

Money and Credit

Level - 1

CORE SUBJECTIVE QUESTIONS

MULTIPLE CHOICE QUESTIONS (MCQs)

1. Option (C) is correct

Explanation: (i) Credit plays a vital and positive role in meeting his target and accelerating his income because it allows him to invest in production during the festive season, where demand is high.

(ii) Credit helps him meet the ongoing expenses of production, such as purchasing raw materials and paying wages.

(iii) Credit helps him complete the production on time by ensuring he has the necessary resources.

(iv) Option is incorrect as it describes a negative outcome that is not related to the importance of credit in achieving production and income goals.

2. Option (C) is correct

Explanation: Average income of family

$$= \frac{\text{Total income of family}}{4}$$

$$\frac{50,000 + 40,000 + 20,000 + 2,000}{4}$$

$$= \frac{1,30,000}{4} = ₹ 32,500$$

3. Option (D) is correct

Explanation: Lenders require collateral to reduce the risk of financial loss if the borrower fails to repay the loan. Collateral acts as a security that the lender can claim and sell to recover the loan amount in case of default. This helps protect the lender's investment.

4. Option (B) is correct

Explanation: The income of the bank primarily comes from the interest rate differential. Banks pay a lower rate of interest to depositors for the money they deposit. Banks charge a higher rate of interest from borrowers for loans they take. The difference between these two interest amounts is the bank's primary source of income. This is represented in the given diagram, where depositors and borrowers interact with the bank.

5. Option (A) is correct

Explanation: Average Income = $\frac{\text{Total income}}{4}$

$$\frac{2,000 + 5,000 + 3,000 + 6,000}{4} = ₹ 4,000$$

6. Option (D) is correct

Explanation: The primary purpose of loans offered by banks is to provide financial resources that help individuals, businesses, and industries grow. By lending money, banks enable businesses to expand and create jobs, individuals to invest in housing, education, or other productive activities, farmers to improve agricultural productivity, infrastructure development and industrial growth. All these activities collectively contribute to economic growth.

7. Option (A) is correct

Explanation: The cheque number is typically printed at the bottom of a cheque, usually on the far left side. From the given cheque image, the cheque number is 362255, as it is the first set of digits printed at the bottom of the cheque.

8. Option (C) is correct

Explanation: The Reserve Bank of India (RBI) is the central bank of India, responsible for:

Issuing currency: The RBI is the sole authority for printing and issuing the currency notes in India (except for coins, which are minted by the Government of India).

Regulating the credit system: The RBI manages monetary policy, regulates interest rates, and oversees the banking system to ensure financial stability.

The other banks mentioned (Punjab National Bank, Indian Bank, and State Bank of India) are commercial banks that provide banking services but do not control the issuance of currency or regulate the credit system.

9. Option (B) is correct

Explanation: Salim uses the credit to meet his working capital needs and ensure the production process is completed on time. This results in an

increase in productivity, which ultimately boosts his income.

Option (A) and (D) refer to negative impacts of credit, which are not applicable in this case as Salim is using the credit effectively. Option (C) is incorrect because the credit allows Salim to maintain or increase production rather than decrease it.

10. Option (D) is correct

Explanation: The farmer initially borrows from a moneylender who charges a high interest rate, making repayment difficult and pushing him toward a debt trap. By borrowing from a bank at a lower interest rate, the farmer is able to gradually repay both the moneylender and the bank, avoiding the debt trap. The bank's role here is to provide affordable credit, which helps the farmer escape the cycle of high-interest loans and financial distress.

11. Option (C) is correct

Explanation: Moneylenders are often the most readily available source of credit in rural areas where formal financial institutions (like banks or co-operative societies) have limited reach. They can provide quick loans, which can be crucial in urgent situations like medical emergencies or immediate crop expenses.

12. Option (C) is correct

Explanation: The primary source of income for banks is the interest charged on loans they provide to borrowers. Banks lend money at a higher interest rate (lending rate) than the rate they pay on deposits (deposit rate), and the difference forms the main component of their income.

13. Option (A) is correct

Explanation: Average Income = $\frac{\text{Total income}}{4}$

$$\frac{10,000 + 20,000 + 30,000 + 40,000}{4} = \frac{1,00,000}{4} = ₹ 25,000$$

14. Option (D) is correct

Explanation: Formal sources of credit are those that are regulated by the government or financial institutions and operate within a legal framework. Co-operative societies fall into this category because they are registered entities that provide credit to their members, often at lower interest rates, and are subject to oversight by regulatory bodies.

15. Option (D) is correct

Explanation: Rich households often have the necessary documentation, collateral, and credit worthiness required to access loans from banks and other formal financial institutions. Banks and formal lenders perceive rich households as low-risk borrowers, making it easier for them to secure loans at favourable interest rates.

16. Option (D) is correct

Explanation: The Reserve Bank of India (RBI) is responsible for issuing currency notes in India under the provisions of the Reserve Bank of India Act, 1934. The RBI manages the design, production, and distribution of currency notes, except for one-rupee notes and coins, which are issued by the Central Government.

17. Option (D) is correct

Explanation: In a Self-Help Group (SHG), decisions regarding savings and loan activities are taken collectively by the members of the group. SHGs are typically small, informal groups of people who come together to save money regularly, pool their resources, and provide loans to members as needed.

18. Option (A) is correct

Explanation: Statement I is correct because Self-Help Groups (SHGs) provide loans to members without requiring collateral. They operate on mutual trust and group guarantees, enabling members to access credit even if they do not have assets to offer as security.

Statement II is false because loans provided by SHGs generally come at low interest rates. The purpose of SHGs is to support members financially in a sustainable and affordable manner.

MATCH THE FOLLOWING QUESTIONS

1. Option (A) is correct

Explanation: Barter system is system where commodity is exchanged for commodity, Cooperative society is a formal source for loan, Reserve bank of India is authorised to supervise the working of other banks.

2. Option (A) is correct

Explanation: The Reserve Bank of India (RBI) is the central banking institution responsible for issuing currency notes and coins in India. The

Ministry of Finance oversees the issuance of one-rupee notes or coins in India. Cooperative societies often provide affordable credit options in rural areas through various financial products and services tailored to the needs of their members. Chit funds, prevalent in India, represent a form of savings arrangement within the unorganised money market, where individuals pool funds through periodic contributions over a defined duration.

ASSERTION-REASON QUESTIONS

1. Option (C) is correct

Explanation: Assertion is true because the Indian Rupee (INR) is the official currency of India and is legally recognised for all transactions within the country. Under the Indian Coinage Act, 2011, the Indian Rupee is the legal tender, and it is the mandatory currency for payments within India. Refusing to accept payment in rupees would be illegal.

Reason is false because the rupee is authorised and issued by the Reserve Bank of India (RBI), which is the central bank of the country, not by state governments. The RBI is responsible for the regulation of currency and monetary policy, while state governments do not have any role in authorizing the rupee.

2. Option (A) is correct

Explanation: Banks typically assess a borrower's credit worthiness before granting loans. Borrowers who cannot provide adequate collateral or proof of repayment capacity may not qualify for loans, leading banks to deny them credit.

Reason is and serves as a key reason why banks are hesitant to lend to certain borrowers. Collateral is an asset that banks use as security against a loan, reducing their risk of non-repayment. Individuals who lack assets such as land, property, or savings often struggle to meet this requirement, making it difficult for banks to justify lending to them.

Both the Assertion (A) and Reason (R) are correct, and the lack of collateral is indeed a major reason why banks may refuse loans to certain borrowers.

3. Option (A) is correct

Explanation: Assertion is true because a significant portion of rural households in India relies on

informal credit sources like moneylenders, traders, and relatives. These sources are more accessible to them despite high-interest rates and exploitative practices.

Reason is also true and explains why rural poor families depend on informal credit. Banks often require collateral (Tangible assets like land, property, or savings as security) and special Documents like identity proof, income proof, or credit history, which rural poor families may not possess. These requirements make it difficult for rural poor families to access formal credit, pushing them toward informal sources, where such conditions are absent.

4. Option (A) is correct

Explanation: Assertion is true because Self-Help Groups (SHGs) empower individuals, especially marginalised sections such as rural women, to collectively make decisions about saving, borrowing, and using resources. This participatory approach fosters economic democracy by decentralising financial decision-making and reducing dependence on exploitative sources of credit.

Reason is also true and explains why SHGs promote economic democracy. By pooling resources and enabling members to access credit and entrepreneurship opportunities.

Both Assertion (A) and Reason (R) are correct, and the Reason (R) provides the correct explanation for the Assertion (A) as SHGs promote economic democracy by ensuring a more equitable distribution of economic power and opportunities.

VERY SHORT ANSWER TYPE QUESTIONS

1. (i) To develop water harvesting.
(ii) Development of irrigation facilities.
(iii) Development of Self-Help Group.
(iv) Development of animal husbandry.
(v) Development of infrastructural facilities.
(vi) Development of cottage industries. (Any two)
2. (i) Repayment of the loan is crucially dependent on the income from farming.
(ii) The failure of the crop made loan repayment impossible.
(iii) Sometimes the borrower is not able to repay the loan.
(iv) Many a times borrower is caught into the situation of debt-trap.
(v) To repay her loan person has to sell a portion of her/his land.
(vi) The situation of the person gets much worse off than before. (Any two)

3. The banks get their income from:

- (i) **Interest on Loans:** Banks earn money by charging interest on the loans they provide to individuals and businesses. The interest rate on loans is higher than the rate they pay on deposits.
- (ii) **Fees and Services:** Banks charge fees for various services, such as account maintenance, ATM transactions, and processing loans.
- (iii) **Investments:** Banks invest in government securities, bonds, and other financial instruments to earn additional income.

4. The terms of credit in Lalita's case are:

- (i) Loan Amount: ₹. 2 lakhs.
- (ii) Rate of Interest: 7% per annum.
- (iii) Repayment Period: 24 monthly instalments.
- (iv) Purpose: To support her small baking business.

SHORT ANSWER TYPE QUESTIONS

1. (i) Credit helps to set up Industries.
(ii) Credit helps to start businesses.
(iii) It helps to improve the standard of living of the people.
(iv) In rural areas, credit helps in the development of agriculture by providing funds to farmers to buy seeds, fertilisers, expensive pesticides etc.
(v) It helps to generate employment. (Any three)
2. (i) A large number of transactions in our day-to-day activities involve credit in some form or the other.
(ii) Credit refers to an agreement in which the lender supplies the borrower with money, goods or services in return for the promise of future payment.
(iii) The credit helps people to meet the ongoing expenses of production, complete production on time and thereby increase his earnings.
(iv) Credit plays a vital and positive role in case people need working capital for production. Like crop production involves considerable costs on seeds, fertilisers, pesticides, water, electricity, repair of equipment etc.
(v) Farmers usually take crop loans at the beginning of the season and repay the loans after harvest. Repayment of the loan is crucially dependent on the income from farming. (Any three)
3. (i) To save poor farmers and workers from the exploitation.
(ii) Formal sector charge a low interest rate on loans.
(iii) To save from debt trap.
(iv) It provides cheap and affordable credit.
(v) RBI supervises the formal sector credit through various rules and regulations which ensures that banks give loans to small cultivators, small borrowers etc. and not just to profit – making business and traders. (Any three)
4. (i) The RBI issues currency notes on behalf of the central government.
(ii) It supervises the functioning of formal sources of loans.
(iii) The RBI monitors the banks to maintain the cash balance.
(iv) The RBI sees that the banks give not just to profit-making businesses and traders but also to small cultivators, small scale industries, to small borrowers etc.
(v) Periodically, banks have to submit information to the RBI on how much they are lending, to whom, at what interest rate, etc. (Any three)
5. (i) Banks accept the deposits and pay an amount as interest on the deposits.
(ii) Banks keep only a small proportion of their deposits as cash with themselves.
(iii) This is kept as provision to pay the depositors who might come to withdraw money from the bank on any given day.
(iv) Banks use the major portion of the deposits to extend loans.
(v) Banks make use of the deposits to meet the loan requirements of the people.
(vi) In this way, banks mediate between those who have surplus funds (the depositors) and those who need these funds (the borrowers).
(vii) Banks charge a higher interest rate on loans than what they offer on deposits.
(viii) The difference between what is charged from borrowers and what is paid to depositors is their main source of income. (Any three)
6. The use of money spans a significant part of our everyday life because it serves as a:
(i) **Medium of Exchange:** Money is used to buy goods and services. For example, we use cash or digital payments to purchase groceries, clothing, or tickets.
(ii) **Store of Value:** Money allows us to save for future needs. For instance, we deposit savings in a bank to use later for education, medical emergencies, or investments.
(iii) **Unit of Account:** Money helps in comparing the value of goods and services. For example, we can compare the price of a laptop to that of a phone and make

LONG ANSWER TYPE QUESTIONS

1. Self Help Groups help the poor to become self-reliant in terms of savings and generating income.
(i) Can avail the facilities of loans from formal sources like banks at a low rate of interest.
(ii) They do not demand collateral and so she can easily access.
(iii) Self-help groups are exclusively meant for rural women like Miss X to make them economically independent through self-employment opportunities.
(iv) This will help her to start and expand her business and thus, improving the standard of living.
(v) **Skill development:** SHGs in India have also been successful in providing skill development and training opportunities to women. Through training programs, she can be equipped with the necessary skills to start and run a successful business.

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- (vi) **Social empowerment:** By providing a platform for women to come together, share their experiences, and support each other, SHGs have empowered women to take charge of their lives and become active participants in their communities.
2. (i) In a barter system where goods are directly exchanged without the use of money, double coincidence of wants is an essential feature. In contrast, in an economy where money is in use, money by providing the crucial intermediate step eliminates the need for double coincidence of wants.
- (ii) People with the help of money can purchase whatever they need. No goods or other items are needed for exchange anymore. Since money acts as an intermediate in the exchange process, it is called a medium of exchange.
- (iii) Modern forms of money include currency — paper notes and coins. Unlike the things that were used as money earlier, modern currency is not made of precious metals such as gold, silver and copper. And unlike grain and cattle, they are neither of everyday use. The modern currency is without any use of its own.
- (iv) It is accepted as a medium of exchange because the currency is authorised by the government of the country. In India, the Reserve Bank of India issues currency notes on behalf of the central government. As per Indian law, no other individual or organisation is allowed to issue currency. Moreover, the law legalises the use of rupee as a medium of payment that cannot be refused in settling transactions in India. No individual in India can legally refuse a payment made in rupees. Hence, the rupee is widely accepted as a medium of exchange.
3. (i) SHGs help the rural poor, in particular women.
- (ii) A typical SHG has 15-20 members, usually belonging to one neighbourhood, who meet and save regularly. Saving per member varies from ₹ 25 to ₹ 100 or more, depending on the ability of the people to save. Members can take small loans from the group itself to meet their needs.
- (iii) The group charges interest on these loans but this is still less than what the moneylender charges. After a year or two, if the group is regular in savings, it becomes eligible for availing loan from the bank.
- (iv) Loan is sanctioned in the name of the group and is meant to create self-employment opportunities for the members.
- (v) For instance, small loans are provided to the members for releasing mortgaged land, for meeting working capital needs (e.g. buying seeds, fertilisers, raw materials like bamboo and cloth), for housing materials, for acquiring assets like sewing machine, handlooms, cattle, etc.
- (vi) Most of the important decisions regarding the savings and loan activities are taken by the group members. The group decides as regards the loans to be granted – the purpose, amount, interest to be charged, repayment schedule, etc.
- (vii) Rural household face a problem of getting loan from the formal sector due to the lack of collateral.
- (viii) Self Help Group helps the poor household in getting loans easily and prevents them from falling under the clutches of moneylenders.
4. (i) Cheap and affordable credit would lead to higher income.
- (ii) If the credit is affordable then many people could borrow variety of needs.
- (iii) People could grow crops, do business, set up small scale industries, etc.
- (iv) People could set up new industries or trade in goods.
- (v) Banks and Co-operatives should increase their lending particularly in the rural areas, so that the dependence on informal sources of credit reduces.
- (vi) It is also necessary that everyone receives these loans.
- (vii) It is important that the formal credit is distributed more equally so that the poor can benefit from the cheaper loans. (Any five)
5. Credit plays two roles-positive and negative.
- Positive role of credit:**
- (i) A large number of transactions in day to day activities involve credit.
- (ii) The credit helps to meet the ongoing expenses of production.
- (iii) Credit plays a positive role when the borrower is able to return the loan amount on time and also makes some profit with the use of that money.
- (iv) It makes a person better off than before.
- Negative role of credit:**
- (i) Sometimes failure of the crop makes loan repayment impossible.
- (ii) Sometimes credit is very painful as it pushes the borrower into such a situation from which recovery is very difficult.
- (iii) In this situation the borrower is not able to repay the loan.

- (iv) Many times caught into the situation of debt-trap.
 - (v) To repay loan one has to sell portion of one's land.
6. Collateral is an asset that the borrower owns and uses this as a guarantee to lenders until the loans are repaid. Property such as land, deposits with banks, livestock are some examples of collateral used for borrowing.

The reason to prevent the poor getting a loan from banks are:

- (i) Absence of collateral with the poor.
- (ii) Absence of documents with them.
- (iii) Absence of formal sources of credit in rural area.
- (iv) Lack of education and awareness among them.

Level - 2 ADVANCED COMPETENCY FOCUSED QUESTIONS

MULTIPLE CHOICE QUESTIONS (MCQs)

1. Option (B) is correct

Explanation: The statement "Money eliminates the need for a double coincidence of wants" highlights one of the main functions of money—it serves as a medium of exchange. In a barter system, a transaction could only occur when both parties wanted what the other had (double coincidence of wants). Money removes this limitation, allowing people to sell goods or services in exchange for money and then use that money to buy what they need from others, even if those others don't want what the first person is offering.

2. Option (C) is correct

Explanation: Formal sources of credit (like banks and cooperatives) are supervised by the Reserve Bank of India (RBI), which ensures fair lending practices, reasonable and regulated interest rates, proper documentation and legal procedures, and transparency in loan terms and conditions. This makes borrowing from formal sources safer and more reliable compared to informal sources like moneylenders, who may charge very high interest and exploit borrowers. Hence, the primary advantage is that the loans are regulated and transparent.

3. Option (C) is correct

Explanation: The statement shows that the impact of credit depends on how it is used and the circumstances of the borrower.

Positive consequence: If the loan is used productively (e.g., to expand a business or buy tools for farming), it can increase income and

improve the borrower's financial condition.

Negative consequence: If the loan is used for non-productive purposes or the borrower is unable to repay, it can lead to a debt trap, causing further financial distress.

Thus, credit is not always good or bad—its effects depend on usage, repayment ability, and loan terms.

4. Option (C) is correct

Explanation: The fact that most poor households in rural areas rely on informal sources of credit indicates that Banks and formal institutions often require collateral, documents, and involve lengthy procedures, making them less accessible to the poor. Informal lenders like moneylenders, relatives, or traders are easier to approach, but they often charge very high interest rates and can be exploitative. This reflects a major challenge in rural India — the lack of access to affordable and fair credit from formal sources.

5. Option (C) is correct

Explanation: Self Help Groups (SHGs) are becoming popular among the rural poor because they allow members (usually women) to save small amounts regularly, provide small loans to members for needs like starting a business, farming, or medical expenses, encourage self-reliance, mutual support, and financial discipline, often get linked to banks, improving access to formal credit. SHGs help reduce the dependence on moneylenders and promote economic independence, especially in rural areas.

ASSERTION-REASON QUESTIONS

1. Option (A) is correct

Explanation: Assertion is true. Money acts as a medium of exchange, which means it is accepted by all in return for goods and services, making transactions easier.

Reason is also true because in a barter system, a transaction could only occur when both parties had what the other wanted — known as the double coincidence of wants. This made trade difficult.

Both assertion and reason are true and the reason correctly explains why money is needed as a medium of exchange — it removes the need for a double coincidence of wants.

2. Option (A) is correct

Explanation: Assertion is true because formal sources of credit (like banks and cooperatives) are generally better than informal sources because they offer lower interest rates, transparency, and legal protection.

Reason is also true:

These formal sources are monitored by the Reserve Bank of India (RBI), which ensures they follow fair lending practices, reasonable interest rates, and do not exploit borrowers.

Both assertion and reason are true and the reason clearly explains why formal credit sources are considered better — due to RBI supervision and regulation.

3. Option (C) is correct

Explanation: Assertion is true. Credit can sometimes lead to a debt trap when a borrower is unable to repay the loan and has to take additional loans to cover the original one. This leads to increasing debt and financial stress.

Reason is false. It is not true that borrowers always benefit from taking credit. If credit is not used wisely or if the borrower cannot repay, it can lead to loss of assets, mental stress, and poverty.

4. Option (A) is correct

Explanation: Assertion is true. Commercial banks keep only a small proportion of customer deposits as cash (usually around 15%) to meet the day-to-day withdrawal needs of depositors.

Reason is also true because the major portion of the deposits is used by banks to provide loans to individuals and businesses. Banks earn interest on these loans, which is their main source of income.

VERY SHORT ANSWER TYPE QUESTIONS

1. Money as a medium of exchange means it is commonly accepted in return for goods and services. Unlike the barter system, which required a double coincidence of wants, money allows people to sell what they have and buy what they need easily. This has made trade more efficient and convenient.
2. Banks keep only a small proportion of deposits as cash to meet the daily withdrawal needs of customers. The rest is used to provide loans to individuals and businesses. Banks earn interest on these loans, which is their main source of income.
3. Formal sources of credit are considered more reliable than informal ones because:
 - (i) They are regulated by the Reserve Bank of India (RBI): This ensures fair lending practices, such as reasonable interest rates and proper documentation.
 - (ii) They offer legal protection and transparency: Borrowers from banks and cooperatives get

clear loan terms, which protect them from exploitation and hidden charges.

4. **Positive Role of Credit:** A farmer takes a loan to buy better seeds and equipment. As a result, his harvest improves, and he earns more income, helping him repay the loan and improve his livelihood.

Negative Role of Credit (Debt Trap): A small trader takes a loan but suffers losses in business. He is unable to repay and has to borrow more, leading to a cycle of debt, or debt trap.

5. (i) **Access to Small Loans at Low Interest:** SHGs provide easy access to credit without collateral, helping rural women and the poor to start small businesses or meet emergency needs.
(ii) **Promotes Self-Reliance and Empowerment:** SHGs encourage saving habits, build confidence, and help rural women become financially independent and socially empowered.

SHORT ANSWER TYPE QUESTIONS

1. Money has removed the major difficulties of the barter system by overcoming the following limitations:
 - (i) **Lack of Double Coincidence of Wants:** In the barter system, both parties had to want exactly what the other had. Money solves this by acting as a common medium of exchange.
 - (ii) **No Standard Measure of Value:** It was difficult to decide how much of one item was equal in value to another. Money provides a uniform value system for goods and services.
 - (iii) **Difficulty in Storing Wealth:** Goods like grains or animals could perish or lose value over time. Money is durable and convenient to store, allowing people to save wealth for the future.
2. Credit can be helpful to borrowers in the following ways:
 - (i) **Promotes Productive Investment:** Borrowers can use credit to buy tools, raw materials, or machinery, helping them to expand their business or farm output, which increases income.
 - (ii) **Helps Meet Emergency Needs:** Credit provides immediate financial support during emergencies like medical expenses, crop failure, or family functions, reducing stress and instability.
 - (iii) **Improves Standard of Living:** With access to credit, people can afford to educate their children, build homes, or start small enterprises, leading to long-term economic and social upliftment.

3. The key differences between formal and informal sources of credit:
 - (i) **Regulation:**
Formal Sources (like banks and cooperatives) are regulated by the Reserve Bank of India (RBI).
Informal Sources (like moneylenders and traders) are not regulated by any government authority.
 - (ii) **Interest Rates:**
Formal Sources charge reasonable and fixed interest rates.
Informal Sources often charge very high and varying interest rates, which may lead to exploitation.
 - (iii) **Documentation and Legal Protection:**
Formal credit involves proper documentation and legal agreements, offering protection to the borrower.
Informal credit usually involves verbal agreements and no legal safeguards, increasing the risk for borrowers.
4. Self Help Groups (SHGs) offer several benefits to the rural poor, especially women:
 - (i) **Easy Access to Credit:** SHGs provide small loans without collateral at low interest rates, helping members to meet urgent needs or start small businesses.
 - (ii) **Economic Empowerment:** By encouraging savings and income-generating activities, SHGs help rural women become financially independent and contribute to their families' income.
 - (iii) **Social Confidence and Collective Strength:** SHGs build a sense of unity, self-confidence, and leadership among women. They often become more involved in decision-making within their homes and communities.
5. Commercial banks in India perform the following key functions that support the economy:
 - (i) **Accepting Deposits:** Banks accept deposits from the public in various forms like savings, current, and fixed deposits. This encourages saving habits and provides a safe place to store money.
 - (ii) **Providing Loans and Advances:** Banks use a major portion of the deposited money to give loans to individuals, farmers, and businesses for productive purposes. This helps in economic growth and development.
 - (iii) **Facilitating Payments and Settlements:** Commercial banks help in transferring money through cheques, demand drafts, debit/credit cards, and online banking, making financial transactions easy and efficient.

CASE BASED QUESTIONS

1. (i) Co-operative society is an example of formal source of credit.
(ii) Co-operative societies meet the requirements of rural people like purchase of agriculture implements, loans for cultivation and agricultural trade, etc.
(iii) (1) Contribution of members
(2) Loans from banks,
(3) Interest on loans given by Self Help Groups. (Any two)
2. (i) The loans meet the needs of buying raw materials and tools. The loans also help to build mud houses and workshops as well.
(ii) Yellamma is a member of a weavers' cooperative that pools money deposited by its members. The co-operative uses the pooled money as collateral to obtain a large loan from the bank. The bank grants the loan to the co-operative, which is then distributed among its members, including Yellamma.
(iii) Yellamma is more likely to get credit from a formal source because she is part of a co-operative, which acts as an intermediary and uses pooled funds as collateral to secure loans from banks. Her repayment history (re-paying two loans successfully) makes her a creditworthy borrower.
3. (i) Pratibha was unable to get a bank loan because she had no collateral or formal documents, which are required by formal credit sources like banks.
(ii) Sarojini benefited because the SHG gave her a loan at a low interest rate, and she became part of a supportive group that encourages savings and economic independence, unlike Pratibha, who was charged high interest by a moneylender.
(iii) Pratibha's experience shows that informal sources charge high interest rates, lack regulation, and often trap borrowers in a debt cycle.
To improve access to formal credit, the government can expand banking services and support Self Help Groups in rural and poor areas, making it easier for people without collateral to get affordable loans.
4. (i) Ravi is not worried because he took a loan from a formal source (bank) that offers flexible repayment terms and crop insurance, which protects him during natural disasters like cyclones.
(ii) Mahesh is under pressure to repay a high-interest loan and has mortgaged his land to a

local trader, which puts him at risk of losing his land and falling into a debt trap.

(iii) The benefits of SHG membership are:

- (1) Access to joint bank loans without needing individual collateral
- (2) Equal sharing of income and mutual financial support among members

SHGs promote financial security by encouraging savings, offering low-interest loans, and building a support system that helps members manage risks and earn regular income.

LONG ANSWER TYPE QUESTIONS

1. Credit plays a dual role in a person's financial life—it can either be helpful and promote economic growth, or it can become a burden, pushing the borrower into a debt trap, depending on how it is used.

Positive Example (Credit is Useful): A farmer takes a loan from a bank to buy good quality seeds and equipment. He gets a good harvest, sells the produce at a profit, repays the loan, and has money left for future use. In this case, credit helped him grow financially.

Negative Example (Credit is Harmful): A small trader borrows money from a moneylender at a high interest rate. His business suffers losses, and he is unable to repay the loan. The lender adds extra charges, and the borrower is forced to take more loans, leading to a debt trap.

The factors that determine whether credit is useful or harmful are:

- (i) **Purpose of the Loan:** If the loan is used for productive purposes (like investment in business or farming), it is more likely to be helpful.
 - (ii) **Source of Credit:** Loans from formal sources (like banks or cooperatives) are regulated and affordable, while informal sources may charge excessive interest, increasing the risk of a debt trap.
 - (iii) **Borrower's Ability to Repay:** If the borrower has a stable source of income and a plan for repayment, credit can be managed well. But if the borrower faces unforeseen losses or lacks income, it can lead to default and further borrowing.
2. Formal sources of credit, such as banks and cooperatives, play a crucial role in ensuring fair, regulated, and productive use of credit, especially in supporting economic growth and reducing poverty.

The features of formal sources of credit are:

- (i) **Regulated by the Reserve Bank of India (RBI):** All formal credit institutions operate under strict guidelines set by the RBI, which ensures transparency and fairness in lending practices.

- (ii) **Reasonable and Fixed Interest Rates:** Formal sources charge lower and regulated interest rates, unlike informal lenders who may exploit borrowers with very high rates.

- (iii) **Legal Documentation and Agreements:** Loans from banks and cooperatives involve proper paperwork, providing legal protection to both the lender and the borrower.

- (iv) **Availability of Long-Term and Purpose-Based Loans:** Formal credit institutions offer loans for specific needs such as agriculture, education, housing, or business, with flexible repayment options.

- (v) **Promotes Financial Inclusion and Development:** By providing access to affordable credit, formal sources help reduce poverty, encourage entrepreneurship, and support rural and urban development.

Difference from Informal Sources of Credit:

Aspect	Formal Sources	Informal Sources
Regulation	Regulated by RBI	Not regulated
Interest Rate	Fixed and reasonable	High and varies widely
Legal Protection	Borrowers are legally protected	No legal protection or accountability
Documentation	Proper documentation required	Usually no paperwork
Risk of Exploitation	Very low	High risk of exploitation and debt traps

3. Self Help Groups (SHGs) are small, voluntary groups of 10–20 rural women who come together to save regularly, provide credit to each other, and support one another financially and socially. They play a vital role in reducing poverty, empowering women, and improving access to credit in rural areas.

The ways in which SHGs benefit the rural poor are:

- (i) **Access to Low-Interest Loans without Collateral:** SHGs enable members to borrow small amounts easily from the group's savings or through bank linkages, without needing any security or collateral.

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- (ii) **Encouragement of Savings Habits:** SHGs help inculcate the habit of regular saving, even in small amounts, which helps build financial discipline and a sense of economic responsibility.
 - (iii) **Women's Empowerment and Confidence Building:** Being part of SHGs boosts self-confidence, leadership, and decision-making skills among rural women. It allows them to participate in economic and community affairs.
 - (iv) **Support for Income-Generating Activities:** SHGs often support members in starting small businesses like dairy farming, tailoring, or handicrafts, helping them earn a steady income and improve their standard of living.
 - (v) **Mutual Support and Social Security:** SHG members support each other during financial emergencies, creating a social safety net. This sense of solidarity reduces dependence on moneylenders and informal sources.
4. Modern forms of money include:
- Currency (paper notes and coins)
 - Bank deposits (money in savings and current accounts)
 - Digital money (used through debit/credit cards, UPI, mobile wallets, etc.)

The modern money is accepted in the economy because:

- (i) **Legally Authorised by the Government:** Modern money is issued and guaranteed by the Reserve Bank of India (RBI) and backed by the Government of India, making it legal tender.
- (ii) **Widespread Trust in the Banking System:** People accept bank-issued money because they trust banks and financial institutions to safely hold and transfer their money.
- (iii) **Ease of Use in Transactions:** Modern money is portable, divisible, and durable, making it convenient for everyday transactions, whether large or small.
- (iv) **Accepted by All in the Economy:** Modern money is universally accepted in exchange for goods and services, unlike the barter system, which required a double coincidence of wants.
- (v) **Supports Digital and Cashless Payments:** With growing digital infrastructure, modern money supports electronic payments, making transactions faster, more secure, and efficient.

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