

## Answers to REC–DS1/Set-2

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1. (c) Both statements 1 and 2 are true
2. (c) Fixed investment
3. (c) The value of rupee against one dollar must be rising before the intervention.
4. (b) Over Full Employment Equilibrium
5. (d) (i), (ii) and (iii)
6. (a) Income receipts and payments
7. (d) Monetary Policy
8. (a) 128, 5000, 1000, 4000

**Working Note:**

Legal Reserve Ratio = 20% or 0.2 and Money Multiplier =  $1/\text{LRR} = 1/0.2 = 5$

(i) Cash Reserves =  $640 \times 20/100 = 128$

(ii) Deposits =  $1000 \times 5 = 5000$

(iii) Cash Reserves =  $200 \times 5 = 1000$

(iv) Loans =  $800 \times 5 = 4000$

9. (a) ₹ 70

**Working Note:**

Equilibrium level of income (Y) is attained when,

$$S = I$$

$$\therefore -10 + 0.2Y = -3 + 0.1Y$$

$$0.2Y - 0.1Y = -3 + 10$$

$$0.1Y = 7$$

$$Y = 70$$

Therefore, equilibrium level of income = ₹ 70 crores

10. (c) one; infinity
11. • BoP transactions independent of all other BoP transactions are called “autonomous transactions” whereas the transactions undertaken to cover deficit or surplus in the autonomous transactions are called “accomodating transactions”.
- Example, an export transaction is undertaken to earn income, so it is an autonomous transaction whereas accomodating transaction is like borrowing from the IMF (International Monetary Fund).
- Autonomous transactions are also called “above the line transactions” whereas accomodating transactions are called “below the line transactions” in the BoP.
12. (A) Domestic Income = (i) + (ii) + (iv) + (vii) + (viii) + (x)
- $$= 2,000 + 800 + 460 + 940 + 300 + 200$$
- $$= ₹ 4,700 \text{ crores}$$

**Or**

- (B) (i) Nominal GDP is the market value of final goods and services produced within the domestic territory of a country, during an accounting year, as estimated at the current year prices.
- (ii) Intermediate goods are those goods which are purchased during the year by one production unit from other production units and completely used up or resold during the same year.
- (iii) Value of output refers to the market value of all goods and services produced during a period of one year.

13. (A) The given statement is refuted. Excess demand is a situation when  $AD > AS$  corresponding to full employment level in the economy. Under this situation of full employment, there is no further possibility of creating more employment opportunities. At full employment level, it is assumed that all the resources are already fully and efficiently employed.

**Or**

- (B) (i) False, as APS is not always greater than zero but its value may be negative. This is so at very low levels of income when consumption expenditure is greater than income. For example, at an income level of ₹ 1000, the consumption expenditure is ₹ 1200, then  $APS = \frac{S}{Y}$
- and savings will be  $= Y - C = 1000 - 1200 = -200 = \frac{-200}{1000}$ .
- $\Rightarrow APS = \frac{S}{Y} = \frac{-200}{1000} = -0.2$ .
- (ii) False, because value of investment multiplier does not vary between 0 and infinity but varies from 1 to infinity ( $\infty$ ).

This can be proved by

- When  $MPC = 0$ , then  $k = \frac{1}{1-MPC} = \frac{1}{1-0} = \frac{1}{1} = 1$
- When  $MPC = 1$ , then  $k = \frac{1}{1-MPC} = \frac{1}{1-1} = \frac{1}{0} = \infty$ .

14. The commercial banks are in need of funds in emergency. This happens in times when banks suffer the 'crisis of confidence' of its depositors. The depositors start fearing that the bank may run out of its cash reserves. So they start withdrawing their deposits beyond the limit the bank can afford at a time. It is in such a crisis that the central bank acts as a 'lender of the last resort'. It comes to the rescue of the commercial banks and advances necessary credit/loan against eligible securities. Thus, in this way the central bank helps the commercial banks to cope up with the crisis.

15. Given that,  $C = 200 + 0.5Y$ ,  $I = 400$  and  $Y = 1,500$

At equilibrium level,  $AD = AS$

or,

$$Y = C + I$$

$$Y = (200 + 0.5Y) + 400$$

$$Y - 0.5Y = 600$$

$$Y = \frac{600}{0.5} = ₹ 1,200 \text{ crore}$$

The given income ₹ 1,500 crore is greater than equilibrium level of income ₹ 1,200 crore. Therefore, the economy is not in equilibrium.

16. (a) (i) Expenditure on maintenance of a building will not included in the estimation of national income because it is an intermediate expenditure incurred on the maintenance of an income generating asset.

(ii) Expenditure on fertilizers by a farmer will not be included in the estimation of national income because it is an intermediate cost for the farmer, as fertilizers are used up in the process of production.

(b) Net factor income from abroad is the difference between the factor income received by residents of a country from abroad and the factor income paid to non-residents by the country. It is a part of national income.

Whereas Net exports are the excess of the value of export of goods or services over value of import of goods and services, i.e.,  $X > M$ . It is a part of domestic income, i.e., NDP at Factor Cost.

17. (A) (i) Revenue deficit = Revenue Expenditure – (Tax Revenue + Non-tax Revenue)  
= 3,821 – (1,000 + 2,000)  
= ₹ 821 crores

(ii) Fiscal deficit = (Revenue Expenditure + Capital Expenditure) – (Non-tax Revenue + Tax Revenue + Recovery of Loans + Disinvestment)  
= (3,821 + 574) – (2,000 + 1,000 + 135 + 100)  
= 4,395 – 3,235  
= ₹ 1,160 crores

(B) The two features of capital goods are:

- They are used in future for productive purposes and have expected life time of several years.
- They do not lose their identity in the production process.

*(or any other relevant point)*

**Or**

(C) Government can, through the budget, influence allocation of resources via the market mechanism, with the help of taxes, subsidies and by direct participation in production. Production units which produce harmful products like liquor, cigarettes, pan masala etc. can be heavily taxed. Tax concessions and subsidies should be given to encourage those production units which produce products that are useful for the masses.

Government can also directly produce goods and services which are normally ignored by the private sector, on account of lack of enough profit from their production.

- (D) The government under *Ujjawala Yojana* is providing free LPG kitchen gas connection to families 'below the poverty line'. This is to help the poor people with a clean fuel for cooking purposes. This will improve their eyesight and health. Through this yojana, the government is trying to boost up 'social welfare'. This step will also boost up the morale of the poor. Their productive efficiency will get enhanced, which will have a favourable impact on the national income. The government is trying to fulfil the objective of reducing inequalities in the income distribution.
18. (c) Unrestricted flow of foreign capital
19. (a) 'Mixed economy' as the strategy of growth
20. (d) (i), (ii), (iii) and (iv)
21. (c) Horticulture
22. (b) Great Proletarian Cultural Revolution
23. (a) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A)
24. (d) (i), (ii) and (iii)
25. (a) 6 to 14
26. (a) Statement 1 is true and statement 2 is false
27. (c) C – (iii)
28. (A) The focus of the industrial policies pursued by the colonial government in India was to make our country a mere supplier of Britain's own flourishing industrial base. The policies were concerned mainly with the fortification and advancement for their own country. The industrial policy pursued by the British colonial administration has the following shortfalls:
- (i) **Neglect of Indian Handicraft Industries:** The British followed a discriminatory tariff policy under which they imposed heavy tariffs (export duties) on India's export of handicraft products while allowed free export of India's raw material to Britain and free import of British products to India. This made Indian exports costlier and its international demand fell drastically leading to the collapse of handicrafts industries. Also, Indian handicrafts faced a stiff competition from machine made textiles of Britain.
  - (ii) **Lack of Investment in Indian Industries :** The modern industries in India demanded investments in capital goods that were beyond the means of Indian investors. On the other hand, British government was least interested in investing in Indian industries. Thus, due to the lack of sufficient investment, the growth of Indian industries was acutely constrained. (or any other relevant point)

**Or**

(B) The sectoral composition of an economy is the contribution of different sectors to total GDP of an economy during a year, *i.e.*, the share of agricultural sector, industrial sector and service sector in GDP.

Yes, it is necessary that at the later stages of development, service sector should contribute the maximum to the total GDP. This phenomenon is called structural transformation. This implies that gradually the country's dependence on the agricultural sector will shift from the maximum to minimum and, at the same time, the share of industrial and service sector in the total GDP will increase. This structural transformation together with the economic growth is termed as economic development.

29. • Human capital refers to the stock of a nation's human skills and expertise at a particular point of time whereas human development refers to holistic development and well-being of a nation's human capital.
- On one hand, human capital considers education and health as a means (skills and expertise) to enhance productive capacity, on the other hand human development considers human beings as end in itself.
- Human capital and human development are interrelated concepts but they are not identical. *(or any other relevant point)*

30. Yes, it cannot be denied that China's rapid industrial growth is an aggregate outcome of the various economic reforms that were introduced in phases since 1978. In the initial phase, reforms were initiated in agriculture, foreign trade and investment sectors.

In agriculture, for instance, commune lands were divided into small plots that were allocated to the individual households. These households were allowed to keep the remaining income from land after paying the taxes to the government. In the later phase, reforms were initiated in the industrial sector.

During this phase, the private firms and village and township enterprises were allowed to produce goods and services and to compete with the State Owned Enterprises.

The reforms also included dual pricing. The dual pricing implies that the farmers and the industrial units were required to buy and sell a fixed quantity of inputs and output at the price fixed by the government and the remaining quantities were traded at the market price. Gradually, with the rapid increase in the aggregate production in the later years, the quantities traded in the market increased by many folds.

The reforms also included setting up of Special Economic Zones to attract foreign investors. Therefore, China's rapid industrial growth is attributable to the success of different phases of its economic reforms.

31. (A) (i) True, as Self-help Groups are micro-credit programmes set up to promote thrift in small proportions by a minimum contribution from each member. Micro-credit is a common form of micro-finance that involves an extremely small loan given to an individual to help them become self-employed or grow a small business.

- (ii) False, as benefits of physical capital accrue to the owner only. However, human capital benefits not only the owner but also the society in general. This is called external benefit. An educated person can effectively take part in a democratic process and contribute to the socio-economic progress of a nation.

**Or**

- (B) A shift from subsistence farming to commercial farming is always useful. Provided, that the shift is economically viable. In India, most farming land is held by a small number of big farmers. A large number of farmers operate small farm-holdings, smaller than even one hectare in size. Shifting from subsistence farming to commercial farming is economically viable only when holdings are large. So large, that mechanisation is possible on these holdings. Only when mechanisation is adopted that the productivity would rise. Only when productivity rises, that the cost of farming would reduce. Only when the cost of farming reduces that the farming becomes economically viable. Mechanisation is not economically viable when holdings are small. This deters the small farmers from shifting to commercial farming. Instead, they stick to subsistence farming. It does not generate any surplus or profits. But, it certainly ensures them the necessary supplies of grains for self-consumption. They are not exposed to the uncertainties of the market.
32. The given picture depicts the situation of disguised unemployment in the Indian economy. Disguised unemployment is a kind of unemployment in which there are people who are visibly employed but are actually unemployed. This situation is also known as hidden unemployment. In such a situation more people are engaged in a work than required. Disguised unemployment is mostly found in agricultural sector in rural areas in India where 10 members of a farmer's family are employed on a small piece of land when five are enough. In India, 25 percent to 30 percent of the working population in rural areas suffer from disguised unemployment.
33. (A) No, 'Modernisation' as a planning objective does not contradict employment generation. In fact both modernisation and employment generation are positively correlated. While modernisation refers to the use of new and modern technology in production process that may make some people lose their jobs in the initial stages. But gradually, the use of modern technology and input will raise the productivity and, consequently, the income of the people that will further raise the demand for goods and services. In order to fulfill this increased demand, there will be more job opportunities that will lead more people to be hired and, hence, more employment opportunities will be generated. Hence, both modernisation and employment generation are not contradictory but are complementary to each other.
- (B) An efficient and profit earning PSU is a revenue generator for the government. But if, a PSU is an inefficient and loss making one, then the same PSU exerts unnecessary burden on the government's scarce revenues and further may lead to budget deficit. The loss making PSUs should be privatised, whereas it would not be fair to privatise a profit making PSU. Privatising a PSU may lead to concentration of monopoly power in the private hands.



Further some of the PSUs like, water, railways, etc. enhance the welfare of nation and is meant to serve general public at a very nominal cost. Privatisation of such important PSUs will lead to loss of welfare of poor people. Hence, only less important PSUs should be privatised while leaving the core and important PSUs to be owned by the public sector. Instead of privatisation of profit-making PSUs, government can allow more degree of autonomy and accountability in their operations, which will not only increase their productivity and efficiency but also enhance their competitiveness with their private counterparts.

**Or**

(C) Under the colonial rule, India was basically an agrarian economy, employing nearly 85% of its population. Nevertheless, the growth of the agriculture sector was meager. The causes explaining stagnancy in Indian agriculture sector during the colonial rule are:

(i) **Introduction of Land Revenue System:** This was due to prevalence of various systems of Land Settlement, particularly *zamindari* system. This system was introduced by Lord Cornwallis in Bengal in 1793. Under this system, the *zamindars* (owners of land) were required to pay very high revenue (*lagaan*) to the British government, which they used to collect from the peasants (landless labourers, who were actually cultivating). The *zamindars* were mainly concerned with extracting high revenues from the peasants but never took any steps to improve the productivity of the land. This resulted in low agricultural productivity and worsened the peasants economically.

(ii) **Forceful Commercialisation:** Initially before the British rule, the farmers were practicing conventional subsistence farming. They used to grow crops like rice and wheat for their own consumption. But afterwards, in order to feed British industries with cheap raw materials, the Indian farmers were forced to grow commercial crops (like indigo required by British industries to dye textiles) instead of food crops (like rice and wheat). This led to the commercialisation of Indian agriculture. This commercialisation of Indian agriculture not only increased the burden of high revenues on the poor farmers but also led India to face shortage of food grains, resources, technology and investment. Therefore, Indian agriculture remained backward and primitive.

(iii) **Lack of Irrigation Facilities and Resources:** Besides the above factors, Indian agricultural sector also faced lack of irrigation facilities, insignificant use of fertilisers, lack of investment, frequent famines and other natural calamities, etc. that further exaggerated the agricultural performance and made it more vulnerable.

(D) The given statement is incorrect as the process of globalisation has produced positive as well as negative results. Globalisation has been criticised because:

- Benefits of globalisation accrue to developed countries as they are able to expand their markets in other countries.

- Globalisation compromises the welfare and identity of people belonging to poor countries.
  - Market-driven globalisation increases the economic disparities among nations and people.
34. (a) Global warming is a gradual increase in the average temperature of the earth's lower atmosphere as a result of the increase in greenhouse gases since the Industrial Revolution.
- (b) Much of the recent observed and projected global warming is human-induced. It is caused by man-made increases in carbon dioxide and other greenhouse gases through the burning of fossil fuels and deforestation. Adding carbon dioxide, methane and such other gases (that have the potential to absorb heat) to the atmosphere with no other changes has made our planet's surface warmer.