activities of residents irrespective of whether performed within the economic territory or outside it.

Gross National Product (GNP). Net National Product (NNP) are some examples.

Illustrative example:

Will the following be included in Gross National Product (GNP)? Give reasons.

(i) Profits earned by a foreign company or a foreign bank in India

(ii) Salary paid to Americans working in Indian Embassy in America

(iii) Salaries received by Indian residents working in Russian Embassy in India

(iv) Dividend received by an Indian from his investment in share of a foreign company

Answers: (I) No, because it is a factor income earned by a non-resident (a foreign company or a foreign bank) from its contribution to production inside the domestic territory of India i.e., factor income paid to abroad.

(ii) No. because this Factor income is paid to non-residents i.e., factor income to abroad.

(iii) Yes, because it is a factor income earned by Indian residents outside the domestic territory of India i.e., factor income from abroad.

(iv) Yes, because it is a factor income earned by a resident from outside the domestic territory of India. i.e., factor income from abroad.

NET FACTOR INCOME FROM ABROAD (NFIA): - Factor Income Received from Abroad (FIFA) – Factor income Paid to Abroad (FITA)

NFIA = Net Compensation of Employees + Net income from property and entrepreneurship + Net Retained earnings.

- Net Factor Income from Abroad is the excess of factor incomes (rent, wages, interest and profit) earned from abroad over factor incomes (rent, wages, interest and profit) paid to abroad. NFIA can be positive, negative or zero.
- it is positive when factor income from abroad is more than factor income paid to abroad.
- It is negative when factor income from abroad is less than factor income paid to abroad.
- it is zero when factor income from abroad is equal to factor income paid to abroad.

PRECAUTIONS OF VALUE-ADDED METHOD:

The various precautions to be taken in Value Added Method are:

Intermediate Goods are not to be included in N.I.

Sale and Purchase of second-hand goods is not included.

Production of services for self consumption (Domestic Services) is not included.

Production of Goods for self consumption is included.

Imputed value of owner-occupied houses should be included.

Change in stock of Goods (inventory) will be included

PRECAUTIONS OF INCOME METHOD - For correct computation of national income by income method, following precautions need to be taken:

Transfer Incomes are not included in the N.I.

Income from sale of second-hand goods will not be included.

Income from sale of shares, bonds and debentures will not be included.

Windfall gains.

Imputed value of services provided by owners of production units will be included.

Payments out of past savings are not included in the N.I.

Indirect Taxes are not included in N.I. at factor cost

PRECAUTIONS OF EXPENDITURE METHOD:

The various precautions to be taken while using the Expenditure Method are:

Expenditure on Intermediate Goods will not be included in the National Income.

Transfer payments are not included.

Purchase of second-hand goods will not be included.

Purchase of financial assets (shares, debentures, Bonds) will not be included.

Expenditure on own account production will be included in the National Income.

REAL GDP AND NOMINAL GDP: -

Nominal GDP: -1 Nominal Gross Domestic Product is a way of measuring the market value of all final goods and services produced in an economy at current market prices in a Financial Year.

Real GDP: - Real Gross Domestic Product is a way of measuring the market value of all final goods and services produced in an economy at base year (constant) prices in a Financial Year.

Basis for Comparison	Nominal GDP	Real GDP
Meaning	The nominal GDP is the sum total of the economic output produced in a year which valued at the current market price	The real GDP is the sum-total of the economic output produced in a year which valued at base year price
How does inflation affect it	The nominal GDP does not take inflation into account.	The real GDP takes inflation into account, It is called inflation adjusted GDP.
Growth of the economy	From the nominal GDP, we cannot analyze economic growth easily	From the real GDP, we can explore economic growth easily
Formula	Real GDP= $Q \times P^*$ where, Q= quantity of final g/s produced during an accounting year. P^*= prices prevailing in the base year.	Nominal GDP= $Q \times P$ where, GDP= $Q \times P$ where, Q= quantity of final g/s produced during an accounting year. P= prices prevailing in the current year.

GNP DEFLATOR: Nominal GDP/ Real GDP X 100

GDP AND WELFARE: - Real GDP is considered as an index of welfare of the people. Welfare of the people is measured in terms of the availability of goods and service per person. Higher the growth of GDP, greater is the flow of goods and services. Greater is the availability of goods and services per person.

Limitations of GDP as the measure of Economic Welfare GDP is the best indicator of economic welfare. But there are many reasons it is not an adequate measure of it. There are many reasons to support this argument

1. Non-Monetary Exchanges: - These activities are non-monetary and non-market transactions. For example: - 1. Services of Housewife. 2. Kitchen gardening 3. Services of family members to each other. 4. Own account production These activities are left out from GDP on account of the non-availability of data and the problem of evaluation. However, such activities contribute to the economic welfare.

2. Externalities: - It refers to the Positive or Negative effect of any Economic activity without paying price or penalty of it. Activities resulting in benefits are called positive externalities and increase in welfare and activities resulting in harm are called negative externalities and resulting in decrease in welfare. GDP does not consider

such externalities. For example, construction of a flyover results in flow of goods and services and counted in GDP. But the flyover reduces the transport cost and journey time to those who have not contributed into its construction. On the other hand, a plastic factory provides employment in the locality. It is counted in GDP, but

the negative externalities such as pollution spread by it making people sick are not counted.

3. Distribution of GDP: - The GDP does not consider the unequal distribution of income in a country. It may possible with rise of GDP, unequal distribution of GDP may also rise. It means the income of rich people rises by many folds than the common man. Overall GDP would seem to rise, but richer are getting richer, poorer are getting poorer.

4. Composition of GDP: - The GDP Consists of both Consumer and Capital Goods. But Consumer goods Contributes directly for the welfare whereas the Capital goods contributes indirectly

NUMERICALS FOR PRACTICE

Calculate Factor Income to abroad	crores)
(i) Gross national product at FC	3,750
(ii) Compensation of employees	2000
(iii) Net exports	(-)50
(iv) Profit	700
(v) Net domestic capital formation	1000
(vi) Opening stock	150
(vii) Closing stock	200

(viii) Gross fixed capital formation	1050
(ix) Interest	600
(x) Rent	400
(xi) Factor income from abroad	20

Ans: (-) 20

Calculate intermediate consumption from the following data	Ans.340
Items	(` in lakhs)
(i) Value of output	2000
(ii) Depreciation	40
(iii) Subsidy	10
(iv) Sales tax	30
(v) Net Value Added at factor cost	1600

From the following data, calculate National Income by Income Method:	Ans.2010
Items	(` in crores)
(i) Interest	150
(ii) Rent	250
(iii) Government final consumption expenditure	600
(iv) Private final consumption expenditure	1200
(v) Profits	640
(vi) Compensation of employees	1000
(vii) Net factor income to abroad	30
(viii) Net indirect taxes	60
(ix) Net exports	-40
(x) Consumption of fixed capital	50
(xi) Net domestic capital formation	340

Calculate net value added at factor cost from the following:	Ans.700
Items	(` in lakhs)
(i) Net factor income from abroad	30
(ii) Sales	3500
(iii) Purchase of intermediate goods	2000
(iv) Consumption of fixed capital	500
(v) Exports	400
(vi) Indirect taxes	350
(vii) Change in stock	50

Calculate GNPFC from the given data: Ans. 190	(` in crores)
(i) Indirect tax	50
(ii) Consumption of fixed capital	60
(iii) Net factor income received from abroad	-10
(iv) NDPFC	120
(v) Net current transfers paid to rest of the world	30
(vi) Subsidies	25

Find Gross Value Added at Market Price from the given data: Ans. 80	(`Lakh)
(i) Depreciation	20
(ii) Domestic sales	200
(iii) Net change in stocks	-10
(iv) Exports	10
(v) Single use producer goods	120

**.From the following data, calculate Gross national product at Market Price by
(i) Income method. (ii) Expenditure method: Ans: 1700 Crs**

(i) Mixed income of self-employed	400
(ii) Compensation of employees	500
(iii) Private final consumption expenditure	900
(iv) Net factor income from abroad	(-)20
(v) Net indirect taxes	100
(vi) Consumption of fixed capital	120
(vii) Net domestic capital formation	280
(viii) Net exports	(-)30
(ix) Profits	350
(x) Rent	100
(xi) Interest	150
(xii) Government final consumption expenditure	450

From the following data calculate National Income by	Ans.3700Cr
(i) Income method and (ii) Expenditure method.	(Rs. In Crores)
(i) Compensation of employees	1200
(ii) Net factor income from abroad	(-)20
(iii) Net indirect taxes	120
(iv) Profit	800
(v) Private final consumption expenditure	2000
(vi) Net domestic capital formation	770
(vii) Consumption of fixed capital	130
(viii) Rent	400
(ix) Interest	620
(x) Mixed income of self- employed	700
(xi) Net exports	(-)30
(xii) Government final consumption expenditure	1,100

CALCULATE NNP AT MARKET PRICE BY PRODUCTION METHOD AND INCOME METHOD (Ans: 1340 Cr)		
1	Inter mediate consumption	
	(a) primary sector	500
	(b) Secondary sector	400
	(c) tertiary sector	300
2	Value of output of	
	(a) primary sector	1,000
	(b) Secondary sector	900
	(c) tertiary sector	700
3	Rent	10
4	Emoluments of employers	400
5	Mixed income	650
6	Operating surplus	300
7	Net factor income from abroad	-20
8	Interest	5
9	Consumptive of fixed capital	40
10	Net indirect tax	10

Ans: NNP_{MP} by production method

(2) Value of output – (1) Intermediate conspn = value added at MP

(2) a + b + c – (1) a + b + c

1000 + 900 + 700 – 500 + 400 + 300

2600 – 1200, 1400 = GDP_{MP}

NNP_{MP} = GDP_{MP} – (9) + (7), = 1400 – 40 + (-20), NNP_{MP} = 1340

KVS ZIET MYSORE

VERY SHORT ANSWER TYPE QUESTIONS AND ANSWERS

1) *Define Macro Economics.*

2) Macro Economics is that branch of economics which studies economic problems relating to economy as whole, like level of output and employment.

3) *What are called Consumption Goods?*

Consumption goods are those goods that satisfy the wants of consumers directly. For example: Television, mobile phones etc.

4) *What are the different types of consumption goods?*

(a) *Durable Goods:* Durable goods are those goods that can be used again and again for a long period of time. For Example: Television, house etc.

(b) *Semi durable goods:* Semi durable goods are those goods that can be used again and again for a short period of time, usually less than a year. Example: foot wear, clothes etc.

(c) *Non – durable Goods:* Goods that can be used only once are called non-durable goods. For example: milk,

(d) bread, food grains etc.

(e) *Services:* Services are non-material goods that directly satisfy human wants. For example: Services of teachers, doctors etc.

5) *What are called Capital Goods?*

Capital goods are those final goods which help in the production of other goods and services. For example: Machines, tools and equipments.

6) *What are called final goods?*

Final goods are those goods which are used either for direct consumption or for investment. Milk and bread are final goods purchased by a household for consumption. Machines and equipments are final goods bought by a firm for capital formation.

7) *What are called Intermediate goods?*

Goods that are used up in production process and goods that are bought for resale are called intermediate goods. Wheat flour bought by a bakery and bread bought by a grocery shop are intermediate goods.

8) *What do you mean by Gross Investment?*

Total addition made to the capital stock of an economy during a period of time/ year is called Gross Investment. Capital stock includes fixed assets and unsold stock. It is also known as Capital formation.

9) *What is Net Investment?*

a. The actual addition made to the capital stock of an economy during a year is called Net Investment.

b. $\text{Net Investment} = \text{Gross Investment} - \text{Depreciation}$.

10) *What is depreciation?*

Depreciation refers to fall in the value of fixed assets as a result of normal wear and tear, passage of time or expected obsolescence.

11) *Define stocks.:*

Variables whose magnitude is measured at a particular point of time are called stock variables. Example: 100 crore population of India in 2001.

12) *Define flows.*

Variables whose magnitude is measured over a period of time are called flow variables. Example:

Monthly wages of a worker, production of cloth during a year

13) *Define gross investment.*

Total addition of capital goods to the existing stock of capital during the given year is called Gross Investment.

14) *Define circular flow of income.*

Circular flow of income refers to flow of income between the major sectors of an economy.

15) *Define National Income*

It is the money value of the final goods and services produced in an economy during a particular year.

16) *Define Gross Domestic Product (GDP).*

Gross domestic product (GDP) refers to the money value of final goods and services produced in an economy during a particular year and is inclusive of consumption of fixed capital.

17) *What are factor incomes?*

Income received in return for rendering productive service is called a factor income (or factor payment.)

The various factor incomes are rent, interest, wages and salaries and profits. They are earned incomes so included in the national income.

18) *What is a positive externality?*

Activity resulting in benefits to others is called a positive externality.

19) *What is a negative externality?*

Activity resulting in harm to others is called a negative externality.

20) *Define 'Nominal GNP'*

GNP measured in terms of current market prices is called nominal GNP.

21) *Define 'Real GNP'.*

GNP that is computed as per constant prices is called real GNP. It is expressed in physical quantities.

22) *Define final product or final goods.*

Final products refer to the products purchased or own produced, for the purpose of consumption and Investment

23) *Define depreciation or consumption of fixed capital formation*

Depreciation/Consumption of fixed capital refers to the fall in the value of fixed capital good due to normal wear and tear and foreseen obsolescence.

24) *What are transfer payments?*

Transfer payments are payments made without rendering any goods or services in return, e.g., old age pension, scholarships, gifts, etc. These are unilateral payments (or receipts)

25. *Who are Normal Residents?*

Normal Residents are those individuals and institutions who normally reside in a country for more than one year, and whose centre of economic interest lies in that country.

26. *What do you mean by domestic territory?*

Domestic territory includes the following:

- (i) Land within the borders of the country.
- (ii) Ships and aircrafts owned and operated by normal residents.
- (iii) Fishing boats, oil and natural gas rigs and floating platforms operated by the residents of a country in the international waters where they have exclusive rights of operation.
- (iv) Embassies, consulates and military establishments of a country located abroad.

27. *Briefly explain the concept of Net Indirect Tax.*

Net Indirect Tax is the difference between Indirect Tax paid by the firms to the Government and the Subsidies paid by the Government to firms. This concept is used to obtain the national income at factor cost or factor prices. The NIT is deducted from market price (MP) to get factor cost (FC).

28. Explain the concept of Net Factor Income from Abroad (NFIA)? What are its components?

NFIA refers to the difference between factor income received from the rest of the world and factor income paid to the rest of the world.

$NFIA = \text{Factor income earned from abroad} - \text{Factor income paid to abroad.}$

29. *Explain the difference between Nominal GDP and Real GDP. Which of these is a better index of welfare of people? Why?*

NOMINAL GDP; - Nominal GDP is the market value of all final goods and services produced in a country in a year. Increase in prices will lead to increase in nominal GDP. $\text{Nominal GDP} = \text{Output} \times \text{Current year prices.}$

REAL GDP; - Real GDP refers to GDP at constant prices. It is the value of goods and services produced in the current year, taking base year prices in to consideration. Formula to calculate real GDP

MULTIPLE CHOICE QUESTIONS (MCQ)

1. Which of the following represents national income?

- (a) GDP_{mp} (b) NDP_{fc} (c) NNP_{fc} (d) GNP_{fc}

2. National income is equal to:

- (a) GDP_{mp} – Depreciation (b) NNP_{mp} – Net indirect taxes
(c) GNP_{fc} – Depreciation (d) Both (b) and (c)

3. Which one of the following statements is correct?

- (a) Market price + Net indirect taxes = Factor cost
 (b) Market price – Net indirect taxes = Factor cost
 (c) Both (a) and (b) (d) None of these
4. Goods purchased for the following purpose are final goods: (Choose the correct alternative)
 a) For satisfaction of wants b) For investment in firm
 c) Both (a) and (b) d) None of these
5. In which type of economy domestic income is equal to national income?
 (a) Open economy (b) Closed economy (c) Capitalist economy (d) Socialist economy
6. Which of the following makes GDP an inappropriate index of welfare?
 (a) Non- monetary transactions (b) Externalities
 (c) Composition and distribution of GDP (d) All of these
7. Real national income refers to:
 (a) National income at current prices (b) National income at factor cost
 (c) National income at constant prices (d) National income at market price
8. Which one of the following is intermediate good?
 (a) Furniture purchased by a school (b) Refrigerator purchased by sweet shop
 (c) Machine installed by a factory (d) Sugar purchased by sweet shop
9. Which of the following is included in domestic territory of India?
 (a) SBI branch in London (b) Microsoft office in USA
 (c) An American company in India (d) American embassy in India
10. What is the basis of the difference between the concepts of market price (MP) and factor cost (FC)
 (A) Net Indirect Taxes (B) Indirect Taxes (C) Direct Taxes (D) Subsidies
11. The difference between the National Income and Domestic Income is
 (A) Consumption of Fixed Capital (B) Net Indirect Taxes
 (C) Net Factor Income From Abroad (D) Both (A) and (B)
12. A sum of Rs.10000 has been given to a flood victim. This will be considered as-
 (A) Compensation of employee (B) Fixed Investment
 (C) Factor Income (D) Transfer Payment
13. In the production of sugar, sugarcane is
 a) A final good b) A capital good c) An intermediate good d) None of these

14. Capital goods are those goods

- a) Which are used in production for several years
- b) Which are used in production process for few years
- c) Which involve depreciation losses d) Both (a) and (c)

15 Net investments is equal to

- a) Gross investment + depreciation b) Gross investment – depreciation
- c) Gross investment X depreciation d) Gross investment/ depreciation

16 Net capital formation causes

- a) Increase in production capacity b) Increase in depreciation
- c) Increase in profit d) Increase in cost

17. Which of the following leads to depreciation?

- a) Normal wear and tear b) Natural calamities
- c) Changes in technology d) None of these

18. A quantity measured per period of time is known as

- a) Stock variable b) Flow variable c) Inventory d) None of these

19. Which of the following is a flow variable?

- a) Consumption b) Wealth c) Quantity of money d) None of these

20. Which one includes depreciation?

- a) GNP at market price b) NNP at market price
- c) NNP at factor cost d) None of these

21. Which of following is not a transfer payment?

- a) Interest on national debt b) Retirement pension
- c) Old age pension d) Donations

22. Goods purchased for the following purpose are final goods: (Choose the correct alternative)

- a) For satisfaction of wants b) For investment in firm
- c) Both (a) and (b) d) None of these

23. Stock of man-made goods which are used for further production is called:

- (A) Investment (B) Capital stock (C) Capital formation (D)Both A and C

24. Which of the following is not a flow variable?

- (A) Income (B) Capital formation (C) Supply of money in a country
(D) Leakage of water from the overhead tank

25. Money flows are the reciprocal of:

- (A) Monetary flows (B) Real flows (C) Circular flows (D) Inventory flows

26. Economic territory of a country in which economic activities of the country generates its domestic income is called:

- (A) National territory (B) Domestic territory
(C) Political territory (D) Geographical territory

27. Which of the following is an example of normal residents of India?

- (A) Foreign worker working in WHO located in India
(B) The German working as director in IMF office located in India
(C) Ambassador in India from rest of the world
(D) Ambassador of India in rest of the world

28. If $NDP_{fc} = 4300$, depreciation = 1350, subsidies = 250, NFIA = 330, GDP_{mp} will be:

- (A) 2370 (B) 2700 (C) 5400 (D) 6230

29. Operating surplus =

- (A) Rent + Interest + Profit (B) COE + Mixed Income Of Self- Employed
(C) COE + Rent + Interest + Profit
(D) COE + Rent + Interest + Profit + Mixed Income Of Self- Employed

30. Why are the intermediate goods not included in the National Income while measuring National Income?

- (A) To avoid double accounting (B) It decreases income
(C) Intermediate goods are not good (D) All of these

31. Goods which are purchased for resale are :

- (A) final goods (B) capital goods (C) intermediate goods (D) none of these

32. Addition to the capital stock of an economy is termed as :

- (A) Investment (B) Capital loss (C) Consumption of fixed capital (D) All of these

33. A car purchased by a dealer of cars is :

- (A) consumer good (B) capital good (C) intermediate good (D) all of these

34. Net factor income from abroad is:

- (A) Exports minus Imports (B) Visible Exports minus Visible Imports
(C) Factor incomes received from abroad minus Factor incomes paid abroad

(D) Factor incomes received from abroad

35. American embassy in India is a part of domestic territory of:

- (A) India (B) America (C) Both (A) and (B) (D) Neither (A) nor (B)

36. Domestic Income is greater than National Income

- (A) Never (B) May or May not (C) Always (D) None of these

37. Which of the following is not a 'factor payment'?

- (A) Free uniform to defence personnel (B) Salaries to the Members of Parliament
(C) Rent paid to the owner of a building (D) Scholarship given to the students

38. If in an economy, the value of Net Factor Income from Abroad is Rs. 200 crores and the value of Factor Income to Abroad is Rs. 40 crores, identify the value of Factor Income from Abroad.

- (A) Rs. 200 crores (B) Rs. 160 crores (C) Rs. 240 crores (D) Rs. 180 crores

39. National Income is the sum of factor incomes accruing to:

- (A) Nationals (B) Economic territory
(C) Residents (D) Both residents and non-residents

40. Which one of the following is an intermediate product? (Choose the correct alternative)

- a) Purchase of pulses by consumers b) Machine purchased by a firm
c) Wheat used by a flour mill d) Wheat used by households

41. Which of the following is an example of an intermediate good?

(Choose the correct alternative)

- a) Copper purchased for making utensils b) Steel and cement used to construct a timer
c) Fertilizers purchased by a farmer d) All of these

42. Which of the following is an example of consumer non-durable good?

(Choose the correct alternative)

- a) Milk b) Bread c) Both (a) and (b) d) Clothes

43. Which of the following does not explain the concept of depreciation?

(Choose the correct alternative)

- a) An annual allowance for wear and tear of a capital good.
b) Cost of the capital good (minus scrap value) divided by number of years of its useful life.
c) Unexpected or sudden destruction or disuse of capital as can happen with accidents, natural calamities etc.
d) Maintenance and replacement cost of existing capital goods. etc.

44. Which of the following is within the domestic territory of India?

(Choose the correct alternative)

- a) State Bank of India in Japan **(b)** Google office in India
- c) Office of Tata Motors in UK (d) The USA Embassy in India

45 Out of the following, who are residents of India?

(Choose the correct alternative)

- (a) Indians working permanently in the office of the United Nations Organization in New York
- (b) Indians working in Indian Embassy in America
- (c) Indians working in a branch of an American Bank in India
- (d) Americans working in India embassy in America

MCQ ANSWER KEY	
1 (c) NNP _{fc}	24 (C)
2 (d) Both (b) and (c)	25 (B)
3 (b) Market price – Net indirect taxes = Factor cost	26 (B)
4 (c)	27 (D)
5 (b) Closed economy	28 (C)
6 (d) All of these	29 (A)
7 (c) National income at constant prices	30 (A)
8 (d) Sugar purchased by sweet shop	31 (C)
9 (c) An American company in India	32 (A)
10 (A) Net Indirect Taxes	33 (C)
11 (C) Net Factor Income From Abroad	34(C)
12 (D) Transfer Payment	35(B)
13 c	36(B)
14 d	37 (D)
15 b	38 (C)

16 a	39(D)
17 a	40 (C)
18 b	41 (D)
19 a	42 (C)
20 a	43 (C)
21 b	44 (B)
22 (c)	45 (C)
23 (B)	

ASSERTION AND REASON QUESTIONS

In the following questions, a statement of Assertion (A) followed by a statement of Reason (R) is given. Choose the correct answer out of the following choices.

- (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A),
- (b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A),
- (c) Assertion (A) is true but Reason (R) is false
- (d) Assertion (A) is false but Reason (R) is true.

1. Assertion (A): Microeconomics is the study of an individual unit of a commodity
Reason(R): - The basic tools of microeconomics are demand and supply
2. Assertion (A): - Stationary purchased in a school is an intermediate good
Reason(R): - Intermediate goods once used in production lose their utility.
3. Assertion (A): - If the GDP of a country is rising the welfare may not rise as a consequence.
Reason(R): - The rise in GDP may be concentrated in the hands of very few individuals.
4. Assertion (A): - Domestic Income is less than National Income, when NFIA is negative
Reason(R): - National Income is transfer Income
5. Assertion (A): - Real GDP is better index of economic growth than the nominal GDP
Reason(R): - The Index of Real GDP always reflects a change in the level of output.
6. Assertion (A): - The difference between Gross and Net investment is Consumption of Fixed capital

Reason(R): The difference between Net indirect tax is Indirect tax and Subsidy-

7. Assertion (A): Real GDP is better indicator of economic growth than nominal GDP.

Reason (R): Real GDP eliminates the change in prices.

8. Assertion (A): Higher level of GDP does not ensure higher level of social welfare.

Reason (R): Level of GDP does not focus on the composition and distribution of income.

9. Assertion (A): GDP_{mp} is the sum total of market value of all final goods and services produced in the domestic territory during an accounting year.

Reason (R): GNP_{fc} is the sum total of market value of final goods and services produced by the normal residents of a country during an accounting year.

10. Assertion (A): We can convert domestic income into national income.

Reason (R): Net indirect taxes are the difference between domestic income and national income.

11. Assertion (A): The concept of normal resident is important for national income estimation.

Reason (R): The concept of normal resident is different from the concept of citizen of a country.

12. Assertion: Gross Domestic Capital Formation can be less than Gross Fixed Capital Formation.

Reason: Change in Stock is negative.

13. Assertion: Government should increase its investment expenditure to increase GDP

Reason: Government should spend more on health infrastructure.

14. Assertion: A change in taste and preference of Indian consumer towards MNCs and imported goods leads to decrease in GDP

Reason: expenditure on imports of goods is subtracted from final expenditure in order to estimate GDP.

15. Assertion: Expansion of Indian industries abroad leads to increase in national income of the country.

Reason: Retained earnings of resident companies abroad are included in national income.

16. Assertion (A) India's GDP is forecast to contract 5.9% in 2020 and recover to 3.9% next year, the UNCTAD report said.

Reason(R) India is experiencing impacts of worldwide deep recession amid a still unchecked pandemic.

- 17 Assertion (A) GDP can never be greater than GNP

Reason (R) NFIA can never be negative

18. Assertion (A) Goods that are ultimately consumed rather than used in the production of another good are known as final goods

Reason(R) Components sold to car manufacturer are type of final goods.

19. Assertion (A) Income from self-consumption is to be included in National Income.

Reason (R) A house owner living in his own house is assumed to be paying rent to himself for using up the factor services.

20. Assertion (A) The GNP is the value of goods and services produced annually in the Nation.

Reason(R) The most comprehensive measure of national output is the GNP.

21. Assertion: Factor income is bilateral income.

Reason: Factor income is earned for contributing to production process.

22. Assertion: Bread is final good for consumers

Reason: Bread is made with wheat flour which is intermediate good

23. Assertion: Transfer income is not included in the national income.

Reason: Transfer income is a unilateral concept.

24. Assertion: Subsidy is transfer payment.

Reason: Subsidy contributes to current flow of goods and services.

25. Assertion: Depreciation is also termed as Consumption of fixed capital.

Reason: Depreciation refers to that value of fixed capital which is used up in the process of production.

26. Assertion: Intermediate goods have direct demand.

Reason: The demand for intermediate goods depends on demand for final goods.

27. Assertion: Domestic income of a country can be more than its National income

Reason: Factor income paid abroad < Factor income received from abroad.

28. Assertion: A good that will not pass through any more stages of production or transformation is called a final good.

Reason: Value of final good is included in National Income.

29. Assertion: Nominal value is money value or value measured in terms of prices that prevail at the time of measurement.

Reason: GDP is measured at both current prices as well as constant prices.

30. Assertion: GDP at MP can be equal to GNP at MP

Reason: NIT = 0

31. Assertion (A). Compensation given to victims of Kerala natural disaster is a commendable welfare measure taken by the government, but it is not included in the estimation of national income.

Reason (R). Transfer payments do not lead to corresponding flow of goods and services in the economy, hence they are not included in the calculation of national income of the country.

Assertion- Reason Answers		
1. (a)Both (A) and (R) true and (R) is correct explanation of (A).		13 a
2. (a)Both (A) and (R) true and (R) is correct explanation of (A).		14 c
3. (c)(A) is true but (R) is false.		15 A. Both A and R are true but R is the correct explanation of A.
4. (c)(A) is true but (R) is false.		16 D. A is false but R is true.
5. (b)Both (A) and (R) true but (R) is not correct explanation of (A).		17 B. Both A and R are true but R is not correct explanation of A.
6 b) Both (A) and (R) true but (R) is not correct explanation of (A).		18 C. A is true but R is false.
7 (A) Both Assertion and reason are true and reason is correct explanation of assertion		19 A. Both A and R are true but R is the correct explanation of A.
8 (A) Both Assertion and reason are true and reason is correct		20 (D)
9 (A) Both Assertion and reason are true and reason is correct ex[;antion of assertion		21 (C)
10. a)		22 (B)
11 b		23 (B)
12) a		24 (C)
		25.(a)

STATEMENT BASED QUESTIONS

In the following questions, there are two statements given. Choose the correct answer out of the following choices.

- (a) Statement 1 is true and Statement 2 is false
- (b) Statement 1 is false and Statement 2 is true
- (c) Both statements 1 and 2 are true.
- (d) Both statements 1 and 2 are false

1. Statement 1: Market price is the difference between factor cost and net subsidies.

Statement 2: Depreciation is added to net investment to convert into gross investment

2. Statement 1: -Flow of goods between households and firms sector known as real flow

Statement 2: Leakage of water for the last two hours known as stock

3. Statement 1: -An American working in International Labour Organisation located in India is a normal resident of India

Statement 2: -Increase in National Income does not always imply increase in domestic income as well.

4. Statement 1: -GDP at MP is the difference between total of gross domestic product at market price and net indirect tax

Statement 2: - GDP at MP is the sum of net domestic product at market price and depreciation.

5. Statement 1: -National Income includes Net factor Income from Abroad

Statement 2: - Domestic Income excludes Net exports

6. Statement 1: -Real GDP increases only when there is increase in the quantum of output in the country.

Statement 2: - Real GDP is estimated by using current year prices.

7. Statement 1: -Income earned by foreigners working in branch of a foreign bank in India is a part of the domestic factor income of India

Statement 2: -Factor income from abroad is a part of domestic factor income of India

8. Statement 1: Gross Domestic capital formation is always greater than Gross Domestic Fixed Capital Formation

Statement 2: Domestic Income will be greater than National Income, when Net Factor Income Paid to Abroad is negative

ANS: 1.c, 2.b, 3.b,4.b,5. a, 6. a, 7. a, 8 b

TRUE AND FALSE QUESTIONS

1. National income is sum of all the transfer income generated in an economy. **Ans: False**
2. NDFfc is equal to NDPmp less Net Indirect Tax. **Ans: True**
3. Double counting can be avoided by summing up total output of firms. **Ans: False**
4. NNPmp is equal to NNPfc when Net Indirect Tax are Zero **Ans: True**
5. Expenditure on electricity by factory is an intermediate cost for the factory. **Ans: True**
6. Bus fare paid by passengers is a final consumption expenditure. **Ans: True**
7. NDPmp is the sum up of operating surplus, compensation of employees, mixed income and Net Indirect Tax.
Ans: True
8. GDPmp is inclusive of indirect taxes but exclusive of subsidies. **Ans: True**
9. Salary of an Indian working in Russian embassy in India is included in National Income of India as Factor income from abroad.
Ans: True
10. Income tax is included for calculating national income by income method. **Ans: False**
11. Old age pension is factor income. **Ans: True**
12. National income can be less than domestic income if $FIFA > FITA$. **Ans: False**
13. If $NDPfc = 80$, $NIT = 10$, Net factor income from abroad (-10), NNPmp is equal to Rs.70,
Ans: False
14. National Income is a flow concept as it measured for an accounting year and not at a point of time.
Ans: True
15. $NVAfc =$ factor payments. **Ans: True**
16. Brokerage on the sale and purchase of shares and bonds is to be included in national income.
Ans: True
17. If Nominal GNP is Rs.1200 and Real GNP is 400, then GNP deflator will be Rs.200.
Ans: False.
18. In a soap factory 5000 cakes @ 10 per unit of soaps remain unsold at the end of financial year, if stock was zero at the beginning of the year. In this situation inventory investment will be Rs.50000.
Ans: True
18. When a farmer keeps a part of crop grown on his farm for consumption by his family, it will be counted as final consumption expenditure. **Ans: True**
19. Increase in the prices of stock lying with a trader must be added to calculate National Income by Value added method. **Ans: False**
20. When Nominal GDP is Rs 840/crore and Price Index is 120, then the Real GDP will be ____ (Rs. 700 crore/ Rs 800 crore)
21. $Nominal\ GDP = Real\ GDP \times (Price\ Index/100)$ (True/ False)
22. Environmental pollution due to an industry is _____ externality (Positive / Negative)

Picture Based Questions

1. Find out ‘?’

Sum of Property Income
(Rent & Interest)

+

Sum of Entrepreneurial
Income (profit)

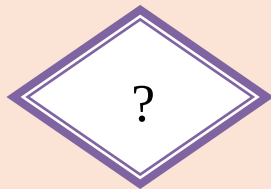
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2.

Pvt Final
Consumption
Expenditure

+

Govt Final
Consumption

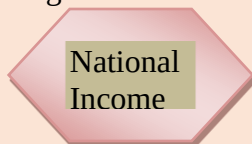
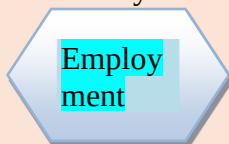
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+

Net Exports

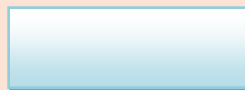
3. Study of the following items is known as



4. Fill the gap with suitable word

GNP at MP

(MINUS



is equal to

GDP at MP

5. Fill the gap with suitable word

[Sales]

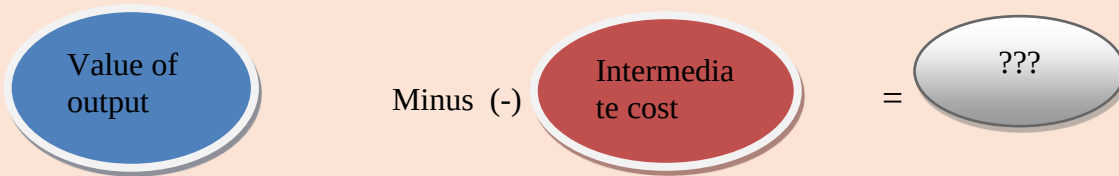
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[Value of Output]

6. Find out '???'



Q 7

Fill up with suitable values by using income & Expenditure methods

COMPLETE THE FOLLOWING TABLE
(INCOME METHOD)

ITEMS	2022	2023	2024
CE	100	50	?
OS	?	100	500
MISE	200	250	100
NDF FC	500	?	800
NIT	50	100	?
NFIA	?	(-)50	?
NNPFC	400	?	1000
NDPMP	?	500	880

Ans: INCOME METHOD

2022: - 300,100,550

2023: - 400,350

2024: -200,80,200

Expenditure Method: -

Part-I: - 400,100,1400

Part-II: - 1400,3120

Part-III: - 1000,800

COMPLETE THE FOLLOWING TABLE
(EXPENDITURE METHOD)

ITEMS	PART-I	PART-II	PART-III
PVT Final Consumption Expenditure	2000	?	1000
?	700	800	3000
Gross domestic capital formation	?	700	5000
Net Exports	(-) 100	220	?
GDPMP	3000	?	10000
CFC	50	20	?
NIT	?	100	200
NDPFC	2850	3000	9000

ANS: 1. Operating Surplus 2. Gross domestic capital formation 3. Macroeconomics 4 net factor income From Abroad

5. Change in stock 6. Value added

Match the following Column I and Column II, and choose the correct alternative			
Column I		Column II	
A	GNP FC-Depreciation	i	GDP at factor cost
B	GNP FC-NFIA	ii	GNP at factor cost
C	GDP FC-Depreciation	iii	NNP at factor cost
D	GNP MP- Net indirect Tax	iv	NDP at factor cost

(a) A-(iii),B-(iv), C-(ii),D-(i)

(b) A-(iii),B-(i), C-(iv),D-(ii)

(c) A-(iv),B-(iii), C-(i),D-(ii)

(d) A-(iv),B-(iii), C-(ii),D-(i)

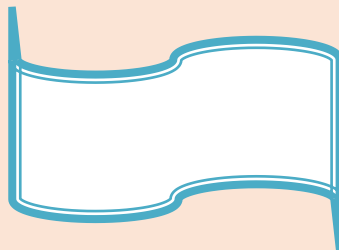
Year	Output (Units)	Market Price per unit in Rs.
2022	1000	10
2023	1100	15

(a) Real GDP in 2022 = $1000 \times 10 = \text{Rs.}10000$ (c) Nominal GDP in 2022 = $1000 \times 10 = \text{Rs.}10000$ (b) Nominal GDP in 2023 = $1100 \times 15 = \text{Rs.}16500$ (d) Real GDP in 2023 =

NDP at FC

Compensation of Employee

+



+

Mixed Income of self employed

Find out the "???"

NET INVESTMENT

+

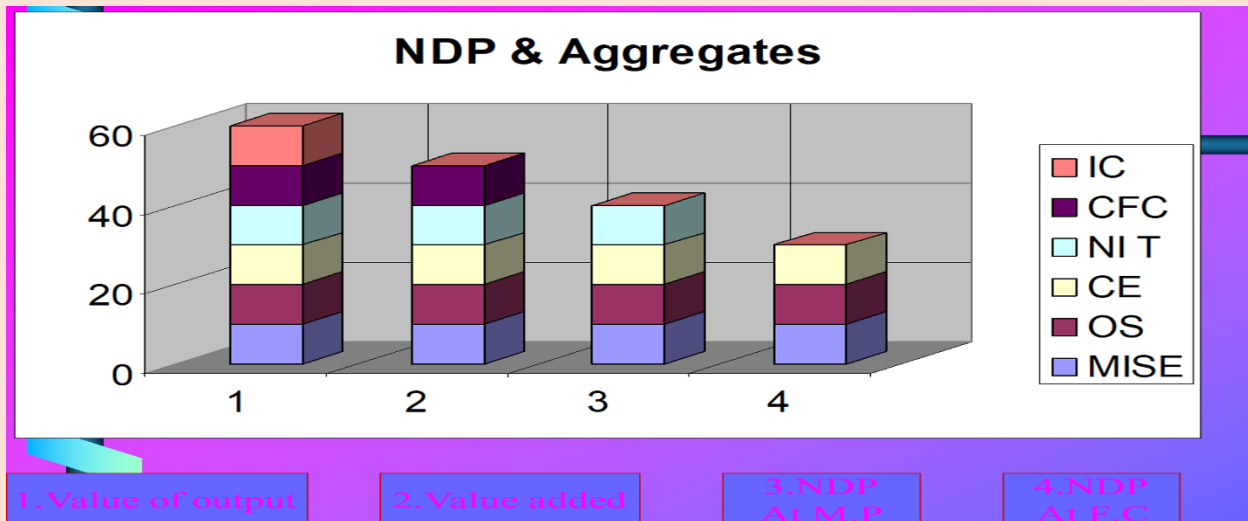
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GROSS INVESTMENT

Write formulae by using the Bar diagram below.

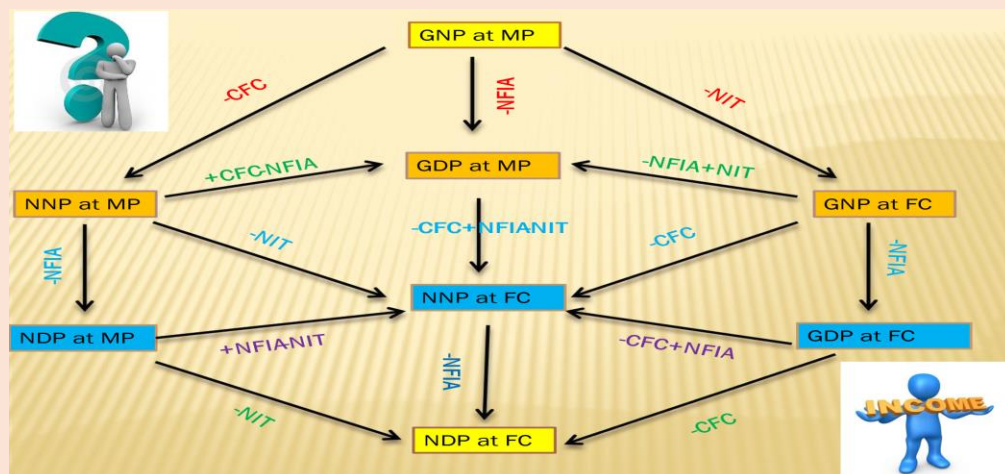
- a) Value of output b) Value Added c) NDP at MP d) NDP at FC



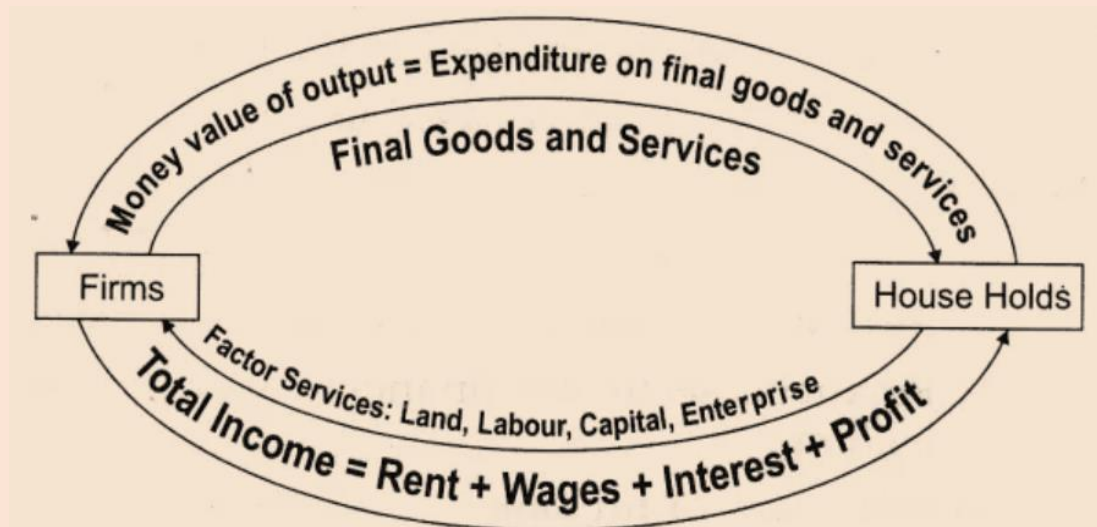
MATCH THE FOLLOWING:

(1) Sum total of all factor payments	(I) Product method
(2) Aggregate value of final goods and services produced by all the firms.	(II) Income method
(3) Aggregate value of spending that the firms receive for the final goods and services which they produce.	(III) Expenditure method

By using the below flow chart derive the NDP at FC and its aggregates



How is outer circle and inner circle known as (Money flow/ Real flow)



CASE STUDY BASED

Read the passage given below and answer the following questions:

1. On 21st June, 2015, the first World Yoga Day was celebrated. In India, it was significantly observed in Delhi, with more than 3500 people, including dignitaries from 84 nations and the Prime Minister Narendra Modi. It was organized by the Ministry of AYUSH. It widely publicised through campaigns on various media to spread awareness about the benefits of Yoga among the masses. T-shirts with the yoga day logo, yoga mats and other related items were distributed to the enthusiasts. Trained yoga experts were appointed to help beginners who participated in the event.

(a) Government's expenditure to popularise yoga among the masses _____ welfare. (b) Government's expenditure to popularise yoga among the masses has no effect on GDP.

(True/ False)

(c) The term 'welfare' refers to :

- (i) Sense of pride in the nation (ii) Increase in purchase of services
- (iii) Sense of well-being among the people (iv) Strict control by the government
- (d) GDP at constant prices is also called _____ (per capita GDP/real GDP).

2.The Economic Survey, 2018-19 describes the vicious cycle of growth where increase in the rate of fixed investment accelerates the growth of GDP that in turn induces a higher growth in consumption. Higher growth of consumption improves the investment outlook, which results in still higher growth of fixed investment that further accelerates the growth of GDP, including a still higher growth of consumption. This cycle of higher fixed investment, higher GDP and higher consumption growth generates economic development in the country.

(a) High_____is a sign of expansion of production capacity in the economy. (i) Gross fixed investment (ii) Inventory investment (iii) Gross investment (iv) Net fixed investment

(b)_____(Gross investment/ Net investment) includes investment for the maintenance of fixed assets.

(c) Inventory investment includes: (i) stock of finished goods (ii) stock of semi-finished goods (iii) stock of raw materials (iv) all of these

(d)Depreciation is a component of Net investment. (True/ False)

ANSWER KEY

Q.1 (a) (b) (c) (d) Increase False (iii) Sense of well-being among the people Real GDP.

Q2 (a) (b) (c) (d) (iv) Net fixed investment Net investment (iv) all of these False

3 Read the passage given below and answer the following questions:

The Indian economy saw its worst contraction in decades, with GDP shrinking by a record 23.9% in the Apr to June quarter in comparison to the same period last year. The contraction reflects the severe impact of the covid-19 lockdown. The economy is in a vicious cycle of low demand and low investment as demand is contracting so heavily, while the government's capacity to neutralize this contraction has been reduced substantially by way of tax revenue contraction. Agriculture was the only sector which recorded modest growth of 3.4%. in year on year term and all other sectors saw contraction.

1 The reason why GDP of India has been decreased is-

- (A) Hyper inflation (B) Reduction in aggregate demand
(C) Low level of fixed investment (D) None of these

2 Only Agriculture sector recorded the modest growth because-

- (A) Government invested heavily in agriculture (B) Government reduced taxes on agriculture products
(C) Demand did not get affected for agriculture produce (D) All the above

3 Impact of covid-19 in India's GDP

(A) GDP increased (B) GDP decreased (C) GDP remain unchanged (D) none of the above

ANS 1 (B) Reduction in aggregate demand 2 (C) Demand did not get affected for agriculture produce much

3 (B) GDP decreased

4. Read the following report and answer the questions based on it.

New Delhi: asserting that the “worst is behind us” veteran banker Deepak Parekh on Thursday said that India's GDP growth will be in positive territory in the fourth quarter as demand has started picking up in all sectors.

Citing an example, he said during the virtual conference organised by Canada – India based Council. he said toll collection are back to 88% of pre Covid level, e way bills are increasing and electricity consumption has stabilized. India is domestic based economy and demand is set to rise in coming future.

a) Do you think higher level of Real GDP always lead to higher availability of goods per person in the domestic economy?

b) Can we say GDP is true indicator of welfare?

c) Real GDP is the index of ____.

ANS: a) NO b) NO c) Economic growth

5. Read the following report and answer the questions based on it.

The Indian economy saw its worst contraction in decade, with GDP shrinking by a record 23% in April to June Quarter in comparison to the same period last year. The contraction reflects the severe impact of the Covid 19 lockdown, which halted most economic activities as well as the slowdown trend of the economy even pre

Covid 19. The Indian economy is in a deeply vicious cycle, where demand is contracting so heavily, while the capacity to neutralise this contraction has also contracted equally because of the tax revenue contraction. Agriculture was the only sector which recorded modest growth of 3.4% in year on year term and all other sectors saw contraction. Answer the following based on the text:

a) The impact of Covid 19 on India's GDP _____. (increasing / decreasing)

b) _____ is crucial for revenue collection. (Nominal GDP/National income)

c) Who are considered as owner of factors of production? (Firms/ Households)

ANS a) Increasing b) Nominal GDP c) Household

6. Read the passage given below and answer the following questions 1 and 2

GDP is a measure of economic prosperity of a country compiled as output or income. However, GDP is regularly criticized for not presenting a fair view of welfare. If GDP is a poor measure of welfare, focusing one sided on increasing GDP may lead to misguided political decision. For example, Nobel Laureate Joseph Stieglitz has argued that the objective of the highest possible GDP growth will result reduced welfare.

1 GDP is not considered as a better measure of development. Which of the following reasons could be accounted for the same?

- (a) Externalities (b) Non-marketable services
(c) Production of harmful goods (d) All of these

2 A course of action by one economic agent which has an adverse impact on the other economic agent without cost sharing, is known as..... (Positive/Negative) externality.

- (A) Positive (B) Negative

ANS 1 (D) All of these 2 (B) Negative

UNIT 2: MONEY AND BANKING

Barter system of exchange: It is a system in which goods are exchanged for goods. Such exchange exists in the C-C Economy (commodity to commodity exchange economy). For example, wheat may be exchanged for cloth; house for horses, etc., or a teacher may be paid wheat or rice as a payment for his/her services.

Difficulties involved in the Barter Exchange:

Lack of a common measure of value.
Lack of double coincidence of wants
Lacks of standard of deferred payments.
Lack of store of value.
Lack of divisibility.

Money: Money may be defined as anything which is generally acceptable as a medium of exchange and at the same time acts as a measure, store of value and standard of deferred payment.

Primary Function

i) Medium of exchange:

It means that money can be used to make payments for all the transactions of goods and services. A buyer can buy goods through money and a seller can sell goods for money.

ii) Measure of value:

Money serves as a measure of value. The value of all goods and services is expressed in terms of money.

Secondary Function

i) Standard of deferred payments:

It means that money acts as a 'standard' for making future payments. It has made deferred payments much easier than before. This function has facilitated borrowing and lending. It has also led to the creation of financial institutions.

ii) Store of value:

A store of value implies a store of wealth. Money can be easily stored for future use.

iii) Transfer of value:

Money also serves for transfer of value. It facilitates buying and selling of goods not only in the domestic country but also in other parts of the world.

Supply of Money: -Supply of Money is a stock concept. It refers to stock of money available with the public/people at a point of time.

Components of Money Supply: -Currency with Public + Demand Deposits with Commercial Banks

Measures of Money Supply

$$M1 = C + DD + OD \text{ (Most liquid asset)}$$

Demand deposits.: Demand deposits are those deposits which can be withdrawn by the depositor at any time by means of cheque. No interest is paid on such deposits.

Central Banks: The central bank is the apex institution of monetary and financial system of a country. It makes monetary policy of the country in public interest. It manages, supervises and facilitates the banking system of the country.

Functions of Central Banks

- ❖ Bank of Issue
- ❖ Banker to the Government
- ❖ Banker's Bank and Supervisor.
- ❖ Controller of credit.
- ❖ Lender of last resort
- ❖ Custodian of foreign exchange reserves

Bank of Issue

The central bank has the sole monopoly to issue currency notes. Commercial banks cannot issue currency notes. Currency notes issued by the central bank are the legal tender money.

Banker's Bank and Supervisor

- (i) Custodian of the cash reserves of the commercial banks: Every commercial bank has to keep a certain percent of its cash reserves with the central bank by law.
- (ii) Lender of the Last Resort.

As banker to the banks, the central bank acts as the lender of the last resort, in case the commercial banks fail to meet their financial requirements from other sources, they can, as a last resort, approach to the central bank for loans and advances.

Banker to the Government

(i) As Banker: As a banker to the government, the central bank performs same functions as performed by the commercial banks to their customers.

(ii) As Fiscal Agent: As a fiscal agent, it performs the following functions:

- It manages the public debt.
- It collects taxes and other payments on behalf of the government.
- (iii) As Adviser: The central bank also acts as the financial adviser to the government.

Control on Credit Creation: -through the monetary policy RBI perform this function. For this RBI uses quantitative instruments and qualitative instruments.

QUANTITATIVE INSTRUMENTS

- **Bank Rate Policy** - It refers to the rate at which the central bank lends money to commercial banks as a lender of the last resort.
- **Repo Rate Policy** – It is the rate at which the central bank of the country (RBI) lends money to the commercial banks to meet their short-term needs.
- **Reverse Repo Rate** – It is the rate at which RBI borrows money from the commercial banks.
- **Open Market Operations** - It refers to the buying and selling of securities by the Central Bank from/ to the public and commercial banks.
- **Legal Reserve Ratio** - R.B.I. can influence the credit creation power of commercial banks by making changes in CRR and SLR.
- **Cash Reserve Ratio (CRR)** - It refers to the minimum percentage of net demand and time liabilities to be kept by commercial banks with central bank.
- **Statutory Liquidity Ratio (SLR)** - It refers to minimum percentage of net demand and time liabilities which commercial banks required to maintain with themselves in the form of specified liquid assets including cash, gold and govt. securities.

• QUALITATIVE INSTRUMENTS:

i) **Margin Requirements**: It is the difference between the amount of loan and market value of the security offered by the borrower against the loan.

ii) Rationing credit: Sometimes the central bank will instruct the commercial bank to give some percent of loan to some sectors. This is called fixing the quota. During deflation rationing will be removed.

(iii) Warning and direct action: The central bank may warn or take direct action against the commercial banks, which do not follow its guide lines. A few months ago, RBI slapped Rs 5 lakhs on IDBI.

(iv) Moral suasion: Sometimes central bank may persuade the commercial banks to follow its guidelines.

• **MONEY CREATION OR CREDIT CREATION BY COMMERCIAL BANKS**

- Commercial banks create credit by accepting deposits and advancing loans. This is based on two assumptions:
- All depositors do not withdraw the money at the same time. There is constant flow of new deposits into the banks.
- The capacity of banks to create money or credit depends on **Amount of primary deposits and Legal reserve ratio (LRR)**.
- Let us understand the process of credit creation with the following example.
- Suppose there is an initial deposit of Rs. 1000 and L.R.R. is 20% i.e., the banks have to keep Rs. 200 and lend Rs. 800/-. All the transactions are routed through banks.
- The deposit creation comes to end when the total cash reserves become equal to the initial deposit.
- **Credit creation = Initial deposit $\times$ $1/LRR$.**
Credit creation = $1000 \times 1/20\%$
- **$1000 \times 100/20 = \text{Rs } 5000$**
- In this way, commercial banks create credit many more times than their cash reserves and contributes to increase money supply in the economy.
- **Numerical example**
- If Initial deposit is Rs. 1000 and LRR = 20%, then

Initials Deposit	Deposit	LRR 20%	Loans
Round -1	1,000	200	800
Round -2	800	160	640
Round -3	640	128	512
	--	--	--
	--	--	--
Total	5,000	1,000	4,000

1.	Which of the following statements is correct? (a) Supply of money refers to stock of money held by public at a point of time (b) Supply of money is a flow variable (c) Supply of money includes cash reserve of banks (d) Supply of money refers to bank money
2.	_____ is the main function of central Bank a. Notes issue b. Credit creation c. Accepting deposits from the public d. None of these
3.	What will be the effect of an increase in the 'Repo Rate on the Money Supply? a) Money supply will increase b) Money supply will decrease c) Money supply will remain the same d) Money supply will initially increase and then it will decrease
4.	_____ is the rate of interest charged by the Central Bank on loans given to commercial banks a. Bank rate b. CRR c. Statutory liquidity Ratio d. Reserve Repo Rate
5.	Ms. Sakshi, an economics teacher, was explaining the concept of 'minimum percentage of the total deposits to be kept by any commercial bank with the Central Bank of the country, as per norms and statute prevailing in the country'. From the following, choose the correct alternative which specifies towards the concept explained by her? a) Cash Reserve Ratio b) Repo Rate c) Bank Rate d) Statutory Liquidity Ratio
6.	Which of the following is not a quantitative Method of Credit Control? a) Open Market Operation b) Margin Requirements c) Variable Reserve Ratio d) Bank Rate Policy
7.	_____ refers to that portion of total deposits of a commercial bank which it has to keep with itself in the form of liquid assets a. Statutory Liquidity Ratio (SLR) b. Cash Reserve Ratio (CRR) c. Bank Rate d. Reserve Repo Rate
8.	If the total deposits created by commercial banks is ₹. 10,000 crores and legal reserve requirements is 40% then amount of initial deposits will be (a) ₹ 2000 (b) ₹ 2500 (c) ₹ 4000 (d) ₹ 10,000

9.	What will be the value of money multiplier when initial deposits are ₹ 500 crores and LRR is 10%? (a) 0.1 (b) 0.2 (c) 10 (d) 20
10.	The amount of initial deposits is 3000 cr and LRR is 25%. Calculate the amount of total deposits created by commercial banks (a) 10000 crore (b) 11000 crore (c) 12000 crore (d) 13000 crore
11.	Deposit creation by bank comes to an end when: (a) Fresh deposit with banks becomes zero (b) LRR become zero (c) Money multiplier become zero (d) Total reserve equal to initial deposit
12.	What would be the total money creation in the economy, If initial fresh deposits with banks = 50,000 and LRR = 20%. (a) `2,50,000 (b) `5,00,000 (c) `10,00,000 (d) `12,00,000
13.	Which one of the following is used for credit creation? (a) $K = 1/LRR$ (b) $K = 1/SLR$ (c) $K = 1/\text{Bank Rate}$ (d) $K = 1/\text{Repo Rate}$
14.	The value of credit multiplier will be high when (a) Cash reserve ratio is high (b) Cash reserve ratio is low (c) Cash reserve ratio is zero (d) Cash reserve ratio is infinity
15.	In a hypothetical economy, Mr. Neeraj has deposited ₹100 in the bank. If it is assumed that there is no other currency circulation in the economy, then the total money supply in the economy will be _____ a) zero b) ₹ 100 c) not defined d) ₹ 120

16.	Two friends Akash and Amit were discussing about the features of central bank. "This feature saves the commercial banks from possible breakdown" The above-mentioned statement was given by Akash, identify the feature was hetaking about... (a) Banker's bank (b) Lender of the last resort (c) Controller of credit (d) Financial advisor
17.	Read the following statements carefully and choose the correct alternatives givenbelow: Statement 1 – Central bank lends money to borrowers at a very low interest. Statement 2 – Ministry of finance circulates all mint and one rupee note in India. Alternatives: a) Both the statements are true. b) Both the statements are false. c) Statement 1 is true and Statement 2 is false d) Statement 2 is true and Statement 1 is false

18.	Read the following statements carefully and choose the correct alternatives given below: Statement 1 – The value of money multiplier is determined by the reserve ratio prevailing in the monetary system. Statement 2 – The process of credit creation directly relates to the value of reserve ratio. Alternatives: a) Both the statements are true. b) Both the statements are false. c) Statement 1 is true and Statement 2 is false d) Statement 2 is true and Statement 1 is false
19.	Choose the correct statement from given below (a) Commercial banks create credit out of primary deposits. (b) The money multiplier is directly related to the legal reserve ratio. (c) The central bank of the country is not authorized to maintain foreign exchange reserves. (d) All of the above
20.	Assertion(A): Currency Held by Public is a monetary liabilities of central bank Reason(R): Central bank control credit, whereas commercial bank create credit with currency held by Public. (a) Both Assertion(A) and Reason(R) are true and Reason(R) is the correct explanation of the Assertion(A) (b) Both Assertion(A) and Reason(R) are true and Reason(R) is not the correct explanation of the Assertion(A) (c) Assertion(A) is true but Reason(R) is false (d) Assertion(A) is false but Reason(R) is true

21.	Assertion (A): Central Bank as a banker to the government, works as a custodian of cash reserves.
	Reason(R): The Central Bank acts as a clearinghouse for the transfer and settlement of mutual claims of commercial banks. (a) Both Assertion(A) and Reason(R) are true and Reason(R) is the correct explanation of the Assertion(A) (b) Both Assertion(A) and Reason(R) are true and Reason(R) is not the correct explanation of the Assertion(A) (c) Assertion(A) is true but Reason(R) is false (d) Assertion(A) is false but Reason(R) is true
22.	Assertion(A): Central bank as a banker to government, work as a financial advisor Reason(R): Government borrow internally from banks and general public. (a) Both Assertion(A) and Reason(R) are true and Reason(R) is the correct explanation of the Assertion(A) (b) Both Assertion(A) and Reason(R) are true and Reason(R) is not the correct explanation of the Assertion(A) (c) Assertion(A) is true but Reason(R) is false (d) Assertion(A) is false but Reason(R) is true
23.	Assertion(A): Demand deposits are also called bank money. Reason(R): Demand deposits are created by commercial banks. (a) Both Assertion(A) and Reason(R) are true and Reason(R) is the correct explanation of the Assertion(A) (b) Both Assertion(A) and Reason(R) are true and Reason(R) is not the correct explanation of the Assertion(A) (c) Assertion(A) is true but Reason(R) is false (d) Assertion(A) is false but Reason(R) is true
24.	Assertion(A): LRR represents the minimum reserve ratio essential to be maintained by banks. Reason(R): Banks create deposits in the process of making loans to their customers. (a) Both Assertion(A) and Reason(R) are true and Reason(R) is the correct explanation of the Assertion(A) (b) Both Assertion(A) and Reason(R) are true and Reason(R) is not the correct explanation of the Assertion(A) (c) Assertion(A) is true but Reason(R) is false (d) Assertion(A) is false but Reason(R) is true
25.	Assertion(A): The Central Bank is also known as the bank of issue. Reason(R): The Central Bank enjoys the sole monopoly of issuing currency to ensure control over volume of currency and money supply. (a) Both Assertion(A) and Reason(R) are true and Reason(R) is the correct explanation of the Assertion(A)

	(b) Both Assertion(A) and Reason(R) are true and Reason(R) is not the correct explanation of the Assertion(A) (c) Assertion(A) is true but Reason(R) is false (d) Assertion(A) is false but Reason(R) is true
26.	Assertion(A): Demand deposits are created by commercial banks. Reason(R): Demand deposits form a significant part of the total money supply in the economy. (a) Both Assertion(A) and Reason(R) are true and Reason(R) is the correct explanation of the Assertion(A) (b) Both Assertion(A) and Reason(R) are true and Reason(R) is not the correct explanation of the Assertion(A) (c) Assertion(A) is true but Reason(R) is false (d) Assertion(A) is false but Reason(R) is true
27.	Assertion(A): Only net demand deposits held by commercial banks are taken as part of money supply. Reason(R): Only deposits of the public held by the banks are included in money supply (a) Both Assertion(A) and Reason(R) are true and Reason(R) is the correct explanation of the Assertion(A) (b) Both Assertion(A) and Reason(R) are true and Reason(R) is not the correct explanation of the Assertion(A) (c) Assertion(A) is true but Reason(R) is false (d) Assertion(A) is false but Reason(R) is true
28.	Assertion(A): Credit creation is inversely related to the Legal Reserve Ratio. Reason(R): LRR is fixed by the market forces of demand and supply. (a) Both Assertion(A) and Reason(R) are true and Reason(R) is the correct explanation of the Assertion(A) (b) Both Assertion(A) and Reason(R) are true and Reason(R) is not the correct explanation of the Assertion(A) (c) Assertion(A) is true but Reason(R) is false (d) Assertion(A) is false but Reason(R) is true
29.	Assertion(A): The monetary policy is the policy formulated by central bank of a country Reason(R): The policy measures involve measures taken by the central bank to regulate the supply of money, availability and cost of credit in the economy. (a) Both Assertion(A) and Reason(R) are true and Reason(R) is the correct explanation of the Assertion(A) (b) Both Assertion(A) and Reason(R) are true and Reason(R) is not the correct explanation of the Assertion(A) (c) Assertion(A) is true but Reason(R) is false (d) Assertion(A) is false but Reason(R) is true

ANSWERS

ANSWERS	Q.NO	ANSWERS
A	20	B
A	21	C
B	22	A
A	23	B
A	24	A
B	25	B
A	26	A
C	27	A
C	28	D
C	29	B
D		
A		
A		
B		
B		
B		
D		
C		
A		

SHORT ANSWER QUESTION (3/4 MARKS)

1. Money acts as a yardstick of standard measure of value to which all other things can be compared. Discuss it.

Money serves as a measure of value in terms of unit of account. Measurement of value was the main difficulty of the barter system. Introduction of money has removed this difficulty. It acts as a yardstick of standard measure of value to which all other things can be compared.” Money measures the value of everything or the prices of all goods and services can be expressed in terms of money.

2. Banks required to keep only a fraction of deposits as cash reserves. Why?

Banks are required to keep only a fraction of deposits as cash reserves because of the following two reasons:

- (a) First, the banking experience has revealed that not all depositors approach the banks for withdrawal of money at the same time and also that normally they withdraw a fraction of deposits.
- (b) Secondly, there is a constant flow of new deposits into the banks. Therefore, to meet the daily demand for withdrawal of cash, it is sufficient for banks to keep only a fraction of deposits as a cash reserve.

(c) First, the banking experience has revealed that not all depositors approach the banks for withdrawal of money at the same time and also that normally they withdraw a fraction of deposits.

(d) Secondly, there is a constant flow of new deposits into the banks. Therefore, to meet the daily demand for withdrawal of cash, it is sufficient for banks to keep only a fraction of deposits as a cash reserve.

3.What do you mean by Money Multiplier/Credit Multiplier?

It refers to the fraction by which commercial banks would be able to multiply money from their initial level of deposits.

$$\text{Money Multiplier} = 1/\text{LRR}$$

4.What do you mean by Legal reserve ratio (LRR)? Explain the components of Legal Reserve Ratio.

The minimum percentage of a bank's total demand and time deposits, that is required to be maintained in the form of cash or specified liquid assets by the commercial banks with the Central Bank is termed as Legal Reserve Ratio.

The components of Legal Reserve Ratio are as follows

- (i) Cash Reserve Ratio: The percentage of total deposits, which a commercial bank needs to keep as reserve with the Central Bank.
- (ii) Statutory Liquidity Ratio: Every commercial bank is required to maintain a fixed percentage of its assets in the form of cash or other liquid assets.

5.‘During the last few years’ initiatives such as Jan Dhan Yojna, Aadhar-enabled payment systems, e-Wallets, National Financial Switch (NFS), and others have strengthened the government's resolve to go cashless.’ Elaborate on how such initiatives may have affected the Indian economy.

Ans. These initiatives affect the economy by:

- increasing the total number of bank deposits, leading to more deposition of money
- the lending capacity of banks increases due to more accounts
- easing of payments systems
- availability of loans, investments increase
- all these lead to more pumping of money into the economy leading to the overall growth in the National Income.

6. Read the following text carefully, and discuss briefly the relevant function of the Central Bank, indicated:

Recently, the Reserve Bank of India (RBI) conducted a statutory inspection for supervisory evaluation against a Commercial Bank. The commercial bank was imposed with stringent penalties, owing to deficiencies in regulatory compliance. As per the Central Bank, the inspection revealed non-compliances vis-à-vis different directions issued by RBI, on the following fronts:

- i. ATM Card fraud**
- ii. Ensuring integrity and quality of data**
- iii. Loans to small borrowers**

Answer: The given text indicates the ‘supervisory function’ of the Central Bank, under which the Reserve Bank of India (RBI) regulates and supervises the routine functioning of commercial banks.

Under this function, the RBI may exercise periodic inspections/audits of commercial banks, filing of reports by commercial banks, and other statutory compliances. Central bank may take necessary corrective and punitive actions against the banks owing to deficiencies in regulatory compliances.

7. With an objective to reduce inflation, Reserve Bank of India may promote the commercial banks to park their surplus funds with it.” Discuss the rationale behind the step taken by the Reserve Bank of India.

Answer: The reverse repo rate is the rate at which commercial banks may park their surplus funds with the Central Bank.

In order to decrease inflation in an economy, the Reserve Bank of India (RBI) may increase the reverse repo rate. With the increase in the reverse repo rate, it becomes lucrative for commercial banks to park surplus funds with the central bank. Consequently, this may lead to a reduction in their lending capacity. Thereby, a fall in Aggregate Demand curbs the level of inflation.

CASE STUDY/SOURCE BASED QUESTIONS

1. Read the following case study paragraph carefully and answer the questions on the basis of the same.

The central bank of India i.e. Reserve Bank of India, is the apex institution that control the entire financial market. It's one of the major functions is to maintain the reserve of foreign exchange. Also, it intervenes in the foreign exchange market to stabilize the excessive fluctuations in the foreign exchange rate.

In other words, it is the central bank's job to control a country's economy through monetary policy; if the economy is moving slowly or going backward, there are steps that central bank can take to boost the economy. These steps, whether they are asset purchases or printing more money, all involve injecting more cash into the economy. The simple supply and demand economic projection occur and currency will devalue.

When the opposite occurs, and the economy is growing, the central bank will use various methods to keep that growth steady and in-line with other economic factors such as wages and prices. Whatever the central bank does or in fact doesn't do, will affect the currency of that country. Sometimes, it is within the central bank's interest to purposefully effect the value of a currency. For example, if the economy is heavily reliant on exports and their currency value becomes too high, importers of that country's commodities will seek cheaper supply; hence directly effecting the economy.

1. Which of the following tools are used by the central bank to control the flow of money in domestic economy?

- | | |
|--------------------------------|---------------------------------|
| (a) Fiscal tools | (b) Quantitative monetary tools |
| (c) Qualitative monetary tools | (d) Both (b) and (c) |

2. Dear money policy of central bank, which is used to keep the growth steady and in-line with other economic factors, refers to

- a) Tighten the money supply in the economy
- b) Ease the money supply in the economy
- c) Allow commercial banks to work under less strict environment
- d) Both (b) and (c)

3. Which of the following tools are used by the central bank to control the flow of money in domestic economy?

- | | |
|--------------------------------|---------------------------------|
| (a) Fiscal tools | (b) Quantitative monetary tools |
| (c) Qualitative monetary tools | (d) Both (b) and (c) |

4. Dear money policy of central bank, which is used to keep the growth steady and in-line with other economic factors, refers to

- e) Tighten the money supply in the economy
- f) Ease the money supply in the economy
- g) Allow commercial banks to work under less strict environment

h) Both (b) and (c)

5. Which of the following steps should be taken by the central bank if there is an excessive rise in the foreign exchange rate?

- (a) Supply foreign exchange from its stock
- (b) Demand more of other foreign exchange
- (c) Not intervene in the market as the exchange rate is determined by the market forces
- (d) Help central government to stabilize the foreign exchange rate.

ANSWERS

1. (d) Both (b) and (c)
2. (a) Tighten the money supply in the economy
3. (a) Supply foreign exchange from its stock

Read the para given below and answer the questions that follow:

The Reserve Bank of India (RBI) on Friday kept interest rates on hold while assuring to maintain support for reflecting the economy by ensuring ample liquidity to manage the government's near-record borrowing.

The six-member Monetary Policy Committee (MPC) voted to continue with the accommodative stance as long as it is necessary to revive growth and mitigate the impact of Covid-19 on the economy while ensuring that inflation remains within the target, Governor Shaktikanta Das said. While the Union Budget 2021 laid down an expansive fiscal strategy over the medium term to strengthen the growth engine in the economy, the RBI affirmed its support to such a plan through appropriate monetary tools.

To absorb higher government borrowings, the Central Bank provided retail investors a direct option to invest in government securities. It also sapped some funds from banks by raising the Cash Reserve Ratio (CRR) and using the money for more targeted market operations.

The MPC, which cut borrowing costs by 115 basis points last year, kept the repurchase or repo rate unchanged at 4 percent. Consequently, the reverse repo rate will also continue to earn 3.35 per cent for banks for their deposits kept with the RBI. Das announced the restoration of CRR - the amount of deposits lenders must set aside as reserves - to 3.5 per cent in March and 4 per cent in May. The cash returning to the central bank can be used by it for open market operations and other liquidity measures.

1. The two essential conditions for a financial institution to become a bank are:
 - (a) accepting deposits and lending
 - (b) printing currency notes
 - (c) both (a) and (b)
 - (d) neither (a) nor (b)
2. Which of the following is not a quantitative method of credit control?
 - (a) open market operation
 - (b) bank rate policy
 - (c) legal reserve requirements
 - (d) margin requirements

3. The central bank does not perform the following functions.
- (a) conducts sale and purchase of securities for foreign governments securities.
 - (b) acts as a lender of the last resort.
 - (c) controls money supply and credit.
 - (d) manages the nation's reserves of international currency.

ANSWERS

1. (a) accepting deposits and lending
2. (d) margin requirements
3. (a) conducts sale and purchase of securities for foreign governments securities.

3. Read the para given below and answer the questions that follow:

Heightened uncertainty in India caused by the Coronavirus pandemic led to a surge in the currency in circulation as people hoarded cash or put money in accessible deposits to safeguard themselves against salary cuts or job losses.

According to RBI data, India's M3 money supply rose 6.7% in the first five months of 2020 compared with the same period in 2019, the highest growth in seven years. Currency in circulation, which measures money with the public and in banks has also surged. Gross capital formation, or total investments toward fixed capital in the country, fell significantly. Savings and current account deposits fell 8% due to higher withdrawals. The growth in currency notes held by the public was much higher than the deposits made in banks.

A rise in money supply usually is seen as a leading indicator of growth in consumption and business investments, but the rise this time was unlikely to bolster either, analysts said. The increase reflected higher cash withdrawals by depositors to meet the needs during the lockdown period, until normalcy returns.

1. _____ (quantitative/qualitative) instruments of monetary policy affect the direction of credit in the economy.

2. Choose the correct pair of statements from the given statements in Column I and II:

S NO	Column I	Column II
1	LRR	A. rate of interest at which Central Bank lends to commercial banks for long term
2	Reverse Repo Rate	B. rate at which the RBI borrows money from commercial banks
3	Bank Rate	C. rate at which Central Bank advances short term loans to commercial banks
4	. Repo Rate	D. minimum reserve maintained by a commercial bank

(a) 1-A

(b) 2-B

(c) 3-C

(d) 4-D

3. Which of the following statements is true?

- (a) Money Multiplier is inversely related to LRR.
- (b) Loans given by Commercial banks are equal to the amount of deposits they receive.
- (c) CRR is decreased to control inflation
- (d) Demand deposits refer to the cash reserves of Commercial Banks.

ANSWERS

1. qualitative

2. 2-B

3. (a) Money Multiplier is inversely related to LRR.



COMIC ON FUNCTIONS OF RBI

BY: G. MADHUNISAA

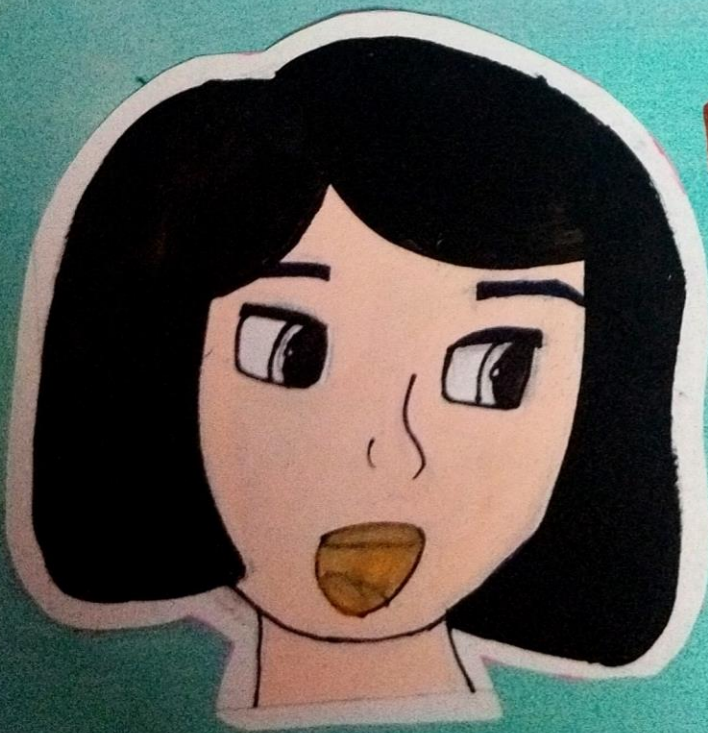
P.M. SHRI KENDRIYA VIDYALAYA MINAMB-
AKKAM, CHENNAI

UNDER THE GUIDANCE OF:
MRS. SHANTHI SEETHARAMAN
P.G.T. ECONOMICS



CHARACTERS

ARJUN
MANAGING DIRECTOR
AT THE COUNTRY'S
MOST POPULAR BANK.



VISHAKA
ARJUN'S
DAUGHTER
STUDYING 5TH
STANDARD



And I said her that
you are working in
the country's most
important & main
bank



Ha Ha Ha... Who
told you that? I
don't work in the
country's main
bank



What? I even saw advertisem-
ents saying that it is no. 1 bank
in India.

Yes my dear! but that doesn't
mean that we are the main
bank of India. The main bank
of India is RBI

What?

What, Let me
explain

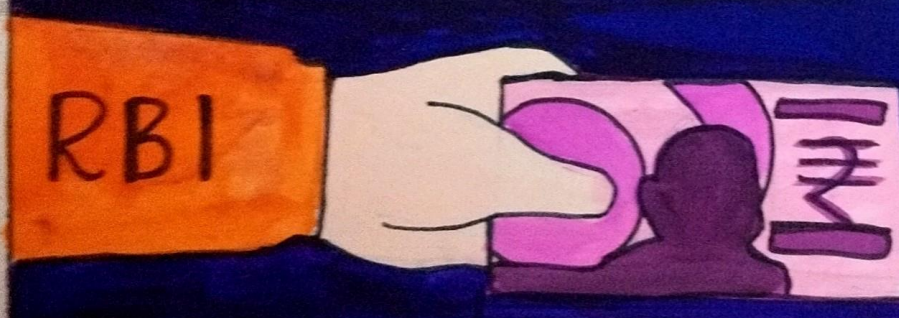
Every country has its own bank
which is controlled by the government
This bank has a set of functions to
do exclusively. In India, it's called
Reserve bank of India. RBI Shortly

भारतीय रिज़र्व बैंक
RESERVE BANK OF INDIA





RBI is a 'bank of issue'. Bank of issue refers to a bank which has the legal right to issue currency. RBI is the sole authority for the issue of currency [except 1 rupee notes & coin which is issued by ministry of finance]. This is done to maintain uniformity.



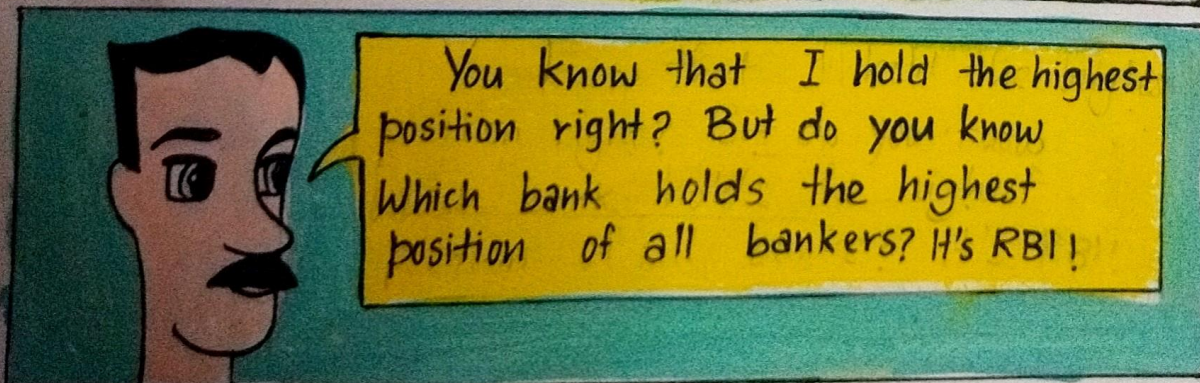
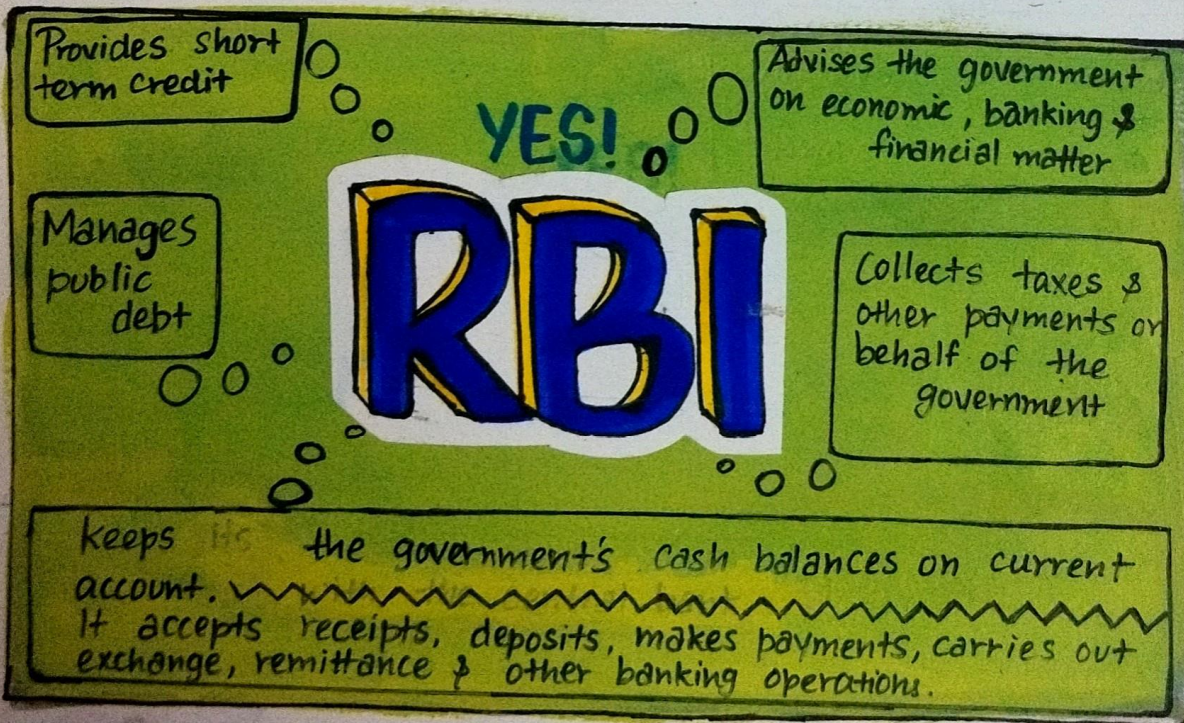
RBI

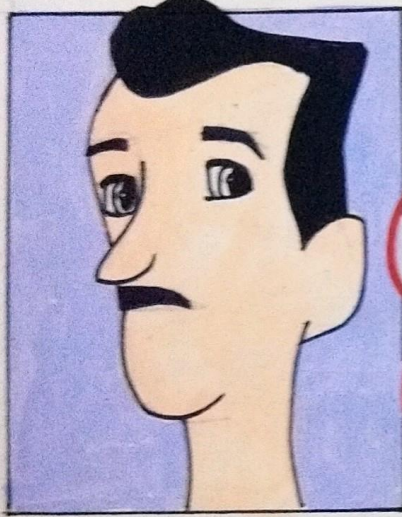
Central government borrows money from RBI to finance its deficit, i.e., when government expenditure exceeds its revenue. This is done by selling security bills to RBI & then RBI issues new currency [deficit financing]



SECURITY
BILLS

INDIAN
GOVERN-
MENT





RBI IS CALLED 'BANKER'S BANK & SUPERVISOR'. IT HOLDS A PART OF THE CASH RESERVES OF BANKS. IT ALSO GIVES FINANCIAL ACCOMMODATION [LOANS] TO COMMERCIAL BANKS AGAINST APPROVED SECURITIES.

IT IS ALSO CALLED 'CONTROLLER OF CREDIT AND MONEY SUPPLY'. MONETARY POLICY OF CENTRAL BANK REFERS TO THE POLICY OF CENTRAL BANK RELATED TO THE CONTROL OF MONEY SUPPLY & THE AVAILABILITY OF CREDIT IN THE SYSTEM. RBI REGULATES THE MONEY SUPPLY IN INDIA THROUGH ITS MONETARY POLICY.



UNIT 3: DETERMINATION OF INCOME & EMPLOYMENT

Introduction:

Determination of income, output & employment is one of the core issues of the Macro Economics. The level of income, output and employment is determined by the Aggregate Demand & Aggregate supply.

The equilibrium level of income output and employment is determined when Aggregate Demand (AD) is equal to Aggregate supply (AS).

At equilibrium

$$\begin{aligned} AD &= AS \\ C+I &= C+S \\ I &= C+S-C \\ \text{Hence } I &= S \end{aligned}$$

1. Concepts of employment

A) Full employment:

Full employment refers to a situation in which no one is unemployed i.e....there is no involuntary unemployment. According to Keynes full employment signifies a level of employment where increase in aggregate demand does not lead to an increase in the level of output and employment. Increase in demand beyond full employment causes prices to go up.

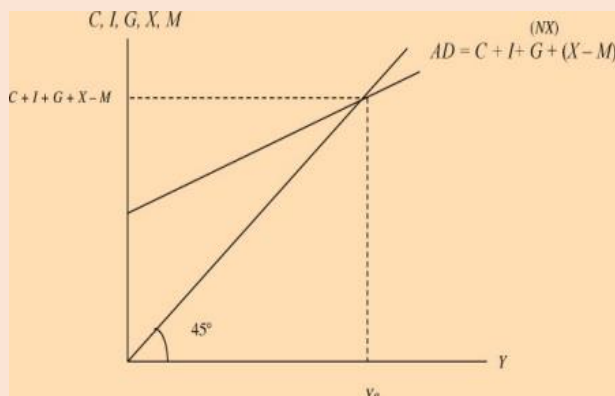
B) Involuntary unemployment is a situation in which a worker is able and willing to work at the existing rate of wages but does not get work .

C) Under employment is a situation where all those who are able to work at existing wage rates, are not getting jobs. It refers to that situation in the economy where $AS = AD$ or $S = I$, but without fuller utilisation of labour force.

2. Aggregate Demand and its components:

a) Meaning of Aggregate demand :

It refers to the sum total of demand made by all the economic units in the economy at a given point of time at full employment level . It can be also defined as the total expenditure incurred by different sectors of an economy .



The level of Aggregate demand in an economy Depends on the levels disposable income(Y) of an economy. AD and levels of income are directly related to each other.

$$AD = f(Y)$$

$$Y = C + I$$

Therefore, the Aggregate demand curve is the positively sloped curve originating from OY Axis. Because when there is no income, even then there can be positive aggregate demand with the help of past savings or autonomous consumption(C)

Hence AD can never be negative or zero.

b) COMPONENTS OF AGGREGATE DEMAND:

Aggregate demand of an economy is the sum of the household consumption demand (C), government demand (G), & investment demand by firms (I) and net export demand (X-M)of the economy at a given point of time.

Hence $AD = C + I + G + (X - M)$ In a two-sector economy $AD = C + I$ As $AD = f(Y)$
Hence $Y = C + I$

Let us discuss the Consumption demand and Investment demand in detail:

3. CONSUMPTION FUNCTION/PROPENSITY TO CONSUME:

Consumption function is the functional relationship between levels of consumption at different levels of income. It explains the portion of income the people are willing / desires to spend on consumption (Propensity to consume) at different levels of disposable income (Y).

Hence $C = f(Y)$ (OR) $C = C + b Y$

C = Consumption level

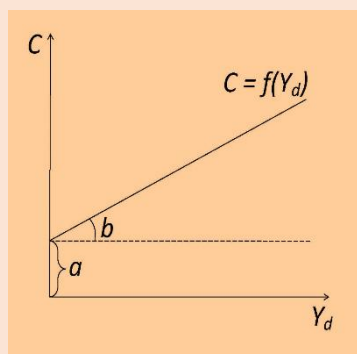
C = Autonomous consumption - (Levels of consumption at zero level of income)

b = Marginal Propensity Consume (MPC)

Y = Levels of income

Hence the consumption curve slopes positively.

Since $C = f(Y)$ when the income rises levels consumption also rises. But at zero level of income also there can be minimum level of consumption with the help of past savings (or) dissaving, which is known as AUTONOMOUS CONSUMPTION (a).



Note : It is assumed that Linear consumption and Saving function operates (which means when the level of income changes consumption and savings changes in equal proportion)

- Average Propensity Consume (APC) is the ratio between consumption and income

$$APC = C/Y$$

- Marginal Propensity Consume (MPC) is the ratio between change in consumption and change in income . $MPC = \text{Change in Consumption} / \text{Change in Income } \Delta C / \Delta Y$

$$MPC = \Delta C / \Delta Y$$

Income (Y)	Consumption (C)
	50
100	100
200	150
300	200
400	250
500	300

However, the levels of consumption (C) are affected by levels of savings also.

Since $Y = C + I$

$I = S$

$Y = C + S$

$C = Y - S$ & $S = Y - C$

Hence, we need to know about savings functions.....

4. SAVINGS FUNCTION/PROPENSITY TO SAVE

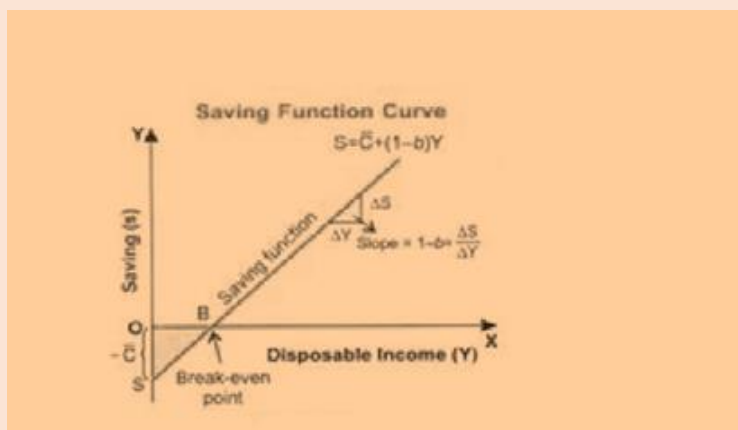
Saving function is the functional relationship between levels of savings at different levels of income .

It explains the portion of income the people are willing / desires to spend on savings (Propensity to save) at different levels of disposable income (Y).

Hence $S = f(Y)$ (OR) $S = -S + b Y$

$$\begin{aligned} S &= Y - C \\ &= Y - (\bar{C} + bY) \quad (\because \bar{C} = bY) \\ &= Y - \bar{C} - bY \\ S &= -\bar{C} + (1 - b) Y \end{aligned}$$

S = Level of Saving , $-S$ = Autonomous Saving (OR) Dissaving (Levels of Savings at zero level of income), b = Marginal Propensity Save (MPS) Y = Levels of income



Income(Y)	Consumption(C)	Savings S
0	50	-50
100	100	0
200	150	50
300	200	100
400	250	150
500	300	200

The saving curve slopes upward which depicts direct relationship between income and saving. The savings functions line SS cuts the income line at point B which is called Break-even point because at this point consumption expenditure is equal to income (or savings are zero).

To the left of break-even point, savings are negative (-) indicating consumption being more than income whereas to the right of break-even point, savings are positive (+) indicating consumption expenditure being less than income. The shaded area reflects dissaving which is equal to the area of autonomous consumption shown as $-C$.

The Savings curve also slopes positively as (i) Saving can be negative (-) at zero or low level of income and (ii) As Income increase, savings also increase but more than the increase in income.

Average Propensity Save (APS) is the ratio between saving and income

$$APS = S/Y$$

Marginal Propensity Saving (MPS) is the ratio between change in Saving and change in income

MPS = Change in Saving / Change in Income $\Delta S / \Delta Y$

$$MPS = \Delta S / \Delta Y$$

Relationship between APC & APS, MPC & MPS:

- **The Sum of APC and APS is equal to 1 i.e, $APS + APC = 1$ (unity)**

Because $Y = C + S$

$$\frac{Y}{Y} = \frac{C}{Y} + \frac{S}{Y}$$

$$1 = APC + APS$$

$$APC = 1 - APS$$

$$APS = 1 - APC$$

- **The Sum of MPC and MPS is equal to 1 i.e, $MPC + MPS = 1$ (unity)**

Because $\Delta Y = \Delta C + \Delta S$

$$\frac{\Delta Y}{\Delta Y} = \frac{\Delta C}{\Delta Y} + \frac{\Delta S}{\Delta Y}$$

$$1 = MPC + MPS$$

$$MPC = 1 - MPS$$

$$MPS = 1 - MPC$$

Note:

1. The value of APS can be negative when the value of consumption exceeds the value of income. At low level of income saving is negative. Example: if income is Rs 1000 and consumption expenditure is Rs 1200

$$Y = C + S \quad S = Y - C$$

$$1000 - 1200 = -200$$

$$APS = -200/1000 = -0.2$$

$$APS = S/Y$$

$$APS = -0.2$$

2. Average propensity to consume can be greater than one:

APC can be greater than one when the consumption exceeds the income. At that level APS will be negative. When the APS is negative APC will be greater than one. e.g.: if the income is 1000 and the consumption is 1200, $APC = 1200/1000 = 1.20$.

3. APC can be equal to one:

APC can be equal to one when $APS = 0$, i.e. when consumption = income.

E.g: $y = 1000$, $c = 1000$.

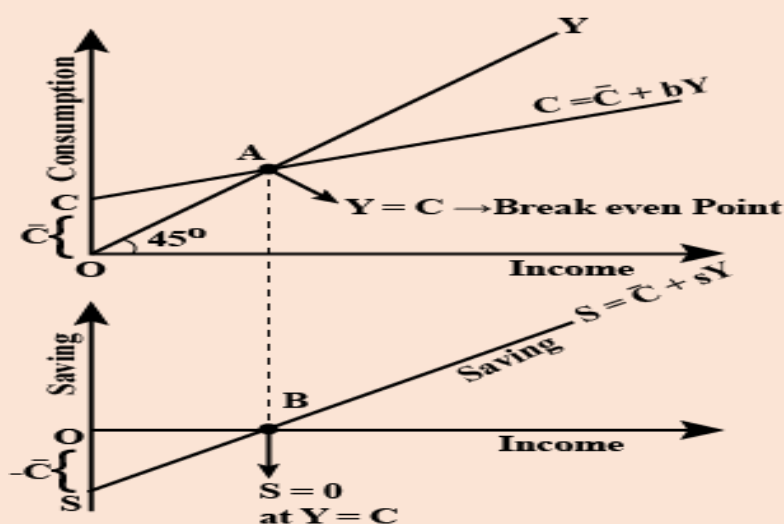
$$APC = C/Y \quad 1000/1000 = 1$$

$$APC = 1$$

$$APC + APS = 1 \quad 1 - APC = APS \quad 1 - 1 = 0$$

How to derive savings curve from consumption curve:

In the diagram $C = \bar{C} + bY$ is the consumption curve.



The 45-degree line is the aggregate supply curve.

At point A, consumption = income i.e. ($Y = C$)

C^- represents the autonomous consumption i.e. consumption at zero level of income.

Steps for derivation of supply curve from consumption curve as follows.

(i) Corresponding to C^- in the consumption function we have $-C^-$ in the saving function.

That is, there are negative savings equal to autonomous consumption at $Y = 0$. This is represented by OS on the negative axis in the lower panel.

(ii) At point B ($Y = C^-$). This implies that all the income is spent on consumption expenditure.

Thus, savings equal to zero. This is shown as $S = 0$ in lower panel. This point is also known as the Break-even point.

(iii) Beyond the break-even point, by connecting points S and Y, we derive the straight upward sloping saving curve. (iv) SS is the required saving curve.

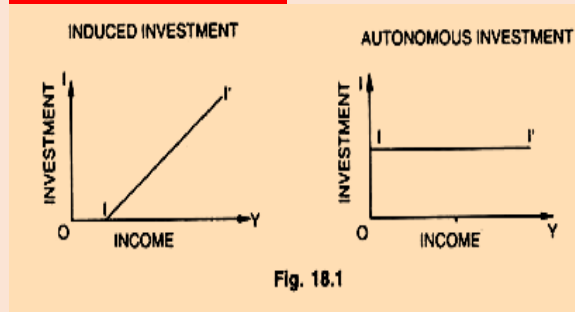
INVESTMENT DEMAND

Meaning of investment (or) Capital formation:

Investment (or) Capital formation is the net addition made to the existing stock of capital during a year in an economy .

Investment is the function of rate of interest.

Types of Investment:



1. Autonomous Investment:

Investments made by the government for social welfare irrespective of levels of income . It remains constant at all levels of Income.

2. Induced Investment:

The Investments made by the private sector with a motive of earning profits. It Increase with an increase in income.i.e. Positively related with levels of income.

Note: to determine equilibrium and levels of AD only

Autonomous investment is considered.

3.Ex-Ante (or) Planned (or) Desired investment :

in realised investment, therefore, realised investment is always equal to realised saving. The investment which is planned or desired to be made by the firms or entrepreneurs in the economy during a period (say, a year) in the beginning of a period is called planned (or ex-ante) investment. The amount of planned (or desired) investment is given by investment demand function (i.e., relationship between investment demand and rate of interest).

4.Ex-post (or) Actual (or) Realised Investment:

It refers to actual investment made by all the entrepreneurs in the economy during a given period. In short, the realised investment of a period, say, a year, is called actual investment (or ex-post investment).

Note: The point to be noted is that ex-post investments of firms are always equal to ex-post savings by households at all levels of income as savings finance investments. Ex-post or realised (or actual) saving and investment are necessarily equal and this is brought about by fluctuations in income. Since unplanned investment also gets included

SHORT-RUN EQUILIBRIUM OUTPUT; INVESTMENT.

DETERMINATION OF EQUILIBRIUM LEVEL OF OUTPUT & EMPLOYMENT:

Short run time period is the period, where technology does not play any role in the determination of the output in an economy. In other words, technology is constant.

Output is only determined exclusively by the level of employment in the economy.

It means, output can be increased by increasing employment and vice-versa.

The equilibrium level of national income is determined at the point where aggregate demand (AD) equals aggregates supply (AS).

$$\boxed{AD = AS \text{ ————— (i)}}$$

As, we have assumed that there is neither foreign trade nor government. Aggregate Demand AD is now reduced to the sum of private consumption expenditure (C) and Investment (I). Therefore,

$$\boxed{AD = C + I \text{(ii)}}$$

Aggregate supply is equal to the national income (Y). It is used either for consumption (C) or saving (S) It can be expressed as:

$$\boxed{AD = Y = C + S \text{ ————— (iii)}}$$

Let's show how both approaches are same.

Putting (i), (ii) and (iii) together, we get:-

$$\begin{aligned} AD &= AS \\ C + I &= C + S \\ I &= S \text{ or } S = I \end{aligned}$$

The above derivation shows, the basic approach $AD = AS$ can also be expressed as $S = I$.

It gives two approaches

$$AD = AS$$

$$S = I$$

DETERMINATION OF INCOME BY AD – AS APPROACH/CONCEPT OF EFFECTIVE DEMAND:

The equilibrium level of income in an economy is determined where Aggregate Demand AD is equal to the Aggregate Supply (AS) (The point where ex ante aggregate demand is equal to ex ante aggregate supply will be equilibrium) $AD = AS$

The point Where $AD=AS$ is called Effective demand which is corresponding to the equilibrium levels of income in an economy, the demand is effective because the equilibrium is decided by levels of AD as AS is perfectly elastic.

Ex-Ante Aggregate Demand (AD) comprises two components, Consumption, and Investment.

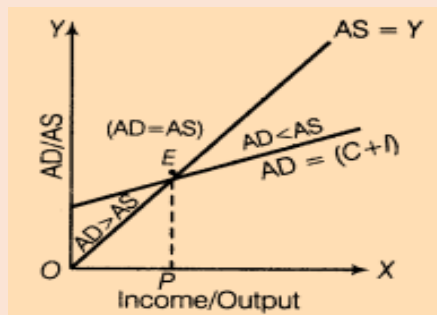
$$AD = C + I$$

to make study simple, Investment is assumed as autonomous (constant). Does not change with the change of level of income. Ex-Ante Aggregate supply is the total planned output and equal to national income ($AS=Y$). It comprises of two components.

$$AS = C + S$$

The curve of the AS is represented by a 45-degree line.

The determination of equilibrium level of income can be better understood with the help of the following schedule and diagram:-



Y	(C)	(S)	(I)	AD	AS	Remarks
0	50	-50	100	150	0	AD > AS
100	100	0	100	200	100	
200	150	50	100	250	200	
300	200	<u>100</u>	<u>100</u>	300	300	AD = AS
400	250	150	100	350	400	AD > AS
500	300	200	100	400	500	

The economy is equilibrium at point E where the AD curve intersects at 45-degree line (AS).

E is the equilibrium level as per the above diagram. At this point planned expenditure equals to the level of output (Ex-ante AD is equal to Ex-Ante AS)

Op is the equilibrium level of Income and output corresponding to point E.

As the above table, Equilibrium of Income is at 300. At this income level AD is equal to AS .

E, is the point of Effective Demand. Effective demand signifies the point where aggregate demand equals to aggregate supply. **Thus, that level where aggregate demand equals aggregate supply is called Effective Demand.**

ADJUSTMENT / CORRECTIVE MECHANISM IF $AD > AS$

Suppose AD is greater than AS . It means that buyers are planning to buy more goods and services than producers are planning to produce. Producers keep a certain stock of goods called inventory. When AD is greater than AS , it means that buyers are buying faster than sellers are expecting. In this situation, inventories start falling and come below the desired level. To bring back the inventories at the desired level producers expand production. This raises the income level which keeps on rising till the AD and the AS once again become equal. This brings the economy back to equilibrium $AD=AS$.

ADJUSTMENT / CORRECTIVE MECHANISM IF $AD < AS$

Now, suppose that AD is less than AS . It means that buyers are planning to buy less than what sellers are planning to produce. As a result, inventories start rising and move above the desired level. As a result, the producers cut back on production and lay off workers.

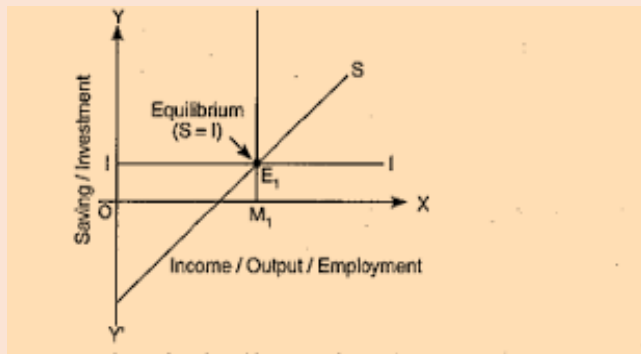
This reduces the income level, i.e. AS. The downward trend continues till AD and AS once again become equal. This brings the economy back to equilibrium.

DETERMINATION OF INCOME BY SAVINGS & INVESTMENT APPROACH

According to this approach, the equilibrium level of income is determined at a level, when planned saving (S) is

equal to planned investment (I).

Let's understand it with the following schedule and diagram



Y	(C)	(S)	(I)	Remarks
0	50	-50	100	S < I
100	100	0	100	
200	150	50	100	
300	200	<u>100</u>	<u>100</u>	S = I
400	250	150	100	S > I
500	300	200	100	

The investment curve is parallel to the X axis as it is not affected by the level of income. The saving curve slopes upwards show a positive relationship with income. The economy is in equilibrium at point E, where planned autonomous investment is equal to planned savings. OY is the equilibrium level of income and output corresponding to point E. The equilibrium level of income as per the table is Rs 400 crore. when ex-ante saving (Planned Saving) is equals to ex-ante investment (Planned Investment).

ADJUSTMENT MECHANISM /What happens when S < I

When planned saving is less than planned investment. It implies households are planning to buy more than what the producer is planning to produce. As a result, planned inventory would fall below the desired level.

In order to bring the inventory back to the desired level, firms would plan to increase the production till saving and investment become equal to each other.

ADJUSTMENT MECHANISM/ What happens When S > I

When planned saving is more than the planned investment. It implies households are planning to buy less than what the producer is planning to produce. As a result, planned inventory would increase above the desired level.

In order to bring the inventory back to the desired level, firms would plan to reduce the production till saving and investment become equal to each other.

INVESTMENT MULTIPLIER AND ITS MECHANISM

MEANING OF INVESTMENT MULTIPLIER: - The investment multiplier is the ratio of change in income to change in investment. Symbolically,

$$\text{Multiplier (K)} = \Delta Y / \Delta I$$

INVESTMENT MULTIPLIER & THE VALUE OF MPC, MPS :

The value of the multiplier (K) depends upon the value of marginal propensity to consume(MPC).

There is a direct relationship between K and MPC i.e., MPC increases K also increases and vice versa. Similarly ,there is an inverse relationship between K and MPS i.e., MPS increases K

decrease and vice versa. If the value of MPC is max. i.e. 1 then K will also max. i.e. ∞

$$\Delta y = K \times \Delta I, \quad \Delta y = 1/(1-MPC) \times \Delta I, \quad \Delta y = 1/MPS \times \Delta I$$

Working of Multiplier:

Investment multiplier works on the fact that the expenditure of one person is income of another person. The working of multiplier can be explained with the help of one numerical example. Here we assume that initially investment is increased by Rs. 100 crores and MPC is 0.5. Multiplier tells us what will be the final change in the income, as a result of change in investment. Change in investment results in the change in income.

Symbolically: $\Delta I \rightarrow \Delta Y \rightarrow \Delta C \rightarrow \Delta Y$.

Following table will explain the working of Investment Multiplier (K)

Round	Change in Investment ΔI	Change in Income ΔY	Change in Consumption ΔC
I	100	100	50
II		50	25
III		25	12.5
---	----	---	---
Total		200	100

The table shows that as additional investment increases by Rs. 100 crore there will be change in income by Rs. 100 Crore in first round, MPC is 0.5 therefore consumption will increase by $100 \times 0.5 = 50$ crore, the remaining amount will be saved.

This increased consumption (50 crore) will increase the income by 50 crores in the second round

This process of income generation will go on and the consumption and income will increase in every round till total income increase by Rs. 200 crores as MPC is 0.5

Forward and Backward action:

Multiplier action is forward when there is multiple increases in income caused by an increase in Investment. On the other hand, multiplier action is backward if there are multiple decreases in income caused by decrease in investment.

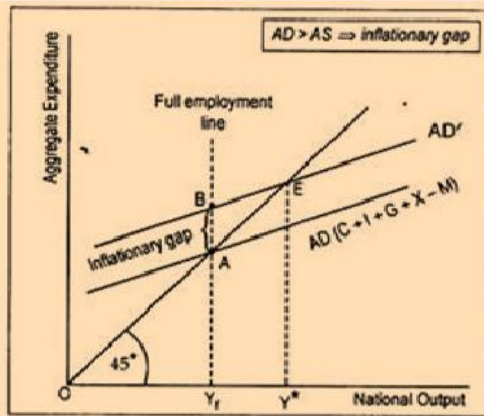
PROBLEMS OF EXCESS DEMAND & DEFICIT DEMAND:

The equilibrium output in the economy also determines the level of employment, given the quantities of other factors of production (think of a production function at aggregate level). This means that the level of output determined by the equality of Y with AD does not necessarily mean the level of output at which everyone is employed. Full employment level of income is that level of income where all the factors of production are fully employed in the production process. Recall that equilibrium attained at the point of equality of Y and AD by itself does not signify full employment of resources. Equilibrium only means that

if left to itself the level of income in the economy will not change even when there is unemployment in the economy. The equilibrium level of output may be more or less than the full employment level of output. Hence an economy may be in the situations Excess demand or Excess supply.

A) EXCESS DEMAND (OR) INFLATIONARY GAP:

If the equilibrium level of output is more than the full employment level, it is due to the fact that the



demand is more than the level of output produced at full employment level. This situation is called the situation of excess demand. It is due to the fact that the aggregate demand is more than the aggregate supply at full employment level.

AD > AS at full Employment

It leads to rise in prices in the long run and hence the amount by which the AD exceeds the AS at full employment level is known as inflationary gap.

B) DEFICIENT DEMAND (OR) DEFLATIONARY GAP:

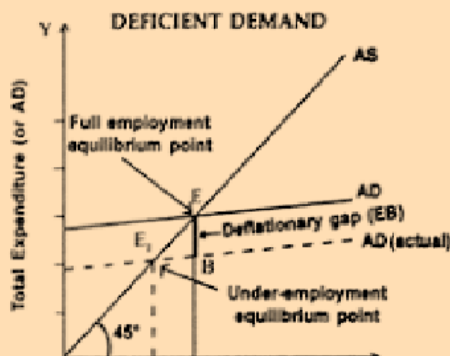
If it is less than the full employment of output, it is due to the fact that demand is not enough to employ all factors of production. This situation is called the situation of deficient demand.

called the situation of excess demand.

It is due to the fact that the aggregate demand is less than the aggregate supply at full employment level.

AD < AS at full Employment

It leads to decline in prices in the long run and hence the amount by which AS exceeds AD at full employment level is known as Deflationary Gap.



MEASURES TO CORRECT EXCESS DEMAND & EXCESS SUPPLY:

For an economy neither Excess demand nor excess supply should prevail, and must ensure equilibrium level of income always. Hence the Government and the Central Bank adopts various policy measures to remove the situations of excess demand & excess supply.

Some of the important measures are:

Changes in government spending

Tax policy by Government

Changes in Money supply by Central Bank

The above three measures are explained in detail in the table given below:

Measure	Tools used	Meaning	Action & Effect during Excess Demand	Action & Effect during Deficit Demand
Changes in Government Spending	Changes in Public (Government Expenditure)	Expenditure incurred by the public authorities for the maintenance of govt and social	Govt will reduce its expenditure on public work like construction of roads, buildings etc. Government will reduce the non-development	Govt will increase its expenditure on public work like construction of roads, buildings etc. Government will increase the non-development expenditure

		welfare.	expenditure which in turn reduce the purchasing power of people and reduce the AD	which in turn boosts the purchasing power of people and raises the AD
Tax Policy	Increase & Decrease in both Direct and Indirect Taxes	Tax is the compulsory legal payment made by the citizens to the government for without any direct return.	<u>Govt will increase the rates of taxes and may introduce new taxes.</u> To reduce the disposable income in the hands of people to reduce the AD.	<u>Govt will decrease the rates of taxes and may withdraw existing taxes.</u> To increase the disposable income in the hands of people to pull the AD up.
Money supply Control Measures by Central Bank (RBI)	1.CRR (Cash Reserve Ratio)	Percentage of net total demand deposits of commercial banks retained with central Bank as reserve.	<u>Central bank will increase the CRR.</u> This will reduce the lending capacity of the commercial banks and will reduce the money supply ,hence AD falls .	<u>Central bank will decrease the CRR.</u> This will rise the lending capacity of the commercial banks and will increase the money supply; hence AD rises.
	2.SLR (Statutory Liquidity Ratio)	Percentage of net total demand deposits of commercial banks kept with themselves in the form of government securities, shares, Gold etc,	<u>Central bank will increase SLR</u> This will reduce the lending capacity of the commercial banks and will reduce the money supply ,hence AD falls	<u>Central bank will decrease SLR</u> This will increase the lending capacity of the commercial banks and will rise the money supply; hence AD rises.
	3.Bank Rate	Interest rate at which Central bank lends to commercial banks in long term .	<u>Central bank will increase bank rate.</u> This will make the credit costlier since commercial bank will increase the lending rates. Hence people may borrow less and decreases the credit creation and thus reduces AD.	<u>Central bank will Decrease bank rate.</u> This will make the credit Cheaper since commercial bank will decrease the lending rates. Hence people may borrow more and increases the credit creation and thus rises AD.
	4.Repo Rate	Interest rate at which Central bank lends to commercial banks on short term basis	<u>Central bank will increase Repo Rate.</u> This will make the loans taken by commercial banks expensive. Hence commercial banks increase their lending rates and thus reduce the credit availability and AD.	<u>Central bank will increase Repo Rate.</u> This will make the loans taken by commercial banks less expensive. Hence commercial banks decrease their lending rates and thus increases the credit availability and AD.
	5.Reverse Repo Rate	Interest rate at which the commercial banks park their surplus funds with central bank .	<u>Central bank will increase the reverse repo rate.</u> This will encourage the commercial banks to park more funds with central bank and will reduce the lending capacity and AD.	<u>Central bank will increase the reverse repo rate.</u> This will encourage the commercial banks to park less funds with central bank and will increase the lending capacity and AD.

6.Open Market Operation	Buying and selling of government securities (Bonds) by the central Bank to public in open market.	<u>Central bank sells the govt. Securities in the open market.</u> By selling securities the central bank soaks the liquidity and reduces the AD.	<u>Central bank sells the govt. Securities in the open market.</u> By buying back the securities the central bank releases the liquidity and rises the AD.
7.Margin Requirement	Margin is the difference between the amount of loan and the market value of securities offered against the loan.	<u>Central bank increases the margin requirement.</u> At higher margin requirement people tend to borrow less, hence AD falls.	<u>Central bank increases the margin requirement.</u> At lower margin requirement people tend to borrow more , hence AD rises.

PRACTICE QUESTIONS

MULTIPLE CHOICE QUESTIONS (01 Marks)

1..Value of Money Multiplier(increases/decreases/remains unchanged) with an increase in Cash Reserve Ratio. (Fill up the blank with correct alternative).

Ans: Decreases

2. In an economy, break-even point and equilibrium point may lie at the same level of income, if ex-ante investments are (Fill up the blank with correct answer) **Ans: Zero**

3. The difference by which actual Aggregate Demand exceeds the Aggregate Demand, required to establish full employment equilibrium is known as.....(inflationary gap/deflationary gap).

Ans: Inflationary Gap

4.If in an economy, the value of investment multiplier is 4 and Autonomous Consumption is Rs 30 Crore,the relevant consumption function would be :

a) $C=30+0.75 Y$ b) $C=(-)30+0.25Y$ c) $C=30-0.75Y$ d) $C=30-0.25Y$ **Ans:c**

5.If increase in National Income is equal to increase in consumption, identity the value of Marginal Propensity to Save :

a) Equal to unity b) Greater than one c) Less than one d) Equal to zero **Ans:d**

6. Read the following statement -Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): Ex-post Investments represent planned Investments; whereas ex-ante Investments represent actual level of investments.

Reason (R): At equilibrium level, Ex-ante Savings and Ex-ante Investments are always equal.

Alternatives:

a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).

b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).

c) Assertion (A) is true but Reason (R) is false.

d) Assertion (A) is false but Reason (R) is true.

Ans: d

7. Suppose for a given economy, $S = -60 + 0.1Y$ and $I = \text{Rs } 4,000$ crore (Where S = Saving Function, Y = National Income and I = Investment Expenditure) Equilibrium level of Income would be Rs _____ crore. (Choose the correct alternative to fill up the blank)

Alternatives:

a) 4,000 b) 40,000 c) 40,600 d) 60,400 **Ans:c**

8. Which of the following can never have negative value

- a. APC b. MPC c. MPS d. APS

Ans: d

9. _____ (Aggregate Demand/Aggregate Supply) refers to total ex-ante expenditure in an economy during an accounting year. (Fill in the blank with the correct alternative).

Ans: Aggregate Demand

10. Complete the flow $\Delta I \rightarrow \Delta Y \rightarrow \Delta C \rightarrow$ _____

- a. ΔY b. ΔS c. ΔD d. ΔC

Ans: a

11. If the initial increase in the investment is Rs 1000 and $MPC = 0.8$, the multiplier will be

- a. 5 b. 4 c. 3 d. 6

Ans: a

12. The level of equilibrium income is also determined by

- a. Planned Savings and Planned Consumption b. Planned AD and Planned national income
c. Planned Savings and Planned Investment d. Planned consumption and Planned AS

Ans: c

13. According to the effective demand principle:

- a) at a certain price, the output shall not be determined by any known factor
b) at a certain price, the output will remain unaffected by rise or fall in demand
c) at a certain price, equilibrium output will be solely determined by the aggregate demand
d) none of the above

Ans: c

14. Read the following statement - Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): Ex-post Investments represent planned Investments; whereas ex-ante Investments represent the actual level of investments.

Reason (R): At the equilibrium level, Ex-ante Savings and Ex-ante Investments are always equal.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
c) Assertion (A) is true but Reason (R) is false.
d) Assertion (A) is false but Reason (R) is true.

Ans: d

15. Multiplier is equal to :

- (a) $\Delta Y / \Delta S$ (b) $\Delta Y / \Delta I$ (c) $\Delta I / \Delta Y$ (d) $\Delta Y / \Delta I$

Ans: d

16. Which of the statements is true about the relationship between planned savings and planned investment?

- a. When planned investment is more than planned savings, the national income may increase
b. When planned investment is more than planned savings, the national income may decrease
c. When planned investment is more than planned savings, there is no effect on the national income
d. None of the above

Ans: b

17. From the following given sets of statements in column I and II, choose the incorrect pair of Statements.

Options:

- a) A-1 b) B-2 c) C-3 d) D-4

Ans: d

18. Which among the following is induced investment

- i. Government has set up public health centres in rural areas.
ii. Government has decided to invest Rs. 1,000 crores to save Sunderban Forests.
iii. Airtel has invested Rs 1,000 crore to improve its services.

Alternatives :

i & ii b) ii & iii c) iii alone d) All of these

Ans: c

19. Piling up of stocks in the warehouses is known as _____. (Fill in the blank with correct alternative)

a) Accumulation of inventories

b) Intended accumulation of inventories

c) Unintended accumulation of inventories

d) None of the above

Ans: a

20. Which of the following statement about investment multiplier is incorrect:

a) Maximum value of investment multiplier is ∞

b) Minimum value of investment multiplier is 0

c) $K = \Delta Y / \Delta I$

d) There is a Direct relationship between investment multiplier and MPC

Ans: a

21. If entire additional income is saved then MPC is

a) Zero b) 1 c) Infinity d) 2

Ans: a

22. At zero level of income, consumption is

a) Zero b) positive c) Negative d) All of these

Ans: b

23. If autonomous consumption is 50 and MPC is 0.75 and national income is 2400 crores, the level consumption will be-

a) 1250

b) 1550

c) 1650

d) 1850

Ans: d24. If $AD > AS$ national income will

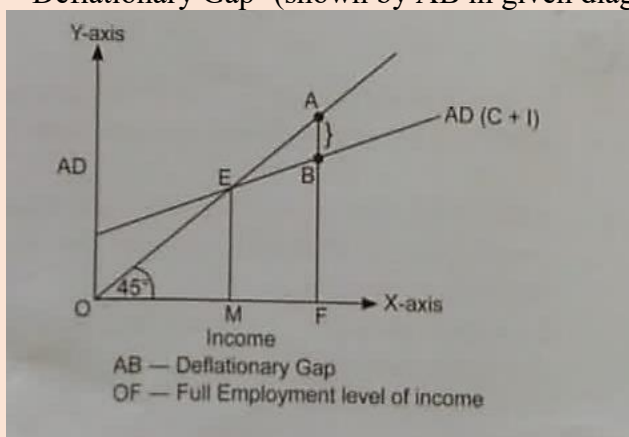
a) Increase b) Decrease c) Not change d) May increase or decrease

Ans: a25. In the consumption function, $200 + 0.6Y$, the value of autonomous saving will be

a) 200 b) -200 c) 0.6 d) 0.4

Ans: b**3 / 4 MARKS QUESTIONS****1. Explain with the help of diagram the concept of deficient demand in macroeconomics.**

When at full employment level income, AD is lesser than AS, the deficiency in AD is termed as "Deficient Demand". As deficient demand leads to deflation in the economy, it is also known as 'Deflationary Gap' (shown by AB in given diagram)



Point E denotes the point of Equilibrium, at this point AD curve intersects the 45° Line. OM denotes the Equilibrium output. Let us suppose that full employment is OF in the diagram. At the full employment level, AD is denoted by BF, while AS is denoted by AF this implies that AD is less than what is necessary to achieve full employment output (OF). It denotes situation of Deficient demand, diagrammatically Shown by 'AB', which denotes the deflationary Gap $(AF - BF) = AB$.

2. The Government has raised the exemption limit for the payment of Income tax from "2 lakhs to 2.5 Lakh." If the situation of deficient demand is prevailing in the economy, what will be the impact of this action Taken by the Government?

Ans. Due to increase in exemption limit from 2 lakhs to 2.5 lakh, disposable income of public will be Increased. Increase in disposable income will help to Generate more demand for consumption. Due to

this, Investment expenditure would also increase to produce More goods in response of increase in demand. Thus, Consumption expenditure and investment expenditure Both will increase. This way deficient demand in the Economy can be removed up to an extent.

3.Explain, how the ‘Reverse Repo Rate’ helps in Correcting Excess Demand in an economy?

Ans. Excess demand exists when aggregate demand exceeds Aggregate supply at the full employment level. Excess Demand leads to inflationary tendencies or rise in prices. Reverse Repo Rate is the rate at which Central Bank Borrows money from commercial banks. During excess Demand, Central Bank increases Reverse Repo Rate. Due to the high rate of interest, more and more banks supply to Central Bank because of more earnings. This decreases the supply of money in the market and thus, reduces the Excess demand.

4. Explain the role of bank rate in dealing with the Problem of deficient demand.

Ans. Bank Rate is the rate at which the Central Bank of A country gives credit to the commercial banks. For Controlling deficient demand, Central Bank should Decrease the Bank Rate. Decrease in Bank Rate reduces the market rate of interest and credit becomes cheaper. Accordingly, demand for credit expands and consequently, Aggregate demand is increased and deficient demand is Checked.

5.Explain briefly how changes in open market operations be helpful in correcting deficient demand.

Ans. Open market operations. For controlling deficient Demand, the central bank should resort to buying of Government securities. By buying government securities, the central bank injects the additional purchasing power into the system which results in the expansion of credit. As a result, aggregate demand increases and the problem of deficient demand can be solved.

6.To boost the falling demand in the economy, Reserve Bank of India recently reduced Repo Rate Reverse Repo Rate.” Elaborate the rationale behind the steps taken by the Central Bank.

Ans. The steps taken by the Central Bank to boost the falling Demand in the economy are justified as the reduction in the repo rate and reverse repo rate will increase the availability of funds in the market through the Commercial banks.

Rationale: A decrease in Repo/Reverse Repo Rate Will Push the commercial banks to reduce the lending rate and will eventually make the borrowings cheaper for the General public. As a result, the consumption demand in the economy may increase.

7.Indian economy saw its worst contraction in Decades. It is in a deep vicious cycle where demand Is contracting heavily.” The Hindu; August 31st, 2020.’ State and discuss any two monetary measures that May be taken by the government of India to correct the situation indicated in the above news report.

Ans. The two monetary measures that may be taken by the Government of India through Central Bank (RBI) to Correct the given situation of deficient demand are:

- (a). Decrease in bank rate. For controlling deficient Demand, the central bank should decrease the bank Rate. A decrease in bank rate lowers the rate of Interest and credit becomes cheaper. Accordingly, the demand for credit expands and Aggregate demand increases.
- (b). Purchase of government securities. For controlling Deficient demand, the central bank should resort to buying of government securities. By buying the government securities, the central bank injects Additional purchasing power in the system which Results in the expansion of credit. As a result, Aggregate demand increases. (or any other relevant monetary measure)

8.While the economy is showing signs of shedding its lockdown inertia, long-term drivers of growth such as Consumption and investment are still in jeopardy. It Will not revive unless there is a pickup in consumer and business sentiments? Hindustan Times, October 2nd, 2020 State and discuss any two fiscal measures which can be taken by the Government of India to correct the Above situation.

Ans. The given situation suggests that there is a situation of “deflation”, i.e., Aggregate Demand is less than Aggregate Supply/output in the economy. In order to Correct/control the given situation, the government can take the following two fiscal measures:

A). Increase in government spending: The government May increase its expenditure, which in turn will Increase the purchasing power in the hands of the Public. As a result, this will lead to an increase in the aggregate demand of the economy which will Then be brought equal to the aggregate supply/output of the economy.

B). Decrease in taxes: The government can also Decrease the taxes in the economy, so as to increase the purchasing power in the hands of the public. This will increase the aggregate demand in the Economy, which will then be brought equal to the Aggregate supply/output of the economy. Thus, The Situation of deflation will be controlled

9. Giving reason, state whether the following statement are true or false:

(a) Average propensity to save is always greater than zero.

(b) Value of investment multiplier varies between zero and infinity.

Ans. (a) False, PS is not always than zero, but it can be negative. This is so at very low level of income, when consumption expenditure exceeds income. E.g. at an income level of Rs100, if the consumption expenditure is Rs 120, the saving is (-20).

$$APS = S/Y = -20/100 = 0.2$$

(b) False, Value of investment multiplier varies between one and infinity.

10. Define:

(a) Autonomous consumption expenditure

(b) Average propensity to consume

Ans. (a) Autonomous consumption expenditure is the expenditure which must be undertaken even at zero level of income. In other words, it refers to the consumption expenditure which does not depend upon level of income, i.e., the minimum consumption level when the level of income is zero.

It is indicated by c.

(b) Average propensity to consume (APC) is the consumption per unit of income. In other words, it is the ratio of the total consumption to total income, i.e., $APC = C/Y$

11. Explain the relationship between marginal propensity to consume and investment multiplier.

Ans. Relationship between multiplier and MPC. The value of the multiplier varies directly with MPC. Higher the MPC, the higher will be the value of the multiplier and lower the MPC, the smaller will be the value of the multiplier. The relationship is expressed as:

$$K = 1/1 - MPC$$

For example, if $MPC = 0.5$

$$\text{Then } k = 1/1 - 0.5 = 1/0.5 = 2$$

For example, if $MPC = 0.75$

$$\text{Then } k = 1/1 - 0.75 = 1/0.25 = 4$$

It is clear from above that higher the MPC, the larger will be the size of the multiplier and lower the MPC, the smaller will be the multiplier. The size of multiplier varies directly with MPC.

12. Define investment multiplier. Explain the relationship between marginal propensity to save and investment multiplier.

Ans. Investment multiplier is defined as the ratio of changes in income due to change in the investment.

Symbolically, multiplier $K = \Delta Y / \Delta I$

Relationship between multiplier and MPS. The value of the multiplier varies with MPS. Higher the MPS, lower will be the size of multiplier and lower the MPS, the larger will be the value of the multiplier.

The relationship can be expressed as

$$K = 1/MPS$$

For example, if $MPS = 0.4$, then

$$K=1/MPS=1/0.4=2.5$$

$$\text{IF } MPS=0.1 \text{ then } k=1/MPS=1/0.1=10$$

Thus, it is clear from above that, higher the MPS, the smaller will be the size of multiplier and lower the MPS, the larger will be the size of multiplier. Thus, the size of multiplier and MPS are inversely related.

13. Calculate the value of Marginal Propensity to Consume (MPC), if in an economy, autonomous consumption is Rs 500 crores, ex-ante investments are Rs 4000 crores and equilibrium level of Income of the economy is Rs 18,000 crores.

Ans: At equilibrium level of Income in the economy $Y = C + I$

Given Autonomous Consumption $\bar{C}$ = Rs 500 crores and Ex-ante Investments $I =$ Rs 4000 crores

$$18\,000 = 500 + MPC \cdot 18\,000 + 4\,000$$

$$18\,000 = 18\,000 - 4\,500 + MPC \cdot 18\,000 \quad \text{MPC} = 0.75.$$

14. If in an economy Saving function is given by $S = (-) 50 + 0.2 Y$ and $Y =$ Rs 2000 crores; consumption expenditure for the economy would be Rs 1,650 crores and the autonomous investment

is Rs 50 crores and the marginal propensity to consume is 0.8. True or False? Justify your answer with proper calculations.

Ans: Yes, all given values are correct. $S = -50 + 0.2Y$

$$= -50 + 0.2 \cdot 2\,000 = -50 + 400 = \text{Rs. } 350 \text{ crores}$$

At equilibrium level of income: $Y = C + S$
 $2\,000 = C + 350$
 $C = 2\,000 - 350 = 1\,650$ in Rs.

15. Explain how the economy achieves equilibrium level of income using Savings Investment (S-I) approach.

Ans: The Savings-Investment (S-I) approach states that an economy reaches equilibrium when planned savings (S) are equal to planned investments (I). At this point, there's no tendency for income or output to change.

• **Equilibrium point:** The equilibrium point is where the saving and investment curves intersect.

Formula: You can calculate the equilibrium level of income using a formula like $AD = AS$, where AD is aggregate demand and AS is aggregate supply.

$$AD = C + I \text{ and } AS = C + S$$

$$\text{At equilibrium } AD = AS \quad C + I = C + S \quad \text{hence } I = S$$

6 MARKS QUESTIONS

1. What is meant by aggregate demand? State its components. (OR)

State and discuss the components of aggregate demand.

Ans. Aggregate demand represents the planned expenditure on final goods and services in an economy during a period of time.

There are four components of aggregate demand (AD):

□ **Private Consumption Expenditure (C).** It is the most important component of aggregate demand. It refers to the total amount of expenditure incurred by the households on the purchase of final goods and services to satisfy their wants.

□ **Investment Expenditure (I).** It refers to the expenditure incurred by the private firm on the purchase of capital goods such as machinery and equipment, construction work, etc.

□ **Government Expenditure (G).** It refers to the expenditure incurred by the government on the purchase of final goods and services. The level of government expenditure is determined by the government's policy.

□ **Net Exports.** Net exports is the difference between export and imports. It shows the effect of domestic spending on foreign goods and services (Imports) and foreign spending on domestic goods and services (Exports).

2.Explain how the level of effective demand is attained in a economy, if the Aggregate Demand is more than the Aggregate Supply.

Ans: Effective demand refers to that level of output where aggregate demand is equal to the aggregate supply. If aggregate demand exceeds aggregate supply, it means buyers are planning to buy more goods and services than producers are planning to produce. Thus, the inventories in hand with the producers will start falling. As a result, producers will plan to raise the production. This will increase the level of income

up to the level aggregate demand is equal to aggregate supply.

3.Explain the consumption function with help of schedule and diagram.

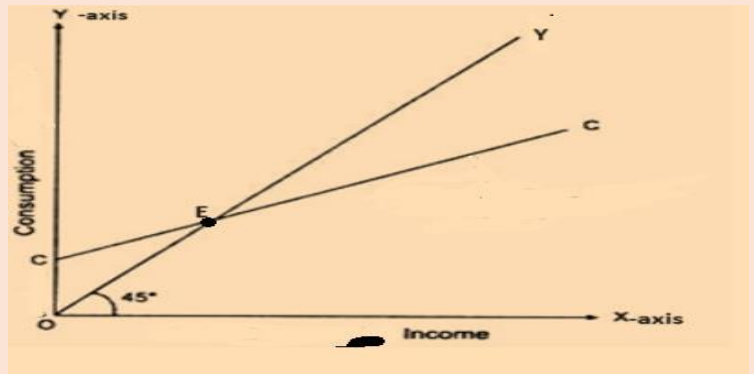
Ans: Consumption function shows the relationship between consumption and income.

$$C = f(Y)$$

This equation states that there is a direct relation between consumption and the level of income. As the level of income increases, consumption is less than the increase in income.

The concept of consumption function can be further explained by following consumption schedule and curve:

Income	Consumption
0	50
100	100
200	150
300	200
400	250
500	300



The above table and diagram show that as the income increases, consumption also increases but the increase in consumption is less than increase in income.

The above table and diagram show that as the income increases, consumption also increases but the increase in consumption is less than increase in income.

4.Explain the components of saving function:

Ans: Saving is defined as the excess of income over consumption expenditure. The concept of saving is closely related to the concept of consumption. Saving is the part of income that is not consumed.

Generally, as the level of income increase, saving also increases and vice versa.

Saving function or the propensity to save expresses the relationship between saving and the level of income. It is simply the desire of the households to hoard a part of their total disposable income.

Symbolically, the functional relation between saving and income can be defined as $S = f(Y)$.

We know,

$$Y = C + S;$$

$$\text{Thus, } S = Y - C;$$

Where, Y = Income; S = Saving; C = Consumption

The equation shows that the remaining amount after the deduction of total expenditure from total income is saving. Thus, saving is that part of income which is not spent on consumption.

Attributes of Saving Function

Saving function or propensity to save has two major attributes:

- Average Propensity to Save (APS)
- Marginal Propensity to Save (MPS)

5.Give two reasons which led to an inflationary gap in the economy and state its two effects. (Or)

Give two reasons which led to a deflationary gap in the economy and state its two effects.

A Reasons for inflationary gap (or excess demand):

- Increase in consumption due to rise the propensity to consume.
- Decrease in tax rates also leads to higher disposable income with people

Effects of inflationary gap

- It causes a continuous rise in the price of goods and producers are able to get abnormal profits due to this.
- It may result in a price – wage spiral i.e. due to rise in prices, the labour unions will demand higher wages. Higher wage will increase the cost of production and it will again lead to a rise in prices.

(Or)

Reasons for deflationary gap (or deficient demand):

- Decrease in consumption due to fall in the propensity to consume.
- Decrease in government expenditure or decrease in exports of the country.

Effects of deflationary gap

- It causes a gradual fall in income, prices, employment and overall output in the economy.
- Due to falling prices, the purchasing power of the consumer increase. On the other hand, producers may suffer losses in deflationary situation.

UNIT 4: GOVERNMENT BUDGET AND THE ECONOMY

Meaning-

A government budget is an annual statement showing item-wise estimates of receipts and expenditures during a fiscal year. A fiscal year is taken from 1st April to 31st March.

A) Objectives of the Government Budget

1) Reallocation of Resources:

Through budgetary policy, the government aims to reallocate resources under the economic (profit maximization) and social (public welfare) priorities of the country.

Government can influence the allocation of resources through the:

a) Tax concessions or subsidies:

To encourage investment, the government can give tax concessions, subsidies, etc. to the producers. For example, the government discourages the production of harmful consumption goods (like liquor, Cigarettes, etc.) through heavy taxes and encourages the use of khadi products by providing subsidies.

b) Directly producing goods and services:

There are many non-profitable economic activities, which are not undertaken by the private sector Like water supply, sanitation, law and order, national defence, etc. These are called public goods. Such activities are necessarily undertaken by the government in the public interest and to raise social Welfare.

2) Reducing Inequalities in Income & Wealth:

Economic inequality is an inherent part of every economic system.

The government aims to reduce such inequalities of income and wealth, through its budgetary policy.

The government aims to influence the distribution of income by imposing taxes on the rich and Spending more on the welfare of the poor. It will reduce the income of the rich and raise the standard of living of the poor, thus reducing inequalities in the distribution of income.

3) Economic Stability:

Economic stability means the absence of large-scale fluctuation in prices. Such fluctuations create uncertainties in the economy. Government can exercise control over these fluctuations through taxes and expenditures. Inflationary tendencies emerge when aggregate demand is higher than aggregate supply. Government can bring down aggregate demand by reducing its expenditure. During deflation, the government can increase its expenditure and give tax concessions and Subsidies. In short, policies of the surplus budget during inflation and deficit budget during deflation help to Maintain the stability

of prices in the economy.

4) **Management of Public Enterprises:**

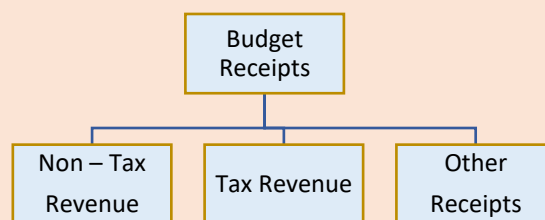
These are large numbers of public sector industries (especially natural monopolies), which are established and managed for the social welfare of the public. The budget is prepared with the objective of making various provisions for managing such Enterprises and providing them with financial help.

5) **Economic Growth:**

Economic growth implies a sustainable increase in the Real GDP of an economy, i.e. an increase in the Volume of goods and services produced in an economy. A budget can be an effective tool to ensure economic growth in a country. If the government provides tax rebates and other incentives for Productive ventures and projects, it can stimulate savings and Investments in an economy.

B) Budget Receipts

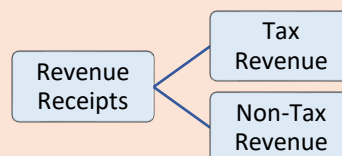
Budget receipts refer to the estimated Money receipts of the government from all sources during a given fiscal Year.



1) Revenue Receipts

Revenue Receipts refer to those receipts which neither create any liability nor Cause any reduction in the assets of the government. They are regular and recurring in nature and the government receives them in its normal course of activities. A Receipt is a revenue receipt if it satisfies the following two essential Conditions: Neither creates a Liability Nor reduces any Asset.

Sources of Revenue Receipts



➤ **Tax Revenue**

Tax revenue refers to the total of receipts from taxes and Other duties imposed by the government. Tax is a compulsory payment, i.e., no one can refuse to pay it;

Tax receipts are spent by the government for the common Benefit of people in the country. A taxpayer cannot expect That the tax amount will be used for his direct benefit.

✓ **Types of Tax Revenue**

Tax Revenue can be further classified as -Direct Tax Indirect Tax

Direct Tax

Direct taxes refer to taxes that are imposed on the property and income of Individuals and companies and are paid directly by them to the government. They are imposed on individuals and companies. They directly affect the income level and purchasing power of people and help to change the level of aggregate demand in the economy. Examples: Income tax, Corporate Tax, Interest Tax, Death duty, Capital gains tax, etc.

Indirect tax

Indirect tax refers to those taxes which can be shifted to another Person/entity. Their monetary burden is ultimately borne by the final users of Goods and services, rather than the person on whom the tax is levied. They are imposed on goods and services.

The liability to pay the tax (i.e. impact) and actual burden of the tax (i.e. Incidence) lie on different persons, i.e. its burden can be shifted to others. Example Goods and Service Tax.

➤ **Non-Tax Revenue**

Non-tax revenue refers to those receipts of the government from all sources other than those of tax receipts.

The Sources of Non – Tax Revenue are as follows:

✓ **Interest**

Government receives interest on loans given by it to the state governments, union Territories, and the general public. Interest receipts from these loans are an important source of non-tax revenue.

✓ **Profits and Dividends**

The government earns profit through public sector undertakings like Indian Railways, LIC, BHEL, etc . It earns profit from the sale proceeds of the product of public enterprises. The government also gets dividends from its investments in other companies.

✓ **Fee**

It refers to charges imposed by the government to cover the Cost of recurring services provided by it. Such services are generally in the public interest and fees are Paid by those who receive such services. E.g. Court Fees, Registration Fees, Import Fees, etc.

✓ **Fines and Penalties**

It refers to the claim of the government on the property of an Escheats person who dies without leaving behind any legal heir or a will. These are in the form of penalties that are imposed by the courts for non-forfeitures compliance with orders or non-fulfilment of contracts.

✓ **Special Assessments**

Government receives gifts and grants from foreign governments and international organizations. Sometimes, individuals and companies also voluntarily Gift money to the government. Such gifts are not a fixed source of revenue and are generally received during national crises such as war, flood, etc.

(II)Capital Receipts

Capital receipts refer to those receipts which either create a liability or cause a Reduction in the assets of the government. They are non-recurring and non-routine.

A receipt is a capital receipt, if it satisfies any one Condition Either creates a Liability Or reduces an Asset

The Sources of Capital Receipts are:

✓ **Recovery of Loans :**

Government grants various loans to the state government or union territories. Recovery of such loans is a capital receipt as it reduces the assets of the government.

✓ **Borrowings:**

Borrowings are the funds raised by the government to meet excess expenditures.

The government borrows funds from:

- a) Open market (public)
- b) Reserve Bank of India (RBI)
- c) Foreign governments (like loans from the USA)
- d) International institutions (like the world bank, international monetary fund).

N; B- Borrowings are capital receipts as they create a liability for the government.

(III) Other Receipts:

These include:

✓ **Disinvestment :**

Disinvestment refers to the act of selling a part or the whole of shares of selected Public sector undertakings (PSUs) held by the government. They have termed capital receipts as they reduce the assets of the government. When the government sells a part or whole of its shares, it leads to the transfer of ownership of PSUs to private enterprises.

✓ **Small Savings :**

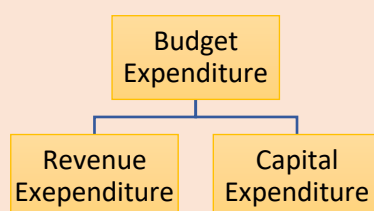
Small savings refer to funds raised from the public in the form of post office deposits, Kisan Vikas Patras, etc. They are treated as capital receipts as they lead to an increase in liability.

Differences between Revenue Receipts & Capital Receipts are:

	Revenue Receipts	Capital Receipts
Meaning	They neither create a Liability nor reduce any Asset of the government.	They either create any liability or reduce any asset of the Government
Nature	They are regular and Recurring in nature.	They are irregular and non-Recurring in nature.
Future Obligations	There is no future Obligation to return the Amount.	In the case of certain capital Receipts (like borrowings), there Is future obligation to return the amount along with interest.
Examples	Tax revenue (like income Tax, goods and services tax, Etc.) and non-tax revenue	(like interest, fees, etc.) Borrowings, disinvestment, etc.

(C) Budget Expenditure

Budget expenditure refers to the estimated expenditure of the government during a given fiscal year. The Budget Expenditure can be broadly Categorized as:



(I) Revenue Expenditure

- ✓ Revenue expenditure refers to the expenditure which neither creates any asset
- ✓ It is recurring in nature.
- ✓ It is incurred on the normal functioning of the government and the provisions

For various services.

- ✓ Examples: payment of salary, pensions, interests, expenditure on Administrative services, Defence services, health services, grants to state, etc.
- ✓ An expenditure is a revenue expenditure, if it satisfies the following two Essential conditions. Nor causes a reduction in any liability of the government.

(II) Capital Expenditure

- ✓ Capital expenditure refers to the expenditure which either creates an asset or causes a reduction in the liabilities of the government.
- ✓ It is non-recurring in nature.
- ✓ It adds to the capital stock of the economy and increases its productivity through expenditure on long-period development programs like metro or flyover.
- ✓ Examples : loan to states and union territories, expenditure on purchase of machinery, etc.
- ✓ An expenditure is a capital expenditure, if it satisfies any one of the following two conditions: Either creates an Asset Or reduces a Liability.

(D)Types of Budget

✓ **Balanced Budget**

A government budget is said to be a balanced budget if estimated Government receipts are equal to the estimated government expenditure.

✓ **Surplus Budget**

If estimated government receipts are more than the estimated Government expenditure, then the budget is termed a 'surplus budget'.

✓ **Deficit Budget**

If estimated government receipts are less than the estimated Government expenditure, then the budget is termed a 'deficit budget'.

(E) Budgetary Deficit

A budgetary deficit is defined as the excess of total estimated expenditure Over total estimated revenue. When the government spends more than it collects, then it incurs a budgetary deficit. Concerning the budget of the Indian government, the budgetary deficit can be of three types.

Types of measures of Budgetary Deficit

- ✓ **Revenue Deficit**
- ✓ **Primary Deficit**
- ✓ **Fisacal Deficit**

(I)Revenue Deficit

- ✓ Revenue deficit refers to the excess of revenue expenditure over revenue receipt during the given fiscal year.
- ✓ $\text{Revenue Deficit} = \text{Revenue Expenditure} - \text{Revenue Receipts}$
- ✓ A revenue deficit signifies that the government's revenue is insufficient to meet the expenditure on the normal functioning of the government departments and provisions for various services.

Implications of Revenue Deficit are:

- ✓ It indicates the inability of the government to meet its regular and recurring expenditure in the proposed budget.
- ✓ It implies that government is dissaving, i.e. government is using up savings of other sectors of the economy to finance its consumption expenditure.
- ✓ It also implies that the government has to make up this deficit from capital receipts, i.e., through borrowings or disinvestment.
- ✓ Use of capital receipts for meeting the extra consumption expenditure leads to an inflationary situation in the economy.
- ✓ Higher borrowings increase the future burden in terms of loan amount and interest payments.
- ✓ A high revenue deficit gives a warning signal to the government to either curtail its expenditure or increase its revenue.

Measures to Reduce Revenue Deficit

- ✓ Reduce Expenditure Government should take serious steps to reduce its Expenditure and avoid unproductive or unnecessary Expenditures.
- ✓ Increase Revenue Government should increase its receipts from Various sources of tax and non-tax revenue.

(II) Fiscal Deficit

- ✓ Fiscal expenditure refers to the excess of total expenditure over total receipts (excluding borrowings) during the given fiscal year.
- ✓ $\text{Fiscal Deficit} = \text{Total Expenditure} - \text{Total Receipts Excluding borrowings}$
- ✓ The extent of the fiscal deficit is an indication of how Far the government is spending beyond its means.
- ✓ Total Receipt excluding borrowings includes :
 - a) Revenue Receipts.
 - b) Capital Receipts excluding borrowing (or non-debt Creating capital receipts such as the recovery of loan or proceeds from disinvestment)

Implications of Fiscal Deficit

Debt Trap:

A fiscal deficit indicates the total borrowing requirements of the government.

Borrowings not only involve repayment of the principal amount but also require payment of interest.

- ✓ Interest payments increase revenue expenditure, which leads to a revenue deficit
- ✓ It creates a vicious circle of fiscal deficit and revenue deficit, wherein the government takes More loans to repay the earlier loans.
- ✓ As a result, the country is caught in a debt trap.

Inflation:

- ✓ The government mainly borrows from the reserve bank of India (RBI) to meet its fiscal deficit.
- ✓ RBI prints new currency to meet the deficit requirements.
- ✓ It increases the money supply in the economy and creates inflationary pressure.

Foreign Dependence

- ✓ The government also borrows from the rest of the world, which raises its dependence on other countries.

Hampers Future Growth

- ✓ Borrowings increase the financial burden for future generations.
- ✓ It adversely affects the future growth and development prospects of the country.

Different Ways to Calculate the Fiscal Deficit are

- 1) $\text{Fiscal Deficit} = \text{Total Expenditure} - \text{Total Receipts excluding Borrowings}$
- 2) $\text{Fiscal Deficit} = (\text{Revenue Expenditure} + \text{Capital Expenditure}) - (\text{Revenue Receipts} + \text{Capital Receipts excluding borrowings})$
- 3) $\text{Fiscal Deficit} = (\text{Revenue Expenditure} - \text{Revenue Receipts}) + (\text{Capital Expenditure} - \text{Capital Receipts excluding borrowings})$
- 4) $\text{Fiscal Deficit} = \text{Revenue Deficit} + (\text{Capital Expenditure} - \text{Capital Receipts excluding borrowings})$

If only the total borrowing is given in the question Then the fiscal deficit is equal to the total borrowings ($\text{Fiscal Deficit} = \text{Total Borrowings}$).

Sources of Financing the Fiscal Deficit

Borrowings

- ✓ Fiscal deficit can be met by borrowings from the Internal sources (public, commercial banks etc)
- ✓ or External sources (foreign governments, international Organizations etc.).

Deficit Financing

(Printing of New Currency)

- ✓ Government may borrow from the RBI against its Securities to meet the fiscal deficit. RBI issues new Currency for this purpose. This process is known as deficit financing.
- ✓ Borrowings are considered a better source as they do not increase the money supply, Which is regarded as the main cause of inflation. On the other hand, deficit financing may Lead to inflationary trends in the economy due to more money supply.

(III) Primary Deficit

- ✓ Primary deficit refers to the difference between the fiscal deficit of the current year And interest payments on the previous borrowings.

Primary Deficit = Fiscal Deficit – Interest Payments

- ✓ The total borrowing requirement of the government includes the interest commitments on Accumulated debts. The primary deficit reflects the extent to which such interest commitments Have compelled the government to borrow in the current period.

Implications of Primary Deficit are:

- ✓ It indicates how much of the government borrowings are going to meet expenses other than the interest payments.
- ✓ The difference between fiscal deficit and primary deficit shows the number of interest payments on the borrowings made in past.
- ✓ A low or zero primary deficit indicates that interest commitments (on earlier loans) have forced the government to borrow.

QUESTIONS AND ANSWER

A. Multiple Choice Questions

Choose the correct option:

1. In the context of government budget, which of the following statements is correct?

- (a) It is a statement of expected annual receipts and expenditures of the government
- (b) It is a detail of actual receipts and expenditures of the government in a financial year
- (c) It offers a detailed description of achievements of the government during the five-year plans
- (d) It indicates BoP status of the domestic economy

2. Which of the following are the objectives of government budget?

- (a) Distribution of income and wealth (b) Economic stability
- (c) GDP growth (d) All of these

3. Which of the following is a non-tax receipt?

- (a) Gift tax (b) Sales tax
- (c) Donations (d) Excise duty

4. Progressive tax is a tax which is:

- (a) charged at a decreasing rate when income of the individual increases
- (b) charged at an increasing rate when income of the individual increases
- (c) a fixed percentage of an individual income
- (d) none of these

5. Revenue earned by the government from the property without any legal heir is called (a) donation (b) escheat

- (c) special assessment (d) both (b) and (c)

6. A tax, the burden of which can be shifted on to others, is called:

- (a) indirect tax (b) direct tax
- (c) wealth tax (d) none of these

7. Tax, the impact of which lies on the person on whom it is legally imposed, is known as:

- (a) indirect tax (b) direct tax
- (c) value added tax (d) none of these

8. Which one of the following is an indirect tax?

- (a) Wealth tax (b) Excise duty
- (c) Income tax (d) None of these

9. Which of the following is a direct tax?

- (a) Income tax
- (c) Sales tax
- (b) Excise duty
- (d) Custom duty

10. Tax that is imposed on value added at the various stages of production is known as:

- (a) corporate profit tax (b) direct personal tax
- (c) value added tax (d) none of these

11. Gift tax is a paper tax because:

- (a) it is an indirect tax (b) it is a direct tax
- (c) it does not have significant revenue yield (d) both (b) and (c)

12. Which of the following is not a non-tax receipt?

- (a) Fees (b) Fines (c) Gift tax (d) Grants and donations

13. Which of the following is a part of the revenue expenditure in the Indian Government budget?

- (a) Interest payments (b) Defence purchases
- (c) Wage bill of the government (d) All of these

14. Capital receipt is that receipt of the government which:

- (a) creates a liability (b) reduces the assets
- (c) both (a) and (b) (d) neither (a) nor (b)

15. Which of the following are capital receipts of the government?

- (a) Recovery of loans (b) Borrowings
- (c) Disinvestment (d) All of these

16. Capital expenditure is that estimated expenditure of the government by which:

- (a) assets are increased (b) liability is decreased
- (c) both (a) and (b) (d) assets and liabilities do not change

17. Deficit budget refers to that situation in which government's budget expenditure is:

- (a) less than its budget receipts (b) more than its budget receipts
- (c) equal to its budget receipts (d) none of these

18. Fiscal Deficit =

- (a) Total expenditure - Total receipts other than borrowing
- (b) Revenue expenditure - Revenue receipts
- (c) Capital expenditure - Capital receipts
- (d) Revenue expenditure + Capital expenditure - Revenue receipts

19. In which of the following ways, can deficit in budget be financed?

- (a) Borrowing from RBI (b) Borrowing from the public
- (c) Both (a) and (b) (d) Neither (a) nor (b)

20. Which of the following is/are implication/s of fiscal deficit?

- (a) Crowding-out (b) Inflationary spiral
- (c) Erosion of government credibility (d) All of these

21. A budget is a balanced one when:

- (a) Total expenditure = Total receipts
- (b) Total expenditure > Total receipts

22. Surplus budget is that budget wherein:

- (a) Estimated revenue of the government < Estimated expenditure of the government
- (b) Estimated revenue of the government > Estimated expenditure of the government
- (c) Estimated revenue of the government = Estimated expenditure of the government
- (d) none of these

23. The difference between fiscal deficit and interest payment is called:

- (a) revenue deficit (b) primary deficit
- (c) budget deficit (d) capital deficit

24. If primary deficit is 3,500 and interest payment is 500, then fiscal deficit is:

- (a) 2,900 (b) 4,000
- (c) 4,100 (d) 4,200

Answers

1. (a) 2. (d) 3. (c) 4. (b) 5. (b) 6. (a) 7. (b) 9. (a) 10. (c)
 11. (c) 12. (c) 13. (d) 14. (c) 15. (d) 16. (c) 17. (b) 18. (a) 19. (c) 20. (d)
 21. (a) 22. (b) 23. (b) 24. (b)

B. Fill in the Blanks**Choose appropriate word and fill in the blank**

1. The programmes and policies of the government as presented in the budget are known as _____ policy of the government. (fiscal/monetary)
2. On the _____ side, the budgetary policy reveals expected receipts of the government. (revenue/expenditure)
3. receipts do not create any corresponding liability for the government. (Revenue/Capital)
4. is the excess of total expenditure over total receipts, other than borrowings. (Budget deficit/Fiscal deficit)
5. Fiscal discipline refers to the state of government _____ between revenues and expenditures of the
6. Fiscal Deficit = _____ + Interest payment. (balance/equilibrium)
7. A _____ budget is that budget in which government receipts are equal to government expenditure. (Revenue deficit/Primary deficit)
8. Recovery of loan is a receipt.
9. _____ expenditure creates assets for the government

Answers

1. fiscal 2. Revenue 3. Revenue 4. Fiscal deficit 5. balance
 6. Primary deficit 7. Balanced 8. Revenue 9. capital

C. HOTS & Applications

1. Revenue deficit can be managed through borrowing or disinvestment. But fiscal deficit can be managed only through borrowing. Do you agree? State reason in support of your answer.

Ans. The statement is true. Because disinvestment is already included as an item of capital receipt in the estimation of fiscal deficit. So that, borrowing is the only window available to manage fiscal deficit. On the other hand, estimation of revenue deficit does not account for borrowing as well as disinvestment. So that, both these windows are available to manage revenue deficit.

2. A persistent recession leads to low revenue receipts of the government. Comment.

Ans. Economic recession is a situation when low AD leads to low investment and therefore, low growth rate of GDP. When growth rate of GDP falls, tax revenue of the government (through direct as well as indirect taxation) tends to suffer. Implying slowdown of revenue receipts of the government during recession.

4. A rise in fiscal deficit when the government revises salary structure of its employees leads to a rise in primary deficit as well. Comment.

Ans. Revision of salary structure enhances revenue expenditure of the government. It would mean a rise in fiscal deficit of the government. If interest payments are constant, a rise in fiscal deficit would amount to a rise in primary deficit as well ($\text{Fiscal deficit} - \text{Interest payment} = \text{Primary deficit}$).

4. Is it correct that if revenue budget balances, capital budget also balances.

Ans. No, the given statement is incorrect. Because revenue budget shows revenue receipts and revenue expenditure while capital budget shows capital receipts and capital expenditure.

5. Is government budget a statement of government receipts and expenditure over the past one year?

Ans. No, government budget is a statement of estimated receipts and expenditure of the government for the fiscal year which is to begin.

6. Budgetary deficit points to failure of the government to manage its budget. Defend or refute.

Ans. The above statement is incorrect. Budgetary deficit reflecting borrowing by the government may in fact be a part of designed strategy of the government to accelerate the pace of growth or to achieve macro stability in the economy.

7. Do you agree that revenue deficit increases when the government fails to recover its loans?

Ans. No, it is incorrect. Revenue deficit is the excess of revenue expenditure over revenue receipts. While the recovery of loans by the government is a capital receipt.

8. Briefly describe how the government budget contributes to the process of growth and stability.

Ans. The government budget contributes to growth, because a significant percentage of budgetary expenditure is committed to the growth and expansion of public sector enterprises. The government also offers subsidies to the producers to maintain high level of production of the essential goods. Stability is promoted by combating inflation through fiscal discipline and combating deflation through liberal spending by the government. Fiscal discipline aims at lowering AD during inflation. Liberal spending promotes AD during deflation.

9. Government has raised its expenditure on free services like education and health to the poor.

Explain the economic value it reflects.

Ans. Two observations can be made in this respect:

- (i) Higher expenditure on health is expected to make our workforce strong and efficient. Rise in efficiency implies a rise in productivity which leads to a rise in GDP. It is an index of economic growth.
- (ii) Higher expenditure on education is expected to boost skill formation in the country. It facilitates the use of new technology. Application of new technology would shift PPC of the economy to the right. Implying a higher level of output with the same resources.

10. Find Primary Deficit from the following data:

Ans.

Items (f in crore)

(i) Revenue deficit 8,800

(ii) Fiscal deficit 11,600

(i ii) Interest payment by the government

Primary Deficit = Fiscal deficit - Interest payment by the government

= " 11,600 crore - " 1,600 crore

= " 10,000 crore

Primary deficit =" 10,000 crore.

1,600

11. Calculate Revenue Deficit, Fiscal Deficit and Primary Deficit from the following data:

Ans.

Items in crore

(i) Revenue expenditure-22,250

(ii) Capital expenditure-28,000

(i ii) Revenue receipts -17,750

(iv) Capital receipts (net of borrowing)-20,000

(v) Interest payments-5000

(vi) Borrowings -12,500

Revenue Deficit = Revenue expenditure - Revenue receipts

= 22,250 crore -17,750 crore

= 4,500 crore

Fiscal Deficit = Revenue expenditure + Capital expenditure - Revenue receipts - Capital receipts (net of borrowing)

= Borrowings

= , 12,500 crore

Primary Deficit = Fiscal deficit - Interest payments

= , 12,500 crore - , 5,000 crore

= , 7,500 crore

Revenue deficit = 4,500 crore.

Fiscal deficit =12,500 crore.

Primary deficit = 7,500 crore.

D. Analysis & Evaluation**1. How can the government impact allocation of resources through its budgetary policy?**

Ans. Following observations highlight how the government can impact a location of resources through its budgetary policy:

(i) The government can offer subsidies on such goods (like coarse cloth) the production of which is essential for poorer sections of the society. So that, the resources are shifted from the production of 'goods for the rich' to the production of 'goods for the poor'.

(ii) The government can grant 'tax holiday' (exemption from tax payments) to induce investment in the production of essential goods like 'life saving drugs'. So that the resources are shifted from the production of non-essential drugs to the life-saving drugs.

(iii) The government can impact allocation of resources by shifting its own investments from inefficient to efficient units of production. Also, allocation of resources would be impacted when the government increases investment on the production of public goods.

(iv) High taxation can be imposed on such goods (like cigarettes and liquor), the production of which is harmful to the society. Accordingly, the resources would shift to the production of socially useful production activities.

(v) The government can make larger budgetary allocations for its 'Support Price Policy' in favour of food crops. This would shift resources from non-food crops to food crops. This would make the country self-sufficient in food grain production.

2. Do you approve of disinvestment as an appropriate policy of financing budgetary deficit?

Ans. Disinvestment occurs when the government chooses to sell its stake in public sector or joint sector enterprises. This leads to 'privatization'. Presently, this seems to be the only effective remedy available with the government to finance the deficit. However, the government should be careful about two points:

- (i) It should unload shares of only inefficient enterprises. Otherwise, it would not only be lowering its asset holding, but also closing a regular source of income, and
- (ii) Money received through disinvestment should not be used for purpose of political popularity

(to garner votes). Instead, it should be used as productive investment.

3. Subsidy on diesel oil is a wasteful expenditure by the government. Write one point in support of this observation and one against it.

Ans. It is a wasteful expenditure: Because the benefit of subsidy (on diesel oil) is unduly reaped by a richer section of the society who get cheaper oil to run their luxury cars. It is not a wasteful expenditure. Because, farmers need to be given diesel at the low price. So that, the cost of farming does not rise and farming remains a profitable occupation.

4. Do you agree with the view that demonetisation of 500- and 1,000-rupee notes would help the government in lowering its fiscal deficit?

Ans. It is true that demonetization would help the government to lower its fiscal deficit. Because of demonetization, shadow economy (black money economy) will shrink. Unaccounted output would now be accounted as a part of GDP. This would increase revenue receipts of the government by way of direct and indirect taxation. Accordingly, fiscal deficit must reduce.

ASSERTION AND REASONING

Alternatives:

- (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A)
- (b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A)
- (c) Assertion (A) is true but Reason (R) is false.
- (d) Assertion (A) is false but Reason (R) is true.

Q1. ASSERTION (A): GST is an indirect tax.

REASON (R): All indirect taxes are imposed on the production and sale of goods and services

Ans: (b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A)

Q2. ASSERTION (A): Interest paid on National Debt is a revenue expenditure.

REASON (R): Revenue expenditure refer to those expenditure which neither create any liability nor causes any reduction in the assets of the government.

Ans: (c) Assertion (A) is true but Reason (R) is false.

Q3/ASSERTION (A): Capital receipts of the government leads to decrease in assets or increase in liabilities.

REASON (R): Tax and non-tax receipts are the two sources of capital receipts.

Ans: (c) Assertion (A) is true but Reason (R) is false.

Q4. ASSERTION (A): Fiscal deficit is greater than budgetary deficit.

REASON (R): Fiscal deficit is the borrowing from the RBI plus other liabilities of the Government to meets its expenditure.

Ans: (d) Assertion (A) is false but Reason (R) is true.

Q5. ASSERTION (A): Tax payments to the government do not provide any direct benefit to the tax payer.

REASON (R): Government spends tax receipts for common benefit of the society.

Ans: (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A)

CASE STUDIES

Q.1 There is a constitutional requirement in India (Article 112) to present before the Parliament a Statement of estimated receipts and expenditures of the government in respect of every financial Year which runs from 1 April to 31 March. This 'Annual Financial Statement' constitutes the Main budget document of the government. Although the budget document relates to the receipts and expenditure of the government for a Particular financial year, the impact of it will be there in subsequent years. There is a need therefore to have two accounts- those that relate to the current financial year only are included in the revenue account (also called revenue budget) and those that concern the assets and liabilities of the government into the capital account (also called capital budget). In order to understand the Accounts, it is important to first understand the objectives of the government budget.

Q1. Revenue budget do not affect:

A) Assets and liabilities B) Only assets C) Both A and B D) None of these

Ans. A

Q2. Capital expenditure:

A) Either create assets or reduce liabilities B) Either create liabilities or reduce assets
C) Both A and B D) None of these

Ans. A

Q3. Which of the following is indirect tax?

A) Income tax B) Corporate tax C) Wealth tax D) None of these

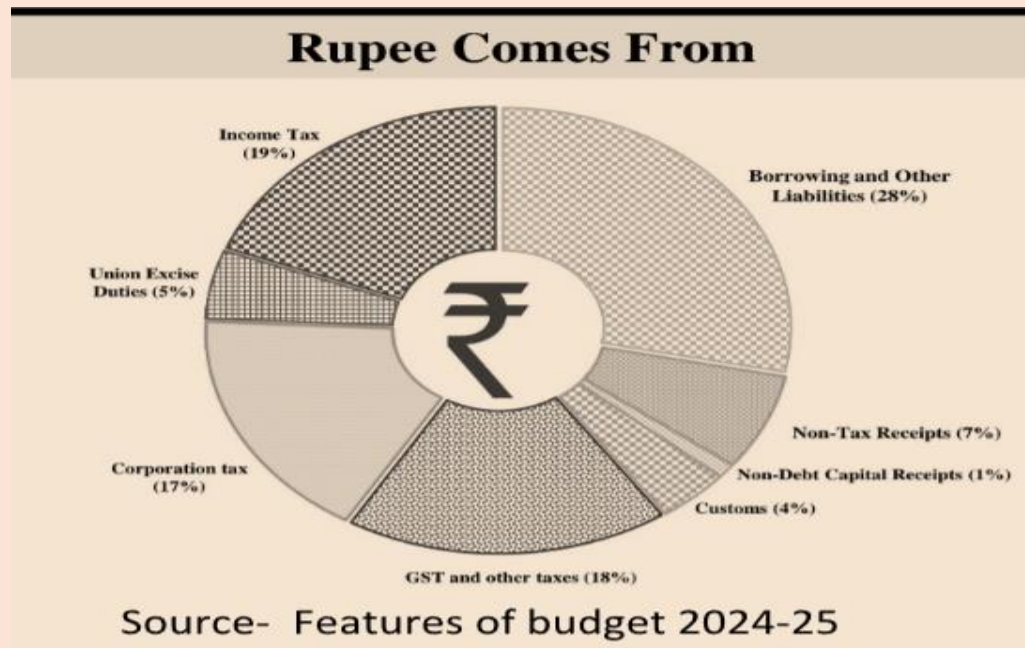
Ans. D

Q4. Who present the Union Budget in Parliament?

A) Defence minister B) Finance minister
C) Home minister D) Commerce and textile minister

Ans. B

Q.2 From the following information given in the diagram, categorize the items into revenue receipts and capital receipts, stating valid reasons.



UNIT 5: BALANCE OF PAYMENTS

Meaning: Balance of payments (BOP) is an accounting statement that provides a systematic record of all economic transactions, between the residents of a country and the rest of the world in the given period of time. The BOP accounting must be balanced always, i.e., total amount of debits must be equal to total amount of credits. If BOP account is still not balanced then accommodating transactions are undertaken to balance the BOP account.

COMPONENTS OF BALANCE OF PAYMENTS:

1. Current Account
2. Capital Account

COMPONENTS OF CURRENT ACCOUNT:

Current Account of BOP records all those transactions between the residents of a country and the residents of the rest of the world which do not cause a change in the assets or liabilities of the residents of the country or its government. It includes:

1. Export and Import of Goods (Tangible)
2. Export and import of Services (Intangible)
3. Unilateral Transfers
4. Incomes (from Investment and COE)

BALANCE ON CURRENT ACCOUNT:

1. In current account, receipts are entered as credit items as they represent inflow of foreign exchange
2. Payments are entered as debit items as they represent outflow of foreign exchange
3. The net value of credit and debit balance is the balance on current account.

CURRENT ACCOUNT SURPLUS:

When credit items are more than debit items. It implies net inflow of foreign exchange.

CURRENT ACCOUNT DEFICIT:

When debit items are more than credit items. It implies net out flow of foreign exchange.

COMPONENTS OF CAPITAL ACCOUNT:

Capital account records all those transactions between the residents of a country and the rest of the world, which cause a change in the liabilities or assets of the country or its government.

Transactions in capital account are undertaken:

- a) To adjust surplus of current account by making investments and strengthening foreign exchange reserves
- b) To finance deficit in current account through borrowings and reduction in foreign exchange reserves.

COMPONENTS OF CAPITAL ACCOUNT:

1. Borrowing and Lending:
 - A. Private transactions
 - B. Official transaction
2. Investments:
 - A. Foreign Direct Investment
 - B. Portfolio Investment
3. Changes in foreign exchange reserves (Official reserve transactions)

BALANCE OF PAYMENTS – SURPLUS AND DEFICIT:

Disequilibrium in BOP is a state of either deficit or surplus in BOP. There are two types of disequilibrium.

SURPLUS BOP: When the payments (debit) of the country are less than the receipts (credit), the BOP is said to be surplus BOP. It happens when inflow of foreign exchange is more than its outflow.

DEFICIT BOP: When the payments (debit) of the country are more than its receipts (credit) the BOP is said to be deficit BOP. It happens when outflow of foreign exchange is more than its inflow.

AUTONOMOUS AND ACCOMMODATING TRANSACTIONS:

Autonomous transactions with the rest of the world takes place due to some economic motive for maximizing profits. These are independent of the country's BOP situation. It takes place both in current and capital account. These items are also known as "below the line items."

Accommodating transactions with the rest of the world takes place to adjust or deficit in autonomous transactions. For example, if there is a current account deficit in the BOP, then it is financed by borrowings from the rest of the world. These items are also known as "below the line items."

FOREIGN EXCHANGE

All currencies other than domestic currency of a given country are called foreign exchange.

Foreign Exchange Rate: The rate at which currency of one country can be exchanged for currency of another country is called the rate of foreign exchange. It is the price of a country's currency in terms of other country's currency.

TYPES OF EXCHANGE RATE:

Fixed Exchange Rate: It is the rate which is officially fixed by the government for conversion of domestic currency into foreign currency.

Flexible Exchange Rate: It is the rate which is determined by the market forces of demand and supply.

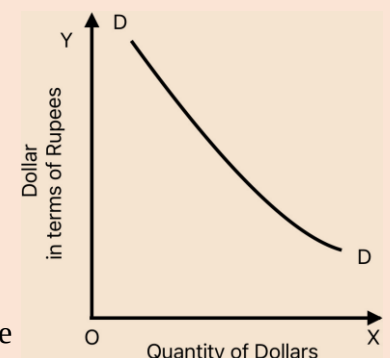
Managed Floating Exchange Rate: It is the rate which is determined by the market forces and influenced or managed by the central bank of the country.

SOURCES OF DEMAND FOR FOREIGN EXCHANGE:

Foreign exchange is demanded for the following reasons:

- Import of goods and services
- Tourism
- Repayment of interest and loans
- Extension of loans to foreigners
- Investments.

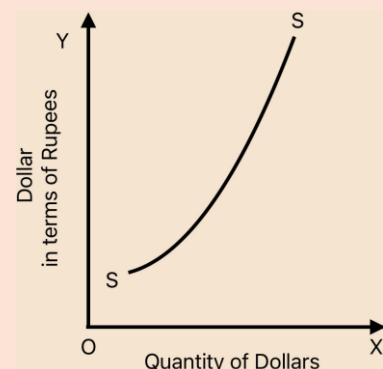
Other things being equal, there is an inverse relationship between price and the demand for foreign exchange, i.e., at a higher price, less of the foreign exchange is demanded vice versa. As a result, the demand curve for foreign exchange is negatively sloped.



SOURCES OF SUPPLY OF FOREIGN EXCHANGE:

The major sources supply of foreign exchange is:

- Export of goods and services
- Foreign tourists
- Remittances by Indians working abroad.
- Foreign direct investment
- Portfolio investment by foreign investors.
- Deposit by Non-Resident Indians.



Other things being equal, there is positive relationship between price of foreign exchange and its supply, i.e., if the price of foreign exchange goes up, the quantity supplied of foreign exchange will also rise. As a result, the supply curve for foreign exchange is positively sloped.

TYPES OF FOREIGN EXCHANGE RATE SYSTEM:

- 1) **Fixed Exchange Rate System:** Under this system, the rate of exchange is fixed by the government and the government is responsible to stabilize the exchange rate. In this system, each country maintains value of its currency fixed in terms of gold, silver or another country's currency etc.

Merits:

- a) Ensures stability in exchange rate
- b) Prevents speculation in foreign exchange market.

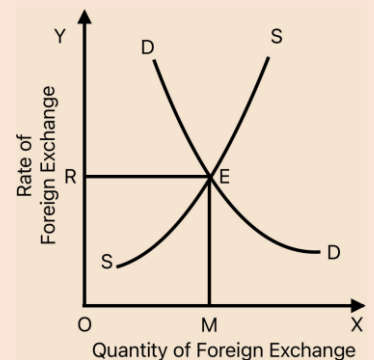
Demerits:

- a) Possibility of under or over valuation of the currency
- b) Government must maintain gold reserves.

- 2) **Flexible Exchange Rate System:** It refers to a system in which the rate of exchange is determined by the market forces of demand and supply. There is no government intervention in the foreign exchange market. It is flexible because it tends to change with changes in the market forces of demand and supply. It is further clarified with the help of a diagram.

Merits:

- a) It solves the problem of overvaluation or undervaluation of currencies.
- b) There is no requirement of government to hold 100 percent gold reserves.
- c) reserves.
- d) It encourages venture capital.



Demerits:

- a) There is no stability. Flexible exchange rate keeps fluctuating according to demand and supply.
- b) This discourages international trade and coordination of macro policies becomes inconvenient.

3. Managed Floating Rate System: It refers to a system in which foreign exchange rate is determined by the market forces of demand and supply and Central bank stabilizes the exchange rate. It is a hybrid system between fixed and flexible exchange rate systems. The central bank sets rules and regulations to influence the exchange rate. The central bank intervenes as a bulk buyer or seller of foreign exchange to control fluctuations in the exchange market.

Merits:

- a) Balanced monetary policy
- b) Flexibility
- c) Trade balance adjustment

Demerits:

- a) Uncertainty for businesses and investors
- b) Limited control of central bank
- c) Lack of co-ordination among countries

APPRECIATION OF DOMESTIC CURRENCY: Appreciation of currency refers to increase in the value of home currency in terms of foreign currency. It occurs when there is a decrease in the domestic currency price to buy a unit of foreign currency e.g. if one dollar is exchanged for Rs 70 and now the exchange rate falls to Rs 60 for one dollar. This is appreciation of domestic currency. It is related to flexible exchange rate system where exchange rate is determined by the market forces of demand and supply.

It discourages exports

It encourages imports.

DEPRECIATION OF DOMESTIC CURRENCY: It refers to decrease in the value of domestic currency in terms of foreign currency. It occurs when there is an increase in the domestic currency price to buy a unit of a foreign currency e.g. if price of one dollar rises from Rs 70 to Rs 80. This is currency depreciation for domestic currency. It is related flexible exchange rate system where exchange rate is determined by the market forces of demand and supply.

It encourages exports

It discourages imports.

REVALUATION OF DOMESTIC CURRENCY: This refers to rise in the value of domestic currency against a foreign currency in a fixed exchange rate system where exchange rate is fixed by the government.

DEVALUATION OF DOMESTIC CURRENCY: This refers to decrease in the value of domestic currency against a foreign currency in a fixed exchange rate system where exchange rate is fixed by the government.

QUESTION ANSWERS

MCQ -1 Mark

1) Foreign exchange transactions dependent on other foreign exchange transactions are called:

- a) Current account transaction b) Capital account transactions
c) Autonomous transactions d) Accommodating transactions

Ans: d) Accommodating transactions

2) Exports of COVID- 19 vaccines manufactured in India has led to_____.

- a) Inflow of Indian currency
b) Outflow of foreign currency
c) Inflow of foreign currency and employment generation
d) Outflow of foreign currency and employment generation

Ans: c) Inflow of foreign currency and employment generation

3) In a hypothetical economy, the following data is given:

	Item	Amount (Rs in crores)
i)	Merchandise exports	100
ii)	Merchandise imports	90
iii)	Tourism	70
iv)	Net remittances from abroad	(-) 20

The value of Balance on Current Account would be Rs. _____

- a) 100 b) 70 c) 80 d) 60

Ans: d) 60 crores

4) If the value of export of merchandise is Rs.1500 Crore and imports of goods are 20 % more than exports, the value of imports and trade deficit will be Rs. _____Crore and Rs. _____ Crores respectively.

- a) 1800, 3300 b) 1800,300 c) 1200,300 d) 1200, 3300

Ans: b) 1800,300

5) If Balance of Trade of a nation shows deficit of Rs.300 Crores, the value of exports is Rs.400 Crores and transfer payments are Rs.50 Crores. Rs._____ crores will be the value of imports.

- a) 1700 b) 1500 c) 300 d) 700

Ans:700

ASSERTION AND REASON

1) Read the following statements –Assertion (A) and reason (R). Choose one of the correct alternatives given below:

Assertion (A): In both the accounting and the economic sense, Balance of Payment account is always in balance.

Reason (R): In accounting sense, Balance of Payment account is prepared on the basis of double entry system.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and reason (R) is the correct explanation of Assertion (A)
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but reason (R) is false.
- d) Assertion (A) is false but reason (R) is true.

Ans: (d) Assertion (A) is false and Reason (R) is true.

2) Read the following statements –Assertion (A) and reason (R). Choose one of the correct alternatives given below:

Assertion (A): Imports of crude oil by India will have a favorable impact on Balance of Payment of India.

Reason (R): Imports of goods are recorded on the debit side of current account as it leads to outflow of foreign exchange.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and reason (R) is the correct explanation of Assertion (A)
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).

- c) Assertion (A) is true but reason (R) is false.
- d) Assertion(A) is false but reason (R) is true.

Ans: (d) Assertion (A) is false and Reason (R) is true.

3) Read the following statements –Assertion (A) and reason (R). Choose one of the correct alternatives given below:

Assertion (A): Economic transaction of Indians investing in assets (foreign direct investments or portfolio investments) abroad is recorded under debit side of capital account in balance of payments account.

Reason (R): Balance of payments is the difference between inflow of foreign exchange and outflow of foreign exchange on account of economic transactions. An outflow of foreign exchange is entered as a negative (debit) item in BOP accounts and inflow as positive (credit) item in BOP account.

Alternatives

- a) Both (A) and Reason (R) are true and reason (R) is the correct explanation of Assertion (A)
- b) Both Assertion (A) and Reason (R) are true and Reason (R) are true and reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but reason (R) is false.
- d) Assertion(A) is false but reason (R) is true.

Ans: (a) Both Assertion (A) and Reason (R) are the true and Reason (R) is the correct explanation of Assertion (A)

STATEMENT BASED QUESTIONS

1) Read the following statements carefully

1. Statement 1: Export of financial services by India will be recorded on credit side of current account.

Statement 2: Foreign Direct Investments in India will be recorded on credit side of capital account.

In the light of the given statements, Choose the correct alternative:

- a) Statement 1 is true and statement 2 is false
- b) Statement 1 is false and statement 2 is true
- c) Both the statements 1 and 2 are true
- d) Both statements 1 and 2 are false

Ans: (c) Both the statements 1 and 2 are true.

2) Read the following statements carefully

Statement 1: Transfer payments are the receipts which the residence of a country gets for “free”.

Statement 2: Transfer payments could be given by the government or by foreign citizens.

In the light of the given statements, Choose the correct alternative:

- a) Statement 1 is true and statement 2 is false
- b) Statement 1 is false and statement 2 is true.
- c) Both the statements 1 and 2 are true
- d) Both the statements 1 and 2 are false.

Ans: (c) Both the statement 1 and 2 are true.

3). Read the following statements carefully

Statement 1: Balance of Payment is an accounting statement which records all the economic transactions that take place between the residents of a country during a given period of time.

Statement 2: Current account of Balance of Payment records all the transactions that relate to assets or liabilities.

In the light of the given statements, Choose the correct alternative:

- a) Statement 1 is true and statement 2 is false
 - b) Statement 1 is false and statement 2 is true.
 - c) Both the statements 1 and 2 are true
 - d) Both the statements 1 and 2 are false
- Ans: (1) Statement 1 is true and statement 2 is false

SHORT ANSWER TYPE QUESTIONS (3/4 Marks)

1) Distinguish between current account and capital account of balance of payment account. Is import of machinery recorded in current account or capital account?

Ans: Current account transactions of balance of payment includes

- a) Imports
- b) Exports
- c) Unilateral Transactions. (These transactions may not change the asset and liability)

Capital Account Transactions of Balance of Payment Includes

- a) Private Transactions
- b) Official Transactions
- c) Direct Investment
- d) Portfolio Investment

(These transactions may change assets and liabilities.)

Import of machinery is recorded in current account BOP.

2) In the context of BOP account, state whether the following statements are true or false.

Give reasons for your answer.

- (i) Profit received from investments abroad is recorded in capital account.
- (ii) Import of machines is recorded in current account.

Ans: i) False, it is recorded in current account as it neither affects foreign exchange assets nor its liabilities.

ii) True, all imports and exports of goods are recorded in trade account which is a part of current account because it is simply import and export of a good

3) "Current account deficit may be financed with the help capital account surplus". Do you agree with the given statement? Give valid reasons in support of your answer.

Ans: I agree with the given statement. Since, in accounting sense; current account + Capital account = 0. If an economy is facing the situation of current account deficit (CAD), the same must be financed through surplus in capital account. CAD may be set off through net capital inflows. Transactions like selling off assets or borrowings from abroad may be instrumental in balancing CAD in Balance of Payments account.

4) Distinguish between a current account deficit and trade deficit.

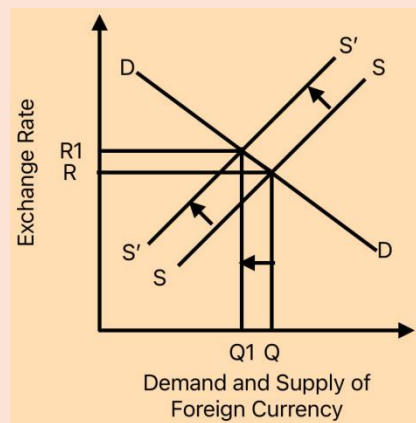
CURRENT ACCOUNT DEFICIT	TRADE DEFICIT
1. Current account exhibits deficit when payments for imports of goods and services, unilateral transfers and income paid for investment and work are more than receipts from exports of goods and services, unilateral transfers and income from investment and work. 2. When outflow of foreign exchanges is more than its inflow, it implies net outflow of foreign exchange. 3. Value of debit (negative) items is more than value of credit (positive) items.	1. The difference between all visible and all exports and imports is known as a trade deficit. 2. At a point when the imports surpass the exports, it is known as a trade deficit. 3. If it imports more than it exports, it will have a trade deficit.

LONG ANSWER TYPE QUESTIONS (6 Marks)

1. Indian investors lend abroad. Answer the following questions: (a) In which sub-account and on which side of the Balance of Payments Account such lending is recorded? Give reasons. (b) Explain the impact of this lending on market exchange rate.

Ans: (a) In Capital Account and on debit side of BOP the lending of Indian investors to abroad will be recorded. Indian investors lending abroad cause an outflow of foreign exchange from the country. Thus, it is recorded as negative item in the Capital Account of BOP.

(b) Lending to abroad by Indian investors will decrease the supply of foreign currency. This would shift the supply curve towards left and the new equilibrium is established at point E' where the exchange rate rises from OR to OR1.



2. a) In which sub-account and on which side of balance of payments account will foreign investments in India be recorded? Give reasons.

(b) What will be the effect of foreign investments of India on exchange rate? Explain.

Ans: (a) Foreign investments in India will be recorded in the Capital Account of Balance of Payments Account. It is recorded on the credit side of Balance of Payments Account as it leads to inflow of foreign exchange

(b) Foreign investment in India will lead to increase in the supply of foreign exchange. If the supply of foreign exchange increases in the foreign exchange market it will lead to decrease in exchange rate.

3. Indian investors borrow from abroad. Answer the following: (a) In which sub-account and on which side of the Balance of Payments Account will this borrowing be recorded? Give reason. (b) Explain its impact of this borrowing on exchange rate.

Ans: (a) In Capital Account of BOP because these give rise to foreign exchange liabilities, and on credit side of BOP as they bring foreign exchange to the country.

(b) Borrowing from abroad by Indian investors will increase the supply of foreign currency. This would increase the supply of foreign exchange and hence exchange rate decline

FOREIGN EXCHANGE RATE

MCQs (1 Mark)

Depreciation of domestic currency occurs when value of domestic currency __inrelation to the value of foreign currency.

- a) Increases b) decreases
c) remains constant d) all of these

Ans: b) decreases

If \$ 1 = Rs.80.50, then \$ ____ (approximately) would be needed to exchange Rs.2, 00,000. (Fill in the blank by choosing the correct alternative)

- a) 2,484 b) 2,844
c) 2,448 d) 2,882

Ans: a) 2,484

Due to fall in the value of Indian currency in the foreign exchange market, the Reserve Bank of India decides to buy Indian currency. This type of action by the Central Bank is possible under _____ exchange rate system.

- a) Flexible b) Managed floating
c) Fixed floating d) Fixed Ans: b) Managed floating

ASSERTION AND REASON

Read the following statements –Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): Other things remaining unchanged, when in a country the price of domestic currency rises, national income in the country is likely to rise.

Reason (R): Depreciation of domestic currency refers to decrease in the value of domestic currency in terms of foreign currency. Depreciation of domestic currency encourages exports and discourages imports.

Alternatives.

Both (A) and Reason (R) are true and reason (R) is the correct explanation of Assertion (A)

Both Assertion (A) and Reason (R) are true and Reason (R) is not correct explanation of Assertion (A).

Assertion (A) is true but reason (R) is false.

Assertion (A) is false but reason (R) is true.

Ans: (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).

Read the following statements –Assertion (A) and reason (R). Choose one of the correct alternatives given below:

Assertion (A): Foreign exchange rate supports the comparison of International cost and prices.

Reason (R): Foreign exchange rate is the price of one currency in terms of other commodities.

Alternatives:

Both (A) and Reason (R) are true and reason (R) is the correct explanation of Assertion (A)

Both Assertion(A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
Assertion (A) is true but reason (R) is false.

Assertion(A) is false but reason (R) is true. Ans: (c) Assertion (A) is true and Reason (R) is false.

Read the following statements –Assertion (A) and reason (R). Choose one of the correct alternative given below

Assertion (A): The Central Bank intervenes as a bulk buyer or seller of foreign exchange to control fluctuations in the exchange rate.

Reason (R): When foreign exchange rate is high, the Central Bank sells foreign exchange from its foreign- exchange reserves to bring it down.

Alternatives.

Both (A) and Reason (R) are true and reason (R) is the correct explanation of Assertion (A)

Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A)

Assertion (A) is true but reason (R) is false.

Assertion(A) is false but reason (R) is true.

Ans: (a) Both Assertion (A) and Reason (R) is the true and Reason (R) is the correct explanation of Assertion (A).

STATEMENT BASED QUESTIONS

Read the following statements carefully

Statement 1: The rate at which current transactions in foreign exchange take place is called spot rate.

Statement 2: Forward rate is the rate at which forward transactions take place in foreign Exchange market.

In the light of the given statements, Choose the correct alternative:

- a) Statement 1 is true and statement 2 is false
- b) Statement 1 is false and statement 2 is true.
- c) Both the statement 1 and 2 are true
- d) Both statements 1 and 2 are false.

Ans: c) Both the statements 1 and 2 are true.

Read the following statements carefully

Statement 1: Other things being equal, there is positive relation between the price of foreign exchange and its demand.

Statement 2: Other things being equal, there is negative relation between the price of foreign exchange and its supply.

In the light of the given statements, Choose the correct alternative:

Statement 1 is true and statement 2 is false

Statement 1 is false and statement 2 is false.

Both the statement 1 and 2 are true

Both statements 1 and 2 are false.

Ans: d) Both the statements 1 and 2 are false

Read the following statements carefully

Statement 1: Devaluation and Depreciation of currency are one and the same thing.

Statement 2: Depreciation of currency has same effect on exports as devaluation of currency. In the light of the given statements, Choose the correct alternative:

Statement 1 is true and statement 2 is false

Statement 1 is false and statement 2 is true

Both the statement 1 and 2 are true

Both statements 1 and 2 are false.

Ans: b) Statement 1 is true and 2 is false.

SHORT ANSWER TYPE QUESTIONS (3/4 Marks)

When price of a foreign currency falls, the demand for that foreign currency rises. Explain

Ans: i) With a fall in price of foreign exchange the exchange value of domestic currency increases and that of foreign currency falls and foreign goods become cheaper in relation to domestic goods. The rising domestic demand of foreign goods implies higher demand for foreign exchange.
ii) When Price of the foreign currency reduces tourists from home country find it cheaper to visit abroad. Accordingly demand for foreign currency rises.

[OR]

When price of a foreign currency falls, the supply of that foreign currency also falls. Explain Why?

Ans: There is a direct relation between foreign exchange rate and supply of foreign exchange. Higher the exchange rate higher the supply of foreign exchange and lower the exchange rate lower the supply of foreign exchange. Suppose the price of US \$ in India falls from Rs.50 to Rs.40 it means earlier USA people could buy Rs.50 worth of good from India by giving one dollar. Now they can buy only Rs.40 worth of good from India. Indian goods become costlier for USA. Therefore, USA buys less of Indian goods this reduces the supply of dollar to India and vice versa.

Recently the Government of India has doubled the import duty on gold. What impact is it likely to have on Foreign exchange rate and how?

Ans: Increased Import duty on gold will make imports of gold costly. It will reduce demand for import of gold and consequently of foreign exchange. Supply of foreign exchange remaining unchanged price of foreign exchange is likely to change accordingly.

‘Devaluation and Depreciation of currency is one and the same thing’. Do you agree? How do they affect the exports of a country?

Ans: Devaluation is the fall in the value of domestic currency in relation to foreign currencies as planned by the government in a situation when exchange rate is not determined by the forces of demand and supply, but is fixed by the government.

Whereas, depreciation is the fall in the value of domestic currency in relation to foreign currency in a situation when exchange rate is determined by the forces of demand and supply in the international currency market.

As a general phenomenon, any depreciation or devaluation of currency may result into increase in exports of the goods and services from the country since it would increase the global competitiveness of the goods by making them cheaper.

“A country deliberately keeps the value of its currency low under the managed floating System “. Discuss briefly how it will affect imports of the country.?”

Ans: If a country deliberately keeps the value of its currency low under the managed floating system, it can have a negative effect on the imports of the country. A low-valued currency makes the country's imports costlier in foreign markets, which can decrease the demand for those imports. This is because domestic buyers can purchase less units of the country's imports for the same amount of their own currency, making the imports less attractive.

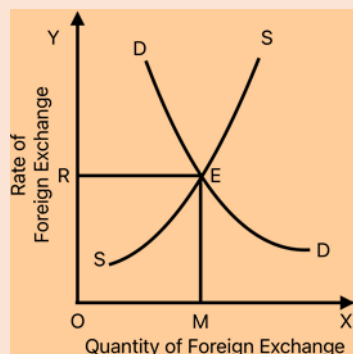
“Depreciation of the Indian currency will lead to promotion of Indian exports.”. Explain.

Ans: Depreciation of the Indian currency means that the value of the Indian rupee has decreased in relation to other currencies, making Indian goods relatively cheaper for foreign buyers. This makes Indian exports more competitive in international markets and can lead to an increase in exports.

LONG ANSWER TYPE QUESTIONS (6 Marks)

Define fixed exchange rate. How is the exchange rate determined in a flexible exchange rate system?

Ans: A fixed exchange rate is a regime imposed by a government or central bank which ties the official exchange rate of the country's currency with the currency of another country or the gold price. Under flexible exchange rate regime, the rate of exchange is determined by the forces of demand and supply. In other words, the equilibrium rate of exchange occurs where demand and supply are equal to each other. This can be illustrated with the help of the given figure:



In the figure, x-axis represents demand for and supply of foreign currency and y-axis represents the exchange rate. DD is the demand curve that is downward slopping showing an inverse relationship between the rate of exchange and demand for foreign currency and SS is the supply curve that indicates the positive relationship between the rate of foreign exchange and its supply. Point E shows equilibrium and R is the equilibrium exchange rate.

Mention the sources of demand and supply of foreign exchange.

Demand for foreign exchange:

Imports of goods and services; Needs foreign exchange

Tourism: Tourists need foreign exchange to meet their expenditure abroad.

Repayment of interest and loans: Foreign exchange is required to pay interest on loans or to repay loans.

Supply of foreign exchange:

Exports of goods and services: It increases the supply of foreign exchange.

Foreign tourists: Foreign tourists spend in foreign exchange in the country

Foreign investments: It will increase the supply of foreign exchange.

CASE-BASED STUDY

Read the following and answer the questions:

India's balance of payments position improved dramatically in 2013-14 particularly in the last three quarters. This moved in large part to measure taken by the government and the Reserve Bank of India (RBI) and to some part to the overall macro-economic slowdown that fed into the external sector.

Current account deficit (CAD) declined sharply from a record high of U.S. dollar 88.2 billion (4.7% of GDP) in 2012-13 to U.S. dollars 32.4 billion (1.7% of GDP) in 2013-14. After staying at perilously unsustainable levels of well over 4.0 percentage of GDP in 2011-12 and 2012-13, the improvement in BOP position is a welcome relief, and there is need to sustain the position going forward. This is because even as CAD came down, net capital flows moderated sharply from U.S. dollars 92.0 billion in 2012-13 to U.S. dollar 47.9 billion in 2013-14.

The RBI under the non-resident Indian (NRI) scheme / overseas borrowings of banks alone yielded U.S. dollar 3 4.0 billion. This led to some increase in the level of external debt, but it has remained at the manageable levels. the large depreciation of the rupee during the course of the year, note with standing sizable accretion to reserve in 2013 – 14, could partly be attributed to frictional forces and partly to the role of expectations in the forex market. the rupiah has stabilized the recently, reflecting an overall sense of confidence in the forex market as in the other financial markets of a change for better economic

prospects there is a need to nurture and build upon this optimism through creation of an enabling environment for investment inflows so as to sustain the external position in an as yet uncertain global milieu. ----- The Hindu, archives

1 External debt is recorded at:

- a) credit, capital account
- b) debit, capital account
- c) credit, current account
- d) debit, current account

2 Money sent by NRI to their families in India included in:

- a) credit, capital account
- b) debit, capital account
- c) credit, current account
- d) debit, current account

3 Which of the following is not a component of BOP?

- a) current account
- b) revenue account
- c) capital account
- d) official reserves

4 Positive balance of net capital flow shows:

- a) outward flow of foreign exchange
- b) inward flow of foreign exchange
- c) decrease in the level of external debt
- d) decrease in future claims

Answers: 1.b 2. c 3. b 4. d

UNIT -6: DEVELOPMENT EXPERIENCE (1947-90) AND ECONOMIC REFORMS SINCE 1991

INDIAN ECONOMY ON THE EVE OF INDEPENDENCE.

INTRODUCTION

Before British colonization, India was known as “Sone ki Chidiya” or “The Golden Bird”. It was a reference to the wealth and economic prosperity of India before its colonization.

However, during the colonial rule (which lasted for almost two centuries before India finally won its independence on 15th August 1947), the British extracted the wealth of India as much as they could. as their economic policies were concerned with the protection and promotion of the economic interests of their home country Britain rather than with the development of India.

STATE OF INDIAN ECONOMY ON THE EVE OF INDEPENDENCE:

(1) Low level of economic development under colonial rule

A. Before the advent of British rule-

- i) Had an independent
- ii) Main source of livelihood was Agriculture
- iii) Economy was characterized by Various kinds of manufacturing activities
- iv) Well known for handicraft industries-like in the fields of
 - a) cotton (like Muslin, Daccai Muslin) and silk textiles
 - b) metal and precious stone works etc.
- v) Enjoyed world-wide market due to----
 - a) its reputation of the fine quality of material used and
 - b) high standard of craftsmanship seen in all imports from India.

i) During the British rule-

ii) Focus of economic policies - Colonial government in India followed such economic policies which were concerned with the protection and promotion of the economic interests of their home country Britain rather than with the development of India.

iii) Impact of such economic policies- Brought fundamental change in the structure of the economy

- a) Transformed India into supplier of raw materials
- b) Transformed India into consumer of finished products from Britain.

B. Estimation of national Income and per capita income :

The colonial govt. never made any sincere attempt to estimate India's national and per capita income. But some individual attempts were made.

Some of the notable economists who were engaged in estimation of national Income and per capita income are

- 1). Dadabhai Naoroji 2). William Digby 3). Findlay Shirras 4). VKRV Rao 5). RC Desai
- The estimates given by Dr. V.K.R.V. Rao suggested that growth rate of GDP was about 2% per annum while the growth of per capita output was just 1/2 (0.5) percent per annum.

(2) Agricultural sector - Experienced stagnation

- i) Land tenure system- Exploitative zamindari system- landowners extracted high rents from peasants.
- ii) Forced commercialization of Agriculture
- iii) Lack of Irrigational Facilities
- iv) Insignificant use of fertilizers,
- v) Lack of investment,
- vi) Use of out-dated modes of production
- vii) Frequent famines and other natural calamities etc.
- viii) Partition of the country.

(3) Industrial sector - No sound industrial base

- i) Adoption of the policy of Systematically De-industrializing India
- ii) Decline of Indian handicraft industry.
- iii) Lack of modern industries
- iv) Lack of Capital good industries
- v) Low contribution to GDP
- vi) Limited operation of public sector

(4) Foreign trade –Drain of India’s wealth

- i) Exporter of raw materials (primary products) and importer of finished consumer goods.
- ii) Monopoly control of Britain over India’s foreign trade.
- iii) Opening of Suez Canal in 1869 further intensified the British control over India’s foreign trade.
- iv) Generation of large export surplus and drain of India’s wealth.

(5) Demographic condition -Worsening Profile

First official census of British India-1881- revealed unevenness in India’s population growth. Year 1921 is known as the year of great divide.

- i) High death and Birth rate-40 and 48 per thousand respectively.
- ii) High infant mortality rate-218 per thousand.
- iii) Illiteracy-84% illiterate. Female Literacy level was about 7%.
- iv) Low life expectancy- less than 32 years
- v) Low standard of living and widespread poverty- People used to spend 80% to 90% of their income on basic needs.
- vi) Lack of public health facilities

(6). Occupational structure: More dependency on agriculture and growing regional variation

- i) More dependency on primary sector
 - a) Largest share of work force which was 70-75% was engaged in agriculture.
 - b) 10% in manufacturing while
 - c) 15-20% workforce were engaged in service sector.
- ii) Regional variation in occupational structure was also seen
 - a) Parts of the then Madras Presidency Bombay and Bengal witnessed a decline in the dependence of the workforce on the agricultural sector with a commensurate increase in the manufacturing and the services sectors.
 - b) However, during the same time in states such as Orissa, Rajasthan and Punjab there had been an increase in the share of workforce in agriculture

(7). Infrastructure: Motive behind Infrastructural facilities - to subserve their colonial interest.

Some efforts have been made to develop basic infra-structure like roads, railways, ports, water transport, post & telegraph by the British rulers. The main motive was not to provide basic amenities to the Indian people but to subserve their colonial interest.

SOME POSITIVE SIDE-EFFECTS OF THE BRITISH RULE IN INDIA

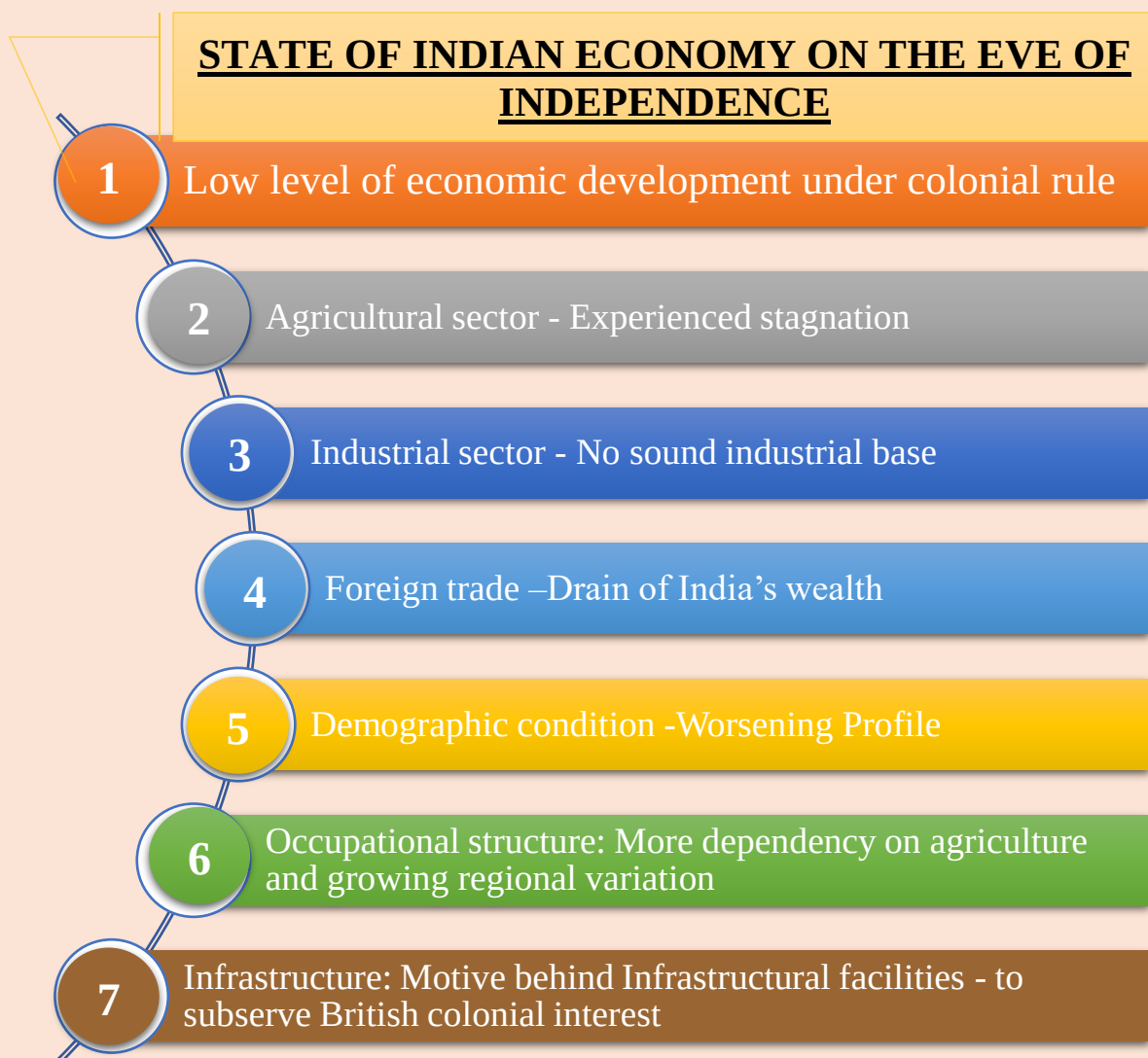
- A. Provided transport facilities, largely in terms of railway.
- B. Development of ports.
- C. Provision of post and telegraph services.
- D. British Govt. left a base of a strong and efficient administrative set up.
- E. Evolution of banking and monetary system.

CONCLUSION

The social and economic challenges before the country were quite enormous at the time of independence.

- i) The agricultural sector was already saddled with surplus labour and extremely low productivity.
- ii) The industrial sector was crying for modernisation, diversification, capacity building and increased public investment.
- iii) Foreign trade was oriented to feed the Industrial Revolution in Britain.
- iv) Infrastructure facilities, including the famed railway network, needed upgradation, expansion and public orientation.
- v) Prevalence of rampant poverty and unemployment required welfare orientation of public economic policy.

MIND- MAPPING



QUESTION ANSWERS

MCQs (1 mark each)

1. The main causes of India's agricultural stagnation during the colonial period are

- i) Exploitative zamindari system
- ii) Lack of Irrigational Facilities
- iii) Significant use of fertilizers
- iv) Lack of investment

Choose the correct option:

- a) Only (i) is true
- b) Both (i) and (ii) are true
- c) (i), (ii) and (iii) are true
- d) All are true

2. Which crop became less prevalent due to the focus on cash crops during British rule?

- a) Cotton
- b) Jute
- c) Tea
- d) Food grains

3. The decline of traditional industries during British rule resulted in:

- a) Increased employment in the industrial sector
- b) Mass unemployment and poverty
- c) Growth of modern industries
- d) Improvement in the standard of living

4. Look at the image given below and answer the question by choosing the correct alternative:



The opening of the Suez Canal in 1869

*Suez Canal: Used as highway between India and Britain
Trade through the Suez Canal*

- a) Further intensified British control over India's foreign trade
- b) Reduced the cost of transportation
- c) Made access to the Indian market easier
- d) All of the above

5. Arrange the following in the chronological order. (Choose the correct alternative)

- i) The year of great divide.
- ii) Establishment of Tata Iron and Steel Industry
- iii) Introduction of railways in India by the British
- iv) Opening of Suez Canal

Alternatives:

- a) (i), (ii), (iii), (iv)
- b) (iii), (i), (ii), (iv)
- c) (iii), (iv), (ii), (i)
- d) (ii), (i), (iii), (iv)

6. Match the following economic sectors with their characteristics on the eve of independence:

Sector	Characteristic
I. Agriculture	i) Decline of traditional industries
II. Industry	ii) Low productivity and traditional methods
III. Trade	iii). High dependence on foreign trade
IV. Infrastructure	iv. Poor connectivity and limited reach

Alternatives:

	I	II	III	IV
a) (i)	(ii)	(iii)	(iv)	
b) (iii)	(i)	(ii)	(iv)	
c) (iii)	(iv)	(i)	(ii)	
d) (ii)	(i)	(iii)	(iv)	

7. Choose the correctly matched pair:

- i) Commercialization of agriculture - Increased food grain production
- ii) Introduction of railways - Enhanced British economic interests
- iii) Zamindari system - Direct collection of revenue from farmers
- iv) De-industrialization - Promotion of Indian industries

8. The export surplus during the British rule was used _____. (Choose the correct alternative)

- i) To make payments for expenses incurred by an office set up by the colonial government in Britain.
- ii) To meet expenses on war fought by the British government.
- iii) To import invisible items

Alternatives:

- a) Only (i) is true
- b) Only (ii) is true
- c) Only (iii) is true
- d) All are true

9. The first official census of British India was conducted in the year_____.

- a) 1851
- b) 1881
- c) 1951
- d) 1981

10. Read the following statements carefully:

Statement I: The commercialization of agriculture under British rule led to the production of cash crops like cotton and jute.

Statement II: This shift towards cash crops increased the production of food grains and improved food security

In the light of the given statements, choose the correct alternative from the following:

- a) Statement I is true and statement II is false.
- b) Statement I is false and statement II is true.
- c) Both statements I and II are true.
- d) Both statements I and II are false.

11. Read the following statements carefully:

Statement I: The colonial government never made any sincere attempt to estimate India's national and per capita income.

Statement II: Among the notable estimators — Dadabhai Naoroji, William Digby, Findlay Shirras, V.K.R.V. Rao, R.C. Desai — it was V.K.R.V Rao, whose estimates during the colonial period was considered very significant.

In the light of the given statements, choose the correct alternative from the following:

- a) Statement I is true and statement II is false.
- b) Statement I is false and statement II is true.
- c) Both statements I and II are true.
- d) Both statements I and II are false

12. Read the following statements carefully:

Statement I: The most important characteristic of India's foreign trade throughout the colonial period was the generation of a large export surplus.

Statement II: The export surplus during colonial period did not result in any flow of gold or silver into India.

In the light of the given statements, choose the correct alternative from the following:

- a) Statement I is true and statement II is false.
- b) Statement I is false and statement II is true.
- c) Both statements I and II are true.
- d) Both statements I and II are false.

13. Read the following statements carefully:

Statement I: The introduction of Railways enabled people to undertake long distance travel and thereby break geographical and cultural barriers.

Statement II: The introduction of Railways fostered commercialisation of Indian agriculture which adversely affected the self-sufficiency of the village economies in India.

In the light of the given statements, choose the correct alternative from the following:

- a) Statement I is true and statement II is false.
- b) Statement I is false and statement II is true.
- c) Both statements I and II are true.
- d) Both statements I and II are false

14. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): British destroyed the indigenous handicraft market in India.

Reason (R): India was made market for British manufactured products.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

15. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): The economic policies pursued by the British colonial transformed India into supplier of raw materials and consumer of finished industrial products from Britain.

Reason (R): The economic policies of the British colonial government were concerned more with the protection and promotion of the economic interests of their home country than with the development of the Indian economy.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

16. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): India could not develop a sound industrial base during the British rule.

Reason (R): British followed restrictive trade policies, which led to the rise of Indian handicraft industries.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

17. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): Agricultural productivity became low during British rule in India.

Reason (R): The productivity was low mainly due to various systems of land settlement introduced by the colonial government.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).

- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

18. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): The colonial government never made any sincere attempt to estimate India's national and per capita income.

Reason (R): Growth of aggregate real output during the first half of the twentieth century was less than two per cent.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

19. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): More than half of India's Foreign trade was restricted to Britain.

Reason (R): Britain maintained Monopoly control on India's imports and exports.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

20. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): The economic condition of farmers under British rule improved a lot.

Reason (R): Commercialization of agriculture took place under British rule.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

ANSWERS FOR MCQs

Q.NO. ANSWER

- 1) d) All are true
- 2) d) Food grains
- 3) b) Mass unemployment and poverty
- 4) d) All of the above

- 5) c) (iii), (iv), (ii), (i)
- 6) d) (ii) (i) (iii) (iv)
- 7) b) Introduction of railways - Enhanced British economic interests
- 8) d) All are true.
- 9) b) 1881
- 10) a) Statement I is true and statement II is false.
- 11) c) Both statements I and II are true.
- 12) c) Both statements I and II are true.
- 13) c) Both statements I and II are true.
- 14) a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- 15) a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- 16) c) Assertion (A) is true but Reason (R) is false.
- 17) a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- 18) a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- 19) a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- 20) d) Assertion (A) is false but Reason (R) is true.

SHORT ANSWER TYPE QUESTIONS (3/4 Marks Each)

What was the main focus of the economic policies undertaken by the British government in India? What were the impacts of these policies?

Ans: The economic policies pursued by the colonial government in India were concerned more with the protection and promotion of the economic interests of their home country than with the development of the Indian economy. Such policies brought about a fundamental change in the structure of the Indian economy — transforming the country into supplier of raw materials and consumer of finished industrial products from Britain.

“During the colonial period, a number of socio-economic indicators were in a dilapidated state.” List any three such indicators that led to the worsening of India’s demographic profile

Ans: India’s demographic indicators were in a dilapidated state during the colonial period as:

- The overall literacy level was less (below 16%).
- Life expectancy was very low (32 years).
- Alarming infant mortality rate (218/1000).

“The pre-independent India’s occupational structure experienced growing regional variation.” Justify the above statement with valid explanation.

Ans: The pre-independent India’s occupational structure experienced growing regional variation as:

- Parts of Madras Presidency, Bombay and Bengal witnessed a decline in the dependence of the workforce on the agricultural sector with a commensurate increase in the manufacturing and the services sectors.
- There had been an increase in the share of workforce in agriculture in states such as Orissa, Rajasthan and Punjab.

Indicate the volume and direction of trade at the time of independence.

Ans: India became an 8 exporter of primary products such as raw silk, cotton, wool, sugar, indigo, jute etc. and an importer of finished consumer goods like cotton, silk and woollen clothes and capital goods like light machinery produced in the factories of Britain. For all practical purposes, Britain maintained a monopoly control over India's exports and imports. As a result, more than half of India's foreign trade was restricted to Britain while the rest was allowed with a few other countries like China, Ceylon (Sri Lanka) and Persia (Iran). The opening of the Suez Canal further intensified British control over India's foreign trade.

What do you mean by export surplus? How was it generated during British period? what was its effect on Indian economy?

Ans: When exports of a country are more than its imports it is known as Export Surplus. During the British period this surplus came at a huge cost to the country's economy. Several essential commodities—food grains, clothes, kerosene etc., were scarcely available in the domestic market. this export surplus did not result in any flow of gold or silver into India. it was used to make payments for: -

- the expenses incurred by an office set up by the colonial government in Britain
- expenses on war fought by the British government
- the import of invisible items, all of which led to the drain of Indian wealth.

LONG ANSWER TYPE QUESTIONS (6 Marks each)

1. What were the main causes of India's agricultural stagnation during the colonial period?

Ans:

- i) Land Revenue System under the British Rule: The Britishers in India established the zamindari system. Under this system, the zamindars were the permanent owners of the land. They were required to pay a fixed sum to the government as land revenue and they were given full freedom to charge any revenue they wanted from the tillers. The zamindars mercilessly exploited the poor tillers, and did nothing for their upliftment.
- ii) Lack of Resources: Because the tillers had to pay huge amounts of rent, they were not left with any surplus to be able to provide for resources needed in agriculture in the form of fertilisers or providing for irrigation facilities. This further lowered the agricultural productivity.
- iii) Commercialisation of Agriculture: Instead of producing food crops, farmers were producing cash crops, which were ultimately used by British industries. This further compounded the plight of the tillers. While earlier they were growing crops to meet their family needs, now they had to purchase from the market. This led to an increase in indebtedness and they were constantly borrowing from moneylenders and landlords at very high rates of interest.

2. Give a quantitative appraisal of India's demographic profile during the colonial period.

Ans: The overall literacy level was less than 16 per cent. Out of this, the female literacy level was at a negligible low of about seven per cent. Public health facilities were either unavailable to large chunks of population or, when available, were highly inadequate. Consequently, water and air-borne diseases were rampant and took a huge toll on life. No wonder, the overall mortality rate was very high and in that, particularly, the infant mortality rate was quite alarming—about 218 per thousand in contrast to the present infant mortality rate of 33 per thousand. Life expectancy was also very low—32 years in contrast to the present 69 years.

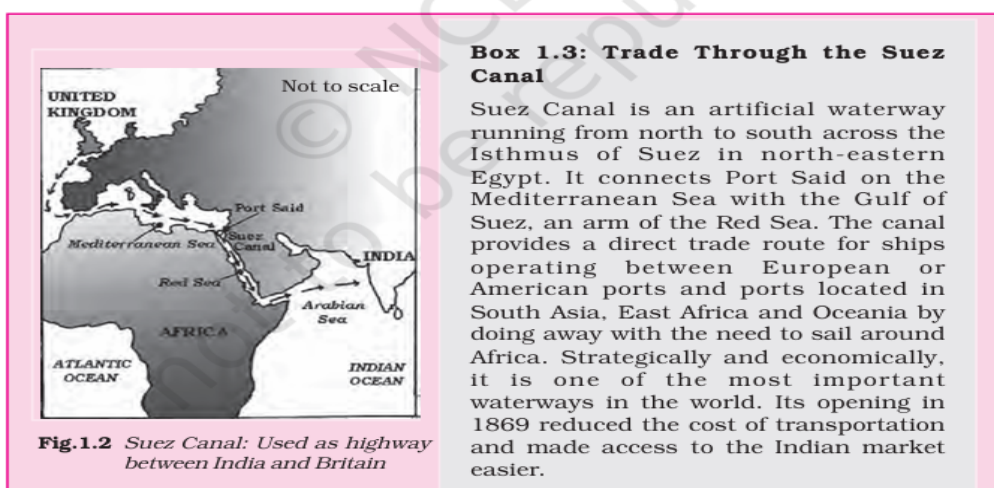
Extensive poverty prevailed in India during the colonial period which contributed to the worsening profile of India's population of the time

3. Highlight the salient features of India's pre-independence occupational structure.

Ans: During the colonial period, the occupational structure of India, i.e., distribution of working persons across different industries and sectors, showed little sign of change. The agricultural sector accounted for the largest share of workforce, which usually remained at a high of 70-75 per cent while the manufacturing and the services sectors accounted for only 10 and 15-20 per cent respectively. Another striking aspect was the growing regional variation. Parts of the then Madras Presidency (comprising areas of the present-day states of Tamil Nadu, Andhra Pradesh, Kerala and Karnataka), Bombay and Bengal witnessed a decline in the dependence of the workforce on the agricultural sector with a commensurate increase in the manufacturing and the services sectors. However, there had been an increase in the share of workforce in agriculture during the same time in states such as Orissa, Rajasthan and Punjab

CASE BASED QUESTIONS

1. Go through the following image and text and answer the questions that follow.



i) What are the two water bodies connected by Suez Canal?

Ans: Red Sea and Mediterranean Sea

ii) When did Suez Canal start working?

Ans: 1869

iii) What was strategic importance of opening of Suez Canal?

Ans: Strategically and economically, it is one of the most important waterways in the world. Its opening in 1869 reduced the cost of transportation

iv) How did opening of Suez Canal benefit British in India?

Ans: The opening of the Suez Canal made access easy and cheap to the Indian market further intensified British control over India's foreign trade

2. Read the following passage and answer the questions that follow:

The Indian economy on the eve of independence was predominantly agrarian, with a majority of the population dependent on agriculture. The sector, however, faced numerous challenges such as low productivity, fragmented landholdings, and heavy dependence on monsoon rains. The commercialization of agriculture during British rule led to an increased focus on cash crops like cotton, jute, and tea, which were exported to Britain. This shift in agricultural practices resulted in reduced production of food crops, contributing to frequent famines and widespread poverty among the peasantry.

i) What were the primary challenges faced by the agricultural sector in India on the eve of independence?

- a) High productivity and extensive irrigation.
- b) Fragmented landholdings and dependence on monsoon.
- c) Advanced farming techniques and surplus food production
- d) Large-scale mechanization and modern irrigation

Ans: b) Fragmented landholdings and dependence on monsoon.

ii) What was the impact of the commercialization of agriculture under British rule?

- a) Increased food crop production
- b) Enhanced agricultural productivity
- c) Focus on cash crops and reduced food crop production
- d) Decrease in the number of famines

Ans: c) Focus on cash crops and reduced food crop production

iii) Which cash crops were primarily cultivated for export to Britain during the British rule in India?

- a) Rice and wheat
- b) Cotton, jute, and tea
- c) Maize and barley
- d) Sugarcane and tobacco

Ans: b) Cotton, jute, and tea

iv) What was one of the major consequences of the shift in agricultural practices during British rule?

- a) Increase in food security
- b) Frequent famines and widespread poverty
- c) Industrial growth in rural areas
- d) Enhanced irrigation facilities

Ans: b) Frequent famines and widespread poverty

3. Read the following passage and answer the questions that follow:

Textile Industry in Bengal Muslin is a type of cotton textile which had its origin in Bengal, particularly, places in and around Dhaka (spelled during the pre-independence period as Dacca), now the capital city of Bangladesh. 'Daccai Muslin' had gained worldwide fame as an exquisite type of cotton textile. The finest variety of muslin was called malmal. Sometimes, foreign travelers also used to refer to it as malmal shahi or malmal khas implying that it was worn by, or fit for, the royalty.

i) What does Muslin refer to here in the passage?

Ans: Muslin is a type of cotton textile which had its origin in Bengal, particularly, places in and around Dhaka, now the capital city of Bangladesh.

ii) For whom Muslin was made for?

Ans: Muslin was made for the Royal people

iii) The traditional handicrafts industries though famous world-wide were ruined under the British rule. Do you agree? Give reasons.

Ans: British followed discriminatory tariff policy. It allowed free export of raw materials from India and free import of British final goods to India, but placed heavy duty on the export of Indian handicrafts. In this way, Indian markets were full of manufactured goods from Britain which were low priced. Indian handicrafts started losing both domestic market and export market. Ultimately, the handicraft industry declined.

INDIAN ECONOMY 1950-90

India achieved its independence on 15th August 1947.

India decided to adopt

- i) Mixed economic system in which much emphasis will be laid on public sector.
- ii) Five-year planning method

AN ECONOMIC SYSTEM, or economic order, is a system of production, resource allocation and distribution of goods and services within a society or a given geographic area.

NOTE:

There are three basic central problems of an economy.

What to produce and in what quantities.

How to produce and

For whom to produce.

TYPES OF ECONOMIC SYSTEMS: -

We can classify the economic systems into three different types

- i) Capitalist economic system: - is that type of economic system in which means of production are in the hands of private individuals and the main aim of production is to earn more and more of profit.
In capitalist economy the central problems are solved through the price mechanism.
It is also known as market economy.
- ii) Socialist economic system: - is that type of economic system in which the means of production are in the hands of government and the main aim of production is to promote social welfare.
In the socialist economy, the central problems are solved through the central planning authority or the government.
It is also known as planned economy.

- iii) Mixed economic system: - is that type of economic system in which the means of production are in the hands of government as well as private individuals and the main aim to production is to promote social welfare as well as to earn profit.

In the mixed economy, the central problems are solved through the help of government and price mechanism.

Our first Prime Minister Jawaharlal Nehru preferred the socialist model. But in a democracy like India, a pure socialist economy cannot flourish.

Capitalism was also not suited since the government had to build up an economy and look after the common man and his needs. So as a solution, our economy combined aspects of both socialism and capitalism.

Planning commission was established in 1950 and first five-year plan was implemented from 1951 onwards.

ECONOMIC PLANNING: It is the deliberate attempt made by the government to put the resources of a country in its best use to achieve certain pre-determined objectives within a specified period of time.

A PLAN spells out how the resources of a country should be put to use in order to achieve certain pre-determined objectives within a specified period of time.

A plan document specifies
General goals as well as
Specific objectives

TYPES OF PLANS IN INDIA

Short term plans /specific plans/five-year plans-These are those plans in which the objectives stated are to be achieved over a short period of time. i.e. five years.

Long term plans /perspective plans- These are those plans in which the objectives stated are to be achieved over a period of 20 years.

LONG TERM GOALS / OBJECTIVES OF PLANNING

Economic Growth – Increase in the country's capacity to produce Goods & services.

Modernization – Adoption of new technology and changes in social outlook

Self-reliance – Reducing dependence on imports.

Equity – Reduction in inequality of income and wealth

SHORT TERM GOALS / OBJECTIVES OR OBJECTIVES OF FIVE-YEAR PLANS

Short term objectives vary from plan to plan depending on current needs of the country. For example, first plan (1951-56) focused on higher agricultural production while in second plan (1956-61) shifted the focus from agriculture to Industry.

LIST OF FIVE-YEAR PLANS INDIA

FIVE YEAR PLAN	PERIOD	MAIN OBJECTIVES/ REMARKS
I	1951-1956	Agricultural development of the country.
II	1956-1961	Rapid Industrial development of the country.
III	1961-1966	To make India a self-reliant and self-generating economy
THREE ANNUAL PLANS	1966 -1969	

IV	1969-1974	Growth with stability
V	1974-1979	Removal of poverty and attainment of self-reliance
ROLLING PLAN	1978-1980	
VI	1980-1985	Increase in national income, modernization of technology
VII	1985-1990	Raising agricultural productivity, creation of more employment opportunities
TWO ANNUAL PLANS	1990-1992	
VIII	1992-1997	Human resource development
IX	1997-2002	Growth with social justice
X	2002-2007	To double the per capita income in 10 years, reduction in poverty ratio
XI	2007-2012	Faster and more inclusive growth
XII	2012-2017	Faster and more inclusive and sustainable growth

On 1 January 2015, a Cabinet resolution was passed to replace the Planning Commission with the newly formed NITI Aayog (National Institution for Transforming India).

NITI Aayog	Planning Commission
It serves as an advisory Think Tank.	It served as extra-constitutional body.
It does not possess mandate to impose policies.	Imposed policies on states and tied allocation of funds with projects it approved.
It does not have powers to allocate funds.	It had powers to allocate funds to ministries and state governments.

STRUCTURAL CHANGE

In economics, structural change is a shift or change in the basic ways an economy functions or operates. The structural change in an economy is an important feature of the economic development process.

The structural change of an economy takes place mainly along two dimensions i.e. it can take two forms.:

One is the CHANGES IN STRUCTURAL COMPOSITION i.e. change in sector-wise share in GDP and

The second one is the CHANGES IN THE OCCUPATIONAL STRUCTURE OF THE WORK FORCE i.e. changing share of the work force, engaged in each sector.

In India, the service sector has grown by bye-passing the secondary sector.

AGRICULTURE, INDUSTRY AND FOREIGN TRADE DURING 1950-1990 PERIOD

I. AGRICULTURE

Main Features of Indian Agriculture

- 1) Low productivity
- 2) Disguised unemployment.
- 3) Dependency on rainfall
- 4) Subsistence farming-objective of farmer is to secure subsistence for his family not to earn profit.
- 5) Use of traditional inputs
- 6) Small size of land holdings
- 7) Backward technology.
- 8) Landlord tenant conflict.

Reforms in Indian Agriculture

A. Institutional Reforms also called Land reforms.

- i) Abolition of intermediaries.
- ii) Consolidation of holdings.
- iii) Ceiling on land holdings.
- iv) Cooperative Farming

Land reforms were successful in Kerala and west Bengal

B. Technical Reforms or Green Revolution

- i) Use of HYV seeds
- ii) Use of chemical fertilizers.
- iii) Use of insecticides and pesticides for crop protection
- iv) Adoption of Scientific farm management practices
- v) Mechanized means of cultivation.

Achievements of Green Revolution

- i) Rise in production and productivity.
- ii) Increase in income.
- iii) Helped in attaining marketable surplus
- iv) Buffer stock of foodgrains
- v) Benefit to low income groups

Failures of Green Revolution

- i) **Inter-Crop Imbalances:** Restricted to limited crops and areas such as two crops wheat & rice growing states like Punjab, Haryana, U.P. and Andhra Pradesh.
Regional Disparities: Increase in income disparity between small and big farmers
- ii) Ecological degradation.

Debate over Subsidies in Agricultural Sector

Subsidy -- It refers to the Monetary assistance given by the government for production activities.

Subsidy in agriculture means provision of some important inputs to farmers by the government at a concessional rate that is much lower than its market rate.

Arguments in favour of subsidies

- i) It was necessary to use subsidies to provide an incentive for adoption of the new HYV technology by farmers especially the small farmers.
- ii) Any new technology is considered as being risky by farmers. Subsidies were, therefore, needed to encourage farmers to adopt the new technology initially.
- iii) Farming in India is still a risky business and subsidies provide hedging against the risk of climatic conditions.
- iv) Most farmers are very poor and they will not be able to afford the required inputs without subsidies.
- v) Subsidies bring about equity between rich and poor farmers by enabling the poor farmers to use modern technology and inputs.

Arguments against subsidies

- i) Some economists say that subsidies should be phased out since their purpose has been served and the technology is now widely adopted due to its profitability.
- ii) Subsidies are benefiting the fertilizer industry more than farmers and it is not making any efforts towards increasing its efficiency as it is protected from market competition by subsidies.
- iii) Subsidies are mainly being availed by big farmers in affluent regions who do not actually need them.
- iv) It may lead to wastage of resources and thus put an excessive burden on the government.
- v) Suitable reforms need to be undertaken in order to ensure allocation of subsidies in a targeted manner only to the needy farmers.

II) INDUSTRY

- 1) Industrialisation is important for an economy as it:
- 2) Provides employment.
- 3) Raises national income.
- 4) Promotes regional balance.
- 5) Leads to modernisation.
- 6) Helps to modernise agriculture.
- 7) Imparts Dynamism to Growth Process
- 8) Industrialisation is a pre-condition for the final take-off of an economy.

Role of Public Sector/Government in Industrial Development

There was need for the leading role of public sector due to the following reasons.

- 1) Lack of capital with the private entrepreneurs.
- 2) Lack of incentive for the Pvt. entrepreneurs
- 3) social welfare - to generate employment rather than profits.
- 4) Development of infrastructure.
- 5) Development of backward areas.
- 6) To prevent concentration of economic power.
- 7) To promote import substitution.

Industrial Policy Resolution (IPR) 1956

Industrial policy is an important instrument through which the govt. regulates the industrial activities in an economy.

The 1956 resolution laid down the following objectives of industrial policy.

- i) To accelerate the growth of industrialization.
- ii) To develop heavy industries.
- iii) To expand public sector.
- iv) To reduce disparities in income and wealth.
- v) To prevent monopolies and concentration of wealth and income in the hands of a small member of individuals.

Features of Industrial Policy Resolution (IPR) of 1956

Features of Industrial policy resolution of 1956 were:

- 1) **New classification of Industries:** Industries were classified into three schedules depending upon role of state.
 - a) Schedule-A- 17 industries were included in schedule-A which would be exclusively owned by the State.
 - b) Schedule-B- 12 industries were included in schedule-B, in which Private sector could supplement the efforts of the Public Sector, with the state taking sole responsibility for starting new units.
 - c) Schedule-C – other remaining industries which were left open to private sector. Industrial
- 2) **licensing:** Industries in the private sector could be established only through a license from the government.
Note- Industrial Licensing: - Licensing is a tool for channelizing scarce resources in predetermined priority sector of an economy.
- 3) **Stress on the role of cottage and small-scale industries.** (in 1955 by Karve Committee stressed the importance of SSI)
- 4) **Industrial concessions-**were offered- to pvt. entrepreneurs for establishing industry in the backward regions of the country. Such as tax benefit and concessional rates for power supply.

Development of Small-Scale Industries (SSI)-Reservation of some products

Characteristics of SSI or Role of Small-Scale Industries

- i) Labour intensive-employment oriented
- ii) Self-employment.
- iii) Less capital intensive.
- iv) Shows locational flexibility.

Problems of Small-Scale Industries

- i) Difficulty of finance.
- ii) Shortage of raw material.
- iii) Difficulty of marketing.
- iv) Outdated machines & equipment
- v) Competition from large scale industries.

Critical appraisal of industrial development

- i) Rise in industrial sectors share in GDP
- ii) Industrial diversification
- iii) Promotion of SSI
- iv) Protection from foreign competition
- v) Licensing policy helped the government to monitor and control industrial production.
- vi) Role of public sector-created a strong industrial base.

III) FOREIGN TRADE

Trade Policy –Import substitution policy

In the first seven five-year plans of India, the trade was commonly called an ‘inward looking’ trade strategy. This strategy is technically known as ‘import substitution’.

Import substitution means substituting imports with domestic production.

Domestic firms from foreign competition were protected by

- i) Imposition of tariff and
- ii) Imposition of quotas

Impact of Inward-looking Trade strategy

- i) It helped to save foreign exchange by reducing import of goods.
- ii) Created a protected market and large demand for domestically produced goods.
- iii) Helped to build a strong industrial base in our country which directly lead to economic growth.

Criticism of Inward-looking strategy (import substitution strategy)

- i) It did not lead to increase in efficiency.
- ii) Lack of competition implied lack of modernisation.
- iii) Growth of inefficient public monopolies.

The need for reform was widely felt in the context of changing global economic scenario and the new economic policy was initiated in 1991 to make our economy more efficient.

Moral of the lesson –Nurse the baby, feed the child and free the adult.

MCQs (1 mark each)

1. The main objective of India's foreign trade policy during 1950-1990 was:

- a) Import substitution
- b) Export promotion
- c) Balanced trade
- d) Trade liberalization

2. What type of economy is followed in India?

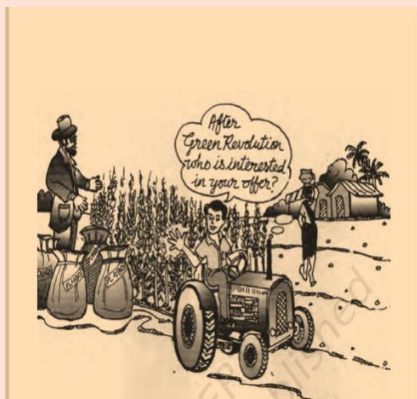
- a) Communist Economy
- b) Capitalist Economy
- c) Mixed Economy
- d) Socialist Economy

3. What was the main objective of the First Five-Year Plan (1951-1956)?

- a) Industrial development
- b) Agricultural development

- c) Infrastructure development
- d) Social development

4. Look at the image given below and answer the question by choosing the correct alternative:



Green revolution led to _____

- a) Attainment of marketable surplus
- b) Buffer stock of food grains
- c) Benefit to low-income groups
- d) All of the above

5. Arrange the following in the chronological order. (Choose the correct alternative)

- i) Constitution of Karva Committee
- ii) Beginning of first Five Year Plan
- iii) Establishment of Planning commission
- iv) Establishment of NITI Aayog

Alternatives:

- a) (i), (ii), (iii), (iv)
- b) (iii), (ii), (i), (iv)
- c) (iii), (iv), (ii), (i)
- d) (ii), (i), (iii), (iv)

6. Select the correct combination between the following columns

Column A

- I. Tariff
- II. Quota
- III. Make in India
- IV. Trade policy

Column B

- a) Increase in manufacturing sector
- b) Policy governing international trade
- c) Tax on imported goods
- d) Quantitative restrictions on import

Alternatives

- | | I | II | III | IV |
|----|-------|------|-------|------|
| a) | (i) | (ii) | (iii) | (iv) |
| b) | (iii) | (i) | (ii) | (iv) |
| c) | (iii) | (iv) | (i) | (ii) |
| d) | (ii) | (i) | (iii) | (iv) |

7. Which sector was given the highest priority in the Second Five-Year Plan (1956-1961)?

- a) Agriculture
- b) Heavy industries
- c) Services
- d) Transport

8. Small scale industries _____ (Choose the correct alternative)

- i) Use Labour intensive techniques of production
- ii) Shows locational flexibility.
- iii) Are Less capital intensive.

Alternatives:

- a) Only (i) is true
- b) Only (ii) is true
- c) Only (iii) is true
- c) All are true

9. The Green Revolution in India was primarily focused on increasing the production of which crops?

- a) Pulses and oilseeds
- b) Fruits and vegetables
- c) Wheat and rice
- d) Cotton and jute

10. Read the following statements carefully:

Statement I: The green revolution enabled the government to procure sufficient amount of food grains to build a stock which could be used in times of food shortage.

Statement II: The risk of the small farmers being ruined when pests attack their crops was considerably reduced by the services rendered by research institutes established by the government.

In the light of the given statements, choose the correct alternative from the following:

- a) Statement I is true and statement II is false.
- b) Statement I is false and statement II is true.
- c) Both statements I and II are true.
- d) Both statements I and II are false.

11. Read the following statements carefully:

Statement I: the Industrial Policy Resolution of 1956 formed the basis of the Second Five Year Plan, the plan which tried to build the basis for a socialist pattern of society.

Statement II: Although there was a category of industries left to the private sector, the sector was kept under state control through a system of licenses.

In the light of the given statements, choose the correct alternative from the following:

- a) Statement I is true and statement II is false.
- b) Statement I is false and statement II is true.
- c) Both statements I and II are true.
- d) Both statements I and II are false

12. Read the following statements carefully:

Statement I: The first seven five-year plans gave importance to self-reliance which means avoiding imports of those goods which could be produced in India itself.

Statement II: Domestic industries were protected through heavy duty on imports and fixation of import quotas.

In the light of the given statements, choose the correct alternative from the following:

- a) Statement I is true and statement II is false.
- b) Statement I is false and statement II is true.

- c) Both statements I and II are true.
- d) Both statements I and II are false.

13. Read the following statements carefully:

Statement I: Tariffs are a tax on imported goods

Statement II: Tariffs make imported goods more expensive and discourage their use

In the light of the given statements, choose the correct alternative from the following:

- a) Statement I is true and statement II is false.
- b) Statement I is false and statement II is true.
- c) Both statements I and II are true.
- d) Both statements I and II are false

14. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): India adopted a mixed economy after independence.

Reason (R): A mixed economy combines features of both capitalism and socialism.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

15. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): Land reforms were needed in India as the majority of its population depended on agriculture.

Reason (R): Ownership of land would give incentives to the actual tillers to make improvements.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

16. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): Industries were classified into three categories, viz., Schedule A, Schedule B, and Schedule C in Industrial Policy Resolution (IPR) 1956.

Reason (R): The system of Industrial Licensing was not applicable for Schedule C in Industrial Policy Resolution (IPR) 1956.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).

- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

17. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): Land reforms were successful in Kerala and Uttar Pradesh

Reason (R): Governments of these states were committed to the policy of land reforms

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

18. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): HYV seeds were the main reason for the agricultural revolution in India.

Reason (R): The major benefit of HYV seeds was that they needed less irrigation facilities.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

19. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): Small scale industries promote equity.

Reason (R): Small scale industries are labour intensive in nature.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

20. Read the following statements-Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): Land ceiling promotes equity in the agricultural sector.

Reason (R): Land ceiling policy fixes a minimum size of land which could be owned by an individual.

Alternatives:

- a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A).
- c) Assertion (A) is true but Reason (R) is false.
- d) Assertion (A) is false but Reason (R) is true.

ANSWERS FOR MCQs

Q.NO. ANSWER

- 1) a) Import substitution
- 2) c) Mixed Economy
- 3) b) Agricultural development
- 4) d) All of the above
- 5) b) (iii), (ii), (i), (iv)
- 6) c) (iii) (iv) (i) (ii)
- 7) b) Heavy industries
- 8) d) All are true.
- 9) c) Wheat and rice
- 10) a) Statement I is true and statement II are true.
- 11) c) Both statements I and II are true.
- 12) c) Both statements I and II are true.
- 13) c) Both statements I and II are true.
- 14) a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- 15) a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- 16) c) Assertion (A) is true but Reason (R) is false.
- 17) a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- 18) c) Assertion (A) is true but Reason (R) is false.
- 19) a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A).
- 20) c) Assertion (A) is true but Reason (R) is false.

SHORT ANSWER TYPE QUESTIONS (3/4 Marks Each)

1. Explain 'growth with equity' as a planning objective.

Ans. Both growth and equity are dual objectives of Indian planning. While growth refers to the increase in national income over a long period of time, equity refers to an equitable distribution of this income so that the benefits of higher economic growth can be passed on to all sections of the population to bring about social justice.

2. Why was it necessary for a developing country like India to follow self-reliance as a planning objective?

Ans. On the eve of independence, India was poor, stagnant and backward. There were heavy imports of foodgrains. It was important to be self-reliance.

Features of Self-reliance are:

- a) Self-sufficiency in foodgrains.
- b) Fall in foreign aid and reduced dependence on imports which is possible when there is growth in domestic production.

- c) Rise in exports.
- d) Rise in contribution of industries in gross domestic product.

3. While subsidies encourage farmers to use new technology, they are a huge burden on government finances. Discuss the usefulness of subsidies in light of this fact.

Ans. Subsidy is an economic benefit, direct or indirect, granted by a government to domestic producers of goods or services, often to strengthen their competitive position against foreign companies. It helps farmers to buy HYV seeds, fertilizers and other inputs. The burden of granting subsidies falls on the government. The government has to bear the burden of financing subsidies. There is scope for improving the resource use efficiency by reducing subsidies and aiming them better to small farmers and regions lagging behind.

4. Explain the policy of land to a tiller

Ans. The policy of 'land to the tiller' is based on the idea that the cultivators will take more interest—they will have more incentive—in increasing output if they are the owners of the land. This is because ownership of land enables the tiller to make profit from the increased output. Tenants do not have the incentive to make improvements on land since it is the landowner who would benefit more from higher output.

5. Why was the protection policy of our domestic economy criticized?

Ans. The protection from foreign competition was also being criticized on the ground that it continued even after it proved to do more harm than good. Due to restrictions on imports, the Indian consumers had to purchase whatever the Indian producers produced. The producers were aware that they had a captive market; so, they had no incentive to improve the quality of their goods. Competition from imports forces our producers to be more efficient.

LONG ANSWER TYPE QUESTIONS (6 Marks each)

1. Though public sector is very essential for industries, many public sector undertakings incur huge losses and are a drain on the economy's resources. Discuss the usefulness of public sector undertakings in the light of this fact.

Ans. Though many public sector undertakings are incurring huge losses, they are still very useful in the areas of strategic concerns and hazardous chemicals. Public sector undertakings are required for:

1. Creation of a Strong Industrial Base
2. Development of Infrastructure
3. Development of Backward Areas
4. To Mobilize Savings and Earn Foreign Exchange
5. To Prevent Concentration of Economic Power
6. To Promote Equality of Income and Wealth Distribution
7. To Provide Employment
8. To Promote Import Substitution.

2. What is Green Revolution? Why was it implemented and how did it benefit the farmers? Explain in brief.

Ans. Green revolution refers to the large increase in food grains resulting: -

- i) Use of HVY seeds
- ii) Use of chemical fertilizers
- iii) Use of insecticides and patricides for crop protection (iv) Mechanized means of cultivation

It was implemented as the agricultural productivity was very low and 75 % of the country's population was dependent on agriculture.

Benefits to Farmers:

1. Increase in income followed the green revolution as most of the areas that cultivated wheat and rice were witnessing great production, which helped in removing poverty from these areas.
2. With the increase in the production of crops, age-old customs were abolished, and the farmers began to adopt new agricultural methods, which were instrumental in bringing change in productivity.
3. It helped reduce unemployment as the lands were used for growing two varieties of the crop as per season, and therefore, it helped removed seasonal unemployment.
4. With nationalizing of banks, farmers were given subsidies on loans for cultivation, which improved production as more farmers were able to take a loan

3. Why and how was private sector regulated under the IPR 1956?

Ans. IPR or Industrial Policy Resolution, 1956, was a resolution that was adopted by the Indian parliament for industrial development in India. This resolution aimed at creating a socialistic pattern of society. Under this rule there were three categories of industries which were:

- i) Schedule A: Industries that are exclusive responsibility of the state
- ii) Schedule B: Industries that will be pre-dominantly owned by the public sector while private sector will be supplementing the efforts of the public sector
- iii) Schedule C: The remaining industry types that will be managed by private sector

Although the government wanted to define a separate category for the private sector, it wanted to keep the sector under state control and hence created a rule that in order to open a new industry or to expand an existing one, a license was required to be obtained from the government. If the industry was opened in a backward area, the government would offer subsidy and other facilities such as easy licensing. This step was taken to maintain regional equality. In order to increase production, a license was required so that no socially undesirable goods were produced.

CASE BASED QUESTIONS

Read the following hypothetical text and answer the given questions:

The performance of Indian economy during the period of first seven five-year plans (1950-1990) was satisfactory if not very impressive. On the eve of independence, India was an industrially backward country, but during this period of first seven plans our industries became far more diversified, with the stress being laid on the public investments in the industrial sector. The policy of import substitution led to protection of the domestic industries against the foreign producers but we failed to promote a strong export surplus. Although public sector expanded to a large extent but it could not bring desired level of improvement in the secondary sector. Excessive government regulations prevented the natural trajectory of growth of entrepreneurship as there was no competition, no innovation and no modernization on the front of the industrial sector. Many Public Sector Undertakings (PSU's) incurred huge losses due to operational inefficiencies, red-tapism, poor technology and other similar reasons. These PSUs continued to function because it was difficult to close a government undertaking even it is a drain on country's limited resources. On the Agricultural front, due to the measures taken under the Green Revolution, India more or less became self-sufficient in the production of food grains. So, the

needs for reform of economic policy were widely felt in the context of changing global economic scenario to achieve desired growth in the country.

1. Which of the following was not a reason for the public sector to play a major role in the initial phase of Indian Economic Planning? (choose the correct alternative)

- a) Private entrepreneurs lacked sufficient capital for investment.
- b) Government aimed at social welfare.
- c) The market was big enough to encourage private industrialists for investment.
- d) The government wanted to protect the indigenous producers from the foreign competition.

Ans: c) The market was big enough to encourage private industrialists for investment

2. Read the following statements - Assertion (A) and Reason (R)

Assertion (A): Many public sector undertakings incurred huge losses due to operational inefficiencies.

Reason (R): Red-tapism was one of the reasons for continuation of such enterprises.

Select the correct alternative from the following:

- a) Both Assertion (A) and Reason (R) are true.
- b) Both Assertion (A) and Reason (R) are false.

Ans: a) Both Assertion (A) and Reason (R) are true.

3. Inward looking trade strategy aimed at _____ (fill up the blank with correct answer)

Ans: Protecting domestic industries from international competition. (or any other valid answer)

4. State whether the given statement is true or false:

Mechanization of the Indian agriculture was one of the causes of Green Revolution in India.

Ans: True, it has led to tremendous increase in productivity and thereby tremendous increase in production

Read the following passage and answer the questions that follow:

The economic justification of subsidies in agriculture is, at present, a hotly debated question. It is generally agreed that it was necessary to use subsidies to provide an incentive for adoption of the new HYV technology by farmers in general and small farmers in particular. Any new technology will be looked upon as being risky by farmers. Subsidies were, therefore, needed to encourage farmers to test the new technology. Some economists believe that once the technology is found profitable and is widely adopted, subsidies should be phased out since their purpose has been served. There is no case for continuing with fertilizer subsidies.

a) What do you mean by subsidies?

Ans: The monetary assistance given by government for production activities.

b) Give any one argument in favour of subsidies.

Ans: A Large number of farmers are poor and they do not have sufficient means to purchase the required inputs.

c) Some say that agricultural subsidy a vice? Give reasons.

Ans: Subsidies pose a huge burden on Government finances.
Benefits of Subsidies are reaped by the farmers in prosperous regions.

New Economic Reforms / Liberalization, Privatization, and Globalization

(LPG) Reforms in 1991



- **Background:** Severe economic crisis characterized by **high fiscal deficit, balance of payments crisis, and dwindling foreign exchange reserves.**
- **Need:** Necessitated a shift from a state-controlled, inward-looking economy to a market-oriented and globally integrated economy.
- **Implementation:** Initiated by Prime Minister Narasimha Rao and Finance Minister Manmohan Singh through policy changes and legislative measures.

Liberalization:



- **Definition:** Relaxation of government controls and regulations on economic activities.
- **Objectives:** Reduce the state's role in the economy, promote competition, and encourage private enterprise.
- **Measures:** Deregulation of industries, easing of trade barriers, and liberalizing policies in sectors like finance and telecommunications.

Features of Liberalization:

- **Market Deregulation:** Reduced government control over the economy by easing restrictions on private sector participation and foreign investments.
- **Trade Liberalization:** Encouraged trade by reducing tariffs and barriers, facilitating easier imports and exports.
- **Financial Sector Reforms:** Introduced liberalized policies in banking, finance, and insurance sectors to promote competition and efficiency.

Privatization:



- **Definition:** Transfer of ownership and management of state-owned enterprises to the private sector.
- **Objectives:** Improve efficiency, competitiveness, and profitability of industries by reducing government control and introducing private management practices.
- **Measures:** Disinvestment and sale of shares in public sector companies, encouraging private investment in key sectors.

Features of Privatization:

- o **Public Sector Reforms:** Disinvestment of public sector enterprises to reduce government ownership and encourage private investment.
- o **Encouraging Private Sector:** Facilitated private participation in sectors traditionally reserved for the public sector, such as telecommunications and infrastructure.

Globalization:



- **Definition:** Integration of national economies with the global economy through trade, investment, and technological exchanges.
- **Objectives:** Integrate India into the global economic framework, attract foreign investment, and access global markets.
- **Measures:** Opened up the Indian economy to foreign direct investment (FDI), liberalized trade policies, and encouraged exports.

Features of Globalization:

- o **Integration with Global Economy:** Opened up the Indian economy to foreign investments, technology transfers, and global trade.

- **Impact on Industries:** Fostered competition, innovation, and efficiency in industries through exposure to global markets and practices.

Impact of LPG Reforms:

- **Economic Growth:** Accelerated economic growth, modernization of industries, and improved productivity.
- **Global Integration:** India became a significant player in the global economy, attracting foreign investments and participating in international trade.
- **Challenges:** Brought income disparities, regional imbalances, and environmental concerns, which required subsequent policy interventions.

Appraisal of LPG Reforms (1991):

1. Positive Aspects:

- **Economic Growth:** Transformed India into a dynamic global player, significantly boosting GDP growth rates.
- **Foreign Direct Investment (FDI):** Increased FDI inflows attracted foreign capital, technology, and expertise.
- **Job Creation:** Expansion of private sector industries and services created employment opportunities.
- **Technological Advancement:** Access to global technology and best practices improved productivity and competitiveness.

2. Challenges and Criticisms:

- **Income Inequality:** Widened income disparities between rich and poor, exacerbating social inequalities.
- **Regional Disparities:** Development was uneven, with urban areas benefitting more than rural regions.
- **Environmental Impact:** Industrial growth and urbanization led to environmental degradation and resource depletion.
- **Vulnerability to Global Shocks:** Increased integration made India susceptible to global economic downturns and financial crises.

3. Policy Adjustments:

- **Social Safety Nets:** Interventions like MGNREGA aimed at mitigating adverse effects on vulnerable sections.
- **Sustainable Development:** Emphasis on balancing economic growth with environmental conservation.
- **Inclusive Growth:** Focus on addressing income disparities and regional imbalances.

4. Conclusion:

- **Significance:** Marked a pivotal moment in India's economic history, fostering liberalization, privatization, and globalization.
- **Outcome:** Accelerated economic growth and global integration, while posing challenges requiring policy interventions for inclusive and sustainable development.

Recent Reforms: Demonetization and Goods and Services Tax (GST) in India

DEMONETIZATION

Introduction:

- **Definition:** Act of stripping a currency unit of its status as legal tender to curb corruption, counterfeiting, and black money.
- **Context:** on November 8, 2016., India invalidated Rs.500 and Rs.1,000 currency notes.

Impact:

- **Short-term Effects:**
 - Liquidity crunch and economic slowdown in cash-dependent sectors.
 - Disruption in informal sectors.
- **Long-term Effects:**

- Encouraged shift towards digital payments and formal economy.
- Increased use of banking services and digital payment platforms.
- Aimed at reducing black money circulation.

Government Policies and Measures:

- Introduction of new currency notes (Rs.2,000 and redesigned Rs.500).
- Promotion of digital payments through initiatives like BHIM app and UPI.

Evaluation and Analysis:

- **Successes:** Initial increase in digital transactions and symbolic gesture against black money and corruption.
- **Challenges:** Economic disruption and GDP slowdown.

Conclusion: Mixed outcomes, aimed at curbing black money and promoting a digital economy, but faced challenges in implementation and economic disruption.

GOODS AND SERVICES TAX (GST):

Background and Introduction:

- **Objective:** Replace multiple indirect taxes with a unified tax to create a seamless national market.
- **Origin:** Proposed by the Indian government in 2000 and enacted in 2017.

Key Features:

- **Unified Tax Structure:** Subsumed various indirect taxes.
- **Dual GST Model:** CGST, SGST, and IGST for intra-state and inter-state transactions.

Structure:

- **Tax Slabs:** Different rates for various categories: 0%, 5%, 12%, 18%, and 28%.
- **Threshold Limits:** Small businesses with annual turnovers below specified thresholds can avail of composition schemes.

Implementation Process:

- **Constitutional Amendment:** Enabled GST levy and established the GST Council.
- **GST Council:** Chaired by the Union Finance Minister and comprising state finance ministers.

Impact:

- **Benefits:** Unified market, reduction in tax cascading, and boost to GDP.
- **Challenges:** Initial implementation issues and adaptation for businesses.

Future Prospects:

- **Policy Adjustments:** GST Council continues to make adjustments.
- **Further Integration:** Aimed at integrating informal sectors and expanding the tax base.

Conclusion: Significant reform aimed at simplifying taxation, enhancing efficiency, and fostering economic growth, despite initial challenges.

Online Resources and Government Websites:

1. Government of India. *Press Information Bureau (PIB) Releases and Updates*. Press Information Bureau, <https://pib.gov.in>.
2. Reserve Bank of India. *Reports and Bulletins*. Reserve Bank of India, <https://rbi.org.in>.
3. Government of India. *India Budget*. Ministry of Finance, <https://www.indiabudget.gov.in>.
4. GST Council. *Official Website of GST Council*. GST Council, <https://www.gstcouncil.gov.in>.

QUESTION & ANSWERS (1 MARKS)

1. **What was the primary objective of the New Economic Policy (NEP) of 1991 in India?**
 - A. To promote socialism and strengthen public sector enterprises
 - B. To address the balance of payments crisis and stabilize the economy
 - C. To nationalize foreign-owned enterprises
 - D. To increase tariffs on imports
2. **Which sector saw significant reforms through privatization under the New Economic Policy of 1991?**
 - A. Agriculture
 - B. Healthcare
 - C. Education
 - D. Public sector enterprises
3. **What was the main strategy used to dismantle the License Raj under the New Economic Policy?**
 - A. Increasing bureaucratic controls
 - B. Imposing stricter industrial licensing requirements
 - C. Reducing industrial licensing requirements
 - D. Nationalizing private enterprises
4. **How did trade liberalization contribute to the New Economic Policy of 1991?**
 - A. By increasing tariffs on imports to protect domestic industries
 - B. By promoting competition, enhancing efficiency, and integrating India into the global economy
 - C. By nationalizing key industries
 - D. By imposing strict controls on foreign investment
5. **What impact did the New Economic Policy of 1991 have on foreign direct investment (FDI) in India?**
 - A. It discouraged FDI by imposing stringent regulations
 - B. It had no impact on FDI
 - C. It liberalized FDI norms to attract capital inflows
 - D. It nationalized foreign-owned enterprises
6. **What was the main objective behind the implementation of GST in India?**
 - A. To reduce income tax rates
 - B. To simplify indirect taxes and create a unified national market
 - C. To promote privatization of public sector enterprises
 - D. To increase import tariffs
7. **Under the GST regime, which taxes were subsumed into a single tax system?**
 - A. Only central excise duty
 - B. Only service tax
 - C. Both central excise duty and service tax
 - D. None of the above
8. **What was the primary objective of demonetization in India in 2016?**
 - A. To eliminate counterfeit currency
 - B. To promote digital transactions
 - C. To curb black money and corruption
 - D. To increase liquidity in the economy
9. **Which denomination currency notes were demonetized by the Government of India in November 2016?**
 - A. Rs.500 and Rs.2000
 - B. Rs.1000 and Rs.5000
 - C. Rs.100 and Rs.500
 - D. Rs.50 and Rs.100

- **Read the following statements – Assertion (A) and reason (R). Choose one of the correct alternatives given below**
- Both assertion (A) and reason (R) are true and reason is the correct explanation of assertion.
 - Both assertion (A) and reason (R) are true and reason is not the correct explanation of assertion.
 - Assertion (A) is true but reasons (R) is false
 - Assertion (A) is false but reasons (R) is true
- Assertion:** The New Economic Policy of 1991 aimed to address the balance of payments crisis in India.
Reasoning: By liberalizing trade and reducing import tariffs, the policy sought to stabilize the external sector and enhance foreign exchange reserves.
 - Assertion:** Liberalization under the New Economic Policy led to increased competition among industries in India.
Reasoning: Dismantling the License Raj removed barriers to entry and encouraged new players to enter the market, fostering competitive dynamics.
 - Assertion:** Privatization was a key component of the New Economic Policy of 1991.
Reasoning: The policy aimed to reduce the government's role in business operations, improve efficiency, and raise resources for public expenditure.
 - Assertion:** The New Economic Policy of 1991 emphasized fiscal consolidation to reduce the fiscal deficit.
Reasoning: Rationalizing subsidies and controlling government expenditure were crucial measures undertaken to achieve fiscal discipline.
 - Assertion:** Trade liberalization was essential under the New Economic Policy to integrate India into the global economy.
Reasoning: By reducing tariffs and removing quantitative restrictions on imports, the policy aimed to enhance competitiveness and expand export opportunities.
 - Assertion:** The New Economic Policy of 1991 aimed to promote technological advancements in Indian industries.
Reasoning: By encouraging foreign direct investment (FDI), the policy facilitated technology transfer and adoption of global best practices.
 - Assertion:** The New Economic Policy of 1991 contributed to the growth of service sectors like information technology in India.
Reasoning: Liberalization created favorable conditions for the service sector by relaxing regulations and promoting innovation-driven industries.
 - Assertion:** The agricultural sector remained largely unchanged by the reforms introduced under the New Economic Policy of 1991.
Reasoning: The policy primarily focused on industrial and trade reforms, with minimal impact on agricultural policies and practices.
 - Assertion:** The New Economic Policy of 1991 aimed to reduce the dependency of Indian industries on government approvals and licenses.
Reasoning: By streamlining bureaucratic processes and reducing regulatory burdens, the policy aimed to enhance operational efficiency and promote entrepreneurship.
 - Assertion:** The New Economic Policy of 1991 contributed to widening income inequalities in India.
Reasoning: While promoting economic growth, the policy disproportionately benefited urban areas and certain industries, exacerbating income disparities.
 - Assertion:** GST aimed to streamline the indirect tax structure in India.
Reasoning: By subsuming multiple indirect taxes into a single tax, GST aimed to reduce tax cascading and create a seamless national market.
 - Assertion:** Demonetization aimed to reduce the circulation of black money in the Indian economy.
Reasoning: By invalidating high-denomination currency notes, the government aimed to bring unaccounted wealth into the formal banking system.

22. From the set of statements given in Column I and Column II, choose the correct pair of statements:

Column I	Column II
A. Outsourcing B. Foreign exchange reforms C. GST D. Contraction of public sector	)i) An important outcome of the process of liberalisation)ii) Initiated with the devaluation of the Indian rupee against foreign currency)iii) A direct tax)iv) A measure of privatization

Alternatives:

- A-(1)
B-(ii)
C-(iii)
D-(iv)

ANSWERS FROM QUESTION NO 1 TO 22

1	2	3	4	5	6	7	8	9	10		
B	D	C	B	C	B	C	C	A	A		
11	12	13	14	15	16	17	18	19	20	21	22
A	A	A	A	A	A	B	A	A	A	A	B

QUESTION ANSWERS (3 MARKS, 4 MARKS, AND 6 MARKS)

CASE /SOURCE-BASED QUESTIONS AND ANSWERS

Source 1: New Economic Policy (NEP) 1991

Source: "In 1991, India faced a severe economic crisis. The country's foreign exchange reserves had plummeted, and it was on the verge of defaulting on its international debt obligations. To address this crisis, the Government of India, led by then Finance Minister Dr. Manmohan Singh, introduced the National Economic Policy (NEP) of 1991. This policy aimed at liberalizing the Indian economy by reducing government controls and promoting private enterprise. Major reforms included de-licensing of industries, reduction in import tariffs, and opening up sectors like telecommunications and insurance to foreign investments."

23. What were the main reasons behind the introduction of the National Economic Policy (NEP) 1991?

Answer: The NEP 1991 was introduced due to a severe economic crisis in India, characterized by plummeting foreign exchange reserves and the threat of defaulting on international debt obligations.

24. Who was the Finance Minister responsible for implementing NEP 1991, and what were the key reforms introduced?

Answer: The Finance Minister responsible was Dr. Manmohan Singh. The key reforms included de-licensing of industries, reduction in import tariffs, and opening up sectors like telecommunications and insurance to foreign investments.

25. **The 1991 economic crisis in India highlighted the need for structural reforms. Which of the following was NOT a feature of the NEP 1991?**
- a) De-licensing of industries
 - b) Nationalization of banks
 - c) Reduction in import tariffs
 - d) Encouragement of foreign direct investment
26. **How did the NEP 1991 aim to attract foreign investments?**
- a) By increasing import tariffs
 - b) By offering subsidies to domestic industries
 - c) By allowing 100% foreign equity in certain sectors
 - d) By reducing the value of the Indian Rupee
27. **Which of the following is a likely consequence of the de-licensing of industries as per NEP 1991?**
- a) Increase in bureaucratic delays
 - b) Growth in private sector participation
 - c) Decline in foreign investments
 - d) Increase in state control over the economy
28. **The reduction of import tariffs under NEP 1991 was aimed at:**
- a) Protecting domestic industries
 - b) Making imports more expensive
 - c) Increasing competition and efficiency
 - d) Reducing foreign trade
29. **Which of the following was a significant impact of the NEP 1991 on the Indian economy?**
- a) Decrease in foreign exchange reserves
 - b) Increased government regulation
 - c) Boost in economic growth and employment
 - d) Reduction in foreign direct investment

Answers

- 25. **b) Nationalization of banks**
- 26. **c) By allowing 100% foreign equity in certain sectors**
- 27. **b) Growth in private sector participation**
- 28. **c) Increasing competition and efficiency**
- 29. **c) Boost in economic growth and employment**

Source 2: Demonetization

Source: "On November 8, 2016, the Government of India announced the demonetization of all ₹500 and ₹1000 banknotes, which constituted 86% of the cash in circulation. This move aimed to curb black money, counterfeit currency, and corruption. The sudden announcement led to long queues at banks and ATMs as people rushed to exchange or deposit their old notes. While the move was praised by some for its bold approach to tackling black money, it also faced criticism for causing disruption to the economy, particularly in the informal sector, which relies heavily on cash transactions."

30. What were the primary objectives of the demonetization policy announced on November 8, 2016?

Answer: The primary objectives of the demonetization policy were to curb black money, counterfeit currency, and corruption.

31. What were some immediate effects of the demonetization move on the public and the economy?

Answer: Immediate effects included long queues at banks and ATMs as people rushed to exchange or deposit their old notes. The move caused significant disruption to the economy, particularly in the informal sector, which relies heavily on cash transactions.

32. What was a primary objective of the demonetization policy announced in 2016?

- a) To introduce new denominations
- b) To reduce interest rates
- c) To curb black money and counterfeit currency
- d) To increase foreign investments

33. How did demonetization impact the informal sector?

- a) Increased digital transactions immediately
- b) Caused disruption due to reliance on cash
- c) Improved access to formal banking
- d) Reduced unemployment rates

34. Which of the following was an immediate effect of demonetization on the banking system?

- a) Decrease in bank deposits
- b) Surge in bank deposits
- c) Reduction in bank liquidity
- d) Increase in interest rates

35. What percentage of the cash in circulation was demonetized in November 2016?

- a) 50%
- b) 60%
- c) 70%
- d) 86%

36. Which Indian Prime Minister announced the demonetization policy in 2016?

- a) Manmohan Singh
- b) Narendra Modi
- c) Atal Bihari Vajpayee
- d) Rajiv Gandhi

Answers

- 32. c) To curb black money and counterfeit currency
- 33. b) Caused disruption due to reliance on cash
- 34. b) Surge in bank deposits
- 35. d) 86%
- 36. b) Narendra Modi

Case Study 3: Goods and Services Tax (GST)

In July 2017, India implemented the Goods and Services Tax (GST), which aimed to create a single, unified market by replacing multiple indirect taxes levied by the central and state governments. GST is a value-added tax levied on most goods and services sold for domestic consumption. It is a multi-stage, destination-based tax that is collected at every stage of the production process but refunded to all parties except the final consumer. The GST Council, which includes representatives from the central and state governments, is responsible for deciding the tax rates and ensuring smooth implementation of the tax system.

37. What is the main objective of implementing the Goods and Services Tax (GST) in India?

Answer: The main objective of implementing GST in India was to create a single, unified market by replacing multiple indirect taxes levied by the central and state governments.

38. Explain the role of the GST Council in the GST system.

Answer: The GST Council is responsible for deciding the tax rates and ensuring the smooth implementation of the GST system. It includes representatives from the central and state governments.

39. What is the main purpose of implementing GST in India?

- a) To increase indirect tax rates
- b) To create a unified national market
- c) To reduce government revenue
- d) To promote cash transactions

40. Which of the following best describes the GST system in India?

- a) Single-stage tax system
- b) Multi-stage, destination-based tax
- c) Origin-based tax
- d) Direct tax system

41. The GST Council is responsible for:

- a) Implementing direct taxes
- b) Deciding tax rates and policies under GST
- c) Managing foreign exchange reserves
- d) Regulating state-owned enterprises

42. One of the benefits of GST is the elimination of the 'tax on tax' effect. This is referred to as:

- a) Cascading effect
- b) Direct tax benefit
- c) Reverse charge mechanism
- d) Input tax credit

43. Which of the following is a challenge faced by businesses due to GST implementation?

- a) Increased manual record-keeping
- b) Complex compliance requirements
- c) Higher corporate tax rates
- d) Reduced access to foreign markets

Answers

- 39. b) To create a unified national market
- 40. b) Multi-stage, destination-based tax
- 41. b) Deciding tax rates and policies under GST
- 42. a) Cascading effect
- 43. b) Complex compliance requirements

44. Discuss the objectives and key measures of the New Economic Policy of 1991 in India.

Answer: The New Economic Policy of 1991 was introduced in response to India's severe economic crisis, aiming to transition from a centrally planned economy to a market-oriented one. Its key objectives included stabilizing the balance of payments, promoting economic growth, enhancing efficiency, and integrating into the global economy. To achieve these goals, the policy implemented several measures:

Liberalization: This involved dismantling the License Raj, reducing industrial licensing requirements, and easing restrictions on foreign investment and trade. It aimed to foster competition, innovation, and efficiency in Indian industries.

Privatization: The policy initiated the privatization of public sector enterprises to improve their efficiency, reduce the burden on the government's finances, and attract private investment.

Fiscal Reforms: Measures included rationalizing subsidies, controlling government expenditure, and reducing the fiscal deficit to ensure macroeconomic stability and investor confidence.

Global Integration: Trade liberalization measures such as reducing tariffs and removing quantitative restrictions aimed to integrate the Indian economy into the global market, boost exports, and attract foreign investment.

45. Evaluate the impact of the New Economic Policy of 1991 on industrial growth in India.

Answer: The New Economic Policy of 1991 had a profound impact on industrial growth in India by removing barriers to entrepreneurship and fostering a competitive business environment. Key impacts include:

End of License Raj: Dismantling industrial licensing and reducing bureaucratic controls allowed industries to operate more freely, encouraging new investments and technological upgrades.

Foreign Investment: Liberalization policies attracted foreign direct investment (FDI), bringing in capital, technology, and managerial expertise that accelerated industrial growth.

Privatization: Privatizing state-owned enterprises improved their efficiency and productivity, contributing to overall industrial output and competitiveness.

Technological Advancement: Integration into the global economy facilitated technology transfer and adoption of best practices, enhancing the technological base of Indian industries. However, the policy also faced criticisms for widening income disparities and neglecting certain sectors like agriculture. Nevertheless, its overall impact on industrial growth was significant, positioning India as a key player in global manufacturing and services sectors.

46. Explain the role of liberalization in the New Economic Policy of 1991 and its implications for India's economy.

Answer: Liberalization was a cornerstone of the New Economic Policy of 1991, aimed at reducing government control and promoting market forces in India's economy. Its role and implications are as follows:

Trade Liberalization: Reduced tariffs and removal of quantitative restrictions on imports promoted competition, expanded market access, and integrated Indian industries into global supply chains.

Industrial Deregulation: Ending the License Raj encouraged entrepreneurship, innovation, and efficiency in industries previously stifled by bureaucratic controls.

Financial Sector Reforms: Liberalization of the financial sector allowed for the entry of private banks, enhanced access to credit, and improved efficiency in capital allocation.

Foreign Investment: Policies liberalizing FDI norms attracted foreign capital, technology, and managerial expertise, contributing to economic growth and modernization.

47. Discuss the reasons behind the introduction of the New Economic Policy of 1991 in India. Evaluate its impact on the Indian economy.

Answer: Introduction of the New Economic Policy (NEP) of 1991: The New Economic Policy of 1991 was introduced in response to a severe balance of payments crisis and economic stagnation in India. The country faced dwindling foreign exchange reserves, high inflation, unsustainable fiscal deficits, and stagnant industrial growth. The policy was necessitated by the need to move away from a highly regulated, centrally planned economy towards a market-oriented approach.

Objectives and Measures:

Liberalization: The NEP aimed to liberalize the Indian economy by dismantling the License Raj, which imposed stringent controls and bureaucratic hurdles on industry. This included reducing industrial licensing requirements, easing restrictions on foreign investment, and liberalizing trade through reduced tariffs and removal of quantitative restrictions.

Privatization: Another key objective was the privatization of state-owned enterprises (SOEs). This aimed to improve efficiency, enhance competitiveness, and reduce the burden on government finances. Strategic disinvestment in SOEs was undertaken to encourage private sector participation and improve resource allocation.

Fiscal Reforms: The policy emphasized fiscal discipline by rationalizing subsidies, controlling government expenditure, and reducing the fiscal deficit. This was crucial for macroeconomic stability, reducing inflationary pressures, and improving investor confidence.

Global Integration: Trade and financial sector reforms were aimed at integrating the Indian economy into the global market. Trade liberalization policies sought to boost exports, attract foreign investment, and enhance India's competitiveness on the global stage.

Impact on the Indian Economy:

The NEP of 1991 had profound impacts on the Indian economy:

Economic Growth: Liberalization and reforms unleashed economic potential, leading to higher GDP growth rates. India transitioned from the sluggish growth of the pre-reform era to becoming one of the fastest-growing major economies globally.

Industrial Growth: Dismantling the License Raj and promoting competition spurred industrial growth. Key sectors like information technology, telecommunications, and services flourished, attracting investments and creating jobs.

Foreign Investment: Liberalization of FDI norms attracted foreign capital, technology, and managerial expertise. This contributed to modernizing industries, improving productivity, and integrating India into global supply chains.

Sectoral Reforms: Privatization and reforms in sectors such as telecommunications and banking improved efficiency and service delivery. The entry of private players in previously monopolized sectors enhanced competition and consumer choice.

Social Impact: While economic growth improved living standards for many, income disparities widened between urban and rural areas and among different income groups. Social safety nets and inclusive growth strategies became crucial to address these disparities.

Conclusion: In conclusion, the New Economic Policy of 1991 marked a turning point in India's economic history, steering the country towards liberalization, privatization, and globalization. While it brought about significant economic benefits, challenges such as income inequality and environmental concerns emerged.

48. Discuss its impact on India's industrial and technological development.

Answer: Role of Foreign Investment: Foreign investment played a pivotal role in the economic reforms introduced under the New Economic Policy (NEP) of 1991 in India. The policy aimed to attract foreign capital, technology, and managerial expertise to modernize Indian industries and integrate them into the global economy.

Impact on Industrial Development:

Technological Advancement: Foreign Direct Investment (FDI) brought advanced technology and best practices to Indian industries, particularly in sectors like telecommunications, automobiles, and pharmaceuticals. This accelerated technological adoption and innovation, enhancing industrial competitiveness.

Infrastructure Development: FDI inflows facilitated infrastructure development, especially in sectors requiring substantial capital investments such as telecommunications, power generation, and transport.

Job Creation: Foreign investments created employment opportunities across various sectors, directly through new enterprises and indirectly through supply chains and support services.

Impact on Technological Development:

Knowledge Transfer: Multinational corporations (MNCs) brought global expertise and research capabilities, fostering knowledge transfer and skill development among the local workforce.

R&D Investments: Many foreign companies established Research and Development (R&D) centers in India, contributing to innovation and product development in fields such as IT, pharmaceuticals, and automotive engineering.

Competitiveness: Access to global markets and technology through FDI enhanced the competitiveness of Indian industries, enabling them to produce high-quality goods and services for domestic and export markets.

Challenges and Considerations: Despite these benefits, challenges such as technology dependency, repatriation of profits, and environmental impacts of industrialization required careful management. The government's policies aimed to balance the benefits of FDI with safeguarding national interests and promoting sustainable development.

Conclusion: In conclusion, foreign investment under the NEP of 1991 played a pivotal role in transforming India's industrial and technological landscape. It catalyzed industrial growth, technological innovation, and infrastructure development, making India a globally competitive economy. However, continued policy attention is necessary to ensure that FDI contributes to inclusive and sustainable development while addressing associated challenges effectively.

49. Discuss the impact of GST on the Indian economy.

Answer: GST (Goods and Services Tax) was implemented in India with the aim of simplifying the indirect tax structure and creating a unified national market. Its impact on the economy includes:

Simplification: GST replaced multiple indirect taxes at the central and state levels with a single tax, reducing tax cascading and compliance costs.

Unified Market: It created a seamless national market by standardizing tax rates and procedures across states, facilitating interstate trade and reducing logistical inefficiencies.

Business Environment: GST improved ease of doing business by streamlining tax administration and reducing bureaucratic hurdles, thereby promoting investment and economic growth. Overall, while GST faced initial implementation challenges, it has contributed to enhancing tax compliance, boosting government revenue, and fostering a more integrated economy.

50. Evaluate the impact of demonetization on the Indian economy.

Answer: Demonetization, implemented in November 2016, aimed to curb black money, corruption, counterfeit currency, and promote digital transactions. Its impact on the Indian economy includes:

Short-term Disruption: Demonetization led to temporary cash shortages and disrupted economic activity, particularly in the informal sector.

Digital Transactions: It accelerated the adoption of digital payment methods and formalized financial transactions, promoting financial inclusion and transparency.

Tax Compliance: Demonetization increased the tax base as previously unaccounted wealth was deposited or declared, enhancing tax revenues.

Long-term Effects: While the immediate impact on black money circulation was debated, demonetization spurred reforms in digital infrastructure and tax administration. In conclusion, demonetization had mixed outcomes but catalyzed shifts towards a less-cash economy and underscored the importance of comprehensive reform.

UNIT 7-CURRENT CHALLENGES FACING INDIAN ECONOMY

HUMAN CAPITAL FORMATION

1. Human capital formation means how people become resource by imparting knowledge, and skill that converts a human being into human capital.

HEALTH AND EDUCATION:

Expenditure on health is an important source of human capital formation.

The amount of money spent on

- ★ preventive medicine (vaccination),
- ★ curative medicine (medical intervention during illness),
- ★ social medicine (spread of health literacy) and
- ★ provision of clean drinking water and good sanitation

Health expenditure directly increases the supply of healthy labour force

Spending on education by individuals

- ★ Is similar to spending on capital goods by companies
- ★ Individuals invest in education with the objective of increasing their future income.
- ★ It results in optimum resource utilisation.

ON THE JOB TRAINING:

- ★ The workers may be trained in the firm itself under the supervision of a skilled worker;
- ★ The workers may be sent for off-campus training.
- ★ Expenditure regarding on-the-job training is a source of human capital formation as the return in the form of enhanced labour productivity is more than the cost of it.

MIGRATION:

- ★ Technically qualified persons, like engineers and doctors, migrate to other countries because of higher salaries
- ★ Migration involves cost of transport, higher cost of living in the migrated places and psychic costs of living in a strange sociocultural setup.
- ★ The enhanced earnings in the new place outweigh the costs of migration; hence, expenditure on migration is also a source of human capital formation

INFORMATION:

- ★ Expenditure on information is necessary to make decisions regarding investments in human capital
- ★ For efficient utilisation of the acquired human capital stock.
- ★ For acquiring information relating to the labour market and other markets is also a source of human capital formation.

Role of human capital in economic development

- ★ Both go hand in hand
- ★ Better handling of techniques and technology raises the productivity
- ★ Innovation is possible which increases GDP
- ★ Higher rate of participation means increased living standard
- ★ Per capita income has direct relation with positive education and health

★ Human capital and human development

Human capital considers education and health as a means to increase labour productivity.

Human development is based on the idea that education and health are intergral to human well being

Growth of Education Sector in India: Can be explained in two manners:

★ IN TERMS OF INCREASED EXPENDITURE**★ IN TERMS OF INCREASED SHARE IN GDP**

★ In 2009, the Government of India enacted the Right of Education Act to make free education a fundamental right of all children in the age group of 6-14 years.

★ 2% education cess on all union taxes – will be spent on elementary education

★ Along with RTE, NATIONAL LITERACY MISSION, SARVA SHIKSHA ABHIYAAN, NATIONAL PROGRAMME FOR EDUCATION OF GIRLS AT ELEMENTARY EDUCATION, KASTURBA GANDHI BALIKA VIDHYALAYAS AND MID DAY MEAL Scheme are the programmes to promote literacy and elementary education

Secondary Education

Navodaya Vidyalayas and Kendriya vidyalayas NCERT

Higher Education

Universities, Colleges, Professional and Technical education. The following main institutions are working in the field of higher education.

UGC, IGNOU, AICTE, ICMR etc

★ Total 23 IITs, 31 NITs, 48 central universities, more than 800 universities, 13 AIIMS with 6 new AIIMS are in pipeline. 3870 medical colleges

★ Atal Innovation mission: Atal Tinkering Labs- 5450

★ Problems facing human capital formation

i) Rising population

ii) High regional and gender inequality

iii) Brain-drain

iv) Insufficient manpower planning

v) High levels of poverty

vi) Low levels of academic standard

★ Highlights of education sector in India NEP -2020

5+3+3+4 curricular structure

Vocationalisation in education

Equitable and inclusive education with an emphasis on GENDER EQUITY

Teacher recruitment etc

Elementary Education

Various policies such as Sarva Shiksha Abhiyan, Mid-day meal scheme, District Primary Education programme, right to education have been playing a major role

Secondary Education

Navodaya Vidyalayas and Kendriya vidyalayas NCERT

Higher Education

Universities, Colleges, Professional and Technical education. The following main institutions are working in the field of higher education.

UGC, IGNOU, AICTE, ICMR etc

Problems relating to development of education in India

- i) Inadequate vocationalisation
- ii) Gender bias
- iii) Low level of rural accessibility
- iv) Low government expenditure on education

CASE BASED QUESTIONS

1. Read the following paragraph carefully and answer the following questions:

Human Capital can be defined as the body of knowledge possessed by the population and the capacity of the population to use the knowledge effectively. Until the late 1950s, no economist and any other social scientist did pay much attention to the role of investment in human beings as an important determinant of economic development. The birth of this idea can be dated from the presidential address of Prof. Theodore W. Schultz to the American Economic Association in December 1960. As a result, the concept of human capital formation came to the

lime light. A circular relationship between human development and economic growth has come to be established. Economic growth creates conditions for better health and education facilities, which in turn spur economic growth.

i) Human Capital came into existence in _____

a. 1950 b. 1960 c. 1970 d. 1980

ii) Economists say that the main key player of economic development is _____

a. Human capital b. Physical capital c. Real Capital d. None of these

iii) In _____ Five Year plan, India emphasised on human Capital formation.

a. 2nd b. 3rd c. 5th d. 7th

iv) _____ means an improvement in quality of life and living standards in terms of measures of literacy, life expectancy and health care.

a. Economic growth b. Economic Development c. Investment d. none

2. Read the following paragraph carefully and answer the following questions:

Traditional economic theory viewed capital in physical terms only. Economists during the

late 1950s based on the aggregate production function found that the standard measures of simple labour and physical capital were incapable of explaining adequately the rapid post war growth.

Speculations on what was missing were diverse. Some argued that the principal explanation lays in the lack of appropriate adjustments for improvement in the quality of physical capital and the embodiment of technical progress in that capital. Others suggested that the most important omission pertains to the organizational advance or a vaguely specified human capital. The residual of unexplained growth was at first ascribed to technology by Solow, but later the residual was defined to include improvements in the quality of capital and the investment in human beings.

Human capital is formed with improvement in skill, education. Improved health and education are merit as well as a public good is associated with a large number of externalities which are often indirect, indivisible and non-quantifiable.

i) Which of the following gives the definition of public goods?

a) Excludable and non-rivalrous in nature.

b) Non- Excludable and non-rivalrous in nature.

- c) Excludable and rivalrous in nature
 - d) Non- Excludable and rivalrous in nature.
- ii) Standard economic theories failed to explain the post war rapid growth due to a) measuring growth in terms of physical growth only
- b) ignoring other important inputs such as improved skills and education
 - c) Both (a) and (b) d) None of the above
- iii) In the context of the above paragraph, residual factor includes:
- a) Improvement in the quality of human capital
 - b) investment in human beings
 - c) improvement in technology
 - d) All of the above

ASSERTION AND REASONING QUESTIONS

Read the following statements – Assertion (A) and reason (R). Choose one of the correct alternatives given below.

- a) Both assertion (A) and reason (R) are true and reason is the correct explanation of assertion.
- b) Both assertion (A) and reason (R) are true and reason is not the correct explanation of assertion.
- c) Assertion (A) is true but reason (R) is false
- d) Assertion (A) is false but reason (R) is true

3. Assertion (A): High level of human capital implies not only high earning potential but also change in the social and economic outlook.

Reason (R): It transforms the way of thinking and allows an individual to make well-informed and rational decisions.

4. Assertion (A): Human capital formation increases productivity of physical capital.

Reason (R): Larger the number of skilled and trained personnel, lesser the possibility of innovations, inventions and technical improvements in the area of production.

5. Assertion (A): There is a need to bridge the skill-gap in India in order to enhance human capital and bring about more productive labor force.

Reason (R): Skills are tangible in nature and can be separated from its owner.

6. Assertion (A): Human capital formation refers to adding on to the existing stock of skill, expertise and talent of people.

Reason (R): Expenditure on information is not a determinant of human capital formation.

7. Assertion (A): People migrate because that can fetch them high earning jobs than what they

get in their native places/ countries.

Reason (R): Enhanced earnings in the new place exceed the cost of migration.

8. Assertion (A): Brain drain is a serious threat to the process of human capital formation in the country.

Reason (R): People of high caliber such as scientists, engineers, educationists, etc, may decide to migrate.

9. Assertion (A): Education is wider concept and encompasses literacy.

Reason (R): A person is considered literate if he has ability to read and write in any language.

10. Assertion (A): Rapidly rising population adversely affects the quality of human capital.

Reason (R): Population reduces per head availability of the existing facilities relating to housing, sanitation, drainage, etc.

MULTIPLE CHOICE QUESTIONS

11. Both human capital and _____ are related to each other.

a) Human resource b) Human development c) Human being d) All of these

12. _____ refers to the produced means of production.

a) Human capital b) Human development c) Physical capital d) both a and c

13. Addition to the stock of capital can be done by

a) Expenditure on Education b) Expenditure on Health

c) Study Programme for adults d) All of these

14. Which cost is involved in Migration?

a) Transportation cost b) Higher Living cost in different place

c) Both a and b d) None of these

15. Problems in Human Capital Formation is

a) Low academic standards b) Brain Drain c) Rising population d) All of these

16. Which organization enforces the rules and regulations regarding technical education?

a) NCERT b) AICTE c) ICMR d) UGC

17. Education is important because

a) Expands mental horizon b) Develops human personality

c) Helps in economic development d) All of these

18. Which five-year plan recognizes the importance of human capital?

a) Second b) Fourth c) Seventh d) Eighth

19. Which institution is the primary funding authority for universities?

- a) NCERT b) AICTE c) ICMR d) UGC

20. Expenditure on health can be done in the form of: –

- a) Preventive Medicine b) Curative Medicine c) Social Medicine d) All of these

21. Which organization enforces the rules and regulations relating to education and research in health?

- a) NCERT b) AICTE c) ICMR d) UGC

22. There is a growing trend towards ____ of education, which makes it expensive for poor people.

- a) Socialization b) Privatization c) Both a and b d) None of these

23. The enrolment ratio of female students in schools is ____ and their drop- out ratio is ____

- a) High, Less b) Less, High c) Less, Less d) None of these

24. ____ capital is tangible and can be sold in the market.

- a) Human b) Physical c) Service d) None of these

25. ____ of human capital refers to the ways of adding to the stock of capital.

- a) Sources b) Determinants of physical capital
c) Both a and b d) None of these

26. ____ on health makes human more efficient and productive.

- a) Expenditure b) Investment c) Both a and b d) None of these

27. Human development is ____ of human welfare.

- a) A Parameter b) An Index c) An Attribute d) None of these

28. Expenditure on health makes a person more efficient and productive.

- a) True b) False

29. ____ creates public and private benefits. (Fill in the blank with correct alternative)

- a) Human Capital b) Physical capital c) Both (a) and (b) d) None of the above

30. Human capital treats human being as ____ (Fill in the blank with correct alternative)

- a) Separable elements b) Intangible elements c) Means to end d) As ends

31. ____ is based on the idea that education and health are integral to human beings. (Fill in the blank with correct option)

- a) Human capital b) Human development
c) Human capital formation d) None of the above

STATEMENT BASED QUESTIONS

Read the following statement given below and choose the correct alternative

- a) Both the statements are correct b) Both are statements incorrect
 c) Statement 1 is correct and statement 2 is incorrect
 d) Statement 1 is incorrect and statement 2 is correct

32. **Statement 1**- Education and health causes private benefits.

Statement 2- AICTE is the regulatory body for medical studies.

33. **Statement 1**- Percentage of education expenditure of total government expenditure indicates how much of people's income is committed to education in a country

Statement 2- Percentage of educational expenditure of GDP shows the importance of education in the government's scheme.

34. **Statement 1**- Migration involves cost of transportation and high cost of living

Statement 2- Education is the process of teaching, training and learning to improve knowledge

35. **Statement 1**- On the job training helps workers to acquire new specialized skills

Statement 2- On the job training takes place in the firm itself

36. **Statement 1**- The expenditure on education and health makes short term impact

Statement 2- The expenditure on education and health can be reversed

37. **Statement 1**- In India, there is gender biases in offering education to all

Statement 2- After 1991 reforms, there has been growing tendency towards privatization of education

ANSWERS

1. i. 1960 ii. Human capital iii. 5th iv. Economic Development

2. i. Non- Excludable and non-rivalrous in nature. ii. Both A and B iii. all of the above

3. a 4. B 5. C 6. C 7. A 8. A 9. B 10. a 11. b 12. c 13. d 14. C in economic development of India.

15. d 16. b 17. D 18. c 19. d 20. d 21. b 22. B 23. b 24. b 25. a

26. c 27. B 28. a 29. a 30. c 31. b 32. C 33. b 34. a 35. c 36. b 37. A

RURAL DEVELOPMENT

Rural development is a comprehensive term which focuses on action for the development of village economy.

Objectives of rural development:

1. Increasing productivity of agricultural sector.
2. Generating alternative means of livelihood in rural sector.
3. Promoting education and health facilities in the rural areas.

Key issues in rural development.

Land reforms

Development of human resources

Measures of poverty alleviation

Development of infrastructure

Credit facilities

Rural credit means credit for the farming communities for various purposes like purchasing agricultural tools and machines, digging wells and tube wells, purchasing seeds, fertilizers, pesticides, etc.

Sources of rural credit in India.

1. Non-institutional sources are money lenders, traders and commission agents, landlord, relatives and friends.
2. Institutional sources are as follow:
 - (i) Co-operative credit societies.
 - (ii) Commercial Banks
 - (iii) Regional Rural Banks
 - (iv) NABARD (National Bank for Agriculture and Rural Development.) (established in 1982)
 - (v) Self Help Groups (SHGs)

The above institutional structure of rural banking which is called multi-agency system which has initiated by govt. in 1969.

Agricultural marketing means all those activities which includes-gathering the produce after harvesting, processing the produce, grading the produce according to its quality, packaging the produce according to preferences of buyers, storing the produce for future sale and selling the produce when price is lucrative.

Defects of agricultural marketing

- (i) Inadequate warehouses
- (ii) Multiplicity of middlemen
- (iii) Malpractice in unregulated markets.
- (iv) Lack of Adequate finance
- (v) Inadequate means of transport and communication.

Measures adopted by the government to improve marketing system.

- (i) Regulation of markets.
- (ii) Co-operative agricultural marketing societies.
- (iii) Provision of warehousing facilities.
- (iv) Subsidised transport.
- (v) Dissemination of marketing information.
- (vi) Buffer stocks and minimum support price (MSP)
- (vii) Public Distribution System (PDS)
- (viii) Alternative marketing channels
- (ix) Improvement of physical Infrastructure

Diversification in agriculture activities-It has the two aspects.

1. **Diversification of crop production** refers to a system of multiple cropping rather than mono cropping.

2. Diversification of productive activities imply a shift from crop farming to non-farming areas of employment like animal husbandry, fisheries, Horticulture etc.

It has following advantages:

1. Reduce the risk from agriculture sector.
2. Provide ecological balance.
3. Provide sustainable livelihood option to people living in village.

Organic farming is a system of farming that maintains, enhances and restores the ecological balance. It helps in sustainable development of the agricultural sector, In organic farming, farmers use organic manure, bio fertilizers and organic pesticides.

Advantages of organic farming:

- (i) Inexpensive process.
- (ii) Generates income.
- (iii) Healthier and tastier food.
- (iv) Solves unemployment problem.
- (v) Environment friendly.

Limitation of Organic farming:

- (i) Yields from organic farming is less than modern agricultural farming in initial years.
- (ii) Organic produce have shorter shelf life than sprayed produce.
- (iii) Choice in production of off-season crops is quite limited in organic farming.

Organic farming involves labour-intensive process of production of labour so India has comparative advantage in organic farming.

Operation Flood

It is a system of milk co-operatives, launched in 1966. This system emphasised the pooling of milk by farmers through co-operatives societies.

Non-farm sector: It refers to jobs in govt. manufacturing, services, construction, mining, retail, etc.

Labour intensive Process: It refers to the process or industry that requires a large amount of labour.

1. Read the following statement given below and choose the correct alternative

Assertion (A)- Farmers cannot reach nearby markets to sell their products at fair prices

Reason (R)- There is lack of transportation in agricultural marketing

- a) Both assertion and reason are true. Reason is the correct explanation of assertion
- b) Both assertion and reason are true. Reason is not the correct explanation of assertion
- c) Assertion is true but reason is not
- d) Reason is true but assertion is not

2. What are the measures to improve agriculture marketing?

- a) Regulation of markets
- b) Provision of infrastructure
- c) Encouragement of cooperative marketing
- d) All of the above

3. What are the policy instruments to improve agriculture marketing?

- a) Public distribution system
- b) Minimum support price
- c) Both (a) and (b)
- d) None of the above

4. Read the following statement given below and choose the correct alternative

Assertion (A)- Livestock sector alone provides alternative livelihood options to over 70 million farmers in India.

Reason (R)- Livestock production provides increased income

- a) Both assertion and reason are true. Reason is the correct explanation of assertion
- b) Both assertion and reason are true. Reason is not the correct explanation of assertion
- c) Assertion is true but reason is not
- d) Reason is true but assertion is not

5. Choose the correctly matched pair from the following

Column A	Column B
A. Animal husbandry.	1. Organic farming
B. Food processing	2. IT sector
C. Use of animal manure	3. Diversification of agriculture
D. Dissemination of information	4. Dynamic sector

a) A- 3 b) B- 4 c) C- 2 d) D-1

6. Read the following statement given below and choose the correct alternative

Statement 1- TANWA project was initiated to train women in agricultural practices.

Statement 2- Dynamic sectors include agro- processing industries

- a) Both are correct b) Both are incorrect
c) Statement 1 is correct and statement 2 is incorrect
d) Statement 1 is incorrect and statement 2 is correct

7. _____ includes all these processes between harvesting and final sale of the produce by the farmers.

- a) Agricultural Marketing
b) Rural Marketing
c) Rural Agriculture
d) All of these

8. _____ refers to a situation when the farmers are compelled to sell the produce just after harvest even in low prices.

- a) Surplus sale
b) Distress sale
c) Commercial farming
d) None of these

9. Horticulture contributes ___ of value of agricultural output and ___ per cent GDP of India. a)

- Two-third,5
b) One-third,6
c) One-fourth,8
d) None of these

10. Rural development is a ___ term.

- a) Comprehensive c) Deceptive
b) Selective d) None of these

11. _____ is the apex body which coordinates the functioning of different financial institutions working for the expansion of rural credit.

- a) NABARD b) Self help groups c) Regional Rural Banks b) d) Commercial Banks

12. Which of the following is true about organic farming?

- a) Organically grown food is healthier and tastier
b) Yields in organic farming are lower than in chemical farming
c) it adversely affects the fertility of the soil.
d) it is quite expensive method of farming.

13. Which source of credit had emerged to fully integrate the formal credit system into the overall rural social and community development?

- a) Self – help Groups b) Regional Rural Banks
c) Commercial Banks d) Land Development Banks

14. Which among the following is a process that involves the assembling storage, processing, transportation, packaging, grading, and distribution of different agricultural commodities across the country?

- a) Agricultural Management b) Agricultural Banking
c) Agricultural Diversification d) Agricultural Marketing

15. Why is the minimum support price fixed by the government?

- a) For government own benefit b) To safeguard the interest of farmers
c) To safeguard the interest of consumers d) None of these

16. Read carefully and answer the following Case based question.

The central government will spend Rs. 9800 crores on livestock development over the next five years in a bid to leverage almost Rs. 55000 crores of outside investment into the Animal Husbandry Sector. It would do this by merging a slew of schemes of the Department of Animal Husbandry and Dairying into three main programmes, focused on indigenous cows and dairy development, livestock health and infrastructure development, an official statement said. The Cabinet Committee on Economic Affairs approved the implementation of the special livestock sector package by revising and realigning the various components of the existing schemes in order to boost growth and make animal husbandry more remunerative for the 10 crore farmers engaged in it.

(i) Livestock production provides ----- for the family without disrupting other food producing activities

- a) Increased stability in income b) food security c) transport and fuel d) all of these

(ii) The central bank undertakes to invest on livestock development in ----- ((a)horticulture/ (b)Animal husbandry) sector.

(iii) Livestock is _____

- a) Only Sheep b) Buffalo c) Goats d) All the above

17. Read carefully and answer the following Source based question.

The revolutionary, 'Billion-litre idea' and execution of the world's largest dairy-agricultural development programme, 'Operation Flood' transformed India from a nation with potential in the dairy industry to a nation with massive production of milk and dairy products.

Operation Flood is the programme initiated by the National Dairy Development Board to speed up "the White Revolution." It created a national milk grid linking producers throughout India with consumers in over 700 towns and cities, reducing seasonal and regional price variations while ensuring that the producer gets a major share of the price, consumers pay, by cutting out middlemen. The bedrock of Operation Flood that made the White Revolution a success, was village milk producers' cooperatives, which procured milk and provided inputs and services, making mode management and technology available to members. Mother dairy, AMUL dairy, Nandini, are some of the biggest dairies which provide milk and dairy products in India.

i. Operation Flood is an example of..... of productive activity in the rural areas.

- a) Centralization b) Diversification c) Both [a] and [b] d) None of the above

ii). Who is the father of White Revolution?

- a) Dr. Kurien c) Mr. Rajendra Singh b) Mr. Somnath Chatterjee d) Dr. Swaminathan

ii. Which is the biggest dairy in India?

- a) Mother dairy c) Vijaya dairy b) AMUL dairy d) None of the above

ANSWERS

1.a 2. D 3.c 4. B 5.a 6. A 7.a 8. B 9.a 10. b 11.a
 12. a 13. b 14. A 15. C 16.a 17. D 18.a 19. d 20.d 21. B 22.d
 23. i-a, ii-c, iii-d, iv-a 24. i-d, ii-b, iii-d 25. i-b, ii-a, iii-b

EMPLOYMENT: GROWTH INFORMALISATION AND OTHER ISSUES

Gist of the lesson

- Worker: A worker is an individual, who is involved in some productive activity, to earn a living.
- Economic Activity: An economic activity refers to the activity performed by people to earn the living. The main three types of economic activities are consumption, production and distribution.
- Production activity refers to all those activities which are under taken to produce goods and services for generation of income.
- Labor force: All persons, who are working (have a job) and those are not working but able to work and willing to work at the existing wage rate constitutes labor force.
 Labor Force: Persons working + persons seeking and/or available for work.
- Work force: The numbers of persons, who are actually employed at a particular time, are known as workforce. It includes all those persons who are actually engaged in productive activities. This includes person between age group of 15-60 years.
- Labor supply: It refers to various amount of labor that workers are willing to work, corresponding to a particular wage rate.
- Work Force Participation Rate (Ratio): - It is measured as the ratio between workforce and total population of a country.

Types of workers:

- (a) Self employed
- (b) Hired workers
 - i. Casual Workers
 - ii. Regular Workers (Salaried)

(a) Self Employed: - The workers who own and operate an enterprise to earn their livelihood are known as self-employed.

(b) Hired workers: - Those people who are hired by others and are paid wages or salaries as a reward for their services is called hired workers.

Casual Workers: - Those people, who are not hired by their employers on a regular/permanent basis and do not get social security benefits are said to be casual workers.

Regular Workers (Salaried): –

- When a worker is engaged by someone or by an enterprise and paid his or her wages on a regular basis, they are known to as regular salaried employees or regular workers.
- About two-fifth of the total population in the country is engaged in various economic activities.
- Men particularly rural men, form the major section of workforce in India.

- Majority of workers in India are self-employed, casual wage labourers and regular salaried employees' together account for less than half the proportion of India's workforce.
- About three fifth of India's workforce depends on agriculture and other allied activities as the major source of livelihood.
- Jobless Growth: It is defined as a situation where GDP grows faster than the employment opportunities resulting in unemployment.

Casualization and informalization of employment:

- ❖ Casualization refers to a situation when the percentage of casually hired workers in the total workforce tends to rise over time.

- ❖ **Formal sector**-formal sector refers to organized sector of the economy.

It includes all government departments, public enterprises and private establishments which hire 10 or more workers.

Those working in the organized sector are called formal workers.

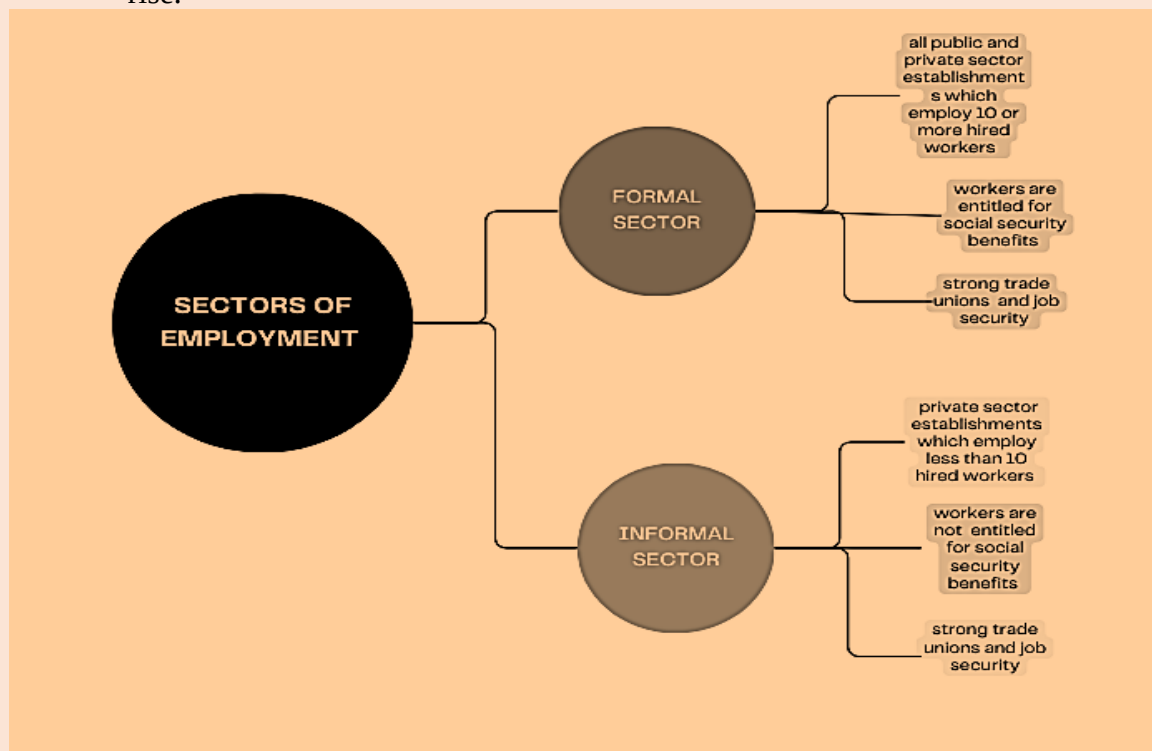
- ❖ **Informal sector**-

Informal sector refers to unorganized sector of the economy.

It includes all such private enterprises which hire less than 10 workers besides farming and self-employment ventures.

Those working in unorganized sector are called informal workers.

- ❖ **Informalization of workforce**- it is defined as a situation where percentage of workforce in the formal sector tends to decline and that in the informal sector tends to rise.



Unemployment:

- It is a situation where a person is ready and willing to work at the prevailing wage rate but doesn't get work.

Unemployment Rate:

It is calculated as percentage of labor force who are unemployed, not as percentage of total population.

Types of unemployment:**1. Rural unemployment**

- a. Seasonal Unemployment
- b. Disguised Unemployment

2. Other types of unemployment

- a. Open
- b. Frictional
- c. Structural
- d. Cyclical

3. Urban Unemployment

- a. Industrial Unemployment
- b. Educated Unemployment
- c. Technological Unemployment

- **Frictional unemployment:** it is defined as the unemployment that occurs because of people moving or changing occupations.
- **Structural unemployment:** it is defined as unemployment arising from technical change such as automation, or from changes in the composition of output due to variations in the types of products people demand. For example, a decline in the demand for typewriters would lead to structurally unemployed workers in the typewriter industry.
- **Cyclical unemployment:** it is defined as workers losing their jobs due to business cycle fluctuations in output, i.e. the normal up and down movements in the economy as it cycles through booms and recessions over time.
- **Open Unemployment:** it refers to that situation wherein the worker is willing to work and has the necessary ability to work yet he does not get work and remains unemployed for full time.
- **Seasonal Unemployment:** It refers to a situation where a number of people are not able to find a job in a particular season.
- **Disguised unemployment:** it is a kind of unemployment in which some people look like being employed but are actually not employed fully. This situation is also known as Hidden Unemployment. In such a situation more, people are engaged in a work than required. In other words, it refers to a situation of employment with surplus manpower in which some workers have zero marginal productivity. For example, in rural areas, this type of unemployment is generally found in agricultural sector.
- **Educated Unemployment:** - Among the educated people, apart from open unemployment, many are underemployed because their qualification does not match the job. Faulty education system, mass output, preference for white collar jobs, lack of employable skills and dwindling formal salaried jobs are mainly responsible for unemployment among educated youths in India. Educated unemployment may be either open or underemployment

Causes of unemployment:

- a. Slow rate of economic growth
- b. Population explosion
- c. underdeveloped agriculture
- d. Defective educational system
- e. Slow growth of Industry
- f. Decline of cottage and small industry.
- g. Faulty planning
- h. Inadequate employment planning.
- i. Low capital formation.
- j. Excessive use of Foreign Technology

- k. Lack of financial resources
- l. Increase in labor force

Remedial measures for unemployment:

- a. Accelerating growth rate of GDP
- b. Control of population growth
- c. Development to small scale enterprises.
- d. Encouragement in infrastructure.
- e. Special employment programs.
- f. Rapid industrialization.

Special programs to fight poverty and unemployment:

Most poverty alleviation programs implemented are based on the perspective of the Five-Year Plans. Expanding self-employment programs and wage employment programs are being considered as the major ways of addressing poverty. **Self-employment programs:** - (i) Rural Employment Generation Program (REGP), (ii) Prime Minister's Rozgar Yojana (PMRY) and Swarna Jayanti Shahari Rozgar Yojana (SJSRY) (iii) Swarnajayanti Gram Swarozgar Yojana (SGSY) (iv) National Rural Livelihoods Mission (NRLM). **Wage employment programs:** - (i) Mahatma Gandhi National Rural Employment Guarantee Act 2005. (MGNREGA): - The Parliament passed a new Act to provide guaranteed wage employment to every rural household whose adult volunteer is to do unskilled manual work for a minimum of 100 days in a year. (ii) Pradhan Mantri Gram Sadak Yojana, (iii) Pradhan Mantri Gramodaya Yojana, (iv) Valmiki Ambedkar Awas Yojana (v) Development of small and cottage industries (vi) Minimum needs program (vii) Twenty- point program (viii) Micro Units Development Refinance Agency Bank (MUDRA BANK) Government has set up MUDRA Bank in April 2015. Its objective is to meet credit needs of micro enterprise and self- employed persons. Under MUDRA yojana, a micro enterprise is entitled for a loan up to Rs. 10 lakh per unit.

QUESTION-ANSWERS

1MARK QUESTIONS

1. A situation in which growth rate in GDP in the economy is not accompanied by commensurate growth in Employment opportunities is called as

- A. unemployment
- B. Informalization of work force
- C Jobless Growth.
- D. Sustainable growth

Ans: jobless growth

2. Workers who are on permanent pay-roll of their employer are called:

- (A) Self- employed workers
- (B) Casual workers
- (C) Regular workers
- (D) None of the above

Ans: regular workers

3. Unemployment is defined as:

- (A) The section of the population that is not capable of being employed
 - (B) The section of population willing to work but unable to find employment
 - (C) The section of population that is waiting to be employed
 - (D) The section of population that are without the skills needed by employers
- Ans: The section of population willing to work but unable to find employment

4. Data on unemployment in India can be obtained from which source?

- (A) Reports of Census of India
- (B) National sample survey organization (NSSO)
- (C) Directorate general of employment
- (D) All the above

Ans: All the above

5. When more persons are working in a job than actually required, it is known as _____.

- (A) Disguised unemployment
- (B) Seasonal unemployment
- (C) Educated unemployment
- (D) Open unemployment

Ans: Disguised unemployment

6. Those who work in their own establishment using their own resources are called _____.

- (A) Hired workers
- (B) Casual workers
- (C) Regular workers
- (D) Self-employed

Ans: Self-employed

CASE-BASED QUESTION:

Year 2020 began with the once-in-a-century pandemic, which saw the frontline workers working tirelessly to save human lives from COVID-19. The pandemic caused its ripples on the economy and on social sectors. Governments, at all levels, intervened in a timely manner to respond to the pandemic.

India has one of the lowest case fatalities rates of less than 1.5%. India has been able to save lakhs of lives through its effective policy responses. Public spending on social sector was increased in 2020 – 21 to mitigate the hardships caused by the pandemic and the loss to livelihood due to the lockdown.

The lockdown period saw the growth of the 'gig economy' and increasing 'work from home' in the organised sector. As per the Periodic Labour Force Survey (PLFS) report 2018 – 19, there was an increase in workforce totalling 48.78 crores in 2018 – 19 as compared to 47.14 crores during 2017 – 18. Out of 1.64 crores increased workforce, 1.22 crores were in rural sector and 0.42 crores in urban sector.

The female labour force participation rate increased from 17.5% in 2017 – 18 to 18.6% in 2018 – 19. The net payroll data of Employees' Provident Fund Organisation (EPFO) as on 20th December, 2020 shows a net increase of new subscribers of 78.58 lakhs in 2019 – 20 as compared to 61.1 lakhs in 2018 – 19. The PLFS report also showed improvement in 2020 – 21 (Quarter 4) when compared to 2019 – 20 (Quarter 4).

Considering the proportion of the male workforce, casual labour decreased by 1% points, while self-employed and salaried workers increased by 0.6% points and 0.4% points respectively. Similarly, in case of female workforce, self-employed increased by 2% points, regular/wage salaried workers decreased by 0.7% points and casual labour decreased by 1.4% points.

Source : Economic Survey 2020 – 21, Volume II, Chapter 10 (excerpt)

Q1(a). Analyze the nature/ distribution of Indian workforce for the fourth quarter of the year 2020-21. (2 Marks)

Ans. In the quarter of the year 2020-21, as per the given text, the total casual labor employment has decreased. Also, the said period saw a growth in the economy and increase in the work from home in the organized sector.

Q1 (b): State and discuss any two initiatives taken by the Government to control the adverse impacts of the pandemic. (3 Marks)

Ans. Two initiatives taken by the government to control the adverse impact of pandemic.

- (i) Imposition of Lockdown to save human lives.
- (ii) Increase in Public spending (any other argument with valid explanation)

3- & 4-MARKS QUESTIONS

1. Distinguish between formal and informal sector employment.

FORMAL SECTOR	INFORMAL SECTOR
1. All public and private sector establishments which employ 10 or more hired workers comprise the formal sector.	All establishments which employ less than 10 workers employ comprise the informal sector
2. Government exercises control over this sector by passing necessary acts and formulating rules and regulations.	2. Government has no control over this sector. Except for the Minimum Wages Act, no other act is applicable on this sector
3. Workers working in this sector are entitled to social security benefits.	3. Workers working in this sector are not entitled to social security benefits.

2. Briefly explain about jobless growth?

ANS: Jobless growth is an economic phenomenon in which an economy experiences growth without reducing unemployment or we can say with decreasing the level of employment. The term Jobless growth was coined by the Economist Nick Perna in early 1990s'. Situation of 'jobless growth' arises due to various reasons. Sometimes increased productivity through automation allow economic growth with decrease in employment. Many times, it also arises when economy experiences structural changes. Besides growing population may be another reason for this situation.

6 MARKS QUESTIONS

1. Explain the different types of unemployment.

ANS: Unemployment: It is a situation where a person is ready and willing to work at the prevailing wage-rate but doesn't get work.

Types of unemployment:

1. Rural unemployment
 - a. Seasonal Unemployment
 - b. Disguised Unemployment
2. Other types of unemployment
 - a. Open
 - b. Frictional
 - c. Structural
 - d. Cyclical
3. Urban Unemployment

- a. Industrial Unemployment
- b. Educated Unemployment
- c. Technological Unemployment

Rural unemployment: It refers to non-availability of employment in rural areas.

Seasonal Unemployment: - It refers to a situation where a number of people are not able to find a job in a particular season.

Disguised unemployment: is a kind of unemployment in which some people look like being employed but are actually not employed fully. This situation is also known as Hidden Unemployment. In such a situation more, people are engaged in a work than required. In other words it refers to a situation of employment with surplus manpower in which some workers have zero marginal productivity. For example, in rural areas, this type of unemployment is generally found in agricultural sector. Frictional unemployment is defined as the unemployment that occurs because of people moving or changing occupations.

Structural unemployment: is defined as unemployment arising from technical change such as automation, or from changes in the composition of output due to variations in the types of products people demand. For example, a decline in the demand for typewriters would lead to structurally unemployed workers in the typewriter industry.

Cyclical unemployment: it is defined as workers losing their jobs due to business cycle fluctuations in output, i.e. the normal up and down movements in the economy as it cycles through booms and recessions over time.

Open Unemployment: refers to that situation wherein the worker is willing to work and has the necessary ability to work yet he does not get work and remains unemployed for full time.

Educated Unemployment: - Among the educated people, apart from open unemployment, many are underemployed because their qualification does not match the job. Faulty education system, mass output, preference for white collar jobs, lack of employable skills and dwindling formal salaried jobs are mainly responsible for unemployment among educated youths in India. Educated unemployment may be either open or underemployment.

Technological Unemployment: This type of unemployment takes place every time technology upgrades and the existing workforce are unable to cope with the new technology. If the skills required to meet the new technology do not match the existing skill-sets of the employed workers and they cannot adapt, they become unemployed. Up gradation is a natural process, with cyclical obsolescence as one set of technology becomes irrelevant and gets replaced by another.

Industrial Unemployment: Unemployment among industrial labor has assumed alarming proportion as the modern industrial development based on latest capital-intensive technology has not been able to absorb the ever-increasing labor force. Lakhs of people pour into cities every year from the distant rural places in search of jobs and better living standards. But the slow growth of industry and the fixed capital coefficient in the modern industrial sector make it impossible to provide jobs to the migrated labor force. This causes widespread unemployment among the industrial workers.

2. Explain the reasons for unemployment along with remedies for it.

ANS: Unemployment: It is a situation where a person is ready and willing to work at the prevailing wage-rate but doesn't get work.

Causes of unemployment:

- Slow rate of economic growth: slow rate of economic growth leads to slow growth of job opportunity for rising population which in turn causes increase in unemployment.
- Population explosion: Constant increase in population has been a big problem in India. It is one of the main causes of unemployment as number of people demanding job exceeds the number of job available at a particular time.
- Underdeveloped agriculture: Agriculture is underdeveloped in India. It provides seasonal

employment. Large part of population is dependent on agriculture. But agriculture being seasonal provides work for a few months. So, this gives rise to unemployment

- Defective educational system: The number of universities and educational institutions has increased manifold. But the education system prevailed in these institutions are not as per the requirement of industries and society. This causes rise in educational unemployment in India
- Slow growth of Industry: The rate of industrial growth is slow. Though emphasis is laid on industrialization yet the avenues of employment created by industrialization are very few.
- Decline of cottage and small industry: The industrial development had adverse effect on cottage and small industries. The production of cottage industries began to fall and many artisans became unemployed.
- Faulty planning: Defective planning is the one of the causes of unemployment. There is wide gap between supply and demand for labor. No Plan had formulated any long-term scheme for removal of unemployment.
- Low capital formation. The major cause of unemployment and underemployment in underdeveloped countries like India is the deficiency of the stock of capital in relation to the needs of the growing labor force. With the growth of technology and specialization, he needs much more capital with which to engage in the productive activity. if the working force grows faster than the stock of capital of a country, the entire addition of labor force cannot be absorbed in productive employment because not enough instruments of production would be there to employ them. The resulting unemployment is known as the long-term or chronic unemployment.
- Excessive use of Foreign Technology: An important factor responsible for slow growth of employment has been the use of capital-intensive techniques of production. Foreign technology is based on capital intensity. Private sector prefers to invest in highly capital-intensive plants and equipment on the basis of technology developed in labor-scarce western countries. It is argued by them that the alternative labor-intensive techniques have low productivity and low surplus-generating capacity. Capital intensive foreign technology has replaced the labor force by machines in performing various activities and hence has retards the opportunity of employment generation.

Remedial measures for unemployment:

- Accelerating growth rate of GDP: increase in growth rate of GDP leads to increase in employment opportunity, which reduces unemployment.
- Control of population growth: The growth of population should be checked in order to solve unemployment, problem. Family planning program should be implemented widely and effectively. So that the demand and supply mismatch of labor force can be minimized.
- Development to small scale enterprises: In the Indian context, cottage and household industries which are often associated with agriculture play a vital role in the development of economy. Hence, they should be given due encouragement. Basket making, brick-making, toy-making, agarbati making, carpentry and furniture making, leather works, carving, smothery, and such other works are to be encouraged to keep our people engaged with work that fetch economic rewards.

Special employment programs: Depending upon the local needs and feasibility new agricultural programs and projects are to be launched so that the young people of the area get new opportunities to use their talents and energy for the developmental programs.

Rapid industrialization:

- Planned development of industries is essential for creating more and more job opportunities.
- Development of industries may include:
 - (a) large-scale industries,
 - (b) small scale industries, and
 - (c) Village and cottage industries including handicrafts.
- Proper balance should be maintained between agricultural growth and industrial

development, so that industry would not destroy handicrafts and household industries.

- The unchecked process of mechanization and the domination of multinational companies are adversely affecting the creation of new job opportunities.
- In the name of industrial growth new labor-saving machine are installed which are taking away the jobs of men.
- Gandhi had opposed the process of mechanization in this regard.
- Sufficient care should be taken to see no new machine takes away the jobs of existing workers.
- The process of economic liberalization let loose by the central government recently has given new scope for the multinational companies to establish their domination over the indigenous industries.
- The governmental invitation for these companies may erode the job opportunities for millions of people.
- Educational reforms: The present education system needs a thorough overall check to meet the changing pattern of demand not only through re-orientation but also by diversifying the courses in the field of commerce, trade, banking, insurance, technical and managerial personnel so that the adjustments of demand and labor in various occupations become easy

Promoting self -employment: Self-employment schemes for the unemployed youth have to be launched to enable them to start their own business or small-scale firm, which can also generate employment for many others.

- Special programs to fight poverty and unemployment:
- Mahatma Gandhi National Rural Employment Guarantee Act (MNREGA)
- It's a significant recent attempt of government offering guaranteed employment to those in the rural areas who are below poverty line.

ENVIRONMENT AND SUSTAINABLE DEVELOPMENT

INTRODUCTION: -

❖ Since independence, India has launched a number of economic plans, to attain economics development at a quicker pace. However, the economic development that we have achieved so far has come at a very heavy price- at the cost of environment quality.

❖ Liberalization, Privatization and Globalization (LPG) have resulted in the development of the economy, but with the adverse consequences on our environment. So, we have to bear in mind to adverse consequences of the past development path on our environment and consciously choose a path of sustainable development.

MEANING OF ENVIRONMENT

Environment is defined as the total planetary inheritance and the totality of all resources.

- Environment is the sum total of external forces which surround us.
- It includes all the biotic factors that influence each other.
- Biotic element: -Biotic elements include all living element like birds, humans and plants, forests, fisheries, etc.
- Abiotic Elements: -Abiotic elements include non- living element like air, water, land, etc.

FUNCTIONS OF THE ENVIRONMENT

The environment performs four vital functions:

- i. Provides resources for production
- ii. Environment assimilates waste

- iii. Environment sustains life
- iv. It provides aesthetic services

REASONS FOR ENVIRONMENTAL CRISIS:

- i. Population explosion and advent of industrial revolution
- ii. Intensive and extensive extraction of both renewal and non-renewal resources.
- iv. Extinction of many resources.
- iv. Affluent consumption and production standards of the developed world.
- v. Development process has polluted the atmosphere and has resulted in increased incidence of respiratory and water –borne diseases.
- vi. Global environmental issues such as global warming and ozone depletion.

GLOBAL WARMING

It is the observed and projected increase in the average temperature of the earth's atmosphere and oceans. The global warming is due to increase in the greenhouse gas concentrations, like water vapor, carbon dioxide, Methane and ozone in the atmosphere.

OZONE DEPLETION

It refers to destruction of ozone in the ozone layer due to presence of chlorine from manmade chlorofluorocarbons (CFCs) and other forces. It is caused by high level of chlorine and bromine compounds in the stratosphere.

MONTREAL PROTOCOL

It is a historical treaty designed by the members of united nations to protect the ozone layer by phasing out CFC, which is supposed to be the main reason for ozone depletion. Under the Montreal protocol, all the signing members agreed to freeze the consumption and production of CFC by the year 2013.

CHALLENGES TO INDIA'S ENVIRONMENT

Air pollution, water contamination, soil erosion, deforestation and wildlife extinction are some of the most pressing environmental concerns of India. The priority issues identified are:

- i. Land degradation
- ii. Degradation of forest or deforestation
- iii. Soil erosion
- iv. Biodiversity loss
- v. Air pollution

LAND DEGRADATION

Refers to decline in the overall quality of soil, water or vegetation condition, commonly caused by human activities.

DEGRADATION OF FORESTS OR DEFORESTATION

Involves the permanent destruction of indigenous forest and woodlands.

SOIL EROSION

Takes place when the surface soil is washed away through excessive rains and floods.

BIODIVERSITY LOSS:

Biodiversity defined as the variability among living organisms from all sources.

Biodiversity loss has serious economic and social costs for any country as many plant and animal species are severely threatened by the destruction of their habitat and over

exploitation of resources.

AIR POLLUTION

Is the presence of materials in air in such concentration, which are harmful to humans and the environment.

SUSTAINABLE DEVELOPMENT

It is the development, which will allow all future generation to have a potential average quality of life, that is, at least as high, which is being enjoyed by the current generation.

WAYS TO ACHIEVE SUSTAINABLE DEVELOPMENT

Restrict use of renewable resources
 Substitute non-renewable with renewable resources
 Become input efficient
 Control pollution
 Control the growth of population

STRATEGIES FOR SUSTAINABLE DEVELOPMENT

Use of non- conventional sources of energy
 Use of cleaner fuels
 Establishment of mini-hydel plants
 Traditional knowledge and practices
 Use of Bio compost
 Control of Bio pest
 Change in unsustainable patterns of consumption and production

CONCEPTS OF

A) CARRYING CAPACITY

B) ABSORPTIVE CAPACITY

A) Carrying capacity of the environment implies that the resources extraction is not above the rate of regeneration of the resources and the wastes generated are within the assimilating capacity of the environment.

B) Absorptive capacity means the ability of the environment to absorb degradation.

VERY SHORT TYPE QUESTIONS (1 Mark)

REASONING AND ASSERTION BASED

1. Read the following statements: Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): Sustainable development is essential for the economic growth of the country.

Reason (R): Sustainable development ensures that environment-friendly measures are adopted for carrying out the production process.

Alternatives:

- a) Both Assertion and Reason are true and Reason (R) is the correct explanation of Assertion (A)
- b) Both Assertion and Reason are true and Reason (R) is not the correct explanation of Assertion (A)

- c) Assertion (A) is True but Reason (R) is False
- d) Assertion (A) is False but Reason (R) is True

Ans – a)

2. Read the following statements: Assertion (A) and Reason (R). Choose one of the correct alternatives given below:

Assertion (A): Non-renewable resources are abundant in nature.

Reason (R): Non-renewable resources will get exhausted after several years of usage.

Alternatives:

- a) Both Assertion and Reason are true and Reason (R) is the correct explanation of Assertion (A)
- b) Both Assertion and Reason are true and Reason (R) is not the correct explanation of Assertion (A)
- c) Assertion (A) is True but Reason (R) is False
- d) Assertion (A) is False but Reason (R) is True

Ans – d)

3.Alternatives:

- (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A)
- (b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A)
- (c) Assertion (A) is true but Reason (R) is false.
- (d) Assertion (A) is false but Reason (R) is true.

4.ASSERTION (A): The environment fails to perform its vital function of life sustenance and this results in an environmental crisis.

REASON (R): Many resources have become extinct and the wastes generated are beyond the absorptive capacity of environment.

Ans: (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A)

5.ASSERTION (A): The environment has an important function of supplying resources, both renewable and non-renewable resources.

REASON (R): The environment is able to perform its functions as long as the demand on these functions is within its carrying capacity.

Ans: (b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A)

6. ASSERTION (A): Sustainable development is the development that meets the need of present generation without compromising the ability of the future generations to meet their own needs.

REASON (R): Conservation and promotion of natural resources.

Ans: (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A)

7. ASSERTION (A): Environmental degradation owes a great deal to supply demand reversal of resources over time.

REASONING (R): Global warming is wake up call to save environment.

Ans: (b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A)

8. ASSERTION (A): Deforestation is rising at such a rapid scale that it has totally disturbed the ecological balance of the country.

REASON (R): Deforestation is one of the major reasons for soil erosion.

Ans: (b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A)

MCOs/BRIEF ANSWER

1. Which of the following statements is correct about achieving sustainable development? a) Sustainable development can be achieved by restricting the usage of renewable resources
b) Sustainable development can be achieved by controlling the growth rate of world's population
c) Sustainable development can be achieved by controlling the menace of pollution
d) All of the above

Answer: d

2. What is meant by biodiversity?

Ans. Biodiversity is defined as the variability among living organisms from all sources, including terrestrial marine and another aquatic ecosystem and the ecological complexes of which they are a part.

3. State the two major environmental issues that the world is facing today.

Ans. 1. Depletion of natural resources; 2. Environmental degradation

SHORT ANSWER TYPE QUESTION (3-4 MARKS)

1. What are the functions of the environment?

Ans. The environment performs four vital functions:

- a. Environment supplies resource
- b. Environment sustain life
- c. Environment Assimilates waste
- d. Environment enhance quality of life

2. Mention the strategies for sustainable development.

Ans. The strategies are: -

- Use of non – conventional sources of energy
- Encouraging use of cleaner fuel
- Setting mini hydel plants
- Using traditional practices
- Bio composting
- Bio-pest control

3. Explain how the opportunity costs of negative environmental impacts are high.

Ans. Opportunity cost is the cost of alternative opportunity give up. The country has to pay huge amount for damages done to human health. The health cost due to degraded environmental quality has resulted in diseases like asthma, cholera, etc. Huge expenditure is incurred in treating the diseases.

4. Is environmental crisis are recent phenomenon? If so, why?

Ans. Yes, because India is suffering from population explosion.

- a. India has approximately 20% of livestock population on a mere 2.5 % of the world's geographical area. The high density of population and livestock and the completing uses of land forestry, agriculture, pastures, human settlements and industries exert an enormous pressure on country's finite land resources.
- b. The per capita forestland in the country is only 0.08 hectare. There is an excess felling of about 15 million cubic matter forest over the permissible limit. Indiscriminate felling of trees has led to destruction of forest cover.

LONG ANSWER TYPES QUESTION (6 MARKS)

1. Identify six factors contributing to land degradation in India

Ans.

- (i). Loose of vegetation due to deforestation.
- (ii). Overgrazing i.e. grazing of natural pastures at stocking intensities above the livestock carrying capacity.
- (iii). Encroachment into forest lands.
- (iv). Non-adoption of adequate soil conservation measures.
- (v). Unsustainable fuel wood and fodder extraction.
- (vi). Improper crop rotation.

2. 'India has abundant natural resources. Substantiate the statement.

- Ans. The black soil of Deccan plateau is particularly suitable for civilization of cotton leading industries in the region.
- The Indo-Gangetic plains from the Arabian sea to the Bay of Bengal are one of the most fertile intensively cultivated and density populated region in the world.
- India's forest though unevenly distributed, provide green cover for a majority of its population and natural cover for its wildlife.
- Large deposits of iron-ore, coal and natural gas are found in the country. India alone accounts for nearly 20% of the world's total iron-ore reserves.
- Bauxite, copper, chromite, diamonds, gold, lead, lignite, manganese, zinc, uranium, etc. are also available in different parts of country

UNIT 8: COMPARATIVE DEVELOPMENT EXPERIENCE OF INDIA AND ITS NEIGHBOURS

INTRODUCTION

Over the last two decades or so, the economic transformation that is taking place in different countries across the world, partly because of the process of globalization, has both short as well as long term implication for each country, India, China and Pakistan. Nations have been primarily trying to adopt various means which will strengthen their own domestic economies. To this effect they are forming regional and global economic grouping such as SAARC, European Union, ASEAN, G-8, G-20, BRICS etc. In addition, there is also an increasing eagerness on the parts of various nations to try and understand the developmental process pursued by their neighbouring nations as it allows them to better comprehend their own strengths and weaknesses vis- a- vis their neighbours.

SIMILARITIES IN THE DEVELOPMENT STRATEGIES OF INDIA, CHINA, PAKISTAN.

- 1) All the three countries started their development path at the same time. India and Pakistan got independence in 1947 and people's Republic of China was established in 1949.
- 2) All the three countries had started planning their development strategies in similar ways. India announced its First Five-Year Plan in 1951, Pakistan announced in 1956 and China in 1953.

- 3) India and Pakistan adopted similar strategies, such as creating a large public sector and raising public expenditure on social development.
- 4) Both India and Pakistan had adopted 'mixed economy' model but China had adopted 'Command Economy' model of economic growth.
- 5) Till 1980s, all the three countries had similar growth rates and per capita incomes.
- 6) Economic Reforms were implemented in China in 1978, in Pakistan in 1988 and in India in 1991.

DEVELOPMENT STRATEGIES OF INDIA

- 1) Sound Trade System:** India was the country which had the history of closed trade. Because of this historical background; there is a critical challenge for India to make a new policy which can support the new trade system. This new reform has been introduced in the economy of India and accelerates the growth of India.
- 2) Reduction in Poverty:** India has adopted several poverty alleviations programs to reduce poverty in India. This would help in increasing per capita income, rise in nutrition levels and reduction of poor in some states.
- 3) Rural Development:** Under this strategy, India adopted various measures of development of areas that are lagging in the overall development of village economy.
- 4) Employment Generation:** Several economic reforms were initiated to generate employment in the country and their aim is to provide gainful self-employment and skilled wage employment opportunities.

ECONOMIC DEVELOPMENT STRATEGY AFTER INDEPENDENCE-(INDIA)

- 1) Both public and private sectors were allotted to carry business activities. Public sector was allotted activities like coal, mining, steel, power, roads etc. Private sector was allotted to establish industries subject to control and regulations in the form of law.
- 2) Public sector was given major push by the Government. Maximum revenues in this sector was invested which increased from Rs. 81.1 crore in First Five-Year Plan (1951-56) to Rs 34,206 crores in Ninth Five-Year Plan (1992-97).
- 3) Public sector was given importance to eliminate poverty, unemployment etc.
- 4) Public sector contributed to the industrialisation of the economy. It also helped Indian economy to achieve a considerable degree of self-sufficiency.

DEVELOPMENT STRATEGIES OF CHINA

- 1) Great Leap Forward Campaign (1958):** This Campaign was started in 1958 aimed at industrializing the country on a massive scale. People were encouraged to set up massive industries in their backyards.
- 2) Commune System:** Under the commune system, people collectively cultivated lands. In 1958, there were 26000 communes covering almost all the farm population
- 3) Great Proletarian Cultural Revolution (1966-1976):** In 1965, Mao Se Tung introduced the Great Proletarian Revolution under which students and professionals were sent to work and learn from the countryside.

- 4) **Economic Reforms in China 1978:** In 1978, China began to introduce many reforms in phases.

Initial Phase- Reforms were initiated in agriculture, foreign trade and investment sectors.

Later Phase- Reforms were initiated in the industrial sector. The goal of Chinese economic reforms were to generate sufficient surplus the finance the modernisation of mainland Chinese economy.

- 5) **Concept of “Dual pricing”:** This means fixing the prices in two ways; farmers and industrial units required to buy and sell fixed quantities of inputs and outputs on the basis of prices fixed by the government and rest were purchased and sold at market prices.
- 6) **Special Economic zones (SEZs):** In order to attract foreign investments and technology, Special Economic Zones (SEZs).

DEVELOPMENT STRATEGIES OF PAKISTAN

1. **Mixed Economy:** Pakistan follows a mixed economy system where both public and private sector co-exists.
2. **Import Substitution:** Pakistan adopted a regulatory framework in the late 1950s and 1960s for import industrialization. The policy combined tariff protection for manufacturing of consumer goods together with direct import controls on competing imports.
3. **Green Revolution:** This was introduced to increase the productivity and self-sufficiency in food. This increased the output of food grains. This changed the agrarian system dramatically.
4. **Nationalization of capital goods industries:** In the 1970s, nationalization of capital goods industries took place. During this period, Pakistan also received financial support from western nations and remittances from continuously increasing outflow of emigrants to the middle east.
5. In 1988 **economic reforms** were initiated in the country.

COMPARATIVE STUDY – INDIA, PAKISTAN, AND CHINA:

- 1) The population of Pakistan is very small and accounts for roughly about one-tenth of China and India.
- 2) Though China is the largest nation geographically among the three, its density is the lowest.
- 3) Population growth is highest in Pakistan followed by India and China. One child norm which was introduced in China in the late 1970s is the major reason for low population growth. But this measure led to a decline in the sex ratio, that is the proportion of females per 1000 males.
- 4) The sex ratio is low and biased against females in all the three countries. There is strong son preference prevailing in all these countries.
- 5) The Fertility rate is low in China and very high in Pakistan.
- 6) Urbanisation is high in both China and Pakistan- with India having 28 percent of its people living in Urban areas.

DEMOGRAPHIC INDICATORS

Country	Estimated Population (in million) (2015)	Annual Growth of Population (2015)	Density (per sq. km)	Sex Ratio (2015)	Fertility Rate (2015)	Urbanisation (2015)
India	1311	1.2	441	929	2.3	33
China	1371	0.5	146	941	1.6	56
Pakistan	188	2.1	245	947	3.7	39

Source: World Development Indicators 2017, www.worldbank.org

(1) Size of population- (a) China has the highest population closely followed by India. India and China together are a habitat for 38% of the world's population.

(b) China with nearly 1371 million (2015) is a habitat for nearly 20 % of world population

(c) India with nearly 1311million people (2015) is a habitat for nearly 18% of world population.

(d) The population of Pakistan is very small and accounts for roughly about one- tenth of China or India.

(2) Growth rate of population- (a) The population growth is the highest in Pakistan followed by India and China.

(b) One Child Norm introduced in China in the late 1970s is the major reason for low population growth.

(c) The trend of growth rate tells that the population of India would exceed China soon.

(3) Density of Population- It is estimated to be 148 persons per square kilometer in China 275 per sq.km in Pakistan, and 455 persons per sq.km in India.

(4) Sex Ratio- The sex ratio is low and biased against females in all three countries 'preference for son' prevailing in all these countries is the reason for low sex ratio

(5) Urbanization- In India 34% of population is urbanized compared with 37% in Pakistan and 59% in China.

Note- One child norm and resultant arrest in growth of population also have other implications. For instance, after a few decades, in China there will be more elderly people in proportion to young people. This led to allowing couples to have two children from 2016 and allowing three children from 2021

GROWTH RATE OF GROSS DOMESTIC PRODUCT (GDP)

Annual Growth of Gross Domestic Product (%), 1980-2017		
Country	1980-90	2015-2017
India	5.7	7.3
China	10.3	6.8
Pakistan	6.3	5.3

Source: Key Indicators for Asia and Pacific 2016, Asian Development Bank, Philippines; World Development Indicators 2018

- China has the second largest GDP of 19.8 trillion dollars. India's GDP is 8.07 trillion dollars. Pakistan's GDP is 0.94 trillion dollars.

- In the 1980s Pakistan was ahead of India, China was having double digit growth and India was at the bottom.
- In 2011-15 there has been decline in China's growth rates, whereas, Pakistan met with drastic decline at 4 percent. Some scholars hold the reform processes introduced in 1988 in Pakistan and political instability over a long period as reasons behind the trend.

SECTORAL CONTRIBUTION TOWARDS GDP & SECTORAL SHARE OF EMPLOYMENT

Sectoral Share of Employment and GDP (%) in 2015-2017						
Sector	Contribution to GDP			Distribution of Workforce		
	India	China	Pakistan	India	China	Pakistan
Agriculture	17	9	25	42.7	17.5	42
Industry	30	43	21	23.8	26.5	3.7
Services	53	48	54	33.5	56	54.3
Total	100	100	100	100	100	100

Source: Human Development Report 2018 ; Key Indicators of Asia and Pacific 2016.

- In both India and Pakistan, the contribution of agriculture to GDP was 17 and 25 per cent, respectively, but the proportion of workforce that works in this sector is more in India. In Pakistan, about 42 per cent of people work in agriculture, whereas in India, it is 43 per cent.
- The sectoral share of output and employment also shows that in all three economies, the industry and service sector have less proportion of workforce but contribute more in terms of output.
- In China manufacturing and service sector which contribute the highest to GDP at 43 and 48 per cent respectively whereas in India and Pakistan, it is the service sector which contributes the highest by more than 50 per cent of GDP
- The contribution of industries to GDP is at 30 per cent in India and 21 per cent in Pakistan.

HUMAN DEVELOPMENT INDEX

- China is moving ahead of India and Pakistan. This is true for many indicators of human development-

(1) **Income indicators** such as GDP per capita, proportion of population below poverty line.

(2) **Health indicators** such as mortality rates, access to sanitation, adult literacy rate, life expectancy, malnourishment

- Pakistan is ahead of India in reducing proportion of people below the poverty line and also its performance in sanitation.
- Neither of these two countries- India and Pakistan- have been able to save women from maternal mortality.
- In China, for one lakh births, only 27 women die whereas in India and Pakistan, about 178 and 174 women die respectively.

(3) **Liberty Indicators-** Liberty indicators are those indicators which represent the degree of social and political freedom to individuals in a country

Examples- A measure of the extent of democratic participation in social and political decision making. A measure of the extent of constitutional protection given to rights of citizen A measure of the extent of constitutional protection of the independence of the judiciary and the Rule of Law

Some Selected Indicators of Human Development, 2016–2017

<i>Item</i>	<i>India</i>	<i>China</i>	<i>Pakistan</i>
Human Development Index (Value)	0.640	0.752	0.562
Rank (based on HDI)	130	86	150
Life Expectancy at Birth (years)	68.8	76.4	66.6
Mean years of Schooling (% aged 15 and above)	6.4	7.8	8.6
GDP per capita (PPP US\$)	6,427	15,309	5,035
People Below Poverty Line (at \$3.20 a day ppp) (%) (2011)	60.4	23.5	46.4
Infant Mortality Rate (per 1000 live births)	34.6	8.5	64.2
Maternal Mortality Rate (per 1 lakh births)	174	27	178
Population using Improved Sanitation (%)	44.2	75	58.3
Population with Sustainable Access to improved Water Source (%)	94	96	91
Percentage of Undernourished Children	37.9	8.1	46.4

Source: Human Development Report 2018 and World Development Indicators (www.worldbank.org).

DEVELOPMENT STRATEGIES — AN APPRAISAL

CHINA

China introduced reforms in 1978 to address the slow pace of economic growth. They felt that Maoist vision of economic development based on decentralization, self-sufficiency and shunning of foreign technology, goods and capital had failed. Various factors that led to the rapid growth in economic development in China

- Establishment of infrastructure in the areas of education and health, land reforms, long existence of decentralized planning and existence of small enterprises helped positively in improving the social and income indicators in the post reform period.
- Through the commune system, there was more equitable distribution of food grains. Each reform measure was first implemented at a smaller level and then extended on a massive scale
- The experimentation under decentralized government created favorable condition for agriculture. It created conditions for subsequent phenomenal growth in rural industries and built up a strong support base for more reforms.

PAKISTAN:

Pakistan Reasons for the slow growth and re-emergence of poverty in Pakistan

- Agricultural growth and food supply situation were based not on an institutionalized process of technical change but on good harvest. When there was a good harvest, the economy was in good condition, when it was not, the economic indicators showed stagnation or negative trends
- If a country is able to build up its foreign exchange earnings by sustainable export of manufactured goods, it need not worry. In Pakistan most foreign exchange earnings came from

remittances from Pakistani workers in the Middle –east and the exports of highly volatile agricultural products.

- There was also growing dependence on foreign loans on the one hand and increasing difficulty in paying back the loans on the other.

CONCLUSION:

INDIA

- Indian economy performed moderately, but majority of its people still depend on agriculture.
- Many initiatives to develop the infrastructure and improve the standard of living.
- It is yet to raise the level of more than one-fourth of its population that lives below the poverty line.

PAKISTAN

Pakistan has performed poorly. The reasons for the slowdown of growth and reemergence of poverty in Pakistan's economy are

1. Political instability.
2. Volatile performance of agriculture sector.
3. Over dependence on remittances.
4. Growing dependence on foreign loans on the one hand and increasing difficulty in paying back the loans on the other.

CHINA:

China has performed comparatively the best as it is clear from:

- Success in raising the level of growth along with alleviation of poverty.
- It used the market mechanism to create additional social and economic opportunities without political commitment.
- By retaining collective ownership of land and allowing individuals to cultivate lands, China has ensured social security in rural areas.
- Public intervention in providing social infrastructure has brought about positive results in human development indicators in China

MULTIPLE CHOICE QUESTIONS (1mark)

1. **Arrange the following events in chronological order and choose the correct answer from the given alternatives:**

- (i) Establishment of People's Republic of China
- (ii) Creation of Pakistan
- (iii) First Five-Year Plan of India
- (iv) First Five-Year Plan of China

Alternatives:

- (a) (i), (iv), (ii), iii) (b) (iii), (ii), (i), iv)
- (c) (ii), (i), (iii),(iv) (d) (iv), (iii), (ii), (i)

2. Commune system is the feature of

- (a) India (b) China (c) Pakistan d) All the above

3. Mao initiated the 'Great Leap Forward' in the year-----

- (a) 1951 (b) 1955 (c) 1958 (d) 1962

4. India is not a member of which of the following regional / global economic group:

- (a) European Union (b)BRICS (c) G-20 (d)SAARC

5. "Multiple reasons for economic slowdown and re-emergence of poverty in Pakistan may be enumerated". Identify which of the following might not be one of them.

- (i) Rising dependence on foreign loans (ii) Stable macroeconomic indicators
- (iii) Unstable agricultural growth

Alternatives:

- (i), (ii) and (iii) (b) (ii) and (iii) (c) (i) and (iii) (d) Only (ii)

6. Introduction of economic reforms in China took place in the year

- (a) 1978 (b)1980 (c) 1988 (d)1991

7. The main aim of Great Leap Forward in China was to ensure rapid increase of

- (a)Agriculture (b) Industries (c) Services (d)Export

8. Under_____ in China, farmers and industrial units required to buy and sell fixed quantities of inputs and outputs on the basis of prices fixed by the government and rest were purchased and sold at market prices.

- (a). Commune system (b) Great Leap Forward Campaign
- (c) Dual Pricing (d) Great Proletarian Cultural Revolution

9. Great Proletarian Cultural Revolution was introduced under the leadership of _____.

- (a) Mao Zedong (b) J.L. Nehru (c) M.K. Gandhi (d) M.A. Jinnah

10. Identify the incorrect statement from the following:

- (a) China's Economic growth rate is better than that of Pakistan
- (b) Pakistan is behind India in HDI ranking
- (c) One child Policy norm was adopted in Pakistan
- (d) In 1991, India adopted New economic reforms

ASSERTION AND REASONING BASED QUESTIONS

Read the following statements- Assertion(A) and Reasoning (R). Choose one of the correct alternative s given below:

- (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A)*
- (b) Both Assertion (A) and Reason (R) are true and Reason (R) is not the correct explanation of Assertion (A)*
- (c) Assertion (A) is true but Reason (R) is false.*
- (d) Assertion (A) is false but Reason (R) is true.*

11. **ASSERTION (A):** Great Leap Forward (GLF) campaign initiated in China brought a new era of industrialisation and agricultural development.

REASON (R): Students and professionals were sent to countryside under the Great Leap Forward (GLF) campaign.

12. **ASSERTION (A):** GLF campaign initiated in 1958 aimed at industrializing the country on a massive scale.

REASON (R): Under the commune system, people collectively cultivated lands.

13. **ASSERTION (A):** India adopted a mixed economy model of growth.

REASON (R): People's Republic of China as a growth model was established in 1949.

14. **ASSERTION (A):** China's rapid industrial growth can be traced back to its reforms introduced in 1978.

REASON (R): Private Sector firms and township and village enterprises (enterprises which were owned and opened and operated by local collectives) were allowed to produce goods.

15. **ASSERTION (A):** India is moving ahead of both China and Pakistan.

REASON (R): India introduce economic reforms like GLF campaign of China, to industrialize the country on a massive scale.

STATEMENT BASED QUESTIONS

(Q.NO.16-20) Read the following statement-based questions carefully and choose the correct alternative from the following

Alternatives:

- a) Statement 1 is true and Statement 2 is false
- b) Statement 2 is true and Statement 1 is false
- c) Both the statements are true
- d) Both the statements are false

16. Statement-1: All the three countries, China, India, Pakistan introduced the reforms in the same year.

Statement-2: China's annual growth rate of Population is more than India and Pakistan.

17. Statement-1: Both India and Pakistan initiated their economic reforms without any external pressures.

Statement-2: Pakistan has successfully implemented the SEZ policy and reaped its benefits using the Export Promotion Policy

18. Statement-1: In both India and Pakistan, the service sector has been emerging as a major source of development.

Statement-2: Amongst the neighbors of India, China has highest life expectancy rate.

19. Statement-1: Special Economic Zones (SEZs) policy has led to huge Foreign Direct Investment (FDI) flow to China.

Statement-2: China's rapid Industrialization growth was the result of its economic reforms in 1981.

20. Statement-1: 'Liberty indicators' measure the extent of constitutional protection given to the citizens.

Statement-2: India provides fair constitutional protection to its citizens.

MATCHING TYPE OF QUESTIONS

21. Match the statements given in column I with the correct option given in Column II

Column I	Column II
(i) India	A. One-child policy
(ii) China	B. Reforms were initiated in the year 1988
(iii) Pakistan	C. Highest density of population

22. From the set of events/ systems given in column I and corresponding relevant fact given in Column II, about China, choose the correct pair of statement.

Column I	Column II
A. Great leap Forward	(i) Cultivating land collectively
B. Commune system	(ii) Opening of industries in their homes.
C. Proletarian cultural Revolution	(iii) Students were sent to work and learn from the countryside
D. Economic reforms in China	(iv) 1988

Alternatives:

- a) A-i b) B-ii c) C-iii d) D-iv

23. Choose the correct sequence of options in Column II by matching them options in Column I

Column I	Column II
A. 1949	(i) Great Proletarian Cultural Revolution
B. 1953	(ii) Establishment of People's republic of China
C. 1965	(iii) Reforms introduced in China
D. 1978	(iv) First Five-year Plan of China

24. From the set of events given in column I and corresponding relevant fact given in Column II, choose the correct pair of statement.

Column I	Column II
A. Dual Pricing	(i) Economic reforms in 1991
B. Setting up of Special Economic Zones in China	(ii) To attract foreign Direct Investment
C. Commune system	(iii) Backyard based industrial production units
D. Great Proletarian Cultural Revolution	(iv) Collective farming

Alternatives:

- a) A-i b) B-ii c) C-iii d) D-iv

25. From the set of statements given in Column I and Column II, Choose the correct pair of statements:

Column I	Column II
A. Medium Term Development Plan	(i) China model of growth
B. NITI Aayog	(ii) Reforms in India
C. Command Economy	(iii) Pakistan's Five-year Plans
D. Economic Reforms in 1991	(iv) Planning Commission is replaced

Alternatives:

- a) A-ii, B-i, C-iii, D-iv c) A-i, B-ii, C-iv, D-iii
 b) A-iii, B-iv, C-i, D-ii d) A-iv, B-iii, C-ii, D-i

ANSWERS:

1.c	2.b	3.c	4.a	5.d
6.a	7. b	8. c	9. a	10.c
11. c	12. b	13. b	14.a	15.d
16.d	17.d	18.c	19.a	20.c
21. (i)c; (ii) a; (iii) b	22. c	23. (i)b; (ii) d; (iii) a; (iv)c.	24. b	25.b

3, 4 MARKS QUESTIONS

Q.1. India and Pakistan initiated their journey of development, nearly at the same time, yet the two economies have travelled different distances. Justify the given statement with the valid arguments.

Ans. It is true that India and Pakistan started their journey of development nearly at the same time, in a similar way. Both the nations adopted policies like economic planning, dominance of public sector, high public expenditure etc. In the post 1947 period. There has been a decline in the annual growth of GDP in Pakistan over the year, whereas India met with moderate increase in GDP. The probable reasons for slower growth in Pakistan are political instability, overdependence on remittance and foreign aid along with volatile performance of agricultural sector. However, India met with greater success owing to efficient economic planning and better implementation vis-à-vis Pakistan.

Q.2. Explain the Great Leap Forward campaign of China as initiated in 1958.

Ans- In 1958 'The Great Leap Forward' was initiated by Mao to modernise China's economy.

- Its aim was to industrialize the country on a large scale and in as short a time as possible.
- For this, people were encouraged to set up industries in their backyards.
- In villages, village Communes or cooperatives were set up. Communes mean collective cultivation of land.
- Around 26000 communes covered almost all the farm population in 1958.

The Great Leap Forward program faced many problems. These were:

- In the earlier phase, a severe drought occurred in China and it killed some 3-crore people.
- Soviet Russia was a comrade to communist China, but they had border dispute. As a result, Russia withdrew its professionals who had been helping China in its industrialisation bid.

Q.3. Briefly explain the development strategies followed by China for its development

Ans- Policies followed by China are: -

a) Great leap forward (GLF) – The campaign initiated in 1958 aimed at industrializing the country on a massive scale. People were encouraged to setup industries in their backyards. There were no restrictions which provide momentum for economic growth.

b) Commune system – In rural areas, people collectively cultivate lands, In 1958, there were 26,000 communes covering almost all the farm population

c) Great Proletarian Cultural Revolution (1966-1976) – Under this revolution, students and professionals were sent to work and learn from the countryside.

d) One child policy – One child policy norm introduced in China to control its population growth.

e) Setting up of Special economic zones and opening of economy in 1978

Q4. Mention the salient demographic indicators of China, Pakistan and India.

Ans: . Following are the salient demographic indicators of China, Pakistan and India:

i) Population: The population of Pakistan is very small and accounts for roughly about one tenth of China and India.

ii) Population Density: Though China is the largest nation geographically among the three, but its density is the lowest.

iii) Population Growth: Population growth is highest in Pakistan followed by India and China. One-child norm introduced in China in the late 1970s is the major reason for low population growth. But this measure led to a decline in the sex ratio.

iv) Sex Ratio: The sex ratio low and biased against females in all the three countries. There is strong son-preference prevailing in all these countries as the reason.

Q.5. Define the liberty indicator. Give some examples of liberty indicators.

Ans. Liberty Indicator may be defined as the measure of the extent of demographic participation in the social and political decision making.

Examples of liberty indicators:

- (i) Measures of the extent of the Constitutional Protection Rights given to the citizens;
- (ii) Extent of the Constitutional Protection of the independence of the Judiciary and Rule of Law.

Q.6. Write three observations pointing to re-emergence of poverty in Pakistan.

Ans. Following observations pointing to re-emergence of poverty in Pakistan:

- Lack of institutional reforms in agriculture because of which this sector has remained volatile (devoid of stability).
- Lack of political stability in Pakistan, leading to huge public expenditure on the maintenance of law and order.
- Allocation of huge funds to build a strong defense-system at the cost of developmental expenditure.

Q. 7. Write three observations pointing to growth story of India, China and Pakistan.

Ans. Following observations highlight the growth story of India, China and Pakistan:

- China has outpaced both India and Pakistan with regard to GDP growth.
- India has performed better than Pakistan. But compared with China, India is way behind.
- The relative success of China is credited to political stability in China. China has proved that the more relevant factor in the context of GDP growth is not the availability of resources but good governance by the state and 'good compliance' by the citizens.

Q.8. Write three observations highlighting global exposure of the economy of China.

Ans. Following observations highlight the global exposure of the economy of China:

- Inward looking policy of self-sufficiency and protection of domestic industry from foreign competition has gradually been replaced by the policy of growth through competition.
- It allowed the foreign investors the freedom to 'hire and fire' the workers. It also offered them a lucrative infrastructure.
- China allowed foreign investors 100 per cent equity investment across most sectors of the economy.

Q.9. Write three observations on the structure of growth in India, Pakistan and China.

Ans. Following observations highlight the structure of growth in India, Pakistan and China:

- (i) Indian and Pakistan adopted a 'mixed-economy' model of growth. While, China adopted 'Statism' as a model of growth.
- (ii) India and Pakistan have relied more on tertiary sector while the economy of China has relied more on secondary sector for the GDP growth.
- (iii) In China, contribution of secondary sector to GDP is much more than in India and Pakistan.

Q.10. The complementarity between the structure of growth and the GDP growth appears quite different from that shown by the historical experience of the developed countries. Comment.

Ans. Historical experience of the developed countries shows that in terms of the percentage share in GDP, it was first the secondary sector and later the tertiary sector which emerged as the leading sectors of the economy. However, in the Indian context, what was witnessed was that a major shift directly from primary sector to the tertiary sector. Primary sector on the eve of independence was the largest contributor to GDP. Now, tertiary sector has the lead in terms of contribution to GDP. Thus, a major shift directly from primary sector to tertiary sector has been observed in India. This implies a lesser emphasis has been accorded to industrial expansion in India.

Q.11. How do you view the opposition to FDI in retail in India? Compare it with the situation of smooth operation of FDI in retail in China.

Ans: It is an undisputed fact that FDI is growth-friendly. After all, it is an investment and increases production capacity of the nation. The opposition to FDI in retail in India is not because it may be a roadblock in the process of growth. It is because it may generate unwarranted competition for the retail traders in India who may be marginalized and finally driven out of the market. Such a situation may erode the opportunity of self-employment in the country, and may also lead to concentration of economic power with the foreign investors. On the other hand, China was liberal in allowing FDI in retail. China allowed foreign investors 100 per cent equity investment.

Q.12. Analyse the role assigned to public sector in the process of development in India and Pakistan in comparison to that in China.

Ans: India, Pakistan and China relied on planned development programs as their basic strategy of growth and development. But, whereas in India and Pakistan, mixed economy served as the basic premise of the growth model, in China, all critical areas of production were brought under state ownership, and command economy served as the basic premise of the growth model. Thus, China adopted 'statism' as the model of growth.

Q.13. 'GDP growth rate in China has slowed down in the recent past'. Give the reasons for this.

Ans- Some notable reasons in this regard are

- a) Slowdown in the global economies has dampened the demand for the Chinese products.
- b) Growth of domestic demand in China is slowing down. This is because of rising propensity to save in the Chinese economy.
- c) Corruption and economic crimes have tended to rise over time.
- d) Chinese people are now exploring higher wage opportunities of employment in the rest of the world where government intervention is minimum.

Q.14. Compare and analyse the given data of India and China, with valid reasons.

Country	Annual Growth Rate of Population (2015)	Sex Ratio (Per thousand males)
India	1.2 %	929
China	0.5%	941

Ans. Comparison and observations:

- (i) Annual Growth rate of population is much lower in China (0.5%) than India (1.2%). It possible only successful implementation of One child policy introduced in China in 1979.
- (ii) Gender ratio is more skewed in India 929 per 1000 males than China 941 per 1000 males (No. of Females per Thousand Males).
- iii) This reflect a strong preference for a male child in the Indian society, it is sign of higher social backwardness in India than China.

Q.15. Compare the analyse the given data of India, China and Pakistan.

Annual growth of Gross Domestic Product in %(1980-2017)

Country	1980-90	2015-17
India	5.7	7.3
China	10.3	6.8
Pakistan	6.3	5.3

- The above table states that, during 1980-90 China was having double- digit growth rate of 10.3%, Whereas Pakistan's growth rate was 6.3%, and India was bottom with just 5.7% growth rate.
- During 2015-17, there was a drastic fall in China's growth rate from 10.3% to 6.8%.
- Pakistan also met with a decline in annual growth of GDP from 6.3% to 5.3%.
- India recorded an increase from 5.7% to 7.3% owing to efficient economic planning and better implementation as compared to Pakistan.

16. Compare and analyse the following information related to Imports and Exports of the three neighboring nations:

Country	Exports from India (in ₹ Crore)			Imports to India (in ₹ Crore)		
	2004-05	2018-19	Annual rate of growth (%)	2004-05	2018-19	Annual rate of growth (%)
Pakistan	2,341	14,426	3.7	427	3,476	5.1
China	25,232	1,17,289	2.6	31,892	4,92,079	10.3

Ans: The above table shows that during the given periods the Exports from India to Pakistan have increased at an annualized rate of 3.7 % while the same with China shows 2.6% of growth. On the other hand, India's import from China accounted for a massive 10.3 %. The corresponding figure with Pakistan witnessed an average of 5.1% respectively.

- The situation indicates that Indian imports from China are too high in comparison to the exports to China. This shows that Indian economy was over-dependent on Chinese economy for goods and services, over the given period of time.

6 MARK QUESTIONS**Q.1. Describe the important parameters of HDI with reference to the performance of India and China.**

Ans a) In the year 2014, HDI for China and India was estimated to be 0.719 and 0.586 respectively.

b) Global ranking of these countries found to be 91 and 135.

c) In the year 2011 China's GDP per capita was estimated to be US \$8394, while it was merely US\$3703 for India.

d) 55% of China's population has access to improved sanitation compared with 31% in India.

e) Infant Mortality Rate is as low as 15.62 per thousand. In China compared with 46 per

thousand in India.

f) Maternal Mortality Rate is just 38 per lakh in China Compared with 230 in India.

Q.2. “India, China and Pakistan have travelled more than seven decades of development path with varied result.” Explain the given statement with valid argument.

Ans. India, China and Pakistan have travelled more than seven decades of development path simultaneously, but the result is substantially different. China has edge both India and Pakistan, both are lagging far be India, China and Pakistan have travelled more than seven decades of development path with varied hind. The principal reasons are as under.

I. Great Leap Forward (GLF 1958) campaign of China: -

1. GLF was started in 1958 with a view to propelling the pace of economic and industrial development
2. Which aimed at Country's industrialization and agriculture on a large scale
3. China resorted to “Commune System of Production” Under which people cultivated land collectively.

II. Great Proletarian Cultural Revolution: Mao (Chinese communist revolutionary) believed that both had to grow to allow the other to grow. Mao introduced the Great Proletarian Cultural Revolution (1966–76) under which students and professionals were sent to work and learn from the countryside.

5. It focused on widespread industrialization of the economy
6. People to set-up household industry in their backyard.

III. One Child policy in China: - OCP adopted by China in 1979 has been very successfully pursued. Consequently,

1. Growth rate of population has reduced to nearly half, from 1.33 per cent in 1979 to 0.47 per cent in recent past
2. With a check on population growth, China focusses on raising the quality of life.

IV. Growth story of China: - (i) In 2017, GDP in China was estimated to be 12.40 trillion.

V. Special Economic Zones (SEZ) in China

VI. High Labour Supply in China.

VII. GNI per capita (PPP \$ US): In China, GNI per capita is highest amongst the three nations followed by India and Pakistan.

Q. 03. Mention salient demographic indicators of China, Pakistan and India.

- Ans-**
1. The population of Pakistan is very small & account for roughly about one tenth of China or India.
 2. China is largest nation geographically among the three, its density is lowest
 3. The population growth is highest in Pakistan followed by India. One child normal introduce in China in late 1970s is the major reason for low population growth.
 4. The sex ratio is low & based against females in all three countries
 5. The fertility rate is low in China & very high in Pakistan

6. Urbanization is high in both Pakistan & China with India having 28 per cent of its people living in areas.

Q.4. Compare and contrast India and China's sectoral contribution towards GVA/GDP. what does it indicate.

Sectoral Contribution to GVA/GDP in % (2018-19)

Sector	India	China
Agriculture	16	7
Industry	30	41
Service	54	52
Total	100	100

Answer:

- **Contribution to Agriculture sector:** The contribution of agriculture to GVA/GDP was 7% in case of China, whereas, it was 16% in case of India.
- **Contribution to Industrial sector:** The contribution of Industrial sector to GVA/GDP was 41% in case of China, whereas, it was 30% in case of India.
- **Contribution to Service sector:** The contribution of Service sector to GVA/GDP was 52% in case of China, whereas, it was 54 % in case of India.
- By these points we can conclude that service sector is contributing highest in both the countries. The industrialization in China is highest as the contribution from industrial sector is highest in China. The service sector in China has also expanded proportionate to the industrial sector which is not the case in India.

Q. 05. Compare and analyse the given data of distribution of workforce (in 2018- 19) with valid reasons.

Country	Agriculture sector (%)	Industrial sector (%)	Service sector (%)
India	43	25	32
China	26	28	46
Pakistan	41	24	35

Source: NCERT

- **Ans.** As evident from the table, the percentage of workforce engaged in agricultural sector is the highest in case of India, which stands at 43 per cent. The corresponding rates for China and Pakistan are 26 per cent and 41 per cent respectively.
- The percentage of workforce engaged in industry is the highest in China, which stands at 28 per cent. The corresponding rates for India and Pakistan are 25 per cent and 24 per cent respectively.
- The percentage of workforce engaged in services sector is again the highest in China, which stands at 46 per cent. The corresponding rates for India and Pakistan are 32 per cent and 35 per cent respectively.

- These observations point to a fact that China is far ahead of India and Pakistan in industrialising its production activity which is a sign of long period growth and development.
- Higher percentage of workforce in services sector in China is also a sign of its faster growth compared to India and Pakistan. However, the fact should also be not ignored that Pakistan has taken over India as regards the growth of services sector. This points to rapid urbanization in Pakistan.

Q.6. Based on the given data, compare any two parameters for the economies of India and China.

Some selected indicators of Human Development, 2017-19

Items	Human development index (HDI)	HDI (Rank)	Life Expectancy at birth (in years)	GNI per capita (PPP \$ US)
India	0.645	130	69.7	6,681
China	0.761	87	76.9	67.3

- **Source:** HDI Report 2019 and 2020 and world development indicators.
- **Ans. HDI (value) :** (i) HDI is an important indicator of socio- economic development. Higher value of HDI shows higher level of growth and development of a nation. As per given report, HDI for India is 0.645, which is lesser than that of China (0.761).
- **(ii) HDI Rank:** HDI values are used to create ranking of different countries. China is placed at 87th position in the world whereas, India stands at 130th position. Higher rank indicates socio-economic development.
- **(iii) Life Expectancy at birth (in years):** A country which provides better health and civic facilities secure a higher life expectancy for its citizens. China has higher life expectancy than India by a margin of approximately 8 year.

CASE STUDY BASED QUESTIONS

I. Read the following text carefully and answer the questions given below:

SINO-PAK FRIENDSHIP CORRIDOR

The China-Pakistan Economic Corridor (CPEC) has deepened the decades long strategic relationship between the two nations. But it has also sparked criticism for burdening Pakistan with mountains of debt and allowing China to use its debt-trap diplomacy to gain access to strategic assets of Pakistan.

The foundations of CPEC, part of China's Belt and Road Initiative, were laid in May 2013. At the time, Pakistan was reeling under weak economic growth. China committed to play an integral role in supporting Pakistan's economy.

Pakistan and China have a strategic relationship that goes back decades. Pakistan turned to China at a time when it needed a rapid increase in external financing to meet critical investments in hard infrastructure, particularly power plants and highways. CPEC's early harvest projects met this need, leading to a dramatic increase in Pakistan's power generation capacity, bringing an end to supply-side constraints that had made rolling blackouts a regular occurrence across the country.

Pakistan leaned into CPEC, leveraging Chinese financing and technical assistance in an attempt to end power shortages that had paralyzed its country's economy. Years later, China's influence in Pakistan has increased at an unimaginable pace.

China as Pakistan's Largest Bilateral Creditor: China's ability to exert influence on Pakistan's economy has grown substantially in recent years, mainly due to the fact that Beijing is now Islamabad's largest creditor. According to documents released by Pakistan's finance ministry, Pakistan's total public and publicly guaranteed external debt stood at \$44.35 billion in June 2013, just 9.3 percent of which was owed to China. By April 2021, this external debt had ballooned to \$90.12 billion, with Pakistan owing 27.4 percent-\$24.7 billion - of its total external debt to China, according to the International Monetary Fund (IMF).

Additionally, China provided financial and technical expertise to help Pakistan build its road infrastructure, expanding north-south connectivity to improve the efficiency of moving goods from Karachi all the way to Gilgit-Baltistan (POK). These investments were critical in better integrating the country's ports, especially Karachi, with urban centres in Punjab and Khyber Pakhtunkhwa provinces. Despite power asymmetries between China and Pakistan, the latter still has tremendous agency in determining its own policies, even if such policies come at the expense of the long-term socioeconomic welfare of Pakistani citizens.

(<https://www.usip.org/publications/2021/05/pakistans-growing-problem-its-china-economic-corridor> - Modified)

QUESTIONS:

1Q. Outline and discuss any two economic advantages of China Pakistan Economic Corridor (CPEC) accruing to the economy of Pakistan.

2Q. Analyse the implication of bilateral 'debt-trap' situation of Pakistan vis-a-vis the Chinese Economy.

Answer:

Economic advantages of China Pakistan Economic Corridor (CPEC) to the economy of Pakistan are: China provided financial and technical expertise to help Pakistan build its road infrastructure, supporting employment and income in the economy.

CPCE has led to a massive increase in power generation capacity of Pakistan. It has brought an end to supply-side constraints in the nation, which had made blackouts a regular phenomenon across the country.

China has become famous for its 'Debt Trap Diplomacy' in recent times. Under this China provides financial and technical expertise/assistance to help various nations to bring them under its direct or indirect influence.

The first and the foremost implication of the diplomacy is that Beijing has now become Islamabad's largest creditor. According to documents released by Pakistan's finance ministry, its total public external debt stood at \$44.35 billion in June 2013, just 9.3 percent of which was owed to China. By April 2021, this external debt had ballooned to \$90.12 billion, with Pakistan owing 27.4 percent-\$24.7 billion - of its total external debt to China, according to the IMF.

II. Read the following case study carefully and answer the questions that follow.

Special Economic Zones (SEZs) are intended to function as zones of rapid economic growth by using tax and business incentives to attract foreign investment and technology. The first four economic zones were created in 1980 in southeastern coastal China and consisted of what were then the small cities of Shenzhen, Zhuhai, and Shantou in Guangdong province and Xiamen in Fujian province. In these areas, local governments have been allowed to offer tax incentives to foreign investors and to develop their own infrastructure without the approval of the central government.

Business enterprises have made most of their own investment, production and marketing decisions and foreign ownership of such ventures have been legalized. Though some of them began a little more than small towns, the new SEZs soon attracted foreign investment and became boom towns, with rapidly expanding light and consumer goods industries and growing population. Encouraged by the zone's success, the Chinese government in 1984 opened 14 larger and older cities along the coast of foreign trade and investment. In 1988, Hainan Island was made a separate province and a special economic zone, and in 1990 the Pudong area within the Shanghai municipality became a special economic zone with policies even more flexible than those already in force in the original four Special Economic Zones (SEZs).

QUESTIONS:

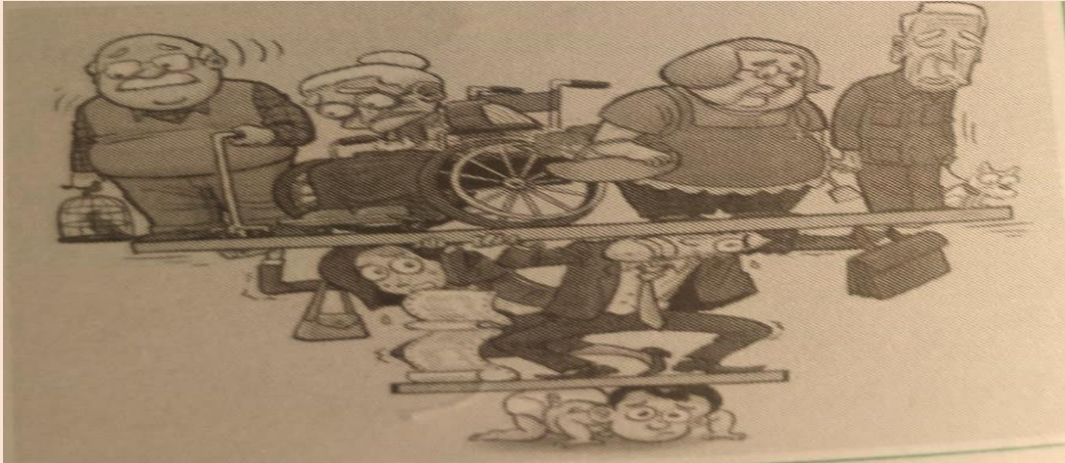
- (a) What were Special Economic Zones (SEZs)? Name any two cities in which special economic zones were started in China in 1980.
- (b) When were economic reforms initiated in China? What autonomy was given to local government for motivating foreign investors in China under special Economic Zones?

ANSWERS:

A special economic zone (SEZ) is an area in a country that is designed to generate positive economic growth. An SEZ is normally subject to different and more favorable economic regulations compared to other regions in the same country, including tax incentives and the opportunity to pay lower tariffs. The first four economic zones were created in 1980 in China were the small cities of Shenzhen, Zhuhai, and Shantou in Guangdong province.

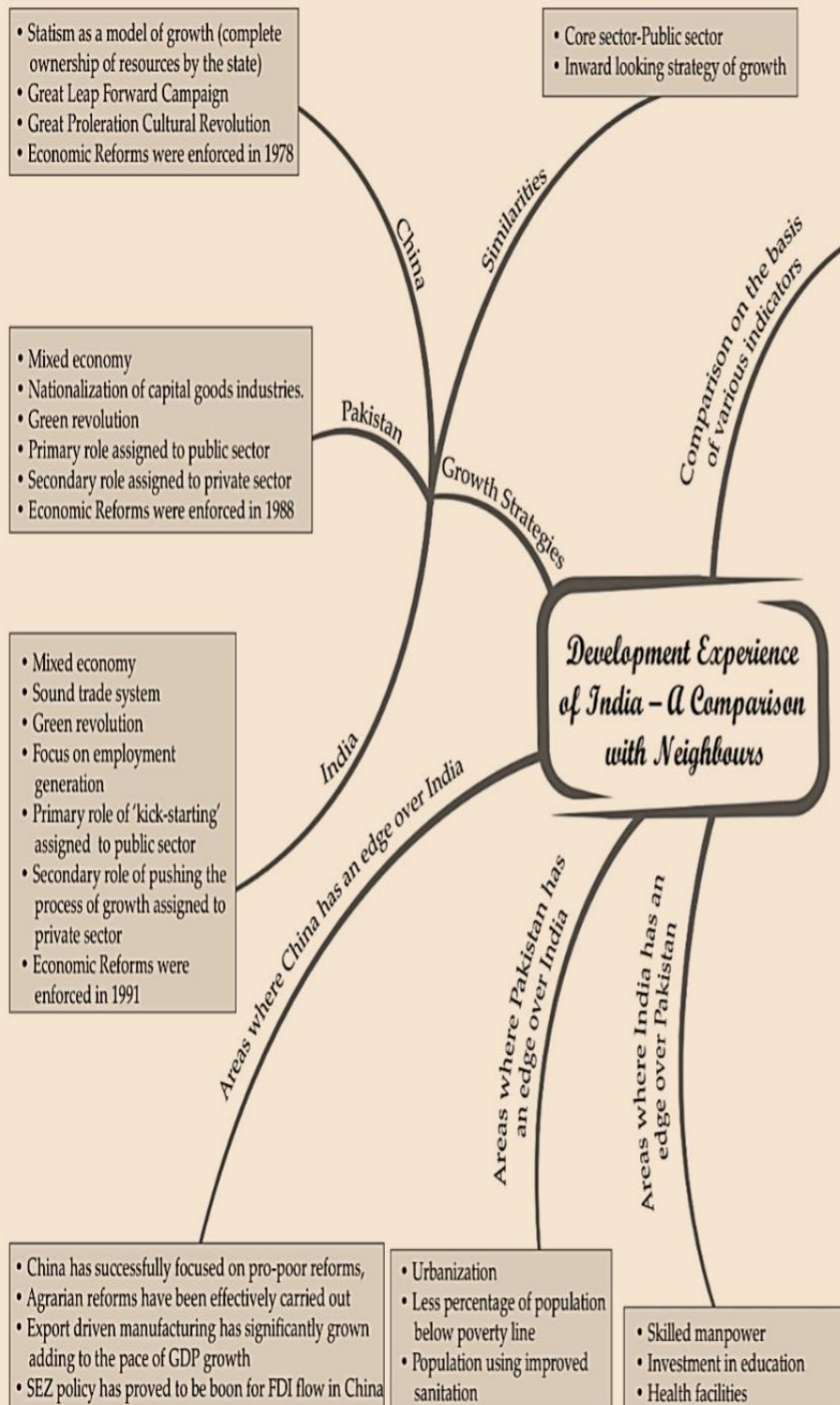
In late 1978. In these areas, local governments have been allowed to offer **tax incentives** to foreign investors and to develop their own infrastructure without the approval of the central government.

III. Interpret the given image on account of population policy and resultant effects in China.



Ans: “One child” norm/policy introduced in China in the late 1970s and the resultant arrest in the growth of population and lower fertility rate has one significant implication. In a few decades, in China, there will be more elderly people in portion to young people. This has led China to allow couples to have two children.

MIND MAP



Indicators	India	China	Pakistan
Estimated Population (in million)	1311	1371	188
Density(per sq.km)	441	146	245
Sex Ratio	929	941	947
Fertility Rate	2.3	1.6	3.7
Urbanization	33	56	39
Annual growth of GDP	7.3	6.8	5.3
Sectoral Contribution to GDP:			
Agriculture	17	9	25
Industry	30	43	21
Service	53	48	54
Sectoral Distribution of work force:			
Agriculture	42.7	17.5	42
Industry	23.8	26.5	3.7
Service	33.5	56	54.3
Human Development Index (value)	0.640	0.752	0.562
Rank (based on HDI)	130	86	150
Life Expectancy at Birth (years)	68.8	76.4	66.6
GDP per capita (PPP US \$)	6,427	15,309	5,035
Infant Mortality Rate (per 1,000 births)	34.6	8.5	64.2
Maternal Mortality Rate (per 1,000 births)	174	27	178
People Below Poverty Line (2011) (%)	60.4	23.5	46.4
Population using improved sanitation(%)	44.2	75	58.3
Population with Sustainable access to improved water resources (%)	94	96	91
Percentage of Undernourished Children	37.6	8.1	46.4

Guidelines for Project Work in Economics (Class XI and XII)

The **objectives** of the project work are to enable learners to:

- probe deeper into theoretical concepts learnt in classes XI and XII
- analyse and evaluate real world economic scenarios using theoretical constructs and arguments
- demonstrate the learning of economic theory
- follow up aspects of economics in which learners have interest
- develop the communication skills to argue logically

The **expectations** of the project work are that:

- learners will complete only **ONE** project in each academic session
- project should be of 3,500–4,000 words (excluding diagrams & graphs), preferably hand-written
- it will be an independent, self-directed piece of study

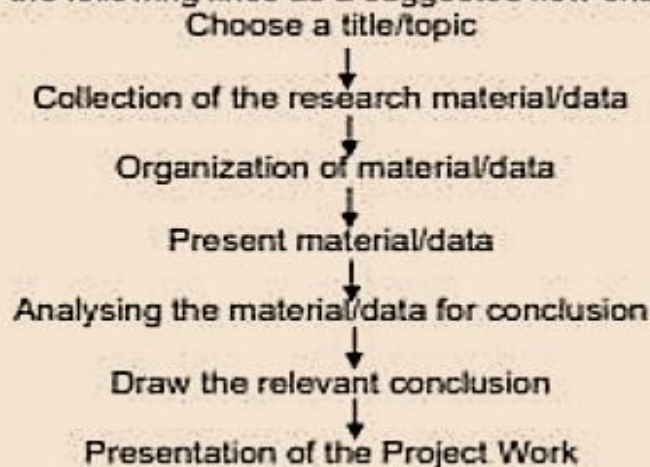
Role of the teacher:

The teacher plays a critical role in developing thinking skills of the learners. A teacher should:

- help each learner select the topic based on recently published extracts from the news media, government policies, RBI bulletin, NITI Aayog reports, IMF/World Bank reports etc., after detailed discussions and deliberations of the topic
- play the role of a facilitator and supervisor to monitor the project work of the learner through periodic discussions
- guide the research work in terms of sources for the relevant data
- educate learner about plagiarism and the importance of quoting the source of the information to ensure authenticity of research work
- prepare the learner for the presentation of the project work
- arrange a presentation of the project file

Scope of the project:

Learners may work upon the following lines as a suggested flow chart:



Expected Checklist:

- Introduction of topic/title
- Identifying the causes, consequences and/or remedies
- Various stakeholders and effect on each of them
- Advantages and disadvantages of situations or issues identified
- Short-term and long-term implications of economic strategies suggested in the course of research
- Validity, reliability, appropriateness and relevance of data used for research work and for presentation in the project file
- Presentation and writing that is succinct and coherent in project file
- *Citation of the materials referred to, in the file in footnotes, resources section, bibliography etc.*

Mode of presentation/submission of the Project:

At the end of the stipulated term, each learner will present the research work in the Project File to the External and Internal examiner. **The questions should be asked from the Research Work/ Project File of the learner. The Internal Examiner should ensure that the study submitted by the learner is his/her own original work.** In case of any doubt, authenticity should be checked and verified.

Marking Scheme:

Marks are suggested to be given as –

S. No.	Heading	Marks Allotted
1.	Relevance of the topic	3
2.	Knowledge Content/Research Work	6
3.	Presentation Technique	3
4.	Viva-voce	8
	Total	20 Marks

Suggestive List of Projects:

Class XII	
• Micro and Small Scale Industries	• Food Supply Channel in India
• Contemporary Employment situation in India	• Disinvestment policy of the government
• Goods and Services Tax Act and its Impact on GDP	• Health Expenditure (of any state)
• Human Development Index	• Inclusive Growth Strategy
• Self-help group	• Trends in Credit availability in India
• Monetary Policy Committee and its functions	• Role of RBI in Control of Credit
• Government Budget & its Components	• Trends in budgetary condition of India
• Exchange Rate determination – Methods and Techniques	• Currency War – reasons and repercussions
• Livestock – Backbone of Rural India	• Alternate fuel – types and importance
• Sarva Shiksha Abhiyan – Cost Ratio Benefits	• Golden Quadrilateral- Cost ratio benefit
• Minimum Support Prices	• Relation between Stock Price Index and Economic Health of a Nation
• Waste Management in India – Need of the hour	• Minimum Wage Rate – Approach and Application
• Digital India- Step towards the future	• Rain Water Harvesting – A solution to water crisis
• Vertical Farming – An alternate way	• Silk Route- Revival of the past
• Make in India – The way ahead	• Bumper Production- Boon or Bane for the farmer
• Rise of Concrete Jungle- Trend Analysis	• Organic Farming – Back to the Nature
• Aatmanirbhar Bharat	• e-Rupee (e- ₹)
• Sri Lanka's Economic Crisis	• Sustainable Development Goals (SDG's)
• Environmental Crisis	• Comparative Study of Economies (Maximum three economies)
• New Education Policy (NEP) 2020: A Promise for a New Education System	• G-20: Inclusive and Action Oriented
• Amrit Kaal: Empowered and Inclusive Economy	• Cashless Economy
• Any other newspaper article and its evaluation on basis of economic principles	• Any other topic

**LINK FOR THREE SETS OF CBSE 2023-24 QUESTION PAPERS
WITH MARKING SCHEME**

https://drive.google.com/drive/folders/1BQkpi2cjm-shCBcvLE6p-opvA6_-wEa9?usp=drive_link

LINK FOR UNSOLVED SAMPLE QUESTION PAPERS

<https://drive.google.com/drive/folders/1xqVnLg78gktog6RE0EJhdGYr2P3PuZMG?usp=sharing>

LINK FOR MARKING SCHEME TO UNSOLVED SAMPLE QUESTION PAPERS

https://drive.google.com/drive/folders/15fZH_vRr7QIGzquY-4AUpn-ftAZ7stl_?usp=sharing

LINK FOR VIDEO ON HOW TO SOLVE ASSERTION & REASONING QUESTIONS:

<https://drive.google.com/file/d/1rrFmD9OHf7bH31tWNK-uqwAw-ggP5C3x/view?usp=sharing>