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Class: X	Subject: Social Science	Session: 2025-26
Book: Economics	Type: PYQ (Board Exam)	Board: CBSE

Chapter 3 : Money and Credit

SECTION A : Multiple Choice Questions

(1 Mark Each)

Q1. What is the main reason why banks charge a higher interest rate on loans than they offer on deposits? [CBSE 2023] [1]

- (a) To earn profit (b) To pay tax (c) To help the poor (d) Government mandate

Ans: (a) To earn profit. The difference between interest charged on loans and interest paid on deposits is the main source of income for banks.

Q2. What is collateral? [CBSE 2022] [1]

- (a) A type of loan (b) Asset used as guarantee against a loan (c) A bank account (d) A cheque

Ans: (b) An asset that the borrower owns and uses as a guarantee to the lender until the loan is repaid. E.g., land, building, vehicle, livestock, deposits.

Q3. Which of the following is a formal source of credit? [CBSE 2024] [1]

- (a) Moneylender (b) Trader (c) Commercial bank (d) Relative

Ans: (c) Commercial bank. Formal sources include banks and cooperatives supervised by RBI. Informal sources include moneylenders, traders, employers, and friends.

Q4. Which organisation supervises the functioning of formal sources of loans in India? [CBSE 2021] [1]

- (a) Finance Ministry (b) Reserve Bank of India (c) SEBI (d) NABARD

Ans: (b) Reserve Bank of India (RBI). It ensures banks maintain minimum cash balance, lend to all sectors including agriculture and small industry, and don't charge excessive interest.

Q5. Self-Help Groups (SHGs) typically have how many members? [CBSE 2020] [1]

- (a) 5-10 (b) 15-20 (c) 50-100 (d) 100-200

Ans: (b) 15-20 members. SHGs are small groups of poor people, usually women, who pool their savings and give loans to members at reasonable interest rates.

Q6. What is the barter system? [CBSE 2023] [1]

- (a) Exchange of money for goods (b) Exchange of goods for goods without money
(c) Bank transaction (d) Online payment

Ans: (b) Exchange of goods for goods without using money. Its main drawback is the "double coincidence of wants" - both parties must want what the other has.

Q7. What is meant by "double coincidence of wants"? [CBSE 2021] [1]

- (a) Both buyer and seller agree on price (b) Both parties have what the other wants
(c) Two banks agreeing to transfer money (d) Government fixing prices

Ans: (b) Both parties have what the other wants. In a barter system, a person wanting shoes must find someone who has shoes AND wants what the first person has to offer.

Q8. Which type of deposits in a bank earn interest? [CBSE 2022] [1]

- (a) Demand deposits only (b) Fixed/term deposits (c) Both demand and fixed deposits (d) Neither

Ans: (c) Both demand and fixed deposits earn interest. Fixed deposits earn higher interest as money is locked for a specific period.

Q9. What percentage of their deposits are banks required to keep as cash? [CBSE 2020] [1]

- (a) 100% (b) About 50% (c) About 15% (d) 0%

Ans: (c) About 15%. Banks keep only a small fraction as cash for day-to-day withdrawals. The remaining major portion (about 85%) is given out as loans.

Q10. Assertion (A): Formal sector loans are cheaper than informal sector loans.

Reason (R): RBI supervises formal lenders and ensures fair interest rates. [CBSE 2024] [1]

- (a) Both true and (R) correctly explains (A) (b) Both true but (R) does not explain (A)
(c) (A) is true but (R) is false (d) (A) is false

Ans: (a) Both are true and (R) correctly explains (A). RBI supervision keeps formal sector interest rates reasonable (8-12%) compared to informal (36-60% or more).

SECTION B : Short Answer Questions

(3 Marks Each)

Q11. Why are formal sources of credit preferred over informal sources? [CBSE 2023] [3]

- **Lower Interest:** Banks charge 8-12% interest while moneylenders charge 36-60% or more. This makes formal credit much cheaper.
- **RBI Supervision:** RBI ensures banks follow rules, maintain transparency, and don't exploit borrowers. No such regulation exists for moneylenders.
- **Debt Trap Prevention:** Informal credit often leads to debt traps where borrowers can never repay. Formal credit has structured repayment and legal protection.

Q12. Explain the role of Self-Help Groups (SHGs) in rural India. [CBSE 2024] [3]

- **Pooling Savings:** 15-20 members (mostly women) save small amounts regularly. These savings are pooled and given as loans to members in need.
- **Collateral-Free:** SHG loans don't need collateral. The group itself serves as guarantee. Interest rates are reasonable compared to moneylenders.
- **Women Empowerment:** SHGs help rural women become financially independent, gain confidence, and discuss social issues like health, nutrition, and education.

Q13. How do banks mediate between those who have surplus money and those who need money? [CBSE 2022] [3]

- **Accept Deposits:** People with surplus money deposit it in banks as demand deposits or fixed deposits, earning interest.
- **Give Loans:** Banks use the deposited money to give loans to those who need it for business, agriculture, housing, etc., at higher interest rate.
- **Profit:** The difference between interest charged on loans and interest paid on deposits is the bank's income. Banks keep only 15% as cash reserves.

Q14. What is the role of RBI in regulating formal sector loans ? [CBSE 2021] [3]

- **Sets Rules:** RBI ensures banks keep minimum cash reserves (CRR). This protects depositors' money and maintains stability in the banking system.
- **Interest Regulation:** RBI sets lending rates and ensures banks don't charge excessive interest. This keeps credit affordable for common people.
- **Priority Lending:** RBI directs banks to lend to agriculture, small industries, and weaker sections of society, not just profitable urban businesses.

Q15. Explain the term " debt trap " with reference to informal credit. [CBSE 2020] [3]

- **High Interest:** Moneylenders charge 36-60% or even higher interest rates. Borrowers find it impossible to repay the principal plus accumulated interest.
- **Cycle of Debt:** To repay one loan, borrowers take another loan at even higher rates. They get trapped in an ever-increasing cycle of debt.
- **Exploitation:** Moneylenders may seize land, crops, or force bonded labour. Poor farmers and labourers are most vulnerable to this exploitation.

SECTION C : Long Answer Questions

(5 Marks Each)

Q16. "Banks and cooperatives need to lend more to the rural poor." Justify this statement. [CBSE 2024] [5]

Ans: Rural poor desperately need formal credit access:

- **Current Reality:** About 85% of rural credit comes from informal sources - moneylenders, traders, landlords - who charge very high interest.

- **Debt Trap:** High informal interest rates push poor farmers into debt traps. Many commit suicide due to unpayable debts.
- **Cheap Credit Needed:** Formal credit at 8-12% interest can help farmers buy seeds, fertilizers, and equipment, improving productivity and income.
- **SHG Support:** Banks should link with Self-Help Groups to reach the last mile. SHGs have proven successful in providing collateral-free credit.
- **Economic Growth:** When rural poor get affordable credit, they invest in farms and businesses, creating employment and boosting the rural economy.

Q17. Explain the modern forms of money with their advantages . [CBSE 2023] [5]

Ans: Modern forms of money have evolved significantly:

- **Currency:** Paper notes and coins issued by RBI on behalf of the central government. Accepted as medium of exchange throughout India by law.
- **Demand Deposits:** Money deposited in banks that can be withdrawn on demand using cheques, ATM, or online banking. Safer than carrying cash.
- **Cheques:** A paper instructing the bank to pay a specific amount from the person's account. Eliminates need for cash transactions.
- **Digital Payments:** UPI, mobile banking, debit/credit cards make transactions instant, secure, and traceable. India leads in digital payments globally.
- **Advantages:** Modern money is easily portable, accepted universally, divisible into smaller units, and allows saving in banks that earn interest.

Q18. Compare formal and informal sources of credit in India. [CBSE 2022] [5]

Ans: Credit sources in India can be formal or informal:

- **Formal Sources:** Banks, cooperatives, and micro-finance institutions. Supervised by RBI. Charge 8-12% interest. Require documentation and collateral.
- **Informal Sources:** Moneylenders, traders, employers, relatives. No RBI supervision. Charge 36-60%+ interest. May exploit borrowers.
- **Access:** Only about 50% of rural households access formal credit. The rest depend on informal sources due to lack of collateral and documentation.
- **Debt Trap:** Informal sources often lead to debt traps. Farmers and labourers suffer most. Many cases of farmer suicides linked to informal debt.
- **Solution:** Expanding formal credit through bank branches, SHGs, and digital banking can reduce dependence on exploitative informal sources.

Q19. How do Self-Help Groups help the poor? Explain their working and importance. [CBSE 2021] [5]

Ans: Self-Help Groups (SHGs) are vital for financial inclusion:

- **Formation:** 15-20 members, mostly women from similar economic backgrounds, form a group. They meet regularly and save small amounts.
- **Internal Lending:** Pooled savings are given as small loans to members at low interest. No collateral needed - the group acts as mutual guarantee.
- **Bank Linkage:** If a SHG functions well for a year, it becomes eligible for bank loans. Banks lend to the group at lower interest rates.
- **Women Empowerment:** Women gain financial independence, decision-making power, and social confidence. They discuss issues beyond finance - health, education, violence.
- **Rural Development:** SHGs have helped millions escape poverty. The model has been particularly successful in states like Andhra Pradesh, Tamil Nadu, and Kerala.

Q20. Why is cheap and affordable credit important for the country's development? [CBSE 2020] [5]

Ans: Cheap credit is essential for India's development:

- **Agricultural Growth:** Farmers need credit for seeds, fertilizers, and equipment. Affordable loans help them invest and increase productivity.
- **Small Business:** Small manufacturers and traders need working capital. Cheap credit helps them expand business, create employment, and earn more.
- **Poverty Reduction:** When poor people get affordable loans, they can start small enterprises, educate children, and improve their standard of living.
- **Prevents Exploitation:** Cheap formal credit reduces dependence on moneylenders who charge 36-60% interest and push borrowers into debt traps.
- **Economic Growth:** Overall, affordable credit increases investment, production, and employment across sectors, driving national economic growth.

--- End of Chapter 3 PYQ ---

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