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INDIAN ECONOMY

for

State Engineering Services Exams, SSC, PSUs, Banking, RRB and Other Exams

by Mr. B. Singh

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Preface

This comprehensive textbook on **Indian Economy** provides all the requirements of the students, i.e., comprehensive coverage of theory, fundamental concepts and objective type questions articulated in a lucid language. This concise presentation will help the readers grasp the topics of **Indian Economy** with clarity and apply them with ease to solve objective questions quickly.

This book covers the syllabus of States Engineering Services Exams including APPSC, MPPSC, MPSC, BPSC, UPPSC; SSC, PSUs, Banking, RRB and other examinations. All the topics are given the emphasis they deserve so that mere reading of the book clarifies all the concepts. The book incorporates theory as well as previous years' questions of various State Engineering Services Examinations, UPSC ESE, etc. It also contains plenty of objective type questions for practice. This book has been very well targeted for aforementioned exams covering all the aspects of subject matter required for these examinations.

We have put-in our sincere efforts to present detailed theory and MCQs without compromising the accuracy of answers. For the interest of the readers, some notes, do you know and interesting facts are given in the comprehensive manner.

Our team has made their best efforts to remove all possible errors of any kind. Nonetheless, we would highly appreciate and acknowledge if you find and share with us any printing and conceptual errors. It is impossible to thank all the individuals who helped us, but we would like to sincerely thank all the authors, editors and reviewers for putting-in their efforts to publish this book.

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INDIAN ECONOMY

1 BASICS OF ECONOMY

Introduction

Economics is the science of analyzing the production, distribution and consumption of goods and services. In other words, what choices people make; how and why they make them when making purchases.

The study of economics can be categorized into Microeconomics and Macroeconomics.

- **Microeconomics** is the study of economics at the individual or business level; how individual people or businesses behave given scarcity and government intervention. Microeconomics includes concepts such as supply and demand, price elasticity, quantity demanded and quantity supplied.
- **Macroeconomics** is the study of the performance and structure of the whole economy rather than individual markets. Macroeconomics includes concepts such as inflation, international trade, unemployment, and national consumption and production.

Factors of Production

Factors of production is an economic term to describe the inputs that are used in the production of goods or services in the attempt to make an economic profit.

The factors of production include land, labour, capital and entrepreneurship.

The factors of production

1. Land : Natural resources
2. Labour : Human skill and effort
3. Capital : Equipment and materials
4. Enterprise : Organisation and undertaking production

Together produce goods and services

Land

- Land is an economic resource encompassing natural resources found within a nation's economy. This resource includes timber, land, fisheries, farms and other similar natural resources.
- Land is usually a limited resource for many economies. Example: India has 15% of the global population but only 2.4% of the global land.

Labour

- Labour represents the human capital available to transform raw material or national resources into consumer goods.
- Human capital includes all able-bodied individuals capable of working in the nation's economy and providing various services to other individuals or businesses.
- This factor of production is a flexible resource as workers can be allocated to different areas of the economy for producing consumer goods or services.

MICROECONOMICS 2

Introduction

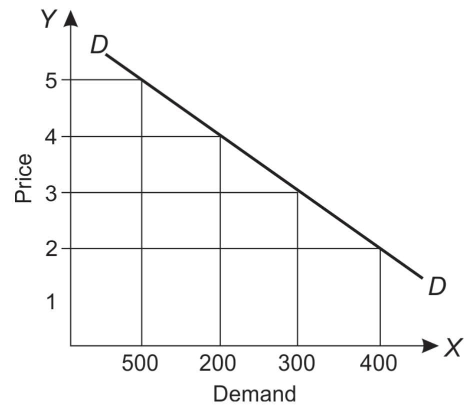
Microeconomics is the study of economic tendencies, or what is likely to happen when individuals make certain choices or when the factors of production change. Individual actors are often broken down into micro-economic subgroups, such as buyers, sellers and business owners.

Demand Curve

The demand curve is a relation between the quantity of the good chosen by a consumer and the price of the good. The independent variable (price) is measured along the vertical axis and dependent variable (quantity) is measured along the horizontal axis. The demand curve gives the quantity demanded by the consumer at each price.

Law of Demand

- Law of Demand states that the other factors remaining constant, price and quantity demanded of any good and services are inversely related to each other. When the price of a product increases, the demand for the product will fall.
- In other words, higher price leads to a lower quantity demanded and that a lower price leads to a higher quantity demanded, assuming the other factors affecting demand remain constant. The given below diagram explains the law of demand clearly:
- As the Price of commodity decreases from ` 5 to ` 2, the quantity demanded of the commodity increases from 100 units to 400 units.



Income Effect and Substitution Effect

- **The substitution effect** is the economic understanding that as prices rise — or income decreases — consumers will replace more expensive items with less costly alternatives.
- Conversely, as the wealth of individuals increases, the opposite tends to be true, as lower-priced or inferior commodities are eschewed for more expensive, higher-quality goods and services, known as the **income effect**.

Giffen Goods

- A Giffen good is a good for which demand increases as the price increases, and falls when the price decreases. A Giffen good has an upward-sloping demand curve, as shown in the graph, which is contrary to the fundamental law of demand.

- A Giffen good is typically an inferior good that does not have easily available substitutes, as a result of which the income effect dominates the substitution effect.
- Staple foods are an example of Giffen Goods. They are consumed by people living in poverty for the sole reason that they are unable to afford superior foodstuffs. As the price of a staple food rises, consumers are unable to supplement their diet with the more expensive foods, causing demand to increase as the price of the staple food increases.

Veblen Goods

- A good for which demand increases as the price increases, because of its exclusive nature and appeal as a status symbol.
- However, a Veblen good is generally a high-quality, coveted product, in contrast to a Giffen good which is an inferior product that does not have easily available substitutes. As well, the increase in demand for a Veblen good reflects consumer tastes and preferences, unlike a Giffen good, where higher demand is directly attributable to the price increase.

Demand Elasticity (DE)

Demand elasticity refers to how sensitive the demand for a good is to changes in other economic variables, such as the prices and consumer income. Demand elasticity is calculated by taking the percent change in quantity of a good demanded and dividing it by a percent change in another economic variable. Higher demand elasticity for a particular economic variable means that consumers are more responsive to changes in this variable, such as price or income.

- **Case 1: DE > 1,** it is called elastic that is it reacts proportionately higher to changes in other economic factors.
- **Case 2: DE < 1,** it is called inelastic and the demand reacts proportionately lower to changes in another variable.

Types of Demand Elasticity

1. Cross Elasticity of demand

The measure of responsiveness of the demand for a good towards the change in the price of a related good is called cross price elasticity of demand. It is always measured in percentage terms.

- **Substitute Goods:** The cross elasticity of demand for substitute goods is always positive because the demand for one good increases if the price for the other good increases.
- **Complementary Goods:** The cross elasticity of demand for complementary goods is negative. As the price for one goods increases, an item closely associated with that item and necessary for its consumption decreases because the demand for the main good has also dropped.

2. Price Elasticity of Demand

Price elasticity of demand is a measure of the relationship between a change in the quantity demanded of a particular good and a change in its price. The degree to which rising price translates into falling demand is called demand elasticity or price elasticity of demand.

ECONOMIC PLANNING IN INDIA

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Introduction

Planned economy is one in which the state owns (partly or wholly) and directs the economy. Economic planning meant allocation of limited resources among different users in such a way so to promote maximum welfare of the people. Given the low rate of savings and structural limitations in converting savings to investment, it was felt that basic question of how much to save, where to invest, and in what forms to invest could be best handled with the help of a plan.

Types of Planning

Types of Planning	
Planning	**Features**
Planning by Direction	• In planning by direction, targets of plans are pre-determined and executed with the help of the government in power. • In this form of planning all the important positions and decisions are taken by the state. State directly controls financial institutions, the industrial sector, transport, and infrastructure.
Planning by Inducement	• In planning by inducement the government tries to achieve its objectives by influencing investment decisions of the entrepreneurs by offering the necessary incentives. It means Planning by manipulating the market. • Government has full control over certain sectors like atomic energy, defense while in certain other sectors like agriculture, small scale and cottage industries etc. the private sector is given many incentives.
Democratic Planning	• In Democratic planning, plans are prepared according to the requirements and needs of the people. • A democratic plan is prepared after discussion with various stakeholders involved in the economy- government agencies, civil society or private enterprises. • Main goal of democratic planning is to eradicate inequalities of income and wealth through peaceful means by taxation and government spending on social welfare and social security schemes.

Planning under Mixed Economy	• Under this system there is freedom of economic activities and government interference for social welfare. • According to Prof. Samuelson, "Mixed economy is that economy in which both public and private sectors cooperate". • The main responsibility of the government in this system is to ensure rapid economic growth without allowing concentration of economic power in the few hands. India introduced planning under a mixed economy.
Perspective Planning	• Perspective planning refers to long-term planning in which long range targets are set in advance for a period of say 15 or 20 years. • A prospective plan, however, does not imply one plan for the entire period of 15 or 20 years. • In reality, the broader objectives and targets are to be achieved within the specified period of time by dividing the prospective plan into several short-period plans of say three years or annual plans.
Indicative Planning	• This is a French system of planning which is based on the principle of Decentralisation in the operation and execution of national plans. • In Indicative Planning the private sector is neither rigidly controlled nor directed to fulfill the targets and priorities of the plan. • The State provides all types of facilities to the private sector but does not direct it, rather indicates the area in which it can help in implementing the plan.
Imperative Planning	• Under Imperative Planning, all economic activities and resources of the economy operate under the direction of the state. There is complete control over the factors of production by the state. • The entire resources of the country are used to the maximum in order to fulfill the targets of the plan. There is no consumers' sovereignty in such planning.
Totalitarian Planning	• In totalitarian or authoritarian planning, all economic activity is in accordance with a single plan as per the central control and direction. • The consumption, production, exchange, and distribution are all controlled by a state. Under the Totalitarian Planning, the planning authority is the supreme body. • The Planning body takes decisions in regards to the targets, schemes, allocation, methods and procedures of implementation of the plan.
Rolling Plan	• In a rolling plan, every year three plans are made and acted upon. • First, there is a plan for the current year which includes the annual budget and the foreign exchange budget. • Second, there is a plan for a number of years, say three, four or five. • Third, a prospective plan for 10, 15 or 20 or even more years is presented every year in which the broader goals are stated and the outlines of future development are forecast. • The annual one-year plan is fitted into the same year's new three, four or five year plan, and both are framed in the light of the prospective plan.
Fixed Plan	• Fixed plan lays down definite aims and objectives which are required to be achieved during the plan period. For this purpose, physical targets are fixed along with the total outlay. • Physical targets and financial outlays are seldom changed except under emergencies.

MONETARY POLICY

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Introduction

- Money is defined as something which is generally accepted by the society as a medium of exchange and which can act as a unit of account, can store value and be used for repayment of debt.
- Money is the commonly accepted medium of exchange. Economic exchanges without the mediation of money are referred to as barter exchanges.

Functions of Money

- Money acts as a medium of exchange of all goods and services.
- Money helps to measure the value of goods and services in terms of price.
- Money is the most convenient and economical means to store wealth which does not lose its value so quickly over time.
- Deferred payments are those payments which are promised to be made in future. Money acts as a means of deferred payments mainly because it has general acceptability.
- Money is used to transfer value from one place to another or from one person to another.

Types of Money		
Type	**Definition**	**Example**
Commodity Money	Commodity money is that type of money that possesses intrinsic value on its own, independent of any governing body. This means the money itself contains its own worth.	Numerous commodities such as gold, silver, copper, chocolate beans etc., have been effectively utilized as this form of currency.
Metallic Money	Discovery of precious metals and the spread of civilization and trade relations by land and sea, led metallic money to take the place of commodity money.	Gold and silver were the metals mostly used to form metallic money. Because of their scarcity, usefulness and attractiveness, gold and silver were regarded as natural money.

Types of Money		
Paper Money	Money made of paper is called paper money. Paper money consists of currency notes issued by the government or the central bank of a country.	Rupee, Dollar
Credit Money (Bank Money)	Credit Money or Bank money was used due to the development of banking institutions and their credit creation activities.	The term 'credit money' refers to the demand deposits of the commercial banks. Demand deposits of banks are withdrawable through cheques. It serves as money and the cheques are accepted as a means of payments.
Plastic Money	Plastic money is a term that is used predominantly in reference to the hard plastic cards in place of actual bank notes.	They can come in many different forms such as cash cards, credit cards, debit cards, prepaid cash cards and store cards.
Fiat Money	Fiat money is money which does not have any intrinsic value, unlike commodity money. This is the money that only contains any value because the government decrees it has the full faith and credit of the nation backing it.	Currency notes and coins are called fiat money. They do not have intrinsic value like a gold or silver coin.
Helicopter Money: Helicopter money is a reference to an idea made popular by the American economist Milton Friedman in 1969. The basic principle is that direct money transfers is one of the most effective tools by the central bank to raise inflation and output in an economy that is running substantially below potential.		

Money Supply

The total stock of money in circulation among the public at a particular point of time is called money supply (By public, it refers to the households, firms, local authorities, companies etc.). Thus, public money does not include the money held by the government and the money held as CRR with RBI and SLR with themselves by commercial banks. This money may be in the following forms:

- **Currency Notes and Coins:** In India, Currency notes are issued by the Reserve Bank of India (RBI), which is the monetary authority in India. However, coins are issued by the Government of India (GoI) and circulated by the Reserve Bank of India (RBI) on behalf of the GoI.
- **Demand Deposits Such as Saving Banks Deposits:** These are those deposits that can be withdrawn on demand from banks.
- **Other Deposits Such as Time Deposits/Term Deposits/Fixed Deposits:** These are those deposits that can be withdrawn only after a specific time.
- Post Office Saving Accounts.
- Deposits of Banks in other Banks/RBI (except CRR).

Cryptocurrency

Cryptocurrency is a digital currency created, stored and transacted using blockchain technology. It is secured by cryptography and uses a decentralized network called distributed ledger. This decentralized structure allows them to exist outside the control of governments and central authorities.

INDIAN ECONOMY

Previous Years' Questions & Practice Questions

1. What were the parameters adopted by Suresh Tendulkar Committee to estimate poverty in India?
(a) Money required for stipulated minimum calorie intake
(b) Spending on transport and housing
(c) Spending on food, education, health, electricity, clothing and footwear
(d) None of the above

[APPSC (AEE) : 2016]

Ans. (c)

2. What is "The Limits to Growth" ?
(a) Limits set by Society on growth
(b) Limits set by Industry Cartels on growth
(c) A 1972 book on computer simulation of growth with finite resource supplies
(d) Government's inability to improve growth

[APPSC (AEE) : 2016]

Ans. (c)

3. As recommended by the 14th Finance Commission, the primary route for transfer of resources from Centre to States shall be through
(a) Devolution of taxes
(b) On the basis of population
(c) On the basis of economic backwardness
(d) None of the above

[APPSC (AEE) : 2016]

Ans. (a)

4. Small scale industries
(a) produce small items
(b) have small machines
(c) use small machines
(d) deal with small capital, few workers and small bulk of raw materials

[BPSC (AE) : 2001]

Ans. (d)

5. Which is a nationalized bank?
(a) HDFC Bank
(b) Federal Bank
(c) Citi Bank
(d) Dena Bank

[BPSC (AE) : 2006]

Ans. (d)

6. What is NSE?
(a) National Saving Exchange
(b) National Storage Engine
(c) National Statistics Economy
(d) National Stock Exchange

[BPSC (AE) : 2006]

Ans. (d)

7. Who performs the Central Banking in India?
(a) Reserve Bank of India
(b) Central Bank of India
(c) State Bank of India
(d) Finance Ministry

[BPSC (AE) : 2006]

Ans. (a)

8. In banking, the full form of RTGS is
(a) Rapid Transfer Gross Scheme
(b) Rapid Transfer Gross Settlement
(c) Real Time Gross Settlement
(d) Real Time Gross Scheme

[BPSC (AE) : 2017]

Ans. (c)