

Answers to REC/Set 2

1. (a) A
2. (a) Foreign Direct Investment inflow and outflow
3. (a) Statement 1 is true and statement 2 is false
4. (a) Reduce cash reserve ratio
5. (c) Assertion (A) is true but Reason (R) is false
6. (c) $GNP_{MP} = GDP_{MP} + \text{Net Factor Income from Abroad}$
7. (d) ₹ 800 crores

Working Note:

Given that, $MPC = 0.75$

Change in investment (ΔI) = ₹ 200 crores

$$\text{Multiplier } (k) = \frac{1}{1 - MPC} = \frac{1}{1 - 0.75} = \frac{1}{0.25} = 4$$

$$k = \frac{\Delta Y}{\Delta I}$$

$$\begin{aligned} \therefore \text{Increase in income } (\Delta I) &= 4 \times 200 \\ &= ₹ 800 \text{ crores} \end{aligned}$$

8. (a) Economic growth and redistribution of income
9. (d) None of the above
10. (c) Both statements 1 and 2 are true
11. (A) Government's spending on child immunisation programme is government's final consumption expenditure. Hence, it will raise the Gross Domestic Product (GDP). Such a programme like child immunisation improves the health of the children. It will raise the efficiency level in the long-run, as these children will grow up into healthy adults with a higher efficiency level. This will thereby increase the welfare of the people.

Or

(B) Yes, I agree with the given statement. In a two-sector economy model, households are the owners of factors of production (Land, Labour, Capital, Entrepreneur). Firms combine these factors of production to produce goods and services. They make factor payments (Rent, Wages, Interest, Profits) to households, which in turn, are completely spent by the households on the consumption of final goods and services. Thus, the income earned by the factors of production flows back to the production units in the form of aggregate consumption expenditure.

12. (i) $\text{Fiscal deficit} = \text{Borrowings}$
 $= ₹ 15,000 \text{ crore}$
- (ii) $\text{Revenue deficit} = \text{Revenue expenditure} - \text{Revenue receipts}$
 $= 70,000 - 50,000$
 $= ₹ 20,000 \text{ crores}$
 $\text{Interest payments} = 25\% \text{ of revenue deficit}$
 $= 20,000 \times \frac{25}{100}$
 $= ₹ 5,000 \text{ crore}$

$$\begin{aligned}
 \text{Primary deficit} &= \text{Fiscal deficit} - \text{Interest payments} \\
 &= 15,000 - 5,000 \\
 &= ₹ 10,000 \text{ crore}
 \end{aligned}$$

13. The two monetary measures that can be used by the Central Bank to control the inflation are:
- Increase in policy rate (Repo rate/Bank rate):** Raising the repo or bank rate makes short-term funds costlier for commercial banks when they borrow from the central bank. Banks pass on this higher cost to borrowers by increasing lending rates, which discourages new loans for consumption and investment. As borrowing falls, aggregate demand softens and price pressures ease. Over time higher policy rates also encourage saving, further reducing spending — both effects help cool inflation.
 - Open Market Operations (Sale of government securities):** When the central bank sells government securities in the open market, buyers pay for those securities using their bank balances, so liquidity is withdrawn from the banking system. With less cash available, banks have fewer funds to lend, which tends to push up market interest rates and reduces credit creation. The resulting contraction in money supply and credit dampens consumer spending and investment, thereby reducing demand-driven inflation. *(or any other relevant point)*
14. The different functions of money being performed in the given case are:
- Medium of Exchange:** Mr. Dev uses money to buy coffee beans and milk, to pay his barista's wages and utility bills, and customers use money (UPI/card/cash) to buy coffee. This shows money's role as a medium of exchange that facilitates transactions and eliminates the need for barter.
 - Store of Value:** The day's receipts are kept in the cash box and the surplus is deposited into a bank savings account. This demonstrates money's function as a store of value — it preserves purchasing power so Mr. Dev can use it in the future.
 - Unit of Account (Measure of Value):** Prices such as ₹ 2,500 for beans, ₹ 600 wage, and ₹ 80 per cup express value in monetary terms. This shows money acting as a unit of account, providing a common measure for valuing goods and services and comparing costs.
 - Standard of Deferred Payments:** When Mr. Dev allows a regular customer to pay after a week, the repayment is agreed in monetary terms (e.g., ₹ X after 7 days). This illustrates money's role as a standard of deferred payments — it is acceptable for settling debts at a future date.

15. (A) No, I do not agree with Ravi's classification.

The receipt of \$3 million for software exports is recorded as a credit entry in the current account under export of services. This is an autonomous transaction because it is undertaken for profit and is not related to correcting a Balance of Payments deficit.

The purchase of \$2 billion by the Reserve Bank of India from the foreign exchange market is an official reserve transaction aimed at influencing the exchange rate. Such transactions are accommodating transactions as they are meant to correct imbalances in the Balance of Payments, not for earning profits.

Therefore, only the first transaction is autonomous, while the second is accommodating.

Or

- (B) Devaluation and Depreciation of currency are not one and the same thing. This is because devaluation refers to the fall in the value of domestic currency w.r.t. foreign currency as planned by the government (it is fixed by the government) whereas depreciation refers to the fall in the value of domestic currency in relation to foreign currency w.r.t. a situation where exchange rate is determined by the market forces of demand and supply for foreign exchange in the international money market. No matter both cause a fall in the value of domestic currency.

16. (A) (i) $NDP_{FC} = (ii) + (i) + (iv)$
 $= 3,000 + 700 + 700$
 $= ₹ 4,400 \text{ crore}$

(ii) The statement stands defended as the 'Interest on National Debt' should not be included in the estimation of national income, because it is treated as a transfer payment. It is presumed to be paid for unproductive borrowing. It does not contribute to the current flow of goods and services.

Or

(B) (i)

Firms	Value of Output (in ₹) (i)	Intermediate Consumption (in ₹) (ii)	Value Added (in ₹) {(i) – (ii)}
A	2,000 + 1,200	1,100	2,100
B	1,100 + 3,500	2,000	2,600
C	5,700	1,200 + 3,500	1,000
	13,500	7,800	5,700
Gross Domestic Product at Market Price (GDP_{MP})			

Net Domestic Product at Market Price (NDP_{MP}) = $GDP_{MP} - \text{Depreciation}$
 $= 5,700 - 120$
 $= ₹ 5,580$

(ii) No, as capital goods are those final goods which help in the production of other goods and services. A machine purchased by a firm will be a capital good when it is used for the production of other goods and services. However, if it is purchased by a firm for resale purposes in the same year, it will be considered as an intermediate good and not a capital good.

17. (a) The effects of GST rationalisation on AD and AS are:

- (i) **Higher Aggregate Demand (AD):** With a lower tax burden on essential and commonly used goods, consumers now have more disposable income in hand. This has increased their purchasing power and led to greater overall consumption in the economy.
- (ii) **Boost to Investment:** A stable and transparent GST structure has created more certainty for businesses. As compliance has become easier and profits have improved, firms are encouraged to invest more in production and expansion.
- (iii) **Improved Aggregate Supply (AS):** Simplified GST rules have reduced compliance costs for firms and lowered overall production expenses. This makes it easier for businesses to operate efficiently, expand their scale, and contribute to higher supply in the economy.
(or any other relevant point)

(b) The difficulties after GST rationalisation are:

- (i) **Revenue Concerns:** With reduced tax slabs and rationalised rates, the government may face challenges in collecting enough revenue. This could limit its ability to finance developmental programmes and welfare schemes.

- (ii) **Inflationary Pressure:** Certain goods and services have been moved to higher tax slabs. This can lead to an increase in their prices, creating inflationary pressure and reducing affordability for consumers.
- (iii) **Unequal Benefits:** While large firms benefit quickly due to better resources and systems, small businesses and weaker sections may not gain equally. The benefits of GST simplification may not reach them in the same way, creating inequality.

(or any other relevant point)

18. (a) A – (iii), B – (iv), C – (i), D – (ii)
19. (b) Liberty indicator
20. (b) Assertion (A) and Reason (R) are true but Reason (R) is not the correct explanation of Assertion (A)
21. (a) Karve
22. (c) Moneylenders
23. (d) BRICS
24. (b) Statement 1 is false and Statement 2 is true
25. (a) Mao Zedong
26. (c) Temporary inconvenience and economic disruption
27. (d) Only (ii)
28. (A) The formal sector workers can form trade unions and are entitled to fair wages and other social security measures. However, workers in the informal sector do not get regular income. Additionally, they do not have any protection/regulation from the government. Many a times, workers may be dismissed without any compensation.

Hence, formal sector employees are generally in a better position as compared to informal sector employees. Therefore, it is essential to generate employment in the formal sector rather than the informal sector.

Or

(B) Rapid expansion of the banking system had positive effect on rural farm and non-farm output, income and employment. In spite of it, following problems have been faced in the rural banking:

- The volume of rural credit in the country is still insufficient in comparison to its demand and institutional sources have failed to cover the entire rural farmers of the country.
- Less attention has been given on the credit requirements of needy (small and marginal farmers) and the problem of overdue in agricultural credit continues.

(or any other relevant point)

29. Yes, I agree with the given statement. Basic infrastructure such as railways, posts and telegraphs were developed to serve the interest of the colonial regime. Roads and railways were built primarily to mobilise the army within India, drawing out raw materials from the countryside. In addition, communication tools like telephone and telegraph were introduced to maintain law and order. Thus, the real motive behind this development was not to provide basic amenities to the people of India but to serve various colonial interests.

30. (a) Panel A – Global warming and environmental degradation
Panel B – Sustainable development and environmental conservation
- (b) **Advantage of Panel B:** Cleaner environment, use of renewable resources, healthier ecosystems, and long-term survival of life *(or any other relevant point)*
Disadvantage of Panel B: High initial cost of renewable energy and sustainable practices, requiring more investment and awareness *(or any other relevant point)*
31. (a) China is the most populous country in the world. Its annual population growth rate was very high. The one-child norm introduced in China in the late 1970s is the major reason for fall in the population growth rate. However, this measure led to a decline in the sex ratio. The number of females per 1000 males in China is approximately 949. One-child policy and prevalent son-preference is the prime reason behind the skewed sex ratio.
- (b) The reasons for the slow growth and re-emergence of poverty in Pakistan are:
- Agricultural growth and food supply situation were not based on institutional process of technical change but on good harvest. Hence, Pakistan faced a volatile performance in the agriculture sector.
 - Overdependence on remittances and foreign aid on the one hand and increasing difficulty in paying back the loans on the other. *(or any other relevant point)*
32. (A) 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. *(or any other relevant point)*

Or

- (B) 'Organic farming' is a whole system of farming that restores, maintains and enhances the ecological balance. It promotes sustainable development by offering a means to substitute costlier agricultural inputs with locally produced organic inputs that are cheaper and thereby fetch good returns on investment.
- It generates income, by way of exports, on account of rising demand for organically grown crops.

- It provides people with healthy foods.
 - Since it requires more labour input than conventional farming, so it turns out to be an attractive proposition.
 - The organic produce is pesticide-free and produced in an environmentally sustainable way.
33. (A) (i) Yes, in order to improve efficiency, infuse professionalism and enable Public Sector Undertakings (PSUs) to compete more effectively in the liberalised global environment, the government identified profit making PSUs. Government declared them as Maharatnas, Navratnas and Miniratnas. PSUs were given greater managerial and operational autonomy, in taking various decisions. As a result, over the years these Maharathas, Navratnas and Miniratnas have performed exceedingly well and established themselves as market leaders.
- (ii) Land reforms were inevitable in the post-independence era. The policy makers of independent India introduced land reforms such as land ceiling, abolition of intermediaries etc.
- Land ceiling means fixing up the maximum size of landholding which could be owned by an individual. This step was essential to promote equity in the agricultural sector so as to reduce the concentration of land ownership in a few hands.

Or

- (B) (i) In order to protect domestic industries, India followed the import substitution policy. This policy aimed at substituting imports with domestic production. The domestic industries were protected from foreign competition by using the following tools:
- **Tariffs:** Tariffs are a tax on imported goods that make imported goods dearer and discourage their usage.
 - **Quotas:** Quotas specify the quantity of goods that can be imported.
- (ii) Before the advent of Green Revolution, a large proportion of agricultural produce was consumed by the farmers themselves instead of being sold in the market. Green Revolution led to an increase in the growth of agricultural output.
- After the Green Revolution, a greater proportion of the agro-produce (wheat and rice) was sold by the farmers in the market. That led to the attainment of marketed surplus and converted India into a food surplus economy from the food scarce one.
34. (a) Human capital considers education and health as a means to increase labour productivity. On the other hand, human development considers education and health as being integral to human well-being because only when people are educated and healthy, they will be able to make better choices.
- (b) Enlarging the range of people's choices, increasing their opportunities for education, health care, income and empowerment and covering the full range of human choices from a sound physical environment to economic, social and political freedom are the significant aspects of human development.
- (c) The Human Development Report is published by the United Nations Development Programme (UNDP) since 1990.