

Answers to REC–DS2/Set-2

1. (c) Income and Consumption
2. (b) appreciated; depreciated
3. (b) AD is greater than AS
4. (c) Ministry of Finance
5. (c) Both statements 1 and 2 are true
6. (a) 1280, 10000, 2000, 8000

Working Note:

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

(i) Loans = $1600 \times 80/100 = 1280$

(ii) Deposits = $2000 \times 5 = 10000$

(iii) Cash Reserves = $400 \times 5 = 2000$

(iv) Loans = $1600 \times 5 = 8000$

7. (a) National income will fall
8. (d) ₹ 80,000

Working Note:

Given that, $\Delta I = ₹ 20,000$ and $\text{MPC} = 0.75$

We know that, Multiplier (k) = $\frac{1}{1 - \text{MPC}}$

$$= \frac{1}{1 - 0.75} = \frac{1}{0.25} = 4$$

or, Multiplier (k) = $\frac{\Delta Y}{\Delta I}$

$$4 = \frac{\Delta Y}{20,000}$$
$$\Delta Y = 80,000$$

∴ Change in income = ₹ 80,000 crores

9. (b) (i) and (iii)
10. (d) Current transfers

11. Demand for domestic goods and services includes the total demand for goods and services from within the domestic territory as well as outside the territory, *i.e.*, the total demand of goods and services which is produced domestically, from people living within the domestic country as well as abroad.

On the other hand, **domestic demand for goods and services** includes only the demand of goods and services from within the domestic country, *i.e.*, it includes only the domestic demand of goods and services by consumers living within the domestic territory.

- 12. (a)** (i) Purchase of shares of X Ltd. by an investor in the National Stock Exchange will not be included in the estimation of national income because such transactions are mere paper claims and do not lead to any value addition.
- (ii) Compensation paid by the Government of India to the victims of floods will not be included in the estimation of national income because it is a mere transfer payment and does not lead to any flow of goods and services in an economy. Net factor income from abroad is the difference between factor incomes earned from rest of the world and factor incomes paid to rest of the world.

Or

- (B) (i) **Depreciation:** It means fall in value of fixed capital goods due to normal wear and tear and expected obsolescence. It is also known as consumption of fixed capital.
- (ii) **Flow variable:** The variables whose magnitude is measured over a period of time are called flow variables. For example, national income, change in stock etc.
- (iii) **Investment:** The addition made to the physical stock of capital during a period of time is called investment. It is also known as capital formation.

13. Given that, $S = (-) 50 + 0.2 Y$, $Y = ₹ 2,000$ crores, Consumption Expenditure = ₹ 1,650 crores and Autonomous Investment = ₹ 50 crores

Now,

$$\begin{aligned} S &= (-) 50 + 0.2 (2,000) \\ &= - 50 + 400 = ₹ 350 \text{ crores} \end{aligned}$$

At equilibrium level of income,

$$Y = C + S$$

$$\therefore 2,000 = C + 350$$

$$\begin{aligned} C &= 2,000 - 350 \\ &= ₹ 1,650 \text{ crores} \end{aligned}$$

As $MPS = 0.2$

$$\therefore MPC = 0.8$$

Also, at equilibrium level of income,

$$Y = AD$$

or, $Y = C + I$

$$2,000 = 1,650 + I$$

$$I = ₹ 350 \text{ crore}$$

Autonomous investment will be ₹ 350 crore and not ₹ 50 crore.

So, all the given values are not correct.

14. (A) Inflationary gap refers to excess of aggregate demand over aggregate supply at full employment level of income. This leads to an inflationary situation in the economy.

For controlling inflationary gap, the Central Bank can raise CRR to restrict the flow of credit. If the Central Bank raises CRR, the amount of deposits with the commercial banks are reduced. This reduces the capacity of the commercial banks to create credit. Lending falls and as a result investment falls. Thus, aggregate demand falls and the problem of inflationary gap can be solved.

Or

- (B) When aggregate demand (AD) falls short of aggregate supply (AS) at full employment level of income, there is deficient demand in the economy which leads to deflation. In other words, a situation of deficient demand arises in an economy when $AD < AS$ at the full employment level of income. It causes fall in the price level.

The margin requirement of a loan refers to the difference between the value of the security offered for loan and the value of the loan granted. During deficient demand, Central Bank lowers the margin requirement enabling the borrowers to secure larger loan from the banking system. This helps in increasing the demand for goods and in services in the economy and thereby in removing the deflationary gap.

15. The recent initiatives have affected the banking system in the following ways:

- Total number of bank accounts increased
- Lead to more deposits of money
- Lending capacity of banks increases
- Easing of payments systems
- Availability of loans and investments increased

All these lead to more pumping of money into the economy leading to the overall growth in the national income.

16. (A) (i) Revenue deficit = Revenue expenditure – Revenue receipts

$$\begin{aligned}
 &= [(v) + (vii) + (ix)] - [(i) + (iii)] \\
 &= [300 + 1,700 + 1,200] - [1600 + 700] \\
 &= ₹ 900 \text{ crores}
 \end{aligned}$$

(ii) Fiscal deficit = Revenue deficit – (ii) – (iv) + (viii)

$$\begin{aligned}
 &= 900 - 120 - 150 + 700 \\
 &= ₹ 1,330 \text{ crores}
 \end{aligned}$$

(B) The two examples of non-tax revenue are:

(i) Interest

(ii) Dividend

(or any other relevant example)

Or

(C) Through its budgetary policy, the government directs the allocation of resources in a manner such that there is a balance between the goal of profit maximisation and social welfare. Government can provide subsidy and reduction in tax rate to motivate investment into areas where private sector initiative is not coming. Production of goods which are injurious to social life is discouraged through heavy taxation.

(D) Revenue expenditure is the expenditure made by the government that neither creates any asset nor reduces any liability, whereas the capital expenditure is the expenditure incurred by the government that either creates assets or reduces liabilities.

Example of Revenue Expenditure: Expenditure on salaries, interest, are examples of revenue expenditure.

Example of Capital Expenditure: Expenditure on land, machinery etc. are examples of capital expenditure.

17. Operating Surplus = $(ii) - (iv) - (i) - (vi)$
= $4,200 - 200 - 2,400 - 400$
= ₹ 1,200 crores

Net Exports = $(ii) - (iv) + (xi) + (viii) - (vii) - (x) - (v)$
= $4,200 - 200 + 100 + 150 - 2000 - 1000 - 1,100$
= ₹ 150 crores

18. (b) Literacy rate

19. (b) Pt. Jawaharlal Nehru

20. (d) (ii) and (iii)

21. (a) Animal husbandry

22. (c) Both (i) and (ii)

23. (b) Pakistan

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

25. (b) Regional balanced development

26. (b) Statement 1 is false and Statement 2 is true

27. (b) B – (ii)

28. (A) Brain drain refers to migration of skilled manpower to developed countries of the world. Obviously, they migrate for greener pastures. Those who migrate include scientists, engineers, doctors and educationists. These are the people of high calibre. Migration of such people is a serious bottleneck in human capital formation in India. We know skill is an important ingredient of growth. Loss of skill causes a dent in the process and pace of growth.

Or

(B) Human capital formation is an important means of reducing inequality of income. Higher the rate of capital formation, greater would be the rate of participation. Increase in the rate of participation would lead to increase in the share of wages in national income. Accordingly, inequality would reduce.

29. The following are the various steps initiated by the Indian government to develop the rural markets:

(a) **Regulated Markets:** The government came up with the concept of regulated markets where the sale and purchase of the products are monitored by the Market Committee. This Market Committee consists of farmers, government agents and traders. This practice infuses greater transparency in the marketing system through the use of proper scales and weights. Such committees ensure the farmers and the consumers in receiving fair price in exchange of their products.

(b) **Infrastructure Development:** The present infrastructure is not sufficient to meet the growing demands of the farmers. Indian government provided cold storages and warehouses that help the farmers to sell their product at the time when the price is attractive. Also, railways offer subsidised transport facilities to the farmers. This enables the farmers to bring their product to urban areas where they can earn huge profits.

(c) **Co-operative Agricultural Marketing Societies:** The government also started co-operative marketing under which the farmers get access to fair prices. This is due to the better and enhanced bargaining power of the farmers via collective sale in the market.

(d) **MSP Policy:** Minimum Support Price is a minimum legislated price that a farmer may charge in exchange for his products. This enables them to sell their products in the open market at a higher price. The MSP insulates the farmers in case of price fall as this is the minimum price that they can receive. The need of such assurance to the farmers is of immense importance as farming in India is subject to many uncertainties. (any three)

30. Yes, outsourcing is good for India. The following points suggest that outsourcing is good for India.

- (a) **Employment:** For a developing country like India, employment generation is an important objective and outsourcing proves to be a boon for creating more employment opportunities. It leads to generation of newer and higher paying jobs.
- (b) **Exchange of technical know-how:** Outsourcing enables the exchange of ideas and technical know-how of sophisticated and advanced technology from developed to developing countries.
- (c) **International worthiness:** Outsourcing to India also enhances India's international worthiness credibility. This increases the inflow of investment to India.
- (d) **Contributes to human capital formation:** Outsourcing helps in the development and formation of human capital by training, imparting them with advanced skills, thereby, increasing their future scope and their suitability for high ranked jobs.
- (e) **Better standard of living and eradication of poverty:** By creating more and higher paying jobs, outsourcing improves the standard and quality of living of the people in the developing countries. It also helps in reducing poverty.
- (f) **Greater infrastructural investment:** Outsourcing to India requires better quality infrastructure. This leads to the modernisation of the economy and larger investment by the government to develop quality infrastructure and develop quality human capital. (any three)

However, Outsourcing to India is good but developed countries oppose this because outsourcing leads to the outflow of investments and funds from the developed countries to the less developed countries. Also the MNCs contribute more to the development of the host country than the home country. Further, outsourcing reduces the employment generation in the developed countries as the same jobs can be done in the less developed countries at relatively cheap wages.

31. (A) (i) False, as foreign trade was characterised by inward looking trade strategy, known as import substitution, in which the government makes serious efforts to replace imported goods by domestically produced goods. The objective of this policy was to make India self-reliant.
- (ii) True, as according to Industrial Policy Resolution 1956, the industries were classified into three categories, *i.e.*,
- Schedule A:** Comprised industries owned by the state.
- Schedule B:** In this schedule 12 industries were placed which would be progressively state owned.
- Schedule C:** Consisted of remaining industries which were to be in the private sector.

Or

- (B) Green Revolution led to an increase in the production of food grains. With the use of modern technology, extensive use of fertilisers, pesticides and HYV seeds, there was a significant increase in the agricultural productivity and product per farm land. In addition, the spread of marketing system, abolition of intermediaries and easy availability of credit has enabled farmers with greater portion of marketable surplus. All these factors enabled the government to procure sufficient food grains to build the buffer stock and to provide cushion against the shocks of famines and shortages.
32. The given image depicts the situation of rural unemployment. The following are the suggestions that can generate employment opportunities in village:
- (a) **Increase production:** It is of prime importance to increase production in the agricultural and industrial sectors in order to increase employment. For this purpose, small scale and cottage industries should be promoted. This will not only generate new employment opportunities but also assist the industrial sector, as the production of the small scale and cottage industries act as subsidiaries to the industrial sector.
- (b) **Increase Productivity:** The demand and productivity for labour are directly related to each other. The higher productivity generates higher profits that in turn implies higher investment and generates higher demand for labour. Rural workers should be imparted technical knowledge and modern know-how that will not only increase their productivity but also enhance their acceptability of modernisation.

- (c) **Creating non-agricultural employment:** India being an agrarian economy employs a major proportion of workforce in the agricultural sector. The development of this sector is still a far cry and, consequently, suffers from disguised unemployment. Moreover, as agriculture is a seasonal occupation, so, many farmers remain unemployed for three to four months in a year. Thus, it is necessary to engage these people in non-agricultural sectors for the phase they are off from cultivation. Creation of non-agricultural job like pottery, handicrafts, not only reduces disguised unemployment but also contributes to enhanced income to the farmers in the off-season, which could be invested in the farm to improve farm productivity and farm products.
- (d) **Easy credit and finance:** Often, the rural people find it difficult to access finance due to the lack of sufficient financial institutions in the rural areas. Even if the finance or the credit is available, then this is provided at higher lending rates. The lack of credit acts as a bottleneck for the rural growth. Thus, financial institutions and banks should be set up to provide easy credit to the rural people.
- (e) **Education and Health Facilities:** Rural areas have always lagged behind in education and health care facilities. This not only impedes their productivity but also reduces their life expectancy and quality of standard of living. Along with primary and secondary schools, night schools for adults, imparting technical education and technical know-how, proper sanitation and hospitals should be established in the rural areas. (any three)
33. (A) The Great Leap Forward (GLF) was a campaign initiated in 1958 in China. The aim of the campaign was to initiate large scale industrialisation in the country concentrating not only in the urban areas but also in the rural ones. The people in the urban areas were motivated to set up industries in their backyards. In the rural areas, Commune System was implemented. Under this system, people were engaged in collective farming.
- (B)
- With the aim of economic development, Pakistan adopted the pattern of mixed economy where both private and public sectors coexist.
 - Pakistan introduced a variety of regulated policy frameworks for import substitution, industrialisation during 1950s and 1960s. This implies producing goods domestically to substitute imports, thereby, discouraging imports and simultaneously encouraging and developing domestic industries.
 - In order to protect domestic industries producing consumer goods, policy measures were initiated to create tariff barriers.

- The introduction of Green Revolution mechanised agriculture leading to the increase in the production of food grains.
- The mechanisation of agriculture was followed by the nationalisation of capital goods industries in 1970s.
- In the late 1970s and early 1980s, Pakistan shifted its policy orientation by denationalising the thrust areas, thereby, encouraging the private sector.

All these above measures created an environment conducive to initiate the economic reforms that were ultimately initiated in 1988.

OR

(C) Liberty indicators may be defined as the measure of the extent of demographic participation in the social and political decision-making. In other words, it is an index used to measure the participation of the people in taking decisions. Some examples of liberty indicators are the measures of the extent of the Constitutional Protection Rights given to the citizens and the extent of the Constitutional Protection of the independence of the Judiciary and Rule of Law.

(D) India, with democratic institutions, performed moderately, but the majority of its people still depend on agriculture. Infrastructure is lacking in many parts of the country. It is yet to raise the standard of living of more than one-fourth of its population that lives below the poverty line.

On the other hand, the lack of political freedom and its implications in China are the major concern in the last two decades. The country used the market system without losing political commitment and succeeded in raising the level of growth along with poverty alleviation. China used the market mechanism to create additional social and economic opportunities. It has also ensured social security in the rural areas by retaining collective farming known as Commune System.

34. (a) Global warming refers to the phenomenon of sustained increase in global temperature due to environmental pollution and deforestation. It is caused by the emission of green house gases that include, particularly, carbon dioxide. The increase in the level of carbon dioxide raises the temperature of the earth surface. This risen temperature accelerates the melting of polar ice that further leads to the rise in the sea level. Thus, the incidence of natural calamities rises due to disturbed ecological balance, thereby, posing a threat to human life.

(b) Some of the major effects of global warming are:

- (i) **Rise in temperature:** Global warming has led to an incredible increase in earth's temperature. Since 1880s, the earth's temperature has increased by 1 degrees. This has resulted in an increase in the melting of glaciers, which have led to an increase in the sea level. This could have devastating effects on coastal regions.
- (ii) **Threats to the ecosystem:** Global warming has affected the coral reefs that can lead to the loss of plant and animal lives. Increase in global temperatures has made the fragility of coral reefs even worse.
- (iii) **Climate change:** Global warming has led to a change in climatic conditions. There are droughts at some places and floods at some. This climatic imbalance is the result of global warming.
- (iv) **Spread of diseases:** Global warming leads to a change in the patterns of heat and humidity. This has led to the movement of mosquitoes that carry and spread diseases.
- (v) **High mortality rates:** Due to an increase in floods, tsunamis and other natural calamities, the average death toll usually increases. Also, such events can bring about the spread of diseases that can hamper human life.
- (vi) **Loss of natural habitat:** A global shift in the climate leads to the loss of habitats of several plants and animals. In this case, the animals need to migrate from their natural habitat and many of them even become extinct. This is yet another major impact of global warming on biodiversity.

(any four)