ForumIAS

Prelims Marathon

3rd Week July, 2025

HISTORY
ECONOMICS
POLITY
SCIENCE AND TECHNOLOGY
GEOGRAPHY AND ENVIRONMENT

INDEX

SOME BASIC CONCEPTS OF MACROECONOMICS

1. Consider the following statements regarding the types of Gross Domestic Product (GDP):
1. Nominal GDP is always lower than Real GDP since it does not account for inflation.
2. Real GDP enables comparison across years by adjusting for inflation using a price deflator.
3. GDP at Purchasing Power Parity (PPP) helps in comparing living standards across countries.

Which of the above statements is/are **correct**?
A. 2 and 3 only
B. 1 and 2 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: A. 2 and 3 only
Explanation:
- **Nominal GDP is usually higher** than Real GDP in times of inflation, not lower.
- Real GDP uses a **price deflator** to adjust for inflation and allow **inter-year comparison**.
- GDP at PPP adjusts for **cost of living and price differences**, allowing for **better international comparisons**.

Source: Laxmikant (Polity)

2. With reference to the methods of calculating Gross Domestic Product (GDP), consider the following statements:
1. The income method includes the total earnings of factors of production like labour and capital.
2. The expenditure method includes consumption, investment, government spending, and net exports.
3. The production method calculates GDP by adjusting nominal GDP for taxes and subsidies to derive real GDP.

Which of the statements given above is/are correct?
(a) 1 and 2 only
(b) 2 and 3 only
(c) 1 and 3 only
(d) 1, 2 and 3

Answer: (a) 1 and 2 only
Explanation:
- The income method considers the income of labour and capital (factors of production).
- The expenditure method is calculated as **C + I + G + (X - IM)**.
- The production/output method involves calculating the market value of all goods/services produced, and *Real GDP is GDP at constant prices*. It does not derive real GDP by subtracting taxes and adding subsidies from nominal GDP. In fact, **GDP at market price = GDP at factor cost + Indirect Taxes – Subsidies**, not Real GDP.

Source: Laxmikant (Polity)

3. Consider the following statements regarding national income aggregates:
1. GDP at Factor Cost is derived by subtracting depreciation and indirect taxes from GDP at Market Price.
2. NNP at Market Price is calculated by adjusting NNP at Factor Cost for indirect taxes and subsidies.
3. GNP at Factor Cost includes net income from abroad added to GDP at Factor Cost.

Which of the statements given above is/are correct?
(a) 2 and 3 only
(b) 1 and 2 only
(c) 1 and 3 only
(d) 1, 2 and 3

Answer: (a) 2 and 3 only
Explanation:
- Depreciation is not subtracted while calculating GDP at Factor Cost from GDP at Market Price. The correct formula is:
  GDP at Factor Cost = GDP at Market Price – Indirect Taxes + Subsidies
- **NNP at Market Price = NNP at Factor Cost + Indirect Taxes – Subsidies**
- **GNP at Factor Cost = GDP at Factor Cost + Net Income from Abroad (Exports – Imports)**

Source: Laxmikant (Polity)

4. With reference to the GDP Deflator, consider the following statements:
1. The GDP deflator includes both final goods and imports while measuring price changes in the economy.
2. A rise in the GDP deflator indicates an increase in the overall price level in the economy.
3. Real GDP is always higher than Nominal GDP in times of high inflation.

Which of the statements given above is/are correct?
(a) 2 only
(b) 1 and 3 only
(c) 2 and 3 only
(d) 1, 2 and 3

Answer: (a) 2 only
Explanation:
- The GDP deflator includes the value of **final goods including exports** but **excludes imports**, because imports are not produced domestically.
- A higher GDP deflator implies that prices have increased compared to the base year → it's a measure of inflation.
- During inflation, **Nominal GDP > Real GDP** (because Nominal includes inflation, Real removes it).

Source: Laxmikant (Polity)

5. Consider the following statements regarding the Expenditure Method of calculating GDP:
1. Expenditure on intermediate goods is included in GDP since they form part of the production process.
2. In the expenditure method, GDP is calculated as the sum of consumption expenditure, investment, government spending, and net exports.

Which of the statements given above is/are correct?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: B. 2 only
Explanation:

- **Expenditure on intermediate goods is *not included* in GDP** to avoid double-counting. Only **final expenditure** (not meant for further production) is considered in GDP calculations.
- The Expenditure Method formula is:
  GDP = C + I + G + (X – M)
  where:
  - **C** = Final Consumption Expenditure
  - **I** = Investment Expenditure
  - **G** = Government Expenditure
  - **X** = Exports
  - **M** = Imports
- The formula ensures that only **domestically produced final goods and services** are counted.

Source: Laxmikant (Polity)

6. With reference to **Green GDP**, consider the following statements:

1. Green GDP accounts for environmental degradation and depletion of natural resources while measuring economic growth.
2. Green GDP incorporates investments in both carbon-intensive and zero-carbon technologies while evaluating capital formation.
3. Green GDP excludes government revenue and subsidies related to environmental sectors to avoid bias in measurement.

Which of the statements given above is/are correct?
(a) 1 only
(b) 1 and 2 only
(c) 2 and 3 only
(d) 1, 2 and 3

Answer: (b) 1 and 2 only
Explanation:

- Green GDP adjusts traditional GDP by **accounting for environmental degradation** and **resource depletion**.
- Green GDP **differentiates investments** into zero-carbon and carbon-intensive categories.
- It **includes** taxation and subsidies related to polluting and environment-friendly industries to highlight fiscal policy impacts on sustainability.

Source: Laxmikant (Polity)

7. Consider the following statements regarding the treatment of taxes in National Income accounting:

1. Direct taxes do not require any adjustment whether national income is measured at factor cost or market cost.
2. Indirect taxes are deducted from NNP at market cost to arrive at national income at factor cost.

Which of the above statements is/are correct?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: C. Both 1 and 2
Explanation:

- Direct taxes are imposed on income and are accounted for in both factor cost and market cost identically. Hence, no adjustment is needed for national income calculations.
- Indirect taxes are included in market prices. To get the national income at **factor cost**, they must be **deducted** from NNP at market cost.

Source: Laxmikant (Polity)

8. Consider the following statements regarding basic concepts of macroeconomics:

1. Capital goods are final goods that do not undergo transformation during the production process and contribute to future production cycles.
2. Intermediate goods are included in the calculation of national income to ensure a complete measure of economic activity.

Which of the statements given above is/are correct?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: A. 1 only
Explanation:

- Capital goods like machines or tools are final goods used in the production of other goods. They do not get transformed in the production process and are durable, aiding future production.
- Intermediate goods are not included in the calculation of national income because their value is already embedded in the value of final goods. Including them would lead to double counting.

Source: Laxmikant (Polity)

9. Consider the following statements regarding the Product or Value Added Method of measuring National Income:

1. In value added method, the value of intermediate goods is subtracted from the value of output to avoid the problem of double counting.
2. Unplanned accumulation of inventories is excluded from the calculation of Gross Value Added (GVA) as it is not a deliberate production activity.

Which of the statements given above is/are correct?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: A. 1 only
Explanation:

- To avoid double counting, intermediate goods (like raw materials already included in the output of other firms) are subtracted from total output to arrive at Value Added. This ensures only the net contribution of each firm is measured.
- Both planned and unplanned accumulation or decumulation of inventories are included in Gross Value Added because they reflect production activities, even if they are not sold. Inventory changes are treated as part of investment, and hence are included in GDP.

Source: Laxmikant(Polity)

10. Consider the following statements regarding the Income Method of measuring GDP:
1. The income method calculates GDP by summing up all factor incomes such as wages, profits, interest, and rents earned by households from firms.
2. The income method includes only those factor incomes which are received from production activities within the domestic territory of the country.

Which of the statements given above is/are correct?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: C. Both 1 and 2
Explanation:
- GDP by the Income Method = Wages + Profits + Interest + Rents These are the remunerations paid by firms to the factors of production owned by households.
- Only incomes generated within the domestic territory from productive economic activities are included in GDP. Transfer payments (like pensions, gifts) or foreign incomes are excluded from GDP (though they may be relevant for GNP).

Source: Laxmikant (Polity)

Money Supply and Banking

1. Consider the following statements regarding the **money supply and banking system in a modern economy:**
1. High-powered money refers to the currency issued by the central bank and held by the public and commercial banks.
2. Commercial banks are mandated to keep the entire amount of public deposits as reserves and cannot lend them out.

Which of the statements given above is/are correct?
(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (a) 1 only
Explanation:
- High-powered money (also called reserve money or monetary base) refers to the currency issued by the central bank that is held by the public and commercial banks. This forms the basis for credit creation in the economy.
- Commercial banks **do not** keep the entire amount of public deposits as reserves. They retain only a portion (known as reserve ratio) to meet withdrawal demands and **lend out the rest** to earn interest. This process enables credit creation, as described in the story of Lala the goldsmith.

Source: Laxmikant (Polity)

2. **With reference to the nature of Monetary Policy, consider the following statements:**
1. An expansionary monetary policy is used to control inflation by decreasing the money supply and raising interest rates.
2. A contractionary monetary policy aims to reduce inflationary pressure in the economy by tightening liquidity and increasing borrowing costs.

Which of the statements given above is/are correct?
(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (b) 2 only
Explanation:
- Expansionary (or accommodative) monetary policy is aimed at boosting economic activity by **increasing** the money supply and **lowering** interest rates—not for controlling inflation but for stimulating growth and reducing unemployment.
- Contractionary (or tight) monetary policy is adopted to **reduce inflation** by **reducing the money supply** and **increasing interest rates**, thereby discouraging excessive spending and borrowing.

Source: Laxmikant (Polity)

3. **Consider the following statements regarding Open Market Operations (OMO):**
1. When the RBI buys government securities through OMO, it reduces the money supply in the economy.
2. Outright OMO refers to the permanent purchase or sale of government securities without any repurchase agreement.

Which of the statements given above is/are correct?
(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (b) 2 only
Explanation:
- When RBI **buys** government bonds, it **injects** money into the system, thereby **increasing** the money supply.
- Outright OMO implies **permanent** transactions without a repurchase clause.

Source: Laxmikant (Polity)

4. **Which of the following best describes the term 'Repo Rate'?**
(a) The rate at which the RBI permanently sells government securities to commercial banks.
(b) The rate at which the RBI lends to commercial banks through a repurchase agreement.
(c) The rate at which commercial banks lend to the public for housing loans.
(d) The interest rate offered by commercial banks on term deposits.

Answer: (b) The rate at which the RBI lends to commercial banks through a repurchase agreement.
Explanation:
- **Repo Rate** is the interest rate at which the RBI lends to commercial banks through **repurchase agreements**, where it temporarily buys securities with a promise to sell them back.

Source: Laxmikant (Polity)

5. **Consider the following statements regarding instruments used by RBI to control money supply:**
1. An increase in the Cash Reserve Ratio (CRR) by the RBI leads to a reduction in money supply in the economy.
2. The RBI uses moral suasion and margin requirements as qualitative tools to influence lending behaviour of commercial banks.

Which of the statements given above is/are correct?
(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (c) Both 1 and 2
Explanation:
- Increasing CRR reduces the amount available with banks for lending, thus reducing money supply.
- **Moral suasion** and **margin requirements** are qualitative tools used by RBI to **encourage or discourage specific lending behaviour**.

Source: Laxmikant (Polity)

6. Consider the following statements regarding the Monetary Policy Committee (MPC) of India:
1. The Monetary Policy Committee is a statutory body constituted under the RBI Act, 1934 as amended by the Finance Act, 2016.
2. The committee is chaired by the Finance Minister of India and is responsible for targeting wholesale price index (WPI) inflation.

Which of the statements given above is/are correct?
(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (a) 1 only
Explanation:
- The MPC is a **statutory body** formed by amending the **RBI Act, 1934** through the **Finance Act, 2016.** It is tasked with setting the **benchmark interest rate (repo rate)** and guiding monetary policy.
- The **RBI Governor**, not the Finance Minister, is the **ex-officio chairperson** of the MPC. Also, the MPC targets **Consumer Price Index (CPI)-based inflation**, **not WPI**.

Source: Laxmikant (Polity)

7. Which of the following are considered Qualitative Instruments of monetary policy?
1. Repo Rate
2. Moral Suasion
3. Selective Credit Control
4. Cash Reserve Ratio

Select the correct answer using the code below:
(a) 1 and 4 only
(b) 2 and 3 only
(c) 1, 2 and 3 only
(d) 1, 2, 3 and 4

Answer: (b) 2 and 3 only
Explanation:
- **Moral Suasion** and **Selective Credit Control** are qualitative tools used to **influence lending behaviour** and direct credit to preferred sectors.
- **Repo Rate** and **Cash Reserve Ratio** are **quantitative tools** aimed at adjusting the **total money supply**.

Source: Laxmikant (Polity)

8. Which of the following statements regarding instruments of monetary policy is/are correct?
1. **Open Market Operations** are a qualitative instrument used by the RBI to direct credit toward priority sectors.
2. **Statutory Liquidity Ratio (SLR)** is a quantitative instrument that influences the overall credit availability in the economy.

Select the correct answer using the code below:
(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (b) 2 only
Explanation:
- Open Market Operations (OMO) are a **quantitative** instrument, **not qualitative**. They are used to manage the **overall money supply** by buying/selling government securities.
- SLR is a **quantitative tool** used to control the amount of funds banks can use for credit creation. It affects the **total supply of credit** in the economy.

Source: Laxmikant (Polity)

9. Consider the following statements regarding instruments of monetary policy:
1. Moral suasion and selective credit control are qualitative instruments used by the RBI to influence the allocation of credit.
2. The Repo Rate and Cash Reserve Ratio (CRR) are tools used by the RBI to influence the total volume of credit in the economy.

Which of the statements given above is/are correct?
(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (c) Both 1 and 2
Explanation:

- **Moral suasion** and **selective credit control** are **qualitative instruments** used to direct credit flow to or from specific sectors.
- **Repo Rate** and **CRR** are **quantitative instruments** used to regulate the **overall supply of money** or liquidity in the economy.

Source: Laxmikant (Polity)

10. Consider the following statements about quantitative instruments of monetary policy:
1. The **Cash Reserve Ratio (CRR)** and **Statutory Liquidity Ratio (SLR)** are tools used to control liquidity and credit creation by banks.
2. The **Repo Rate** and **Reverse Repo Rate** are tools through which the RBI manages short-term borrowing and lending with commercial banks.

Which of the statements given above is/are correct?
(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (c) Both 1 and 2
Explanation:
- **CRR**: Percentage of total deposits banks must hold as reserves with the RBI—reduces lendable funds.
- **SLR**: Percentage of deposits banks must maintain in liquid assets (like gold, government securities)—controls credit growth and liquidity.
- **Repo Rate**: Rate at which the RBI lends to banks (injects liquidity).
- **Reverse Repo Rate**: Rate at which the RBI borrows from banks (absorbs liquidity).
- These are key quantitative tools used by the RBI for liquidity management and credit control.

Source: Laxmikant (Polity)

GOVERNMENT BUDGET AND THE ECONOMY

1**. With reference to the Government Budget in India, consider the following statements:**
1. The Revenue Budget includes all those receipts and expenditures which are confined to the current financial year and do not affect the government's assets or liabilities.
2. The Capital Budget comprises those items that lead to creation or reduction of government assets and liabilities.

Which of the statements given above is/are correct?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: C. Both 1 and 2
Explanation:
- The **Revenue Budget** deals with the regular, day-to-day income and expenditure of the government during a financial year (1 April to 31 March). These do **not** result in any asset creation or liability for the government.

- The **Capital Budget** includes receipts and expenditures that affect the **assets and liabilities** of the government. These items, such as infrastructure investments or borrowings, often have a multi-year impact beyond the current financial year.

Source: Indian Economy (NCERT)

2**. With reference to the objectives of the Government Budget in India, consider the following statements:**

1. The allocation function of the budget implies the provision of public goods like national defense and pollution control, which are non-rivalrous and non-excludable in nature.
2. The redistribution function of the budget aims to ensure a fair distribution of income by altering personal disposable income through taxation and transfer payments.

Which of the statements given above is/are correct?

A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: C. Both 1 and 2

Explanation:

- The **allocation function** of the government budget deals with the provision of **public goods**, which are **non-rivalrous** (consumption by one does not reduce availability for others) and **non-excludable** (no one can be prevented from enjoying them). Examples include **national defense, public parks, roads, and pollution control**. These goods are not efficiently provided by the market due to the **free-rider problem**, so the government intervenes.
- The **redistribution function** is performed by the government through its budget by collecting **taxes** and making **transfer payments** (such as subsidies, pensions, welfare schemes). This affects the **personal disposable income** and helps reduce inequality in income distribution, aiming for **social justice and economic fairness**.

Source: Indian Economy (NCERT)

3**. With reference to the Stabilisation Function of the Government Budget, consider the following statements:**

1. The stabilisation function aims to correct fluctuations in income, employment, and prices by influencing aggregate demand in the economy.
2. During periods of low demand and underutilization of resources, the government may intervene to reduce aggregate demand through restrictive fiscal measures.
3. In situations of excessive demand and inflation, the government can adopt policies to contract demand and stabilise prices.

Which of the statements given above is/are correct?

A. 1 and 2 only
B. 1 and 3 only
C. 2 and 3 only
D. 1, 2 and 3

Answer: B. 1 and 3 only

Explanation:

- The **stabilisation function** refers to the government's role in maintaining economic stability by correcting **fluctuations in income, employment, and prices**, typically through **fiscal policy** measures that influence **aggregate demand**.
- During **low demand and underutilisation**, the government does **not reduce aggregate demand**. Instead, it adopts **expansionary fiscal policy** (e.g., increased spending or tax cuts) to **raise** aggregate demand and stimulate employment.
- When **demand exceeds output** and inflation arises, the government may implement **restrictive (contractionary)** measures like reducing public expenditure or increasing taxes to **curb excess demand** and bring **stability**.

Source: Indian Economy (NCERT)

4**. With reference to the classification of receipts in the Government Budget, consider the following statements:**

1. Revenue receipts do not create any future liability for the government and are therefore non-redeemable.
2. Capital receipts include both debt-creating sources such as borrowings and non-debt-creating sources such as disinvestment.
3. All forms of tax revenue are progressive in nature and aim to reduce income inequality.

Which of the statements given above is/are correct?

A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: A. 1 and 2 only
Explanation:

- Revenue receipts, such as taxes and non-tax revenues, **do not create any liability** for the government and hence are called **non-redeemable**.
- Capital receipts include both:
  - **Debt-creating receipts** (e.g., borrowings and loans)
  - **Non-debt-creating receipts** (e.g., **disinvestment** of PSUs, which reduces government's financial assets)
- Not all tax revenues are **progressive**.
  - **Direct taxes** like personal income tax can be progressive.
  - However, **indirect taxes** like excise duties or GST are often **regressive**, since they apply equally regardless of income, and may disproportionately affect lower-income groups.

Source: Indian Economy (NCERT)

5**. With reference to the classification of government expenditure in India, consider the following statements:**

1. Revenue Expenditure does not lead to the creation of physical or financial assets and includes interest payments, subsidies, and salaries.
2. Capital Expenditure includes spending that results in the acquisition of assets or reduction of liabilities, such as investments in shares or construction of infrastructure.
3. According to the Fiscal Responsibility and Budget Management Act (FRBMA), revenue expenditure must always be financed through capital receipts and borrowings.

Which of the statements given above is/are correct?

A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: A. 1 and 2 only

Explanation:

- Revenue Expenditure includes expenses that **do not create assets or reduce liabilities**. This includes **interest payments, defence, subsidies, salaries, and pensions**.
- Capital Expenditure includes outlays that **create assets** (e.g., buildings, roads, investments) or **reduce liabilities** (e.g., loan repayments). This type of expenditure enhances the productive capacity of the economy.
  The **FRBMA** encourages **sustainable financing** of revenue expenditure **through revenue receipts**, not capital receipts or borrowings. It seeks to avoid using borrowed money for regular (revenue) expenses.

Source: Indian Economy (NCERT)

6**. With reference to government deficit measures in India, consider the following statements:**

1. Revenue deficit occurs when the government's total expenditure exceeds its total receipts, excluding borrowings.
2. Fiscal deficit represents the total borrowing requirement of the government and includes revenue deficit as a component.
3. Primary deficit helps isolate the current fiscal imbalance by subtracting interest payments from the fiscal deficit.

Which of the statements given above is/are correct?

A. 2 and 3 only
B. 1 and 2 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: A. 2 and 3 only

Explanation:

- **Revenue deficit** = **Revenue Expenditure – Revenue Receipts**
  It refers only to the imbalance in the **revenue account**, not total receipts and expenditures.
- **Fiscal deficit** = **Total Expenditure – (Revenue Receipts + Non-debt creating capital receipts)**.
  It **includes the revenue deficit** and reflects the **total borrowing requirement** of the government.
- **Primary deficit = Fiscal deficit – Net interest liabilities**.
  It gives a measure of **current fiscal imbalance** by excluding the burden of past debt (interest payments).

Source: Indian Economy (NCERT)

7**. Consider the following statements regarding government budgets:**
1. A balanced budget is when government expenditure is equal to its revenue.
2. A budget surplus occurs when government revenue falls short of its expenditure.
3. A budget deficit is a situation where government expenditure exceeds its revenue.

Which of the statements given above is/are **correct**?
A. 1 and 2 only
B. 1 and 3 only
C. 2 and 3 only
D. 1, 2 and 3

Answer: B. 1 and 3 only
Explanation:
- A **balanced budget** means government expenditure equals revenue.
- A **budget surplus** means revenue is **more than** expenditure, not less.
- A **budget deficit** occurs when expenditure **exceeds** revenue.

Source: Indian Economy (NCERT)

8**. Consider the following statements with reference to government budgeting terms:**
1. Receipts include both the money earned by the government and the money it borrows or receives as repayment of loans.
2. Plan expenditure includes routine items like pensions, interest payments, and statutory transfers to states.
3. Non-plan expenditure covers spending on infrastructure projects like electricity, roads, and irrigation.

Which of the statements given above is/are **correct**?
A. 1 only
B. 1 and 2 only
C. 2 and 3 only
D. 1, 2 and 3

Answer: A. 1 only
Explanation:
- "Receipts" include both earned income (like taxes, dividends) and borrowed funds, as well as repayments of loans by states.
- Plan expenditure includes developmental activities like infrastructure, not routine items like pensions or interest payments.
- Non-plan expenditure includes routine and obligatory expenses like pensions and interest payments, not developmental or infrastructure projects.

Source: Indian Economy (NCERT)

9. **Consider the following statements regarding types of budgeting followed by the Government of India:**
1. Zero-Based Budgeting requires justification for all expenditures from a zero base in each new budget cycle.
2. Outcome Budget was introduced in 2005 to link the money allocated to ministries with measurable results.
3. Gender Budgeting focuses solely on increasing the overall budget allocation for women-centric ministries.

Which of the statements given above is/are **correct**?
A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: A. 1 and 2 only
Explanation:
- Zero-Based Budgeting (ZBB) starts from scratch ("zero base") and every expense must be justified anew.
- Outcome Budgeting, introduced in 2005, links budget outlay with the actual performance and results of government schemes.
- Gender Budgeting is not merely about increasing budget allocations for women-specific ministries; it is about integrating a gender perspective across all departments and restructuring expenditures to promote **gender equity**.

Source: Indian Economy (NCERT)

10. **With reference to the Fiscal Responsibility and Budget Management (FRBM) Act, 2003, consider the following statements:**
1. The FRBM Act mandates the elimination of revenue deficit and creation of a revenue surplus thereafter.
2. Under the FRBM Act, the Central Government is allowed to borrow from the RBI only under exceptional circumstances like national security or natural calamity.
3. The FRBM Act requires the government to present a Medium Term Fiscal Policy Statement and Fiscal Policy Strategy Statement before the Parliament annually.

Which of the statements given above is/are **correct**?
A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: D. 1, 2 and 3
Explanation:
- One of the core mandates of the FRBM Act is to eliminate the **revenue deficit** and subsequently create a **revenue surplus**.
- The Act prohibits borrowing from the RBI **except** under certain **exceptional circumstances** like national security and natural calamity.
- As per the **2012 Amendment**, the government must annually present the **Macro-Economic Framework Statement**, **Medium Term Fiscal Policy Statement**, and **Fiscal Policy Strategy Statement** before Parliament along with the **Annual Financial Statement.**

Source: Indian Economy (NCERT)

Open Economy Macroeconomics

1. Which of the following statements best describes an open economy?
A. An economy that does not interact with other economies in any form.
B. An economy that only allows the movement of goods, not financial assets.
C. An economy that engages in trade of goods, services, and often financial assets with other countries.
D. An economy that has no restrictions on the movement of labour across borders.

Answer: C
Explanation:
- An open economy is defined as one that interacts with other countries, primarily through the output market (goods and services) and the financial market (assets).
- While labour market integration exists, it is typically restricted by immigration laws.

Source: Economy (NCERT)

2. Consider the following statements about the impact of foreign trade on aggregate demand in India:
1. Imports lead to a leakage from the circular flow of income, thus decreasing aggregate demand.
2. Exports act as an injection into the circular flow of income, increasing aggregate demand.

Which of the statements given above is/are correct?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: C
Explanation:
- When Indians buy imports, money goes out of the Indian economy — this is a leakage, reducing aggregate demand.
- When foreigners buy Indian exports, money comes into India — this is an injection, increasing aggregate demand.

Source: Economy (NCERT)

3. With reference to the Balance of Payments (BoP), consider the following statements:
1. The Current Account records transactions related to trade in goods, services, and unilateral transfers.
2. Import of goods leads to an increase in domestic demand for goods and services in the country.
3. Remittances sent by citizens living abroad are considered transfer payments in the Current Account.

Which of the statements given above is/are correct?
A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: C. 1 and 3 only
Explanation:
- The Current Account includes trade in goods and services and unilateral transfers (like remittances, gifts, and grants).
- Imports represent expenditure to foreign countries and reduce the *domestic* demand for goods and services as money flows out.

- Remittances from abroad are unilateral transfers and are part of the Current Account under transfer payments.

Source: Economy (NCERT)

4. With reference to the Balance on Current Account in the Balance of Payments (BoP), consider the following statements:

1. A Current Account surplus implies that a country is a net lender to the rest of the world.
2. Balance on Current Account comprises only the trade in goods, i.e., exports and imports.
3. A Current Account deficit occurs when the payments on the current account exceed the receipts.

Which of the statements given above is/are correct?

A. 1 and 2 only
B. 1 and 3 only
C. 2 and 3 only
D. 1, 2 and 3

Answer: B. 1 and 3 only

Explanation:

- A surplus on the current account indicates that the country's receipts exceed its payments, making it a net lender to other countries.
- The Current Account includes both trade in goods (balance of trade) and invisibles (like services, income, and transfers), not just goods.
- A Current Account deficit means payments are more than receipts — the country is a net borrower.

Source: Economy (NCERT)

5. With reference to the Balance of Trade (BOT) and Net Invisibles in the Balance of Payments, consider the following statements:

1. A trade surplus occurs when the value of a country's imports of goods exceeds the value of its exports.
2. Net Invisibles include services like banking and tourism, as well as transfers and factor income.
3. In the Balance of Trade, exports are recorded as credit and imports as debit.

Which of the statements given above is/are correct?

A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: B. 2 and 3 only

Explanation:

- A trade *surplus* occurs when exports exceed imports, not the other way around. The given statement describes a *trade deficit*.
- Net Invisibles include services (like tourism, banking, software), transfers (like remittances), and factor income (like wages and returns on capital).
- In Balance of Trade (BOT), *exports* are recorded as credit and *imports* as debit entries.

Source: Economy (NCERT)

6. **With reference to the Capital Account in the Balance of Payments (BoP), consider the following statements:**
Statement I: Purchase of foreign assets by Indian residents is recorded as a debit item in the Capital Account.
Statement II: A debit entry in the Capital Account represents an inflow of foreign exchange into the country.
Which one of the following is correct?
A. Both Statement I and Statement II are correct, and Statement II is the correct explanation of Statement I.
B. Both Statement I and Statement II are correct, but Statement II is not the correct explanation of Statement I.
C. Statement I is correct, but Statement II is incorrect.
D. Statement I is incorrect, but Statement II is correct.

Answer: C. Statement I is correct, but Statement II is incorrect.
Explanation:
- When Indian residents purchase foreign assets (like buying a UK car company), it leads to an outflow of foreign exchange and is therefore recorded as a **debit** in the Capital Account.
- A **debit** entry in the Capital Account implies **outflow** of foreign exchange, not an inflow.

Source: Economy (NCERT)

7. **With reference to the Balance on Capital Account in the Balance of Payments (BoP), consider the following statements:**
1. A surplus in the Capital Account indicates that a country is receiving more capital from abroad than it is sending out.
2. Capital Account is said to be in balance when the total capital inflows equal the total capital outflows.

Which of the statements given above is/are correct?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: C. Both 1 and 2
Explanation:
- A surplus in the Capital Account occurs when **capital inflows > capital outflows**, meaning the country is receiving more investment or borrowing from abroad than it is paying out.
- When **capital inflows = capital outflows**, the Capital Account is said to be in balance.

Source: Economy (NCERT)

8. **With reference to Balance of Payments (BoP) Surplus and Deficit, consider the following statements:**
1. A Current Account deficit must be financed either through capital account surplus or official reserve sales.
2. In a BoP equilibrium, a Current Account deficit is exactly matched by a Capital Account surplus with no change in official reserves.
3. An increase in official reserves by the central bank indicates a Balance of Payments deficit.

Which of the statements given above is/are correct?
A. 1 and 2 only
B. 1 and 3 only
C. 2 and 3 only
D. 1, 2 and 3

Answer: A. 1 and 2 only

Explanation:

- A Current Account deficit (when a country imports more than it exports) must be financed through *capital inflows* or *drawing down foreign exchange reserves*.
- BoP is in equilibrium when the Current Account deficit is fully matched by a Capital Account surplus (no net change in official reserves).
- An *increase* in official reserves (i.e., accumulation of foreign exchange) implies a *BoP surplus*, not a deficit. A *decrease* in reserves indicates a deficit.

Source: Economy (NCERT)

9**. With reference to the Foreign Exchange Rate in an open economy, consider the following statements:**

1. An increase in the foreign exchange rate makes imports costlier and tends to reduce the demand for foreign exchange.
2. A higher foreign exchange rate can make a country's exports cheaper for foreigners and may lead to an increased supply of foreign exchange.
3. The demand for foreign exchange increases when foreigners buy domestic financial assets.

Which of the statements given above is/are correct?

A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: A. 1 and 2 only
Explanation:

- When the foreign exchange rate rises (e.g., ₹ becomes weaker vs $), imports become costlier in rupees, reducing demand for imports and thereby foreign exchange.
- A higher forex rate makes Indian goods cheaper for foreign buyers (in dollar terms), potentially boosting exports and increasing foreign exchange supply.
- When **foreigners** buy **Indian financial assets**, it leads to an **inflow** of foreign exchange (i.e., it affects **supply**, not demand). Demand for forex increases when **Indians** buy foreign assets.

Source: Economy (NCERT)

10**. With reference to the Flexible Exchange Rate system, consider the following statements:**

1. In a flexible exchange rate regime, the value of a currency is determined entirely by the forces of demand and supply in the foreign exchange market.
2. An increase in demand for foreign currency leads to depreciation of the domestic currency under a flexible exchange rate regime.
3. Central banks frequently intervene in the foreign exchange market to stabilize the exchange rate in a purely flexible exchange rate system.

Which of the statements given above is/are correct?

A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: A. 1 and 2 only
Explanation:

- Under a **flexible (floating)** exchange rate system, the exchange rate is determined purely by market forces — i.e., **demand and supply** of foreign exchange — without government or central bank interference.
- When demand for foreign currency (like the US dollar) increases, the domestic currency (like the Indian rupee) **depreciates** because more rupees are needed to buy the same amount of dollars.
- In a **purely flexible exchange rate system**, **central banks do not intervene**. Intervention happens under **managed float** or **fixed** exchange rate systems.

Source: Economy (NCERT)

Inflation and Business Cycle

1. With reference to inflation, consider the following statements:

1. Inflation is said to occur only when there is a general and sustained increase in the prices of most goods and services in an economy.
2. A rise in the price of a single essential commodity can also be considered inflation.

Which of the statements given above is/are correct?

(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (a) 1 only
Explanation:

- Inflation is defined as a sustained rise in the general price level of most goods and services, not just a few items.
- An increase in the price of a single commodity does not constitute inflation.

Source: Indian economy (Dr.Ramesh Singh)

2. Consider the following statements regarding the measurement and concept of inflation:

1. Inflation is measured using price indices such as the Wholesale Price Index (WPI) and Consumer Price Index (CPI).
2. In contemporary economics, deflation always refers to a fall in the general price level of goods and services.

Which of the statements given above is/are correct?

(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (a) 1 only
Explanation:

- Inflation is measured using indices like WPI and CPI, which are weighted averages of price changes in a basket of goods.
- In modern macroeconomic policy terms, deflation or disinflation does not necessarily mean a fall in price levels; rather, it refers to a fall in the inflation rate or a slowing down of price increases.

Source: Indian economy (Dr.Ramesh Singh)

3. **With reference to the monetarist view on inflation, consider the following statements:**

1. Demand-pull inflation occurs when excess money is created without a corresponding increase in production.
2. Cost-push inflation cannot occur without an increase in money supply.

Which of the statements given above is/are correct?

(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (c) Both 1 and 2
Explanation:

- Demand-pull inflation means excess money creation over the same level of production causes inflation.
- Cost-push inflation is not independent and requires financing through additional money supply; without it, rising costs would lead to lower demand, not inflation.

Source: Indian economy (Dr.Ramesh Singh)

4. **According to monetarist theory, which of the following is the most appropriate tool to control inflation?**

(a) Wage increase for workers
(b) Increase in government expenditure
(c) Tight monetary policy
(d) Higher subsidies for essential goods

Answer: (c) Tight monetary policy
Explanation:

- Monetarists believe inflation is caused by excessive money supply.
- Therefore, controlling inflation requires tightening monetary policy—through measures like raising interest rates, reducing money printing, and limiting public borrowing.

Source: Indian economy (Dr.Ramesh Singh)

5. Which of the following best describes 'Galloping Inflation'?

(a) A gradual rise in the general price level, typically in the range of 1–5% annually
(b) A sharp but temporary increase in prices, followed by quick stabilisation
(c) A rapid increase in prices at double- or triple-digit annual rates, typically between 10% and 50%, severely affecting economic stability and purchasing power
(d) A fall in the general price level sustained over time, often indicating economic contraction

Answer: (c)
Explanation:

- **Galloping inflation** is a **rapid increase in prices** at double- or triple-digit annual rates, typically between **10% and 50% annually**.
- It disrupts macroeconomic balance and harms consumer purchasing power.

Source: Indian economy (Dr.Ramesh Singh)

6. Consider the following statements regarding Hyperinflation:

1. Hyperinflation involves an extremely rapid and accelerating rise in prices, sometimes reaching millions or trillions percent annually.
2. During hyperinflation, people often lose faith in the domestic currency and resort to alternative stores of value like gold, foreign currency, or barter.

Which of the statements given above is/are correct?

(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (c) Both 1 and 2

Explanation:

- Hyperinflation is described as a situation where prices rise **extremely fast**, often in the **millions or trillions annually**. For eg, Germany (1923), Bolivia (1985), and Yugoslavia (1993).
- Due to the collapse in the value of money, people **lose confidence in the domestic currency** and shift to **gold, foreign currency, or barter**, seeking inflation-proof assets.

Source: Indian economy (Dr.Ramesh Singh)

7. **Consider the following statements:**

1. An inflationary gap arises when total government spending exceeds national income, leading to a fiscal deficit and increased price levels.
2. A deflationary gap occurs when total government spending falls short of national income, causing a fiscal surplus and potential economic slowdown.

Which of the statements given above is/are correct?

(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (c) Both 1 and 2

Explanation:

- An **inflationary gap** represents a **fiscal deficit** situation where government spending exceeds national income. This injects excess money into the economy, leading to **demand-pull inflation** and price rise.
- A **deflationary gap** is a **fiscal surplus** situation where government spending is less than the national income, leading to **reduced demand**, underutilised capacity, and potential **economic slowdown** or output gap.

Source: Indian economy (Dr.Ramesh Singh)

8. **Consider the following statements:**
1. Reflation refers to government efforts to boost demand and reduce unemployment through higher spending, tax cuts, or interest rate reductions.
2. Stagflation is a situation where high inflation and high unemployment exist together, often with low economic growth.

Which of the statements given above is/are correct?
(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Answer: (c) Both 1 and 2
Explanation:
- Reflation is a **deliberate government policy** to revive a sluggish or recession-hit economy by increasing **public spending, cutting taxes, or reducing interest rates**, even if it temporarily raises inflation.
- **Stagflation** is an unusual economic condition where **inflation and unemployment are both high**, along with **low or stagnant growth**, contradicting the Phillips Curve. It was first observed in the **1970s in the US** due to oil shocks.

Source: Indian economy (Dr.Ramesh Singh)

9. Consider the following statements:
Statement I: GDP deflator is considered a better measure of inflation than the Wholesale Price Index (WPI) in India.
Statement II: GDP deflator includes prices of all goods and services produced in the economy, while WPI does not adequately cover the service sector.
Which one of the following is correct with respect to the above statements?
(a) Both Statement I and Statement II are correct, and Statement II is the correct explanation of Statement I
(b) Both Statement I and Statement II are correct, but Statement II is not the correct explanation of Statement I
(c) Statement I is correct, but Statement II is incorrect
(d) Statement I is incorrect, but Statement II is correct

Answer: (a) Both Statement I and Statement II are correct, and Statement II is the correct explanation of Statement I
Explanation:
- The **GDP deflator** is often considered a better and broader measure of inflation than WPI because it reflects price changes across the entire economy.
- Unlike **WPI**, which largely covers goods and gives little weight to services, the **GDP deflator** includes both **goods and services**, making it more comprehensive.

Source: Indian economy (Dr.Ramesh Singh)

10. Consider the following statements:
Statement I: Demand-pull inflation arises when demand for goods and services exceeds the economy's ability to produce them.
Statement II: An increase in input costs or disruption in commodity supply chains is the primary cause of demand-pull inflation.
Which one of the following is correct with respect to the above statements?
(a) Both Statement I and Statement II are correct, and Statement II is the correct explanation of Statement I
(b) Both Statement I and Statement II are correct, but Statement II is not the correct explanation of Statement I
(c) Statement I is correct, but Statement II is incorrect
(d) Statement I is incorrect, but Statement II is correct

Answer: (c) Statement I is correct, but Statement II is incorrect
Explanation:
- **Demand-pull inflation** occurs when **rising demand**, driven by increased money supply and credit, **outpaces the economy's capacity to produce**, pushing prices upward.
- The cause described in Statement II refers to **cost-push inflation**, where inflation results from **rising production costs** or **supply shocks**, not demand.

Source: Indian economy (Dr.Ramesh Singh)

Inflation and Business Cycle

1. Consider the following statements regarding the Wholesale Price Index (WPI) in India:
1. The WPI compiled by the Central Statistical Organisation (CSO).
2. The WPI primarily captures price changes at the production or primary transaction stage and not at the consumption stage.
3. The WPI is compiled weekly and is based on price quotations for selected items collected through both official and non-official sources.

Which of the statements given above is/are correct?
A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: B. 2 and 3 only
Explanation:
- The Wholesale Price Index (WPI) series with base 1993-94 is compiled by the Office of Economic Adviser (OEA),
- WPI reflects price changes **at the producer or primary transaction stage**, such as farm-gate, mine-head, or factory-gate prices, and **does not capture retail margins or consumption-side inflation**.
- The WPI is compiled **weekly** and uses **price quotations from both official and non-official sources**, although this voluntary method has been criticized for timeliness and non-response issues.

Source: Indian economy (Dr.Ramesh Singh)

2. Consider the following statements regarding the Consumer Price Index (CPI) in India:
1. The CPI measures price changes from the perspective of a wholesale trader.
2. The CPI (Rural) is compiled by the National Statistical Office (NSO).
3. The CPI includes sub-groups such as food and beverages, fuel and light, housing, and clothing.

Which of the statements given above is/are correct?
A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: B. 2 and 3 only
Explanation:
- The CPI measures price changes **from the perspective of a retail buyer (consumer)**, not a wholesale trader. That is the domain of the WPI (Wholesale Price Index).
- The **CPI (Rural/Urban/Combined)** is compiled by the **NSO**, which is under the **Ministry of Statistics and Programme Implementation (MoSPI)**.
- The CPI includes multiple sub-groups, including **food and beverages, fuel and light, housing, and clothing, bedding and footwear**, which reflect retail consumption patterns.

Source: Indian economy (Dr.Ramesh Singh)

3. Consider the following statements regarding the Consumer Price Index for Urban Non-Manual Employees (CPI-UNME):
1. The CPI-UNME is primarily used for computing dearness allowance for government employees in India.
2. It is used under the Income Tax Act to determine capital gains.
3. Data for CPI-UNME is collected monthly across selected centres in India with a time lag of two weeks.

Which of the statements given above is/are correct?
A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: B. 2 and 3 only
Explanation:
- CPI-UNME is **not primarily used for computing DA of government employees**. It is used **for determining DA for employees of some foreign companies operating in India** like embassies, airlines, and financial institutions.
- **CPI-UNME is used under the Income Tax Act to determine capital gains**, particularly for indexing the cost of acquisition in long-term capital gains.
- Data is collected for **365 commodities** at **59 centres**, **monthly**, with a **two-week time lag**.

Source: Indian economy (Dr.Ramesh Singh)

4. With reference to **Structural (Bottleneck) Inflation** in India, consider the following statements:
1. Structural inflation is primarily demand-driven and arises due to excessive consumer spending in the economy.
2. It is caused by a mismatch between rising demand and inadequate supply due to lack of investible capital.
3. Higher government expenditure in non-developmental areas contributes to low growth and persistent inflation.

Which of the statements given above is/are correct?

A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: **B. 2 and 3 only**

Explanation:
- Structural inflation is **not primarily demand-driven** in the usual Keynesian sense. Instead, it results from **supply-side bottlenecks**, such as **insufficient capital, poor infrastructure, and production constraints**, typical of a **developing economy** like India.
- **I**nflation occurs due to **rising demand with inadequate supply**, stemming from a **lack of investible capital** — the defining feature of **structural inflation**.
- **Even when the government managed higher expenditure**, much of it went to **non-developmental areas**, which leads to **low growth alongside high inflation** — a sign of stagnation.

5. With reference to the phases of the business cycle, consider the following statements:
1. The peak stage is marked by the highest level of economic growth and maximum employment before the economy starts to contract.
2. During a recession, key economic indicators such as GDP, corporate profits, and employment tend to rise steadily.

Which of the statements given above is/are correct?

A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: **A. 1 only**

Explanation:
- The **peak stage** is when all economic indicators (GDP, employment, prices, etc.) are at their **maximum levels**. After this, the economy usually **enters a contraction or recession phase**.
- In a **recession**, economic indicators like **GDP, profits, and employment fall**, not rise. There is a general **slowdown or contraction in economic activity**.

6. With reference to the business cycle, consider the following statements:
1. A depression is identified by a decline in real GDP of at least 10% in a given year or a severe downturn lasting three or more years.
2. A trough represents the point of maximum economic activity before the economy enters a recovery phase.

Which of the statements given above is/are correct?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: **A. 1 only**

Explanation:
- A **depression** is a **severe and prolonged recession**. Economically, it's defined by either a **decline in real GDP of 10% or more in a year**, or a **recession lasting three or more years**.
- A **trough** is the **lowest point of economic activity**, **not the point of maximum** activity. It **marks the end of depression** or recession and the beginning of **recovery**, not the peak.

7. With reference to the economic phases of **Recovery**, **Expansion**, and **Boom**, consider the following statements:
1. Recovery marks the turnaround of the economy after a recession, characterized by low prices and increasing production.
2. Expansion is the final stage of the business cycle, occurring just before a trough.
3. Boom is a phase of high GDP growth and commercial activity, typically following the recovery phase.

Which of the statements given above is/are correct?
A. 1 and 2 only
B. 1 and 3 only
C. 2 and 3 only
D. 1, 2 and 3

Answer: **B. 1 and 3 only**

Explanation:
- **Recovery** follows a recession/depression. It is characterized by **low prices** (from the downturn), **rising demand**, **growing production**, and **falling unemployment**.
- **Expansion is not the final stage** of the business cycle. It is an **early phase** that follows recovery and leads to the **peak or boom**. The **final stage before a trough** is typically **recession**, not expansion.
- **Boom** is marked by **significant economic growth**, rising **GDP, employment, and demand.** It usually **follows recovery and expansion**, before potentially leading into overheating and a new downturn.

8. With reference to a **Double-Dip Recession**, consider the following statements:
1. A double-dip recession refers to two consecutive quarters of negative GDP growth within the same business cycle.
2. It typically involves a brief recovery followed by another downturn, often worsened by reduced consumer demand and spending cutbacks.

Which of the statements given above is/are correct?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: **B. 2 only**

Explanation:

- Two consecutive quarters of negative GDP growth **define a standard recession**, not specifically a double-dip. A **double-dip recession** occurs when an economy **first enters recession, then recovers briefly, and then dips into recession again — not just two back-to-back negative quarters**.
- A **double-dip recession** is marked by a **short-lived recovery followed by another recession**, often caused by weak demand due to **layoffs and prior spending cuts**, as explained in the passage.

9. Which of the following are consequences of inflation on **creditors and lending institutions**?
1. Creditors suffer losses as loans are repaid in depreciated currency.
2. Inflation introduces the need to factor in Time Value of Money (TVM) while determining interest rates.
3. Inflation leads to reduction in nominal interest rates to ease credit flow in the economy.

A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: A. 1 and 2 only
Explanation:
- Creditors (lenders) **lose** during inflation because repayments are made in **money of lower purchasing power**.
- Inflation impacts lending through **Time Value of Money (TVM)**, which influences **interest rates**.
- N**ominal interest rates often rise** during inflation to **compensate for inflation risk**, not fall.

10. Which of the following is/are valid **macroeconomic consequences** of high inflation?
1. It redistributes income from people on fixed incomes to those with variable incomes.
2. It increases exports due to rising domestic prices.
3. It adds inefficiencies in the market, discouraging long-term planning and investment.

A. 1 and 2 only
B. 1 and 3 only
C. 2 and 3 only
D. 1, 2 and 3

Answer: B. 1 and 3 only
Explanation:
- Inflation **hurts people on fixed incomes** (like pensioners) and **benefits those with variable incomes**, causing **redistributive effects**.
- **High inflation makes exports costlier**, reducing export competitiveness and **increasing imports**, which leads to a **trade deficit**.
- Inflation causes **market inefficiencies**, making it hard for businesses to **budget or invest long-term**.

INDIAN FINANCIAL MARKET

1.Consider the following statements regarding the **Indian Money Market**:
1. The discount rate in the money market is guided by the repo rate announced by the RBI.
2. Money market instruments typically have a maturity period exceeding one year.
3. Borrowings in the money market are always backed by collateral.

Which of the statements given above is/are **correct**?
A. 1 only
B. 1 and 2 only
C. 2 and 3 only
D. 1, 2 and 3

Answer: A. 1 only
Explanation:
- The repo rate announced by the RBI guides the discount rate in the money market.
- Money market instruments are for short-term needs, with maturities **up to 364 days**.
- Borrowings **may or may not** be backed by collateral.

Source: Indian Economy (Dr. Ramesh Singh)

2. With reference to the **Unorganised Money Market in India,** consider the following statements:
1. Nidhis and chit funds are examples of unregulated non-bank financial intermediaries.
2. Indigenous bankers in India operate as homogenous groups across regions.
3. All unorganised money market entities in India are outside the recognition of the government.

Which of the statements given above is/are **correct**?
A. 1 only
B. 1 and 2 only
C. 2 and 3 only
D. 1 and 3 only

Answer: A. 1 only
Explanation:
- Chit funds and nidhis are unregulated NBFCs that function as part of the unorganised money market.
- Indigenous bankers are **non-homogenous**, with region-specific types like Gujarati Shroffs, Chettiars, etc.
- Unorganised entities like chit funds are **recognised** by the government even if not regulated.

Source: Indian Economy (Dr. Ramesh Singh)

3. With reference to the **instruments of the organised money market** in India, consider the following statements:
1. Treasury Bills of 14-day maturity are still issued by the Government of India.
2. Certificates of Deposit (CDs) are tradable instruments issued only by commercial banks.
3. Commercial Paper (CP) can be issued only by listed companies with a minimum working capital of ₹3 crore.

Which of the statements given above is/are **correct**?
A. 1 and 2 only
B. 2 and 3 only
C. 3 only
D. 1, 2 and 3

Answer: C. 3 only
Explanation:

- The 14-day Treasury Bills (both intermediate and auctionable) were **discontinued in 2001**. Currently, only the 91-day, 182-day, and 364-day TBs are issued.
- While CDs were initially issued only by banks, **since 1993**, certain financial institutions like IFCI, IDBI, and Exim Bank can issue CDs for periods **above 1 year**.
- Only **listed companies with a minimum working capital of ₹3 crore** and approved credit rating can issue **Commercial Paper**.

Source: Indian Economy (Dr. Ramesh Singh)

4. Consider the following statements about **instruments introduced in the Indian money market** after the 1990s:

1. Call Money Market allows borrowing and lending of funds for up to 14 days and is mainly used by banks and mutual funds.
2. Cash Management Bills (CMBs) were introduced to provide the government flexibility in meeting temporary cash flow mismatches.
3. Reverse Repo transactions involve RBI purchasing government securities from commercial banks.

Which of the statements given above is/are **correct**?

A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: D. 1, 2 and 3
Explanation:

- The **Call Money Market** is an inter-bank market where funds are borrowed and lent for **up to 14 days**. LIC, GIC, and mutual funds can participate **only as lenders**.
- **Cash Management Bills (CMBs)** were introduced in **August 2009** to allow the government to meet **short-term mismatches** in cash flow, with **maturities less than 91 days**.
- In **Reverse Repo**, the RBI **sells securities to banks**, which effectively means **RBI is borrowing** from them. The banks **purchase government securities**, and later, the RBI buys them back.

Source: Indian Economy (Dr. Ramesh Singh)

5. With reference to **Mutual Funds in India**, consider the following statements:

1. Exchange-Traded Funds (ETFs) are always traded at a significant discount to their Net Asset Value (NAV).
2. Mutual Funds are regulated by both RBI and SEBI, but are compulsorily registered with SEBI.
3. In a balanced mutual fund scheme, the proportion of investments in loan and share markets may be adjusted depending on market conditions.

Which of the statements given above is/are **correct**?

A. 2 and 3 only
B. 1 and 3 only
C. 2 only
D. 1, 2 and 3

Answer: A. 2 and 3 only
Explanation:

- ETFs **are traded close to their NAV**, not necessarily at a significant discount. In fact, compared to close-ended funds (which often trade at a discount), ETFs are designed to mirror NAV more closely.

- Mutual Funds were first introduced in the **money market** (under RBI), but they operate in both money and capital markets. Thus, they have **dual regulation**, but they are **compulsorily registered with SEBI**, which acts as the primary regulator for investor protection.
- **Balanced schemes** typically invest around **60% in the loan market and 40% in the share market**, but this ratio can be **adjusted based on the market situation**, as disclosed by the fund.

Source: Indian Economy (Dr. Ramesh Singh)

6. Consider the following statements regarding **Mutual Fund schemes** in India:
1. Open-ended mutual fund schemes allow investors to buy and sell units on an ongoing basis at NAV-based prices.
2. Closed-ended mutual fund schemes can be redeemed only on the stock exchange at market-determined prices before maturity.
3. Net Asset Value (NAV) is calculated as the total value of assets in the fund divided by the total number of units issued.

Which of the statements given above is/are **correct**?
A. 1 and 2 only
B. 1 and 3 only
C. 2 and 3 only
D. 1, 2 and 3

Answer: B. 1 and 3 only
Explanation:
- Open-ended schemes **allow investors to buy/sell units at any time** directly from the fund at prices based on the **Net Asset Value (NAV)**.
- While closed-ended schemes are **traded on stock exchanges**, investors **are not required to redeem only through exchange**. Redemption can occur at maturity, and schemes may be converted into open-ended funds as well.
- NAV is defined as the **total value of investments** in a scheme **divided by the number of units** issued.

Source: Indian Economy (Dr. Ramesh Singh)

7. With reference to the **Call Money Market** in India, consider the following statements:
1. The call money market deals with collateralised borrowing and lending for a period of up to 7 days.
2. Scheduled commercial banks, cooperative banks, and primary dealers participate in the call money market.
3. The Reserve Bank of India specifies prudential limits for participants in the call money market.

Which of the statements given above is/are **correct**?
A. 1 and 2 only
B. 2 and 3 only
C. 1 and 3 only
D. 1, 2 and 3

Answer: B. 2 and 3 only
Explanation:
- The **call money market** deals with **uncollateralised overnight borrowing and lending** (not for up to 7 days, and not collateralised).
- **Scheduled Commercial Banks** (excluding RRBs), **cooperative banks** (except land development banks), and **primary dealers** participate in the market.
- The **RBI specifies prudential limits** on borrowing and lending for each participating entity, as per its guidelines.

Source: Indian Economy (Dr. Ramesh Singh)

8.With reference to **Open Market Operations (OMOs)**, consider the following statements:
1. OMOs involve the sale or purchase of government securities with the objective of controlling rupee liquidity in the market.
2. The effectiveness of OMOs as a monetary policy tool is limited by the availability of government securities with the RBI.

Which of the statements given above is/are **correct**?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: C. Both 1 and 2
Explanation:
- OMOs are used by the RBI to **modulate rupee liquidity** by **buying or selling government securities**.
- The **stock of G-Secs** with the RBI limits its ability to conduct OMOs freely.

Source: Indian Economy (Dr. Ramesh Singh)

9. With reference to the **Liquidity Adjustment Facility (LAF)**, consider the following statements:
1. The LAF allows the RBI to manage liquidity in the banking system on a daily basis through repo and reverse repo operations.
2. Under the reverse repo operation, banks borrow funds from the RBI by pledging securities at a fixed interest rate.

Which of the statements given above is/are **correct**?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: A. 1 only
Explanation:
- The **LAF is a daily liquidity management tool**, allowing the **RBI to lend or borrow** via **repo (inject liquidity)** and **reverse repo (absorb liquidity)** operations.
- Under **reverse repo**, it is the **RBI that borrows funds from banks**, not the other way around. This helps **drain excess liquidity** from the system.

Source: Indian Economy (Dr. Ramesh Singh)

10. With reference to the **differences between the Money Market and the Capital Market in India**, consider the following statements:
1. Transactions in the capital market involve fewer formalities and are conducted without the use of stock exchanges.
2. The money market deals with financial instruments having a maturity period of up to 1 year and is primarily regulated by the RBI.

Which of the statements given above is/are **correct**?
A. 1 only
B. 2 only
C. Both 1 and 2
D. Neither 1 nor 2

Answer: B. 2 only
Explanation:

- **Capital market transactions** are **well-regulated and conducted through stock exchanges**. Fewer formalities apply to the **money market**, not the capital market.
- The **money market** indeed deals with **short-term instruments** (maturity up to 1 year) and is **closely regulated by the RBI**.

Source: Indian Economy (Dr. Ramesh Singh)