

Chapter End Test

Date : _____	Economics	BATCH
Duration: 45 Min. Max. Marks : 45	Topic : Balance of Payment	XII

General Instructions:

1. All questions are compulsory.
2. Use of calculators is not allowed.

Section A

(Objective Type Question)

1. An India company located in India invests in a company located abroad. This transaction is entered in India's Balance of Payment account on:
(a) Credit side of current account (b) Debit side of current account
(c) Credit side of Capital account (d) Debit side of Capital account
2. Surplus on BOP arises when
(a) Autonomous Payment > Autonomous Receipts
(b) Accommodating Receipts > Accommodating Payment
(c) Accommodating Payment > Accommodating Receipts
(d) Autonomous Receipts > Autonomous Payment
3. Gift and Remittances to abroad are recorded on the
(a) Credit side of current Account (b) Debit side of Capital Account
(c) Debit side of Current Account (d) Credit side of capital Account
4. A change from ₹ 60 = 1\$ to ₹ 62 = 1\$ indicates that ₹ has _____ .
(a) Appreciated (b) depreciated
(c) Neither (a) nor (b) (d) either (a) or (b)
5. Depreciation of domestic currency leads to rise in
(a) Exports (b) Imports
(c) Both (a) and (b) (d) neither (a) nor (b)
6. Devaluation of domestic currency means:
(a) Reduction in the value of domestic currency by the market forces.
(b) Reduction in the value of domestic currency by the government
(c) Both (a) and (b) (d) Neither (a) nor (b)
7. Other things remaining constant, when in a country the price of foreign currency falls, National income is _____ .
(a) Likely to rise (b) likely to fall
(c) likely to rise and fall both (d) Not affected
8. Imports of goods & services raises the _____ of foreign exchange.
(a) Supply (b) Demand
(c) Both (a) and (b) (d) Neither (a) nor (b)

9. The value of US dollar \$1 has gone down from ₹ 73 to ₹ 70. It means
 (a) India Rupee has appreciated (b) US Dollar has depreciated
 (c) Both (a) and (b) (d) None of these
10. Balance of payment is a _____ concept
 (a) Stock (b) Flow
 (c) Both (a) and (b) (d) Neither (a) nor (b)
11. Export and imports of goods is also known as
 (a) Invisible trade (b) visible trade
 (c) One-sided transaction (d) unrequited transfer
12. _____ is the difference between value of goods sold to the rest of the world and value of goods imported from rest of the world.
 (a) Balance of payment (b) Balance of trade
 (c) Balance of current account (d) Balance of capital account
13. Export of Goods & services raises _____ of foreign exchange.
 (a) Supply (b) demand
 (c) Both (a) and (b) (d) neither (a) nor (b)
14. A company located in India receives a loan from a company located abroad. How is this transaction recorded in India's BOP account?
 (a) Credit side of Current account (b) Debit side of current account
 (c) Credit side of Capital Account (d) Credit side of capital account
15. Indian Rupees is appreciated in term of British Pound because of
 (a) Falling demand of pounds (b) shortage of pounds
 (c) More supply of Indian Rupee (d) less demand for Indian Rupee

Section B

(Subjective Type Question)

1. Define Balance of payment deficit. [1]
2. Are the following entered (i) on the credit side or the debit side and (ii) in the current account or capital account in balance of payment account? You must give reason for your answer. [3]
- (a) Investment from abroad
 (b) Import of machinery
 (c) Borrowing from abroad

OR

Distinguish between autonomous and accommodating transaction of balance of payment account.

3. Why does the demand for foreign currency fall and supply rises when its price rises? Explain. [4]
4. (a) Define 'Trade Surplus'. How is it different from current account surplus? [3+3=6]
 (b) "Indian Rupee (₹) plunged to all times low of ₹ 74.48 against the US dollar (\$)



Hints/Solutions to Chapter End Test

Date : _____	Economics	BATCH
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[Section – A]

- | | |
|---------|---------|
| 1. (d) | 2. (d) |
| 3. (c) | 4. (b) |
| 5. (a) | 6. (b) |
| 7. (a) | 8. (b) |
| 9. (c) | 10. (b) |
| 11. (b) | 12. (b) |
| 13. (a) | 14. (c) |
| 15. (a) | |

[Section – B]

1. A deficit in the BOP occurs when during the year the autonomous inflow of foreign exchange falls short of autonomous outflow.
i.e. Autonomous payments > Autonomous receipts
2. (a) Credit side of capital account because of increase foreign exchange liability.
(b) Debit side of current account because of no change in asset and liability of the residence country.
(c) Credit side capital account because increase in foreign in exchange liability.

OR

Autonomous	Non- Autonomous/Accommodating items
Autonomous items refer to those transactions which take place due to some economic motive (such as profit maximisation).	Accommodating items refer to the transactions that are undertaken in order to maintain the 'balance' in the BOP account.
Such transactions are independent of the state of BOP account. For example, if an MNC is making investment in India with the aim of earning profit, then such a transaction is independent of the country's BOP situation.	These are capital transactions which are meant to correct the disequilibrium in autonomous items of balance of payments.
These items are also known as 'above the line items'.	These items are also known as 'below the line items'.
Autonomous transactions take place on both current and capital, accounts. e.g. export and import of goods, sale and purchase of assets.	Accommodating transaction take place in the capital A/c e.g. (i) Foreign exchange reserves; (ii) Borrowings from IMF or foreign monetary authorities.

3. Reason for rise in demand for foreign currency when its price falls are:
- (i) When price of foreign currency falls, **imports** from that country become cheaper. For example, when price (exchange rate) of one US dollar falls, say, from 50 to 45, it means less rupees are required to buy one dollar worth of goods from the US. So, imports increase and hence demand for foreign currency rises.
 - (ii) Secondly, when foreign currency becomes cheaper in terms of domestic currency, it promotes **tourism** to that (foreign) country. Therefore, demand for that foreign currency rises.

OR

Reason for Fall in Demand

When price of foreign exchange rises, imports from that country become costly. As a result, imports fall leading to fall in demand for foreign currency,

Reason for increase in supply when rate of foreign exchange rises

- (i) A rise in foreign exchange rate makes home country's (say, India's) goods cheaper to foreigners. As a result, foreign demand for goods increase leading to increase in India's **exports**. This brings a greater supply of foreign exchange (currency).
 - (ii) Again, a rise in foreign exchange rate renders home country's currency cheaper which attracts foreigners and promotes **tourism** to home country (say, India). This also raises supply to foreign exchange.
4. (a) **Trade Surplus:** When the value of countries exports exceeds the value of its imports, the resulting positive balance is called as trade surplus.

Difference between trade surplus and current account surplus

Basis	Trade Surplus	Current Account surplus
Components	Trade surplus includes favourable balance of only visible items.	Current account surplus includes net favourable balance of visible and invisible items.
Scope	It is a narrow concept as it is only a part of current account.	It is a wider concept and it includes trade surplus.

- (b) "Indian rupee (₹) plunged to all time low of 74.48 against the US dollar".
- An increase in the value of US dollar indicates appreciation of US dollar and depreciation of Indian rupee.
- This indicates that India will have to pay more dollars to make its import payments. This will lead to decrease in India imports as it has become expensive for India to buy goods and services from US.
- India shall demand less of foreign exchange due to decreased imports.

