CBSE CLASS X

Social Science (087)

ANSWER KEY

AI-generated question paper

Code: NCX4SV	Questions: 28	Maximum Marks: 62	Generated: 2026-06-26 09:46

SELECTIONS USED

Subject	Social Science
Lessons	3 Money and Credit
Level of understanding	Exam-ready
Question selection	CBSE board paper, whole lesson (~80 marks across Sections A-E)
Model	claude-sonnet-4-6

Composition — Difficulty: 7 straightforward · 15 medium · 6 deep | Types: 8 MCQ · 7 Short · 5 Assertion–reason · 3 Very short · 3 Case-based · 2 Long | Sections: A 13Q/13m · B 3Q/6m · C 7Q/21m · D 2Q/10m · E 3Q/12m

Q1. straightforward exam-ready **[1]**

Which of the following is the primary reason why modern currency is accepted as a medium of exchange even though it has no intrinsic value?

A It is made of durable material
B It is authorised by the government of the country
C It can be exchanged for gold at any time
D It is issued by commercial banks

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Model Answer

Answer: B — Modern currency is accepted as a medium of exchange because it is **authorised by the government of the country**.

Explanation

The textbook explicitly states: *"It is accepted as a medium of exchange because the currency is authorised by the government of the country."* Option C is incorrect — modern currency is not backed by gold. Option D is wrong — currency is issued by the RBI (central bank), not commercial banks.

Q2. straightforward exam-ready **[1]**

In a barter system, which condition is essential for an exchange of goods to take place?

A Presence of a bank as an intermediary
B Use of a common currency
C Double coincidence of wants
D A written agreement between parties

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Model Answer

Option C: Double coincidence of wants

In a barter system, both parties must agree to sell and buy each other's commodities. What one person desires to sell must be exactly what the other wishes to buy.

Explanation

The passage directly states: *"In a barter system where goods are directly exchanged without the use of money, double coincidence of wants is an essential feature."* There is no bank, currency, or written agreement involved in barter — these are features of a modern money economy. Examiners look for the exact term "double coincidence of wants."

Q3. straightforward exam-ready **[1]**

Which of the following is NOT an informal source of credit?

A Moneylenders
B Employers
C Cooperative societies
D Relatives and friends

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Model Answer

Answer: C — Cooperative societies

Cooperative societies are a formal source of credit, supervised like banks. Moneylenders, employers, and relatives/friends are all informal sources.

Source: Money and Credit, Formal Sector Credit in India

Explanation

The textbook explicitly states: *"Among the former (formal) are loans from banks and cooperatives. The informal lenders include moneylenders, traders, employers, relatives and friends."* Examiners expect you to identify cooperatives as formal, not informal. The key distinction is that formal sources are regulated by the RBI or similar bodies, while informal sources are not.

Q4. straightforward exam-ready **[1]**

[mcq] Salma wants to take a loan from a bank but the bank insists she provide 'collateral'. Which of the following would be accepted as collateral by the bank?

(A) Her educational certificates

(B) Her agricultural land with proper ownership documents

(C) Her monthly wages

(D) Her personal guarantee

A The interest rate charged on a loan
B An asset owned by the borrower used as a guarantee to the lender
C The amount of loan sanctioned by a bank
D A certificate issued by the RBI to banks

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Model Answer

(B) Her agricultural land with proper ownership documents

The correct definition of collateral is: **B** — An asset owned by the borrower used as a guarantee to the lender.

Explanation

- The textbook states collateral is "an asset that the borrower owns (such as land, building, vehicle, livestock, deposits with banks) and uses as a guarantee to a lender until the loan is repaid."
- Agricultural land with ownership documents qualifies as a tangible, verifiable asset — exactly what banks accept.
- Educational certificates, monthly wages, and personal guarantees are **not** tangible assets the bank can seize and sell if the borrower defaults, so they are not accepted as collateral.
- Always link collateral to the idea that the lender must be able to **sell** the asset to recover the loan if needed.

Q5. straightforward exam-ready **[1]**

[mcq] Ramesh needs to pay Rs 20,000 to his supplier but does not want to carry cash. He writes an instruction to his bank to transfer the amount from his account. Which instrument does Ramesh use for this purpose?

(A) Promissory note

(B) Cheque

(C) Barter token

(D) Credit card

A Currency notes
B Cheques drawn on demand deposits
C Coins issued by the government
D Loans from moneylenders

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Model Answer

(B) Cheque

Ramesh uses a **cheque** — a written instruction to his bank to transfer money from his account to the supplier, avoiding the need to carry cash.

Source: Money and Credit, Chapter 3

Explanation

- The question describes the classic definition of a cheque: a written order to the bank to pay a specified amount from the account holder's demand deposit.
- The options in the MCQ body (A–D) are the ones that matter; the four alternatives listed below the question belong to a different question and should be ignored.
- Remember: cheques are drawn on **demand deposits** held with banks — a key fact examiners test.

Q6. medium exam-ready **[1]**

Which of the following best describes a 'debt trap'?

- A A situation where the borrower invests the loan in a profitable business
- B A situation where the borrower's debt keeps growing and recovery becomes very painful
- C A government scheme to provide cheap loans to the poor
- D A type of collateral offered to the bank

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Model Answer

Answer: B

A debt trap is a situation where the borrower's debt keeps growing and recovery becomes very painful — as seen in Swapna's case where crop failure made repayment impossible, forcing her to sell land.

Source: Money and Credit, Chapter 3

Explanation

The textbook explicitly defines debt trap using Swapna's example: "Credit pushes the borrower into a situation from which recovery is very painful." Options A, C, and D describe unrelated concepts (profitable credit, government schemes, and collateral respectively). For MCQs, always link your answer to the textbook definition to confirm your choice.

Q7. medium exam-ready **[1]**

Why are banks willing to lend to poor women organised in Self Help Groups even when individual members have no collateral?

A The government provides a guarantee for each member's loan
B The group itself is responsible for repayment and monitors its members
C The RBI instructs banks to waive the collateral requirement for all rural loans
D SHG members deposit gold with the bank before taking a loan

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Model Answer

Answer: B

The group itself is responsible for repayment and monitors its members. Any non-repayment by one member is followed up seriously by other members, so the group acts as a social guarantee replacing collateral.

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

Explanation

The passage explicitly states: *"It is the group which is responsible for the repayment of the loan. Any case of non-repayment... is followed up seriously by other members. Because of this feature, banks are willing to lend to the poor women when organised in SHGs, even though they have no collateral."*

- **Option A** is wrong — no government guarantee is mentioned.
- **Option C** is wrong — RBI does not waive collateral for all rural loans.
- **Option D** is wrong — no gold deposit is mentioned anywhere.

The key concept: **group responsibility replaces collateral** — this is the examiner's expected point.

Q8. straightforward exam-ready **[1]**

[mcq] Banks do not keep all the money deposited with them as cash. Why do banks keep only a small proportion of their deposits as cash reserves?
(A) To pay salaries and operational expenses
(B) Because not all depositors withdraw their money at the same time, and the rest can be lent out
(C) Because the RBI allows banks to destroy excess currency
(D) To meet the collateral requirements of borrowers

A 25 per cent
B 15 per cent
C 5 per cent
D 50 per cent

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Model Answer

(B) Because not all depositors withdraw their money at the same time, and the rest can be lent out.

Banks in India keep about **5 per cent** of deposits as cash reserves (Option C).

Explanation

The question has a mismatch: the question body asks *why* (answered by option B), but the listed options A–D are percentages. The passage clearly states banks hold about **5 per cent** of deposits as cash. Mention both: the correct reason (B) and the correct percentage (5 per cent / Option C) to cover all parts of the question.

Q9. medium exam-ready **[1]**

Assertion (A): The rupee cannot be legally refused as a means of payment for settling transactions in India.
Reason (R): The Reserve Bank of India issues currency notes on behalf of the central government, and the law legalises the rupee as a medium of payment.

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

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Model Answer

Option A: Both A and R are true, and R is the correct explanation of A.

The law legalises the rupee as a medium of payment that cannot be refused, and RBI issues currency notes on behalf of the central government — thus R directly explains A.

Explanation

The passage explicitly states: "the law legalises the use of rupee as a medium of payment that cannot be refused in settling transactions in India" and "the Reserve Bank of India issues currency notes on behalf of the central government." Both statements are true, and the legal backing (R) is precisely why the rupee cannot be refused (A), making R the correct explanation of A.

Q10. medium exam-ready **[1]**

Assertion (A): Informal sector lenders often charge much higher interest rates than formal sector lenders.
Reason (R): The Reserve Bank of India supervises and regulates the loan activities of informal lenders.

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

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Model Answer

Answer: C

Assertion (A) is **true** — informal lenders charge much higher interest rates than formal lenders. Reason (R) is **false** — the RBI supervises only **formal** sector lenders (banks, cooperatives); there is no organisation that supervises informal lenders.

Explanation

The passage clearly states: *"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."* So R incorrectly claims RBI regulates informal lenders — making R false. Since R is false, the answer is **C**.

Q11. medium exam-ready **[1]**

Assertion (A): Demand deposits are considered a form of money in the modern economy.
Reason (R): Demand deposits can be withdrawn on demand and payments can be made through cheques, allowing them to function as a medium of exchange.

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

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Model Answer

Option A is correct. Both A and R are true, and R is the correct explanation of A. Demand deposits can be withdrawn on demand and payments made via cheques, making them a medium of exchange, hence a form of money.

Explanation

The textbook (Chapter 3 – *Deposits with Banks*) explicitly states: "Since deposits in bank accounts can be withdrawn on demand, these deposits are called demand deposits" and "the facility of cheques against demand deposits makes it possible to directly settle payments without the use of cash." This is precisely why demand deposits are considered money — the reason (cheque facility + withdrawal on demand = medium of exchange) directly explains the assertion. So A is the correct option.

Q12. deep exam-ready **[1]**

Assertion (A): Poor households in both rural and urban India depend more on informal sources of credit than rich households do.
Reason (R): Poor households often lack the collateral and documentation required to access formal sector loans from banks.

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

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Model Answer

Answer: A

Both A and R are true, and R is the correct explanation of A. Poor households lack collateral and proper documents required for bank loans, forcing them to depend on informal sources like moneylenders.

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

Explanation

- **A is true**: Graph 2 and the text confirm that 54% of urban poor households' loans come from informal sources vs. only 17% for rich households. A similar pattern exists in rural areas.
- **R is true**: The text explicitly states "Absence of collateral is one of the major reasons which prevents the poor from getting bank loans," and bank loans require "proper documents and collateral."
- **R correctly explains A**: The causal link is direct — because poor households lack collateral/documents (R), they cannot access formal credit and turn to informal sources (A). So option **A** is correct.

Q13. deep exam-ready **[1]**

Assertion (A): Higher cost of borrowing from informal lenders can lead to a debt trap for poor borrowers.
Reason (R): When the interest to be repaid exceeds the income of the borrower, the debt keeps rising and the borrower's situation worsens.

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

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Model Answer

Option A — Both A and R are true, and R is the correct explanation of A.

Informal lenders charge very high interest rates. When the amount to be repaid exceeds the borrower's income, debt keeps rising, directly causing a debt trap.

Source: *Money and Credit*, Formal Sector Credit in India

Explanation

- **A is true**: The textbook explicitly states that high informal borrowing costs can lead to a debt trap (e.g., Rama in Sonpur).
- **R is true and explains A**: R describes the exact *mechanism* — when repayment amount > income, debt increases continuously, which is precisely *why* high-cost borrowing causes a debt trap.
- So R is not just true but is the **direct causal explanation** of A → choose **Option A**, not B.
- Key phrase to remember: *"the amount to be repaid is greater than the income of the borrower → increasing debt → debt trap."*

Q14. straightforward exam-ready **[2]**

State any two components that together make up the 'terms of credit' in a loan agreement.

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Model Answer

Two components that make up the **terms of credit** are:

1. **Interest rate** — the rate the borrower must pay to the lender along with repayment of the principal.
2. **Collateral** — an asset pledged by the borrower as security/guarantee against the loan.

(Documentation requirement and mode of repayment are the other two components.)

Source: *Money and Credit*, Terms of Credit section, Chapter 3

Explanation

The textbook explicitly states: *"Interest rate, collateral and documentation requirement, and the mode of repayment together comprise what is called the terms of credit."* Any **two** of these four components earn full marks. Stating interest rate + collateral is the most straightforward pair to remember. Write the component name **and** a brief one-line definition — that secures both marks cleanly.

Q15. medium exam-ready **[2]**

Why is the absence of collateral a major obstacle for poor people in accessing bank loans?

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Model Answer

Collateral is an asset (such as land, building, or livestock) that a borrower provides as a guarantee for a loan. Poor people often do not own such assets. Since banks require collateral before sanctioning loans, the poor are unable to meet this condition and are denied access to formal bank credit.

Source: Terms of Credit, Chapter 3; Self-Help Groups for the Poor, Chapter 3

Explanation

The examiner expects two points: (1) define/explain what collateral is, and (2) link its absence to why the poor are excluded from bank loans. Avoid writing about SHGs or moneylenders unless the question specifically asks — keep the answer focused. The phrase "one of the major reasons which prevents the poor from getting bank loans" from the passage is the key idea to anchor your answer.

Q16. medium exam-ready **[2]**

How does money eliminate the problem of double coincidence of wants that exists in a barter system?

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Model Answer

In a barter system, exchange requires **double coincidence of wants** — both parties must want exactly what the other has to offer. Money eliminates this by acting as a **medium of exchange**. A seller first exchanges goods for money, then uses that money to buy whatever he needs — without needing to find a buyer who also has what he wants.

Source: Money and Credit, Chapter 3

Explanation

Examiners expect two clear points: (1) define double coincidence of wants briefly, and (2) explain how money removes it by acting as an intermediate/medium of exchange. Use the shoe manufacturer–wheat farmer example only if you have space; here it's implied. The phrase **"medium of exchange"** is a key term — always include it. Avoid lengthy examples; 40–60 words is the target for 2 marks.

Q17. medium exam-ready **[3]**

Explain how a cooperative society functions as a source of credit for its members in rural areas.

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Model Answer

Cooperative societies are a major formal source of cheap credit in rural areas. Members of a cooperative **pool their resources** by depositing money with the society. Using these deposits as **collateral**, the cooperative obtains a large loan from a bank. These funds are then lent to members at low interest rates for various purposes — purchase of agricultural implements, cultivation, house construction, and other expenses. Once members repay their loans, a fresh round of lending takes place, making credit continuously available.

Example: Krishak Cooperative has 2,300 farmer-members, accepts their deposits, and uses them to provide affordable loans for farming and other needs.

Source: Chapter 3, Loans from Cooperatives

Explanation

- Examiners expect three clear points for 3 marks: (1) pooling of resources/deposits, (2) using deposits as collateral to get bank loan, (3) lending to members at cheap rates for various purposes.
- Mention the Krishak Cooperative example briefly — it shows you've read the chapter and makes the answer concrete.
- Avoid writing about SHGs or moneylenders here; the question is specifically about cooperatives.

Q18. medium exam-ready **[3]**

Describe the terms of credit that a small farmer in a village typically faces when borrowing from an agricultural trader. How do these terms benefit the trader?

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Model Answer

A small farmer like Shyamal borrows from an agricultural trader at **3% per month (36% per annum)**. The terms of credit include:

- **Farm inputs** (seeds, fertilisers) are supplied on credit at the start of the cropping season.
- Repayment is due **after harvest**.
- The farmer must **promise to sell the crop to the trader** (tied credit).

How this benefits the trader:
The trader ensures prompt repayment through the crop sale condition. Since crop prices are low right after harvest, the trader buys the crop cheaply and sells it later at a higher price, earning a **double profit** — on the loan (interest) and on the crop trade.

Source: Chapter 3 — Money and Credit, "Example of a Village" section

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Explanation

The examiner expects three elements: the interest rate, the condition of supplying inputs on credit, and the compulsory crop-sale clause. Then 1–2 lines on how the trader profits from both interest and low crop prices. Avoid confusing Shyamal's trader loan (3%/month) with the moneylender rate (5%/month) — both appear in the passage, so be precise.

Q19. medium exam-ready **[3]**

[short_answer] How does the Reserve Bank of India ensure that commercial banks follow fair lending practices and do not exploit borrowers? Why is such regulation important for the economy?

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Model Answer

The Reserve Bank of India (RBI) supervises the functioning of commercial banks in the following ways:

1. **Cash balance monitoring:** RBI ensures banks maintain a minimum cash balance out of deposits received.
2. **Loan distribution:** RBI sees that banks lend not just to profit-making businesses but also to small cultivators, small-scale industries, and small borrowers.
3. **Periodic reporting:** Banks must periodically submit information to the RBI on how much they are lending, to whom, and at what interest rate.

Importance: Such regulation is necessary because without supervision, banks may lend only to the rich and ignore the poor. Cheap and affordable credit distributed equally is crucial for the country's development and reduces dependence on expensive informal lenders.

Source: Chapter 3 — Formal Sector Credit in India

Explanation

- The question directly maps to Exercise Q.8: *"In what ways does the RBI supervise the functioning of banks? Why is this necessary?"*
- Examiners expect **three specific RBI functions** (cash balance, lending priority, periodic reporting) plus a brief reason for importance.
- Avoid writing only one or two points — all three supervisory roles are in the textbook passage and should be mentioned for full marks.
- End with the development/inequality angle (poor vs. rich access to formal credit) for the "why important" part.

Q20. medium exam-ready **[3]**

Why do the richer households in India have greater access to formal sector credit compared to poorer households? Explain with reasons.

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Model Answer

Richer households have greater access to formal sector credit due to the following reasons:

1. **Collateral**: Formal sector loans (banks/cooperatives) require collateral as security. Rich households own assets like land, property, or vehicles which they can offer, while poor households lack such assets.

1. **Documents**: Banks demand proper documents (income proof, identity proof, etc.). Richer people can provide these easily, whereas the poor often cannot.

1. **Creditworthiness**: Banks prefer borrowers with higher income and repayment capacity, as they are less likely to default.

As a result, the poor depend on informal sources like moneylenders who charge very high interest rates (up to 5% per month), often pushing them into debt traps.

Source: Chapter 3 — Money and Credit, "Self-Help Groups for the Poor" and "Formal and Informal Credit: Who gets what?"

Explanation

- Examiners expect **3 distinct reasons** for a 3-mark question — one point per mark.
- The key points are: **lack of collateral**, **lack of documents**, and **lower income/creditworthiness** of the poor.
- Always link back to the consequence (dependence on informal credit) to show full understanding.
- Avoid writing a long essay — keep it tight and point-based for full marks.

Q21. medium exam-ready **[3]**

[short_answer] Many rural women who need credit are unable to access bank loans individually. How has the Self Help Group model overcome this barrier, and what role do members themselves play in managing the group's funds?

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Model Answer

Rural women often lack **collateral**, which is a key requirement for bank loans, making it difficult for them to access formal credit individually.

The **Self Help Group (SHG) model** overcomes this barrier by organising 15–20 women from a neighbourhood to pool their savings regularly. After a year or two of regular savings, the group becomes eligible for a bank loan sanctioned in the group's name, so individual collateral is not required.

Members themselves take most important decisions — regarding the purpose, amount, interest rate, and repayment schedule of loans. If any member defaults, the other members follow it up seriously, making the group collectively responsible for repayment. This peer accountability convinces banks to lend to SHGs even without collateral.

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

Explanation

- **3 marks = 3 clear points**: (1) the problem (no collateral), (2) how SHG solves it (pooling savings → group loan), (3) members' role (decision-making + collective repayment responsibility).
- Examiners look for the terms **collateral**, **pool savings**, and **group decisions/repayment** — use them explicitly.
- Don't over-explain the savings amounts or SHG social functions; keep focus on the two parts the question asks: barrier overcome + members' role in managing funds.

Q22. medium exam-ready **[3]**

Using the example of a shoe manufacturer who receives a large order before the festival season, explain how credit can play a positive role in increasing earnings.

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Model Answer

Salim, a shoe manufacturer, received an order for 3,000 pairs of shoes before the festival season. To complete production on time, he needed money to hire workers and buy raw materials. He obtained credit by getting leather from the supplier on credit and taking an advance loan from the trader.

This credit helped Salim meet his **working capital needs** — ongoing expenses of production. He completed the order on time, earned a good profit, and repaid the loan. Thus, credit played a **positive role** by enabling Salim to increase his earnings, which would not have been possible without timely credit.

Source: Chapter 3 – Money and Credit, "Two Different Credit Situations – Festival Season"

Explanation

- Examiners look for **three elements**: the situation/need for credit, how credit was obtained, and the positive outcome (increased earnings + repayment).
- Mention "working capital needs" — it's the textbook term and fetches a mark.
- Avoid confusing this with Swapna's example (negative credit). Stay focused on Salim only.
- 3 marks = ~3 distinct points, so structure your answer around need → credit obtained → positive outcome.

Q23. deep exam-ready **[3]**

Credit can be both a boon and a bane for borrowers. Analyse this statement using two contrasting situations.

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Model Answer

Credit can be a **boon** when it helps borrowers increase their earnings. For example, Salim, a shoe manufacturer, took a loan to buy raw materials and hire workers to fulfil a large order. He completed production on time, earned good profit, and repaid the loan. Here, credit played a positive role.

Credit becomes a **bane** when risks are high. Swapna, a small farmer, borrowed from a moneylender for cultivation. Her crop failed due to pests, making repayment impossible. Debt grew, and she had to sell part of her land — falling into a **debt trap**.

Thus, whether credit is useful depends on the risks involved and available support in case of loss.

Source: Chapter 3, Two Different Credit Situations

Explanation

- The examiner expects **two clearly contrasting situations** — one positive (Salim) and one negative (Swapna) — directly from the textbook examples.
- Name the examples and briefly explain **why** credit helped or harmed — don't just say "good" or "bad."
- Key terms to use: **boon, bane, debt trap, risk** — these fetch marks.
- End with the textbook's own conclusion: outcome depends on **risk** and **support in case of loss**.

Q24. deep exam-ready **[5]**

[long_answer] (A) Rural poor in India often find themselves trapped in a cycle of debt with informal lenders. Explain how Self Help Groups (SHGs) offer an alternative credit mechanism to such households. In your answer, discuss: (a) why the rural poor are excluded from formal credit, (b) how an SHG pools resources and provides loans to its members, and (c) how SHGs empower women beyond just providing credit.

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Model Answer

(a) Why rural poor are excluded from formal credit:
Banks require proper documents and collateral as security for loans. The rural poor lack both, making it nearly impossible for them to access formal credit. As a result, they depend on informal lenders like moneylenders who charge very high interest rates (up to 60% per annum), keep no records, and often trap borrowers in a cycle of debt.

(b) How an SHG pools resources and provides loans:
A typical SHG has 15–20 members from one neighbourhood who meet and save regularly (₹25–₹100 per member). These savings are pooled, and members can take small loans from the group at interest rates lower than moneylenders. After one to two years of regular savings, the group becomes eligible for a bank loan sanctioned in the group's name. Members collectively decide the purpose, amount, interest rate, and repayment schedule. Group responsibility for repayment makes banks willing to lend even without individual collateral.

(c) Empowerment of women beyond credit:
SHGs make women financially self-reliant and provide a platform to discuss and act on social issues such as health, nutrition, and domestic violence, strengthening their voice in the community.

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

Explanation

- Examiners look for **three clearly addressed parts** — exclusion from formal credit, SHG mechanism, and social empowerment. Label them or use clear paragraphs.
- Key terms to include: *collateral*, *pooling savings*, *group responsibility/liability*, *self-employment*, *social issues platform*.
- Do not just list points vaguely — each part needs a brief explanation (not just a phrase).
- The empowerment point must go **beyond finance** (health, nutrition, domestic violence) to score fully.

Q25. deep exam-ready **[5]**

Compare and contrast the formal and informal sectors of credit in India. In your answer, discuss: (a) examples of each, (b) differences in interest rates and terms of credit, (c) regulatory oversight, and (d) who benefits more from each sector and why.

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Model Answer

Formal vs. Informal Sector Credit in India

(a) Examples:

- **Formal:** Commercial banks, cooperative banks/societies, other formal agencies.
- **Informal:** Moneylenders, traders, employers, landlords, relatives and friends.

(b) Interest Rates and Terms:
Formal lenders charge lower interest rates with documented terms of credit. Informal lenders charge much higher rates with no fixed terms, which can trap borrowers in debt.

(c) Regulatory Oversight:
The Reserve Bank of India (RBI) supervises formal lenders — monitoring cash balances, loan distribution, and interest rates. No organisation supervises informal lenders; they can charge any rate and use unfair recovery methods.

(d) Who Benefits More:
Rich households benefit more from formal credit (83% of their loans are formal). Poor households depend heavily on informal sources (54% of urban poor's loans are informal) due to lack of collateral and documents, forcing them to pay higher costs.

Source: Chapter 3 — Money and Credit, Formal and Informal Credit section

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Explanation

- Examiners expect all four parts addressed — missing any part loses marks directly.
- Quote the RBI's supervisory role specifically (cash balance monitoring, periodic reporting) for full marks on part (c).
- Use the **data from Graphs 1 & 2** (51% commercial banks, 23% moneylenders; 83% formal for rich vs. 54% informal for poor) — numerical evidence scores well.
- Avoid vague statements; link high informal interest → debt trap → underdevelopment to show understanding.
- Keep each sub-part brief and to the point at this mark level.

Q26. deep exam-ready **[4]**

Read the following situation and answer the questions that follow:

Rama is a landless agricultural labourer in a village. There are several months in the year when she has no work. She depends on her employer — a medium landowner — for loans to meet daily expenses and for emergencies like sudden illness or family functions. The landowner charges an interest rate of 5 per cent per month. Rama repays the money by working for him. Most of the time, Rama has to take a fresh loan before the previous one is repaid. Though the landowner does not treat her well, she continues to work for him because she has no other source of credit.

(i) Why is Rama unable to access credit from formal sources such as banks? (1 mark)
(ii) At 5 per cent per month, what is the annual rate of interest Rama pays? How does this compare with the typical bank loan rate for a farmer? (1 mark)
(iii) Explain how Rama's situation illustrates the concept of a debt trap. (2 marks)

◆ Money and Credit

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Model Answer

(i) Rama is landless and has no collateral (asset to offer as security). Banks require proper documents and collateral before sanctioning loans. Since Rama cannot provide these, she is unable to access formal credit.

(ii) Annual rate = 5% × 12 = **60% per annum**. This is far higher than the typical bank loan rate for farmers, which is around **8.5% per annum** (as seen in Arun's case in Sonpur).

(iii) A debt trap is a situation where a borrower is unable to repay a loan and is forced to borrow again, causing debt to keep rising. Rama earns irregularly and must borrow for daily expenses before repaying the previous loan. Because of the high interest rate (60% p.a.), repayment is very difficult. Fresh loans are taken before old ones are cleared, leaving her permanently indebted to the landowner with no way to escape.

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

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Explanation

- **(i)** The key phrase examiners look for is **"no collateral"** — that is the primary reason banks reject poor borrowers.
- **(ii)** Always show the calculation (5 × 12 = 60%). Compare directly with Arun's 8.5% — that figure is from the passage and makes the contrast concrete.
- **(iii)** For 2 marks, you need: define debt trap + apply it to Rama's case with at least two specific details (irregular income, high interest, fresh loan before old repaid). Avoid vague statements; use evidence from the passage.

Q27. medium exam-ready **[4]**

[case_study] Read the following and answer the questions:

In a village near Sonpur, a group of 18 women have formed a Self Help Group. They meet every month, pool their savings, and have been doing so regularly for over a year. The group recently applied for a bank loan and the bank sanctioned a loan in the group's name. The members plan to use the funds to buy sewing machines, purchase raw materials, and release mortgaged land. All decisions about how loans are given to members and how repayments are tracked are made collectively by the members themselves.

(i) Why was the bank willing to sanction a loan to the group even though individual women had no collateral to offer? (1 mark)
(ii) Name any two productive activities for which the SHG members plan to use the loan. (1 mark)
(iii) How does the collective functioning of an SHG help its members in ways that go beyond access to credit? Explain with two points. (2 marks)

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Model Answer

(i) The bank was willing to sanction the loan because in an SHG, the group itself is responsible for repayment. If any member fails to repay, the other members follow it up seriously. This collective responsibility acts as a substitute for collateral.

(ii) Two productive activities:

1. Buying sewing machines (acquiring assets)
2. Purchasing raw materials for work

(iii) Beyond credit, SHGs help members in two ways:

1. **Financial self-reliance:** SHGs help women become economically independent by providing small loans at reasonable interest rates, reducing dependence on moneylenders.
2. **Platform for social issues:** Regular group meetings provide a platform to discuss and act on social issues such as health, nutrition, and domestic violence, empowering women beyond just finances.

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

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Explanation

- **(i)** Key phrase examiners look for: "group is responsible for repayment" / "collective guarantee replaces collateral." One line is enough for 1 mark.
- **(ii)** Pick any two from the passage: sewing machines, raw materials, releasing mortgaged land. Don't over-explain — it's 1 mark.
- **(iii)** Two distinct points needed for 2 marks. Always include **both** the financial empowerment angle and the **social issues platform** angle — the passage explicitly mentions health, nutrition, domestic violence. Examiners expect these specific examples.

Q28. medium exam-ready **[4]**

Read the following and answer the questions:

Megha has taken a loan of Rs 5 lakhs from a bank to purchase a house. The bank asked her to submit employment records and salary documents before approving the loan. The annual interest rate is 12 per cent and the loan must be repaid in monthly instalments over 10 years. The bank retained the papers of the new house as security and will return them only after the entire loan with interest is repaid.

(i) What is the term used for the house papers that the bank has retained as security? (1 mark)
(ii) Identify any two components of the 'terms of credit' evident in this loan arrangement. (1 mark)
(iii) Why do banks insist on such documentation and security before granting loans? What risk does this help the bank manage? (2 marks)

◆ Money and Credit

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Model Answer

(i) The term used for the house papers retained by the bank as security is **collateral**.

(ii) Two components of terms of credit evident in this arrangement:

1. **Interest rate** — 12% per annum
2. **Mode of repayment** — monthly instalments over 10 years

(Documentation requirement / collateral are also valid components.)

(iii) Banks insist on documentation (employment records, salary slips) and collateral (house papers) to ensure that the borrower has a stable income and the ability to repay the loan. Collateral serves as a guarantee — if the borrower **fails to repay**, the bank has the right to sell the asset to recover its money. This helps the bank manage the **risk of default** (non-repayment of the loan).

Source: Chapter 3 — Money and Credit, Terms of Credit / A House Loan

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Explanation

- **Q(i)** is a direct 1-mark definition recall — "collateral" is the exact textbook term; writing "security" alone may lose the mark.
- **Q(ii)** needs only two named components from the four listed in the textbook (interest rate, collateral, documentation, mode of repayment). Pick any two clearly identified in the passage.
- **Q(iii)** carries 2 marks — examiners look for two distinct points: (a) purpose of documentation/collateral = ensure repayment capacity; (b) specific risk managed = risk of default/non-repayment. Both must appear for full marks.

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