

CHAPTER

3

MONEY AND CREDIT

Syllabus

- *Role of money in an economy: Formal and Informal financial institutions for Savings and Credit - General Introduction; Select one formal institution such as a nationalized commercial bank and a few informal institutions; Local money lenders, landlords, chit funds and private finance companies..*



TOPIC-1 Money and Credit

Quick Review

- In the early times, people used to exchange one commodity for another, depending on their requirement under the barter system. However, exchanging goods in the barter system required double coincidence of wants.
- However, money eliminates the need for double coincidence of wants. Since money enables the exchange process, it is also called a medium of exchange. Early forms of money were things of daily use.
- Money is anything which is commonly accepted as a medium of exchange and in discharge of debts.
- Before the introduction of coins, a variety of objects were used as money. For example, since the very early ages, Indians used grains and cattle as money. Thereafter came the use of metallic coins—gold, silver, copper coins.
- **Modern currency :**
 - Uses paper notes and coins made of relatively inexpensive metals.
 - Has no value of its own.
 - Has a value only because it is authorised by the government of the country.
- In India, the Reserve Bank of India is the only legal authority that can issue currency notes and coins on behalf of the central government. The Rupee is India's currency and nobody can refuse to accept a payment made in rupees in India.
- People deposit their extra cash in bank. A bank in addition to keeping the money also pays interest on the deposit to the depositor. Thus, bank deposits are also called Demand Deposits.
- A person simply needs to have an account with the bank to deposit money. A cheque can be used to make payment directly from a bank deposit without using cash.
- A cheque is a written instruction to a bank by an account holder to pay a specific sum to a specific person from his deposit. A cheque has all the information about the person to whom payment is to be made, the amount and date of payment and signature of account holder issuing the cheque.

TOPIC - 1

Money and Credit

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TOPIC - 2

Credit Terms and Types

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Know the Terms

- **Barter System :** Barter refers to the direct exchange of goods and services. In this way, barter system refers to that system by which one commodity is exchanged for another without use of money.

- **Money** : Money may be anything chosen by common consent as a medium of exchange. It can be in the form of coins and bank notes; coins and bank notes collectively.
- **Cheque** : A cheque is a paper instructing the banks in writing to pay a specific amount from the person's account to the person in whose name the cheque has been issued.
- **Reserve Bank of India** : The Reserve Bank of India is the only legal authority that can issue currency notes and coins on behalf of the central government.
- **Investment** : Investment is the amount of money spent with the intention of earning income at regular intervals (in the form of return from funds invested) or in the long run (in the form of capital appreciation).

Know the Links

- www.slideshare.net/DINESH_B001/money-and-credit-14361725
- www.authorstream.com/Presentation/...money-and-credit



Very Short Answer Type Questions

(1 mark each)

U Q. 1. What is Barter System?

(Board Term-II, 2015 Set-I)

Ans. Barter is a system of exchange in which goods are directly exchanged without the use of money. 1

U Q. 2. What is a Cheque?

(Board Term-II, (Foreign Set-I) 2015)

Ans. A Cheque is a paper instruction to the bank to pay a specific amount from the person's account to the person in whose name the cheque has been issued. 1

A Q. 3. Recognize the situation when both the parties in a barter economy have to agree to sell and buy each other's commodities? What is it called?

(CBSE SQP 2016)

Ans. This is known as double coincidence of wants. 1

U Q. 4. What is meant by double coincidence of wants? (Board Term-II, Outside Delhi (Set-I) 2015)

Ans. Both parties, the seller and they buyers have to agree to sell and buy each other commodities. Goods are directly exchanged without the use of money. 1

U Q. 5. How does money eliminate the need for double coincidence of wants?

(Board Term-II, Foreign (Set-III) 2016)

Ans. If you have money in your pocket you can purchase any thing at any time as you wish. 1

A Q. 6. What are the two forms of modern currency?

(Board Term-II, Foreign (Set-III) 2015)

Ans. Two forms of modern currency are:

- (i) Paper notes
- (ii) Coins.

1

A Q. 7. How does money act as medium of exchange?

(Board Term-II, Outside (Delhi Set-I, II, III) 2015)

Ans. It acts as an intermediate in the exchange process and transactions. We can buy things if we have money in our pockets. 1

A Q. 8. Who issues currency notes in India?

(Board Term-II, (Set-RKZQI05) 2015)

Ans. Reserve Bank of India. 1

A Q. 9. Why one cannot refuse a payment made in rupees in India?

(Board Term-II, (Delhi Set-II) 2016)

Ans. One cannot refuse a payment made in rupees because it is accepted as a medium of exchange. The currency is authorized by the government of India. 1

A Q. 10. Who supervises the functioning of formal sources of loan?

(Board Term-II, (Foreign Set-II) 2015)

Ans. Reserve Bank of India (RBI). 1

A Q. 11. Look at a 100-rupee note. What is written on the top? Can you explain this?

Ans. Reserve Bank of India (Guaranteed by the Central Government) is written on a 100-rupee note. This statement means that the Government of India has authorised the Reserve Bank of India to issue this note on behalf of the Government. 1



Short Answer Type Questions

(3 marks each)

U Q. 1. How can money be easily exchange itself for goods or services? Give example to explain.

(Board Term-II, (Delhi Set-I) 2016)

Ans. Money acts as a medium to exchange itself for goods and services: A person holding money can easily exchange it for any commodity or service that he or she might. Everyone prefers to receive payments in money and exchange the money for things they want.

For example : A shoemaker wants to sell shoes in the market and buy wheat. The shoemaker

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

(CBSE Marking Scheme, 2016) 3

Q. 2. How is money used as a medium of exchange? Explain with examples. (Board Term-II, 2013)

Ans. Money acts as a medium of exchange in the following ways :

- (i) Overcomes the problem of double co-incidence of wants. For example, if a person needs wheat in exchange of tea, then he/she must search for a person who is ready to trade wheat for tea. Money made the need for such searches redundant.
- (ii) Acts as a medium of deferred payment.
- (iii) Has a store value. 3

(CBSE Marking Scheme, 2013)

Q. 3. What are the modern forms of money? Why is the 'rupee' widely accepted as a medium of exchange? Explain two reasons. (Board Term-II, 2013)

Ans. The modern forms of money are listed below :

- (i) Paper currency
- (ii) Coins
- (iii) Demand deposits
- (iv) Cheques

The rupee is accepted as a medium of exchange in the following ways :

- (i) It is accepted as a medium of exchange because the currency is authorised by the government of the country.
- (ii) In India, the Reserve Bank of India issues currency notes on behalf of the Central Government.

(CBSE Marking Scheme, 2013) 3

Q. 4. Why is modern currency accepted as a medium of exchange without any use of its own? Find out the reason. (Board Term-II, (Outside Delhi Set-I, II, III) 2015)

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

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

(CBSE Marking Scheme, 2015)

Q. 5. How is money used in everyday life? Explain with examples. (Board Term-II, 2014)

Ans. In modern times, money is used as a medium of exchange because it has been authorized by the government as a currency.

In everyday lives we use money :

- (i) To buy goods and services like in market money can be used to buy clothes, vegetables, etc.
- (ii) To deposits in banks so that money can be saved and used for future use. For example—if a labourer deposits his monthly salary in his bank account, then, he can use it in instalments during the entire month.
- (iii) As a store value. For instance, we cannot store perishable goods like milk, grain, etc., to exchange goods in future. However, we can buy precious metals like gold and save it for future use. $1 \times 3 = 3$

Q. 6. Explain with examples, how people are involved with the banks. (Board Term-II, 2014)

Ans. We know that banks accept the deposits from the people who have surplus money and also pay an interest on the deposits. But banks keep only a small portion (15 percent in India) of their deposits as cash with themselves. This is kept as a provision to pay the depositors who might come to withdraw money from their accounts in the bank on any day. They use the major portion of the deposits to extend loans to those who need money. In this way banks mediate between those who have surplus money and those who need money. 3

Q. 7. How is money transferred from one bank account to another bank account? Explain with an example. (Board Term-II, (Foreign Set-I) 2016)

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

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

(CBSE Marking Scheme, 2016) 3

Q.8. Name the various sources of credit in Sonpur.

Ans. There are various sources of credit which are available in Sonpur. These are as follows :

- (i) Agricultural traders
- (ii) Cooperative societies
- (iii) Moneylenders
- (iv) Commercial banks
- (v) Relative and friends, etc. 3



Long Answer Type Questions

(5 marks each)

Q. 1. Why is money transaction system better than barter system? Explain with examples. (Board Term-II, (Set-2080) 2012)

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

- (ii) For example, shoe manufacturer wants to sell shoes in the market and wants to buy wheat. For this, he would look for a wheat growing farmer who would exchange his wheat with the shoes.
- (iii) In barter system, goods are exchanged without the use of money.
- (iv) In contrast, in an economy where money is in use; money by providing the crucial intermediate step eliminates the need for double coincidence of wants.

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

(CBSE Marking Scheme, 2012)

Q. 2. "The rupee is widely accepted as a medium of exchange." Explain.

(Board Term-II, (Set-68002) 2012)

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

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

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

(CBSE Marking Scheme, 2012)

Q. 3. What are demand deposits? Explain any three features of it?

(Board Term-II, (Set-TCJQ6VD) 2016)

OR

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

(Board Term-II, 2012)

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

- (i) Banks accept the deposits and also pay an interest rate on the deposits. In this way people's money is safe with the banks and it earns an interest.
- (ii) The facility of cheques against demand deposits makes it possible to directly settle payments without the use of cash. Since demand deposits are accepted widely as a means of payment, along with currency, they constitute money in the modern economy.
- (iii) It is authorised by the government of the country.
- (iv) Its demand and supply can be controlled RBI.
- (v) In India, the law legalises the use of rupee as a medium of payment that cannot be refused in settling transaction in the country. No individual can legally refuse a payment made in rupees.

(Any three) $2 + 3 = 5$

(CBSE Marking Scheme, 2012)



TOPIC-2

Credit Terms and Types

Quick Review

- As per the Reserve Bank of India, banks hold about 15% of their deposits as cash to arrange for daily withdrawals by depositors.
- A major portion of the remaining deposits is used by banks to give loans to people. The depositors of a bank are allowed to withdraw their deposits on demand and are paid interest on their deposits. The borrowers taking loans repay it to the bank along with interest.
- The interest charged on loans is more than the interest paid by the banks on deposits. The difference between the interest charged on loans and the interest paid on deposits is the bank's income or profit.
- The loan given by a bank is also referred to as credit.
- The idea behind Self-Help Groups is to organise the rural poor into self-help groups and collect their savings. Members can take small loans from the group itself to meet their own needs.
- **A loan or credit is subject to certain conditions that the borrower must agree to. These conditions are called terms of credit and include :**
 - A specified rate of interest.
 - Security against the loan to recover the money if the borrower fails to repay it. This security is called collateral.
 - The assets accepted as collateral are land or property, vehicles, livestock, standing crops and bank deposits.
 - A borrower needs to submit certain documents like proofs of identity, residence, employment and income to avail a loan.
 - The lender reserves the right to sell the collateral in case of non-repayment to recover the loan amount.
- Collateral is an asset that the borrower owns (such as land, building, vehicles, livestock etc.) and uses this as a guarantee to the lender until the loan is repaid.

- **Formal and Informal Credit**
- **The different sources of credit are:**
 - Banks
 - Traders
 - Cooperative societies
 - Landlords
 - Moneylenders
 - Relatives and friends
- Formal credit is generally available with the banks and cooperatives. They charge lesser rates of interest than informal institutions. The Reserve Bank of India (RBI) supervises the functioning of formal sources of loan.
- Informal lenders include moneylenders, traders, employers, relatives and friends, etc. They charge much higher interest on loans. There is no one to stop them from using unfair means to get their money back.

Know the Terms

- **Credit** : Credit means giving money on loan to needy persons.
- **Financial Formal Institutions** : Commercial banks, cooperatives and the regional rural banks are the formal institutions of credit.
- **Financial Informal Institutions** : The informal framework for deployment of credit and savings in India comprises the local moneylenders, landlords, self-help groups, chit fund, employers, relative, friends and private finance companies.
- **Commercial Bank** : A Commercial bank is an establishment for safe custody of money, which it pays out on customer's demand order or otherwise. In other words, institutions accepting deposits and issuing loans are called Commercial banks.
- **Loans** : A loan is usually given for a specific duration of time and needs to be completely repaid by a specified date.
- **Collateral** : Collateral is the security provided by a borrower (such as land, building, vehicle, livestock, deposits with banks) against a loan, and it can be sold in case of non-payment.
- **APS** : APS stands for Average Propensity to Save.
- **Fiat Money** : State issued money which is neither legally convertible to any other thing nor fixed in value in terms of any objective standard.
- **Fiduciary Money** : Money which is accepted on the basis of the trust that the issuer commands is called fiduciary money.
- **Fixed Deposits** : These are deposits for a fixed term varying from a frequency of a few days to a few years.
- **Actual Investment** : The actual amount of investment is called an actual investment.
- **Deferred Payments** : Payments which are to be made in the future are known as deferred payments.
- **Token coins** : Token coins are the coins where value as money is far above the value of metal contained in.
- **Short-term loans** : Loans given for a short period of time are known as short-term loans.

Know the Links

- www.debt.org/credit/loans
- www.investopedia.com/university/credit-cards/credit



Very Short Answer Type Questions

(1 mark each)

- [A] Q. 1. Prove with an argument that there is a great need to expand formal sources of credit in rural India.
(Board Term-II, (Outside Delhi Set-II) 2016)
- Ans. To expand formal sources of credit in rural India, dependence on informal sources of credit has to be reduced. 1
- [A] Q. 2. Why are most of the poor households deprived from the formal sector of loans?
(Board Term-II, (Outside Delhi) Set-III 2016)
- Ans. They are deprived from the formal sector of loans because of :
- (i) Lack of collateral.
 - (ii) They are illiterate.
 - (iii) They cannot fulfil the formalities of the formal sector of loans. (Any one) 1
- [A] Q. 3. Why is the supervision of the functioning of formal sources of loans necessary?
(Board Term-II, (Outside Delhi Set-I) 2016)
- Ans. It is necessary because banks have to submit information to the RBI on how much they are lending, to whom they are lending and what interest rate, etc. 1

[A] Q. 4. Why do farmers require credit?

(Board Term-II, (Set-KCG34U9) 2016)

Ans. Farmers require credit to purchase the raw material and inputs for agriculture. **1**

[A] Q. 5. Why do banks maintain cash reserve?

(Board Term-II, (Set-TCJQ6VD) 2016)

Ans. Banks maintain cash reserve to arrange for daily withdrawals by depositors. **1**

[U] Q. 6. How do the deposits with banks become their source of income?

(Board Term-II, (Delhi Set-I) 2016)

Ans. Banks charge higher interest rate on loans than what they offer on deposits. The difference of interest is the main source of income of banks. **1**



Short Answer Type Questions

(3 marks each)

[R] Q. 1. Mention three points of difference between formal sector and informal sector loans.

(Board Term-II, (Set-KCG34U9) 2016)

Ans. Formal sector loans :

- (i) Loans from banks and cooperatives.
- (ii) Under supervision of the Reserve Bank of India.
- (iii) Reasonable rates of interest.

Informal sector loans :

- (i) Loans from moneylenders, relatives, friend, traders, etc.
- (ii) No supervision of any institution.
- (iii) Very high rates of interest.

$1\frac{1}{2} + 1\frac{1}{2} = 3$ (CBSE Marking Scheme, 2016)

[R] Q. 2. How does the Reserve Bank of India supervise the functioning of banks? Why is this necessary?

(Board Term-II, 2011)

Ans. Reserve Bank of India (RBI) supervised the banks in the following ways :

- (i) It monitors the balance kept by banks for day-to-day transactions.
- (ii) It checks that the banks give loans not just to profit-making businesses and traders, but also to small borrowers.
- (iii) Periodically, banks have to give details about lenders, borrowers and interest rate to RBI.

It is necessary for securing public welfare. It avoids the bank to run the business with profit motive only. It also keeps a check on interest rate of credit facilities provided by bank. RBI makes sure that the loans from the banks are affordable and cheap. **1×3=3**

(CBSE Marking Scheme, 2011)

[A] Q. 3. "Poor households still depend on informal sources of credit". Support the statement with examples.

(Board Term-II, (Foreign Set-III) 2016)

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

- (i) Banks are not present everywhere on rural area.
- (ii) Even when they are present getting a loan from the bank is much more difficult than tabbing a loan from informal sources.
- (iii) Mega banks or public sector banks require proper documents and collateral.

(iv) Absence of collateral is one of the major reasons which prevent the poor from getting bank loans.

(v) Informal lenders such as money lenders they know the borrowers personally and they are willing to give a loan without collateral. (Any three)

1×3=3

[A] Q. 4. "Deposits with the banks are beneficial to the depositors as well as to the nation". Examine the statement.

(Board Term-II, (Outside Delhi Set-I) 2016)

Ans. The deposits with the banks are beneficial to the depositors because of the following reason :

- (i) Safety
 - (ii) Earn Interest.
 - (iii) Can make payment easily through cheques
- Benefits of Bank deposits to the nation are
- (iv) Availability of cheap loans (with more deposits) to large number of people.
 - (v) Boost the industry by providing cheap loans.
 - (vi) The interest rate provided on deposits adds to the income of the family, thus increasing overall income of the nation.

From the above points, it can be concluded that deposits with the banks are beneficial to the depositors as well as to the nation. (Any three)

1×3=3

[U] Q. 5. Dhananjay is a government employee and belongs to a rich household, whereas Raju is a construction worker and comes from a poor rural household. Both are in need and wish to take loan. Create a list of arguments explaining who between the two would successfully be able to arrange money from a formal source. Why?

(Board Term-II, SQP 2016)

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

Arguments :

Banks are not present everywhere in rural India. Even when they are present, getting a loan from a bank is much more difficult than taking a loan from informal sources.

Bank loans require proper documents and collateral. Absence of collateral is one of the major reasons which prevent the poor from getting bank loans.

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

Q. 6. "The credit activities of the informal sector should be discouraged." Support the statement with arguments.

(Board Term-II, (Delhi Set-I, II,III) 2016)

Ans. The credit activities of the informal sector should be discouraged because :

- (i) 85% of loans taken by the poor households in the urban areas are from informal sources.
- (ii) Informal lenders charge very high interest on their loans.
- (iii) There are no boundaries and restrictions.
- (iv) Higher cost of borrowing means a larger part of the earnings of the borrowers is used to repay the loan.
- (v) In certain cases, the high interest rate for borrowing can mean that the amount to be repaid is greater than the income of the borrower.
- (vi) This could lead to increasing debt and debt trap, therefore the credit activities of the informal sector should be discouraged.

(Any three) $1 \times 3 = 3$
(CBSE Marking Scheme, 2016)

Q. 7. Formal credit meets only about half of the total credit needs of the rural people. Where does the other half come from? (Board Term-II, 2014)

Ans. (i) Compared to formal lenders, most of the informal lenders charge much higher interest rates on loans like 3% to 5% per month, i.e., 36% a year.

(ii) Besides the high interest rate, informal lenders impose various other tough conditions. For example, they make the farmers promise to sell the crop to him at a low price. There is no such condition in formal sector.

(iii) Loans taken by poor people from informal lenders sometimes, lead them to debt trap because of high interest rate.

(iv) The formal sources of credit in India still meets only about half of the total credit needs of the rural people. (Any three) $1 \times 3 = 3$
(CBSE Marking Scheme, 2014)

Q. 8. What is meant by term of credit? What does it include? (Board Term-II, 2011)

Ans. Terms of credit are the requirements need to be satisfied for any credit arrangements. It includes interest rate, collateral, documentation and mode of repayment. However, the terms of credit vary depending upon the nature of lender, borrower and loan. (CBSE Marking Scheme, 2011) 3

Q. 9. Why do lenders ask for collateral while lending? Give any three reasons. (Board Term-II, 2014)

Ans. Lenders ask for collateral as security against loans. If the borrower fails to repay the loan, the lender has the right to sell the asset-or collateral to recover the payment.

Collateral assets (such as land, vehicle, etc.) act as a security for the lenders in case the borrower defaults on repayment of loan. It is for this reason that lenders ask for collateral while lending.

3 (CBSE Marking Scheme, 2014)

Long Answer Type Questions

(5 marks each)

Q. 1. How do banks play an important role in the economy of India? Explain.

(Board Term-II, Outside Delhi (Set-I, II, III) 2015)

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

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

(Any five) $1 \times 5 = 5$
(CBSE Marking Scheme, 2015)

Q. 2. How can the formal sector loans be made beneficial for poor farmers and workers? Suggest

any five measures.

(Board Term-II, Outside Delhi (Set-I, II, III) 2016)

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

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

(Any five) $1 \times 5 = 5$
(CBSE Marking Scheme, 2016)

- Q. 3. How are deposits with the bank beneficial for individual as well as for the nation? Explain with examples. (Board Term-II, 2015)

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

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

(Any five) $1 \times 5 = 5$
(CBSE Marking Scheme, 2015)

- Q. 4. Explain the differences between Formal and Informal Sources of Credit.

(Board Term-II, (Set-2030) 2012)

Ans.

S.No.	Formal Sector Credit	Informal Sector Credit
(i)	Includes banks and cooperatives.	Includes moneylenders, traders, employees, friends and relatives.
(ii)	Banks require collateral and proper documentation for getting a loan.	Repeated borrowing can lead to debt trap.
(iii)	A reasonable rate of interest is charged.	Outer planets are called Jovian planets. These planets are larger in size.
(iv)	Apart from profit-making, they also have an objective of social welfare.	Their only motive is to extract profit as much as possible.
(v)	Terms of credit are fair and reasonable.	They impose very tough and sometimes even unreasonable terms of credit on borrowers.
(vi)	The Reserve Bank of India supervises its functioning.	Banks do not supervise.

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

- Q. 5. "Cheap and affordable credit is crucial for the country's development." Explain the statement with five points.

(Board Term-II, (Set-05/A1) 2011)

Ans. Credit for country development :

- (i) Higher cost of borrowing means a larger part of the earnings of the borrowers is used to repay the loan. Hence, borrowers have less income left for themselves.
- (ii) In certain cases, the high interest rate of borrowing can mean that the amount to be repaid is greater than the income of the borrower. This could lead to increasing debt and debt trap. For these reasons, banks and co-operative societies need to lend more.
- (iii) This would lead to higher incomes and many people could then borrow cheaply for a variety of needs.
- (iv) They could grow crops, do business, Set-up small-scale industries, etc.
- (v) They could Set-up new industries or trade goods.

$1 \times 5 = 5$ (CBSE Marking Scheme, 2011)

- Q. 6. Which are the two major sources of formal sectors in India? Why do we need to expand the formal sources of credit?

(Board Term-II, (Set-2080) 2012, 2011)

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

- (i) Banks and (ii) Cooperatives.

Need to expand formal sources of credit are :

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

$2 + 3 = 5$

(CBSE Marking Scheme, 2012)

- Q. 7. Why is it necessary for banks and cooperatives to increase their lending in rural areas? Explain.

(Board Term-II, 2015, Set 1, 3, 2012)

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

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

$1 \times 5 = 5$ (CBSE Marking Scheme, 2012)

- Q. 8. "Most of the poor households are still dependent on informal sources of credit." Explain the statement.

(Board Term-II, 2012)

Ans. (i) Banks are not present everywhere in rural India, whereas informal sources are easily available in all villages.

(ii) Getting a loan from a bank is much more difficult for poor people than taking a loan from the informal resources, because bank loans require proper documents and collaterals.

(iii) Moneylenders provide loan to the poor people without any collateral.

(iv) Formal sources provide loan only for productive purposes, whereas the informal sources provide credit for productive and non-productive purposes.

(v) Other informal sources of credit are friends and relatives, or traders and landlords, who know the borrowers personally and therefore do not demand collateral. $1 \times 5 = 5$

(CBSE Marking Scheme, 2012)

[A] Q. 9. Describe the vital and positive role of credit with examples.

(Board Term-II, Delhi (Set-I, II, III) 2016)

OR

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

(Board Term-II, Foreign (Set-I) 2015)

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

Credit plays a vital and positive role as :

(i) Credit helps people from all walks of life in setting up their business, increase their income and support their families.

(ii) To some people loan helps a lot in constructing their houses and get relief from monthly rent.

(iii) To others it helps a lot in raising their standards.

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

(CBSE Marking Scheme, 2015)

[R] Q.10. How do banks mediate between those who have surplus money and those who need money?

(Board Term-II, (Set-29/A1) 2011)

Ans. (i) Banks keep small proportion of their deposit as cash with themselves.

(ii) Major portion of deposit is used for extending loans.

(iii) The banks mediate between depositors and borrowers in this way.

(iv) They charge high rate of interest on loans than what they offer on deposits. $1\frac{1}{4} \times 4 = 5$

(CBSE Marking Scheme, 2011)

[A] Q. 11. Explain any two features each of formal sector loans and informal sector loans.

(Board Term-II, (Set-29/A1) 2011)

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

(i) Formal sectors provide cheap and affordable loans and their rate of interest are monitored by Reserve Bank of India.

(ii) Formal sector strictly follows the terms of credit, which includes interest rate, collateral, documentation and the mode of repayment.

Informal Sector Loans : Include loans from moneylenders, traders, employers, relatives, friends, etc. Features for informal sector loans are:

(i) Their credit activities are not governed by any organisation, therefore they charge higher rate of interest.

(ii) Informal sector loan providers know the borrowers personally, and hence they provide loans on easy terms without collateral and documentation. $1\frac{1}{4} \times 4 = 5$

(CBSE Marking Scheme, 2011)

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