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Topic-wise

PREVIOUS YEARS SOLVED PAPERS

2011-2026

GENERAL STUDIES

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UPSC CSE (PRELIMS) PREVIOUS YEARS SOLVED PAPERS: GENERAL STUDIES

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Director's Message

History is full of lessons, and History of UPSC Civil Services Examination lies in its previous year questions. I often tell students that the first and most important step to conquer an examination like UPSC Civil Services is to understand it thoroughly. The best way to understand the exam is through the syllabus and analysis of the previous year's questions. This book is an effort to make sure that you learn the most out of the history of the Civil Services Examination.

The book contains solved previous year questions of UPSC Civil Services (Preliminary) Examination from 2011-2026. The questions have been segregated subject-wise as well as topic-wise to make it more accessible for the students. The rationale behind including the questions starting from 2011 is the major shift in the pattern and difficulty level of the preliminary examination post-2011. A compilation from 2011-2026 ensures that the questions are in-line with the latest trend of the exam.

There are three distinctive features that make this book stand apart from the existing options. First, the answers have been thoroughly verified with the official answer key of UPSC. Second, all the options have been explained comprehensively with special emphasis on conceptual clarity. Third and the most important distinctive feature is its futuristic approach through a section of "Additional information" for each question. The recent trend shows that UPSC often frames questions around the core theme and the options of previous year questions. The section of "Additional Information" is intended to make students future- ready for such types of questions.

The NEXT IAS team has put sincere efforts in preparing this valuable resource for students. I hope this book will stand upto the expectations of aspirants and my desire to serve the student community by providing the best study material will get accomplished.

B. Singh (Ex. IES)
CMD, NEXT IAS & MADE EASY Group

CSE (PRELIMS) PREVIOUS YEARS SOLVED PAPERS (2011-2026)

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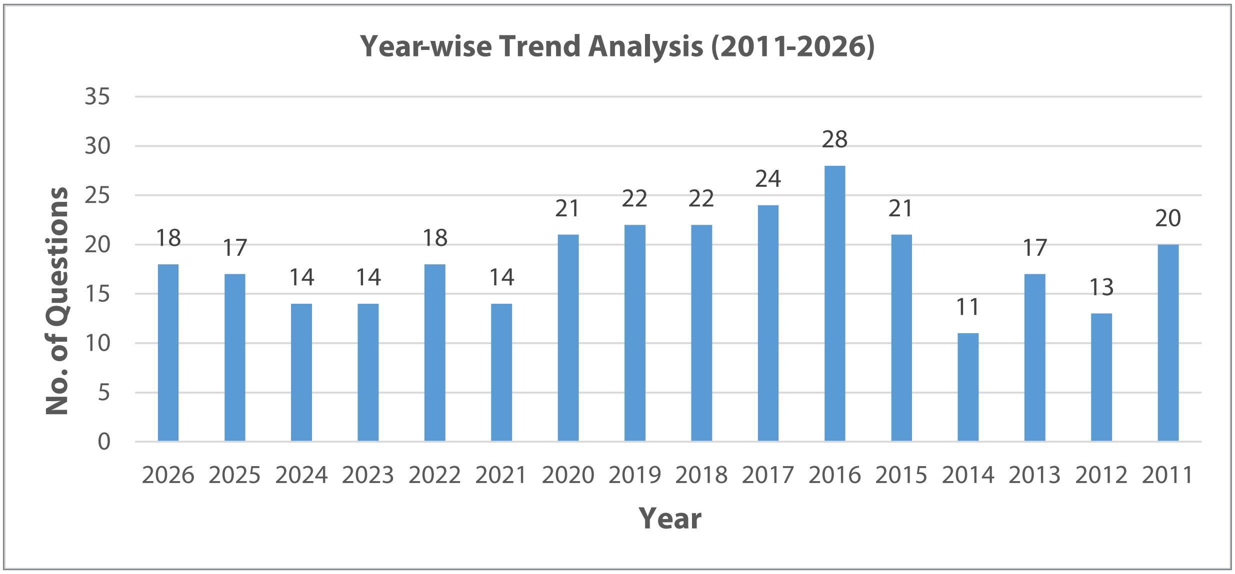
INDIAN ECONOMY



TOPIC-WISE TREND ANALYSIS (2011-2026)

S.No.	Topics	Total Number of Questions
1.	Introduction to Economy	3
2.	National Income Accounting	6
3.	Planning in India	3
4.	Balance of Payment and Foreign Trade	14
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UNIT
I

INDIAN ECONOMY

1. INTRODUCTION TO ECONOMY

1. With reference to the sectors of the Indian economy, consider the following pairs:

Economic activity	**Sector**
1. Storage of agricultural produce	**Secondary**
2. Dairy farm	**Primary**
3. Mineral exploration	**Tertiary**
4. Weaving cloth	**Secondary**

How many of the pairs given above are correctly matched?

(a) Only one **(b) Only two**
(c) Only three **(d) All four**

(2024)

Ans. (b/c) (UPSC Official answer key: B)

- According to the UPSC official answer key, the correct answer is (b). However, as per our opinion, option (c) should be the correct answer.
- Based on the nature of activity, economic activities can be divided into three sectors — primary, secondary, and tertiary.
  - **Primary sector:** It includes economic activities directly tied to any sort of resource extraction, including mining, agriculture, forestry or fishing.
  - **Secondary sector:** It covers activities in which natural products are changed into other forms through ways of manufacturing that we associate with industrial activity. It is the next step after primary.
  - **Tertiary sector:** These are activities that help in the development of the primary and secondary sectors. These activities, by themselves, do not produce a good but they are an aid or a support for the production process. Transport, storage, communication, banking, trade are some examples of tertiary activities.
- **1 is not correctly matched:** Storage of agricultural produce involves activities like warehousing and logistics, which comes under the tertiary sector.
- **2 is correctly matched:** Dairy farms are part of agricultural activity, and hence come under the primary sector.
- **3 is correctly matched:** Mineral exploration includes a range of activities to help determine if there are minerals under the ground. It is different from mining, which includes the process of extraction of minerals out of the ground. Mineral exploration comes under the tertiary sector.

> - **Note:** Mineral extraction is a primary activity, but mineral exploration is considered tertiary. However, UPSC has possibly treated exploration as part of the primary sector, thus marking Pair 3 as incorrect and making option (b) the correct answer.

- **4 is correctly matched:** Weaving clothes involve manufacturing activity, which comes under the secondary sector.
- **Hence, option (c) is the correct answer.**

2. With reference to physical capital in Indian economy, consider the following pairs:

Items	**Category**
1. Farmer's plough	**Working capital**
2. Computer	**Fixed capital**
3. Yarn used by the weaver	**Fixed capital**
4. Petrol	**Working capital**

How many of the above pairs are correctly matched?

(a) Only one **(b) Only two**
(c) Only three **(d) All four**

(2024)

Ans. (b/a) (UPSC Official answer key: B)

- According to the UPSC official answer key, the correct answer is (b). However, as per our opinion, option (b) should be the correct answer.
- **About Physical capital and its types:**
  - Physical capital is one of what economists call the three main factors of production. It consists of tangible, human-made goods that assist in the process of creating a product or service. E.g. Machinery, buildings, office or

warehouse supplies, vehicles etc. Physical capital can be of **two types: Fixed capital and Working Capital.**

- **Fixed capital:** These are long term assets and not consumed or destroyed during the actual production of a good or service, but are reusable.
- **Working capital:** These are short-term assets that are consumed or transformed into final products during the production process. E.g. raw materials.

- **Pair 1 is not correctly matched:** Farmer's plough is a long term asset and can be used repeatedly over a long period, making it fixed capital rather than working capital.
- **Pair 2 is correctly matched:** Computer is a durable good and can be used over years without being consumed during the actual production. Therefore, it is a fixed capital.
- **Pair 3 is not correctly matched:** Yarn is a raw material that gets consumed in the process to create fabric. Therefore, it is a working capital.
- **Pair 4 is not correctly matched:** Petrol is an example of intermediate good, and can not be classified as either fixed or working capital.

- **Note:** Strictly speaking, petrol is neither fixed nor working capital. However, UPSC has likely treated it as working capital, thereby considering Pair 4 correct and making option (b) the correct answer.

3. Consider the following statements:

Other things remaining unchanged, market demand for a good might increase if:

1. Price of its substitute increases
2. Price of its complement increases
3. The good is an inferior good and income of the consumers increases
4. Its price falls

Which of the statements given above are correct?

(a) 1 and 4 only **(b) 2, 3 and 4 only**
(c) 1, 3 and 4 only **(d) 1, 2 and 3 only**

(2021)

Ans. (a)

- **Statement 1 is correct:** Substitute goods are those goods which can easily be used in place of one another for satisfaction of a particular want, like tea and coffee. Since tea is a substitute for coffee, if the price of coffee increases, the consumers can shift to tea, and hence, the consumption of tea is likely to go up. On the other hand, if the price of coffee decreases, the consumption of tea is likely to go down. So, **other things remaining unchanged, the demand for a good usually moves in the direction of the price of its substitutes.**
- **Statement 2 is not correct:** Complementary goods are those goods which are used together to satisfy a particular want, like tea and sugar. Since tea and sugar are used together, an increase in the price of sugar is likely to decrease the demand for tea. Similarly, a decrease in the price of sugar is likely to increase the demand for tea. In general, **the demand for a good moves in the opposite direction of the price of its complementary goods.**
- **Statement 3 is not correct:** When the income of consumers increases, they are likely to spend more on the purchase of some goods such as fruits, milk etc. Such goods are called normal goods. **So, for normal goods, the demand generally increases with the increase in consumer's income.** But there are some goods whose demand decreases when income of the buyer increases, such as coarse cereals. Such goods are called **inferior goods**. **As the income of the consumer increases, the demand for an inferior good falls and vice versa.**
- **Statement 4 is correct:** According to the Law of Demand, there is an inverse relationship between the consumer's demand for a good and the price of the good. **So, when the price of a good falls, its demand will increase.**

ADDITIONAL INFORMATION

The effect of different factors on the market demand of a good can be summarized as:

Factors	Demand might increase	Demand might fall
Price of the good	Decreases	Increases
Price of complementary goods	Decreases	Increases
Price of substitute goods	Increases	Decreases
Income of buyer (if good is normal good)	Increases	Decreases
Income of buyer (if good is inferior good)	Decreases	Increases

2. NATIONAL INCOME ACCOUNTING

1. **Increase in absolute and per capita real GNP *do not* connote a higher level of economic development, if**
   (a) industrial output fails to keep pace with agricultural output.
   (b) agricultural output fails to keep pace with industrial output.
   (c) poverty and unemployment increase.
   (d) imports grow faster than exports.
   (2018)

Ans. (c)

- **Gross National Product (GNP)** is the total monetary value of all final goods and services produced by the nationals of a country during a financial year. GNP is one of the important measures of economic growth of a country. But increase in absolute and per capita real GNP doesn't always translate into economic development.
- **Economic development** is a wider concept than economic growth. It can be defined as sustained improvement in material well being of society. Apart from increase in output of goods and services, economic development also aims to ensure equitable income distribution, greater employment and poverty alleviation. The concept of GNP doesn't capture this aspect of economic development. **If increase in absolute and per capita real GNP leads to growth in income of only a small section of the society, and a large section remains poor and unemployed, then it doesn't connote economic development**. **Hence, option (c) is the correct answer.**

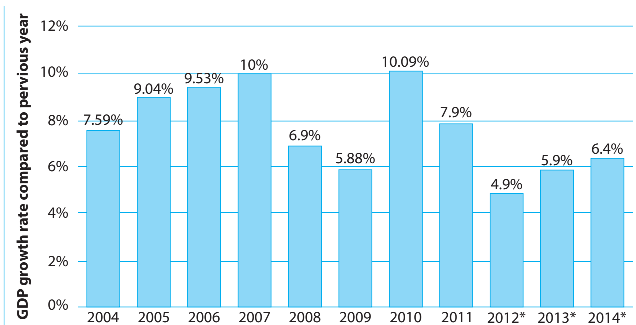
ADDITIONAL INFORMATION

	Economic growth	Economic development
Meaning	Increase in the real output of goods and services in the country.	Sustained improvement in material well being of society.
Measurement	Measured by quantitative concepts like Gross domestic product (GDP), Gross National Product (GNP) etc.	Also includes qualitative measures like HDI (Human Development Index), gender- related index, infant mortality, literacy rate etc
Effect	It brings quantitative changes in the economy.	It leads to qualitative as well as quantitative changes in the economy.

2. **With reference to Indian economy, consider the following statements:**
   1. The rate of growth of Real Gross Domestic Product has steadily increased in the last decade.
   2. The Gross Domestic Product at market prices (in rupees) has steadily increased in the last decade.
   Which of the statements given above is/are correct?
   (a) 1 only (b) 2 only
   (c) Both 1 and 2 (d) Neither 1 nor 2
   (2015)

Ans. (b)

- **Statement 1 is not correct**: As the question was asked in 2015, the "last decade" can be considered as 2005-2015. The rate of growth of Real Gross Domestic Product fluctuated a lot between 2005-15 (see the graph below).
- **Statement 2 is correct**: Since the rate of growth of real GDP was in the positive territory from 2005 to 2015, the **absolute value of GDP at market prices steadily increased each year**.



Real GDP growth rate of India

ADDITIONAL INFORMATION

- **GDP:** Gross Domestic Product is the monetary value of **final goods and services produced in a country in a given period of time.**
- **Nominal GDP:** When the money value of goods and services included in GDP is estimated on the prices of the current year, it is called GDP at current prices or nominal GDP.
- **Real GDP:** When the value of goods and services included in GDP is estimated on the prices of base year, we get GDP at constant prices or real GDP.

3. **Economic growth in country X will necessarily have to occur if**
   (a) there is technical progress in the world economy
   (b) there is population growth in X

(c) there is capital formation in X
(d) the volume of trade grows in the world economy

(2013)

Ans. (c)

- **Option (a) is not correct**: Technical progress in the world economy **does not ensure economic growth** in country X, because we do not know whether that technological progress has reached country X or not.
- **Option (b) is not correct**: Population growth in country X **cannot automatically** lead to economic growth. For economic growth, the population of Country X need to participate in the labor market and perform economic activities.
- **Option (c) is correct**: Capital formation means additions of capital goods (machine, tools, factories, etc.) in an economy. Increased capital goods can lead to **production of more goods and services** which in turn leads to higher economic growth.
- **Option (d) is not correct**: Volume of trade growing in the world economy **cannot ensure economic growth in country X**. We do not know whether country X is an open economy or closed economy or what's the share of country X in international trade.

4. The national income of a country for a given period is equal to the
(a) total value of goods and services produced by the nationals
(b) sum of total consumption and investment expenditure
(c) sum of personal income of all individuals
(d) money value of final goods and services produced

(2013)

Ans. (d)

- Net National Product (NNP) at Factor Cost is referred to as **National Income** of a country. National Income is the sum total of factor incomes earned by the normal residents of a country within and outside the economic territory.
- NNP at Factor Cost = Net Domestic Product at Factor cost + Net Factor Income From Abroad
- **Note:** None of the options given in the question include the complete definition of National Income, however **option (d) is the correct answer as per the UPSC official answer key**. The possible explanation could be that it is the most appropriate one among the given options. Option (a) states "total value", but it should have been "total money value". Option (b) and Option (c) are irrelevant. So, we are left with only option (d).

5. Economic growth is usually coupled with?
(a) Deflation (b) Inflation
(c) Stagflation (d) Hyperinflation

(2011)

Ans. (b)

- **If economic growth is caused by aggregate demand increasing faster than the productive capacity, it is likely to cause inflation.** However, if economic growth is caused by increased productive capacity, then the growth can be sustainable and not cause inflation. **Hence, option (b) is the correct answer.**

ADDITIONAL INFORMATION

- **Inflation** is the sustained increase in the general price level of goods and services.
- **Deflation** is a decrease in the general price level of goods and services.
- **Stagflation** is an economic condition that's caused by a combination of slow economic growth, high unemployment, and rising prices.
- **Hyperinflation** refers to a situation where the prices of goods and services rise uncontrollably over a defined period of time.

6. In the context of Indian economy, consider the following statements:
1. The growth rate of GDP has steadily increased in the last five years.
2. The growth rate in per capita income has steadily increased in the last five years.
Which of the statements given above is/are correct?
(a) 1 only (b) 2 only
(c) Both 1 and 2 (d) Neither 1 nor 2

(2011)

Ans. (d)

- **Statement 1 is not correct**: From the chart 1 (given below), it is clear that the growth rate of GDP from 2005 to 2010 didn't increase steadily. There were periods of high growth (2007-08) as well periods of low growth (2008-09).
- **Statement 2 is not correct**: The growth rate in per capita income also fluctuated between 2005 to 2010. (Refer Chart 2).

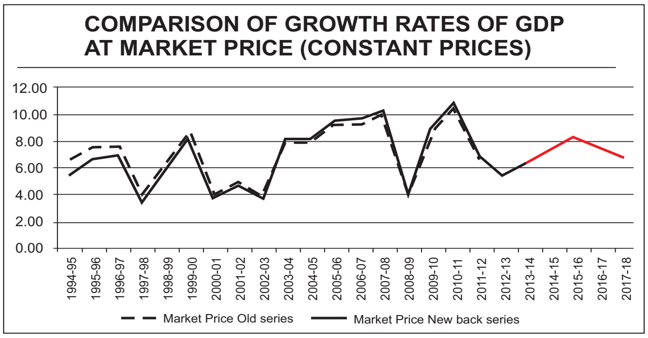


Chart 1: India's GDP growth rate

Year	Growth Rate of Per Capita Net National Product at Constant Prices
2005-06	7.8
2006-07	7.9
2007-08	8.1
2008-09	4.7
2009-10	6.6

Chart 2: Growth in Per capita income

3. PLANNING IN INDIA

1. **With reference to India's Five-Year Plans, which of the following statements is/are correct?**
   1. **From the Second Five-Year Plan, there was a determined thrust towards substitution of basic and capital good industries.**
   2. **The Fourth Five-Year Plan adopted the objective of correcting the earlier trend of increased concentration of wealth and economic power.**
   3. **In the Fifth Five-Year Plan, for the first time, the financial sector was included as an integral part of the Plan.**

   Select the correct answer using the code given below:

   (a) 1 and 2 only **(b) 2 only**

   (c) 3 only **(d) 1, 2 and 3**

   (2019)

Ans. (a)

- **Statement 1 is correct:** India adopted the strategy of **Import Substitution Industrialization (ISI)** in the 1950s. ISI is a development strategy that focuses on promoting domestic production of previously imported goods to foster industrialization. India's ISI strategy was based on the **growth model propounded by Mahalonobis and its chief objective was to build a self-reliant economy**. **From the Second Five Year Plan (1956-61), there was determined thrust towards substitution of basic and capital goods industries.**
- **Statement 2 is correct:** Fourth five year plan (1969-74) focused on reduction of concentration of incomes and economic power so that benefits of development could reach the relatively less privileged classes of society.
- **Statement 3 is not correct:** Third statement is somewhat ambiguous. But none of the authoritative sources claim that the Fifth Five Year Plan was the first to include the financial sector as an integral part of the plan. Moreover, note that the nationalization of 14 large commercial banks took place during the fourth five year plan.

2. **The Government of India has established NITI Aayog to replace the**

   (a) Human Rights Commission

   (b) Finance Commission

   (c) Law Commission

   (d) Planning Commission

   (2015)

Ans. (d)

- Government of India established **NITI Aayog to replace the Planning Commission**. NITI Aayog was formed via a resolution of the Union Cabinet on 1 January 2015 (hence it is neither a constitutional body nor a statutory body). **Hence, option (d) is the correct answer.**

ADDITIONAL INFORMATION

- The organizational structure of NITI Aayog is as follows:
  - **Prime Minister of India as the Chairperson**
  - Governing Council comprising the Chief Ministers of all the States and Lt. Governors of Union Territories
  - Experts, specialists and practitioners with relevant domain knowledge as special invitees nominated by the Prime Minister
  - Vice Chairperson to be appointed by Prime Minister
  - Other members like Union Ministers, CEO etc.
- The NITI Aayog works towards multiple objectives, some of the prominent ones are:
  - To evolve a shared vision of national development priorities, sectors and strategies with the active involvement of States in the light of national objectives.
  - To foster cooperative federalism through structured support initiatives and mechanisms with the States on a continuous basis, recognizing that strong States make a strong nation.

- To develop mechanisms to formulate credible plans at the village level and aggregate these progressively at higher levels of government.
- To create a knowledge, innovation and entrepreneurial support system through a collaborative community of national and international experts, practitioners and other partners.

3. The main objective of the 12th Five-Year Plan is
(a) inclusive growth and poverty reduction
(b) inclusive and sustainable growth
(c) sustainable and inclusive growth to reduce unemployment
(d) faster, sustainable and more inclusive growth
(2014)

Ans. (d)

- The main objective of 12th FYP (2012-17) was '**Faster, Sustainable, and More Inclusive Growth**'. **Hence, option (d) is the correct answer.**

ADDITIONAL INFORMATION

- India had a total of 12 Five-Year Plans, the last one being from 2012-2017.
- With the setting up of NITI Aayog, the practice of formulating Five Year Plans was discontinued. Instead, NITI Aayog would publish a 15 year vision document in tandem with global trends and economic growth.

4. BALANCE OF PAYMENT AND FOREIGN TRADE

1. Consider the following statements:
Statement-I:
India does not import apples from the United States of America.
Statement-II:
In India, the law prohibits the import of Genetically Modified food without the approval of the competent authority.
Which one of the following is correct in respect of the above statements?
(a) Both Statement-I and Statement-II are correct and Statement-II explains Statement-I
(b) Both Statement-I and Statement-II are correct, but Statement-II does not explain Statement-I
(c) Statement-I is correct, but Statement-II is incorrect
(d) Statement-I is incorrect, but Statement-II is correct
(2024)

Ans. (d)

- **Statement I is not correct:** India does import apples from the USA, and these imports have recently increased after India removed the "retaliatory import duty" on US apples. This duty was initially imposed by India in response to the United States' 2019 decision to revoke India's trade benefits under the Generalized System of Preferences (GSP) program.
- **Statement II is correct:** India has specific regulations regarding the import of genetically modified (GM) food. As of March 1, 2021, the Food Safety and Standards Authority of India (FSSAI) requires a "non-GM origin and GM-free certificate" issued by the competent national authority of the exporting country for certain food products. This regulation applies to 24 listed food items imported into India.
- Hence, option (d) is the correct answer.

2. Consider the following statements:
Statement-I: India accounts for 3.2% of global export of goods.
Statement-II: Many local companies and some foreign companies operating in India have taken advantage of India's 'Production-linked Incentive' scheme.
Which one of the following is correct in respect of the above statements?
(a) Both Statement-I and Statement-II are correct and Statement-II is the correct explanation for Statement-II
(b) Both Statement-I and Statement-II are correct and Statement-II is not the correct explanation for Statement-I.
(c) Statement-I is correct but Statement-II is incorrect.
(d) Statement-I is incorrect but Statement-II is correct
(2023)

Ans. (d)

- **Statement 1 is not correct**: India aims to raise the share of its exports in global trade to 3% by 2027 and 10% by 2047 from the current 2.1%, promoting hundred Indian brands as global champions.
- **Statement 2 is correct**: Production-linked Incentive (PLI) schemes aim to boost domestic manufacturing and cut down on import bills by giving companies incentives on incremental sales from products manufactured in domestic units. The PLI scheme is open to both domestic and foreign companies operating in India. Several foreign firms like Samsung, Foxconn, Hon Hai etc. and Indian firms like Lava,

Micromax, Padget have been approved as beneficiaries.

ADDITIONAL INFORMATION

- Government of India has announced an outlay of INR 1.97 Lakh Crores for the Production Linked Incentive (PLI) Schemes across 14 key sectors, to create national manufacturing champions and to create 60 lakh new jobs, and an additional production of 30 lakh crore during next 5 years.

3. Consider the following statements:

1. The value of Indo-Sri Lanka trade has consistently increased in the last decade.

2. "Textile and textile articles" constitute an important item of trade between India and Bangladesh.

3. In the last five years, Nepal has been the largest trading partner of India in South Asia.

Which of the statements given above is/are correct?

(a) 1 and 2 only

(b) 2 only

(c) 3 only

(d) 1, 2 and 3

(2020)

Ans (b)

- **Statement 1 is not correct:** Trade between India and Sri Lanka grew rapidly after the free trade agreement between two countries came into effect in 2000. **However, the Indo-Sri Lanka trade value has not consistently increased in the last decade** — Bilateral trade between the two countries registered a decline in 2012-13 and 2016-17.
- **Statement 2 is correct:** During 2019-20, Bangladesh was the third largest export destination for textile products of India (Top two being USA and UAE). As per a report by World Bank, there are significant value chain linkages between India and Bangladesh in the textile and apparel sector. India specializes in the upstream segment, supplying such intermediate inputs as silk, cotton, yarn, and fabrics to Bangladesh. Bangladesh specializes in the downstream final apparel segment, exporting worldwide as well as to India.
- **Statement 3 is not correct:** In the last five years, Bangladesh has been India's largest trading partner in South Asia with India having a huge trade surplus with Bangladesh.

4. With reference to the international trade of India at present, which of the following statements is/are correct?

1. India's merchandise exports are less than its merchandise imports.

2. India's imports of iron and steel, chemicals, fertilizers and machinery have decreased in recent years.

3. India's exports of services are more than its imports of services.

4. India suffers from an overall trade/current account deficit.

Select the correct answer using the code given below:

(a) 1 and 2 only (b) 2 and 4 only

(c) 3 only (d) 1, 3 and 4 only

(2020)

Ans. (Question dropped by UPSC)

- **Statement 1 is correct:** As per the data of Ministry of Commerce & Industry, India's merchandise export during April-March 2019-20 was estimated to be USD 314.31 billion. Whereas, the merchandise import during the same period stood at USD 467.19 billion. Indian had current account surplus in 2020-21.
- **Statement 2 is not correct:** On the contrary, India's imports of iron and steel, chemicals, fertilizers and machinery have increased in recent years.
- **Statement 3 is correct:** For the last few years, a large part of India's merchandise trade deficit has been offset by the trade in services, where India has a surplus. India's service export during April-March 2019-20 was estimated to be USD 214.14 billion, whereas service imports during the same period stood at USD 131.41 billion.
- **Statement 4 is not correct:** Generally, trade/ current account deficit has been a significant problem of Indian economy, but in 2020-21 the current account balance of Indian economy was surplus of 0.9%.
- **Hence, only statements 1 and 3 are correct, which is not given in any option. That's why UPSC dropped the question.**

Item / Year	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
1. Merchandise										
A) Exports, f.o.b.	306581	318607	316545	266365	280138	308970	337237	320431	296300	429164
B) Imports, c.i.f.	502237	466216	461484	396444	392580	469006	517519	477937	398452	618623

Item / Year	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
Trade balance (A-B)	-195656	-147609	-144940	-130079	-112442	-160036	-180283	-157506	-102152	-189459
II. Invisibles, net	107493	115313	118081	107928	98026	111319	123026	132850	126065	150694
III. Current account (I+II)	-88163	-32296	-26859	-22151	-14417	-48717	-57256	-24656	23912	-38766
IV. Capital account (A to F)	91989	47804	88265	40055	35967	92292	53917	84154	63374	86266
A) Foreign Investment	54723	35792	77476	41264	49981	61595	42898	56558	93653	42160
B) External assistance, net	1268	1231	2053	1966	2186	3013	3487	3856	11211	5379
C) Commercial borrowings, net	8582	10716	232	-5856	-7590	-799	9769	21680	240	7407
D) Rupee debt service	-58	-52	-81	-73	-99	-75	-31	-69	-64	-71
E) NRI deposits, net	14842	38892	14057	16052	-12367	9676	10387	8627	7364	3234
F) Other capital	12631	-38775	-5472	-13297	3857	18881	-12592	-6498	-49030	28158
V. Overall balance (III+1V)	3826	15508	61406	17905	21550	43574	-3339	59498	87286	47501
VI. Monetary movements (VII+VIII+IX)	-3826	-15508	-61406	-17905	-21550	-43574	3339	-59498	-87286	-47501
VII. Reserves (increase -/ decrease +)	-3826	-15508	-61406	-17905	-21550	-43574	3339	-59498	-87286	-47501
VIII. IMF, net	-	-	-	-	-	-	-	-	-	-
IX. SDR allocation	-	-	-	-	-	-	-	-	-	-17862

5. Consider the following statements:

1. **Purchasing Power Parity (PPP) exchange rates are calculated by comparing the prices of the same basket of goods and services in different countries.**
2. **In terms of PPP dollars, India is the sixth largest economy in the world.**

Which of the statements given above is/are correct?

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

(2019)

Ans. (a)

- Purchasing Power Parity (PPP) exchange rates provide a measure of what an economy's local currency can buy in another economy. PPP-based comparisons of economic output of two countries differ from market exchange rate-based comparisons as the latter do not distinguish between the relative price levels of different items in economies.
- **Statement 1 is correct:** Purchasing power parity (PPP) exchange rate is the rate at which the currency of one country would have to be converted into that of another country to buy the same basket of goods and services in each country.

  To understand PPP better, let's consider a simplified example. If the price of one kg apple is 5 USD in the USA and 150 Rs. in India, then this would imply a PPP exchange rate of 1 USD to 30 INR.
- **Statement 2 is not correct: India is the third-largest economy in the world in terms of purchasing power parity (PPP)**, only behind the US and China.

6. Which one of the following is *not* the most likely measure the Government/RBI takes to stop the slide of the Indian rupee?

(a) Curbing imports of non-essential goods-and promoting exports
(b) Encouraging Indian borrowers to issue rupee denominated Masala Bonds
(c) Easing conditions relating to external commercial borrowing
(d) Following an expansionary monetary policy

(2019)

Ans. (d)

- The value of rupee against dollar or any other foreign currency depends on the market forces of demand and supply. If the demand for dollars increases, then the value of the rupee falls and vice-versa. To stop the slide of the Indian rupee, all those steps would be helpful which would reduce the demand of foreign currency (or increase the supply of foreign currency).

- **Option (a) is a measure that the Government / RBI is likely to take:** Curbing imports of non-essentials goods leads to less amount of dollars spent by India on imports. Decrease in demand of dollars will lead to appreciation of the rupee.
- **Option (b) is a measure that the Government / RBI is likely to take:** Masala Bonds are rupee-denominated bonds issued outside India by Indian entities. Masala Bonds were introduced in India in 2014 by International Finance Corporation (IFC). They are debt instruments which help to raise money in local currency from foreign investors. If foreign investors invest in Masala Bonds or bring money into India, this would help in supporting the rupee.
- **Option (c) is a measure that the Government / RBI is likely to take:** External commercial borrowing (ECB) refers to the debt taken by an eligible business entity in India for solely commercial purposes, with the debt being extended by external/foreign sources, i.e., recognized entities from outside India. These borrowings must conform to the rules and regulations of the RBI. Easing conditions on ECB will lead to inflow of foreign currency in India which in turn would strengthen the rupee.
- **Option (d) is not a measure that the Government / RBI is likely to take:** When RBI follows expansionary monetary policy, it usually lowers the policy rates in order to boost the money supply. Lower interest rates in the economy are less attractive for the foreign investors, and hence this step will not help in arresting the slide of Indian Rupee.

7. In the context of India, which of the following factors is/are contributor/contributors to reducing the risk of a currency crisis?

1. The foreign currency earnings of India's IT sector

2. Increasing the government expenditure

3. Remittances from Indians abroad

Select the correct answer using the code given below:

(a) 1 only **(b) 1 and 3 only**

(c) 2 only **(d) 1, 2 and 3**

(2019)

Ans. (b)

- Currency crisis is a situation where there is a sudden and sharp decline in the value of a nation's currency. So, the factors that can arrest the downfall of a nation's currency can provide a cushion against currency crisis risk.
- **Statements 1 and 3 are correct:** Export of IT services from India and remittances sent by Indians working abroad are important sources of foreign currency inflow in India. Increased supply of foreign currency in the market may lead to rise in the Rupee's value against foreign currency, reducing the risk of currency crisis in India.

8. Which of the following best describes the term 'import cover', sometimes seen in the news?

(a) It is the ratio of value of imports to the Gross Domestic Product of a country

(b) It is the total value of imports of a country in a year

(c) It is the ratio between the value of exports and that of imports between two countries

(d) It is the number of months of imports that could be paid for by a country's international reserves

(2016)

Ans. (d)

- **Import cover refers to the number of months of imports that could be paid for from the foreign exchange reserves.**
- Import cover is a trade-based indicator to gauge the adequacy of foreign exchange reserves of a country. It's an important factor in assessing how well a country can withstand external shocks. **Hence, option (d) is the correct answer.**

9. Convertibility of rupee implies:

(a) being able to convert rupee notes into gold

(b) allowing the value of rupee to be fixed by market forces

(c) freely permitting the conversion of rupee to other currencies and vice versa

(d) developing an international market for currencies in India

(2015)

Ans. (c)

- Currency convertibility refers to the freedom to convert the domestic currency into other internationally accepted currencies and vice versa.
- While current account convertibility refers to freedom in respect of 'payments and transfers for current international transactions', capital account convertibility would mean freedom of currency conversion in relation to capital transactions in

terms of inflows and outflows. **Hence, option (c) is the correct answer.**

ADDITIONAL INFORMATION

- India currently has full current account convertibility and partial capital account convertibility. Partial capital account convertibility implies that there are restrictions in the conversion of domestic currency into foreign currency in relation to capital transactions.
- Two committees were set up under the chairmanship of SS Tarapore (1999 and 2006) to look into the feasibility of full capital account convertibility.

10. With reference to Balance of Payments, which of the following constitutes/ constitute the Current Account?

1. Balance of trade

2. Foreign assets

3. Balance of invisibles

4. Special Drawing Rights

Select the correct answer using the code given below.

(a) 1 only (b) 2 and 3 only

(c) 1 and 3 only (d) 1, 2 and 4 only

(2014)

Ans. (c)

- The balance of payments (BoP) records the transactions in goods, services and assets between residents of a country with the rest of the world for a specified time period typically a year. There are two main accounts in the BoP – the current account and the capital account.
- Current account includes Balance of trade and Balance of invisibles.
    - Balance of Trade is obtained by subtracting imports of goods from the exports of goods.
    - Balance of Invisibles includes Trade in services, transfer payments, and income associated with non-resident assets and liabilities (e.g. dividend, investment income etc.). **Hence, option (c) is the correct answer.**

ADDITIONAL INFORMATION

- The capital account records the net change in foreign assets and liabilities held by a country. The components of Capital Account are assets and liabilities covering direct investment, portfolio investment, loans, banking capital and other capital.

11. Which one of the following groups of items is included in India's foreign-exchange reserves?

(a) Foreign-currency assets, Special Drawing Rights (SDRs) and loans from foreign countries

(b) Foreign-currency assets, gold holdings of the RBI and SDRs

(c) Foreign-currency assets, loans from the World Bank and SDRs

(d) Foreign-currency assets, gold holdings of the RBI and loans from the World Bank

(2013)

Ans. (b)

- Foreign Exchange Reserve consists of:
    - Foreign Currency Assets which are maintained as a multi-currency portfolio comprising major currencies such as US dollar, Euro, Pound sterling etc.,
    - Gold holdings
    - Special Drawing Rights
    - Reserve Tranche Position in the International Monetary Fund (IMF). **Hence, option (b) is the correct answer.**

ADDITIONAL INFORMATION

- In India, the **Reserve Bank of India Act 1934** contains the enabling provisions for the **Reserve Bank to act as the custodian of foreign reserves**, and manage reserves with defined objectives.
- **Special Drawing Right (SDR):** It is an international reserve asset, created by the IMF in 1969 to supplement its member countries' official foreign exchange reserves. General allocations of SDRs are distributed across the IMF membership in proportion to IMF quota shares.
- **Reserve tranche position in IMF:** It is a segment of an International Monetary Fund (IMF) member country's quota that is accessible without paying service fees or economic reform conditions. It represents the member's unconditional drawing right on the IMF, that can be accessed at short notice.

12. The balance of payments of a country is a systematic record of

(a) All import and export transactions of a country during a given period of time, normally a year

(b) Goods exported from a country during a year

(c) Economic transaction between the government of one country to another

(d) Capital movements from one country to another

(2013)

Ans. (a)

- The balance of payments (BoP) records the transactions in goods, services and assets between residents of a country with the rest of the world for a specified time period typically a year. There are two main accounts in the BoP – the current account and the capital account. **Hence, option (a) is the correct answer.**

13. Which of the following constitute Capital Account?

1. Foreign Loans
2. Foreign Direct Investment
3. Private Remittances
4. Portfolio Investment

Select the correct answer using the codes given below.

(a) 1, 2 and 3 only **(b) 1, 2 and 4 only**
(c) 2, 3 and 4 only **(d) 1, 3 and 4 only**

(2013)

Ans. (b)

- The balance of payments (BoP) records the transactions in goods, services and assets between residents of a country with the rest of the world for a specified time period typically a year. There are two main accounts in the BoP – the current account and the capital account.
- **Current account records the following transactions:**
    - Export and import of goods and services
    - Transfer payment (e.g. remittances)
    - Income associated with non-resident assets and liabilities (e.g. dividend, investment income etc.)
- **Capital account records the net change in foreign assets and liabilities held by a country. The components of Capital Account are:**
    - Foreign Direct Investment
    - Portfolio investment
    - Foreign loan (External commercial borrowing). **Hence, option (b) is the correct answer.**

14. Consider the following actions which the Government can take:

1. Devaluing the domestic currency.
2. Reduction in the export subsidy.
3. Adopting suitable policies which attract greater FDI and more funds from FIIs.

Which of the above action/actions can help in reducing the current account deficit?

(a) 1 and 2 only **(b) 2 and 3 only**
(c) 3 only **(d) 1 and 3 only**

(2011)

Ans. (d)

- A current account deficit (**CAD) occurs when the value of imports is greater than value of exports**. Therefore, **CAD can reduce by either increasing exports or decreasing imports (or both).**
- **Statement 1 is correct**: Devaluation of currency means deliberately reducing the value of domestic currency vis-à-vis foreign currency within a fixed exchange rate system. Devalued currency makes exports cheaper, which may increase exports. So, Devaluing the domestic currency can help in reducing CAD.
- **Statement 2 is not correct**: Reducing the export subsidy will discourage exports as it will increase the cost for exporters. This step will further widen the CAD.
- **Statement 3 is correct**: FDI is generally known to be the most stable component of capital flows needed to finance the current account deficit. Moreover, it adds to investible resources, provides access to advanced technologies, assists in gaining production know-how and promotes exports. Therefore, it helps in managing CAD.

5. MONETARY SYSTEM AND RBI

1. Which one of the following correctly represents the three key sub-indices of the Financial Inclusion Index (FI-Index) of the Reserve Bank of India (RBI)?

(a) Credit access, Insurance depth, and Pension coverage
(b) Banking access, GDP contribution, and Financial literacy
(c) Access, Usage, and Quality
(d) Access, Affordability, and Transparency

(2026)

Ans. (c)

- **About Financial Inclusion Index (FI-Index):**
    - It was launched by the Reserve Bank of India in 2021 with the aim of capturing financial inclusion across the country while representing different sectors such as banking, investment, insurance, postal and postal and pension.

- The index varies from a scale of 0 to 100 where 0 indicates no financial inclusion and 100 indicates complete financial inclusion.

- **Option (c) is the correct answer: The index has 3 sub-indices, "Access", "Usage" and "Quality",** with each sub-index having respective weights of 35, 45 and 20 per cent respectively.
  - **"Access"** sub-index reflects the availability of the supply **side of financial inclusion** such as physical and digital infrastructure. It is divided into four-dimensions i.e., banking, digital, pension and insurance.
  - **"Usage"** is the sub-index which reflects the **demand side of financial inclusion.** It has 5 dimensions, viz., savings & investments, digital, pension, insurance and credit.
  - "**Quality**" is a three-dimensional sub-index i.e., **financial literacy, consumer protection and inequality**

ADDITIONAL INFORMATION

- **About Eri Silk:**
  - It is renowned as the world's only vegan silk, where, unlike other silks, the moth inside the cocoon is not killed. Instead, the moth naturally exits the cocoon, leaving it behind for us to use.
  - Assam contributes around 65% of the country's Eri production.

2. Which one of the following statements about Unified Payments Interface (UPI) and Central Bank Digital Currency (Digital Rupee) is not correct?

(a) UPI is a real-time payment system but Digital Rupee is akin to sovereign paper currency.

(b) In case of UPI, settlement for end users happens instantly as the money gets immediately debited or credited but in case of Digital Rupee, there is no settlement as the wallet balance gets transferred to another wallet.

(c) UPI transactions are recorded by banks and reflected in bank statements but in case of Digital Rupee, no data is captured in bank statements as transactions are from one wallet to another.

(d) In both the cases (UPI and Digital Rupee), the liability lies with the users and their respective banks.

(2026)

Ans: (d)

- **Option (a) is correct:**
  - Unified Payments Interface (UPI) is an instant payment system developed by the National Payments Corporation of India (NPCI).
  - Whereas, Digital Rupee or e, is India's Central Bank Digital Currency (CBDC). It is the digital form of legal tender issued by the Reserve Bank of India, functioning identically to sovereign physical paper currency.
- **Option (b) is correct:**
  - In case of UPI, settlement for end users happens instantly as the money gets immediately debited or credited. However, interbank settlement happens on a deferred net basis.
  - Whereas, in case of Digital Rupee, there is no settlement as the wallet balance gets transferred to another wallet.
- **Option (c) is correct:**
  - UPI transactions are recorded by banks and reflected in the statement.
  - Whereas, during CBDC wallet transactions, there is no dependency or intermediation by the bank. This implies that the transaction will not be recorded in the statements, making it anonymous.
- **Option (d) is not correct:**
  - In the case of UPI, the underlying funds are bank deposits, meaning the liability lies with the respective commercial banks.
  - Whereas, in case of CBDC, liability lies with the central bank, i.e. the RBI.

3. Which of the following statements about M1xchange's role in Micro, Small & Medium Enterprises (MSMEs) financing is/are correct?

1. M1xchange provides collateral based loans to MSMEs.

2. M1xchange facilitates discounting of invoices and Bills of Exchange for MSMEs.

3. M1xchange functions as a credit rating agency for MSMEs.

Select the answer using the code given below:

(a) 1, 2 and 3 **(b) 2 only**

(c) 2 and 3 only **(d) 1 only**

(2026)

Ans: (b)

- **About M1xchange:**
  - Reserve Bank of India (RBI) granted "in-principle" approval to three companies to set up the Trade Receivable Discounting System (TReDS) platform.
  - Mynd Solutions Pvt Ltd, is one amongst the three companies that set up the TReDS platform 'M1xchange' in 2017 under the Payment and Settlement System (PSS) Act 2007 to facilitate discounting of invoices and Bills of exchange for MSMEs on pan India basis.
  - TReDS is an RBI-regulated electronic platform, operational since 2017, for financing and discounting the trade receivables of MSMEs due from corporate buyers, Government Departments and Public Sector Undertakings, through competitive bidding by multiple financiers.
  - TReDS aims to resolve the chronic problem of delayed payments faced by MSMEs
- **Statement 1 is not correct:** M1xchange does not provide collateral-based loans. It operates under the Trade Receivables Discounting System (TReDS) framework regulated by the Reserve Bank of India (RBI). It offers collateral-free invoice financing to Micro, Small & Medium Enterprises (MSMEs).
- **Statement 2 is correct:** M1xchange's primary purpose is to be a digital platform for discounting of invoices and Bills of Exchange. It enables MSMEs to upload their accepted trade receivables and auction them to multiple participating financiers (including banks and Non-Banking Financial Companies) through a competitive bidding process to obtain quick liquidity.
- **Statement 3 is not correct:** M1xchange is not a credit rating agency. In India, the formal assessment of creditworthiness and the assignment of credit ratings for MSMEs are done by separate agencies registered with the Securities and Exchange Board of India (SEBI), e.g. CRISIL, ICRA and CARE.

4. Which of the following are the sources of income for the Reserve Bank of India?

I. Buying and selling Government bonds
II. Buying and selling foreign currency
III. Pension fund management
IV. Lending to private companies
V. Printing and distributing currency notes

Select the correct answer using the code given below:

(a) I and II only **(b) II, III and IV**
(c) I, III, IV and V **(d) I, II and V**

(2025)

Ans. (d)

- **I is correct:** RBI earns income through Open Market Operations (OMOs), where it buys and sells government securities. The interest earned on government bonds is a major source of revenue.
- **II is correct: Dealings in the foreign exchange market that the RBI engages in may also contribute to the bank's profits.** The RBI, for instance, may buy dollars cheaply and sell them dear in the future to pocket profits.
- **III is not correct: Pension fund management is not a source of income for the Reserve Bank of India (RBI).** The RBI's primary function is to regulate and oversee the financial system and maintain monetary stability, not to manage pension funds.
- **IV is not correct:** RBI does not lend to private companies. It lends to commercial banks and government institutions in its capacity as lender of last resort.
- **V is correct:** RBI's goal is public good, not profit, but some of its actions in financial markets - done to maintain stability - can generate income. **Even printing currency brings income - called seigniorage** — since notes cost less to produce than their face value.

5. Consider the following countries :

I. United Arab Emirates
II. France
III. Germany
IV. Singapore
V. Bangladesh

How many countries amongst the above are there other than India where international merchant payments are accepted under UPI?

(a) Only two **(b) Only three**
(c) Only four **(d) All the five**

(2025)

Ans. (b)

- **About Unified Payments Interface (UPI):** It is an instant real-time payment system, allowing users to transfer money on a real-time basis, across multiple bank accounts without revealing details of one's bank account to the other party. National Payments Corporation of India (NPCI) operates the UPI.
- **Option (b) is the correct answer:** Over the past two years, **many countries have started accepting payments through UPI apps. These are** Bhutan, **France,** Mauritius, Nepal, **Singapore,** Sri Lanka, and **UAE.**

6. With reference to the rule/rules imposed by the Reserve Bank of India while treating foreign banks, consider the following statements:

1. There is no minimum capital requirement for wholly owned banking subsidiaries in India.

2. For wholly owned banking subsidiaries in India, at least 50% of the board members should be Indian nationals.

Which of the statements given above is/are correct?

(a) 1 only (b) 2 only

(c) Both 1 and 2 (d) Neither 1 nor 2

(2024)

Ans. (d)

- **Statement 1 is not correct:** Foreign banks are permitted to operate in India either as branches or Wholly Owned Subsidiaries (WOS). Permission for opening of branches by foreign banks in India is guided by India's commitment to WTO. As per the guidelines of RBI, the initial minimum paid-up voting equity capital for a WOS shall be Rs 500 crore for new entrants. Existing branches of foreign banks desiring to convert into WOS shall have a minimum net worth of Rs 500 crore.
- **Statement 2 is not correct:** The composition of the Board of directors of WOS of foreign banks in India should meet the following requirements:
  - **Not less than 50 per cent directors should be Indian nationals/NRIs/PIOs (therefore not necessarily Indian national) subject to the condition that one-third of the directors are Indian nationals resident in India**
  - Not less than 50 per cent of the Directors should be non-executive directors
  - A minimum of one-third of the directors should be totally independent of the management of the subsidiary in India, its parent or associates.
  - The directors shall conform to the `Fit and Proper` criteria as laid down in our extant guidelines.

7. Consider the following statements in respect of the digital rupee:

1. It is a sovereign currency issued by the Reserve Bank of India RBI alignment with its monetary policy.

2. It appears as a liability on the RBI's balance sheet.

3. It is insured against inflation by its very design.

4. It is freely convertible against commercial bank money and cash.

Which of the statements given above are correct?

(a) 1 and 2 only (b) 1 and 3 only

(c) 2 and 4 only (d) 1, 2 and 4

(2024)

Ans. (d)

- **About Digital Rupee:** Digital Rupee (e) is a Central Bank Digital Currency (CBDC) issued by the Reserve Bank of India (RBI). It is similar to physical cash except that the e-rupee is held electronically in a digital wallet overseen by the RBI. The digital rupee is recognised as legal tender by the RBI, and thus has to be accepted by everyone in the country as a medium of exchange.
- **Statement 1 is correct:** Digital Rupee (e) is a sovereign currency issued by the Reserve Bank of India RBI alignment with its monetary policy.
- **Statement 2 is correct:** Just like physical currency, Digital Rupee represents a claim on the central bank, and therefore will appear as a liability on RBI's balance sheet.
- **Statement 3 is not correct:** Inflation will affect the purchasing power of the Digital Rupee in the same way it affects physical currency. There is nothing inherent in the design of the Digital Rupee that makes it insured against inflation.
- It has no link with its issuance with the inflation in india.
- **Statement 4 is correct:** One of the key features of the digital rupee is its interchangeability with other forms of money, such as commercial bank money and physical cash, at par value.

ADDITIONAL INFORMATION

- Digital Rupee is expected to lower the cost of issuance of money and transactions.
- Holders of Digital Rupee need not have a bank account
- There is no intermediation of bank while making a payment through Digital Rupee
- RBI had launched the first pilot of Digital Rupee-Retail segment (e₹-R) in 2022.

8. Consider the following statements :

Statement-I: In the post-pandemic recent past, many Central Banks worldwide had carried out interest rate hikes.

Statement-II: Central Banks generally assume that they have the ability to counteract the rising consumer prices via monetary policy means.

Which one of the following is correct in respect of the above statements?

(a) Both Statement-I and Statement-II are correct and Statement-II is the correct explanation for Statement-I

(b) Both Statement-I and Statement-II are correct and Statement-II is not the correct explanation for Statement-I

(c) Statement-I is correct but Statement-II is incorrect

(d) Statement-1 is incorrect but Statement-II is correct

(2023)

Ans. (a)

- **Statement I is correct**: Post-pandemic, many central banks had carried out interest rate hikes in response to rising inflation.

- **Statement II is correct:** Central Banks generally assume that they have the ability to counteract the rising consumer prices via monetary policy mean like interest rates hikes. When Central banks hike interets rates, it increases the borrowing costs for customers and business, This, in turn, discourages consumer and business spending and can help in bringing down the consumer prices.

9. Which one of the following activities of the Reserve Bank of India is considered to be part of 'sterilization'?

(a) Conducting 'Open Market Operations'

(b) Oversight of settlement and payment systems

(c) Debt and cash management for the Central and State Governments

(d) Regulating the functions of Non-Banking Financial Institutions

(2023)

Ans. (a)

- Sterilization is a monetary intervention by the Central bank of the country to keep the money supply stable against external shocks such as a sudden increase in foreign exchange inflow.
- Sterilization most frequently involves the **purchase or sale of financial assets by a central bank** and is designed to offset the effect of foreign exchange market intervention. The sterilization process is used to manipulate the value of one domestic currency relative to another and is initiated in the foreign exchange market. So, among the given options, **Open Market Operations** (a term that refers to the purchase and sale of securities in the open market by the RBI) is an activity that will be carried out as part of the sterilization. **Hence, option (a) is the correct answer.**

10. With reference to Central Bank digital currencies, consider the following statements:

1. It is possible to make payments in a digital currency without using US dollar or SWIFT system.

2. A digital currency can be distributed with a condition programmed into it such as a time-frame for spending it.

Which of the statements given above is/are correct?

(a) 1 only **(b) 2 only**

(c) Both 1 and 2 **(d) Neither 1 nor 2**

(2023)

Ans. (c)

- **Statement 1 is correct**: Alternatives to SWIFT and the U.S. dollar are coming from two directions: cryptocurrencies and central bank digital currencies. Central Bank Digital Currency (CBDC) is the legal tender issued by a central bank in a digital form. Digital currencies will render obsolete many existing standards and rules of the international monetary system. Countries will be able to directly exchange digital currencies in a bilateral way and without going through SWIFT or similar settlement systems. When the technology allows seamless and instantaneous convertibility from one sovereign currency into another, it changes the practical need for a dominant global reserve currency.
- **Statement 2 is correct**: One key feature of CBDC is **its programmability**. There is growing interest in the potential of programmability, as it would offer myriad uses. Programmable money is money with in-built rules and that comes with constraints for the user. With these rules, money could also be programmed to **have an expiration date** or be restricted for certain goods, for example. However, a CBDC with these restrictions would affect currency performance – and come with palpable legal implications. This would certainly influence the acceptance of CBDC. Example -the **digital yuan is programmable** to the point that the currency can be **made to expire**, thus forcing consumers to use it up by a certain date.

11. With reference to the Indian economy, consider the following statements:

1. If the inflation is too high, Reserve Bank of India (RBI) is likely to buy government securities.

2. If the rupee is rapidly depreciating, RBI is likely to sell dollars in the market.

3. If interest rates in the USA or European Union were to fall, that is likely to induce RBI to buy dollars.

Which of the statements given above are correct?

(a) 1 and 2 only (b) 2 and 3 only

(c) 1 and 3 only (d) 1, 2 and 3

(2022)

Ans. (b)

- **Statement 1 is not correct:** If inflation is too high, the Reserve Bank of India (RBI) would take steps to lower the money supply in the economy. Hence, **RBI is likely to sell government securities.** On the contrary, when inflation is under control but economic growth rate is low, RBI is likely to increase the money supply by buying government securities.
- **Statement 2 is correct: When rupee depreciates rapidly, RBI sells dollars in the market.** This increases the supply of dollars in the economy, and the rupee price of the dollar (R/$) comes down. On the other hand, **when Rupee appreciates rapidly, RBI buys dollars** and injects rupees into the economy.
- **Statement 3 is correct:** If interest rates in the USA or European Union were to fall, the Foreign Institutional Investors would shift their investment from these countries to India in search of higher return. This will increase the demand for rupees, leading to appreciation of Rupee. In response, RBI will buy dollars and inject rupees in the economy.

ADDITIONAL INFORMATION

- **RBI's Open market intervention (OMO):** Open Market Operations refers to selling and buying of Government security by RBI to and from the market. OMO is a **quantitative monetary policy tool** to control money supply, and stabilize inflation in the economy. Other quantitative monetary policy tools include Bank Rate, Repo Rate, Reverse Repo Rate, Cash Reserve Ratio (CRR), and Statutory Liquidity Ratio (SLR).
- **Depreciation versus devaluation of currency:** Depreciation refers to the fall in market prices of a domestic currency in terms of a foreign currency **due to the market forces of demand and supply.** Whereas, devaluation refers to the reduction in prices of a domestic currency in terms of a foreign currency **due to the actions of the Central Bank and Government Bank.**

12. The money multiplier in an economy increases with which one of the following?

(a) Increase in the Cash Reserve Ratio in the banks.

(b) Increase in the Statutory Liquidity Ratio in the banks.

(c) Increase in the banking habits of the people.

(d) Increase in the population of the country.

(2021)

Ans. (c)

- Money multiplier explains the process through which the "base money" created by a central bank multiplies in the banking system. Banks create new money whenever they make a loan. A higher money multiplier indicates that the banking system generates a higher money supply out of money given by the central bank.

- **Option (a) is not correct:** Cash Reserve Ratio (CRR) is a certain minimum amount of deposit that the commercial banks have to hold as reserves with the Central Bank (RBI). An increase in CRR means that banks have less money to lend, which in turn reduces the money creation by banks, thereby reducing the money multiplier.
- **Option (b) is not correct:** Statutory Liquidity Ratio or SLR is a minimum percentage of deposits that a commercial bank has to maintain in the form of liquid cash, gold or other securities. Increase in SLR also reduces the lending capacity of the bank, thereby reducing the money multiplier.
- **Option (c) is correct:** Increase in the banking habits of the people increases the money multiplier in an economy. When people hold less cash and instead deposit their money in the bank, it increases the bank's lending capacity. Whenever a bank lends, it creates new money and the money supply in the economy increases.
- **Option (d) is not correct:** Increase in the population of the country alone can't increase the money multiplier. More people doesn't mean more money with the bank, as they may hold their money in cash too. So, it's the banking habit of people that will determine the money multiplier.

13. In India, the central bank's function as the 'lender of last resort' usually refers to which of the following?

1. Lending to trade and industry bodies when they fail to borrow from other sources.

2. Providing liquidity to the banks having a temporary crisis.

3. Lending to governments to finance budgetary deficits.

Select the correct answer using the code given below:

(a) 1 and 2 only (b) 2 only

(c) 2 and 3 only (d) 3 only

(2021)

Ans. (b)

- Like individual consumers, banks also need their own mechanism to transfer funds and settle inter-bank transactions. To fulfill this role, the Reserve Bank of India (RBI) acts as the banker to banks. Individual banks maintain current accounts with the Reserve Bank. These current accounts are used for settling inter-bank obligations.
- **Statement 2 is correct: As a Banker to Banks, the Reserve Bank also acts as the 'lender of the last resort'. It means that RBI can come to the rescue of a bank that is solvent but faces temporary liquidity problems by supplying it with much needed liquidity when no one else is willing to extend credit to that bank.** The Reserve Bank extends this facility to protect the interest of the depositors of the bank and to prevent possible failure of the bank, which in turn may also affect other banks and institutions and can have an adverse impact on financial stability and overall economy.

ADDITIONAL INFORMATION

E-kuber system: The current accounts of individual banks are opened with RBI through the e-Kuber system, which is the Core banking solution platform of RBI.

14. Consider the following statements:

1. The Governor of the Reserve Bank of India (RBI) is appointed by the Central Government.

2. Certain provisions in the Constitution of India give the Central Government the right to issue directions to the RBI in public interest.

3. The Governor of the RBI draws his power from the RBI Act.

Which of the above statements are correct?

(a) 1 and 2 only (b) 2 and 3 only

(c) 1 and 3 only (d) 1, 2 and 3

(2021)

Ans. (c)

- **Statement 1 is correct:** According to Section 8 of the Reserve Bank of India Act 1934, the Governor of the Reserve Bank of India (RBI) is appointed by the Central Government. As per the government's reply in Parliament, the decision regarding RBI governor is taken by the Prime Minister's Office (PMO) on the recommendation of the Union Finance Minister.
- **Statement 2 is not correct: Section 7 of the RBI Act, 1934 (and not the Constitution of India)** gives the Central Government the right to issue directions to the RBI in public interest.

- **Statement 3 is correct:** RBI Act, 1934 has detailed provisions regarding the power of Governor as well as Deputy Governor of RBI.

ADDITIONAL INFORMATION

Other important provisions of RBI Act 1934:

- Governor and not more than four Deputy Governors are to be appointed by the Central Government.
- The Governor and a Deputy Governor shall hold office for such term not exceeding five years as the Central Government may fix when appointing them, and shall be eligible for re-appointment.
- The Central Government may remove the RBI Governor and Deputy Governor from their office.
- If in the opinion of the Central Government, the RBI fails to carry out any of the obligations imposed on it by or under this Act, the Central government may declare the Central Board to be superseded. Thereafter the general superintendence of the RBI shall be entrusted to such agency as the Central government may determine.

15. If you withdraw ₹1,00,000 in cash from your Demand Deposit Account at your bank, the immediate effect on aggregate money supply in the economy will be:
(a) to reduce it by ₹1,00,000
(b) to increase it by ₹1,00,000
(c) to increase it by more than ₹1,00,000
(d) to leave it unchanged

(2020)

Ans. (d)

- Money supply in the economy is the total stock of money in circulation among the public at a particular point of time. Reserve Bank of India (RBI) publishes figures for four alternative measures of money supply, viz. M1, M2, M3 and M4.
- M3 is the most commonly used measure of money supply.
- **M3 = (Currency held by the public) + (Demand deposits with the banks) + (Time Deposits with Banks) + (Other deposits with RBI)**
- When a person withdraws ₹1,00,000 from his demand deposit account in the bank, one component of M3 money supply, i.e. "Demand deposit with the banks", decreases by ₹1 lac. But at the same time, another component of M3 money supply, i.e. "Currency held by the public" increases by ₹1 lac. Therefore, the **overall money supply in the economy won't change. Money will just move out from the bank to the public. Hence, option (d) is the correct answer.**

ADDITIONAL INFORMATION

- M1 = (Currency with the public) + (Demand deposits with the banks) + ('Other' deposits with the RBI)
- M2 = (M1) + (Savings deposits of post office savings banks)
- M3 = (M1)+ (Time deposits with the banks)
- M4 = (M3) + (All deposits with post office savings banks excluding National Savings Certificates)
- **M1 and M2 are known as narrow money. M3 and M4 are known as broad money.** These gradations are in decreasing order of liquidity. **M1 is the most liquid and easiest for transactions whereas M4 is the least liquid of all.**

16. If the RBI decides to adopt an expansionist monetary policy, which of the following would it *not* do?
1. Cut and optimize the Statutory Liquidity Ratio
2. Increase the Marginal Standing Facility Rate
3. Cut the Bank Rate and Repo Rate
Select the correct answer using the code given below:
(a) 1 and 2 only (b) 2 only
(c) 1 and 3 only (d) 1, 2 and 3

(2020)

Ans. (b)

- The objective of expansionary monetary policy of RBI is to increase the money supply in the economy and stimulate economic growth. RBI uses monetary policy tools like Repo rate, Marginal Standing Facility Rate, Cash Reserve Ratio (CRR), Statutory Liquidity Ratio (SLR) etc. to change the money supply in the economy.
- **Statement 1 comes under expansionist monetary policy:** Statutory Liquidity Ratio or SLR is a minimum percentage of deposits that a commercial bank has to maintain in the form of liquid cash, gold or other securities. Cutting the SLR increases the lending capacity of the

bank, leading to increased money supply in the economy. **So, cutting the SLR is a step that the RBI would take as part of expansionist monetary policy.**

- **Statement 2 does not come under expansionist monetary policy:** Marginal standing facility (MSF) is an emergency window for banks to borrow from the RBI by pledging government securities at a rate higher than the repo rate. Increase in the Marginal Standing Facility Rate will make the borrowings costly, thereby discouraging the borrowings. So, RBI won't **increase the MSF rate as part of expansionist monetary policy.**
- **Statement 3 comes under expansionist monetary policy:** Bank Rate acts as the penal rate charged on banks for shortfalls in meeting their reserve requirements. Repo rate is the rate at which the central bank (RBI in case of India) lends money to commercial banks against the pledge of government securities. Cutting the Bank Rate and Repo Rate will make the borrowings cheaper, thereby encouraging more borrowings and ultimately increasing the money supply. Therefore, Cutting the Bank Rate and Repo Rate is a step that the RBI would take as part of expansionist monetary policy.

ADDITIONAL INFORMATION

RBI's steps as part of expansionary monetary policy and contractionary monetary policy can be summarized as:

Tool	Expansionary monetary policy	Contractionary monetary policy
Cash reserve ratio	Decrease	Increase
Statutory liquid ratio	Decrease	Increase
MSF rate	Decrease	Increase
Repo rate	Decrease	Increase

17. Consider the following statements:

The Reserve Bank of India's recent directives relating to 'Storage of Payment System Data', popularly known as data diktat, command the payment system providers that

1. **They shall ensure that entire data relating to payment systems operated by them are stored in a system only in India**
2. **They shall ensure that the systems are owned and operated by public sector enterprises**
3. **They shall submit the consolidated system audit report to the Comptroller and Auditor General of India by the end of the calendar year**

Which of the statements given above is/are correct?

(a) 1 only **(b) 1 and 2 only**
(c) 3 only **(d) 1, 2 and 3**

(2019)

Ans. (a)

- **Statement 1 is correct:** As per the RBI notification, all system providers shall ensure that the entire data relating to payment systems operated by them are stored in a system only in India (This covers not only card payment services by Visa and MasterCard but also of companies such as Paytm, WhatsApp and Google which offer electronic or digital payment services)
- **Statement 2 is not correct:** There is no mention that data systems are to be owned and operated by public sector enterprises. Hence all system providers can use private services.
- **Statement 3 is not correct:** System providers shall submit the System Audit Report (SAR) duly approved by the Board to the Reserve Bank of India (not CAG).

18. Which one of the following statements correctly describes the meaning of legal tender money?

(a) The money which is tendered in courts of law to defray the fee of legal cases
(b) The money which a creditor is under compulsion to accept in settlement of his claims
(c) The bank money in the form of cheques, drafts, bills of exchange, etc.
(d) The metallic money in circulation in a country

(2018)

Ans. (b)

- **Legal tender is a money that cannot be refused by any citizen of the country for settlement of any kind of transaction.** Therefore, a creditor is under compulsion to accept legal tender for the settlement of his claims. **Hence, option (b) is the correct answer.**

- **Legal tender in India:**
  - Every banknote issued by Reserve Bank of India (₹2, ₹5, ₹10, ₹20, ₹50, ₹100, ₹200, ₹500 and ₹2000) unless withdrawn from circulation.
  - ₹1 notes issued by Government of India.
  - Coin of any denomination not lower than one rupee for any sum not exceeding 1,000 rupees.
  - Fifty paise (half rupee) coins for any sum not exceeding ten rupees.
- **Note:** While anyone cannot be forced to accept coins beyond the limits mentioned above, voluntarily accepting coins for amounts exceeding the limits mentioned above is not prohibited.

ADDITIONAL INFORMATION

Cheques are not legal tenders as they can be refused as a mode of payment by a party.

19. Which of the following statements is/are correct regarding the Monetary Policy Committee (MPC)?

1. It decides the RBI's benchmark interest rates,

2. It is a 12-member body including the Governor of RBI and is reconstituted every year.

3. It functions under the chairmanship of the Union Finance Minister.

Select the correct answer using the code given below:

(a) 1 only **(b) 1 and 2 only**

(c) 3 only **(d) 2 and 3 only**

(2017)

Ans. (a)

- RBI Act, 1934 provides for a six-member monetary policy committee (MPC) to be constituted by the Central Government. The first such MPC was constituted in 2016.
- **Statement 1 is correct:** MPC determines the benchmark interest rates (e.g. policy repo rate) required to achieve the inflation target.
- **Statement 2 is not correct:** It is a six-member body including the Governor of RBI. MPC consists of three members from RBI and three external experts appointed by the Central Government. Three external experts hold the office for a period of four years.
- **Statement 3 is not correct:** RBI Governor is the Chairperson of MPC.

ADDITIONAL INFORMATION

- Each member of the MPC has one vote. In the event of an equality of votes, the Governor has a second or casting vote.
- MPC is required to meet at least four times in a year. The quorum for the meeting of the MPC is four members.
- Three external expert members of MPC are not eligible for reappointment after completing their term of 4 years.

20. What is/are the purpose/purposes of the 'Marginal Cost of Funds based Lending Rate (MCLR)' announced by RBI?

1. These guidelines help improve the transparency in the methodology followed by banks for determining the interest rates on advances.

2. These guidelines help ensure availability of bank credit at interest rates which are fair to the borrowers as well as the banks.

Select the correct answer using the code given below.

(a) 1 only **(b) 2 only**

(c) Both 1 and 2 **(d) Neither 1 nor 2**

(2016)

Ans. (c)

- RBI instituted a new **lending rate system for banks** – the marginal cost of funds based lending rate (MCLR) system – effective April 1, 2016. The MCLR system **replaced the earlier Base Rate system.**
- **Statement 1 is correct:** Under this system, banks are expected to determine their benchmark lending rate based on the formula prescribed for the calculation of the marginal cost of funds. It reduces the scope for bank's discretion that existed during the base rate regime and enhances the transparency in the methodology followed by banks for determining the interest rates.
- **Statement 2 is correct:** As the MCLR system has a more transparent methodology to determine lending rates by banks, it leads to appropriate pricing of loans which is fair to both banks as well as borrowers.

ADDITIONAL INFORMATION

- The actual bank lending rates for loans of different categories are determined by adding the components of spread to MCLR.
- When the MCLR system was instituted in 2016, it **was expected to improve monetary policy transmission.** (Monetary policy transmission is the process through which policy action of the central bank is transmitted to the financial system and ultimately to other sectors of the economy). But as per an internal study group of RBI, the monetary policy transmission has remained below expectations even under the new MCLR system.

21. When the Reserve Bank of India reduces the Statutory Liquidity Ratio by 50 basis points which of the following is likely to happen?

(a) India's GDP growth rate increases drastically

(b) Foreign Institutional Investors may bring more capital into our country

(c) Scheduled Commercial Banks may cut their lending rates

(d) It may drastically reduce the liquidity to the banking system

(2015)

Ans. (c)

- Statutory Liquidity Ratio or SLR is a minimum percentage of deposits that a commercial bank has to maintain in the form of liquid cash, gold or other RBI approved securities.
- Higher the SLR, higher the amount to be maintained in the form of liquid cash, gold or RBI approved securities. This will reduce the amount of cash that can be disbursed by banks as loan. This increases the lending rates. **On the other hand, when RBI reduces SLR, it frees up the money and thus banks can now lend more easily with lower lending rates. Hence, option (c) is the correct answer.**

ADDITIONAL INFORMATION

Provisions of SLR is applicable to

- All Scheduled Commercial Banks (SCBs) (including Regional Rural Banks)
- Small Finance Banks (SFBs), Payments Banks, Local Area Banks (LABs),
- Primary (Urban) Co-operative Banks (UCBs), State Co-operative Banks (StCBs) and District Central Co-operative Banks (DCCBs).

22. With reference to Indian economy, consider the following:

1. Bank rate

2. Open market operations

3. Public debt

4. Public Revenue

Which of the above is/are component/components of Monetary Policy?

(a) 1 only **(b) 2, 3 and 4 only**

(c) 1 and 2 only **(d) 1, 3 and 4 only**

(2015)

Ans. (c)

- Monetary policy is the policy of the central bank to control and regulate money supply and credit in the economy.
- Under the Reserve Bank of India Act,1934, RBI is entrusted with the responsibility of conducting monetary policy in India with the primary objective of maintaining price stability while keeping in mind the objective of growth.
- Monetary policy tools used by RBI can be divided into: (a) Quantitative tools (b) Qualitative tools.
- **Quantitative tools of monetary policy: Bank Rate**, Repo Rate, Reverse Repo Rate, Marginal standing facility, Cash Reserve Ratio, Statutory Liquidity Ratio, **Open market operations**, Liquidity Adjustment Facility. **Hence, 1 and 2 are correct.**
- **Qualitative tools of monetary policy:** Margin Requirements, Moral Suasion and Credit Rationing
- **Public Debt and Public Revenue are part of the fiscal policy of the government. Hence, 3 and 4 are not correct.**

23. If the interest rate is decreased in an economy, it will

(a) decrease the consumption expenditure in the economy

(b) increase the tax collection of the Government

(c) increase the investment expenditure in the economy

(d) increase the total savings in the economy

(2014)

Ans. (c)

- Interest rate represents the cost of borrowing money. It is generally expressed as a % of the total borrowed money. Interest rates also show the return received on saving money in the bank or from an asset like a government bond.

- **Option (a) is not correct**: Lower interest rate will make borrowing cheaper - allowing people to spend more. Hence, the consumption expenditure will increase.
- **Option (b) is not correct**: There is no direct correlation between interest rate and tax collection. Tax collection depends on various factors and therefore, it can't be concluded that decrease in interest rate will lead to increase in tax collection.
- **Option (c) is correct**: A higher interest rate reduces the investment expenditure and vice versa. This is due to the fact that higher rates increase the cost of borrowing and require investment to have a higher rate of return to be profitable. On the other hand, lower interest rates will make borrowing cheaper - allowing businesses to borrow more. Hence, the investment expenditure will increase.
- **Option (d) is not correct**: If interest rates are lower. people will tend to save less as they will get lower returns. Hence, the total savings in the economy will decrease.

24. The terms 'Marginal Standing Facility Rate' and 'Net Demand and Time Liabilities', sometimes appearing in news, are used in relation to

(a) banking operations
(b) communication networking
(c) military strategies
(d) supply and demand of agricultural products

(2014)

Ans. (a)

- 'Marginal Standing Facility Rate' and 'Net Demand and Time Liabilities' are related to the banking operations.
- **Marginal Standing Facility:**
  - It is one of the monetary policy tools used by RBI. It is the penal rate at which banks can borrow, **on an overnight basis,** from the Reserve Bank by dipping into their Statutory Liquidity Ratio (SLR) portfolio up to a predefined limit (2 per cent).
  - This provides a **safety valve against unanticipated liquidity shocks** to the banking system. The MSF rate is placed at 25 basis points above the policy repo rate.
- **Net Demand and Time Liabilities:**
  - Demand Liabilities' include all liabilities which are payable on demand and they include current deposits, demand liabilities portion of savings bank deposits.
  - Time Liabilities are those which are payable otherwise than on demand and they include fixed deposits, cash certificates etc.
  - **NDTL is the difference between the total demand and time liabilities of a bank and the deposits in the form of assets held by other banks**.
  - Bank's NDTL = Demand and time liabilities (deposits) – deposits with other banks. **Hence, option (a) is the correct answer.**

25. An increase in the Bank Rate generally indicates that the

(a) Market rate of interest is likely to fall
(b) Central Bank is no longer making loans to commercial banks
(c) Central Bank is following an easy money policy
(d) Central Bank is following a tight money policy

(2013)

Ans. (d)

- An increase in the Bank Rate generally indicates that the Central Bank is following a tight money policy. **Hence, option (d) is the correct answer.**
- Bank Rate is the rate at which the Reserve Bank is ready to buy or rediscount bills of exchange or other commercial papers. With the increase in bank rate, the cost of bank's borrowing from RBI would increase. This, in turn, would translate into higher lending rates of banks. Higher lending rates discourage borrowing in the economy, leading to lower money supply.
- **As increase in Bank rate leads to decrease in money supply, it is an example of tight monetary policy.**
- Increase in Bank rate will make the loans taken by commercial banks more expensive; this reduces the reserves held by the commercial bank and hence decreases money supply.
- RBI opts for tight monetary policy, or contractionary monetary policy when it wants to keep inflation under control. Under tight monetary policy, RBI tries to reduce the demand for money and limit the pace of economic expansion. Usually, this involves increasing

interest rates. Thus increasing the Bank Rate would mean a **tight monetary policy**.

ADDITIONAL INFORMATION

- Tight monetary policy will typically be chosen when inflation is above the inflation target or policymakers fear inflation is likely to rise without a tightening of monetary policy.
- On the contrary, expansionist monetary policy is opted by the RBI when inflation is under control, but economic growth is sluggish.

26. Consider the following liquid assets:

1. Demand deposits with the banks
2. Time deposits with the banks
3. Savings deposits with the banks
4. Currency

The correct sequence of these assets in the decreasing order of liquidity is

(a) 1-4-3-2 **(b) 4-3-2-1**
(c) 2-3-1-4 **(d) 4-1-3-2**

(2013)

Ans. (d)

- An asset is said to be liquid if it is easy to sell or convert into cash without any loss in its value.
- The sequence of assets in the decreasing order of liquidity is: **Currency** > **Demand deposits** > **Saving deposits** > **TIme deposits**. **Hence, option (d) is the correct answer.**
- **Currency** is the most liquid asset.
- **Demand deposit** accounts allow the account holders to withdraw money from the account **"on demand," at any time**. Demand deposit accounts generally pay no or little interest. While Savings deposits can also be withdrawn at any time, however, there are **certain interest payable** on the savings deposits which deter the public from withdrawing. In this sense demand deposit is more liquid than savings deposit.
- **Savings deposits** are more liquid than time deposits because one can easily access the money in savings deposit while money in **Time deposits are locked in for a particular period of time** and generally one has to pay a penalty to access the money before the stipulated period of time.

27. The Reserve Bank of India regulates the commercial banks in matters of

1. Liquidity of assets
2. Branch expansion
3. Merger of banks
4. Winding-up of banks

Select the correct answer using the codes given below:

(a) 1 and 4 only **(b) 2, 3 and 4 only**
(c) 1, 2 and 3 only **(d) 1, 2, 3 and 4**

(2013)

Ans. (d)

- **The Banking Regulation Act, 1949** empowers the Reserve Bank of India to inspect and supervise commercial banks. RBI regulates commercial banks in matters of:
    - Issuance of 'licences' for opening of banks
    - **'Authorisations' for opening of branches by banks in India,**
    - Monitoring maintenance of SLR and CRR by banks (which **affects the liquidity**)
    - Overseeing the **amalgamation**, reconstruction and **liquidation of banking** companies,
    - Anti-Money Laundering and Combating Financing of Terrorism and issuing of instructions regarding KYC etc. **Hence, option (d) is the correct answer.**

28. In the context of Indian economy, 'Open Market Operations' refers to

(a) borrowing by scheduled banks from the RBI
(b) lending by commercial banks to industry and trade
(c) purchase and sale of government securities by the RBI
(d) None of the above

(2013)

Ans. (c)

- Open Market Operations (OMO) means the buying and selling of government securities in the open market in order to expand or contract the amount of money in the banking system. **Purchases inject money** into the banking system and stimulate growth while sales of securities do the opposite. **Hence, option (c) is the correct answer.**