FOUNDATON EXAMINATION

(REVISED SYLLABUS - 2008)

Paper - 3 : ECONOMICS AND BUSINESS FUNDAMENTALS

Section - I

[Economics]

Q. 1. (a) Answers the following :

(i) Effective demand is

(A) Demand exceeds supply

(B) Aggregate demand is equal to aggregate supply

(c) Elasticity of demand for a product is high

(D) Difference between actual and forecast demand.

(ii) Progressive taxation means

(A) Tax burden decreases with income

(B) Tax burden increases with income

(C) Large quantity of tax evasion

(D) Large quantity of tax avoidance.

(iii) Cross elasticity of demand relates

(A) Price of one commodity and demand for another commodity

(B) Substitutes and complementary goods

(C) Market and supply

(D) Production and cost

(iv) Central Problem of all Economics are

(A) What to produce?

(B) How to Produce?

(C) For whom to produce?

(D) All the above

(v) Exceptions to the law of demand are

(A) Conspicuous goods

(B) Giffen goods

(C) Shares' speculative market

(D) All the above

(vi) Economics is —
- **(A) Normative science**
- **(B) Positive science**
- **(C) Human science**
- **(D) Political science**

(vii) Inductive Method proceeds from
- **(A) Praticular to General**
- **(B) General to particular**
- **(C) Imagination to reality**
- **(D) None of the above**

(viii) Constituents of money supply are
- **(A) Rupee notes and coins with the public**
- **(B) Credit cards**
- **(C) Traveller's cheques etc.**
- **(D) All the above**

(ix) The author of 'General Theory of Employment, Interest and Money' was
- **(A) Adam Smith**
- **(B) Paul Samuelsen**
- **(C) J. M. Keynes**
- **(D) Robbins**

(x) The law 'supply crates its own demand' was put forth by
- **(A) Marshall**
- **(B) Pigou**
- **(C) Robbins**
- **(D) J. B. Say**

(xi) Deductive method is also known as
- **(A) Hypothetical Method**
- **(B) Abstract Method**
- **(C) Periori Method**
- **(D) All of the above.**

(xii) An individual demand curve sloped downward to the right because
- **(A) Income effect of fall in price**
- **(B) Substitution effect of decrease in price**
- **(C) Diminishing marginal utility**
- **(D) All of the above**

(xiii) Normative secience deals with
- **(A) What ought to be**
- **(B) What is**
- **(C) Individual Consumption**
- **(D) All of the above**

(xiv) The concept of consumer's surplus was propounded by
- **(A) Malthus**
- **(B) Alfred Marshall**
- **(C) Robbins**
- **(D) Pigou**

(xv) Law of Demand Explains
- **(A) Qualitative relationship**
- **(B) Quantitative relationship**
- **(C) Functional relationship**
- **(D) None of the above**

(xvi) Utility is
- **(A) Cardinal**
- **(B) Ordinal**
- **(C) Neutral**
- **(D) Both (A) and (B)**

(xvii) Average cost is calculated as
- **(A) "TC/" output**
- **(B) TC output**
- **(C) AC/output**
- **(D) None of the above.**

(xviii) Exception to the law of supply is :
- **(A) Agricultural product**
- **(B) Scarce goods**
- **(C) Labour market**
- **(D) All of the above**

(xix) Homogeneous product is the characteristics of :
- **(A) Perfect competition**
- **(B) Monopoly market**
- **(C) Monopolistic competition**
- **(D) Oligopoly**

Q. 1. (b) Fill up the blanks :

- **(i) According to Malthus production of food grains increases at an arithmetical ________ .**
- **(ii) Per capital income figure woruld be inflated because of ________ .**
- **(iii) Theory of comparative cost was developed by ________ .**
- **(iv) Fisher's equation is MV = ________ .**
- **(v) The two primary functions of a commercial bank are the ________ and ________ .**
- **(vi) GNP is the ________ of all final goods and services produced by domestic sectors in the country in a year.**

(vii) A central bank has monopoly over ________ .

(viii) Law of variable proportions applies in the ________ .

(ix) Net National Product = Gross National Product Minus ________ .

(x) Per Capita Income = National Income / ________ .

(xi) Balance of payment is ________ than Balance of Trade.

(xii) Cash Balance Approach is based on the ________ of money.

Q. 1. (c) State which of the following statements is true and which is false.

(i) Balance of Payments is wider than Balance of Trade.

(ii) Giffen goods are otherwise known as superior goods.

(iii) Average Fixed cost can never be zero.

(iv) Theory of absolute trade was propounded by J. M. Keynes.

(v) Income tax is an indirect tax.

(vi) Industrial Development Bank of India is an investment bank.

(vii) A country is said to be under populated when optimum population is more than the actual population.

(viii) Quasi rent is earned from land only.

(ix) Average cost is equal to AFC + AVC.

(x) There is continuous rise in price level and the value of money decreases during inflation.

(xi) Central Bank creates credit

(xii) Unit Trust of India is an Investment Bank.

Q. 1. (d) Define the following terms in not more than thatn two lines :

(i) Consumer's surplus

(ii) Shut down point

(iii) Regressive tax

(iv) Fiscal Policy

(v) Human Capital

(vi) Proportional Tax

(vii) Bank Rate

(viii) Marginal Cost

(ix) Cash Reserve Ratio

(x) Repressed Inflation

Answer 1. (a)

(i) (B) — Aggregate demand is equal to aggregate supply

(ii) (B) — Tax burden increases with income

(iii) (a) — Price of one commodity and demand for another commodity

(iv) (D) — All the above

(v) (D) — All the above

(vi) (B) — Positive science

(vii) (A) — Particular to General
(viii) (D) — All of the above
(ix) (D) — J. M. Keynes
(x) (D) — J. B. Say
(xi) (A) — Hypothetical Method
(xii) (D) — All of the above.
(xiii) (A) — What ought to be
(xiv) (B) — Alfred Marshall
(xv) (B) — Quantitative relationship
(xvi) (D) — Both (A) and (B)
(xvii) (A) — "TC/" output
(xviii) (D) — All the above
(xix) (A) — Perfect competition

Answer 1. (b)

(i) Progression
(ii) Inflation
(iii) Ricardo
(iv) PT
(v) Deposit, Loan
(vi) Market Value
(vii) Issue of notes
(viii) Short-run
(ix) Depreciation
(x) Size of population
(xi) Wider
(xii) Store of value

Answer 1. (c)

(i) True
(ii) False
(iii) True
(iv) False
(v) False
(vi) True
(vii) True
(viii) False
(ix) True
(x) True
(xi) False
(xii) True

Answer 1. (d)

(i) **Consumer surplus :** Excess of a price which a person is willing to pay over that which what he actually pays is called consumer's surplus.

(ii) **Shut down point :** A stage when the AR = MR = AVC = MC at this point the firm would be covering only the average variable cost and no part of average fixed cost.

(iii) **Regressive tax :** When the rate of taxation decreases with the increase in income or asset value it is called regressive tax.

(iv) **Fiscal Policy :** That part of economic policy which deals with public revenue, public expenditure, public borrowing and financial administration to attain socio-economic objectives.,

(v) **Human Capital :** Human capital implies man as a means of production just as physical capital brings income to the owner. Investment is human capital earns money repeatedly.

(vi) **Proportional Tax :** A tax is said to be proportional when it is charged at a flat rate of all. For example, tax is imposed at 5% rate on all income groups.

(vii) **Bank Rate :** A Central Bank lends money or rediscounts the bills of commercial banks. The rate of interest charged by the Central Bank is called bank rate.

(viii) **Marginal Cost :** It is defined as the increment of total cost that comes from producing an increment of one unit of output. $MC = \frac{\Delta TC}{\Delta Q}$

(ix) **Cash Reserve Ratio :** Commercial banks are legally bound to keep a portion of their deposits in the form of cash reserve with the Central Banks. This is known as CRR.

(x) **Repressed inflation :** Repressed inflation is where excess demand is prevented from increasing price level through government action.

Q. 2. State the Law of Demand. Explain the exceptions to the law of demand.

Answer 2.

Law of Demand : The law of demand expresses the functional relationship between the price of commodity and its quantity demanded. It states that the demand for a commodity tends to vary inversely with its price– ie, Other things remaining constant, a fall in price of a commodity will lead to a rise in demand of that commodity and a rise in price will lead to fall in demand.

ASSUMPTION :

(1) Income of the people remaining unchanged.

(2) Taste, preference and habits of consumers unchanged.

(3) Prices of related goods i.e., substitute and complementary goods remaining unchanged.

(4) There is no expectation of future change in price of the commodity.

(5) The commodity in question is not consumed for its prestige value.

Exceptions to the law of demand :

(i) **Conspicuous Goods :** These are certain goods which are purchases to project the status and prestige of the consumer. For e.g. expensive cars, diamond jewellery, etc. such goods will be purchased at a higher price and less at a lower price.

(ii) **Giffen Goods :** These are special category of inferior goods whose demand increases even if with a rise in price. For eg. :- coarse grain, clothes, etc.

(iii) **Share's speculative Market :** It is found that people buy shares of those company whose price is rising on the anticipation that the price will rise further. On the other hand, they buy less shares in case the prices are falling as they expect a further fall in price of such shares. Here the law of demand fails to apply.

(iv) **Bandwagon effect :** Here the consumer demand of a commodity is affected by the taste and preference of the social class to which he belongs to. If playing golf is fashionable among corporate executive, then as the price of golf accessories rises. The business man may increase the demand for such goods to project his position in the society.

(v) **Veblen Effect :** Sometimes the consumer judge the quality of a product by its price. People may have the expression that a higher price means better quality and lower price means poor quality. So the demand goes up with the rise in price for eg. : Branded consumer goods.

Q. 3. Define Elasticity of Demand? Discuss its various determinants.

Answer 3.

It is defined as the degree of responsiveness of quantity demanded of a commodity due to change in its price other factor remaining constant. Price elasticity of Demand is usually measured by the following formula :

Price elasticity of demand = % Change in Quantity Demand / % Change in Price

ed = (dq/q) × 100 / (dp/p) × 100

= dq/dp × p/q

Where dq = change in qty. demanded

dp = change in price,

p = Original price,

q = Original quantity

Determinants of Elasticity of demand :

(i) **Nature of necessity of a commodity:** The demand for necessary commodity like rice, wheat, salt, etc is highly inelastic as their demand dose not rise or fall much with a change in price.
On the other demand for luxuries charges considerably with a change in price and than demand is relatively elastic.

(ii) **Availability of Substitutes:** The Demand for commodities having a large no. of close substi-tute is more elastic than the commodities having less or no substitutes. If a commodity has a large No. of substitutes its elasticity is high because when there is a rise in its prices, consumers easily switch over to other substitutes.

(iii) **Variety of uses:** The product which have a variety of uses like steel, rubber etc. have a elastic demands and if it has only limited uses; then it has inelastic demand. For e.g. If the unit price of electricity falls then electricity consumption will increase, more than propor-tionately as it can be put to use like washing, cooking, as the price will go up, people will use etc. it for important purposes only.

(iv) **Possibility of postponed of consumption:** The commodities whose consumption can easily be postponed has more elastic demand and the commodities whose consumption cannot be easily postponed has less elastic demand for eg, for expensive jewellery, perfume it is possible to postpone consumption in case the price is high and so such goods are elastic on the others hand, the necessities of life cannot be postponed and so they are inelastic in demand.

(v) **Durable commodities:** Durable goods like furnitures etc, which will last for a longer time have valuably inelastic demand. This is because in such case, a fall in price will not lead to a large increase in demand and a rise in price again will not load to a huge fall in demand. But in case of perishable goods, the demand is elastic is nature.

Q. 4. Write a short note on Fixed Cost & Variable Cost.

Answer 4.

In the short-run, a firm employs two types of factors : fixed factors and variable factors. Costs are also of two types : fixed costs and variable costs.

(i) **Fixed Costs** – Fixed costs (also known as supplementary costs or overhead costs) are the costs that do not vary with the output. These are the expenses incurred on the fixed factors of production.

Examples : Rent; interest; insurance premium; salaries of permanent employees, etc.

(ii) **Variable Costs** – Variable costs (or prime costs) are the costs that vary directly with the output. These are the expenses incurred on the variable factors of production.

Examples : Expenses on raw materials, power and fuel; wages of daily labourers, etc.

Distinctions between Fixed Costs and Variable Costs

Fixed Costs	Variable Costs
1. Fixed costs do not vary with quantity of output.	1. Variable costs vary with the quantity of output.
2. They are related with the fixed factors.	2. They are related with the variable factors.
3. They do not become zero. They remain same even when production is stopped.	3. They can become zero when production is stopped.
4. A firm can continue production costs are even at the loss of fixed costs.	4. Production is carried on when the variable met.

Q. 5. Distinguish between Return to a Variable Factor and Return to Scale.

Answer 5. (c)

The main differences between returns to a variable factor and returns to scale are as indicated below :

Returns to a Variable Factor	Returns to Scale
1. Operates in the short run or it is related to short-run production-function.	1. Operated in the long-run or it is related to long-run production-function.
2. Only the quantities of a variable factor are varied.	2. All factor-inputs are varied in the same proportion.
3. There is change in the factor proportion. Suppose on 1 acre land 1 labour is employed, then the land labour ratio is 1 : 1. Now if we add one more unit of labour on the 1 acre land, then land-labour ratio would become 1 : 2.	3. There is no change in factor-ratio. For instance, in a firm is employing 1 unit of labour and 2 units of capital, then the labour-capital ratio is 1 : 2. Now if the firm increases is scale of operation and employed 2 units of labour and 4 units of capital, the labour-capital ratio still remains the same as 1 : 2.
4. No change in the scale of production. Because here all the factor-inputs are not changed.	4. There is change in the scale of production because here all the factor-inputs are varied in the same proportion.

Q. 6. Explain features of Monopoly.

Answer 6.

Features of Monopoly :

Monopoly refers to the market situation where there is one seller and there is no close substitute to the commodities sold by the seller. The seller has full control over the supply of that commodity. Since there is only one seller, so a monopoly firm and an industry are the same.

Feature :

(i) **Single seller and large number of buyers :** Under monopoly there is one seller and therefore a firm faces no competition from other firms. Though there are large numbers of buyers, no single buyer can influence the monopoly price by his action.

(ii) **No close substitute :** Under monopoly there is no close substitute for the product sold by the monopolist. According to Prof. Boulding – a pure monopolist is therefore a firm producing a product which has no substitute among the products of any other firms.

(iii) **Restriction on the entry of new firms :** Under monopoly new firms cannot enter the industry.

(iv) **Price maker :** A monopoly firm has full control over the supply of its products and hence it has full control over its price also. A monopoly firm can influence the market price by varying it supply, for eg., It can make the price of its product by supplying less of it.

(v) **Possibility of Price Discrimination :** Price discrimination is defined as that market situation where a single seller sell the same commodity at two different prices in two different markets at the same time, depending upon the elasticity of demand on the two goods in their respective market. Under such circumstances a monopolist can charge incur supernormal loss then firms would leave the industry, thus reducing the supply. As a result, price will again rise and the loss will wiped out.

Q. 7. Critically examine Ricardo's theory of comparative cost.

Answer 7.

Ricardo's Theory of Comparative Advantage or Comparative Cost

It is obvious that if one country has an absolute advantage over the other country in one line of production and the other country has an absolute advantage over the first country in a second line of production, both countries can gain by trading. But what if one country is more productive than another country in all lines of production? If country A can produce all goods with less labour cost than country B, does it still benefit the countries to trade? Ricardo's answer was yes. For this, Ricardo gave the theory of comparative advantage (or the theory of comparative cost) of international trade. According to him, comparative advantage explains the existence of international trade. A detailed explanation of the theory of comparative advantage is given below :

Assumptions

Ricardo's theory of comparative advantage is based on the following assumptions :

(i) It is assumed that there are only two countries in the world, and each country can produce two goods. Thus, this theory is carried out only in two country-two commodity model.

(ii) There is perfect competition both in the commodity market and the factor market.

(iii) There is only one factor of production and that is labour. It implies that the cost is expressed in terms of labour only and the value of the commodity depends only on its labour cost.

(iv) Factors of production are assumed to be perfectly mobile within the country but perfectly immobile between different countries.

(v) The law of constant returns to scale prevails in the economy.

(vi) There are no transport costs between the two countries.

Criticisms of Ricardian Theory of Comparative cost

The theory of comparative cost has been attacked on many fronts by many economists from time to time. Some of the important criticism are given below :

(i) Wrong assumption of labour cost.

(ii) Unrealistic model of two countries two commodities.

(iii) Unrealistic assumption of the law of constant cost.

(iv) Unrealistic assumption of full employment.

(v) Wrong imagination regarding factor mobility.

(vi) Transport costs ignored.

(vii) One sided theory of international trade.

(viii) Unrealistic.

(ix) The theory is static in nature.

(x) Not applicable in underdeveloped economies.

Despite these limitations the theory has a stand. It has narrated the truth that comparative advantage is definitely as advantage which should be gainfully exploited in international trade.

Q. 8. Distinguish between GNP and GDP.

Answer 8.

Gross National Product (GNP) - The GNP of a country in a year is defined as the market value of all final goods and services produced by domestic factors in the country in that year.

Gross Domestic Product (GDP) - GDP can be defined as the sum total of values of all goods and services produced within the geographical boundary of the country without adding the factor income received from abroad.

Distinction between Gross National Product and Gross Domestic Product –

Gross National Product is different from Gross Domestic Product in following respects :

(a) Gross National Product refers to the total market value of all the final goods and services produced in a country during a given year, plus net factor income from abroad.

But Gross Domestic Product refers to the total market value of all the goods and services produced in the given year within the domestic territory of the country.

(b) Gross National Product includes all income earned by the country in abroad. But Gross Domestic Product does not include the income earned by the country from abroad.

(c) Gross Domestic Product does not include the income earned by the country from foreign investments.

(d) G.D.P. includes only those goods and services which can be produced within domestic territory of the country.

(e) G.N.P. is a wider concept than the G.D.P.

But G.N.P. is more useful than G.D.P.

Q.9. What do you understand by the term 'national income'? Discuss different methods of measuring it.

Answer 9. (b)

National Income is nothing but the income of a nation or a country. In real terms a national income is the flow of goods and services produced in an economy in aparticular period — a year. A National Sample survey has, therefore, defined national income as — money measures of the net aggregates of all commodities and services accruing to the inhabitants of a community during a specified period.

There are three alternative ways of estimating National Income of a country. Broadly it may be viewed from income side, output side and expenditure side. Let us discuss these methods :

(a) **Product method** - In simple terms this method implies that by adding the values of output produced and services rendered by different sectors one may find out the national income.

The output method is unscientific. In this method only those goods and services are counted which are paid for, that is marketed. But there are many goods and services that do not have market price and are not paid for. Services of a housewife or a teacher-father; food crop, fruits and vegetable grown in family farm would not be counted as part of the GNP. Similar services or goods would become a part of GNP if they are paid for. Thus GNP at market price invariably leads to an underestimate of gross and services.

Moreover, there lies possibility of double or even triple counting in this method. Counting wheat, flour and bread's value separately is methodologically incorrect because bread's value contains flour's value which, in turn, contains wheat's value. However, this problem can be overcome if only value of final goods are considered excluding primary and intermediate goods. The problem can be overcome in another way known as the value added method whereby only the value added by each firm in the production process is included in the output figure. Thus the value added output of all sectors makes up GNP at factor cost.

(b) **Income method** - In this method all income from employment and ownership of assets before taxation received from productive activities to be counted. It is the factor income method. The summation of incomes earned by the factors of production for their contribution to production. To these be added the undistributed profits of the private sector and trading surplus of the public sector corporations. While all those groups of income generated in production, some other are to be excluded. These are known as Transfer Earnings. Examples of such earnings are pensioner benefits, un employment doles, sickness benefits, interest on national debt etc. These are excluded, as they do not arise from productive activities.

(c) **Expenditure Method** - By measuring total domestic expenditure we can measure the income of a nation. Broadly, total domestic expenditure comprises two elements. First, consumption expenditure of the household sector on goods and services. It also includes the consumption outlays of business sector and public authorities.

Another part of national expenditure is investment expenditure by private sector and public authorities. Expenditure is said to be investment when it is used for making a fixed capital like building, machinery etc. It also means an increase in the stock of inputs and finished products.

In measuring total domestic expenditure we have to take some precautions (a) only new goods be considered. Any spending on old goods is a transfer of asset from one hand to another. There is no new asset coming through production (b) Only the final stage of purchase be included because measuring expenditure for intermediate stage may lead to duplication of spending amounts. (c) Residents of country may spend for foreign goods (import) any may also earn by selling goods abroad (exports). Hence it is necessary to exclude spending on imports and to include value of exports.

Q. 10. Discuss Deductive AND Inductive METHODS OF ECONOMIC ANALYSIS.

Answer 10.

In Economics the issues are analysed either by inductive method or by deductive method. The deductive method tries to draw conclusions from certain fundamental assumptions or truths.

The logic proceeds from general to the particular. For example, we can deduce from the basic truth that a man will buy more at lower prices. The Law of Demand and the Law of diminishing Marginal Utility have been derived from deductive reasoning.

The inductive method, on the other hand, deduce conclusions on the basis of collection and analysis of facts and figures. The Logic proceeds from particular to general. It leads to exact and precise conclusions for policy making.

The Deductive method was used by earlier economists. It is a simple method, obviates the need of experimentation and collection of statistical data. But deductive conclusions are based upon assumptions that may turn out to be untrue or partially true. Hence it is unsuitable for policy making as it is dangerous to claim universal validity for economic generalizations.

Q. 11. Define Central Bank. Distinguish between Central Bank and Commercial Bank.

Answer 11.

Central Bank may be defined as an institution charged with the responsibility of managing the expansion and contraction of the volume of money supply for general Economic Welfare. The Central Bank is the apex institution in the banking and financial structure of the country.

The Central Bank differs from the commercial banks in several respects mentioned as under :-

(a) The Central Bank acts as the supreme monetary authority of the country with wide powers control credit and currency of the country. But a commercial bank has no such powers.

(b) The Central Bank does not exist to make profits for its owners. But commercial banks are organized for profits for their owners.

(c) The Central Bank is the ultimate source of money supply. But a commercial bank is not so.

(d) The Central Bank acts as the banker to the government, but other banks do not act as a rule in this capacity. They are bankers to private industries and institutions.

(e) A Commercial bank undertakes risky business activities and many fail. But the Central Bank never fails.

(f) The Central Bank does neither accept deposits nor lend to the public, but this is the most important functions of commercial banks.

(g) The Central Bank is subordinate to the state and as such most of the Central Banks in the world are now state owned and state managed. But commercial bank in most of the countries are privately owned and privately managed; there is however a growing trend towards the nationalization of even commercial banks in many countries as in India.

(h) The Central Bank issues paper notes in fact it enjoys the monopoly power in this matter. But other banks do not enjoy this power. They create credit.

(i) The basis of credit money is cash deposit while what of cash money is gold and foreign reserve.

Q. 12. What is EXIM Bank? What are its functions?

Answer 12.

The Export Import bank of India commenced operations on March 1, 1982. It is a non-bank financial intermediary confined its area of operations to foreign trade of India. It is a fully statutory company owned by the Government of India with an authorized capital of ₹ 200 crores and paid-up capital of ₹ 50 crores. It is empowered to borrow from RBI and also from foreign economies. It is a lead bank in the finance and promotion of exports and also an apex body for co-ordinating the working of similar organization engaged in promoting our export and import trade.

Functions and Activities :

The EXIM Bank's business is exclusively devoted to India's international activity. The aggregate loans and outstanding reached ₹ 16.16 billion during the first decade of its operation. In annual terms, the business is said to have grown at a rate of 30 per cents.

The Bank has developed "a three dimensional strategy" for export promotion. Firs, the Bank offers fund for product development, long-term export credit, investment capital.

Second gives export advisory services. Research on exports and market opportunities is a third component in the strategy.

Export bids have increased annually by 44 per cent and export contracts financed exceed ₹ 60 billion. Penetration into new markets has been possible because of a variety of lending program of the Bank, it rendered services in product export, project export and services export.

When the Bank commenced operation in early 1982 its catalytic role was mainly confined to granting of post shipment term export credit. Now its horizons have expanded. Now its horizons have expanded. Now it lends product development finance, pre shipment finance, marketing finance, finance for joint ventures, investment capital for export production in addition to term export credit. The Bank is thus involved in more than export finance. In other program include –

(a) Export Bills Re-discounting

(b) Refinance of Suppliers credit

(c) Bulk Import finance

(d) Foreign currency Pre shipment credit

(e) Product equipment finance program

(f) Business Advisory and technical Assistance (BATA).

Q. 13. What are the objectives and functions of IMF?

Answer 13.

The objective for which the IMF was set up and act are as follows : -

(a) To foster international monetary cooperation through joint action of its members.

(b) To promote foreign trade by avoiding restrictive currency practices.

(c) To secure stability of foreign exchange rate.

(d) To recur multilateral convertibility i.e., a borrower nation can borrow the currency of any other member nation.

The Principal functions of the IMF are :

(a) It provides short term credit.

(b) It functions as a leading institution in foreign exchange.

(c) It grants loans for current transactions and not capital transaction.

(d) It helps for the orderly adjustment of exchange rates.

(e) It acts as a store house of foreign exchange rates which is likely to improve the balance of payment position of member countries.

Q. 14. Explain the major canons of taxation.

Answer 14.

Tax is a delicate instrument in the hands of the government. Just as a drug deadly when taken in large doses may have a reviving effect on the body to which it is administered with caution, so also taxation. How can tax be properly administered? Economists have suggested certain principles which the government can follow for ideal tax administration.

Adam Smith long ago propounded four such principles, which he called 'canons' as guiding stars of tax authorities.

(a) **Cannon of Ability** – Smith was of the view that subjects of a state ought to contribute "in proportion to their respective abilities i.e., in proportion to the revenues they respectively enjoy." A proportional tax, as Smith advocated, implies equality of sacrifice.

(b) **Cannon of Certainty** – This cannon lays down that taxes "be certain and not arbitrary." Prior intimation as regards the amount and time of payment was thought necessary for reducing trouble and difficulties of tax payers.

(c) **Cannon of Convenience** – According to Smith taxes be collected according to the convenience of the payers. It should be levied "at the time or in the manner in which it is most likely to be convenient."

(d) **Cannon of Economy** – Smith suggested that tax system be so framed "as both to take out and to keep out of the pockets of the people as little as possible over and above what it brings into the pubic treasure". This implies least cost collection. Even with taking as little as possible from tax payers, tax revenue can be large if small amount is used up for their collection.

Q. 15. Discuss the salient features of International Trade.

Answer 15.

1. The world market is heterogeneous on account of differences in climate, language, level of national income etc.
2. The mobility of factors of production is higher within the country than that between countries. International mobility of labour and capital is strictly restricted by governments. When resources are comparatively immobile, there is no automatic influence equalizing price and cost.
3. It involves the use of different types of currencies. Hence arises the question of foreign rate of exchange.
4. Foreign trade may be free or not. It is free when a country can buy and sell any good or service from world market without any obstruction. In most countries much free flow in and flow out is restricted by the government, looking after the broader national interest.
5. International trade has its impact on a country's gross national product and national income while domestic trade leads to transfer of goods from one region to another and no change in the size of GDP.

Q. 16. Write short notes on the following :

(i) Deficit Financing

(ii) Factors affecting supply

Answer 16.

(i) **Deficit Financing :**

When government spending exceeds its earnings, the budget is said to be deficit and to bridge the gap, if government borrows money from the Central Bank or runs down its accumulated reserves, it leads to a net addition to money supply. It is called deficit financing. It is used as an instrument to remedy depression and unemployment. Deficit financing denotes more spending by the government through created money.

Lord Keynes advocated deficit financing for lifting up of an economy from business depression and unemployment. According to him demand deficiency was the root cause of these problems. Hence the prescription to raise private expenditure comprising consumption and investment. The total expenditure of private sector cannot increase on its own in a depressionary economy. It needs external push. This is what the government should do through a policy of budgetary deficit financed by new money. Creation of new money and its injection into the economy can raise C+I+G curve upward to a level where unused and unemployed resources may be gainfully employed. Once the resources are fully employed more spending by the government will lead to inflationary rise in price.

(ii) **Factors affecting supply :**

Supply is defined as a quantity of a commodity offered by the producers to be supplied at a particular price and at a certain time.

The factors affecting the supply of a commodity are:

(*a*) The price of the commodity in the market. When price rises, there will be more profit and supply increases. The reverse will happen when price falls.

(*b*) Goals of the firm, such as profit maximization, sales maximization and employment maximization.

(*c*) The supply of a commodity is influenced by the prices of raw materials, labour and other inputs.

(*d*) State of technology used for production of a commodity. Improved and advanced technology reduces the cost of production and increases the supply.

(*e*) The government policy with reference to production of commodities, imposition of taxes, such as excise duty, sales tax, subsidy policy etc. influence the supply of a commodity.

(*f*) Expectation about future prices of the commodity.

(*g*) Prices of other commodities, e.g., the supply of one commodity falls as the prices of other goods rise.

(*h*) Number of firms in the market. Decrease in the number of firms reduces the supply.

(*i*) In case of natural disorders like flood, drought, etc. reduce the supply of a commodity specially agricultural produces.

Q. 17. Write notes on the following :

(i) Special drawing rights (SDR)

(ii) Explicit costs

Answer 17.

(i) **Special Drawing Rights (SDR) :**

About two decades ago a new international money was created by the IMF for two reasons. First to overcome the shortage of gold in the world economy leading to fall in international reserves. Second, to avoid the movement of gold across national boundaries. This new international currency is known as Special Drawing Rights (SDR) held with the IMF. The origin of SDR thus lies in the shortage of international liquidity all over the world in the wake of acute shortage of American Dollar in the 60s and early 70s which was then the main reserve currency.

The SDR was first introduced in 1969. Under this scheme the IMF grants its member government special drawing rights from Special Drawing Account (SDA). They are like coupons which can be exchanged for currencies required by its holder for making international payments. They are also, besides gold and key currencies, a component of international reserve of an economy.

Each member of the fund was assigned an SDR quota that was granted in terms of a fixed value of gold. Hence they have been aptly described as "Paper Gold". The member countries are required to provide their currency in exchange for SDR when called upon. The use of SDR would mean a reduction in the country's foreign reserve and a corresponding increase in the SDR holding of the country receiving it.

The mechanism of the SDR system is an economy in need of foreign exchange has to apply to the Fund for the use of SDR. The Fund would designate another country having a sound foreign exchange resources to meet the need of the former. So the debtor country's SDR decreases and that of the creditor increases. The former have to pay interest at 1.5% per annum to the latter country. A designated (creditor) country can not pay more than the amount equal to twice the amount of SDRs allotted to the country. The scheme is flexible in that each country can use its quota to have an equivalent amount of convertible foreign exchange to overcome balance of payment difficulties.

(ii) **Explicit costs :**

Actual payments made by a firm for purchasing or hiring resources (or factor-services) from the factor-owners or other firms are called explicit costs. In other words, explicit costs are actual money expenses directly incurred for purchasing the resources. These are the costs which a cost accountant includes under the head expenses of the firm. Hence explicit costs also. Accounting costs include all costs incurred by the firm in acquiring various inputs from outside suppliers. Thus the examples of explicit costs are: payments for raw materials and power; wages to the hired workers; rent for the factory-building; interest on borrowed money; expenses on transport and publicity, etc.

Q. 18. Discuss the functions of Central Bank.

Answer 18.

Central Bank plays a leading role in organizing, running, supervising, regulating and developing the banking and financial structure of the country.

1. **Monopoly of Note Issue :**

   The Central Bank enjoys the exclusive power of note issue. In India the RBI issues all notes except Re 1 notes and coins. Re 1 notes are issued by the Government of India under the guidance of RBI. The currency notes issued by the Central Bank are declared unlimited legal tender throughout the country. The Central Bank has to keep reserve of Gold, Silver and foreign securities for issuing notes.

2. **Banker, agent, advisor to the Government :**

   The Banking A/c of the government both central and state are maintained by the Central Bank as the commercial bank does for its customers. As a banker and to the government it helps the government in short term loans and advances for temporary requirements and floats public loans for the government.

   As an advisor to the government the Central Bank advices on monetary and Economic matters. It also advices on the ground as to how to maintain the internal and external value of money.

3. **Banker's Bank :**

   All commercial banks keep part of their cash balances as deposits with the Central Bank of the country. This is either because of convention or legal compulsion. The commercial banks regularly draw currency during the busy season and paying in surplus during the slack season. Part of these balances are meant for clearing purposes i.e.; all commercial banks keep deposit account with the Central Bank. The deposit balances of the Central Bank is considered as cash reserves for general purpose.

   Under the Banking Regulations Act of 1949, the Central Bank of India have been empowered with the right to supervise and control the activities of various scheduled commercial banks. These powers are related to licensing, branch expansion, liquidity of assets and methods of working of the Bank.

4. **Clearing House Facility :**

   By virtue of its unique position in dealing with domestic and foreign funds the Central Bank has a special position for conducting

   (a) clearing house Operation;

   (b) Inter bank Transfer of funds;

   (c) Settlement of accounts.

   Clearing house facility means providing an opportunity to member commercial banks to settle their claims on each other mutually. E.g. : Indian Bank has to pay to SBI a sum of 2 lakh and SBI has to pay to Indian bank ₹ 1,50,000. This can be settled with a check of ₹ 50,000 by Indian Bank on the RBI in favour of SBI. As a result Indian Banks accounts will be debited and SBI's account will be credited.

5. **Custodian of Foreign Exchange Reserves :**

   Under this system the RBI controls both receipts and payments of foreign exchange. A country have in its foreign trade favourable or unfavourable balance. Favourable balance helps to bring foreign exchange to the country while unfavourable balance means paying foreign exchange out. As custodian of Foreign Exchange Central Bank keeps a constant watch on the same so that the value of the home currency does not rise or fall adversely in relation to foreign currency.

   During times of emergency the Central Bank may impose restrictions to control on buying or selling of foreign currencies in the market.

6. **Credit Control :**

   In order to ensure price stability and Economic growth of a country, the Central Bank undertakes the responsibility of controlling credit. The Central Bank ensures price stability and avoids inflationary and deflationary tendencies by several monetary methods such as regulation of Bank rate, open market operation, change in variable reserve ratio, etc.

Q. 19. What are the functions of money?

Answer 19.

Functions of money :

Money is a matter of four functions, viz.,

(*a*) ***Medium of exchange*** **:** Money everywhere acts as a common medium of exchange. In an exchange economy, money has an intermediary role. The origin of money lies in the inconveniences of the barter system. The invention of money has made the exchange· system smooth and convenient.

(*b*) ***Measure of value* :** Money measures exchange value of goods and services. Things are said to be cheap or expensive on the basis of amount of money for their possession. This makes exchange mutually profitable.

(*c*) ***Standard of deferred payment* :** Money as a standard of deferred payment implies the role of money in borrowing and lending. Money taken as loan is usually repaid after a time gap. This delayed payment is done through money.

(*d*) ***Store of value* :** Money gives a man command over goods and services because of its purchasing power. This purchasing power of money can be stored by keeping a part for future use. Not being perishable, value of money can be preserved for a long time.

Money plays a dynamic role in a modern economy. It lubricates the wheels of trade and commerce. Money is the lifeblood of industry. Money activates idle resources and puts them into productive channels. It helps in increasing output, employment, income and converting savings into investment.

Q. 20. Discuss merits and demerits of direct taxes.

Answer 20.

Merits of Direct Taxes – The following are the merits of direct taxes.

(i) Progressive in character as the rate of tax increases with the increase in income or value of property.

(ii) They help in the redistribution of income and wealth.

(iii) They are economical and easy to collect.

(iv) They are paid consciously.

(v) They contribute more to the Public authorities.

Demerits of Direct Taxes – The following are the demerits of direct taxes.

(i) They adversely affect the work, income and savings of tax payees.

(ii) They generate black money and wealth as they cannot be shifted.

(iii) They fall more on salaried class.

Section - II

[Business Fundamentals]

Q. 21. (a) Answer the following :

(i) A bull is —
(A) A speculator who expects price to fall
(B) A speculator who expects price to rise
(C) A speculator who invests in mutual fund
(D) A speculator who invests in government bonds.

(ii) One share one vote is applicable to
(A) Joint stock company
(B) Co-operative society
(C) Partnership firm
(D) Joint Hindu family

(iii) Liability clause is contained in
(A) Articles of Association
(B) Prospectus
(C) Memorandum of Association
(D) Special Resolution

(iv) The SWOT analysis stands for
(A) Strength, Weaknesses, Opportunities, Threats
(B) Science, Wisdom, Opportunities, Triumph
(C) Success, Wisdom, Opportunities, truth
(D) Simple, Weakness, Opportunities, Threats

(v) Various objectives of business are
(A) Economic objectives
(B) Social objectives
(C) Human objectives
(D) All of the above

(vi) OTCEI is —
(A) An export organization
(B) Funding agency for industries
(C) A public facility go get schedules drugs
(D) Assisting small and medium firms to get access to share market nationwide.

(vii) Characteristics of the sole proprietorship are :
(A) Capital contribution
(B) Unlimited liabilities
(C) Limited area of operation
(D) All the above

(viii) Proxy has the following connotations :

(A) One

(B) Two

(C) Three

(D) Four

(ix) Semantic barrier to communication is referred as the —

(A) Receiver misinterpreting the symbols used by the sender

(B) Sender misusing the symbols

(C) Receiver clarifying the symbols with sender

(D) Receiver not being able to decode the symbols used by the sender

(x) Mention which of the following are not counted in a private limited company to make the maximum strength of members to 50 :

(A) Present employees and shareholders

(B) Past employees and present shareholders

(C) None of the above

(D) A and B both

Answer 21. (a)

(i) (B) — A speculator who expects price to rise

(ii) (A) — Joint stock company

(iii) (C) — Memorandum of Association

(iv) (A) — Strength, Weaknesses, Opportunities, Threats

(v) (D) — All of the above

(vi) (D) — Assisting small and medium firms to get access to share market nationwide.

(vii) (D) — All the above

(viii) (B) — Two

(ix) (A) — Receiver misinterpreting the symbols used by the sender

(x) (C) — None of the above

Q. 21. (b) Fill in the blanks :

(i) A person who just lends his name and reputation for the benefit of the without taking active part is called ____________ .

(ii) Perpetual existence is a feature of ____________ organization.

(iii) Government policies are an important part of ____________ environment of a company.

(iv) A written communication provides ____________ record for future reference.

(v) Memorandum of Association is one of the basic ____________ of the company.

(vi) The prescribed minimum number of qualified persons authorised to transact the business at meeting is called ____________ .

(vii) ____________ involves sending written message through telecommunication links.

Answer 21. (b)

(i) Sleeping partner
(ii) Joint Stock Company type.
(iii) Political
(iv) Permanent
(v) Document
(vi) Quorum
(vii) E-mail

Q. 21. (c) State which of the following statements is "True" and which is "False". :

(i) Misstatements in prospectus leads to cancellation of listing.
(ii) Where B Ltd. and C Ltd. are subsidiaries of A Ltd., B Ltd. holds 30% shares in D Ltd. an C Ltd. holds 25% shares in D Ltd. Thus, D Ltd. is a subsidiary of A Ltd.
(iii) A sale warrant holder is not treated as the member of that company.
(iv) A sale is not made at the counter or by a salesman. It is made in the mind of seller.
(v) Private company limits its members to fifty.
(vi) Decoding refers to delivery of communication.
(vii) Stock Exchange facilities regular valuation of securities
(viii) For communication to be effective it must be receiver oriented.

Answer 21. (c)

(i) False
(ii) True
(iii) True
(iv) False
(v) True
(vi) False
(vii) True
(viii) True

Q. 21. (d) Define the following terms in not more than two lines :

(i) Unlimited liability
(ii) Special resolution
(iii) Called up capital
(iv) Partner by estoppel
(v) Statement of lieu of prospectus
(vi) Forward delivery contract

Answer 21. (d)

(i) **Unlimited liability :** Unlimited liability implies that the liability of partners extends beyond their organizational property and include personal property.

(ii) **Special resolution :** Special resolution is a type of resolution which is passed in a meeting as spelt out by the Companies Act. Special resolution is passed by a majority of at least 75% of votes of members present in person or by proxy and notice of meeting should mention it as special and should be given at least 21 dayss before the date of meeting.

(iii) **Called up capital :** Called up capital is that part of the capital which is called up by the company at the time of requirement.

(iv) **Partner by estoppel :** A partner by estoppels is a person who has neither contributed any Capital nor takes any part in the management of the firm. If a person styles the character of a partner in a business before third party by his words or acts, he is stopped from denying this fact who believes in him and acts accordingly.

(v) **Statement in lieu of a prospectus :** If a public company does not issue a prospectus, it can Issue a statement in lieu of prospectus. It contains almost the same information as is contained in the prospectus.

(iv) **Forward Delivery contracts :** These dealings are for account and settlement takes place at the end of every fortnight through clearing house only and such transaction can have carry over facilities also. The speculators are the main parties in these dealing.

Q. 22. Discuss the various objectives of a business.

Answer 22.

The various objectives of business could be classified as follows :

(1) Economic objectives
(2) Social objectives
(3) Human objectives
(4) National objectives
(5) Organic objectives

The Economic objectives are :

(a) Earning of adequate profit
(b) Production of tangible form of wealth
(c) Creation of market or creation of customers
(d) Innovation
(e) Best use of available scarce resources.

The Social objectives are :

(a) Providing quality goods and services
(b) Charging reasonable prices
(c) Generation of employment
(d) Avoiding antisocial practices and profiteering
(e) Creating and maintaining better environment.

The Human objectives are :

(a) Giving a fair deal to the employees
(b) Ensuring job satisfaction
(c) Treating employees as partners to prosperity
(d) Development of human resources

The National objectives are :

(a) Producing goods and providing services as per national priorities

(b) Development of small enterprises

(c) Guaranteeing social justice

(d) Export promotion

The Organic objectives are :

(a) Survival

(b) Growth, expansion and diversification

(c) Creating goodwill, prestige and recognition.

Q. 23. Discuss the functions of Stock Exchange and explain the method of trading in Stock Exchange.

Answer 23.

Functions of Stock Exchanges

Stock exchanges play an important role in capitalistic countries. It is indispensable for the proper functioning of joint stock companies. The importance of a stock exchange will be clear from the study of its functions and services.

A stock exchange performs the following economic functions :

(i) Provides ready and continuous market.

(ii) Facilitates regular valuation of securities.

(iii) Encourages capital formation.

(iv) Provides proper direction to invest capital.

(v) Ensures wide ownership of securities.

(vi) Facilitates distribution of new securities.

(vii) Ensures safety of funds.

(viii) Regulates company management and performance.

(ix) Disseminates information.

(x) Facilitates speculation.

(xi) Mirror of business cycle.

Method of Trading :

The way in which the securities are transacted in a stock exchange is much different from trading in ordinary goods. A person who wants to purchase or sell securities cannot do it himself. He is not allowed to enter into the hall of the stock exchange and thus he cannot carry on transaction personally. He has to depend upon the brokers.

There are two types of trading on the stock exchange viz.

1. Ready delivery contacts, and
2. Forward delivery contracts.

Trading Procedure :

Following are various steps involved in completing a transaction through stock exchange brokers :

1. Choice of a broker
2. Placing the order
   (i) Fixed Price order
   (ii) Limit price order
   (iii) Bargain price order

3. Executing the order
4. Settlement of Transactions

Q. 24. Write a short note on Characteristics of a Prospectus.

Answer 24.

The important characteristics of a prospectus.

(i) It is a document described or issued as a prospectus.

(ii) It includes any notice, circular, advertisement, etc., inviting deposits from the public.

(iii) It is an invitation to the public to subscribe to the shares or debentures of the company.

(iv) It is a document through which the company secures the capital required for carrying on its business.

Q. 25. Explain the features of a public company.

Answer 25.

Features of a public company :

(i) It requires a minimum of seven persons to form a public company. There is no restriction on the maximum number of members.

(ii) It can offer shares to the general public in order to raise huge financial resources.

(iii) Shares of a public company are freely transferable like movable property.

(iv) Shareholders have no control over the management of the company.

(v) A public company can choose any name, but it must add the word 'Limited' at the end of its name.

(vi) It cannot commence its operations until it obtains a 'Certificate to Commence Business' in addition to the 'Incorporation Certificate' from the Registrar of Companies.

Q. 26. Explain the role of four animals in stock exchange.

Answer 26.

There are different types of speculators dealing in a stock exchange. There are named after some animals, as they behave like wild animals. Their classification depends upon the nature of their activities in the stock exchange and in general, they are of four types, viz. bulls, bears, lame ducks and stags.

Bull : A bull is speculator who expects a rise in the price of shares of a company. He is an optimist. He aims at making profit out of an expected rise in the price of a particular share. For this purpose he purchases the security for future deliv ery. Generally, he has no intention of taking delivery on the fixed date or settlement day. He may sell before the settlement day He may receive or pay the difference between the purchase price and sale price either on or before the settlement day.

A bear is a speculator who expects a fall in the price of a security. He is a pessimistand he forecasts a fall in price. He aim at making profit out of an expected fall in the price of a particular share. For this purpose he sells the security for future delivery. He may or may not posses the security. Generally, he has no intention of giving delivery on fixed date or the settlement day. He may purchase before the settlement day or settle the transaction on the settlement day.

Lame Duck : In case the bear is unable to strike the bargain immediately, he is said to "be struggling like a lame duck". This may happen on account of the fact that the security which has been agreed to be sold may not be available in the market and in that case the commitment cannot be fulfilled. If the other party agrees to postpone the deal, there would be no trouble but if he does not agree to postpone such a situation would arise.

Stag : Sometimes the shares to be issued by new company may be unofficially quoted at a premium. This happens when the prospectus of the new company. Are expected to be excellent. Some persons may apply for more shares than actually needed. Their object is to sell the shares at a high one as soon as they are allotted by the new company and thus make quick profit. So stag is a person who applies for shares of a new company with a view to selling the shares allotted to him at a profit.

Stags may suffer loss. This happens when the public applies for less number of shares than offered for. Then the stags will be allotted at the number of shares applied for and the shares may be quoted at a discount in the market. Under such circumstances stags will incur a loss, if they sell the allotted shares. The operations of stag create artificial scarcity of shares of the new company would rise. Suppose he purchases 1,000 shares of 'X' company for future delivery at the present market price of ₹ 150 and suppose the price rises to ₹ 160 on or before the settlement day, he will sell at that price. Thus he makes a profit of ₹ 10,000 out of the rise in the price of the security. It should be noted that if his expectation goes wrong. He will incur a loss.

Q. 27. What is a special resolution? For what purposes are such resolution necessary?

Answer 27.

A resolution shall be a special resolution when the votes cast in favour of the resolution by members present in person or, where proxies are allowed, by proxy, are not less than three times the number of votes, if any, cast against the resolution and the has been duly specified in the notice calling the meeting [Sec 189(2)]. In other words, this is a resolution passed by a majority of at least 75 per cent of votes of members present in person or by proxy and a mention of the fact that the resolution shall be passed as a special resolution must have already been made in the notice of the meeting and the notice should have been duly given at least 21 days before the date of the meeting.

The articles of the company may specify purposes for which a special resolution is required.

The Companies Act has also specified certain matters, for which a special resolution must be passed, for example –

(i) to alter the memorandum of the company (Sec. 17),

(ii) to alter the articles of the company (Sec. 31),

(iii) to issue further shares with preemptive rights (Sec. 81), for creation of Reserve Capital (Sec. 99),

(iv) to reduce the share capital (Sec. 100),

(v) to pay interest out of capital to members (Sec. 208),

(vi) authorizing a director to hold an office or place of profit (Sec. 314),

(vii) voluntary winding up of a company (Sec. 484), 'A copy of special resolution must be filed with the Registrar within 30 days of the date of its passing.

Q. 28. What is communication? Explain encoding, decoding and feedback as the elements in the process of communication.

Answer 28.

Communication is a process by which send information and feelings to recipients through one or more channels. It is an change of ideas, facts, opinions, information and understanding between two or more persons. It may also be regarded as the process of meaningfully transferring information from one person to another.

Encoding : This refers to preparing the subject-matter of communication in a suit able language. The purpose of encoding is to translate the thought of the sender into a language or code that can be easily understandable to the receiver of the message.

Decoding : This refers to the conversion of the message by receiver into meaning terms so as to make communication understandable. The effectiveness of commu nication depends on how much the receiver's decoding matches with the sender's message.

Feedback : This refers to the actual response of the receiver to the message communicated to him. It is a reversal of the communication process, in which the receiver expresses his reactions to the sender of the message.

Q. 29. What are the salient features of a good business letter.

Answer 29.

Characteristics of a good business letter :

Business people have to communicate with their customers, suppliers, debtors, creditors, public authorities and the public at large for the purpose of exchanging their views and for sending and receiving information. Written communication is called correspondence. Commercial correspondence means correspondence by business people on matters of commerce.

Following are the characteristics of a good business letter :

(1) Clarity : The language shall be clear so that the ideas are properly expressed and the reader can understand them in the correct sense.

(2) Conciseness : A letter shall not be unnecessarily long. It must be concise and precise.

(3) Completeness : A business letter shall be complete in every sense. The points must be arranged systematically and logically and then a complete and clear picture emerges.

(4) Unambiguous : A business letter must be free from ambiguity.

(5) Courtesy : A business letter must be courteous. This means that the letter should be polite in its form.

(6) Well-planned : Effectiveness of a letter depends on its good planning.

Q. 30. What is written communication? Mention its merits and demerits.

Answer 30.

Written communication means transmission of information through written words. It may consist of messages in the form of letters, circulars, notes, notices, telegrams, bulletins, reports, memoranda, etc. Written communication provides a permanent record for future reference. It enables information to be conveyed far and wide. It should be clear, concise, complete and correct in order to make it effective.

Advantages of written communication :

The advantages of written communication are as follows :

(i) It may be transmitted to numerous persons simultaneously.

(ii) It provides a permanent record for future reference.

(iii) It is more effective than oral communication.

(iv) It is an ideal way of transmitting lengthy messages.

(v) It is a formal communication and it carries more weight.

(vi) It can be quoted as legal evidence in the case of any dispute.

Disadvantages of written communication :

The demerits of written communication are as follows :

(i) It is an expensive and time-consuming method of communication.

(ii) It is very formal and lacks a personal touch of sophistication.

(iii) Written communication finds it difficult to maintain secrecy.

(iv) It may be unsuited if unknown words and unfamiliar phrases are used.