CBSE CLASS X

Social Science (087)

QUESTION PAPER

AI-generated question paper

Code: 1KLEOU **Questions: 49** **Maximum Marks: 133** **Generated: 2026-06-26 09:48**

SELECTIONS USED

Subject	Social Science
Lessons	3 Money and Credit
Level of understanding	Thorough understanding
Question selection	Curated chapter coverage (~5 questions per section + 8 synthesis)
Model	claude-sonnet-4-6

Composition — Difficulty: 2 straightforward · 29 medium · 18 deep | Types: 32 Short · 7 MCQ · 6 Long · 4 Very short

Q1. medium thorough-understanding § NOTES FOR THE TEACHER **[2]**

Why is modern currency accepted as a medium of exchange even though it is not made of precious metals and has no intrinsic use of its own?

◆ **Money and Credit**

Q2. medium thorough-understanding § NOTES FOR THE TEACHER **[3]**

What is meant by 'double coincidence of wants' in a barter economy? Explain why the use of money as a medium of exchange eliminates this requirement.

◆ **Money and Credit**

Q3. deep thorough-understanding § NOTES FOR THE TEACHER **[3]**

Banks hold only a small fraction of their total deposits as cash reserves, yet they are normally able to meet all withdrawal demands. Why is this the case, and what risk does it create?

◆ **Money and Credit**

Q4. medium thorough-understanding § NOTES FOR THE TEACHER **[1]**

Credit helped Salim, the shoe manufacturer, expand his business and increase earnings, but pushed Swapna, the farmer, deeper into debt. Both borrowed money to meet production costs. What factor BEST explains why credit had such opposite outcomes for the two borrowers?
(A) Salim borrowed from a formal source while Swapna borrowed from an informal source
(B) Salim had a higher income than Swapna before taking the loan
(C) Salim's earnings increased as planned, while Swapna's crop failed, leaving her unable to repay
(D) Salim used the loan for manufacturing while Swapna used it for consumption

A Salim borrowed from formal sources while Swapna borrowed from informal sources.
B The level of risk in their situations differed — Salim faced a confirmed order while Swapna's crop was vulnerable to failure.
C Salim repaid his loan faster than Swapna could.
D Swapna had no collateral to offer the moneylender, so she was charged a higher rate.

◆ **Money and Credit**

Q5. deep | thorough-understanding | § NOTES FOR THE TEACHER **[3]**

Poor rural households in India depend far more on informal sources of credit than rich households do. Explain two distinct reasons — one from the side of the banks and one from the side of the poor borrowers — that together account for this pattern.

◆ **Money and Credit**

Q6. deep | thorough-understanding | § NOTES FOR THE TEACHER **[5]**

Poor women with no assets to offer as collateral are generally unable to get loans from banks individually. Yet, banks are willing to lend to Self-Help Groups whose members are the same women. Explain how the way an SHG is organised makes it creditworthy in the eyes of a bank, even in the absence of individual collateral.

◆ **Money and Credit**

Q7. straightforward | thorough-understanding | § MONEY AS A MEDIUM OF EXCHANGE **[1]**

A dairy farmer wants to sell her milk and use the proceeds to buy rice. She approaches several rice sellers, but none of them want milk in return. (i) Explain the specific difficulty the farmer faces in completing this exchange. (ii) How does the use of money resolve this difficulty?

◆ **Money and Credit**

Q8. deep | thorough-understanding | § MONEY AS A MEDIUM OF EXCHANGE **[3]**

In a barter economy, a skilled doctor wants to pay a carpenter to repair her roof. The carpenter, however, is perfectly healthy and needs no medical services.

(i) Explain the exact difficulty the doctor faces in completing this exchange under barter.
(ii) A student argues: "This problem disappears the moment the doctor is paid in money, even if the carpenter still doesn't want medical services." Do you agree? Justify your answer by explaining what property of money makes this possible.

◆ **Money and Credit**

Q9. straightforward | thorough-understanding | § MODERN FORMS OF MONEY **[1]**

Modern currency — paper notes and coins — is not made of precious metals and has no use of its own. Yet people willingly accept it in all transactions. Why?

◆ **Money and Credit**

Q10. medium | thorough-understanding | § MODERN FORMS OF MONEY **[3]**

A leather supplier receives a cheque from a shoe manufacturer instead of cash. Explain, step by step, how the leather supplier actually receives the money owed to him.

◆ **Money and Credit**

Q11. medium | thorough-understanding | § MODERN FORMS OF MONEY **[3]**

Banks hold only a small fraction of their deposits as cash reserves and lend out the rest. Why is this practice not normally a problem, and under what circumstance could it become one?

◆ **Money and Credit**

Q12. medium thorough-understanding § MODERN FORMS OF MONEY **[1]**

Which of the following BEST explains why demand deposits are considered money?

(A) They earn interest, making them more valuable than cash.
(B) They can be withdrawn on demand and used to settle payments directly through cheques.
(C) They are issued by the Reserve Bank of India, giving them legal status.
(D) They are backed by gold reserves held by the government.

A They earn interest, making them more valuable than cash.
B They can be withdrawn on demand and used to settle payments directly through cheques.
C They are issued by the Reserve Bank of India, giving them legal status.
D They are backed by gold reserves held by the government.

◆ **Money and Credit**

Q13. medium thorough-understanding § MODERN FORMS OF MONEY **[3]**

How do commercial banks act as intermediaries between depositors and borrowers? Explain the role this plays in the economy.

◆ **Money and Credit**

Q14. deep thorough-understanding § MODERN FORMS OF MONEY **[5]**

Currency and demand deposits are both described as 'money' in the modern economy, yet they differ in origin and form. Compare the two, and explain why the existence of demand deposits as money depends critically on the banking system working properly.

◆ **Money and Credit**

Q15. deep thorough-understanding § LOAN ACTIVITIES OF BANKS **[3]**

Banks keep only a small fraction of their deposits as cash and lend out the rest. Why does this practice not normally cause a problem for depositors who wish to withdraw their money — and under what circumstance could it become a serious problem?

◆ **Money and Credit**

Q16. medium thorough-understanding § TWO DIFFERENT CREDIT SITUATIONS **[3]**

Salim takes a loan to fulfil a large order of shoes and repays it successfully, while Swapna takes a loan for crop cultivation and ends up selling part of her land. Both borrowed money for productive purposes. Why did credit help one person and harm the other?

◆ **Money and Credit**

Q17. medium | thorough-understanding | § TWO DIFFERENT CREDIT SITUATIONS **[1]**

A fisherman takes a loan at the start of the fishing season to buy nets and equipment, promising to repay after the season ends. During the season, an unexpected storm destroys his boat and catch. Which of the following best explains what will likely happen next?
(A) The loan will be repaid easily since the fisherman can take another loan to cover the loss.
(B) The credit will have played a positive role because the fisherman had a productive intent.
(C) The fisherman may fall into a debt trap, as the loss makes repayment impossible and future loans add to the burden.
(D) The lender will waive the loan since the loss was due to a natural cause.

A The loan will be repaid easily since the fisherman can take another loan to cover the loss.
B The credit will have played a positive role because the fisherman had a productive intent.
C The fisherman may fall into a debt trap, as the loss makes repayment impossible and future loans add to the burden.
D The lender will waive the loan since the loss was due to a natural cause.

◆ **Money and Credit**

Q18. medium | thorough-understanding | § TWO DIFFERENT CREDIT SITUATIONS **[2]**

A borrower who takes a second loan to repay the first often finds the debt growing rather than shrinking. Using the concept of a debt trap, explain why this cycle is so difficult to break and what conditions make a borrower particularly vulnerable to it.

◆ **Money and Credit**

Q19. deep | thorough-understanding | § TWO DIFFERENT CREDIT SITUATIONS **[3]**

Agricultural households typically borrow at the beginning of the crop season and repay only after the harvest, whereas a small manufacturer can repay a loan as soon as an order is fulfilled. Explain why this difference in the repayment pattern makes farming households significantly more vulnerable to a debt trap than small manufacturing units.

◆ **Money and Credit**

Q20. deep | thorough-understanding | § TWO DIFFERENT CREDIT SITUATIONS **[5]**

Credit can either improve a borrower's situation or make it significantly worse. Analyse what factors determine which outcome occurs, using evidence from both the shoe manufacturer and the small farmer examples.

◆ **Money and Credit**

Q21. medium | thorough-understanding | § TERMS OF CREDIT **[3]**

A borrower takes a loan from a bank using his house as collateral. He later fails to repay the loan. Explain how collateral protects the lender's interest both before and after the borrower defaults.

◆ **Money and Credit**

Q22. deep | thorough-understanding | § TERMS OF CREDIT **[3]**

Rama, an agricultural labourer, borrows from her landowner-employer at 5% per month to meet daily expenses. Arun, a medium farmer, borrows from a bank at 8.5% per annum for cultivation. Even though Arun's loan is larger in amount, why is Rama's credit arrangement far more burdensome for her? In your answer, refer to the terms of credit that make the two arrangements different.

◆ **Money and Credit**

Q23. medium | thorough-understanding | § Variety of Credit Arrangements **[3]**

Shyamal, a small farmer, borrows from an agricultural trader instead of the village moneylender. Even though the trader's interest rate is lower, the arrangement still disadvantages Shyamal. Explain how.

◆ **Money and Credit**

Q24. medium | thorough-understanding | § Variety of Credit Arrangements **[3]**

Rama, a landless agricultural labourer, borrows from her employer-landowner at 5% per month to meet household needs. Despite repaying regularly, she finds her total outstanding debt growing each season. Identify the feature of this credit arrangement that makes it exploitative, and explain how it traps the borrower over time.

◆ **Money and Credit**

Q25. medium | thorough-understanding | § Variety of Credit Arrangements **[3]**

Arun owns seven acres of land and borrows from a nationalised bank at 8.5% per annum for cultivation. Shyamal owns 1.5 acres and borrows from a trader at 3% per month. What explains the stark difference in the cost of credit available to these two farmers? What does this reveal about the role of collateral in accessing formal credit?

◆ **Money and Credit**

Q26. medium | thorough-understanding | § Variety of Credit Arrangements **[1]**

An agricultural trader in a village supplies farm inputs on credit at the start of the season and insists that farmers sell their harvested crop exclusively to him. Which of the following best explains why the trader imposes this condition?
(A) To help farmers get a better price for their crops in the market.
(B) To ensure timely repayment and earn additional profit from buying crops at low post-harvest prices.
(C) To prevent farmers from borrowing from the village moneylender.
(D) To comply with rules set by the Reserve Bank of India.

A To help farmers get a better price for their crops in the market.
B To ensure timely repayment and earn additional profit from buying crops at low post-harvest prices.
C To prevent farmers from borrowing from the village moneylender.
D To comply with rules set by the Reserve Bank of India.

◆ **Money and Credit**

Q27. medium | thorough-understanding | § Variety of Credit Arrangements **[3]**

How does a cooperative society like Krishak Cooperative manage to offer cheaper credit to its members, even though it lends mainly to small farmers who may lack individual collateral?

◆ **Money and Credit**

Q28. deep | thorough-understanding | § Variety of Credit Arrangements **[2]**

After the potato harvest, a farmer considers two options: selling the crop immediately at low post-harvest prices, or storing it in a cold storage facility and using the warehouse receipt as collateral to obtain a fresh bank loan. Explain the financial reasoning behind choosing the second option and what it reveals about the relationship between credit access and farmers' bargaining power.

◆ **Money and Credit**

Q29. deep | thorough-understanding | § Variety of Credit Arrangements **[5]**

In Sonpur, different groups of people — a small farmer, a medium farmer with bank access, and a landless labourer — each face very different terms of credit. What does this pattern reveal about the relationship between a person's economic position and the cost of credit they can access? What are the broader consequences of this inequality for rural development?

◆ **Money and Credit**

Q30. medium | thorough-understanding | § FORMAL SECTOR CREDIT IN INDIA **[1]**

[mcq] The Reserve Bank of India issues guidelines on interest rates and lending practices to commercial banks but does not exercise similar control over moneylenders or chit funds. Which of the following BEST explains why this difference in regulation exists?
(A) Moneylenders operate outside village boundaries and are therefore beyond the RBI's jurisdiction.
(B) Informal lenders are too numerous and dispersed, and their transactions are largely unrecorded, making systematic supervision impractical.
(C) Informal lenders charge lower interest rates than banks, so regulation is unnecessary.
(D) The RBI only regulates institutions that accept deposits from the public.

A Informal lenders do not charge interest, so supervision is unnecessary.
B Formal lenders are registered institutions accountable under law, whereas informal lenders operate outside any regulatory framework.
C The RBI only supervises banks in urban areas, leaving rural lenders unregulated.
D Informal lenders lend smaller amounts, making supervision impractical.

◆ **Money and Credit**

Q31. medium | thorough-understanding | § FORMAL SECTOR CREDIT IN INDIA **[3]**

[short_answer] The Reserve Bank of India does not merely allow banks to operate freely in search of profit — it imposes specific obligations on them. What are TWO such obligations, and why does the RBI consider it necessary to impose these restrictions on commercial banks?

◆ **Money and Credit**

Q32. deep | thorough-understanding | § FORMAL SECTOR CREDIT IN INDIA **[3]**

In rural India, commercial banks account for the largest share of credit, yet the poor still rely heavily on moneylenders. Using data on formal and informal credit distribution, explain this apparent contradiction.

◆ **Money and Credit**

Q33. medium | thorough-understanding | § FORMAL SECTOR CREDIT IN INDIA **[3]**

How does a high interest rate charged by an informal lender create a cycle that can make a borrower permanently worse off, rather than simply costing more money in the short term?

◆ **Money and Credit**

Q34. deep | thorough-understanding | § FORMAL SECTOR CREDIT IN INDIA **[5]**

Rich urban households obtain 83% of their loans from formal sources, while poor urban households obtain 54% of their loans from informal sources. What structural barriers prevent the poor from accessing formal credit, and what does this unequal distribution mean for economic inequality?

◆ **Money and Credit**

Q35. medium | thorough-understanding | § FORMAL SECTOR CREDIT IN INDIA **[1]**

[very_short_answer] Unlike commercial banks, informal lenders such as moneylenders are not supervised by any regulatory authority. Identify ONE specific reason why bringing informal lenders under formal regulation is structurally difficult for the government.

◆ **Money and Credit**

Q36. medium | thorough-understanding | § SELF-HELP GROUPS FOR THE POOR **[3]**

A rural woman belonging to a Self Help Group wants to take a small loan. She has no collateral to offer. Why would the SHG still be willing to lend her money, even though a bank in the same situation typically would not?

◆ **Money and Credit**

Q37. medium | thorough-understanding | § SELF-HELP GROUPS FOR THE POOR **[1]**

Which of the following best explains why banks are willing to give loans to Self Help Groups even though the individual members have no collateral?
(A) The government guarantees repayment of all SHG loans.
(B) The group collectively takes responsibility for repayment, so peer pressure among members ensures defaults are followed up seriously.
(C) SHG members always deposit large savings with the bank before receiving a loan.
(D) RBI directs banks to give loans to SHGs without any conditions.

A The government guarantees repayment of all SHG loans.
B The group collectively takes responsibility for repayment, so peer pressure among members ensures defaults are followed up seriously.
C SHG members always deposit large savings with the bank before receiving a loan.
D RBI directs banks to give loans to SHGs without any conditions.

◆ **Money and Credit**

Q38. deep | thorough-understanding | § SELF-HELP GROUPS FOR THE POOR **[5]**

Rama, an agricultural labourer, remains trapped in debt with her landowner-employer despite working for him year after year. How could joining a Self Help Group change her situation? In your answer, address both the financial and non-financial benefits she could gain.

◆ **Money and Credit**

Q39. medium | thorough-understanding | § SELF-HELP GROUPS FOR THE POOR **[3]**

A newly formed SHG applies to a bank for a loan but is rejected. A bank manager explains that the group needs to demonstrate certain creditworthiness before a loan can be sanctioned. What would the bank look for in the group's track record, and how does this criterion protect both the bank and the group's members?

◆ **Money and Credit**

Q40. deep | thorough-understanding | § SELF-HELP GROUPS FOR THE POOR **[2]**

The interest rate charged by an SHG on loans to its members is lower than that of a moneylender but higher than zero. Why do you think the SHG charges any interest at all, rather than lending completely interest-free to its own members?

◆ **Money and Credit**

Q41. medium | thorough-understanding | § SUMMING UP **[3]**

Credit can either lift a borrower out of poverty or push them deeper into a debt trap. Using one concrete example for each outcome, explain what determines whether credit helps or harms a borrower.

◆ **Money and Credit**

Q42. medium | thorough-understanding | § ADDITIONAL PROJECT / ACTIVITY **[3]**

A government employee with a steady salary and a migrant labourer in the city both need loans. Why is the government employee far more likely to receive a bank loan than the migrant labourer, even if both need the same amount? What does this difference reveal about who benefits from formal credit in India?

◆ **Money and Credit**

Q43. medium | thorough-understanding | § (whole-chapter synthesis) **[3]**

Money is described as a medium of exchange. Explain how the modern banking system allows money to fulfil this role even without any physical currency changing hands. Use appropriate examples in your answer.

◆ **Money and Credit**

Q44. deep | thorough-understanding | § (whole-chapter synthesis) **[3]**

Banks keep only a small proportion of their total deposits as cash reserves and lend out the rest. Explain how this practice makes credit possible in the economy, and what risk it creates for depositors and the banking system.

◆ Money and Credit

Q45. medium | thorough-understanding | § (whole-chapter synthesis) **[1]**

Salim the shoe manufacturer and Swapna the groundnut farmer both take credit to meet their production needs, yet credit helps one and harms the other. What single underlying factor best explains this difference in outcome?

◆ Money and Credit

Q46. deep | thorough-understanding | § (whole-chapter synthesis) **[3]**

Collateral is a key term in formal credit arrangements. How does the requirement of collateral simultaneously explain (i) why richer households access formal credit more easily, and (ii) why the poor are pushed towards informal lenders who charge much higher interest rates?

◆ Money and Credit

Q47. medium | thorough-understanding | § (whole-chapter synthesis) **[1]**

Which of the following best explains why cheap and affordable credit is described as crucial for a country's development?
(A) It increases the government's tax revenue by encouraging more commercial activity among large corporations.
(B) It allows borrowers — including small farmers, traders and entrepreneurs — to invest, raise incomes and repay loans without falling into debt traps.
(C) It reduces the need for collateral, making banks more profitable and financially secure.
(D) It enables the Reserve Bank of India to print less currency, keeping inflation under control.

A It increases the profits of banks, allowing them to pay higher interest to depositors.
B It allows borrowers — including small farmers, traders and entrepreneurs — to invest, raise incomes and repay without falling into debt traps.
C It reduces the need for the Reserve Bank of India to supervise informal lenders.
D It eliminates the double coincidence of wants problem that exists in a barter economy.

◆ Money and Credit

Q48. deep | thorough-understanding | § (whole-chapter synthesis) **[3]**

The Reserve Bank of India supervises formal lenders, but no such body oversees informal lenders. Explain how this difference in supervision directly affects (i) the cost of borrowing for the poor and (ii) their vulnerability to a debt trap.

◆ Money and Credit

Q49. medium | thorough-understanding | § (whole-chapter synthesis) **[3]**

The poor in rural areas often find it difficult to access formal credit. Explain how Self Help Groups address the barriers that prevent the poor from borrowing from formal financial institutions.

◆ Money and Credit

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CBSE CLASS X

Social Science (087)

ANSWER KEY

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Q1. medium thorough-understanding § NOTES FOR THE TEACHER **[2]**

Why is modern currency accepted as a medium of exchange even though it is not made of precious metals and has no intrinsic use of its own?

◆ **Money and Credit**

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Model Answer

Modern currency has no intrinsic value and is not made of precious metals, yet it is accepted as a medium of exchange because it is **authorised by the government**. In India, the Reserve Bank of India issues currency notes on behalf of the central government. The law makes it **legal tender** — no individual can legally refuse a payment made in rupees.

Source: Chapter 3, Modern Forms of Money — Currency

Explanation

- The examiner expects two clear points: (1) government authorisation, and (2) legal tender status (no one can legally refuse it).
- Mentioning RBI's role adds precision and is expected at this level.
- Avoid writing about intrinsic value at length — just acknowledge it briefly and move to the actual reason.
- Do not confuse "authorised by government" with "backed by gold" — modern currency is NOT gold-backed; its acceptance rests purely on legal authority.

Q2. medium | thorough-understanding | § NOTES FOR THE TEACHER **[3]**

What is meant by 'double coincidence of wants' in a barter economy? Explain why the use of money as a medium of exchange eliminates this requirement.

◆ Money and Credit

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Model Answer

Double coincidence of wants means that both parties in an exchange must want exactly what the other has to offer. For example, a shoe manufacturer wanting wheat must find a farmer who not only wants to sell wheat but also wants to buy shoes in return. This is an essential feature of a barter system.

Money eliminates this requirement by acting as a **medium of exchange** — an intermediate step. The shoe manufacturer only needs to find a buyer for his shoes, receive money, and then use that money to buy wheat from any seller. Thus, the two transactions are separated, and mutual agreement to exchange is no longer necessary.

Source: Money and Credit, Chapter 3

Explanation

- **1 mark** for defining double coincidence of wants correctly.
- **1 mark** for a relevant example (shoe manufacturer/farmer works perfectly as it's straight from the textbook).
- **1 mark** for explaining how money, as a medium of exchange, removes this requirement by splitting one barter transaction into two separate money transactions.
- Use the textbook example — examiners recognise it and it scores full marks.
- Key phrase to include: **"medium of exchange"** and **"intermediate step"**.

Q3. deep thorough-understanding § NOTES FOR THE TEACHER **[3]**

Banks hold only a small fraction of their total deposits as cash reserves, yet they are normally able to meet all withdrawal demands. Why is this the case, and what risk does it create?

◆ **Money and Credit**

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Model Answer

Banks keep only about 5% of their deposits as cash reserves. On any given day, only **some** depositors withdraw money, not all at once. Since withdrawals and new deposits happen continuously, the small cash reserve is sufficient to meet daily demands.

Risk created: If all depositors were to demand their money simultaneously, the bank would not be able to pay everyone, as the major portion of deposits has been given out as loans. This could lead to a collapse of the bank.

Source: Money and Credit, Loan Activities of Banks

Explanation

- The key phrase from the textbook is: *"only some of its many depositors come to withdraw cash on any given day"* — use this logic directly.
- The risk is hinted at by the textbook's own question: *"What would happen if all depositors came at once?"* — always address this for full marks.
- For 3 marks: ~1 mark for the mechanism, ~1 mark for why it works, ~1 mark for the risk.

Q4. medium | thorough-understanding | § NOTES FOR THE TEACHER **[1]**

Credit helped Salim, the shoe manufacturer, expand his business and increase earnings, but pushed Swapna, the farmer, deeper into debt. Both borrowed money to meet production costs. What factor BEST explains why credit had such opposite outcomes for the two borrowers?

(A) Salim borrowed from a formal source while Swapna borrowed from an informal source
(B) Salim had a higher income than Swapna before taking the loan
(C) Salim's earnings increased as planned, while Swapna's crop failed, leaving her unable to repay
(D) Salim used the loan for manufacturing while Swapna used it for consumption

A Salim borrowed from formal sources while Swapna borrowed from informal sources.
B The level of risk in their situations differed — Salim faced a confirmed order while Swapna's crop was vulnerable to failure.
C Salim repaid his loan faster than Swapna could.
D Swapna had no collateral to offer the moneylender, so she was charged a higher rate.

◆ **Money and Credit**

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Model Answer

Answer: B

Salim faced a confirmed order, guaranteeing income to repay the loan, while Swapna's crop failed due to pests, making repayment impossible and pushing her into a debt trap.

Explanation

The passage explicitly states: *"Whether credit would be useful or not depends on the risks in the situation."* Salim had a confirmed order (low risk), while Swapna faced crop failure (high risk). The question asks for the **best** explanation of opposite outcomes — that is the difference in risk levels, not the source of credit (though informal sources worsened Swapna's situation, it wasn't the direct cause of the opposite outcomes). Option B matches the textbook's own conclusion most precisely.

Q5. deep | thorough-understanding | § NOTES FOR THE TEACHER **[3]**

Poor rural households in India depend far more on informal sources of credit than rich households do. Explain two distinct reasons — one from the side of the banks and one from the side of the poor borrowers — that together account for this pattern.

◆ Money and Credit

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Model Answer

From the bank's side: Banks are not present everywhere in rural India, and where present, they require proper documents and **collateral** to sanction loans. Poor rural households typically lack collateral (land, assets), so banks refuse them loans.

From the poor borrowers' side: Informal lenders such as moneylenders know the borrowers personally and are willing to lend **without collateral**, without paperwork, and even when earlier loans are unpaid. This easy accessibility pushes poor households toward informal credit despite its very high interest rates.

Source: Money and Credit, "Self-Help Groups for the Poor" / "Formal Sector Credit in India"

Explanation

- The question specifically asks for **one bank-side reason** and **one borrower-side reason** — keep them clearly separated.
- The bank-side reason is the **collateral requirement** (and limited rural presence); the borrower-side reason is the **personal relationship and flexible terms** offered by moneylenders.
- Avoid just listing informal vs. formal differences — the examiner wants a causal explanation of *why poor households* end up with informal credit.
- For 3 marks, two well-explained points (one each side) plus a brief linking idea is sufficient.

Q6. deep | thorough-understanding | § NOTES FOR THE TEACHER **[5]**

Poor women with no assets to offer as collateral are generally unable to get loans from banks individually. Yet, banks are willing to lend to Self-Help Groups whose members are the same women. Explain how the way an SHG is organised makes it creditworthy in the eyes of a bank, even in the absence of individual collateral.

◆ Money and Credit

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Model Answer

An SHG is creditworthy to a bank because of the following features of its organisation:

1. **Pooled savings as internal creditworthiness:** A typical SHG has 15–20 members who save regularly (₹25–₹100 per month). This pooled saving over 1–2 years demonstrates financial discipline to the bank.
1. **Loan sanctioned in group's name:** The bank lends to the group collectively, not to an individual. The group itself acts as a guarantee, replacing the need for individual collateral.
1. **Group responsibility for repayment:** The entire group is responsible for loan repayment. If any one member defaults, other members follow up seriously to ensure recovery. This social pressure replaces collateral as security for the bank.
1. **Democratic decision-making:** Members themselves decide the purpose, amount, interest rate, and repayment schedule of loans, ensuring discipline and accountability within the group.
1. **Track record:** Regular savings and internal lending before approaching the bank establish a repayment history, making the group trustworthy in the bank's eyes.

Thus, collective responsibility and savings discipline substitute for individual collateral.

Source: Chapter 3, Self-Help Groups for the Poor

Explanation

The examiner expects students to explain the **mechanism**, not just state that SHGs exist. Key points are: (i) group liability replacing collateral, (ii) social/peer pressure ensuring repayment, (iii) regular savings as proof of discipline, and (iv) the loan being in the group's name. Avoid vague phrases like "women are empowered" — stick to structural reasons the bank finds credible. 5 crisp points with brief elaboration is ideal for 5 marks.

Q7. straightforward | thorough-understanding | § MONEY AS A MEDIUM OF EXCHANGE **[1]**

A dairy farmer wants to sell her milk and use the proceeds to buy rice. She approaches several rice sellers, but none of them want milk in return. (i) Explain the specific difficulty the farmer faces in completing this exchange. (ii) How does the use of money resolve this difficulty?

◆ **Money and Credit**

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Model Answer

(i) The farmer faces the problem of **double coincidence of wants** — she needs a rice seller who also wants milk, but none of them do.

(ii) Money acts as a **medium of exchange** — she can sell milk for money and use that money to buy rice, eliminating the need for double coincidence of wants.

Source: Money and Credit, Medium of Exchange

Explanation

This is technically a 1-mark question but has two sub-parts, so keep each answer to one short line. Examiners look for the exact term **"double coincidence of wants"** for part (i) and **"medium of exchange"** for part (ii). Always use these textbook terms — partial credit may be awarded for explanation alone, but the terms are essential for full marks.

Q8. deep | thorough-understanding | § MONEY AS A MEDIUM OF EXCHANGE **[3]**

In a barter economy, a skilled doctor wants to pay a carpenter to repair her roof. The carpenter, however, is perfectly healthy and needs no medical services.

(i) Explain the exact difficulty the doctor faces in completing this exchange under barter.
(ii) A student argues: "This problem disappears the moment the doctor is paid in money, even if the carpenter still doesn't want medical services." Do you agree? Justify your answer by explaining what property of money makes this possible.

◆ Money and Credit

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Model Answer

(i) The doctor faces the problem of **double coincidence of wants**. In a barter system, exchange requires that both parties want exactly what the other offers. The carpenter has no need for medical services, so despite the doctor needing repairs, no exchange can take place. This makes barter highly inconvenient.

(ii) Yes, I agree. When the doctor is paid in money, she can offer the carpenter money — not medical services. Money acts as a **medium of exchange**, eliminating the need for double coincidence of wants. The carpenter accepts money because he can use it to buy *anything* he needs. Thus, both parties benefit without needing matching wants.

Source: Chapter 3 — Money and Credit, Medium of Exchange

Explanation

- **(i)** centres on the term "double coincidence of wants" — use it explicitly; examiners award marks for this term.
- **(ii)** The key property to name is **"medium of exchange"**. Explain *why* it works: money is universally accepted, so the carpenter doesn't need the doctor's services — he accepts money and spends it elsewhere. The student's argument is correct; your job is to justify it with the concept.
- Keep definitions textbook-close; avoid vague phrases like "money is useful."

Q9. straightforward | thorough-understanding | § MODERN FORMS OF MONEY **[1]**

Modern currency — paper notes and coins — is not made of precious metals and has no use of its own. Yet people willingly accept it in all transactions. Why?

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Model Answer

Modern currency is accepted as a medium of exchange because it is **authorised by the government**. In India, the law makes it legal tender that cannot be refused in settling transactions.

Source: Money and Credit, Chapter 3 — Currency

Explanation

The examiner expects one clear reason: **government authorization / legal tender status**. Mention RBI issuing notes on behalf of the central government and the law making rupee legally acceptable if you have space, but the core point is "government authority." Avoid long explanations about barter or history — this is a 1-mark answer.

Q10. medium thorough-understanding § MODERN FORMS OF MONEY **[3]**

A leather supplier receives a cheque from a shoe manufacturer instead of cash. Explain, step by step, how the leather supplier actually receives the money owed to him.

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Model Answer

The leather supplier deposits the cheque in his own bank. His bank sends the cheque to Salim's (the shoe manufacturer's) bank for clearance. Salim's bank checks whether sufficient funds exist in his account. If yes, the amount is deducted from Salim's account and transferred to the leather supplier's bank, which then credits the amount to the supplier's account. The supplier can then withdraw the money as cash or use it for further transactions.

Source: Money and Credit, Chapter 3

Explanation

The question tests knowledge of how cheques work as a banking instrument — a key concept in "Modern Forms of Money." Examiners expect students to mention: (1) depositing the cheque, (2) the role of both banks, (3) verification/clearance, and (4) final credit to the supplier's account. Four logical steps = 3 marks. Do not write vague statements like "the bank pays him" — show the step-by-step transfer process between two banks.

Q11. medium thorough-understanding § MODERN FORMS OF MONEY **[3]**

Banks hold only a small fraction of their deposits as cash reserves and lend out the rest. Why is this practice not normally a problem, and under what circumstance could it become one?

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Model Answer

Banks keep only about 5% of deposits as cash reserves because on any given day, only a small number of depositors withdraw money simultaneously. The remaining deposits are lent out to borrowers, earning interest — this is how banks function as mediators between depositors and borrowers.

This practice becomes a problem if **all depositors try to withdraw their money at the same time**. In such a situation, the bank would not have enough cash to repay everyone, causing it to fail. This is why the RBI monitors banks to ensure they maintain the required minimum cash balance.

Source: Money and Credit, Loan Activities of Banks / Formal Sector Credit in India

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Explanation

- The examiner wants **two clear parts**: (1) why it normally works — *not all depositors withdraw at once*, and (2) the risk — *if all depositors withdraw simultaneously, the bank cannot pay*. Both are explicitly stated in the textbook passage.
- Mentioning the **RBI's supervisory role** adds a mark-worthy point for a 3-mark answer.
- Avoid over-explaining; keep it tight. The phrase "banks mediate between depositors and borrowers" is a key textbook line — use it.

Q12. medium · thorough-understanding · § MODERN FORMS OF MONEY **[1]**

Which of the following BEST explains why demand deposits are considered money?

(A) They earn interest, making them more valuable than cash.
(B) They can be withdrawn on demand and used to settle payments directly through cheques.
(C) They are issued by the Reserve Bank of India, giving them legal status.
(D) They are backed by gold reserves held by the government.

A They earn interest, making them more valuable than cash.
B They can be withdrawn on demand and used to settle payments directly through cheques.
C They are issued by the Reserve Bank of India, giving them legal status.
D They are backed by gold reserves held by the government.

◆ Money and Credit

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Model Answer

(B) They can be withdrawn on demand and used to settle payments directly through cheques.

Explanation

The textbook explicitly states: "The facility of cheques against demand deposits makes it possible to directly settle payments without the use of cash" — this is what gives demand deposits the essential characteristic of money (medium of exchange). Options C and D are factually wrong (demand deposits are held by commercial banks, not RBI, and are not gold-backed). Option A is a benefit but not the reason they are *money*.

Q13. medium · thorough-understanding · § MODERN FORMS OF MONEY **[3]**

How do commercial banks act as intermediaries between depositors and borrowers? Explain the role this plays in the economy.

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Model Answer

Commercial banks act as intermediaries by accepting deposits from people who have surplus funds and using the major portion of these deposits to extend loans to borrowers who need funds. Banks keep only about 5% of deposits as cash reserve to meet daily withdrawal demands.

Role in the economy:

- Credit reaches those who need it for economic activities like farming, trade, and business.
- Banks charge higher interest on loans than they pay on deposits; this difference is their income.
- This flow of funds supports production, employment, and overall economic development.

Source: Chapter 3, Loan Activities of Banks

Explanation

The examiner expects three things for 3 marks: (1) the mechanism — deposits → cash reserve → loans; (2) the definition of intermediary (surplus funds → deficit needs); (3) the economic role. Mentioning the 5% cash reserve figure shows textbook accuracy. Avoid writing about RBI or informal credit here — keep it focused on banks as intermediaries.

Q14. deep | thorough-understanding | § MODERN FORMS OF MONEY **[5]**

Currency and demand deposits are both described as 'money' in the modern economy, yet they differ in origin and form. Compare the two, and explain why the existence of demand deposits as money depends critically on the banking system working properly.

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Model Answer

Currency is paper notes and coins issued by the Reserve Bank of India on behalf of the central government. It has no intrinsic value but is accepted as a medium of exchange because it is legally authorised — no one can refuse payment in rupees.

Demand deposits are money held in bank accounts that can be withdrawn on demand. They function as money because cheques can be drawn against them, allowing payments to be settled without any physical cash changing hands.

Key difference: Currency is issued by the central government/RBI; demand deposits are created when people deposit money with banks.

Why the banking system is critical: Without banks, there would be no demand deposits and no cheque facility. Banks also hold only a fraction (~5%) of deposits as cash reserve. If the banking system fails — for example, if all depositors demanded cash simultaneously — cheque payments would collapse, destroying demand deposits as a form of money.

Source: Modern Forms of Money; Loan Activities of Banks, Chapter 3

Explanation

- Examiners look for: (1) definition/origin of each form, (2) what makes demand deposits function as money (cheque facility), (3) the specific link to banking — no bank = no demand deposits.
- The fraction-reserve point (banks hold ~5% as cash) is important to explain *why* the system must work properly — it shows demand deposits rest on trust in the banking system.
- Avoid long historical content on barter/coins — not relevant here.

Q15. deep | thorough-understanding | § LOAN ACTIVITIES OF BANKS **[3]**

Banks keep only a small fraction of their deposits as cash and lend out the rest. Why does this practice not normally cause a problem for depositors who wish to withdraw their money — and under what circumstance could it become a serious problem?

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Model Answer

Banks keep only about 5% of deposits as cash because **not all depositors withdraw money at the same time**. On any given day, only a small number of depositors need cash, so this reserve is sufficient to meet daily withdrawal demands. Banks lend out the remaining deposits and earn income from the interest charged.

However, this becomes a **serious problem if all depositors rush to withdraw their money simultaneously**. In such a situation, the small cash reserve would be completely inadequate, and the bank would be unable to honour all withdrawal requests, potentially causing it to collapse.

Source: Money and Credit, Chapter 3 (Loan Activities of Banks)

Explanation

- The textbook directly raises the question: *"What would happen if all depositors went to ask for their money at the same time?"* — your answer must address this.
- Key terms to use: **cash reserve (5%)**, **provision**, **manage withdrawals**, **bank run** (concept, even if not named).
- Examiners look for: (1) why it normally works — staggered withdrawals, and (2) the exceptional risk — simultaneous mass withdrawal. Both parts must be present for full marks.

Q16. medium · thorough-understanding · § TWO DIFFERENT CREDIT SITUATIONS **[3]**

Salim takes a loan to fulfil a large order of shoes and repays it successfully, while Swapna takes a loan for crop cultivation and ends up selling part of her land. Both borrowed money for productive purposes. Why did credit help one person and harm the other?

◆ **Money and Credit**

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Model Answer

Both Salim and Swapna borrowed for productive purposes, but the **risk involved** in each situation was different.

Salim had a confirmed order, so his income was certain. Credit helped him meet working capital needs, complete production on time, and earn a profit. He repaid the loan comfortably.

Swapna's crop failed due to a pest attack, making repayment impossible. Debt accumulated over two years, forcing her to sell part of her land to repay it — a **debt trap**.

Thus, whether credit helps or harms depends on **the risk in the situation** and whether there is support in case of loss.

Source: Chapter 3 — Money and Credit, Two Different Credit Situations

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Explanation

- The key concept examiners expect is **debt trap** and the role of **risk**.
- Mention both cases briefly and contrast them — don't explain only one.
- The textbook's own conclusion is the best closing line: *"Whether credit would be useful or not depends on the risks in the situation and whether there is some support in case of loss."* Use it directly.
- Avoid padding — 3 marks = ~3 distinct points: Salim's outcome, Swapna's outcome, and the reason for the difference.

Q17. medium | thorough-understanding | § TWO DIFFERENT CREDIT SITUATIONS **[1]**

A fisherman takes a loan at the start of the fishing season to buy nets and equipment, promising to repay after the season ends. During the season, an unexpected storm destroys his boat and catch. Which of the following best explains what will likely happen next?

(A) The loan will be repaid easily since the fisherman can take another loan to cover the loss.
(B) The credit will have played a positive role because the fisherman had a productive intent.
(C) The fisherman may fall into a debt trap, as the loss makes repayment impossible and future loans add to the burden.
(D) The lender will waive the loan since the loss was due to a natural cause.

A The loan will be repaid easily since the fisherman can take another loan to cover the loss.
B The credit will have played a positive role because the fisherman had a productive intent.
C The fisherman may fall into a debt trap, as the loss makes repayment impossible and future loans add to the burden.
D The lender will waive the loan since the loss was due to a natural cause.

◆ **Money and Credit**

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Model Answer

(C) The fisherman may fall into a debt trap, as the loss makes repayment impossible and future loans add to the burden.

Explanation

The passage describes Swapna's situation, where crop failure made loan repayment impossible, forcing her to take fresh loans — a classic **debt trap**. Option A is wrong (a new loan adds burden, not relief). Option B is wrong (positive intent does not guarantee positive outcome). Option D is incorrect as lenders are not obligated to waive loans due to natural causes. The textbook explicitly states: *"Whether credit would be useful or not depends on the risks in the situation."*

Source: *Money and Credit*, Chapter 3 — Two Different Credit Situations (Swapna's Problem)

Q18. medium thorough-understanding § TWO DIFFERENT CREDIT SITUATIONS **[2]**

A borrower who takes a second loan to repay the first often finds the debt growing rather than shrinking. Using the concept of a debt trap, explain why this cycle is so difficult to break and what conditions make a borrower particularly vulnerable to it.

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Model Answer

A **debt trap** occurs when a borrower takes a new loan to repay an existing one, causing debt to grow rather than reduce. Swapna's case illustrates this: crop failure made repayment impossible, so debt accumulated, forcing her to sell land. Borrowers are most vulnerable when they face high-risk situations (crop failure, illness), lack collateral for cheap formal credit, and must rely on moneylenders charging very high interest rates (e.g., 60% per annum), making repayment nearly impossible from limited earnings.

Source: Chapter 3, Two Different Credit Situations

Explanation

- Examiners expect: definition/explanation of debt trap + specific vulnerability conditions.
- Key terms to use: *debt trap*, *collateral*, *informal sources*, *high interest rate*, *risk*.
- Swapna's example is the textbook illustration — always anchor answers in it.
- Avoid generic statements; link vulnerability directly to high-risk situations and lack of formal credit access.

Q19. deep | thorough-understanding | § TWO DIFFERENT CREDIT SITUATIONS **[3]**

Agricultural households typically borrow at the beginning of the crop season and repay only after the harvest, whereas a small manufacturer can repay a loan as soon as an order is fulfilled. Explain why this difference in the repayment pattern makes farming households significantly more vulnerable to a debt trap than small manufacturing units.

◆ **Money and Credit**

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Model Answer

Farming households borrow at the start of the crop season and can only repay after harvest — a gap of 3–4 months. During this period, if the crop fails (due to pests, drought, etc.), repayment becomes impossible. The farmer must then take a fresh loan, with interest accumulating on the old one, pushing them into a debt trap (as seen in Swapna's case).

A small manufacturer like Salim, however, repays the loan as soon as an order is fulfilled. The repayment cycle is short and not dependent on uncertain natural factors. If one order is delayed, the next can cover costs. There is no long waiting period with compounding interest, so the risk of falling into a debt trap is much lower.

Source: Chapter 3 — Two Different Credit Situations; Swapna's Problem

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Explanation

- Examiners look for **two clear contrasts**: the long, uncertain repayment cycle of farmers vs. the short, predictable cycle of manufacturers.
- Mention **crop failure risk** and **compounding debt** for farmers — these are the key reasons for vulnerability.
- Refer to **Swapna's example** to show you've read the textbook case.
- Avoid writing more than needed — 3 marks = ~3 distinct points made clearly.

Q20. deep thorough-understanding § TWO DIFFERENT CREDIT SITUATIONS **[5]**

Credit can either improve a borrower's situation or make it significantly worse. Analyse what factors determine which outcome occurs, using evidence from both the shoe manufacturer and the small farmer examples.

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Model Answer

Whether credit improves or worsens a borrower's situation depends on the following factors:

1. **Purpose of credit:** Salim borrowed to meet working capital needs for a confirmed order — a productive, short-term use. Swapna borrowed for cultivation with uncertain returns.
1. **Risk involved:** Salim faced low risk as he already had an order. Swapna faced high risk — crop failure due to pests was beyond her control.
1. **Outcome of the activity:** Salim completed the order, earned profit, and repaid the loan. Swapna's crop failed; she could not repay, leading to a debt trap and forced sale of land.
1. **Support in case of loss:** Swapna had no backup support; debt compounded over years, pushing her further into poverty.

Conclusion: As the text states, "whether credit would be useful or not depends on the risks in the situation and whether there is some support, in case of loss."

Source: Chapter 3, Money and Credit — Two Different Credit Situations

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Explanation

Examiners look for: (1) a clear contrast between Salim and Swapna, (2) identification of key determining factors — risk, purpose, outcome, support — with evidence from both examples, and (3) the textbook conclusion quoted or paraphrased. Avoid writing a narrative retelling; instead, analytically link each factor to the outcome. Using subheadings or numbered points keeps the answer structured and scores well.

Q21. medium thorough-understanding § TERMS OF CREDIT **[3]**

A borrower takes a loan from a bank using his house as collateral. He later fails to repay the loan. Explain how collateral protects the lender's interest both before and after the borrower defaults.

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Model Answer

Collateral is an asset (such as land, building, or house) that a borrower pledges as a guarantee to the lender until the loan is repaid.

Before default: The collateral acts as a security guarantee, ensuring the borrower is committed to repayment. The lender retains the documents of the collateral (e.g., house papers), which are returned only after full repayment.

After default: If the borrower fails to repay, the lender has the right to sell the collateral to recover the loan amount, thus protecting the lender from financial loss.

Source: Chapter 3 – Money and Credit, Terms of Credit

Explanation

- The examiner looks for: (1) definition of collateral, (2) its role *before* default (security/commitment), and (3) its role *after* default (right to sell asset). Each point carries roughly 1 mark.
- Use the textbook phrase **"right to sell the asset"** — this is key CBSE language.
- The house-loan example (Megha) from the textbook is ideal to cite as it shows documents retained as collateral until full repayment.
- Do not confuse collateral with interest rate — they are separate terms of credit.

Q22. deep | thorough-understanding | § TERMS OF CREDIT **[3]**

Rama, an agricultural labourer, borrows from her landowner-employer at 5% per month to meet daily expenses. Arun, a medium farmer, borrows from a bank at 8.5% per annum for cultivation. Even though Arun's loan is larger in amount, why is Rama's credit arrangement far more burdensome for her? In your answer, refer to the terms of credit that make the two arrangements different.

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Model Answer

Rama's credit arrangement is far more burdensome due to the following differences in **terms of credit**:

1. **Interest Rate:** Rama pays 5% per month (60% per annum) to her landowner-employer, whereas Arun pays only 8.5% per annum to the bank — nearly seven times cheaper.
1. **Mode of Repayment:** Rama repays by working for the landowner, which ties her labour to him. Arun can repay anytime within three years after harvest.
1. **Debt Trap:** Rama must often take a fresh loan before repaying the old one, causing her debt to keep rising. Arun has a flexible repayment schedule.
1. **No Collateral/Formal Support:** Rama has no assets to access formal credit; she is entirely dependent on her employer, who exploits this dependence.

Thus, high interest and exploitative conditions make Rama's informal credit far more burdensome than Arun's formal bank loan.

Source: Chapter 3 (Money and Credit), "Example of a Village" and "Formal Sector Credit in India"

Explanation

- Examiners look for **direct comparison** using the term "terms of credit" — interest rate, collateral, repayment conditions, and mode of repayment.
- Always **quantify** the interest rate difference (5%/month vs 8.5%/year) — this is a striking contrast and earns marks.
- Mention the **debt trap** concept explicitly; it directly appears in the chapter.
- Keep the answer point-based for clarity — easier to score full marks this way in a 3-mark question.

Q23. medium | thorough-understanding | § Variety of Credit Arrangements **[3]**

Shyamal, a small farmer, borrows from an agricultural trader instead of the village moneylender. Even though the trader's interest rate is lower, the arrangement still disadvantages Shyamal. Explain how.

◆ **Money and Credit**

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Model Answer

Although the trader charges a lower interest rate (3% per month) than the moneylender (5% per month), the trader imposes an unfair condition: Shyamal must sell his crop only to the trader. Since crop prices are low right after harvest, the trader buys the crop cheaply from Shyamal and sells it later at a higher price, making an extra profit. Thus, Shyamal loses income through this forced sale, and the overall arrangement still works against his financial interest.

Source: Chapter 3 — Money and Credit, "Variety of Credit Arrangements"

Explanation

Examiners want two clear points: (1) the tied condition — Shyamal must sell his crop to the trader, and (2) how the trader profits from low post-harvest prices at Shyamal's expense. Simply stating the interest rates are lower is **not enough** for full marks — you must explain the mechanism of disadvantage. Use the passage details (3% vs 5%, forced crop sale, low harvest prices) directly.

Q24. medium | thorough-understanding | § Variety of Credit Arrangements **[3]**

Rama, a landless agricultural labourer, borrows from her employer-landowner at 5% per month to meet household needs. Despite repaying regularly, she finds her total outstanding debt growing each season. Identify the feature of this credit arrangement that makes it exploitative, and explain how it traps the borrower over time.

◆ **Money and Credit**

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Model Answer

The exploitative feature is the **very high interest rate of 5% per month (60% per annum)** charged by the landowner-employer, who is also Rama's only source of credit.

This traps Rama because: her irregular income as an agricultural labourer is insufficient to clear both principal and interest. She must take fresh loans before repaying old ones, so outstanding debt keeps compounding each season. Additionally, her dependence on the landowner for both livelihood and credit gives her no alternative, forcing her to continue working for him on his terms — a classic **debt-trap**.

Source: Chapter 3, Variety of Credit Arrangements — Rama's case

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Explanation

- **1 mark** — identifying the exploitative feature (5% per month = 60% p.a., informal/unregulated lender who is also the employer).
- **2 marks** — explaining the debt-trap mechanism: compounding debt due to fresh loans before old ones are cleared, no collateral/alternative source, dependence locks her in.
- Examiners expect you to name the feature precisely and then show the *process* by which debt grows — don't just say "high interest"; explain *why* it keeps growing season after season.
- The term **debt-trap** should appear in your answer.

Q25. medium thorough-understanding § Variety of Credit Arrangements **[3]**

Arun owns seven acres of land and borrows from a nationalised bank at 8.5% per annum for cultivation. Shyamal owns 1.5 acres and borrows from a trader at 3% per month. What explains the stark difference in the cost of credit available to these two farmers? What does this reveal about the role of collateral in accessing formal credit?

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Model Answer

Arun, owning 7 acres of land, can offer it as **collateral** to the nationalised bank, which is why he gets credit at a low 8.5% per annum. Shyamal, with only 1.5 acres, cannot provide adequate collateral to a formal bank, so he must borrow from an agricultural trader at a much higher 3% per month (36% per annum).

This reveals that **collateral is a key condition for accessing formal credit**. Borrowers who lack sufficient assets cannot approach banks and are forced into informal sources that charge exploitative interest rates, creating an unequal credit system where the poor pay more for loans.

Source: Chapter 3 – Money and Credit, "Example of a Village" and "Terms of Credit"

Explanation

- Examiners expect you to directly connect land ownership → collateral → formal/informal credit distinction.
- Name both interest rates (8.5% p.a. vs 3% per month) for full marks — the contrast is the evidence.
- The second paragraph must link collateral to inequality in credit access; this is the conceptual point the 3-mark question tests.
- Do not just describe the two farmers separately — the question asks you to *explain* the difference and *reveal* what it shows.

Q26. medium | thorough-understanding | § Variety of Credit Arrangements **[1]**

An agricultural trader in a village supplies farm inputs on credit at the start of the season and insists that farmers sell their harvested crop exclusively to him. Which of the following best explains why the trader imposes this condition?
(A) To help farmers get a better price for their crops in the market.
(B) To ensure timely repayment and earn additional profit from buying crops at low post-harvest prices.
(C) To prevent farmers from borrowing from the village moneylender.
(D) To comply with rules set by the Reserve Bank of India.

A To help farmers get a better price for their crops in the market.
B To ensure timely repayment and earn additional profit from buying crops at low post-harvest prices.
C To prevent farmers from borrowing from the village moneylender.
D To comply with rules set by the Reserve Bank of India.

◆ Money and Credit

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Model Answer

(B) To ensure timely repayment and earn additional profit from buying crops at low post-harvest prices.

Explanation

The passage on Sonpur directly states: "the trader makes the farmers promise to sell the crop to him...to ensure that the money is repaid promptly. Also, since the crop prices are low after the harvest, the trader is able to make a profit from buying the crop at a low price." This makes (B) the only textbook-supported answer. Options A, C, and D are not supported by the passage.

Q27. medium | thorough-understanding | § Variety of Credit Arrangements **[3]**

How does a cooperative society like Krishak Cooperative manage to offer cheaper credit to its members, even though it lends mainly to small farmers who may lack individual collateral?

◆ **Money and Credit**

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Model Answer

Krishak Cooperative manages to offer cheaper credit through a collective collateral mechanism:

1. **Pooling of deposits:** The cooperative's 2,300 farmer members deposit their savings with it, creating a common fund.
2. **Collective collateral:** These pooled deposits are used as collateral to obtain a large loan from a bank at low (formal sector) interest rates.
3. **On-lending to members:** The funds received are then lent to individual members, who may lack personal collateral, at rates far lower than moneylenders or traders charge.

Since the cooperative borrows from the formal sector (bank), its cost of funds is low, and this benefit is passed on to members.

Source: Chapter 3, "Loans from Cooperatives"

Explanation

- The key concept examiners look for is **collective/pooled deposits acting as collateral** — this is what allows members who individually have no collateral to still access formal-rate credit.
- Mention all three steps: members pool savings → cooperative uses deposits as collateral to get bank loan → lends to members cheaply.
- Don't confuse this with SHGs; Krishak is specifically a cooperative society borrowing from a bank using member deposits as collateral.
- 3 marks = 3 clear points. Structure as a brief list or short paragraph with distinct points.

Q28. deep | thorough-understanding | § Variety of Credit Arrangements **[2]**

After the potato harvest, a farmer considers two options: selling the crop immediately at low post-harvest prices, or storing it in a cold storage facility and using the warehouse receipt as collateral to obtain a fresh bank loan. Explain the financial reasoning behind choosing the second option and what it reveals about the relationship between credit access and farmers' bargaining power.

◆ **Money and Credit**

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Model Answer

By storing potatoes and using the cold storage receipt as collateral, Arun can obtain a fresh bank loan at a low interest rate (8.5% p.a.) instead of selling at low post-harvest prices. This allows him to wait for prices to rise before selling, maximizing income. Access to formal credit thus gives farmers bargaining power to avoid distress selling.

Source: Chapter 3, Example of a Village

Explanation

The examiner wants two linked ideas: (1) the financial benefit — avoiding low post-harvest prices by deferring sale, funded by the bank loan; and (2) the connection to bargaining power — formal credit frees the farmer from being forced to sell immediately. Contrast with Shyamal, who borrows from a trader and is forced to sell at harvest time at low prices. Keep both points clear and concise.

Q29. deep | thorough-understanding | § Variety of Credit Arrangements **[5]**

In Sonpur, different groups of people — a small farmer, a medium farmer with bank access, and a landless labourer — each face very different terms of credit. What does this pattern reveal about the relationship between a person's economic position and the cost of credit they can access? What are the broader consequences of this inequality for rural development?

◆ **Money and Credit**

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Model Answer

In Sonpur, the terms of credit differ sharply based on economic position:

- **Arun** (medium farmer, 7 acres) gets a **bank loan at 8.5% per annum** — the cheapest credit — because he can offer collateral.
- **Shyamal** (small farmer, 1.5 acres) borrows from a trader at **3% per month (36% p.a.)** and is forced to sell his crop to the trader at low prices, reducing his income further.
- **Rama** (landless labourer) pays **5% per month (60% p.a.)** to her employer and must repay through labour, trapping her in a cycle of debt.

This reveals that **wealthier individuals with collateral access cheap formal credit, while the poor depend on costly informal sources**. The poor end up spending a large share of earnings on interest repayment, leaving little for savings or investment.

Consequences for rural development: High-cost credit reduces income, creates debt traps, and discourages enterprise. Rural development is hampered as the poor cannot invest in productivity or break the poverty cycle. Expanding formal credit — through banks and cooperatives — is essential for inclusive growth.

Source: Chapter 3 — Money and Credit, "Variety of Credit Arrangements" and "Formal Sector Credit in India"

Explanation

- The examiner expects **three-way comparison** (small farmer, medium farmer, landless labourer) with specific interest rates from the text — these are key scoring points.
- Always link the pattern to the concept: **lack of collateral → no bank loan → dependence on informal credit → high cost**.
- The "broader consequences" part should mention **debt trap, reduced income, hindrance to development**, and the **need to expand formal credit** — all directly from the Summing Up section.
- Do not write a general essay; keep it structured with a clear cause → effect flow.

Q30. medium | thorough-understanding | § FORMAL SECTOR CREDIT IN INDIA **[1]**

[mcq] The Reserve Bank of India issues guidelines on interest rates and lending practices to commercial banks but does not exercise similar control over moneylenders or chit funds. Which of the following BEST explains why this difference in regulation exists?
(A) Moneylenders operate outside village boundaries and are therefore beyond the RBI's jurisdiction.
(B) Informal lenders are too numerous and dispersed, and their transactions are largely unrecorded, making systematic supervision impractical.
(C) Informal lenders charge lower interest rates than banks, so regulation is unnecessary.
(D) The RBI only regulates institutions that accept deposits from the public.

A Informal lenders do not charge interest, so supervision is unnecessary.
B Formal lenders are registered institutions accountable under law, whereas informal lenders operate outside any regulatory framework.
C The RBI only supervises banks in urban areas, leaving rural lenders unregulated.
D Informal lenders lend smaller amounts, making supervision impractical.

◆ **Money and Credit**

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Model Answer

(B) Formal lenders are registered institutions accountable under law, whereas informal lenders operate outside any regulatory framework.

Explanation

The textbook states clearly: "The Reserve Bank of India supervises the functioning of formal sources of loans" and "There is no organisation which supervises the credit activities of lenders in the informal sector." The key distinction is that formal lenders (banks, cooperatives) are registered and legally accountable, making RBI supervision possible, while informal lenders operate outside any regulatory framework. Option B best reflects this from the given options.

Q31. medium | thorough-understanding | § FORMAL SECTOR CREDIT IN INDIA **[3]**

[short_answer] The Reserve Bank of India does not merely allow banks to operate freely in search of profit — it imposes specific obligations on them. What are TWO such obligations, and why does the RBI consider it necessary to impose these restrictions on commercial banks?

◆ Money and Credit

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Model Answer

The RBI imposes two key obligations on commercial banks:

1. **Maintaining minimum cash balance** – Banks must keep a minimum proportion of their deposits as cash (about 15%) to repay depositors on demand. The RBI monitors whether banks actually maintain this balance.
1. **Lending to priority sectors** – Banks must give loans not just to profit-making businesses but also to small cultivators, small-scale industries, and small borrowers. Banks must periodically report to the RBI about how much they lend, to whom, and at what interest rate.

Why necessary: The RBI supervises banks to protect depositors' money, ensure fair distribution of credit, and prevent banks from lending only to the rich and profitable — which would exclude the poor from formal credit.

Source: Chapter 3, Money and Credit — Formal Sector Credit in India

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Explanation

The examiner is looking for:

- **Two specific obligations** (cash balance + priority sector lending) — name both clearly.
- **Why RBI supervision is necessary** — link it to protecting depositors and ensuring equitable credit access.
- The passage explicitly states both obligations, so quote or closely paraphrase it; don't invent obligations.
- Note: The textbook says banks hold "about 15%" as cash reserve (the passage says 5% as *cash with themselves* but the reserve requirement referred to in supervision context is higher). Stick to what the passage says if unsure — the key point is "minimum cash balance" is monitored by RBI.

Q32. deep | thorough-understanding | § FORMAL SECTOR CREDIT IN INDIA **[3]**

In rural India, commercial banks account for the largest share of credit, yet the poor still rely heavily on moneylenders. Using data on formal and informal credit distribution, explain this apparent contradiction.

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Model Answer

Although commercial banks account for **51%** of rural credit (Graph 1), the poor still depend on moneylenders (23%) because:

1. **Banks are not present everywhere** in rural India.
2. Banks require **proper documents and collateral**, which the poor lack.
3. Moneylenders know borrowers personally and give loans **without collateral**, quickly and easily.

Thus, formal credit is cornered by richer households (83% formal loans), while poor households rely heavily on informal sources — despite banks having the largest overall share.

Source: Formal Sector Credit in India; Self-Help Groups for the Poor, Chapter 3

Explanation

Examiners look for: (1) the data point from Graph 1 showing commercial banks at 51%, (2) the barrier of collateral/documents as the key reason poor are excluded, and (3) the contrast — moneylenders' accessibility vs. banks' inaccessibility. Don't just say "banks are better"; explain *why poor people can't access them* despite banks dominating overall figures. Mentioning the rich-poor divide in formal credit access earns the third mark.

Q33. medium | thorough-understanding | § FORMAL SECTOR CREDIT IN INDIA **[3]**

How does a high interest rate charged by an informal lender create a cycle that can make a borrower permanently worse off, rather than simply costing more money in the short term?

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Model Answer

When an informal lender charges a very high interest rate (e.g., 5% per month = 60% per annum), a large part of the borrower's earnings goes toward repaying interest, leaving little income for daily needs. To meet these expenses, the borrower must take **fresh loans before the previous one is repaid**. This creates a **debt trap** — the amount owed keeps growing beyond the borrower's income. As seen in Rama's case, the borrower becomes permanently tied to the lender, losing bargaining power and independence, making their situation **worse off than before borrowing**.

Source: Chapter 3 — Money and Credit, "Variety of Credit Arrangements" and "Formal Sector Credit in India"

Explanation

- Examiners expect **three clear points** for 3 marks: (1) high interest → less income left, (2) need for fresh loans → rising debt, (3) debt trap / permanent worsening.
- Use the **textbook examples** (Rama, Shyamal) to show you've read the chapter — this scores well.
- The key phrase examiners look for is **"debt trap"** — always use it.
- Do not write vaguely; state *why* it is worse off, not just *that* it is.

Q34. deep | thorough-understanding | § FORMAL SECTOR CREDIT IN INDIA **[5]**

Rich urban households obtain 83% of their loans from formal sources, while poor urban households obtain 54% of their loans from informal sources. What structural barriers prevent the poor from accessing formal credit, and what does this unequal distribution mean for economic inequality?

◆ **Money and Credit**

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Model Answer

Structural Barriers Preventing the Poor from Accessing Formal Credit:

1. **Lack of collateral** – Banks require assets as security. Poor households typically own little or no property, making them ineligible for bank loans.
2. **Absence of proper documents** – Banks demand income proof, identity documents, etc., which many poor borrowers cannot provide.
3. **Limited bank presence** – Banks are not present everywhere, especially in rural areas, making access physically difficult.
4. **Strict repayment terms** – Formal loans have fixed schedules that may not suit irregular incomes of the poor.

Impact on Economic Inequality:

Because the poor are forced to borrow from informal sources (moneylenders, traders), they pay much higher interest rates. This means a larger share of their income goes toward repayment, leaving less for consumption or investment. In contrast, rich households access cheap formal credit, invest it productively, and grow wealthier. This cycle deepens economic inequality. Expanding formal credit to the poor is therefore essential for development.

Source: Chapter 3 — Money and Credit, "Formal Sector Credit in India" and "Self-Help Groups for the Poor"

Explanation

- Examiners expect **two clear parts**: barriers + implications for inequality. Label or separate them clearly.
- Key terms to use: **collateral, documents, informal sources, debt trap, high interest rate**.
- The statistic (83% vs. 54%) in the question is from Graph 2 — use it to set up your answer but don't over-explain it.
- Avoid padding; each point should add new information. Five crisp points across both parts score full marks.

Q35. medium thorough-understanding § FORMAL SECTOR CREDIT IN INDIA **[1]**

[very_short_answer] Unlike commercial banks, informal lenders such as moneylenders are not supervised by any regulatory authority. Identify ONE specific reason why bringing informal lenders under formal regulation is structurally difficult for the government.

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Model Answer

Informal lenders like moneylenders operate in scattered, unorganised settings, keep no records of transactions, and are too numerous and dispersed for any regulatory body to effectively monitor or supervise.

Explanation

The source passage directly states that informal lenders "keep no records of transactions." Examiners expect you to link the structural difficulty to this lack of documentation/records and their dispersed, unorganised nature — not just say "there is no RBI for them" (that's the effect, not the structural reason). One precise reason is enough for 1 mark.

Q36. medium thorough-understanding § SELF-HELP GROUPS FOR THE POOR **[3]**

A rural woman belonging to a Self Help Group wants to take a small loan. She has no collateral to offer. Why would the SHG still be willing to lend her money, even though a bank in the same situation typically would not?

◆ Money and Credit

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Model Answer

A bank requires collateral as security against a loan, and since the rural woman has none, the bank refuses to lend her.

An SHG lends to her because:

- The **group itself acts as collateral**. The loan is sanctioned in the group's name, and all members are collectively responsible for repayment.
- If any member fails to repay, **other members follow it up seriously**, ensuring recovery without needing physical assets as security.
- Members know each other personally, and **social pressure within the group** ensures timely repayment.

Thus, the group's collective guarantee replaces the need for collateral, making it safe for the SHG to lend.

Source: Money and Credit, Chapter 3 — Self Help Groups for the Poor

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Explanation

Examiners look for three key ideas here: (1) why banks refuse — no collateral; (2) the SHG mechanism — group liability/collective responsibility replaces collateral; (3) peer pressure/social monitoring ensures repayment. Avoid vague phrases like "they trust her" — be specific about **group responsibility** and **peer monitoring**, which are the textbook reasons. These are the exact points NCERT highlights.

Q37. medium | thorough-understanding | § SELF-HELP GROUPS FOR THE POOR **[1]**

Which of the following best explains why banks are willing to give loans to Self Help Groups even though the individual members have no collateral?
(A) The government guarantees repayment of all SHG loans.
(B) The group collectively takes responsibility for repayment, so peer pressure among members ensures defaults are followed up seriously.
(C) SHG members always deposit large savings with the bank before receiving a loan.
(D) RBI directs banks to give loans to SHGs without any conditions.

A The government guarantees repayment of all SHG loans.
B The group collectively takes responsibility for repayment, so peer pressure among members ensures defaults are followed up seriously.
C SHG members always deposit large savings with the bank before receiving a loan.
D RBI directs banks to give loans to SHGs without any conditions.

◆ Money and Credit

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Model Answer

(B) The group collectively takes responsibility for repayment, so peer pressure among members ensures defaults are followed up seriously.

Explanation

The passage directly states: "It is the group which is responsible for the repayment of the loan. Any case of non-repayment by any one member is followed up seriously by other members." This collective responsibility replaces the need for collateral. Options A and D are factually incorrect; Option C is not stated in the text.

Q38. deep | thorough-understanding | § SELF-HELP GROUPS FOR THE POOR **[5]**

Rama, an agricultural labourer, remains trapped in debt with her landowner-employer despite working for him year after year. How could joining a Self Help Group change her situation? In your answer, address both the financial and non-financial benefits she could gain.

◆ Money and Credit

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Model Answer

Rama is currently trapped in a debt cycle — borrowing from her landowner at 5% per month (60% per annum) and repaying through labour, which keeps her bound to him indefinitely.

Financial Benefits of joining an SHG:

- She can save small amounts (₹25–₹100/month) and borrow from the group at a lower interest rate than the landowner charges.
- After regular savings for a year or two, the SHG becomes eligible for a bank loan — **without collateral** — which Rama cannot provide on her own.
- She could use loans to meet daily expenses, health emergencies, or even acquire productive assets (e.g., cattle, sewing machine), creating self-employment and reducing dependence on her employer.

Non-Financial Benefits:

- Regular group meetings provide a platform to discuss social issues such as health, nutrition, and domestic violence.
- SHGs make women **financially self-reliant** and build collective bargaining power, freeing Rama from the exploitative relationship with her landowner-employer.

Source: Money and Credit, Self-Help Groups for the Poor

Explanation

- Examiners expect you to **link Rama's specific situation** (high interest, labour bondage, no collateral) to SHG features — don't write generically.
- Split your answer clearly into **financial** and **non-financial** as the question demands; losing this structure loses marks.
- Key textbook facts to include: 15–20 members, savings pooled, loans without collateral, bank linkage after one year, social platform for health/nutrition/domestic violence.
- Avoid padding — 5 marks = ~5 distinct, specific points.

Q39. medium | thorough-understanding | § SELF-HELP GROUPS FOR THE POOR **[3]**

A newly formed SHG applies to a bank for a loan but is rejected. A bank manager explains that the group needs to demonstrate certain creditworthiness before a loan can be sanctioned. What would the bank look for in the group's track record, and how does this criterion protect both the bank and the group's members?

◆ Money and Credit

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Model Answer

The bank would examine whether the SHG has been **regular in savings** over a period of one to two years, as this demonstrates financial discipline and trustworthiness among members.

For the bank: A consistent savings track record shows the group can manage money responsibly, reducing the risk of loan default. Since the loan is sanctioned in the group's name, collective responsibility ensures repayment.

For the members: Group accountability means peer pressure prevents any single member from defaulting, protecting everyone's creditworthiness and access to future loans at reasonable interest rates.

Source: Chapter 3 — Money and Credit, Self-Help Groups for the Poor

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Explanation

Examiners expect you to identify the specific criterion (regular savings for 1–2 years) from the textbook and then explain the **dual protection** aspect — one point for the bank (reduced default risk) and one for the members (collective responsibility/peer monitoring). Avoid vague answers like "good financial history"; be specific about savings regularity and group-based repayment as stated in the passage.

Q40. deep | thorough-understanding | § SELF-HELP GROUPS FOR THE POOR **[2]**

The interest rate charged by an SHG on loans to its members is lower than that of a moneylender but higher than zero. Why do you think the SHG charges any interest at all, rather than lending completely interest-free to its own members?

◆ Money and Credit

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Model Answer

The SHG charges interest because it pools members' savings and also borrows from banks — both of which involve costs. The interest collected helps the group repay its bank loan and meet administrative expenses. It also builds a common fund for future lending. Though lower than moneylenders' rates, it ensures the group remains financially self-sustaining.

Source: Chapter 3, Self-Help Groups for the Poor

Explanation

The passage states that the SHG charges interest on loans to members, which is less than what a moneylender charges. Examiners expect you to explain the **reason** interest is charged at all — focus on two points: (1) the group itself borrows from banks and must repay with interest, and (2) interest income keeps the group financially viable. Avoid saying SHGs are profit-driven — they are not; sustainability is the key word here.

Q41. medium | thorough-understanding | § SUMMING UP **[3]**

Credit can either lift a borrower out of poverty or push them deeper into a debt trap. Using one concrete example for each outcome, explain what determines whether credit helps or harms a borrower.

◆ **Money and Credit**

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Model Answer

Credit helping a borrower: Salim, a shoe manufacturer, took a loan to buy raw materials and complete an order. He delivered the goods, earned profit, and repaid the loan. Here, the risk was low and the income from the activity was enough to repay — so credit increased his earnings.

Credit harming a borrower: Swapna, a small farmer, borrowed from a moneylender for crop cultivation. A pest attack destroyed her harvest, making repayment impossible. Debt accumulated, and she had to sell part of her land — a classic debt trap.

What determines the outcome: Credit helps when risks are manageable and returns are sufficient to repay. It harms when risks are high (crop failure, no collateral, high interest) and there is no support in case of loss.

Source: Chapter 3 — Two Different Credit Situations

Explanation

- The examiner expects **two named examples** (Salim and Swapna are textbook examples — use them).
- The key determinant phrase from the textbook is: *"Whether credit would be useful or not depends on the risks in the situation and whether there is some support in case of loss."* Include this idea explicitly.
- Avoid writing only about one side; balance is essential for full marks.
- 3 marks = roughly one example each + one line on the determining factor.

Q42. medium | thorough-understanding | § ADDITIONAL PROJECT / ACTIVITY **[3]**

A government employee with a steady salary and a migrant labourer in the city both need loans. Why is the government employee far more likely to receive a bank loan than the migrant labourer, even if both need the same amount? What does this difference reveal about who benefits from formal credit in India?

◆ **Money and Credit**

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Model Answer

Banks require **collateral** (an asset as security) and proof of steady income before granting loans. A government employee has a fixed salary, a stable job, and can offer assets as collateral, making repayment certain in the bank's view. A migrant labourer has irregular income, no fixed address, and no collateral to offer, so banks consider them too risky to lend to.

This difference reveals that **formal credit in India largely benefits the rich and well-off**, while the poor are pushed toward informal moneylenders who charge very high interest rates, increasing debt burden and the risk of a debt trap.

Source: Chapter 3 — Formal and Informal Credit: Who gets what?

Explanation

- The key concept here is **terms of credit**: collateral, income stability, and documentation. Banks need assurance of repayment.
- The examiner wants you to link the individual example to the **larger pattern**: richer households access formal credit; poorer households are forced into expensive informal credit.
- Mentioning **collateral** explicitly earns a mark. Mentioning the **consequence** (debt trap / high-cost borrowing) earns another. The third mark is for identifying the inequality in formal credit distribution.
- Avoid vague phrases like "banks don't trust poor people" — use precise terms: *collateral, irregular income, formal sector, informal sector*.

Q43. medium | thorough-understanding | § (whole-chapter synthesis) **[3]**

Money is described as a medium of exchange. Explain how the modern banking system allows money to fulfil this role even without any physical currency changing hands. Use appropriate examples in your answer.

◆ **Money and Credit**

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Model Answer

Money acts as a **medium of exchange** by eliminating the need for double coincidence of wants. The modern banking system extends this role through **demand deposits and cheques**, allowing payments without physical cash.

Example: Shoe manufacturer M. Salim pays his leather supplier by writing a cheque. The leather supplier deposits it in his own bank account. The bank transfers the amount from Salim's account to the supplier's account within days — no cash changes hands.

Thus, demand deposits share the essential features of money. Since they are widely accepted as a means of payment, they constitute money in the modern economy.

Source: Money and Credit, Chapter 3 — Deposits with Banks / Cheque Payments

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Explanation

- Examiners expect: definition of medium of exchange → problem it solves (double coincidence) → how demand deposits + cheques replicate this function → example from the textbook (Salim's cheque payment).
- The Salim–leather supplier example is **directly from the textbook** — use it; don't invent a new one.
- Key term to include: **demand deposits**, **cheque**, **transfer between accounts**.
- Do not describe how banks lend money — that is a separate concept and wastes words here.

Q44. deep | thorough-understanding | § (whole-chapter synthesis) **[3]**

Banks keep only a small proportion of their total deposits as cash reserves and lend out the rest. Explain how this practice makes credit possible in the economy, and what risk it creates for depositors and the banking system.

◆ Money and Credit

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Model Answer

Banks accept deposits from the public but keep only a small proportion (about 5%) as cash reserves to meet daily withdrawal demands. The remaining major portion is lent out to borrowers. This way, banks mediate between depositors (surplus funds) and borrowers (need funds), making credit available for various economic activities.

Risk created: Since banks do not hold all deposits as cash, if all depositors demand their money simultaneously, the bank cannot repay everyone. This could cause the banking system to collapse, harming both depositors and the economy.

Source: Chapter 3 – Money and Credit, 'Loan Activities of Banks'

Explanation

- The examiner expects two parts: (1) how lending of deposits makes credit possible, and (2) the risk this creates.
- Quote the key fact: banks hold ~5% as cash reserve in India.
- The textbook's own question — *"What would happen if all depositors asked for money at the same time?"* — is the direct hint for the risk part. Always use it.
- Avoid over-explaining; 3 marks = roughly 3 distinct points stated clearly.

Q45. medium | thorough-understanding | § (whole-chapter synthesis) **[1]**

Salim the shoe manufacturer and Swapna the groundnut farmer both take credit to meet their production needs, yet credit helps one and harms the other. What single underlying factor best explains this difference in outcome?

◆ Money and Credit

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Model Answer

The single underlying factor is **risk in the situation**. Salim's credit was backed by a confirmed order (guaranteed income), so repayment was certain. Swapna's crop failed, making repayment impossible and pushing her into a debt-trap.

Explanation

The textbook explicitly states: *"Whether credit would be useful or not depends on the risks in the situation and whether there is some support in case of loss."* For 1 mark, name the factor (risk/uncertainty of income) and briefly contrast the two cases. Avoid writing more than one–two lines.

Source: Chapter 3, Two Different Credit Situations

Q46. deep thorough-understanding § (whole-chapter synthesis) **[3]**

Collateral is a key term in formal credit arrangements. How does the requirement of collateral simultaneously explain (i) why richer households access formal credit more easily, and (ii) why the poor are pushed towards informal lenders who charge much higher interest rates?

◆ **Money and Credit**

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Model Answer

Collateral is an asset (like land, building, or bank deposits) that a borrower uses as a guarantee against a loan.

(i) Richer households own valuable assets such as land and property, which they can offer as collateral. Banks are therefore willing to lend to them at low interest rates through formal channels.

(ii) Poor households lack such assets, so they cannot meet the collateral requirement of banks. As a result, they are forced to approach informal lenders like moneylenders, who lend without collateral but charge very high interest rates, increasing the debt burden on the poor.

Source: Chapter 3 — Terms of Credit; Self-Help Groups for the Poor; Formal and Informal Credit: Who Gets What

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Explanation

- The examiner expects you to **define collateral** briefly, then address **both parts** clearly — this is a two-part logical explanation.
- The key causal chain is: **no collateral → no formal loan → forced to informal lenders → higher interest rates**. State this chain explicitly.
- Back up with textbook evidence: "Absence of collateral is one of the major reasons which prevents the poor from getting bank loans" — this direct textbook line shows you've read the source carefully.
- Don't just list facts; show the *link* between collateral and access to credit type.

Q47. medium | thorough-understanding | § (whole-chapter synthesis) **[1]**

Which of the following best explains why cheap and affordable credit is described as crucial for a country's development?
(A) It increases the government's tax revenue by encouraging more commercial activity among large corporations.
(B) It allows borrowers — including small farmers, traders and entrepreneurs — to invest, raise incomes and repay loans without falling into debt traps.
(C) It reduces the need for collateral, making banks more profitable and financially secure.
(D) It enables the Reserve Bank of India to print less currency, keeping inflation under control.

A It increases the profits of banks, allowing them to pay higher interest to depositors.
B It allows borrowers — including small farmers, traders and entrepreneurs — to invest, raise incomes and repay without falling into debt traps.
C It reduces the need for the Reserve Bank of India to supervise informal lenders.
D It eliminates the double coincidence of wants problem that exists in a barter economy.

◆ Money and Credit

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Model Answer

(B) It allows borrowers — including small farmers, traders and entrepreneurs — to invest, raise incomes and repay without falling into debt traps.

Explanation

The textbook explicitly states: "Cheap and affordable credit is crucial for the country's development" because it enables small cultivators, traders, and entrepreneurs to borrow at low cost, invest productively, earn higher incomes, and repay loans — avoiding the debt trap caused by high-interest informal credit. Option B directly reflects this reasoning. The other options are either incorrect or not supported by the chapter.

Q48. deep thorough-understanding § (whole-chapter synthesis) **[3]**

The Reserve Bank of India supervises formal lenders, but no such body oversees informal lenders. Explain how this difference in supervision directly affects (i) the cost of borrowing for the poor and (ii) their vulnerability to a debt trap.

◆ **Money and Credit**

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Model Answer

The RBI regulates formal lenders by monitoring interest rates, ensuring loans reach small borrowers, and requiring periodic reporting. No such body oversees informal lenders like moneylenders, who can charge any interest rate and use unfair means to recover money.

(i) Cost of borrowing: Without supervision, informal lenders charge very high interest rates. The poor, who mostly depend on informal credit, thus pay a much higher cost of borrowing compared to richer households who access cheap formal credit.

(ii) Vulnerability to debt trap: High interest means a larger part of the borrower's income goes towards repayment. In some cases, the amount to be repaid exceeds the borrower's income, leading to ever-increasing debt and a debt trap.

Source: Money and Credit, Formal Sector Credit in India

Explanation

- The question directly maps to the RBI supervision passage — quote or paraphrase its key lines.
- Two parts (i) and (ii) must be answered separately; examiners award marks for each.
- "Debt trap" must be explicitly named and briefly explained (repayment > income → growing debt).
- Avoid padding; 3 marks = roughly 3 distinct, pointed statements.

Q49. medium | thorough-understanding | § (whole-chapter synthesis) **[3]**

The poor in rural areas often find it difficult to access formal credit. Explain how Self Help Groups address the barriers that prevent the poor from borrowing from formal financial institutions.

◆ Money and Credit

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Model Answer

Formal banks require **proper documents and collateral**, which poor rural borrowers usually lack. SHGs address this in the following ways:

1. **Collateral problem solved:** The group itself acts as a guarantee. Since all members are collectively responsible for repayment, banks are willing to lend even without individual collateral.
2. **Access to credit:** After regular savings for 1-2 years, the group becomes eligible for a bank loan sanctioned in the group's name.
3. **Lower interest rates:** Members can borrow from the group's pooled savings at rates lower than moneylenders.
4. **Peer monitoring:** Any default by a member is followed up seriously by others, ensuring repayment and building trust with banks.

Source: Chapter 3, Self-Help Groups for the Poor

Explanation

Examiners expect you to identify **the specific barriers** (no collateral, no documents, bank inaccessibility) and then explain **how SHGs overcome each one**. Three clear, labelled points earn full marks. Avoid vague statements like "SHGs help the poor" — always link the mechanism to the barrier it removes. The collective responsibility / peer pressure point is frequently tested and must be included.

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