

ICSE SEMESTER 2 EXAMINATION

SAMPLE PAPER - 2

ECONOMIC APPLICATIONS

Maximum Marks: 50

Time allowed: One and a half hours

Answers to this Paper must be written on the paper provided separately.

You will not be allowed to write during the first 10 minutes.

This time is to be spent in reading the question paper.

The time given at the head of this Paper is the time allowed for writing the answers.

*Attempt **all** questions from **Section A** and **any four** questions from **Section B**.*

SECTION A

*(Attempt **all** questions)*

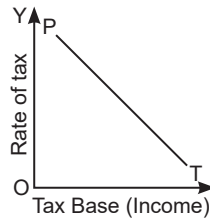
Section-A (Attempt all questions)

Question 1.

Choose the correct answers to the questions from the given options. (Do not copy the question, write the correct answer only)

- (i) Locker facility, cheques, letter of credit are what kind of functions of commercial bank?
 - (a) General utility
 - (b) Agency function
 - (c) Primary function
 - (d) Secondary function
- (ii) Which institute work as banker to the government?
 - (a) Central bank
 - (b) Private bank
 - (c) Commercial bank
 - (d) Government bank
- (iii) When the rise in prices is very slow like that a snail or creeper is called as:
 - (a) Walking inflation
 - (b) Running inflation
 - (c) Hyperinflation
 - (d) Creeping inflation
- (iv) Currency notes or coins are form of:
 - (a) Standard money
 - (b) Bank money
 - (c) Near money
 - (d) Electronic money
- (v) General acceptability, durability, homogeneity all are features of:
 - (a) Money
 - (b) Tax
 - (c) Policies
 - (d) None of these
- (vi) What can be the objective of privatization?
 - (a) Rising budgetary deficit
 - (b) Increase in investment
 - (c) Reducing state interference
 - (d) Increase in production

- (vii) Corruption, bribery are very commonly seen defects of which type of sector?
- (a) Private sector enterprise (c) Capitalist economy
(b) Public sector enterprise (d) Mixed
- (viii) The following graph show which type of tax?



- (a) Progressive tax (c) Proportional tax
(b) Regressive tax (d) Degressive tax
- (ix) Which of the following statement is true in relation with Indirect tax?
- (a) They can be shifted on to others (c) It is imposed on income and wealth
(b) They cannot be shifted on to others (d) Directly paid to government
- (x) Fiscal policy mainly focuses towards which two components to produce desirable effects on national income, production and employment?
- (a) Expenditure, revenue (c) Foreign income, export
(b) Income, tax (d) Import, export

Section-B (Attempt any four questions from this Section)

Question 2.

- (i) What do you understand by hyperinflation?
- (ii) How central bank work as a clearing agent for commercial banks? Explain.
- (iii) Write three differences between central bank and commercial bank.
- (iv) Money is the basis of credit system. Explain in brief.

Question 3.

- (i) What do we mean by central bank?
- (ii) Write down two differences between demand deposit and fixed deposit.
- (iii) Mention three important differences between direct and indirect taxes.
- (iv) Explain the benefits of privatization in economy.

Question 4.

- (i) Define cost push inflation.
- (ii) Write four points in favour of depositing money with commercial bank.
- (iii) Discuss the importance of banks in modern economy. Write three points.
- (iv) Mention the type of loans advanced by the commercial banks.

Question 5.

- (i) What is the advantage of indirect taxes? Write any two.
- (ii) Give two characteristics of money.
- (iii) What is the effect of inflation on production? explain.
- (iv) Explain clearly how indirect taxes can be both regressive and progressive.

Question 6.

- (i) What is inflation?
- (ii) How public expenditure does promotes economic development. Give two points.
- (iii) Money is standard of deferred payments. Explain this statement.
- (iv) Suggest three measures to control inflation in the nation.

Question 7.

- (i) State two objectives of fiscal policy.
- (ii) Can direct tax reduce income inequality? Explain.
- (iii) Write down three differences between fiscal policy and monetary policy
- (iv) What is CRR? How does it affect the creation of money by banks?



Section-A

Answer 1.

- (i) (a) General utility

Explanation :

There are several general utility services that commercial banks offer like: Issuing traveller cheques. Offering locker facilities for keeping valuables in safe custody. Also, issuing debit cards and credit cards, etc.

- (ii) (a) Central bank

Explanation :

Central bank work as banker of the government and provide assistance whenever required. Central Bank keeps the cash balances of commercial banks and issues loans to them on requirements in the same manner as the commercial banks do for its customers. That's why it is also called as bankers' bank.

- (iii) (d) Creeping inflation

Explanation :

Creeping inflation means rise in price with slow speed. This is also known as mild inflation or moderate inflation. This type of inflation occurs when the price level persistently rises over a period of time at a mild rate.

- (iv) (a) Standard money

Explanation :

Standard money or currency money includes currency notes and coins. a monetary unit which is designated by a government to serve as the basis of its currency system and into which other types of money in the country are convertible as compare standard of value.

- (v) (a) Money

Explanation :

The characteristics of money are durability, portability, divisibility, uniformity, limited supply, and acceptability.

- (vi) (a) Rising budgetary deficit

Explanation :

Rising budgetary deficit means increase in expenditure as compare to the income due to which the need for privatization arises of a public sector enterprise that's make it an objective of privatization.

(vii) (b) Public sector enterprise

Explanation :

Corruption, bribery are commonly seen defects in public sector enterprise. Which work as limitations of public sector enterprise and effects its working efficiency.

(viii) (b) Regressive tax

Explanation :

Regressive tax means decrease in tax rate as the income increases. A regressive tax is a tax imposed in such a manner that the tax rate decreases as the amount subject to taxation increases. "Regressive" describes a distribution effect on income or expenditure, referring to the way the rate progresses from high to low, so that the average tax rate exceeds the marginal tax rate.

(ix) (a) They can be shifted on to others

Explanation :

One of the main feature of indirect tax is tax liability which means:-

Tax liability: The service provider or seller pays indirect taxes to the government, and the liability is transferred to the consumer. One feature of indirect tax is that it can be shifted on to the others.

(x) Expenditure, revenue

Explanation :

Fiscal policy mainly focuses towards expenditure and revenue to produce desirable effects on national income, production and employment.

Section-B

- (i) Hyperinflation is a situation when the rise in prices is 20% to 30% or more. This rise is uncontrollably high. Basically, hyperinflation is accelerating inflation. Hyperinflation very quickly diminishes the value of the currency and individuals tend to minimize their holding in the currency.
- (ii) As the custodian of cash reserves of the commercial banks, the central bank acts as the clearing house for these banks. Since all banks have their accounts with central bank, the central bank can easily settle the claims of various banks against each other simply by book entries of transfer from and to their accounts. This method of settling accounts is called clearing house function of the central bank.
- (iii)

Central bank	Commercial bank
Central bank is the apex institution of the monetary and banking structure of the country. It regulates the entire banking system of the country.	Commercial bank is a bank which deals in money and credit for purposes of earning profit.
Its main objective is to promote social welfare	It main objective is to earn profit
Central bank is generally a government owned institution	Commercial banks may be both privately owned or government owned institutions.

- (iv) In modern economic system, credit plays a key role and money constitutes the basis of credit. Money facilitates the functioning of credit instruments such as cheques, promissory notes, bills of exchange etc. such credit instruments facilitate transfer of value from one person to another and these instruments cannot be used without existence of money.

Answer 3.

- (i) Central bank is an apex institution of the monetary and banking structure of the country. It regulates the entire banking system of the country. Central Bank of India is an Indian nationalised bank. It is under the ownership of Ministry of Finance, Government of India and is one of the oldest and largest nationalised commercial banks in India.

(ii)

Demand deposit	Fixed deposit
A demand deposit account (DDA) is a bank account from which deposited funds can be withdrawn at any time, without advance notice. The interest rate in demand deposit is very low	In a Fixed Deposit, the sum of money is blocked for the period of the deposit. Banks allow depositors the flexibility to invest their funds from periods as low as 7 days to 10 years. Since the interest rate and the period of this deposit are fixed, banks refer to this type of deposit as a Fixed Deposit.
Demand deposits are chequable, i.e. they can be withdrawn through cheques.	Fixed deposits are not chequable, i.e they can't be withdrawn through cheques.

- (iii) Difference between Direct Taxes and Indirect Taxes

Direct Taxes	Indirect Taxes
The tax is paid by the person, on whom it is imposed, e.g., income tax, property tax, profit tax, etc.	The tax is imposed on one person but the burden is borne by some other person, e.g., excise duty, sales tax etc.
They promote civic consciousness.	They do not promote civic consciousness.
They are more susceptible to evasion.	They are less susceptible to evasion.

- (iv) The benefits of privatization are as shown:

- **Improved performance:** private companies are profit incentivized rather than politically motivated. Privatization allows companies to turn more efficient by eliminating unnecessary elements within organization like overwhelming bureaucracy & red tape. Moreover, private companies assess their employees based on their performance and adequately incentivise better performance. This factor spurs overall performance in an organisation.
- **Reduction in Unproductive Expenditure:** Due to unproductive expenditure, most of the public sector units are running under heavy loss. Hence, the governments has to incur huge sum of subsidy every year to keep them running. It increases financial burden on the government. Hence there is a move of privatisation—particularly that of loss making units in India.
- **Improved management:** privatization fosters improved management of a company. As managers of a privately owned organization are accountable to the company's owners, it becomes their responsibility to ensure efficient management. This factor of accountability is less intense in public sector companies which results in poor and inefficient operations that may ultimately harm the economy.

Answer 4.

- (i) Cost-push inflation is a type of inflation caused by substantial increases in the cost of important goods or services where no suitable alternative is available. Higher prices are then the result, as costs of production increase due to decreased aggregate supply.
- (ii) Commercial banks are one of the best options to opt for depositing money by the customers. Reasons in favour are as shown:
 - (i) **Safety:** Banks provide safe and secure place to keep customers money as compare to the house or a working place.
 - (ii) **Earning via interest:** Depositors can earn interest on the basis of their deposits. This is the advantage of depositing money in banks that they provide the means to earn on your deposits for fixed time period.
 - (iii) **Easy withdrawal:** People have the provisions to withdrawn the money as and when they require. customers can withdraw there money any time by following simple procedures decided by the banks on the basis of their type of deposits.
 - (iv) **Fast Payments:** People can also make payment through cheques or by online transfers. banks make tranfer of money easy and fast by the feature of online transferring of money.
- (iii) On the basis of these Important Functions of Banks, we may easily describe the importance of banks in today's global life.
 - 1. **Collections of Savings and Advancing Loans:** Acceptance of deposit and advancing the loans is the basic function of commercial banks. On this function, all other functions depend accordingly. Bank operates different types of accounts for its customers.
 - 2. **Money Transfer:** Banks have facilitated the making of payments from one place or persons to another by means of cheques, bill of exchange and drafts, instead of cash. Payment through cheques, the draft is more safe and convenient, especially in case of huge payments, this facility is a great help for traders and businessmen. It really enhances the importance of banks for the business community.
 - 3. **Encourages Savings:** Banks perform an invaluable service by encouraging savings among the people. They induce them to save for profitable investment for themselves and for the national interest. These savings help in capital formation.
- (iv) Loans can be granted in the form of cash credit, demand loans, short term loan, overdraft, discounting of bills etc.
 - **Cash credit:** under the cash credit system the borrower is sanctioned a credit limit up to which he can borrow from the bank. The interest payable by the borrower is calculated on the amount of credit limit actually drawn.
 - **Demand loan:** demand loan granted by a bank is those loans that can be recalled on demand by the bank at any time. Short term loans (car loans, housing loan etc) are given as personal loans against some security. The interest is payable on the entire sum of loans granted.
 - **Overdraft:** In case of overdraft facility, an account holder is allowed to withdraw a sum of money in excess of the amount deposited with the bank. Here, the borrower who has received this facility has to pay interest on the amount overdrawn.

Answer 5.

- (i) Advantages of indirect taxes are as follows:
 - 1. **Convenient:** They are convenient to both the tax-prayer and the State. I he tax-payers do not feel the burden much partly because an indirect tax is paid in small amounts and partly because it is paid only when making purchases.
 - 2. **Broad-based:** Indirect taxes can be spread over a wide range. Very heavy direct taxation at just one point may produce harmful effects on social and economic life. As indirect taxes can be spread widely, they are more beneficial and suitable.

(ii) **The two characteristics of money are:**

1. **Acceptability** supports the function of medium of exchange. The essential quality of money is that it must act as an item being acceptable to all, without having any hesitation in the exchange for goods and services. Acceptability means that everyone must be able to accept the money for transactions. Money is universally accepted around the world as a universal mean for transaction.
2. **Portability:** which also serves as a medium of exchange means that money can be movable from place to place to be used as monetary transaction to be exchanged for goods and services. Portability also means that consumers are now able to carry money along with them to be used as transactions for goods and services. In modern days, money is carried from one location to another without needing much effort as all types of money such as cash notes, coins and cards are carried easily in a wallet.

(iii) Effects of inflation are wide-ranging in terms of the type of impact, recipient of impact, or even on the different economic scenarios. As mentioned earlier the impacts of inflation on production and distribution of wealth are prominent. The impact of inflation on production also depends on the type of inflation.

1. If inflation is a cost-push, then there will be a decline in production as the increase in production cost will hamper the confidence as well as meet the budget constraints of the producer.
2. In demand-pull inflation, there are high chances for an increase in production. The increase in money supply pushes the demand for goods and services up and this increased demand for existing goods will have a positive impact on the prices. As higher prices are a production incentive, the producers tend to ramp up their production to meet the high demand. The demand-pull inflation also has a short-run positive impact on the stakeholders of production including the laborers as they tend to receive a higher wage.

- (iv) 1. Indirect taxes are progressive when they are imposed on luxury goods which are consumed by the richer sections of the society. They generate economic resources which can be spent on necessities of the poor masses.
2. Indirect taxes do not remain equitable when they are imposed on necessities. They become regressive in nature. They affect the poor more than the rich man. For example, a commodity tax imposed on food ingredients will affect a poor family to a much greater degree than a rich family.

Answer 6.

(i) Inflation refers to a situation in which prices rise and value of money falls or we can say inflation is the rate of increase in prices over a given period of time. For example, a sudden decrease in the supply of oil, leading to increased oil prices, can cause cost-push inflation.

(ii) Public expenditure promotes economic development in various ways:-

1. **Public sector & capital formation:** This sector has been a major reason for the generation of capital in the Indian economy. A large amount of the capital comes from the Public sector Units in India
2. **Creation of Employment opportunities:** Public sector has brought about a major change in the employment sector in the country. They provide a lot of opportunities under various domains and thus help in uplifting the Indian economy and society.

(iii) When money is generally accepted as a medium of exchange and a unit of value, it naturally becomes the unit in terms of which deferred or future payments are expressed. This function in fact is an extension function of money. The amount of loan is measured in terms of money and it is paid back in money. A large number of credit transactions involving huge future payments are made daily. Money performs this function of standard for deferred payments because its value remains more or less stable.

(iv) Three measures adopted by government to control inflation in the nation are:-

1. **Monetary measures:** Monetary policy is one of the most commonly used measures taken by the government to control inflation. The government of a country takes several measures and formulates policies to control economic activities. Monetary policy is one of the most commonly used measures taken by the government to control inflation.
2. **Fiscal Measures:** Apart from monetary policy, the government also uses fiscal measures to control inflation. The two main components of fiscal policy are government revenue and government expenditure. In fiscal policy, the government controls inflation either by reducing private spending or by decreasing government expenditure, or by using both.
- **Price Control:** Another method for ceasing inflation is preventing any further rise in the prices of goods and services. In this method, inflation is suppressed by price control, but cannot be controlled for the long term.

Answer 7.

(i) Two objectives of fiscal policy are:

1. **Economic growth:** Reduction in inequalities of Income and Wealth: Fiscal policy aims at achieving equity or social justice by reducing income inequalities among different sections of the society. The direct taxes such as income tax are charged more on the rich people as compared to lower income groups. Indirect taxes are also more in the case of semi-luxury and luxury items which are mostly consumed by the upper middle class and the upper class. The government invests a significant proportion of its tax revenue in the implementation of Poverty Alleviation Programmes to improve the conditions of poor people in society.
2. **Reduction in inequalities of Income and Wealth:** Fiscal policy aims at achieving equity or social justice by reducing income inequalities among different sections of the society. The direct taxes such as income tax are charged more on the rich people as compared to lower income groups. Indirect taxes are also more in the case of semi-luxury and luxury items which are mostly consumed by the upper middle class and the upper class. The government invests a significant proportion of its tax revenue in the implementation of Poverty Alleviation Programmes to improve the conditions of poor people in society.

(ii) All those taxes which are directly imposed on income wealth and property are called as direct tax.

They usually increase with increase in income. That is the reason we can say that direct tax reduces income equality. Taxes and benefits have an impact on income being shared more equally between households. Both cash benefits and income tax lead to an overall reduction in income inequality. For example- Income tax.

It is a form of direct tax. People with more income will pay more tax and people with less income will pay less.

(ii)

Monetary policy	Fiscal policy
It is a financial tool that is used by the central banks in regulating the flow of money and the interest rates in an economy	It is a financial tool that is used by the central government in managing tax revenues and policies related to expenditure for the benefits of the economy.
Managed by central bank	Managed by finance ministry
Focuses on stability of an economy	Focuses on growth of an economy.

(iii) Cash reserve ratio (CRR) is the percentage of a bank's total deposits that it needs to maintain as liquid cash. This is an RBI requirement, and the cash reserve is kept with the RBI.

The higher the CRR, the lower is the liquidity with the banks and vice-versa. During high levels of inflation, attempts are made to reduce the flow of money in the economy. For this, RBI increases the CRR, lowering the loan able funds available with the banks. In other words If a depositor has made a stock investment in a bank, a higher CRR rate indicates that the bank will have lesser margins. Similarly, when the CRR rate is low, banks have more money to invest in other firms, lowering loan interest rates. A bank does not earn interest on this liquid cash maintained with the RBI and neither can it use this for investing and lending purposes.

