

H.W
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Date

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Exercise

1. In situations with high risks, credit might ~~cause~~ create further problems for the borrower. Explain.

Ans In situations with high risks, credit might create further problems for the borrower. This is also known as a debt-trap. Taking credit involves an interest rate on the loan and if this is not paid back, then the borrower is forced to give up his collateral or asset used as the guarantee, to the lender. If a farmer takes a loan for crop production and the crop fails, loan payment becomes impossible. To repay the loan the farmer may sell a part of his land making the situation worse than before. Thus, in situations with high risks, if the risks affect a borrower badly, then he ends up losing more than he would have without the loan.

2. How does money solve the problem of double coincidence of wants?

Explain with an example of your own.

Ans In a barter system where goods are directly exchanged without the use of money, double coincidence of wants is an essential feature. By serving as a medium of exchanges, money removes the need for double coincidence of wants and the difficulties associated with the barter system. For example, it is no longer necessary for the farmer to look for a book publisher who will buy his cereals at the same time sell him books. All he has to do is find a buyer for his cereals. If he has exchanged his cereals for money, he can purchase any goods or service which he needs. This is because money acts as a medium of exchange.

3. How do banks mediate between those who have surplus money and those who need money?

Ans Banks keep small portion deposits as cash (15%) for themselves.

(to pay the depositors on demand). They use the major portion of the deposits to extend loans to those who need money. In this way banks mediate between those who have surplus money and those who need money.

4. Look at a 10 rupee note. What is written on top? Can you explain this statement?

Ans On the top written as "Reserve Bank of India" and "Guaranteed by the Government".

In India, Reserve Bank of India issues currency notes on behalf of the central government. The statement means that the currency is authorized or guaranteed by the Central Government. That is, Indian law legalizes the use of rupee as a medium of payment that can not be refused in setting transaction in India.