PART- A: INTRODUCTORY MACROECONOMICS
UNIT – 2 : MONEY AND BANKING

CHAPTER-1
MONEY AND BANKING

Revision Notes

Money

- **Definition of Money:** Money may be defined as anything which is generally acceptable as a medium of exchange and also acts as common measures of value, store of value and standard of deferred payment.
- **Money Supply:** Total of money (currency notes, coins and demand deposits of banks) in circulation held by the public at a given point of time.
- **Measures of Money Supply:** In India, RBI uses four measures of money supply. These are M_1, M_2, M_3 and M_4.
- **Narrow Approach of Money Supply:** In narrow sense, we include only liquid assets which are easily acceptable for payments. It includes M_1 and M_2.
- **Broad Approach of Money:** It refers to currency held by public, demand deposits and time deposits. It includes M_3 and M_4.
- **Currency with Public (C):** Currency of a country is issued either by the government or by the Central Bank. It is called Legal Tender Money.
- **Demand Deposits (DD):** Public deposits with bank which public may withdraw at any time or on demand, bank has to pay it.

  Other Deposits (OD): These deposits include:

  (i) Demand Deposits of public financial institutions with RBI

  (ii) Demand Deposits of international financial institutions with RBI

  (iii) Demand Deposits of foreign government and central banks with RBI
- **Time Deposits (TD):** Those deposits of public with bank which can be withdrawn only after completion of that period for which it has been deposited with banks.
- **Stock of Money:** If supply of money is studied at a point of time; it is called Stock of Money.
- **Flow of Money:** When supply of money is considered over a period of time; it is called Flow of Money.
- **High Powered Money or Reserve Money:** It is the sum of **(i)** Currency held by the public **(ii)** Cash reserve of the banks.

  H = C + R
- **Factors affecting Money supply:**

  (i) Central Bank

  (ii) Commercial Banks

  (iii) Government

  (iv) Banking habits

  (v) Velocity of Circulation

  (vi) Volume of trade

  (vii) Amount of demand deposits

- **Who Supplies Money:** Central Bank of the country. In India, Reserve Bank of India is the Central Bank.

Commercial Banks and Central Bank

- **Money creation by Commercial Banks:** Money creation is a process in which a Commercial Bank creates total deposits many times the initial deposits.
  The capacity of Commercial Bank to create money depends on two factors:
  (i) Amount of initial fresh deposit
  (ii) Legal Reserve Ratio (LRR)
  Money Multiplier = 1/LRR
  Money Creation = Initial Deposit × Money multiplier.
  Working: Suppose **(i)** Initial Deposit = ₹1,000
  (ii) LRR = 20%
  As required, the bank keeps 20% i.e., ₹200 as cash reserve and lends the remaining ₹800. Those who borrow, use the money for making payments. As assumed, those who receive these payments put the money back into their bank accounts. This creates a fresh deposit of ₹800. The bank again keeps 20%, *i.e.*, ₹160 and lend ₹640. In this way the money goes on multiplying leading to total money creation of ₹5,000.
- **Central Bank:** A Central Bank is an apex institution in the banking structure of the country. It supervises, controls and regulates the activities of Commercial Banks and acts as a Banker to them. RBI (Reserve Bank of India) is the Central Bank of India.
- **Functions of RBI/Central Bank:**
  (i) Monopoly of Note Issue/Bank of Issue
  (ii) Banker to the Government
  (iii) Bankers' Bank
  (iv) Controller of Credit

Know the Terms

- **Asset:** Something that is owned.
- **Liability:** An obligation, debt, or other object, due to someone in the future.
- **Fiat Money:** Money that holds value only because the government declares it as legal tender.
- **Narrow Money:** $M_1 + M_2$
- **Broad Money:** $M_3 + M_4$
- **Reserves:** The money deposited in a bank.
- **Reserve requirement:** The fraction of all reserves of a bank that must be held by the bank in vaults.
- **Legal reserves:** The money held by the bank in vaults to satisfy the reserve requirement.
- **Excess reserves:** Money that is not required to be stored by the bank. This money can be loaned out.
- **Discount rate:** Interest rate on a loan from the federal reserve to a bank.
- **Federal funds rate:** Interest rate on a loan from a bank to another bank.

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UNIT – 4 : GOVERNMENT BUDGET AND THE ECONOMY

CHAPTER-2

GOVERNMENT BUDGET AND THE ECONOMY

Revision Notes

- **Budget:** Budget is a financial statement showing the expected receipt and expenditure of Government for the coming fiscal or financial year. It is a constitutional requirement in India (Article 112).
- **Objectives of Government Budget:**
  (i) Encouragement to economic development
  (ii) Balanced regional development

(iii) Redistribution of income and property
(iv) Economic stability
(v) Generation of employment
(vi) Management of public enterprises

- **Components of Government Budget**:
- **Revenue Budget:** It shows revenue receipts and revenue expenditure of the government related to the current financial year only.
- **Revenue Receipts: (a)** Which do not cause any reduction in assets; and **(b)** Which do not create any corresponding liability to the government. Example: Tax receipts of the government.
- **Tax:** It is a compulsory contribution by an individual, household or a firm to the government without receiving anything in return directly. Government uses these receipts for social and development work.
- **Direct Tax:** When Government imposes a tax on a person and it is paid by the same person it is called direct tax. Its burden cannot be shifted to others. For example: Income Tax, Property Tax.
- **Indirect Tax:** It is a tax on goods and services. It is to be initially paid by the producers / traders but its final burden can be passed on to the final buyers by way of inclusion or increase in price of the taxed commodity. GST or VAT is an example of it.
- **Non-Tax Receipts: Non-Tax Receipts** are those receipts which are received from sources other than taxes, e.g., Fees, Fines, Escheats, Grants / Donations, etc.
- **Revenue Expenditure:** It is the expenditure by the government that is related to the current financial year. These expenses:

  (i) Do not cause increase in government assets, and;

  (ii) Do not cause any reduction in government liability.
- **Capital Budget:** It shows capital receipts and capital expenditure of the government.
- **Capital Receipts: (a)** Which create corresponding liability for the government. Example: Loans by the Government; and **(b)** Which cause reduction in assets of the government. Example: Disinvestment.
- **Capital Expenditure:** It is the expenditure by the government which:

  (i) Causes increase in government assets; and

  (ii) Causes reduction in government liability.
- **Budget Deficit:** It is the excess of total estimated expenditure over total estimated revenue.

  (i) Revenue Deficit: Revenue Receipts – Revenue Expenditure.

  (ii) Fiscal Deficit: [Revenue Expenditure + Capital Expenditure] – [Revenue Receipts + Capital Receipts (other than government borrowings)].
- **Primary Deficit:** By deducting interest payment from fiscal deficit, we get primary deficit.

  Primary Deficit = Fiscal Deficit – Interest Payment
- **Types of Budgets**

  (i) Balanced Budget: Total Expenditure = Total Revenue

  (ii) Deficit Budget: Total Expenditure > Total Revenue

  (iii) Surplus Budget: Total Anticipated Expenditure < Total Anticipated Revenue
- **Measures to Correct Different Deficit:**

  (i) Raising government revenue

  (ii) Monetary Expansion or Deficit Financing

  (iii) Borrowing from general public

  (iv) Disinvestment

  (v) Lowering government expenditure

Know the Terms

- **Financial Year:** Year for which Government budget is presented- 1st April of one year to the 31st of March of the succeeding/next year.
- **Development Expenditure:** These are directed towards development programmes of the country, and directly contributes to the flow of goods and services in the economy. Example: education, health, scientific research, etc.
- **Non-Development Expenditure:** These are not directly related to development programmes of the country, and do not directly contribute to the flow of goods and services in the economy. These expenses are routine

and administrative expenses like defence, payment of salary to police, judiciary, subsidies on food, etc. They are indirectly important to the economy.

- **Planned Expenditure:** These are incurred in accordance with planned development programmes of the country.
- **Non-Planned Expenditure:** These refers to general expenditure incurred on essential general services of routine nature.
- **Dis-investment:** It refers to withdrawal of existing investment, e.g., Government of India is undertaking dis-investment by selling the shares of Maruti Suzuki.

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UNIT – 5 : BALANCE OF PAYMENTS

CHAPTER-3
BALANCE OF PAYMENTS

Revision Notes

- **Balance of Payments:** The Balance of Payments (BoP) records the transactions in goods, services and assets between residents of a country with rest of the world for a specified time period (a year).
- **Components of BoP (Balance of Payments) Account:** The transactions entering into the balance of payments account can be grouped under three broad accounts:
  (i) Current Account **(ii)** Capital Account
  (iii) Official International Reserve Account
- **Current Account:** Transactions related to trade in goods and services and transfer of payments constitute the current account. The components of current account do not cause a change in assets or liabilities status of the residents of a country or its government.
- **Items of Current Account:**
  (i) Merchandise account
  (ii) Invisible items and
  (iii) Unilateral transfers
- **Capital Account:** Capital account represents international capital transactions which include sale and purchase of assets such as bonds, equities, lands, loans, bank accounts, etc. The components of capital account cause a change in assets and liabilities status of the residents of a country or its government.

Know the Terms

- **Balance of Trade:** Balance of trade is the net difference of import and export of all visible items between the normal residents of a country and rest of the world.
- **Autonomous Transactions:** Autonomous items are those items of balance of payments which are related to such transactions as are determined by the motive of profit maximisation and not to maintain equilibrium in Balance of Payments. These items are generally called 'Above the Line Items' in balance of payments.
- **Accommodating Items:** Refers to all the items related to the monetary transfers (or official reserve transactions), correcting balance of payments disequilibrium. Accommodating item refers to transactions that take place because of other activities in Balance of Payments. These transactions are meant to restore the Balance of Payments identity. These items are generally called 'Below the Line Items'.
- **Unilateral transfers:** Transfer of goods or services from one country to another without receiving anything in return, e.g., foreign aid.
- **Open Economy:** An economy which interacts with other economies through trade, movement of finance and labour.

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CHAPTER-4
FOREIGN EXCHANGE RATE

Revision Notes

- **Foreign Exchange Rate:** Foreign exchange rate refers to the rate at which one unit of the currency of a country can be exchanged for the number of units of the currency of another country.

SYSTEM OF EXCHANGE RATE

Fixed Exchange Rate | Managed Floating Exchange Rate | Flexible Exchange Rate

- **Types of Foreign Exchange Rates:**
  - **(i) Fixed Exchange Rate:** When the Central Bank of a country fixes (or pegs) the value of exchange rate, it is called Fixed Exchange Rate system or Pegged Exchange Rate System.
  - **(ii) Flexible Exchange Rate System:** The system of exchange rate in which value of a currency is allowed to adjust freely or to float as determined by the demand for and supply of foreign exchange is called Flexible Exchange Rate System.
  - **(iii) Managed Floating System:** It is a system in which the Central Bank allows the exchange rate to be determined by market forces but intervenes at times to influence the rate. When Central Bank finds the rate is too high, it starts selling foreign exchange from its reserve to bring it down. When it finds that the rate is too low, it starts buying to raise the rate.

Know the Terms

- **Gold Standard System of Exchange Rate:** According to the Gold Standard System of Exchange Rate, value of one currency in terms of the other currency was fixed considering gold value of each currency. This system was prevailing before 1920's where gold was taken as the common unit of parity between the currencies of different countries.
- **Nominal Exchange Rate:** It refers to the number of units of domestic currency, one must give up getting a unit of foreign currency. In simple terms, it refers to the price of foreign currency in terms of domestic currency.
- **Real Exchange Rate:** It refers to the relative price of foreign goods in terms of domestic goods.
- **Dirty Floating:** When adjustment of exchange rates is done without following the rules and regulations of Foreign Exchange Market, it is termed as Dirty Floating.
- **Devaluation of a Currency:** When government or monetary authority of a country officially lowers the external value of its domestic currency (in respect of all other foreign currencies) it is called devaluation of a currency. It takes place by government order under fixed exchange rate system.
- **Revaluation of a currency:** When government or monetary authority of a country officially raises the external value of its domestic currency (in respect of all other foreign currencies) it is called revaluation. It takes place by government order under fixed exchange rates system.
- **Depreciation of Currency:** In currency depreciation, there is a fall in the value of domestic currency, in terms of foreign currency due to change in demand and supply of the currency under flexible exchange rate system.
- **Appreciation in Currency:** In currency appreciation, there is a rise in the value of domestic currency in terms of foreign currency due to change in demand and supply of the currency under flexible exchange rate system.

PART – B : INDIAN ECONOMIC DEVELOPMENT
UNIT – 6 : DEVELOPMENT EXPERIENCE (1947-90) AND ECONOMIC REFORMS SINCE 1991

CHAPTER-5

DEVELOPMENT EXPERIENCE (1947-90) AND ECONOMIC REFORMS SINCE 1991

Revision Notes

Indian Economy on the Eve of Independence

- India had an independent economy before the advent of British rule. Though agriculture was the main source of livelihood for most of people, yet, the economy of the country was characterised by various kinds of manu facturing activities. The objective of policies adopted by the colonial government was to export raw materia from India and import manufactured goods from England.
  The colonial government never made any sincere attempt to estimate India's national income and per capita income. First scientific estimate was made by **V.K.R.V. Rao** in 1931-32 during colonial rule.
- **Agriculture sector on the Eve of Independence:** Indian economy under the British colonial rule remained fundamentally agrarian. The main causes of stagnation of agricultural sector were as follows:
  Change in Tenurial system and Commercialization of agriculture:
  Change in System and Tenure: **(i)** Permanent settlement or Zamindari system, **(ii)** Ryotwari system, and **(iii)** Mahalwari system.
  Commercialisation of Agriculture: Main causes were:
  (i) Industrial revolution **(ii)** Commercial policy of British Government, **(iii)** Increase in foreign trade, **(iv)** Payment of Land Revenue in cash, **(v)** Use of money, **(vi)** Development of the means of transportation and communication, **(vii)** Expansion of the agricultural market, **(viii)** High price of cash crops.
- **Industrial Sector on the Eve of Independence:** Like agriculture, industrial sector of India could not develop. At the time of independence, the condition of industrial sector was as follows: **(i)** De-industrialisation or decline of Indian handicraft industry, **(ii)** One sided modern industrial structure, **(iii)** Lack of capital goods industries, **(iv)** Limited operation of public sector.
- **Main characteristics of Industrial Development during British rule:** **(i)** Development of consumer product industries, **(ii)** Rising share of Indian capital, **(iii)** Concentration of enterprises in few hands, **(iv)** Dominance of foreign capital, **(v)** Investment of own capital of capitalists, **(vi)** Industrial policy, **(vii)** Regional imbalance in industrial development.
- **Foreign Trade on the Eve of Independence:** India was a trading nation before the advent of colonial rule. But due to restrictive policies adopted by the colonial government, India's foreign trade was affected adversely. Foreign trade conditions on the eve of independence were as follows: **(i)** Export of primary products and import of finished goods, **(ii)** Monopoly control of Britain on foreign trade, and **(iii)** Drain of Indian wealth.
- **Demographic conditions on the eve of Independence:** First Census of population of British India was made in 1881. At the time of independence, the features of demographic conditions were as follows:
  (i) High birth and death rate, **(ii)** High infant mortality rate, **(iii)** Low life expectancy ratio, **(iv)** Low literacy rate, **(v)** Low standard of living.
- **Occupational structure on the eve of independence:** Occupational structure refers to distribution of working population across different industries and sectors. During colonial rule, occupational structure did not change much. The state of occupational structure during the British rule was as follows:
  (i) Pre-dominance of agricultural sector, and **(ii)** Growing regional variation.
- **Infrastructure on the eve of independence:** Under infrastructure, we include all those industries and services which are used to develop other industries. Development of infrastructure during colonial rule was not to provide better facilities to general public but serve the British interest only. We include the following under infrastructure:
  (i) Railway, **(ii)** Roads, **(iii)** Water and Air transport, **(iv)** Communication system.

- **Indian Economy on the Eve of Independence: (i)** Colonial economy, **(ii)** Semi-feudal economy, **(iii)** Backward economy, and **(iv)** Stagnant economy.
- **Positive contribution of British rule: (i)** Self-sufficiency in food grain production, **(ii)** Better means of transportation, **(iii)** Check on famines, **(iv)** Shift to monetary economy, and **(v)** Effective administration set up.
- After independence, India envisaged an economic system which combines the best features of socialism and capitalism — this culminated in the mixed economic model.

Common Goals of Five Year Plans

- **Meaning of Planning:** Planning is a technique and a means to attain goals. These pre-determined goals are specially formulated by the central planning authority.
- **Characteristics of Economic Planning: (i)** Organisation System, **(ii)** Maximum utilisation of Resources, **(iii)** Applicable on the whole economy, **(iv)** Central Planning Authority, **(v)** Interference by the State, **(vi)** Changes in the economy, **(vii)** Long term process, **(viii)** Pre-determined objectives, **(ix)** Existence of valuation mechanism, **(x)** Achievement of objectives.
- **Plan period in India:** India has completed 12 Five Year Plans. Time Period of 12^{th} Plan was 2012-2017.
- **Indian Planning Commission:** The Planning Commission of India was established on 15^{th} March, 1950, to evaluate the physical, capital and human resources and on this basis make programmes for the Plan Development and its evaluation. The Planning Commission of India has now been dissolved in 2015 and replaced with National Institution for Transforming India (NITI) Aayog.
- **National Development Council (NDC):** As an apex body to planning, it was constituted on 6^{th} August, 1952. No plan was implemented without its approval.
- **Objectives of Planning in India: (i)** Economic growth, **(ii)** Modernisation, **(iii)** Self-reliance, and **(iv)** Economic equity.
- **Achievements of Indian Plans:**
  (i) Growth-Oriented Development Strategy (1951-65): In first plan, actual growth rate was higher than targeted. But in second and third plans, it was less than targeted.
  (ii) Equity Oriented Development Strategy (1966-90): There are two big achievements in the field of self-reliance. **(i)** India attained almost self-sufficiency in the field of food grains, and **(ii)** due to development of heavy engineering, machinery equipment, iron and steel and other capital goods industries, India become self-sufficient in machinery equipment and other capital goods.
- **Failures of Economic Planning: (i)** Slow progress in per capita and national income, **(ii)** Unemployment, **(iii)** Increase in economic disparity, **(iv)** Economic instability, **(v)** Failure in agriculture sector, **(vi)** Failure in industrial sector, **(vii)** Failure in resource mobilisation, **(viii)** Dependence on foreign aid, **(ix)** Defective regulatory policy.
- **Suggestions for the Success of Plans: (i)** Widespread mass participation, **(ii)** Control on prices, **(iii)** Co-ordination between public and private sector, **(iv)** Integration between long term and short term programmes, **(v)** Physical achievements should be basis of success, **(vi)** Encouragement of saving and investment, **(vii)** Control on population growth, **(viii)** Job oriented economic planning, **(ix)** Coordination between capital intensive and consumption oriented industries, **(x)** Utilisation of human power, **(xi)** Clean administration.

Agriculture: Features, Problems, and Policies

- During the Colonial rule, there was neither growth nor equity in agriculture sector. The policy makers of independent India had to address these issues which they did through land reforms and promote the use of High Yielding Varieties of Seeds which ushered revolution in Indian agriculture.
- **Importance of Agriculture in Indian Economy: (i)** Main source of employment, **(ii)** Contribution in National Income, **(iii)** Base of industrialisation, **(iv)** Base of economic development, **(v)** Importance in Foreign Trade, (vi) Supply of food grains, **(vii)** Contribution in revenue, **(viii)** Dependence on trade and transport, **(ix)** Capital formation, **(x)** Rainbow of revolution.
- **Characteristics of Indian Agriculture: (i)** Main source of livelihood, **(ii)** Disguised and seasonal unemployment, **(iii)** Labour intensive agriculture, **(iv)** Excess dependence of agriculture on monsoon, **(v)** Small size of land holdings, **(vi)** Low level of productivity, **(vii)** Old and defective agricultural production, **(viii)** Pre-dominance of food crops.
- **Land Reforms:** Land reforms primarily refer to change in the ownership of holdings. It was done with the purpose of increasing agricultural production, the direct intervention of government in agrarian structure.
- **Need for Land Reforms: (i)** Retrograde agrarian structure and agrarian relation and **(ii)** Small and fragmented agricultural holdings.
- **Land Reform Measures: (i)** Abolition of intermediaries, **(ii)** Tenancy Reforms, **(iii)** Re-organisation of agriculture.

- **Land Ceiling:** It was the policy which recommended the fixation of maximum size of land which would be owned by an individual. The purpose of land ceiling was to reduce the concentration of land ownership in a few hands.
- **Green Revolution:** Green Revolution implies the strategy related to improving production technique and productivity in agriculture.
- **Features of Green Revolution:** **(i)** High Yielding Varieties of seeds, **(ii)** Extensive use of fertilisers, **(iii)** Expansion of irrigation facilities, **(iv)** Plant protection, **(v)** Establishment of different institutions, **(vi)** Agro-service centres, **(vii)** Multiple cropping programme, **(viii)** Mechanisation, **(ix)** Scientific method of agriculture, **(x)** Development of agricultural land, **(xi)** Improvement of animal husbandry, **(xii)** Fixation of Minimum Support Prices.
- **Achievements of Green Revolution:** **(i)** Rise in production and productivity, **(ii)** Increase in income, **(iii)** Increase in employment, **(iv)** Rural prosperity, **(v)** Industry and agriculture relationship, **(vi)** Innovation.
- **Economic Subsidies:** To assure availability of fertilizers to the farmers at reasonable prices government is providing subsidies. A current debate is should subsidy continue or we may go without subsidy. Arguments are put forward both in favour and against subsidy

Industes: Features, Problems, and Policies

- In the Pre-British period, India was an industrially advanced country. But the British rule systematically destroyed the Indian industries. As a result, at the time of independence, India had a weak industrial base, poorly developed infrastructure and a stagnant economy.
- **Basic features of India's industrial development during Plan Period:** **(i)** Increase in industrial growth rate, **(ii)** Increase in contribution of industrial sector in GDP, **(iii)** Rapid development of basic industries, **(iv)** Strong infrastructural base, **(v)** Import substitution, **(vi)** Establishing enterprises with foreign assistance, **(vii)** Increase in export of industrial products, **(viii)** Establishment of financial institution, **(ix)** Development of information technology and electronics industries, **(x)** Development of small and cottage industries, **(xi)** Disinvestment in public sector, **(xii)** Development of food processing industry, and **(xiii)** Emergence of consultancy services.
- **Problems of Industrial Development in India:** **(i)** Problem of Energy, **(ii)** High cost, **(iii)** Shortage of capital, **(iv)** Shortage of foreign exchange, **(v)** Lack of able entrepreneurs, **(vi)** Irregular rate of industrial growth, **(vii)** Unemployment problem ignored, **(viii)** Industrial unrest, **(ix)** Small and medium sector neglected, **(x)** Problem of industrial sickness, **(xi)** Less utilisation of installed capacity, **(xii)** Regional disparity, **(xiii)** Increase in concentration of economic power, **(xiv)** Failure of public sector enterprises.
- **Measures to Encourage Industrial Development:** **(i)** Creation of economic and social infrastructure, **(ii)** Development of entrepreneurial skill, **(iii)** To ensure availability of capital, **(iv)** Financial stability, **(v)** Rehabilitation of sick units, **(vi)** Removal of control, **(vii)** Human capital formation, **(viii)** Modernisation, **(ix)** Improvement in industrial relation, **(x)** Professionalisation of management, **(xi)** Industrial research.
- **Industrial Policy:** It refers to such formal declaration made by the Government which describes the general policies which will be adopted by the Government towards the industries.
- **Industrial Policy Resolution, 1956:** **(i)** Classification of industries into public and private sectors, **(ii)** Stress on the role of cottage and small-scale industries, **(iii)** Reduction in regional disparities, **(iv)** Foreign capital, **(v)** Facilities for labourers.
- **Industrial Licensing Policy:** Industrial licensing is an authority issued by the government organisation to permit the institutions for starting an industry or to start a function. In India it was started in 1952. The basis of this policy was Industries (Development and Regulation) Act, 1951, and New Industrial Policy for 1991.
- **Public Sector Enterprises:** A public sector enterprise is that enterprise which is owned and managed by the government.
- **Characteristics of Public Enterprises:** **(i)** Public ownership, **(ii)** Socio-economic objective, **(iii)** Accountability towards public, **(iv)** Financing from government funding.
- **Role of Public Sector in Industrialisation:** **(i)** Contribution in National Income, **(ii)** Contribution in Employment generation, **(iii)** Contribution in export, **(iv)** Development of small-scale sector, **(v)** Development of backward area, **(vi)** Expansion of technological base, **(vii)** Help in achievement of self-sufficiency.
- **Problems of Public Sector:** **(i)** Bureaucratic delays, **(ii)** Lack of technical efficiency, **(iii)** Discriminating policy of organisation, **(iv)** Lack of incentives, **(v)** Inadequate control of parliament, **(vi)** Lack of mutual co-operation, **(vii)** Over capitalisation, **(viii)** Operational and Managerial inadequacies, **(ix)** Under utilisation of production capacity, **(x)** Over-sized plants, **(xi)** Take-over of sick units, **(xii)** Long gestation period.
- **Suggestions for Reforms of Public Sector:** **(i)** Appropriate pricing policy, **(ii)** Test of efficiency, **(iii)** Full utilisation of production capacity, **(iv)** Quantitative determination of objectives, **(v)** Use of latest techniques, **(vi)** Precautions in appointment of employees.

- **Disinvestment in Public Sector:** It refers to the dilution of stake (claims) of the government in the equity of public sector undertaking so as to transfer the ownership rights to private hands.
- **Small Scale Sector in India:**

  Cottage Industry: These industries are mostly traditional, producing traditional products by employing traditional methods.

  Small Sector Industries: These are defined in relation to capital investment in machines and buildings. Presently, this limit is ₹5 crores.
- **Role of Small Sector in Indian Economy:** **(i)** Provide economic equality, **(ii)** Production of artistic goods, **(iii)** Protection from clan-struggle, **(iv)** Need less technology, **(v)** Protection from bad effects of urbanisation and industrialisation, **(vi)** Less dependency on imports, **(vii)** Important place in country's exports.
- **Problems of Small Sector:** **(i)** Shortage of capital, **(ii)** Undeveloped production system, **(iii)** Problem of raw material, **(iv)** Lack of organised market, **(v)** Competition from large scale units, **(vi)** Lack of education, **(vii)** Lack of standardization, **(viii)** Export neglected, **(ix)** Dis-interest of consumers, **(x)** Non-receipt of payments in time.

Foreign Trade of India: Features and Policies

- In the first seven plans, trade was characterised by what is commonly called an inward looking trade strategy. Technically, this policy is called Import Substitution Policy.
- **Role and Importance of Foreign Trade:** **(i)** Advantage of advance technology, **(ii)** Increases consumption capacities, **(iii)** Benefits to participating countries, **(iv)** Increases production capacity, **(v)** Serves as a transmission belt for capital, **(vi)** Creates fair competition.
- **Features of India's Foreign Trade:** **(i)** Increase in the value and volume of trade, **(ii)** Increasing share in the gross national product, **(iii)** Increasing share in the world trade, **(iv)** Changes in the composition of exports, **(v)** Changes in the composition of import, **(vi)** Export-Import ratio, **(vii)** Changes in the direction of foreign trade, **(viii)** Adverse balance of trade.
- **Problems of India's Foreign Trade:** **(i)** Adverse balance of trade, **(ii)** Rapid increase in imports, **(iii)** Comparatively lower growth in exports, **(iv)** Increase in domestic demand, **(v)** Rising prices, **(vi)** Increasing foreign debt.

  Foreign Trade Policy in India
- **Import substitution in India:** It is a process to produce the alternate or close substitute of imported goods in the country itself.
- **Need for Import Substitution:** **(i)** Scarcity of foreign exchange, **(ii)** Un-favourable balance of trade, **(iii)** Devaluation of rupee, **(iv)** Scarcity of foreign aid, **(v)** Shortage of essential commodities, **(vi)** Need for industrial development, **(vii)** Increase in self-sufficiency.
- **Export Promotion:** It is a process in which incentives are provided to old exporter and new entrepreneurs to increase the exportable surplus.
- **Export Promotion Policies (Pre-Reform Period):** **(i)** Establishment of various organisations, **(ii)** Export-Import bank, **(iii)** Export processing zones, **(iv)** Special economic zone, **(v)** Export promotion industrial park, **(vi)** Export promotion capital goods, **(vii)** Adoption of Liberalised Licensing System.
- **Foreign Trade Policy (2009-14):** **(i)** DEPB extended till Dec. 2010, **(ii)** Relaxation in export promotion of capital goods, **(iii)** Tax refund scheme for Jewellery sector, **(iv)** Single window scheme, **(v)** Re-export of unused leather, **(vi)** Export units allowed to sell 90 percent of goods in domestic market, **(vii)** Provision of dollar credits, **(viii)** Addition of new markets and, **(ix)** Zero duty under technology upgrade scheme.

Economic Reforms in India

- New Economic Policy (NEP) refers to the efforts made through different policy decisions and changes that were made to create competitive environment and increase in productivity and efficiency.
- **Need for Economic Reforms:**

  Problems facing Economy: **(i)** Unsatisfactory performance of public sector, **(ii)** High rate of inflation, **(iii)** Increasing debt burden, **(iv)** Problem of balance of payment.

  Immediate crisis: **(i)** Gulf crisis, **(ii)** Inadequate Foreign Exchange Reserves.
- **Main components of New Economic Policy:** **(i)** New industrial policy, **(ii)** New trade policy, **(iii)** New fiscal policy, **(iv)** New monetary policy, **(v)** New investment policy, **(vi)** Globalisation of finance.
- **Main Phases of New Economic Policy:** **(i)** Liberalisation, **(ii)** Privatisation, and **(iii)** Globalisation.
- **Meaning of Liberalisation:** Liberalisation means removing all unnecessary controls and restrictions like permits, licenses, protectionist duties, etc., imposed by the government.

- **Measures adopted for Liberalisation:**
  - **(i) Soft Liberalisation Policy (1985-1991):** The era of liberalisation started with the period of Rajiv Gandhi, the then Prime Minister, in 1985. In this period of modernization, a large number of incentives and exemptions were granted.
  - **(ii) Extensive Liberalisation Policy [After 1991 period]:** **(a)** Liberalised licensing policy, **(b)** Expansion of industries, **(c)** Concession from Monopolies, **(d)** Extending investment limits for small industries, **(e)** Free import of machinery and raw materials, **(f)** Freedom to import technology, **(g)** Freedom to financial institution, **(h)** Reduction in tax rates.
- **Meaning of Privatisation:** Transfer of ownership from government to private sector of organisations which are presently run and controlled by government.
- **Measures of Privatisation:**
  - **(i) Ownership Measures: (i)** Total Denationalisation, **(ii)** Joint venture.
  - **(ii) Organisational Measures: (i)** Holding company, **(ii)** Leasing, **(iii)** Disinvestment.
- **Factors encouraging Privatisation in India: (i)** New economic reforms programmes, **(ii)** Increasing debt burden on government, **(iii)** Presence of foreign companies, **(iv)** To make Indian companies more competitive, **(v)** Broad base for increasing production.
- **Steps of Indian Economy towards Privatisation: (i)** Contraction of public sector, **(ii)** Participation of private sector, **(iii)** Abolition of industrial licensing, **(iv)** Improvement by MOU, **(v)** Re-organisation of public sector, **(vi)** Disinvestment of equity of public sector, **(vii)** Establishment of National Renewable Fund, **(viii)** Removal of investment control on big houses, **(ix)** Policy related to sick units, **(x)** Sale of shares of public sector undertaking.
- **Arguments in Favour of Privatisation: (i)** Reduction in Budgetary Deficit, **(ii)** Less political intervention, **(iii)** Improvement in economic efficiency and technical efficiency, **(iv)** Increased accountability, **(v)** Globalisation of economy, **(vi)** Sources of new job, **(vii)** Increase in industrial growth, **(viii)** Increase in foreign investment, **(ix)** In line with international trade, **(x)** Encouragement to new inventions.
- **Arguments Against Privatisation: (i)** Concentration of economic power, **(ii)** Substitution of monopoly power, **(iii)** Lop-sided development of industries, **(iv)** Industrial sickness, **(v)** Entry of multinationals, **(vi)** No safety for the weaker sections, **(vii)** Social institutions, **(viii)** Corruption.
- **Globalisation:** Globalisation means integrating the economy of the country with the world economy.
- **Factors fostering Globalisation in India: (i)** Technical changes, **(ii)** Competition, **(iii)** Liberalisation policies, **(iv)** Emergence of United States as a super power, **(v)** Experiences of developing countries, **(vi)** Other factors.
- **Effects of Globalisation:**
  - **(1) Favourable Effects: (i)** Increasing share of exports in world trade, **(ii)** Favourable effect on Export-Import Ratio, **(iii)** Application of high technology, **(iv)** Stable and strong exchange rate.
  - **(2) Adverse Effects: (i)** Decrease in revenue of Indian industries, **(ii)** Increasing share in capital and management by foreign entrepreneurs, **(iii)** Increasing regional disparities, **(iv)** Export of profit.
- **Suggestions Regarding Globalisation: (i)** Improvement in Competitiveness of Indian producers, **(ii)** Alliance with MNCs, **(iii)** Self-sufficiency in technology, **(iv)** Facing international protectionism, and **(v)** Modernisation of agriculture and small sector.
- **Outsourcing:** Outsourcing means obtaining goods and services by contract from an outside source.
- **World Trade Organisation:** From January 1, 1995, WTO has been working. It has replaced the GATT. The objective of WTO was free trade in order to help in the growth and development of all member countries. The WTO acts as a permanent watch dog of international trade.
- **Achievements of LPG Policies: (i)** Rise in GDP growth, **(ii)** Rise in foreign exchange reserves, **(iii)** Control of inflation, **(iv)** Rise in flow of foreign capital, **(v)** Rise in competitiveness of industrial sector, **(vi)** Rise in integration with the world economy.
- **Demonetisation:** It is the process of stripping a currency unit from its status as legal tender in the country.
  Demonetisation results in change in national currency.
  The present currency in circulation is pulled off and new currency is circulated.
- **Types of Demonetisation**
  - **(i)** Total Demonetisation
  - **(ii)** Partial Demonetisation
- **Purposes sought by Demonetisation**
  - **(i)** Stripping corruption
  - **(ii)** Combating inflation
  - **(iii)** Curbing counterfeit currency
  - **(iv)** Combating tax evasion
  - **(v)** Increasing performance of economy

- **History of Demonetisation in India:**
  (i) On 12/01 /1946 - all notes of denominations of ₹500 and ₹1,000 were demonetised with a time limit of 10 days to exchange demonetised notes. Its purpose was to catch tax evaders.
  (ii) On 16/01/1978 - all notes of denominations of ₹1,000, ₹5,000 and ₹10,000 were demonetised with a time limit of 3 days to exchange demonetised notes. Its purpose was to catch corrupt leaders and officials in predecessor governments.
  (iii) On 08/11/2016 - all notes of denominations of ₹500 and ₹1,000 were demonetised with a time limit of 50 days to exchange demonetised notes from banks and some essential service stores.
- **Demonetisation of 2016**
  (i) On 8 November, 2016, the Government of India announced the demonetisation of all ₹500 and ₹1,000 bank notes of the Mahatma Gandhi Series.
  (ii) ₹500 (new series) and ₹2,000 notes were introduced.
  (iii) 50 days' time limit given for exchange of demonetised notes.
  (iv) Limits were put on exchange per day and withdrawal per day (and week) during this time.
  (v) Mixed reaction by public but strongly criticized by opposition.
- **Effects of 2016 Demonetisation**
  (i) Pushed India towards cashless economy
  (ii) Raised tax payments
  (iii) Brought an end to black money
  (iv) Curbed terrorist funding
  (v) Curbed effect on growth and revenues of MSMEs
- **Goods and Service Tax (GST)**
- **Objectives of GST**
  (i) To eliminate the cascading impact of taxes on production and distribution cost of goods and services
  (ii) Streamlining indirect tax regime
  (iii) Growth of revenue in States and Union Territories
  (iv) Reduction in transaction costs and unnecessary wastages
  (v) Elimination of the multiplicity of taxation
  (vi) One Point Single Tax
  (vii) Reduction in average tax burdens
  (viii) Reduction in the corruption
- **Types of GST laws**
  (i) At the centre level - Central GST (CGST)
  (ii) At the state level - State GST (SGST)
- **Benefits of GST**
  (i) GST provides comprehensive and wider coverage of input credit set off. You can use service tax credit for the payment of tax on sale of goods, etc.
  (ii) Many indirect taxes in state and central level have been included by GST. You need to pay a single GST instead of all.
  (iii) Uniformity of tax rates across the states.
  (iv) Ensure better compliance due to aggregate tax rate reduction.
  (v) By reducing the tax burden, the competitiveness of Indian products in international market has increased and thereby development of the nation.
  (vi) Prices of goods are expected to reduce in the long run as the benefits of less tax burden would be passed on to the consumer.

Know the Terms

- **Economic Development:** It is a comprehensive concept including increasing real per capita income of a country over a long period of time along with reduction in poverty, inequality and unemployment.
- **Per Capita Income:** The average of the national income with respect to the population of the country.
- **Demography:** The type of population living within the territory of a country.
- **Growth:** It refers to increase in the country's capacity to produce the output of goods and services within the country.
- **Modernisation:** Adaptation of new technology for economic growth and development.
- **Self-reliance:** The state of being self-sufficient so as to decrease imports.
- **Agriculture:** The economic activity that is related to growing of food and other related activities.

- **HYV seeds:** The variety of seeds that gives more agricultural produce.
- **Marketed Surplus:** The portion of the produce sold by the farmers in the market.
- **Fertilizers:** The chemical used to increase the fertility of the soil.
- **Pesticides:** The chemical used to kill the pests.
- **Competitiveness:** The degree to which a firm succeeds in selling its product when there is competition in the market place.
- **Contracting out:** Buying in inputs from an independent supplier rather than sourcing all inputs from inside the organisation.
- **Food Processing Industry:** The industries that are completely dependent on agriculture.
- **Urbanisation:** The process of growth in the urban areas in a country.
- **Industrialisation:** The process of growth of industry in a country or area.
- **Tariff:** Tariff are the tax imposed on imported goods.
- **Quota:** Quota is the specific quantity that can be imported from a foreign nation.
- **Domestic Firm:** The firm that operates and is registered within the territory of the country.
- **Balance of payment crisis:** If imports persistently exceed exports and if holders of the currency begin to lose confidence in the capacity of the economy to pay for their imports, it is said to be the balance of payment crisis.
- **Bank note:** A note issued by a bank which makes a promise to pay on demand of the bearer.
- **Economic integration:** Refers to the increasing interdependence of modern economies. Integration grows through increased international trade and increases further within economic unions such as EU.
- **Economic Union:** It involves the creation of an area composed of several different economies in which all agree to use the same economic policies and regulations.

UNIT – 7 : CURRENT CHALLENGES FACING INDIAN ECONOMY

CHAPTER-6

CURRENT CHALLENGES FACING INDIAN ECONOMY

Revision Notes

Poverty

- **Meaning of Poverty:** Poverty refers to a state in which an individual is unable to fulfill even the basic necessities of life.
- **Relative Poverty:** It refers to poverty of people in comparison to other people, regions or nations.
- **Absolute Poverty:** It means the inability to arrange for the basic human needs such as food, clothing, health facilities, housing, etc.
- **Causes of Poverty in India**
  - **(i) Economic Causes:** **(a)** Excessive dependence on agriculture, **(b)** Lack of industrialisation, **(c)** Lack of capital formation, **(d)** Lack of efficient entrepreneurship, **(e)** Rapid increase in population, **(f)** Un-equal distribution of National Income, **(g)** Low productivity, **(h)** Unemployment and semi-employment, **(i)** Inflationary pressure, and **(j)** Vicious circle of poverty.
  - **(ii) Social Causes:** **(a)** Traditional Conventions, **(b)** Belief in destiny, **(c)** Policy of non-violence **(d)** Prevalent child marriage, **(e)** Illiteracy and ignorance, and **(f)** Caste system.
  - **(iii) Political and Administrative Causes:** **(a)** Political instability, and **(b)** Failure of government policies.

  Special Programmes of Poverty Alleviation:
- **Self-Employment or Wage Employment Programme**
  - **(i)** Rural Employment Generation Programme
  - **(ii)** Prime Minister's Rozgar Yojana
  - **(iii)** Swarna Jayanti Shahari Rozgar Yojana
  - **(iv)** Sampoorna Grameen Rozgar Yojana

- **Programmes to improve the food and nutritional status of the poor**
  - **(i)** Public Distribution System
  - **(ii)** Integrated Child Development Scheme
  - **(iii)** Mid-day Meal Scheme
- **Programmes to develop infrastructure**
  - **(i)** Pradhan Mantri Gram Sadak Yojana
  - **(ii)** Pradhan Mantri Gramodaya Yojana
  - **(iii)** Valmiki Ambedkar Awas Yojana
- **National Social Assistance Programmes**
  - **(i)** Indira Gandhi National Old Age Pension Scheme
  - **(ii)** Indira Gandhi National Widow Pension Scheme
  - **(iii)** Indira Gandhi National Disability Pension Scheme
  - **(iv)** National Family Benefit Scheme
  - **(v)** Annapurna Scheme
- **Other Programmes**
  - **(i)** Food for Work Programme
  - **(ii)** National Maternity Benefit Yojana
- **Flaws in Anti-Poverty Programmes**
  - **(i)** Inadequate Financial Limits
  - **(ii)** Lack of Interest
  - **(iii)** Poor targeting
  - **(iv)** Lack of Accountability and
  - **(v)** Chain of mediators

Rural Development

- India is primarily a country of villages. Our most of the poor people live in villages. In our almost all the five year plans focal point has been rural development. Even though, we could not develop our villages. If we are really interested in rural development, we will have to develop villages.
- **Rural Development:** Process of improving living standard in terms of quality of life and economic well-being of low income group people living in rural areas and making these development efforts permanent.
- **Key Issues in Rural Development:** **(i)** Development of human resources, **(ii)** Land reforms, **(iii)** Development of basic infrastructure, **(iv)** Poverty alleviation, **(v)** Development of productive resources.
- **Rural Credit:** That need of agriculture credit which are required for the completion of agriculture works is known as agricultural credit/finance.
- **Classification of Agricultural Credit:**

  Short-Term Credit: It is required for a period of 6 to 12 months for buying seeds, tools, manure, fertilizers, etc.

  Medium-Term Credit: It is required for about one to five years for digging wells, buying machinery, etc.

  Long-Term Credit: It is required for the period of 5 to 20 years for the purchase of tractors, land, costly equipment, tube wells, etc.
- **Sources of Agricultural Credit:** **(i)** Non-Institutional Credit and **(ii)** Institutional Credit.

  (i) Non-Institutional Sources: **(a)** Moneylender, **(b)** Sahukars, **(c)** Commission agents, **(d)** Zamindars, **(e)** Relatives and friends, etc.

  (ii) Institutional Sources: **(a)** Government, **(b)** Co-operative credit societies, **(c)** Commercial banks, **(d)** Regional Rural Banks, **(e)** NABARD, **(f)** Micro Finance Programmes and **(g)** Kisan Credit Card.
- **Problems of Agricultural Credit**: **(i)** Lack of financing institutions, **(ii)** Lack of co-ordination, **(iii)** Loss of time and money, **(iv)** Problem of agriculture warehousing, **(v)** High rate of interest, **(vi)** Non-availability of credit at proper time, **(vii)** Differences in working system.

- **Agricultural Marketing:** "Agriculture Marketing includes all those activities which are related with the agricultural produce to deliver from farmers to ultimate consumers."
- **Defects of Agricultural Marketing in India: (i)** Forced sale, **(ii)** Lack of transportation, **(iii)** Lack of institutional finance, **(iv)** Lack of organisation, **(v)** Inadequate and unscientific storage system, **(vi)** Lack of grading, **(vii)** Lack of market information, **(viii)** Predominance of intermediaries, **(ix)** Fraudulent practices, **(x)** Lack of financial facilities.
- **Government Measures to Improve the System of Agricultural Marketing: (i)** Establishment of regulated markets, **(ii)** Facilities for storage, **(iii)** Construction of village storage, **(iv)** Facilities of grading and standardisation, **(v)** Improvement in weight and measurement measures, **(vi)** Better transport arrangements, **(vii)** Price stabilisation, **(viii)** Establishment of special boards, **(ix)** Organisation of co-operative marketing societies, **(x)** State trading in food-grains, **(xi)** Scientific storage in rural areas, **(xii)** Establishment of TRIFED.
- **Diversification of Agricultural Activities:** Diversification of agricultural activities mean basically to grow multiple crops and extension of activities subsidiary to agriculture. It has two aspects:

  (i) Change in cropping pattern

  (ii) Diversification of agricultural activities
- **Need of Diversification: (i)** To reduce the risk of agriculture, **(ii)** To meet challenges of poverty and other odd situations, **(iii)** To reduce the burden of population on agriculture.
- **Diversification of Agriculture Activities in India: (i)** Animal husbandry, **(ii)** Fisheries, **(iii)** Poultry, **(iv)** Horticulture, **(v)** Use of I.T.

Human Capital Formation

- **Human Capital Formation:** It refers to the process of acquiring and increasing the number of persons who have the skill, education and experience which are critical for the economic and political development of a country.
- **Difference between Human Capital and Physical Capital Formation:** In physical capital, the entrepreneur possesses knowledge to calculate the expected rate of return on a range of investment and then rationally decides which investment should be made. In human capital, an individual is influenced by the peers, educators and society regarding human capital investment.
- **Importance of Human Capital Formation in Economic Development: (i)** Optimum utilisation of resources, **(ii)** Helpful in production of National Wealth, **(iii)** Co-ordination, **(iv)** Speed up the rate of economic growth, and **(v)** Changes in the outlook of the labour force.
- **Sources of Human Capital: (i)** Investment on health and nutrition, **(ii)** Investment on education and training, **(iii)** Housing development, **(iv)** Migration, and **(v)** Expenditure on information.
- **Human Development Index (HDI):** Human development index is broadly an arrangement of social aggregates, average of longevity, knowledge and access to resources.
- India's position is 130th out of 189 countries of the world. It is from the HDI prepared by UNDP in 2018. The value of HDI is 0.638.
- **Problems of Human Capital Formation: (i)** Problem of estimation of total stock of human capital, **(ii)** Problem of estimation of growth rate of human capital formation, **(iii)** Neglect of on-the-job training programme, **(iv)** Lack of initiative, **(v)** Regional disparities, **(vi)** Lack of foreign exchange funds, and **(vii)** Brain drain.
- **Education:** An essential element of human resource development.
- **What is Education:** It refers to the process of teaching, training and learning especially in schools or colleges, to improve knowledge and develop skill.
- **Human Capital and Economic Growth:** Economic growth means the increase in real national income of a country. Higher rate of economic growth is possible only through human capital. In fact, there are two main sources of human capital: **(i)** Education, and **(ii)** Health.

  These two sources play an important role in the economic growth.
- **Human Capital and Human Development:** The two terms human capital and human development seems similar but there is a big difference between the two. Human capital increases knowledge, skills and capacities of the people of the country. Human development, on the other side, considers education and health as integral to human well-being. In the human development, human beings are considered as ends themselves.

Know the Terms

- **Chronic Poor:** Those who are always poor but sometimes have a little more money are grouped together as chronic poor.
- **Churning Poor:** Those who regularly move in and out of poverty line are grouped together as churning poor.
- **Occasionally Poor:** The people who are mostly rich but have a patch of time for poverty.
- **Transient Poor:** Those who are rich most of the time but may sometimes have a patch of bad luck are grouped together as transient poor.
- **Poverty line:** A cut-off point on the income distribution which divides the population as poor and non-poor. People below poverty line are poor and above that line are average or rich.
- **Trickle-down effect:** The transfer of income from assets owing person to non-assets owing person is called trickle-down effect.
- **Poverty Alleviation:** The reduction of poverty.
- **Co-operative Marketing:** A measure to ensure a fair price to farmers. Member farmers sell their surplus to the co-operative society which substitutes collective bargaining in place of individual bargaining. It links rural credit farming marketing processes to the best advantage of the farmers.
- **Self Help Groups (SHGs):** A group formed by some people to promote thrift in small proportions by a minimum contribution from each member. From the pooled money, credit is given to the needy members to be repayable in small instalments at reasonable interest rates.
- **Warehouse:** A storage facility for storing tangible goods.
- **Animal Husbandry:** The process of nurturing and rearing animals to earn from selling their produce.
- **Horticulture:** The growing of fruits, flowers, plantation crops, spices, vegetables, tuber crops, flowers, medicinal and aromatic plants.
- **Brain Drain:** A large scale emigration of a large group of individuals with technical skill of knowledge.
- **Preventive medicine:** Vaccination given at the time of the disease to control its spread.
- **Curative medicine:** Medical intervention during illness to cure a person.
- **Social medicine:** Spread of health literacy in order to spread awareness with regard to a particular disease.

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