

# MONEY AND CREDIT

## Syllabus

- *Money as a medium of exchange*
- *Modern forms of money*
- *Loan activities of Banks*
- *Two different credit situations*
- *Terms of credit*
- *Formal sector of credit in India*
- *Self Help Groups for the Poor*



## Learning Outcomes

- *Understand money as an economic concept.*
- *Understand the role of financial institutions from the point of view of day-to-day life.*

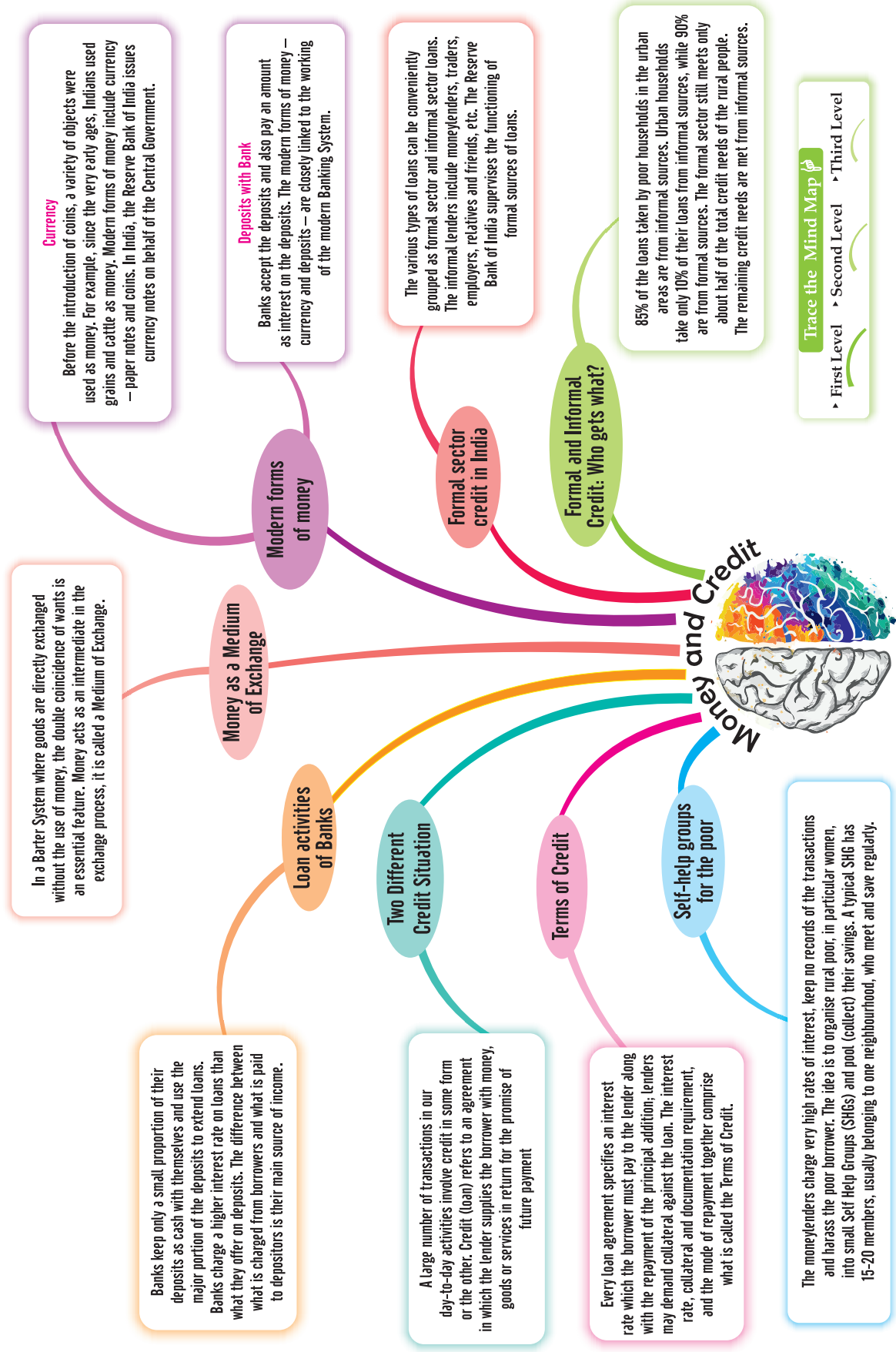


## Revision Notes

## Money and Credit

### Introduction

- In the early times, people used to exchange one commodity for another, depending on their requirement under the Barter System. However, exchanging goods in the barter system required a double coincidence of wants.
  - Barter system was used in ancient times for the exchange goods. It was a system where one commodity, product or some goods was exchanged for another. For instance, if a person has 1 kg of sugar and he wants to have 1 kg of jaggery in exchange for that, he can exchange the same if there is someone who is willing to exchange jaggery for sugar. This process was called a commodity for commodity exchange.
- However, money eliminates the need for double coincidence of wants. Since money enables the exchange process, it is also called a medium of exchange.
  - **Limitations of Barter Exchange:**
    1. Lack of Double Coincidence of Wants
    2. Lack of Common Measure of Value
    3. Lack of Standard of Deferred Payment
    4. Lack of store of value



Trace the Mind Map

► First Level ► Second Level ► Third Level

- Money is anything which is commonly accepted as a medium of exchange and in the discharge of debts.
- Before the introduction of coins, a variety of objects were used as money. For example, since the very early ages, Indians used grains and cattle as money. Thereafter, came the use of metallic coins—gold, silver, copper coins.
- **Modern currency:**
  - Modern forms of money include
  - currency — paper notes and coins.
  - money is as deposits with banks.

The other forms is which people hold.
- In India, the Reserve Bank of India is the only legal authority that can issue currency notes and coins on behalf of the Central Government. The rupee is India's currency and nobody can refuse to accept a payment made in rupees in India.
- People deposit their additional cash in the bank. A bank in addition to accepting deposits, also pays interest on the deposit to the depositor. Thus, bank deposits are also called demand deposits.
- A person simply needs to have an account with the bank to deposit money. A cheque can be used to make payment directly from a bank deposit without using cash.
- A cheque is a written instruction to a bank by an account holder to pay a specific sum to a specific person from his deposit. A cheque has all the information about the person to whom payment is to be made, the amount and date of payment and signature of account holder issuing the cheque.

## Credit Terms and Types

- As per the Reserve Bank of India, banks hold about 15% of their deposits as cash to arrange for daily withdrawals by depositors.
- A major portion of the remaining deposits is used by banks to give loans to people. The depositors of a bank are allowed to withdraw their deposits on demand and are paid interest on their deposits. The borrowers taking loans to repay it to the bank along with interest.
- The interest charged on loans is more than the interest paid by the banks on deposits. The difference between the interest charged on loans and the interest paid on deposits is the bank's income or profit.
- The loan given by a bank is also referred to as a credit.
- Credit (loan) refers to an agreement in which the lender supplies the borrower with money, goods or services in return for the promise of future payment.
- The idea behind Self-Help Groups is to organise the rural poor into self-help groups and collect their savings. Members can take small loans from the group itself to meet their own needs.
- A typical SHG has 15-20 members who meet and save regularly. Saving per member varies from Rs 25 to Rs 100 or more, depending on the ability of the people to save.
- **A loan or credit is subject to certain conditions that the borrower must agree to. These conditions are called terms of credit and include:**
  - A specified rate of interest.
  - Security against the loan to recover the money if the borrower fails to repay it. This security is called collateral.
  - The assets accepted as collateral are land or property, vehicles, livestock, standing crops and bank deposits.
  - A borrower needs to submit certain documents like proofs of identity, residence, employment and income to avail a loan.
  - The lender reserves the right to sell the collateral in case of non-repayment to recover the loan amount.
- Collateral is an asset that the borrower owns (such as land, building, vehicles, livestock etc.) and uses this as a guarantee to the lender until the loan is repaid.
  - Interest rate, collateral and documentation requirement, and the mode of repayment together comprise what is called the terms of credit.
- **The different sources of credit are:**
  - Banks
  - Traders
  - Cooperative societies
  - Landlords
  - Moneylenders
  - Relatives and friends
- **Formal and Informal Credit**
  - Formal credit is generally available with the banks and cooperatives. They charge lesser rates of interest than informal institutions. The Reserve Bank of India (RBI) supervises the functioning of the formal sources of loan.
  - Informal lenders include moneylenders, traders, employers, relatives and friends, etc. They charge much higher interest on loans. There is no one to stop them from using unfair means to get their money back.



## Know the Terms

- **Barter System:** Barter refers to the direct exchange of goods and services. In this way, the barter system refers to the system by which one commodity is exchanged for another without the use of money.
- **Money:** Money may be anything chosen by common consent as a medium of exchange. It can be in the form of coins and bank notes collectively.
- **Cheque:** A cheque is a paper instructing the banks in writing to pay a specific amount from the person's account to the person in whose name the cheque has been issued.
- **Reserve Bank of India:** The Reserve Bank of India is the only legal authority that can issue currency notes and coins on behalf of the central government.
- **Investment:** Investment is the amount of money spent with the intention of earning income at regular intervals (in the form of return from funds invested) or in the long run (in the form of capital appreciation).
- **Credit:** Credit means giving money on loan to needy persons.
- **Financial Formal Institutions:** Commercial banks, cooperatives and the regional rural banks are the formal institutions of credit.
- **Financial Informal Institutions:** The informal framework for the deployment of credit and savings in India comprises the local moneylenders, landlords, self-help groups, chit fund, employers, relatives, friends and private finance companies.
- **Commercial Bank:** A commercial bank is an establishment for safe custody of money, which it pays out on customer's demand order or otherwise. In other words, institutions accepting deposits and issuing loans are called commercial banks.
- **Loans:** A loan is usually given for a specific duration of time and needs to be completely repaid by a specified date.
- **Collateral:** Collateral is the security provided by a borrower (such as land, building, vehicle, livestock, deposits with banks) against a loan, and it can be sold in case of non-payment of loan.
- **Fixed Deposits:** These are deposits for a fixed term varying from a frequency of a few days to a few years.
- **Actual Investment:** The actual amount of investment is called an actual investment.
- **Deferred Payments:** Payments which are to be made in the future are known as deferred payments.
- **Token coins:** Token coins are the coins where value as money is far above the value of metal contained in it.
- **Short-term loans:** Loans given for a short period of time are known as short-term loans.



## (A) OBJECTIVE TYPE QUESTIONS

1 Mark Each



### Stand Alone MCQs

(1 Mark Each)

1. Which one of the following options describe 'Collateral'? [CBSE SQP, 2020-21]  
 (A) Double coincidence of wants  
 (B) Certain products for barter system  
 (C) Trade in barter system  
 (D) Asset as guarantee for loan

Ans. Option (D) is correct.

**Explanation:** The collateral acts as a form of protection for the lender. That is, if the borrower defaults on their loan payments, the lender can seize the collateral and sell it to recoup some or all of its losses.

2. Which one of the following is not a limitation of the barter system? [A]  
 (A) Lack of double coincidence of wants.  
 (B) Certain products can't be divided.  
 (C) Most often double coincidence of wants is not available.  
 (D) None of the above

Ans. Option (D) is correct.

**Explanation:** Barter system had many limitations like lack of double coincidence of wants, lack of a common unit of value, difficulty of future payments or contractual payments and difficulty of storage of value and transfer of value.

3. Which one of the following was not a traditional form of money? [R]  
 (A) Grains (B) Paper notes  
 (C) Cattle (D) Gold coins

Ans. Option (B) is correct.

**Explanation:** Paper notes were introduced very late. Sheep, camels, and other livestock, were the first and oldest form of money.

4. Who issues currency notes in India? [R]  
 (A) Reserve Bank of India  
 (B) State Bank of India  
 (C) Ministry of Finance  
 (D) Government of India

Ans. Option (A) is correct.

**Explanation:** The Reserve Bank of India is Central bank. It is responsible for the issue and supply of the Indian rupee and the regulation of the Indian banking system.

5. A cheque like currency notes act as: [U]

- (A) cash
- (B) a store of value
- (C) a medium of exchange
- (D) a demand deposit

Ans. Option (C) is correct.

**Explanation:** Money is accepted as a medium of exchange because:  
The currency is authorised by the government of the country.  
The Reserve Bank of India issues currency notes on behalf of the Central Government.

6. A deposit with a bank that can be withdrawn whenever the depositor likes to do so, is termed as: [E]

- (A) a demand deposit
- (B) a time deposit
- (C) a fixed deposit
- (D) a legitimate deposit

Ans. Option (A) is correct.

AI 7. Which of the following does not constitute a part of informal credit in India? [A]

- (A) Commercial Bank
- (B) Moneylenders
- (C) Friends and relatives
- (D) Zamindars

Ans. Option (A) is correct.

**Explanation:** Commercial banks are a part of formal credit as the bank's funds come from money deposited by the bank customers in saving accounts, checking accounts, money market accounts.

AI 8. The functioning of the formal source of credit is supervised by: [R]

- (A) Government of India
- (B) Reserve Bank of India
- (C) Ministry of Finance
- (D) None of the above

Ans. Option (B) is correct.

**Explanation:** The RBI supervises the functioning of formal sources of credit in India.  
The RBI monitors that the banks actually maintain the required cash balance out of the deposits they receive.

9. Banks do not give loans to: [A]

- (A) small farmers.
- (B) marginal farmers.
- (C) industries.
- (D) people without proper collateral and documents.

Ans. Option (D) is correct.

**Explanation:** Banks require it to know financial condition of borrower and make sure he/ she can pay loan on time.

10. The number of members in a typical SHG varies between: [R]

- (A) 5 and 10
- (B) 15 and 20
- (C) 15 and 25
- (D) 20 and 30

Ans. Option (B) is correct.

**Explanation:** A Self-help group (SHG) is a financial intermediary committee usually composed of 15 to 20 local women or men.

11.	Column A	Column B
(i)	Barter system	(a) Supervises the functioning of banks
(ii)	Debt-trap	(b) Commodity for commodity exchange system
(iii)	Formal sector loans	(c) Pushes the borrower into a situation from which recovery is very painful
(iv)	Reserve Bank of India	(d) Loans from banks and co-operatives

(A) (i)-(a), (ii)-(b), (iii)-(c), (iv)-(d)

(B) (i)-(b), (ii)-(c), (iii)-(d), (iv)-(a)

(C) (i)-(d), (ii)-(c), (iii)-(b), (iv)-(a)

(D) (i)-(c), (ii)-(a), (iii)-(b), (iv)-(d)

Ans. Option (B) is correct.

12.	Column A	Column B
(i)	Financial Formal Institutions	(a) Payments which are to be made in future
(ii)	Financial Informal Institutions	(b) The actual amount of investment
(iii)	Actual Investment	(c) Commercial banks, co-operatives, Rural Banks
(iv)	Deferred Payments	(d) Moneylenders, landlords, employers, relatives, friends etc

(A) (i)-(c), (ii)-(d), (iii)-(b), (iv)-(a)

(B) (i)-(a), (ii)-(b), (iii)-(c), (iv)-(d)

(C) (i)-(b), (ii)-(a), (iii)-(d), (iv)-(c)

(D) (i)-(d), (ii)-(c), (iii)-(a), (iv)-(b)

Ans. Option (A) is correct.

13. Arrange the following in the correct sequence:

- (i) Online payment, Debit card, Credit cards
- (ii) Precious metal coins (gold, silver, copper)
- (iii) Grain and Cattle
- (iv) Modern Currency-Paper notes and coins

Options:

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

Ans. Option (C) is correct.

**Explanation:** Initially grains and cattle were used as money. Before the introduction of coins a variety of objects was used as money. Thereafter, came the use of metallic coins. As time progressed, trade increased and a global market was created. With the global market came the need for a more convenient medium of exchange. Thus, was born the modern forms of money - paper notes (currency) and coin. With the advancement of technology, online payments have become the new form of contactless payment.

14. Analyze the information given below, considering one of the following correct options:

Rita has taken a loan of ₹ 7 lakhs from the bank to purchase a car. The annual interest rate on the loan is 14.5 per cent and the loan is to be repaid in 3 years in monthly instalments. The bank retained the papers of the new car as collateral, which will be returned to Rita only when she repays the entire loan with interest.

- (A) Mode of re-payment
- (B) Terms of credit
- (C) Interest on loan
- (D) Deposit criteria

[CBSE SQP, 2020-21]

Ans. Option (B) is correct.

**Explanation:** Terms of credit are the requirements need to be satisfied for any credit arrangements. It includes interest rate, collateral, documentation and mode of repayment. However, the terms of credit vary depending upon the nature of lender, borrower and loan.

15. Analyze the information given below, considering one of the following correct options:

Mohan is an agricultural labourer. There are several months in a year when he has no work and needs credit to meet his daily expenses. He depends upon his employer, the landowner for credit who charges an interest rate of 5 per cent per month. Mohan repays the money by working physically for the landowner on his farmland.

[CBSE SQP, 2020-21]

Over the years his debt will –

- (A) Increase - because of increasing interest and non-payment of monthly amount.

(B) Remain constant - as he is working for the employer but is repaying less.

(C) Reduce - as amount equivalent to his salary is being counted as monthly repayment.

(D) Be totally repaid - as he is repaying the debt in the form of physical labour.

Ans. Option (A) is correct.

**Explanation:** Compared to the formal lenders, most of the informal lenders charge a much higher interest on loans. Thus, the cost to the borrower of informal loans is much higher.

16. Analyze the information given below, considering one of the following correct options:

Mahesh is a small farmer. He has taken a loan of ₹ 2 lakhs from the money lender to meet the expenses of cultivation. The annual interest rate on the loan is very high, so he is unable to repay the loan and he is caught in a debt. He has to sell a part of the land to pay off the debt.

- (A) Terms of credit
- (B) Interest on loan
- (C) Debt-trap
- (D) Mode of repayment

Ans. Option (C) is correct.

**Explanation:** Debt -trap is a situation in which a poor person falls in debt i.e he/she is not able to pay the interest rate or loans .

17. Analyze the information given below, considering one of the following correct options:

Ramu is a shoe manufacturer and he wants to directly exchange shoes for rice without the use of money. Now he will have to look for a rice growing farmer who not only wants to sell rice but also wants to buy the shoes in exchange.

- (A) Double coincidence of wants
- (B) Goods exchange with goods
- (C) Goods exchange with money
- (D) None of the above

Ans. Option (A) is correct.

18. Analyze the information given below, considering one of the following correct options:

Megha has taken a loan of ₹ 6 lakhs from the bank to purchase a house. The annual interest rate on the loan is 14 per cent and the loan is to be repaid in 12 years in monthly installments. Megha had to submit to the bank, documents showing her employment records and salary before the bank agreed to give her the loan.

- (A) Interest on loan
- (B) Formal source of loan
- (C) Informal source of loan
- (D) None of the above

Ans. Option (B) is correct.

**Explanation:** Formal source of loan demands the submission of collateral and all loan related documentation before processing the loan.

19. Analyze the information given below, considering one of the following correct options:

A shopkeeper Sudha has to make a payment to the wholesaler and writes a cheque for a specific



amount to the wholesaler. The wholesaler takes this cheque and deposits it in his own account in the bank. The money is transferred from one bank account to another bank account in a couple of days. The transaction is completed without any payment of cash.

- (A) Check payment      (B) Interest on deposits  
(C) Demand deposit      (D) Money transfer

**Ans. Option (C) is correct.**

**Explanation:** In case of Demand Deposit deposited funds can be withdrawn at any time, without advance notice.

**20. Find the incorrect option from the following:**

- (A) Demand deposit share the essential features of money.  
(B) With demand deposit payments can be made without cash.  
(C) Demand deposits are safe way of money transformation.  
(D) Demand deposit facility is like cheque.

**Ans. Option (D) is incorrect.**

**Explanation:** The facility of cheques against demand deposits makes it possible to directly settle payments without the use of cash. Since demand deposits are accepted widely as a means of payment, along with currency, they constitute money in the modern economy.

**21. Find the incorrect option from the following:**

- (A) Banks accept deposit and also pay an amount as interest.  
(B) People's money is safe with banks.  
(C) Banks provide loans only to profit-making businesses.  
(D) It is easy for individuals to get credit who have savings and current account in the banks.

**Ans. Option (C) is incorrect.**

**22. Find the incorrect option from the following:**

- (A) Poor households still depend on informal sources of credit.  
(B) RBI supervises the functioning of informal sources of loans.  
(C) Banks are not present everywhere in the rural areas.  
(D) RBI monitors the banks in actually maintaining cash balance.

**Ans. Option (B) is incorrect.**

**Explanation:** The RBI monitors the banks in actually maintaining cash balance. Periodically banks have to submit information to the RBI on how much they are lending to whom at what interest rate, etc.



## Assertion and Reason Based MCQs (1 Mark Each)

**Directions :** In the following questions, A statement of Assertion (A) is followed by a statement of Reason (R). Mark the correct choice as:

- (A) Both A and R are true and R is the correct explanation of A.  
(B) Both A and R are true but R is NOT the correct explanation of A.  
(C) A is true but R is false.  
(D) A is false and R is true.

(D) A is wrong and R is correct.

**1. Assertion (A):** No individual or organisation is allowed to issue currency notes in India.

**Reason (R):** In India, only RBI issues currency notes on behalf of the Central Government.

**Ans. Option (A) is correct.**

**2. Assertion (A):** Banks keep a small proportion of their deposits as cash with themselves.

**Reason (R):** This is kept to meet the loan requirements of the people.

**Ans. Option (C) is correct.**

**Explanation:** Banks keep only a small proportion of their deposits as cash with themselves. This is kept as a provision to pay the depositors who might come to withdraw money from the bank on any given day.

**3. Assertion (A):** Banks give loans not only to profit-making businesses but also to small cultivators.

**Reason (R):** The RBI supervises the functioning of formal sources of loans.

**Ans. Option (A) is correct.**

**Explanation:** The RBI sees the the banks give loan not just to profit - making business and traders but also to small cultivators, small-scale industries, small borrowers, etc. Periodically, banks have to submit information to the RBI on how much they are lending, to whom, at what interest rate, etc.

**4. Assertion (A):** Periodically, banks have to submit information to the Finance Minister on how much they are lending, to whom, at what interest rate, etc.

**Reason (R):** The Finance Minister monitors the banks in actually maintaining cash balance.

**Ans. Option (D) is correct.**

**Explanation:** The RBI monitors that the banks actually maintain the cash balance.

**5. Assertion (A):** The facility of demand deposits makes it possible to settle payments without the use of cash.

**Reason (R):** Demand deposits are paper orders which make it possible to transfer money from one person's account to another person's account.

**Ans. Option (D) is correct.**

**Explanation:** The facility of cheques against demand deposits makes it possible to directly settle payments without the use of cash. Since demand deposits are accepted widely as a means of payment, along with currency, they constitute money in the modern economy.

6. **Assertion (A):** Banks charge a higher interest rate on loans than what they offer on deposits.

**Reason (R):** The difference between what is charged from borrowers and what is paid to depositors is their main source of income.

**Ans. Option (A) is correct.**

**Explanation:** Banks in India hold about 15 per cent of their deposits as cash as the remaining deposits are used to provide loans. The interest charged on loans is higher than the interest paid on deposits and the difference between the two interest rates is the major source of income for banks.



### Case-based MCQs

(1 Mark Each)

- I. Read the extract given below and answer the questions that follow:

Bartering is the act of trading one good or service for another without using a medium of exchange such as money. A bartering economy differs from a monetary economy in a variety of ways. When barter was used as an exchange medium, the needs of people were very limited. This trading method doesn't involve money and it relies solely on exchanging goods and services for other services and goods in return.

The use of money spans a very large part of our everyday life. To understand the usefulness of money, we must consider what the world would be like without money. How would people exchange goods and services? Economies without money typically engage in the barter system. Barter is highly inefficient for trying to coordinate the trades in a modern advanced economy. In an economy without money, an exchange between two people would involve a double coincidence of wants, a situation in which both the parties have to agree to sell and buy each other's commodities. This is known as double coincidence of wants. What a person desires to sell is exactly what the other wishes to buy. In a barter system where goods are directly exchanged without the use of money, double coincidence of wants is an essential feature.

Another problem with the barter system is that it does not allow us to easily enter into future contracts for purchasing many goods and services. Money solves the problems that the barter system creates. Money serves as a medium of exchange, which means that money acts as an

intermediary between the buyer and the seller. Modern forms of money include currency — paper notes and coins. The other form in which people hold money is as deposits with banks.

**Answer the following MCQs by choosing the most appropriate option:**

1. Which of the following can be considered as modern form of Money?

(A) Paper note (B) Gold Coins  
(C) Silver Coins (D) Copper coins

**Ans. Option (A) is correct.**

**Explanation:** They are accepted as a modern form of money because of government authorization.

2. Which of the following has an essential feature of double coincidence?

(A) Money system (B) Barter system  
(C) Financial system (D) Banking system

**Ans. Option (B) is correct.**

**Explanation:** Barter system is direct exchange of goods and services. It requires the double coincidence of wants. Barter system eliminates the use of money. It generally flourishes among uncivilized and backward communities. Barter system is possible where the area of exchange is limited.

3. In a barter system:

(A) goods are exchanged for money.  
(B) goods are exchanged for foreign currency.  
(C) goods are exchanged without the use of money.  
(D) goods are exchanged on credit.

**Ans. Option (C) is correct.**

**Explanation:** Barter is an act of trading goods or services between two or more parties without the use of money. Barter system involves the provision of one good or service by one party in return for another good or service from another party.

4. Which of the following feature of money acts as an intermediate in the exchange process?

(A) Medium of exchange  
(B) Unit of value  
(C) Store of value  
(D) None of the above

**Ans. Option (A) is correct.**

**Explanation:** By serving as a medium of exchange money removes the difficulties associated with the Barter System. Money is authorised by the government of the country and nobody can legally refuse it as a medium of exchange for goods or services.

- II. Read the source given below and answer the questions that follow:

Banks use the major portion of the deposits to extend loans. There is a huge demand for loans



for various economic activities. Banks make use of the deposits to meet the loan requirements of the people. In this way, banks mediate between those who have surplus funds (the depositors) and those who are in need of these funds (the borrowers). Banks charge a higher interest rate on loans than what they offer on deposits. A large number of transactions in our day-to-day activities involve credit in some form or the other. Credit (loan) refers to an agreement in which the lender supplies the borrower with money, goods or services in return for the promise of future payment. In rural areas, the main demand for credit is for crop production. Crop production involves considerable costs on seeds, fertilisers, pesticides, water, electricity, repair of equipment, etc. The various types of loans can be conveniently grouped as formal sector loans and informal sector loans. Among the former are loans from banks and cooperatives. The informal lenders include moneylenders, traders, employers, relatives and friends, etc. The Reserve Bank of India supervises the functioning of formal sources of loans. For instance, we have seen that the banks maintain a minimum cash balance out of the deposits they receive. The RBI monitors the banks in actually maintaining cash balance. There is no organisation which supervises the credit activities of lenders in the informal sector. They can lend at whatever interest rate they choose. There is no one to stop them from using unfair means to get their money back. Compared to the formal lenders, most of the informal lenders charge a much higher interest on loans. Thus, the cost to the borrower of informal loans is much higher. In recent years, people have tried out some newer ways of providing loans to the poor. The idea is to organise rural poor, in particular women, into small Self-Help Groups (SHGs) and pool (collect) their savings.

**Answer the following MCQs by choosing the most appropriate option:**

1. Compared to the formal lenders, most of the informal lenders charge a much \_\_\_\_\_ interest on loans:

(A) lower (B) constant  
(C) higher (D) no interest

**Ans. Option (C) is correct.**

*Explanation:* Informal lenders charge high rate interest. They make loans very expensive as they are no external organizations controlling the credit activities of lenders

2. Formal sector loans include loans from:

(I) Banks (II) Moneylenders  
(III) Cooperatives (IV) Traders  
(A) (i) and (iii) (B) (ii) and (iv)  
(C) (ii) and (iii) (D) (i) and (iv)

**Ans. Option (A) is correct.**

*Explanation:* These organizations provide cheap and affordable loans and their rate of interest is monitored by RBI.

3. An agreement in which the lender supplies the borrower with money, goods or services in return for the promise of future payment.

(A) Credit (loan) (B) Chit fund  
(C) Bank (D) Cheque

**Ans. Option (A) is correct.**

*Explanation:* Credit is generally defined as a contract agreement in which a borrower receives a sum of money or something of value and repays the lender at a later date, generally with interest.

4. Banks use the major portion of the deposits to:

(A) keep as a reserve so that people may withdraw.  
(B) meet their routine expenses.  
(C) extend loans.  
(D) meet renovation of the bank.

**Ans. Option (C) is correct.**

*Explanation:* Major portion of the deposits is used by banks for extending loans to borrowers.

### III. Read the source given below and answer the questions that follow:

The use of money spans a very large part of our everyday life. Look around you and you would easily be able to identify several transactions involving money in any single day. Can you make a list of these? In many of these transactions, goods are being bought and sold with the use of money.

In some of these transactions, services are being exchanged with money. For some, there might not be any actual transfer of money taking place now but a promise to pay money later. Have you ever wondered why transactions are made in money? The reason is simple. A person holding money can easily exchange it for any commodity or service that he or she might want. Thus, everyone prefers to receive payments in money and then exchange the money for things that they want. Take the case of a shoe manufacturer. He wants to sell shoes in the market and buy wheat. The shoe manufacturer will first exchange shoes that he has produced for money, and then exchange the money for wheat. Imagine how much more difficult it would be if the shoe manufacturer had to directly exchange shoes for wheat without the use of money. He would have to look for a wheat growing farmer who not only wants to sell wheat but also wants to buy the shoes in exchange. That is, both parties have to agree to sell and buy each other's commodities. This is known as double coincidence of wants. What a person

desires to sell is exactly what the other wishes to buy. In a barter system where goods are directly exchanged without the use of money, double coincidence of wants is an essential feature. In contrast, in an economy where money is in use, money by providing the crucial intermediate step eliminates the need for double coincidence of wants. It is no longer necessary for the shoe manufacturer to look for a farmer who will buy his shoes and at the same time sell him wheat. All he has to do is find a buyer for his shoes. Once he has exchanged his shoes for money, he can purchase wheat or any other commodity in the market. Since money acts as an intermediate in the exchange process, it is called a medium of exchange.

Answer the following MCQs by choosing the most appropriate option:

1. Why transactions are made in money?

- (A) Money is easy to get.
- (B) Money is accepted as a medium of exchange.
- (C) Everyone has money reserves in their house.
- (D) All of the Above.

Ans. Option (B) is correct.

*Explanation:* Money is accepted as a medium of exchange because the currency is authorised by the Government of India.

2. In \_\_\_\_\_ both parties have to agree to sell and buy each other's commodities.

- (A) Double Coincidence of wants
- (B) Barter System
- (C) Bank Regulation
- (D) Personal Agreements

Ans. Option (B) is correct.

*Explanation:* Barter system is exchange of commodities of two parties, without paying or taking money. In double coincidence of wants a person willing to sell something is bought by another person.

3. How would had the shoe manufacturer directly exchanged shoes for wheat without the use of money?

- (A) Both parties have to agree to sell and buy each other's commodities.
- (B) He compels the farmer to give him wheat on compassionate grounds.
- (C) He forces the farmer to take the shoes from him in exchange of wheat.
- (D) He approaches the bank authorities.

Ans. Option (A) is correct.

*Explanation:* When two parties agree to sell and buy each other's commodities, this situation is known as 'double coincidence of wants'. That is, what a person desires to sell is exactly what the other wishes to buy. Such a situation is a feature of the barter system.

4. Why barter system is no longer practiced?

- (A) Considered illegal.
- (B) People do not have that much things to exchange.
- (C) It is difficult to find two parties that have something they both want to trade.
- (D) Government keeps a check on such an activity.

Ans. Option (C) is correct.

*Explanation:* A barter system lacked not only a common medium of exchange but also a standard unit of account in which prices could be measured and quoted.

## ✓ (B) SUBJECTIVE QUESTIONS



### Very Short Answer Type Questions (1 Mark Each)

1. Why do banks or lenders demand collateral against loans? [U] [Delhi Set-I, 2019]

Ans. Bank or lenders demand collateral against loans as it is used as a guarantee to a lender until the loan is repaid. [CBSE Marking Scheme, 2019] 1

Detailed Answer:

Collateral is demanded by the banks or lenders before granting a loan as it is an asset that is owned by the borrower and it can be used as a guarantee to the banks until the loan is repaid. The banks can sell the collateral in case the borrower is unable to pay off his loan.

2. Explain the importance of 'Collateral'.

[A] [Delhi Set-II, 2019]

Ans. Importance of 'Collateral':

It is used as a guarantee to a lender until the loan is repaid. [CBSE Marking Scheme, 2019] 1

Detailed Answer:

Collateral refers to assets or personal property that a borrower uses to secure a loan. If the borrower defaults on a loan secured with collateral, the lender can seize his property to repay the debt.

3. Explain the importance of formal sector loans in India. [A] [Delhi Set-III, 2019]

Ans. Importance of formal sector loans in India:

Low interest rate.

[CBSE Marking Scheme, 2019] 1

Detailed Answer:

Importance of formal sector loans in India:

Banks and cooperatives are the formal sources of loans in India.

#### Advantage:

- (i) As these institutions are regulated by the Reserve Bank of India, their rates of interest for loans are controlled. The rates and terms are also fixed.
- (ii) There is no exploitation by the lenders.
- (iii) Everyone can take a loan, including big businessmen as well as small cultivators or borrowers.
- (iv) The cost of borrowing is usually less. (Any one)

4. Give one example each of modern currency and old currency. [R] [OD Set-I, 2019]

Ans. Modern currency – Paper notes/coins, old currency – metallic coins like gold, silver & copper coins.

[CBSE Marking Scheme, 2019] 1

#### Detailed Answer:

- (i) One example of modern currency- Paper notes and coins,
- (ii) One example of old currency- Commodity currency.

5. Give any one example of the methods to make payment without using cash. [R] [OD Set-II, 2019]

Ans. Online transfer, by cheque (Any one)  
(Any other relevant point)

[CBSE Marking Scheme, 2019] 1

6. Give one example of money which is not in the form of currency (cash). [R] [OD Set-III, 2019]

Ans. By cheque (Any other relevant point)

[CBSE Marking Scheme, 2019] 1

OR

Debit/Credit Card.

7. Give any two examples of informal sector of credit.

[R] [Delhi & OD, 2018]

- (i) Credit from 'moneylenders'.
- (ii) Credit from 'family members'.

8. What is Barter System? [U] [O.E.B.]

Ans. It is a system of exchange in which goods are directly exchanged without the use of money.

9. What are the two forms of modern currency?

[R] [O.E.B.]

Ans. Paper notes and coins.

10. Why one cannot refuse a payment made in rupees in India? [A] [O.E.B.]

Ans. Because it is authorized by the Government of India.

11. Who supervises the functioning of formal sources of loan? [R] [O.E.B.]

Ans. Reserve Bank of India (RBI).

12. Why are most of the poor households deprived from the formal sector of loans? [A] [O.E.B.]

Ans. Because they cannot fulfil the formalities of the formal sector of loans.

13. Why do farmers require credit? [A] [O.E.B.]

Ans. To purchase the raw materials and inputs for agriculture.

14. Why do banks maintain cash reserve?

[A] [O.E.B.]

Ans. To arrange for daily withdrawals by depositors.



## Short Answer Type Questions

(3 Marks Each)

1. Describe the significance of the Reserve Bank of India. [OD Set-I, 2020]

Ans. It is the Reserve Bank of India, which controls the functioning and supervises the activities of the formal sectors in India.

It also acts as the guardian of all the monetary policies in our country.

It monitors the balance kept by banks for day-to-day transactions.

Periodically, banks have to give details about lenders, borrowers and interest rate to RBI.

Thus, RBI plays a significant role in our country.

2. How can money be easily exchange itself for goods or services? Give example to explain.

[U] [Board Term-II, Delhi Set-I, 2016]

Ans. Money acts as a medium to exchange itself for goods and services:

A person holding money can easily exchange it for any commodity or service that he or she wants. Everyone prefers to receive payments in money and exchanges the money for things he wants.

**For example:** A shoemaker wants to sell shoes in the market and buy wheat. The shoemaker will first exchange shoes for money and then exchange the money for wheat. If the shoemaker had to directly exchange shoes for wheat without the use of money, he would have to look for wheat growing farmer who not only wants to sell wheat but also wants to buy the shoe in exchange. Both parties have to agree to sell and buy each other's commodities. This process is very difficult, time consuming and unhealthy.

[CBSE Marking Scheme, 2016] 3

3. How is money transferred from one bank account to another bank account? Explain with an example. [U] [Board Term-II, 2016]

Ans. Money transfer from one bank account to another bank account:

If a person has to make a payment to his or her friend and writes a cheque for a specific amount, this means that the person instructs his bank to pay this amount to his friend. His friend takes this cheque and deposits it in his account in the bank. This said amount is transferred from one bank account to another bank account.

[CBSE Marking Scheme, 2016] 3

4. Why is modern currency accepted as a medium of exchange without any use of its own? Find out the reason. [R] [Board Term-II, OD Set-I, II, III, 2015]

**Ans.** Modern currency is accepted as a medium of exchange without any use of its own because:

- (i) Modern currency is authorised by the government of a country.
- (ii) In India, the Reserve Bank of India issues all currency notes on behalf of the central government.
- (iii) No other individual or organisation is allowed to issue currency.
- (iv) The law legalises the use of rupee as a medium of payment that cannot be refused in settling transactions in India.
- (v) No individual in India can legally refuse a payment made in rupees. (Any three)  $1 \times 3 = 3$

[CBSE Marking Scheme, 2015]

### COMMONLY MADE ERROR

- ➔ Students should remember the laws of RBI.

### ANSWERING TIP

- ➔ Few students do not give a detailed description about RBI as the issuing authority for Indian currency.

- [AI] 5. Imagine yourself to be XYZ, a member of a women Self Help Group. Analyse the ways through which your group provides loan to the members.

[CBSE SQP 2020-21]

- Ans.** (i) Self Help Groups pool their savings.  
 (ii) A typical SHG has 15–20 members, usually belonging to one neighbourhood, who meet and save regularly.  
 (iii) Saving per member varies from Rs. 25 to Rs. 100 or more, depending on the ability of the people to save.  
 (iv) Members can take small loans from the group itself to meet their needs.  
 (v) The group charges interest on these loans but this is still less than what the moneylender charges.  
 (vi) After a year or two, if the group is regular in savings, it becomes eligible for availing loan from the bank. (Any Three Points)  $(1 \times 3 = 3)$

[CBSE Marking Scheme, 2020]

- [AI] 6. Explain the role of Self Help Groups in the rural economy. [OD SET II 2020]

**Ans.** The role of Self-Help Groups:

- (i) Self-Help Groups are small groups (especially from rural areas) who pool their resources and

individual savings together to help the others in need of funds.

- (ii) Facilitates the members to employ themselves in numerous self-employment opportunities.
- (iii) Help in raising the living standards of the concerned members.
- (iv) Reduces the dependence on the informal credit sources.
- (v) Thus, with the help of SHGs, the rural poor become economically independent and their dependence on the local moneylenders who charge a high rate of interest is also reduced.

7. Why do we need to expand formal source of credit in India? [U] [CBSE SQP-2020]

OR

Explain any three reasons for the banks and cooperative societies to increase their lending facilities in rural areas. [U] [Delhi 2019]

**Ans.** Expand formal sources of credit in India

- (i) To save people from the exploitation of Informal sector,
- (ii) Formal charge a low interest on loans,
- (iii) To save from debt trap,
- (iv) It provides cheap and affordable credit,
- (v) RBI also supervises the formal sector credit through various rules and regulations which ensures that banks give loans to small cultivators, small borrowers, etc. and not just to profit making business and traders.

(Any three points to be explained) [3]

### COMMONLY MADE ERROR

- ➔ Mention some advantages of formal sources and disadvantages of informal sources in this answer.

### ANSWERING TIP

- ➔ Alternative and role of RBI is not discussed in the answers.

OR

**Ans.** Banks and Cooperatives can help people in obtaining cheap and affordable loans. This will help people to grow crops, do business set up small scale industries or trade goods and also help indirectly in the country's development.

- (i) They should do so, so that relatively poor people do not have to depend on informal sources of credit.
- (ii) Formal sector loans need to expand. It is also necessary that everyone receives these loans.
- (iii) At present it is the richer households who receive formal credit whereas the poor have to depend on informal sources. It is important that the formal credit is distributed more equally so that poor can be benefitted from the cheaper loans.



Detailed Answer:



### Topper's Answer, 2019

Sol. 14. The banks and cooperative societies should increase their lending facilities in rural areas for the following reasons:

- (i) The poorer section of the society can get a greater share of formal credit and hence prosper.
- (ii) The dependence on money lenders and traders, who charge extraordinary high rates, decrease.
- (iii) People can borrow cheaply for meeting the working capital requirement and thus develop their business and agriculture.

**AI 8. Why do banks and co-operative societies need to lend more? Explain. [A] [CBSE SQP, 2019-20]**

**Ans. Banks and cooperative societies need to lend more:**

- (i) This would lead to higher incomes.
- (ii) People could borrow cheaply for a variety of needs.
- (iii) They could grow crops and set up small-scale industries, etc.
- (iv) Cheap and affordable credit is crucial for the country's development.
- (v) To save and reduce the dependence on informal sources of credit.
- (vi) It is important that the formal credit is distributed more equally so that the poor can benefit from the cheaper loans.

#### COMMONLY MADE ERROR

- ➔ Banks and cooperatives role in rural areas should be discussed and not the urban issues.

#### ANSWERING TIP

- ➔ Banks and cooperatives are formal sources and not informal sources.

**AI 9. Describe the importance of formal sources of credit in the economic development. [A] [Delhi Set-I, 2019]**

**Ans. Importance of formal sources of credit in the Economic Development:**

- (i) Formal sources provide cheap credit.

- (ii) Credit at affordable rate is available through formal sources.
- (iii) Terms and conditions of credit through formal sources are regulated by government.
- (iv) Credit from formal source are favourable.
- (v) Any other relevant point.

**(Any three points to be described)  
[CBSE Marking Scheme, 2019] 3**

**Detailed Answer:**

We need to expand the formal sources of credit for economic development because of the following reasons:

- (i) **Supervision:** The formal sources work under the supervision of the RBI. The RBI monitors that the banks actually maintain cash balance and give loans to small cultivators and farmers too. On the other hand, there is no organization which supervises the credit activities of lenders in the informal sector. They can lend at any interest rate as per their discretion.
- (ii) **Lower rate of interest:** The rate of interest in the formal sectors is decided by the RBI. So normally, the interest rate is low.
- (iii) **Formal sources of credit:** Banks might not be willing to give loans to certain borrowers if they already have procured a loan or if they don't have enough cash balance in that bank or if they don't have anything that they can use as a collateral. In such conditions, development of formal sources of credit can prove to be useful.



## COMMONLY MADE ERROR

- ➡ Rules and regulations of Banks and RBI should be added in this answer.

## ANSWERING TIP

- ➡ Economic development is discussed vaguely in some answers.

**AI** 10. Describe the bad effects of informal sources of credit on borrowers. **A** [Delhi Set-I, 2019]

**Ans. Bad effects of informal sources of credit on borrowers:**

- (i) Higher interest rate.
- (ii) Higher cost of borrowing means a larger part of the earnings of the borrowers is used to repay the loan.
- (iii) In certain cases, the high interest rate for borrowing can mean that the amount to be repaid is greater than the income of the borrower.
- (iv) This could lead to increasing debt and debt trap.
- (v) Any other relevant point.

(Any three points to be described)  
[CBSE Marking Scheme, 2019] 3

**Detailed Answer:**

**Bad effects of informal sources of credit on borrowers:**

- (i) Most of the informal lenders charge a much higher interest on loans. Thus, the cost to the borrower of the informal loans is much higher.
- (ii) Higher cost of borrowing means a larger part of earning of the borrowers is used to repay the loan and they have less income left for themselves.
- (iii) The high rate of interest of borrowing can mean that the amount to be repaid is greater than the income of the borrower and it can lead to increasing debt and debt-trap.
- (iv) People who might wish to start an enterprise by borrowing may not do so because of the high cost of borrowing.

(Any three points)

## COMMONLY MADE ERROR

- ➡ Only the bad effects on borrowers is required.

## ANSWERING TIP

- ➡ Some students were confused with 'bad effects'. The bad treatment of moneylenders point of view is discussed.

**AI** 11. Why is it necessary to increase of a large number of banks mainly in rural areas? Explain.

**A** [OD Set-I, 2019]

**Ans. Increase large number of banks:**

- (i) To reduce the dependence on informal sector of credit.
- (ii) To provide cheaper loans.
- (iii) To provide accessibility towards loans for the poor.
- (iv) Any other relevant point to be explained.

(Any three)

[CBSE Marking Scheme, 2019] 3

**Detailed Answer:**

**It is necessary to increase a large number of banks mainly in rural areas because:**

- (i) The cost of informal loans is much higher and often leads to a debt trap. Also, people who might wish to start a new enterprise by borrowing may not do so because of the high cost of borrowing in such a case.
- (ii) Most loans from informal lenders carry a very high interest rate and make less increase in the income of the borrowers. Thus, it is necessary that banks and cooperatives should increase their lending particularly in the rural areas, so that the dependence of the poor on informal sources of credit reduces.
- (iii) It is important that the formal credit sources like banks are distributed more equally in rural and urban areas so that the poor can benefit from the cheaper loans.

## COMMONLY MADE ERROR

- ➡ The necessities of large number of banks in rural areas is to save poor people from the debt-trap of moneylenders.

## ANSWERING TIP

- ➡ Rate of borrowing interest is not mentioned in the answer.

**AI** 12. Why are service conditions of formal sector loans better than informal sector? Explain.

**A** [OD Set-I, 2019]

**Ans. Formal sector are better than informal sector:**

- (i) Low interest rate.
- (ii) Transparency.
- (iii) Supervision by the Reserve Bank of India on the functioning of the formal sector.
- (iv) No use of unfair means for getting the money back.

(Any three)

[CBSE Marking Scheme, 2019] 3

**Detailed Answer:**

**Service conditions of formal sector are better than those of informal sector because:**

- (i) These resources work under the supervision of the Reserve Bank of India. Their rate of interest is very low.

- (ii) Commercial banks and cooperative societies are the main source of formal source of credit. They provide ensured services and also have a set protocol for deliverance of loan services.
- (iii) In formal sector- interest rate, collateral and documentation requirement, and the mode of repayment together comprise what is called the terms of credit. The terms of credit vary substantially from one credit arrangement to another. They may vary depending on the nature of the lender and the borrower.

### COMMONLY MADE ERROR

- ➡ Service conditions of both the sectors has to be compared.

### ANSWERING TIP

- ➡ Most of the students fail to answer about the service conditions.

**AI** 13. Why is cheap and affordable credit important for the country's development? Explain any three reasons.

**A** [Delhi & OD Set-I, 2018]

**Ans. Importance of cheap and affordable credit for the country's development:**

- (i) Cheap and affordable credits would lead to higher income.
- (ii) Many people could borrow for a variety of needs.
- (iii) It encourages people to invest in agriculture, do business and set up small scale industries, etc.
- (iv) It enables more investment which will lead to acceleration of economic activities.
- (v) Affordable credit would also end the cycle of debt-trap.
- (vi) Any other relevant point. (Any three points)

[CBSE Marking Scheme, 2018]

14. Why are formal sources of credit preferred over the informal source of credit? Give three reasons.

**A + U** [CBSE SQP, 2018]

**Ans. Formal sources of credit preferred over informal sources of credit because:**

- (i) Formal sources have low cost of borrowing.
- (ii) Higher Income through cheap borrowing.
- (iii) No exploitation and debt trap.
- (iv) Any other relevant point

1 × 3 = 3

[CBSE Marking Scheme, 2018]

**AI** 15. "The credit activities of the informal sector should be discouraged." Support the statement with arguments.

**A** [CBSE Compartment Set 2018]

[Board Term-II, Delhi Set 2016]

**Ans. Credit activities of the informal sector should be discouraged:**

- (i) Most loans from informal lenders carry a very high interest rate and do little to increase the income of the borrowers.
- (ii) The poor households have to pay a large amount for borrowing.
- (iii) 85% of the loans taken by poor households in the urban areas are from informal sources.
- (iv) Cheap and affordable credit is crucial for the country's development.
- (v) Any other relevant point.

(Any three points to be explained) 1 × 3 = 3

[CBSE Marking Scheme, 2018]

**Q 16. Explain any three loan activities of banks in India.**  
**[OD Set-II, 2017]**

**Ans. Loan activities of Banks in India:**

- (i) Banks use the major portion of the deposits to extend loans.
- (ii) Banks make use of the deposits to meet the loan requirements of the people.
- (iii) Banks mediate between those who have surplus funds (the depositors) and those who are in need of these funds (the borrowers).
- (iv) Banks charge a higher interest rate on loans than what it offers on deposits.
- (v) Any other relevant point.

(Any three points to be explained)

[CBSE Marking Scheme, 2017] 3

17. "Deposits with the banks are beneficial to the depositors as well as to the nation". Examine the statement.

**E** [OD Set-I] 2016]

**Ans. Refer to Ans. of Long 9.**

18. Mention three points of difference between formal sector and informal sector loans.

**R** [Board Term-II, 2016]

**Ans. Refer to Ans. of Long 14.**

19. Dhananjay is a government employee and belongs to a rich household, whereas Raju is a construction worker and comes from a poor rural household. Both are in need and wish to take loan. Create a list of arguments explaining who between the two would successfully be able to arrange money from a formal source. Why?

**U** [Board Term-II, SQP, 2016-17]

**Ans. Dhananjay will be able to get a loan from a formal source.**

**Arguments:**

- Banks are not present everywhere in rural India.
- Even when they are present, getting a loan from a bank is much more difficult than taking a loan from informal sources.
- Bank loans require proper documents and collateral. Absence of collateral is one of the major reasons which prevents the poor from getting bank loans.

Informal lenders such as moneylenders, on the other hand, know the borrowers personally and hence, are often willing to give a loan without collateral. [CBSE Marking Scheme, 2016] 3

**AI** 20. "Poor households still depend on informal sources of credit". Support the statement with examples.

**A** [Board Term-II, 2016]

**Ans.** Poor households still depend on informal sources of credit because:

- (i) Banks are not present everywhere in the rural areas.
- (ii) Even when they are present, getting a loan from the bank is much more difficult than taking a loan from informal sources.
- (iii) Mega banks or public sector banks require proper documents and collateral.
- (iv) Absence of collateral is one of the major reasons which prevents the poor from getting bank loans.
- (v) Informal lenders such as moneylenders know the borrowers personally and they are willing to give a loan without collateral.

(Any three)

### COMMONLY MADE ERROR

- Students should mention the reasons in detail.

### ANSWERING TIP

- Reasons of choosing informal sources by poor households is not given in the answers.

**AI** 21. What is meant by term of credit? What does it include? **U**

**Ans.** Terms of credit are the requirements need to be satisfied for any credit arrangements. It includes interest rate, collateral, documentation and mode of repayment. However, the terms of credit vary depending upon the nature of lender, borrower and loan.



### Long Answer Type Questions

(5 Marks Each)

1. "Bank plays an important role in the economic development of the country." Support the statement with examples. [Delhi Set-I, 2020] **A**

**Ans.** Bank plays an important role in the economic development of the country in many ways:

- (i) Bank provides loan in rural area for crop production ultimately resulting in the development of many places.
- (ii) Bank provides loan to create fixed assets that will create employment opportunities.
- (iii) It acts as a link between savers and investors i.e. people who have surplus money and those who are in need of money.

(iv) Banks accept the deposit and pay an amount as interest on the deposit which mobilizes savings.

(v) Bank uses major portion of these deposits to extend loan for the industrial and agricultural sector. They also provide funds to different organisations.

2. What are demand deposits? Explain any three features of it. **U** [Board Term-II, 2016]

OR

**AI** Which type of deposits with the banks are called demand deposits? State some important features of demand deposits. **U**

**Ans.** People save their money in banks by opening an account. The deposits in the bank accounts can be withdrawn on demand, so these deposits are called demand deposits.

- (i) Banks accept the deposits and also pay an interest rate on the deposits. In this way, people's money is safe with the banks and it also earns interest.
- (ii) The facility of cheques against demand deposits makes it possible to directly settle payments without the use of cash. Since, demand deposits are accepted widely as a means of payment, along with currency, they constitute money in the modern economy.

(iii) It is authorised by the government of the country.  $2 + 3 = 5$

[CBSE Marking Scheme, 2016]

**AI** 3. "The rupee is widely accepted as a medium of exchange." Explain. **U**

**Ans.** The rupee is widely accepted as a medium of exchange because:

- (i) The currency is authorised by the government of the country.
- (ii) In India, the Reserve Bank of India issues currency notes on behalf of the central government.
- (iii) The law legalises the use of rupee as a medium of payment that cannot be refused in settling transactions in India.
- (iv) No individual in India can legally refuse a payment made in rupees. Hence, the rupee is widely accepted as a medium of exchange.  $1\frac{1}{4} \times 4 = 5$

**AI** 4. Why is money transaction system better than barter system? Explain with examples. **U**

**Ans.** (i) Transaction system is better than a barter system because the double coincidence of wants creates a problem.

(ii) For example, a shoe manufacturer wants to sell shoes in the market and wants to buy wheat. For this, he would look for a wheat growing farmer who would exchange his wheat with the shoes.

(iii) In a barter system, goods are exchanged without the use of money.

(iv) In contrast, in an economy where money is in use; money provides the crucial intermediate step.

$1\frac{1}{4} \times 4 = 5$

5. "Credit sometimes pushes the borrower into a situation from which recovery is very painful." Support the statement with examples.

**A** [Delhi SET I, 2020]

**Ans.** It is true that credit sometimes pushes the borrower into a situation from which recovery is very painful. It happens in cases like:

- (i) In case of rural area if crop fails due to natural factors, it will be difficult to repay.
- (ii) In case of failure of a business it will be difficult to repay interest.
- (iii) In situations with high risks, credit might create further problems for the borrower.
- (iv) In the situation when borrower is unable to pay previous loan and he takes new loan.
- (v) Loans taken by poor people from informal lenders sometimes, lead them to debt trap because of high interest rate.

**6. Why is cheap and affordable credit important for the country's development? Explain any three reasons.** [A] + [U] [Delhi & OD, 2018]

OR

**Why is credit a crucial element in the economic development?** [U] [CBSE SQP, 2018-19]

OR

**[AI] "Cheap and affordable credit is crucial for the country's development." Explain the statement with five points.** [E]

**Ans.** Importance of cheap and affordable credit for the country's development:

- (i) Cheap and affordable credit would lead to higher income.
- (ii) Many people could borrow for a variety of needs
- (iii) It encourages people to invest in agriculture, do business and set up small scale industries etc.
- (iv) It enables more investment which will lead to the acceleration of economic activities.
- (v) Affordable credit would also end the cycle of the debt trap.
- (vi) Any other relevant point.

[CBSE Marking Scheme, 2018]  $1 \times 5 = 5$

**7. Describe the vital and positive role of credit with examples.** [A] [Board Term-II, Delhi, 2016]

OR

**What is credit? How does credit play a vital and positive role? Explain with an example.**

[A] [Board Term-II, 2015]

**Ans.** 'Credit' refers to an agreement in which the lender supplies the borrower with money, goods or services in return for the promise of future payment.

**Credit plays a vital and positive role as:**

- (i) Credit helps people from all walks of life in setting up their business, increase their income and support their families.
- (ii) To some people, loan helps a lot in constructing their houses and get relief from monthly rent.
- (iii) To others, it helps a lot in raising their standards of living.

- (iv) Example of Salim, credit helps him and he is able to increase his earnings.  $1 + 4 = 5$

[CBSE Marking Scheme, 2016]

**8. How can the formal sector loans be made beneficial for poor farmers and workers? Suggest any five measures.** [U] [Board Term-II, OD, 2016]

**Ans.** Formal sector loans can be made beneficial for poor farmers and workers in the following ways:

- (i) Create awareness to farmers about formal sector loans.
- (ii) Process of providing loans should be made easier. It should be simple, fast and timely.
- (iii) More number of Nationalized Banks/Cooperative Banks should be opened in the rural sector.
- (iv) Banks and cooperatives should increase facility of providing loans so that dependence on informal sources of credit reduces.
- (v) The benefits of loans should be extended to poor farmers and small scale industries.
- (vi) While formal sector loans need to expand, it is also necessary that everyone receives these loans.

(Any five)  $1 \times 5 = 5$

[CBSE Marking Scheme, 2016]

**9. How are deposits with the bank beneficial for individual as well as for the nation? Explain with examples.** [U] [Board Term-II, 2015]

**Ans.** The deposits with banks are beneficial for the individual as well as for the nation:

- (i) Banks accept deposit and also pay an amount as interest and in this way people earn money.
- (ii) People's money is safe with banks.
- (iii) It is easy for individuals to get credit who have savings and current account in the banks.
- (iv) Poor people who are engaged in production need credit.
- (v) Credit provided by the banks for government projects helps in the development of the nation.
- (vi) Banks provide loans for the promotion of International trade.
- (vii) Development of infrastructure is undertaken with the loans provided by the banks.

(Any five)  $1 \times 5 = 5$

[CBSE Marking Scheme, 2015]

**10. Why is it necessary for banks and cooperatives to increase their lending in rural areas? Explain.**

[U] [Board Term-II, 2015]

**Ans.** Necessity for the banks and cooperative societies to increase their lending facilities in rural areas:

- (i) Dependence on informal sources of credit reduces.
- (ii) To provide more loan facilities to rural households.

- (iii) To save rural people from exploitation.
- (iv) It is important that the formal credit is distributed more equally so that the poor can benefit from the cheaper loans.
- (v) The bank and the cooperative societies have to increase the lending facilities to improve the livelihood of the people in the rural areas.

[CBSE Marking Scheme, 2015]  $1 \times 5 = 5$

11. How do banks play an important role in the economy of India? Explain.

[U] [Board Term-II, OD, 2015]

**Ans. Banks play an important role in developing the economy of India:**

- (i) They keep the money of the people in their safe custody.
- (ii) They give interest on the deposited money to the people.
- (iii) They mediate between those who have surplus money and those who are in need of money.
- (iv) They provide loan to a large number of people at the low interest rate.
- (v) They promote agricultural and industrial sector by providing loans.
- (vi) They also provide funds to different organisations.

(Any five)  $1 \times 5 = 5$

[CBSE Marking Scheme, 2015]

12. How do banks mediate between those who have surplus money and those who need money?

[R] [O.E.B.]

- Ans. (i)** Banks keep a small proportion of their deposits as cash with themselves.
- (ii)** Major portion of deposits is used for extending loans.
- (iii)** The banks mediate between depositors and borrowers in this way.
- (iv)** They charge high rate of interest on loans than what they offer on deposits.  $1\frac{1}{4} \times 4 = 5$

**[AI] 13. Which are the two major sources of formal sectors in India? Why do we need to expand the formal sources of credit?**

[R] [O.E.B.]

**Ans. The two major sources of formal sources of credit are:**

- (i) Banks and (ii) Cooperatives.

**Need to expand formal sources of credit are:**

- (i) To save the poor farmers and workers from the exploitation by the informal sector credit.
- (ii) Informal sector charges a higher interest on loans which means that a large part of the earnings is used to repay the loan.
- (iii) Formal credit can fulfil various needs of the people by providing cheap and affordable credit.

$2 + 3 = 5$

14. Explain any two features each of formal sector loans and informal sector loans.

[A] [O.E.B.]

**Ans. Formal Sector Loans:** Include loans from banks and cooperatives. Features of formal sector loans are:

- (i) Formal sectors provide cheap and affordable loans and their rate of interest is monitored by Reserve Bank of India.
- (ii) Formal sector strictly follows the terms of credit, which include interest rate, collateral, documentation and the mode of repayment.

**Informal Sector Loans:** Include loans from moneylenders, traders, employers, relatives, friends, etc.

**Features of informal sector loans are:**

- (i) Their credit activities are not governed by any organisation, therefore they charge a higher rate of interest.
- (ii) Informal sector loan providers know the borrowers personally, and hence they provide loans on easy terms without collateral and documentation.

### COMMONLY MADE ERROR

- ➡ The student should mention the examples for both type of loans.

### ANSWERING TIP

- ➡ Names of Banks, Cooperatives, Moneylenders, traders were not written in few answers.