

P.S : I have written pages as per UPSC GCAB

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(To be filled by candidate)

Name of Candidate : Ayush Agrawal

Roll No. :

Registration Number : Date of Examination : 17/7/22

Exam Centre : Old Rajinder Nagar ☐

Online ☒

CSE (Main) Test Series - 2022

Test-2

ECONOMICS OPTIONAL
International Economics/Growth and Development

Time Allowed : Three Hours

Maximum Marks : 250

QUESTION PAPER SPECIFIC INSTRUCTIONS

(Please read each of the following instructions carefully before attempting questions)

There are **EIGHT** questions divided in two Sections and printed in ENGLISH.

Candidate has to attempt **FIVE** questions in all.

Question Nos. 1 and 5 are compulsory and out of the remaining, **THREE** are to be attempted choosing at least **ONE** from each Section.

The number of marks carried by a question/part is indicated against it.

Answers must be written in the medium authorized in the Admission Certificate which must be stated clearly on the cover of this Question-cum-Answer (QCA) Booklet in the space provided. No marks will be given for answers written in a medium other than the authorized one.

Word limit in questions, wherever required, may be drawn/given in the space provided for answering the question itself.

Attempts of questions shall be counted in sequential order. Unless struck off, attempt of a question shall be counted even in attempted party. Any page or portion of the page left blank in the question-cum-Answer Booklet must be clearly struck off.

(For filling by Examiners only)

Q. No.	Page No.	Max. Marks	Marks	Total	Signature
1.(a)	4	10			
1.(b)	6	10			
1.(c)	8	10			
1.(d)	10	10			
1.(e)	12	10			
2.(a)	14	20			
2.(b)	18	15			
2.(c)	21	15			
3.(a)	24	15			
3.(b)	27	20			
3.(c)	31	15			
4.(a)	34	15			
4.(b)	37	20			
4.(c)	41	15			
5.(a)	44	10			
5.(b)	44	10			
5.(c)	44	10			
5.(d)	44	10			
5.(e)	44	10			
6.(a)	54	20			
6.(b)	58	20			
6.(c)	62	10			
7.(a)	64	20			
7.(b)	68	10			
7.(c)	70	20			
8.(a)	74	20			
8.(b)	78	15			
8.(c)	81	15			
Grand Total					

Remarks

Observations:



SECTION 'A': INTERNATIONAL ECONOMICS

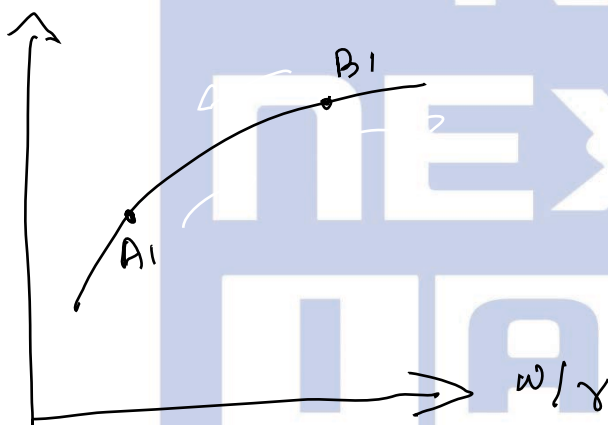
1. Answer the following questions in about 150 words:

(10 × 5 = 50)

- (a) What is the implication on direction of income distribution in case of Factor Intensity Reversal? (10)

Factor Intensity Reversal takes place when a commodity being produced by labour intensity in country A starts being produced by Capital Intensive methods in Capital Surplus Country and Vice Versa.

IMPLICATIONS ON INCOME DISTRIBUTION



Under Factor Intensity Reversal, the impact on income distribution direction is uncertain.

Under H-O model, trade led to relative factor price equalisation. For this w/r of country with labour surplus increased and that of capital surplus decreased [A1 & B1 converged]

Under Factor Intensity Reversal, relative factor prices and therefore their income shares move in the same direction for both countries.

① If Country 1 faces factor intensity reversal: w/r in both will fall and Capitalists' share in income rises

② If Country 2 faces FIR: w/r in both countries rise and Labourers' share in income rises in both the countries.

FIR is thus a scenario where Heckscher-Ohlin model and its inferences break down.

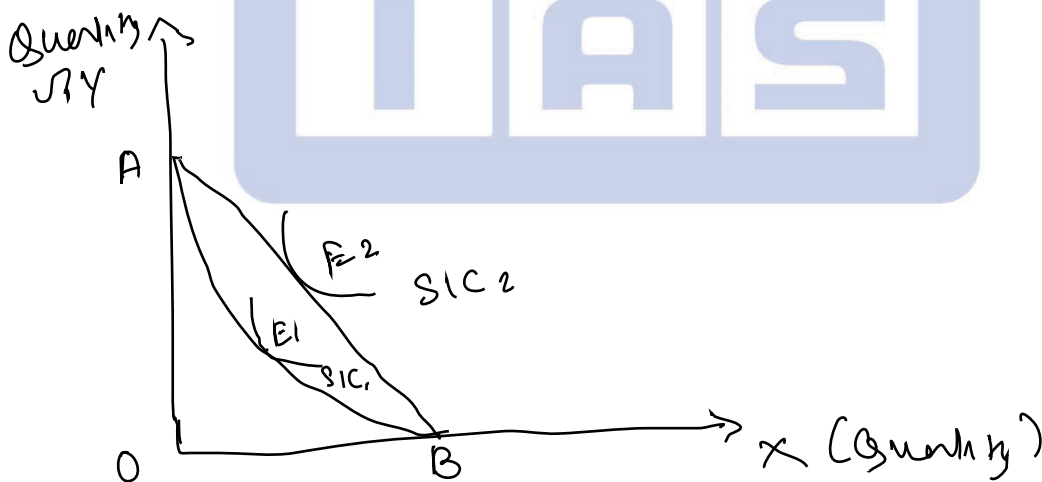
- (b) How a mutually beneficial trade between two nations can be explained in case of increasing returns to scale, assuming the two nations are identical in every respect? (10)

Lyndall gave a model for mutually beneficial trade under increasing returns to scale on COMPLETE SPECIALISATION.

Assumptions

- ① Two countries A & B
- ② Concave PPCs which are identical as increasing returns to scale.
- ③ Identical preferences $\Rightarrow$ Same SIC^s

MODEL



Initially in no trade condition, both countries are at E_1 on SIC_1 . As trade opens up, one country starts specialising in X and the other starts

specialising in Y . Both finally reach E_2 on SLC_2 .

Clearly $SLC_2 > SLC_1$ & $E_2 > E_1$.

Therefore, trade is mutually beneficial.

INFERENCES

- ① Any country can specialise in any commodity, based on domestic market size for respective commodity.
- ② It explains intra-industry trade which is very prevalent in today's world. India exporting Hatchbacks while importing sedans.

CRITICISMS

- ① Two countries can't have identical PPCs & resource endowments.
- ② Increasing returns to scale are not observed without large markets.

Mutually beneficial trade is therefore possible under increasing returns.

(c) Explain Rate of Effective Protection.

(10)

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Rate of Effective Protection refers to the effective protection observed by a domestic producer on an imposition of import tariff on inputs as well as final products.

$$g = \frac{T - A_i \times T_i}{1 - A_i} \quad \text{where 'g' is effective protection}$$

T = nominal tariff rate on final product

T_i = Nominal tariff on imported inputs

A_i = Proportion of imported inputs to value of final product before tariff

EXAMPLE

If a car worth \$ 500 is manufactured in India using imported components of \$ 400. $\Rightarrow A_i = 0.8$ ($400/500$)

Assume a nominal tariff rate of 10% on same car is applied (\$50) and a 5% nominal tariff on inputs

that are imported.

$$\therefore g = \frac{10 - 5 \times 0.8}{1 - 0.8} = \underline{\underline{30\%}}$$

INFERENCES

- ① If $T_i < T$, then $g > T$. Thus effective protection exceeds nominal protection.
- ② If $T_i > T$ (Inverted Duty Structure), $g < T$. Thus effective protection is low.
- ③ If $T_i \gg T$ then effective protection rate (g) can even be NEGATIVE.
- ④ For $T > T_i$, ' g ' will increase as ' A_i ' increases and vice versa.

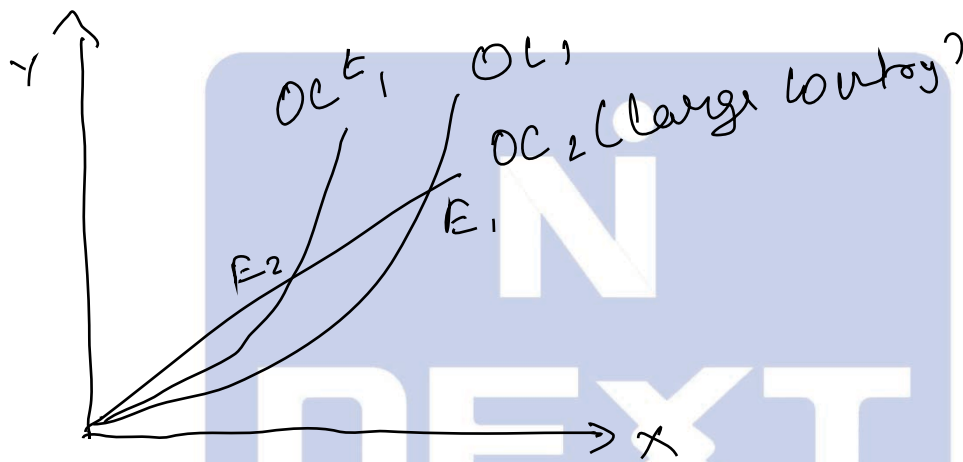
Therefore, in a complex global supply chain, government must look at effective rate of protection and not nominal protection.

- (d) Explain the impact of tariff in a small country using general equilibrium framework. (10)

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Tariff by a small country is always welfare reducing as it forus no improvement in Terms of Trade.

GENERAL EQUILIBRIUM IN TARIFF



On imposition of tariff by a small country '1', its offer curve bends / rotate towards axis of commodity on which tariff is imposed.

OC^T_1 intersects OC_2 at E_2 and trade volume reduces, while Terms of Trade remain unchanged.

There is a dead weight loss as trade volume reduces.

The small size of the country is

evident from the fact that the offer curve of 'I' interest OC₂ in its straight line position.

IMPACT ON INCOME DISTRIBUTION

As trade volume reduces for country 1, exports of X reduces and imports of Y fall.

The abundant factor (Labour here) will face lowering of wages while returns to scarce factor (Capital) will increase.

In small countries with a labour surplus, capitalists thus lobby for a tariff protection wall.

(e) Explain the policy issues in case of Keynesian Open Economy.

(10)

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Keynesian Open Economy is a demand side view of economy with spare production capacity.

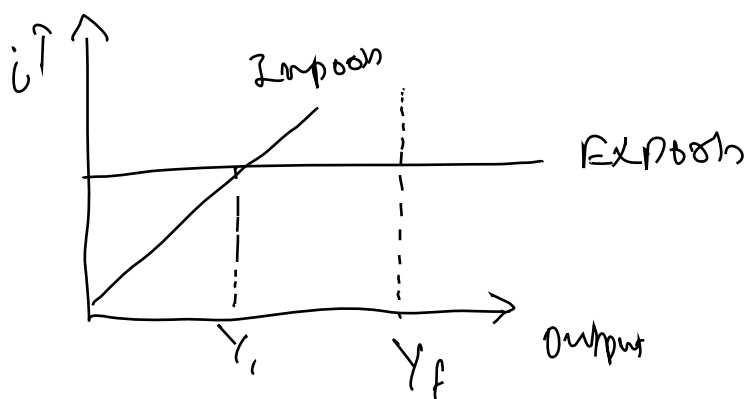
MODEL

- ① The LM schedule remains unchanged as domestic investors are not considered to invest abroad.
- ② IS schedule also depends positively on exchange rates.
- ③ Imports are a function of domestic income & exchange rates.
- ④ Exports are a function of exchange rates and foreign income.
- ⑤ Capital flows depend on difference between domestic & foreign interests.

POLICY ISSUES

- ① Under fixed exchange rate, policy makers face a dilemma whether to reach full employment output or

equilibrate Balance of Trade.



Whereas, Trade is balanced at income Y_1 , full employment is at Y_f .

② Monetary Policy Independence

An expansionary monetary policy, reduces interest rates and increase incomes. Former leads to Capital Outflows, while latter leads to higher imports. Thus BoP deficit.

A flexible exchange rate system is therefore more preferable as it also protects from global shocks and resolves policy issues.

2.

- (a) "Trade is always growth promoting." Do you agree? Substantiate your arguments on the basis of established theories. (20)

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Trade impacts growth through the twin effect of 'Wealth Effect' and 'Terms of Trade' effect. The cumulative effect decides whether trade promotes growth or leads to immiserisation.

Wealth Effect

Due to increase in exports, the exporting sector's income increases.

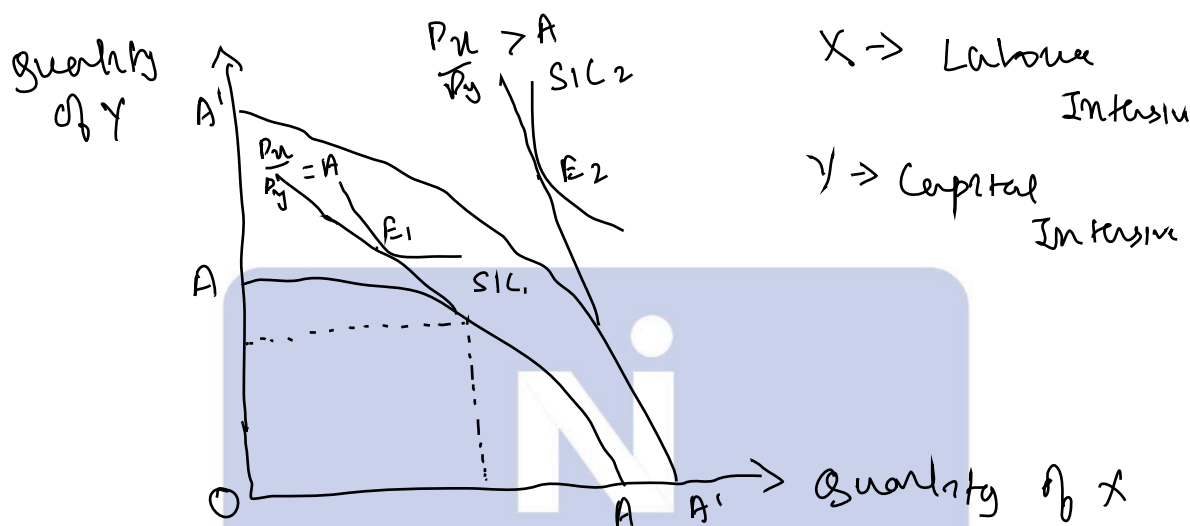
Terms Of Trade Effect

As quantity of exports rise, the relative prices of exports vis-a-vis imports fall.

TRADE PROMOTING GROWTH

When trade leads to an accumulation of scarce factor of production, the terms of trade

effect is favourable and trade is welfare enhancing as shown in Fig 1 below.



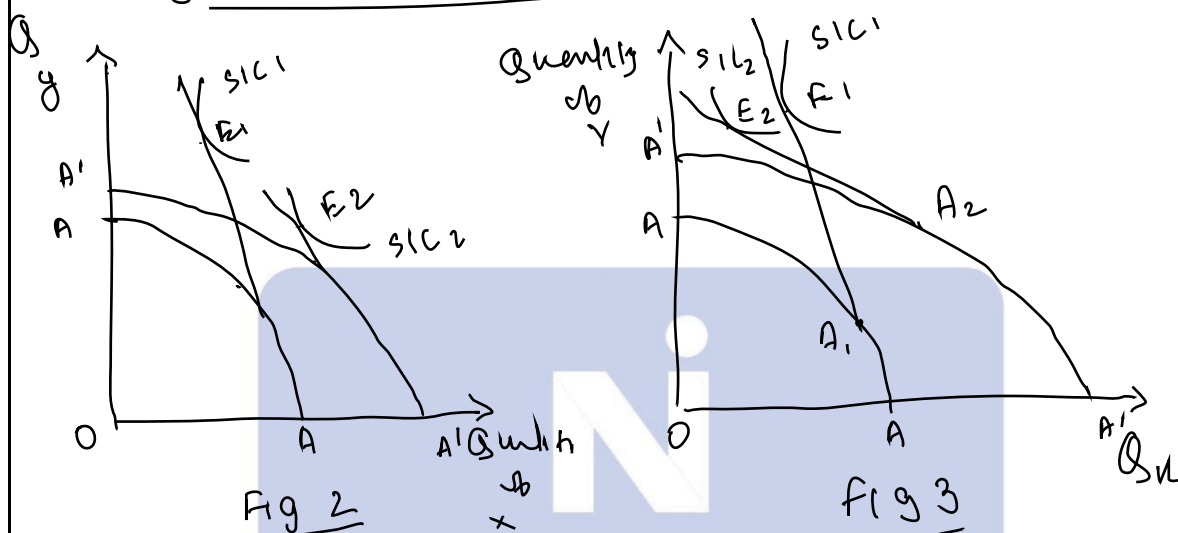
As production possibility function shifts outwards from AA to A'A' more on Y axis, than on X axis. Terms of Trade for country A (Labour surplus) improves. The new equilibrium point is now E2 on SIC2. It is clear that E2 lies to the North-East of E1 and therefore $E_2 > E_1$.

AMBIGUOUS CASE

When the growth is export oriented, PPC shifts more on X axis than on Y axis, Wealth Effect is positive. But

Terms of Trade Effect is negative.

If TOT effect < Wealth Effect, trade is growth enhancing as in Fig 2.



Bhagwati's Immiserizing Growth

Bhagwati asserted that Terms of Trade effect for a developing country is much higher and unfavourable as shown in Fig 3. The overall impact is IMMISERIZATION as $SI_2 < SI_1$.

E_2 was available to country A earlier as well, but it chose $E_1 \Rightarrow E_1 < E_2$.

A country which is largely dependent on exports, whose exports are price inelastic is more prone to face immiserization due to trade.

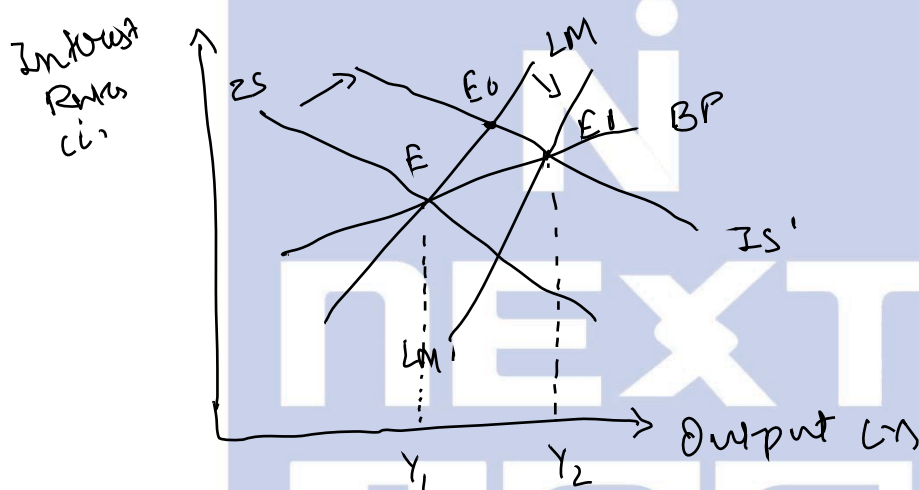


- (b) In an open economy, with high capital mobility, fiscal management is as best as doing nothing. Do you agree? (15)

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The effectiveness of Fiscal Policy in an open economy with high capital mobility also depends upon the exchange rate system adopted by the economy.

FIXED EXCHANGE RATES



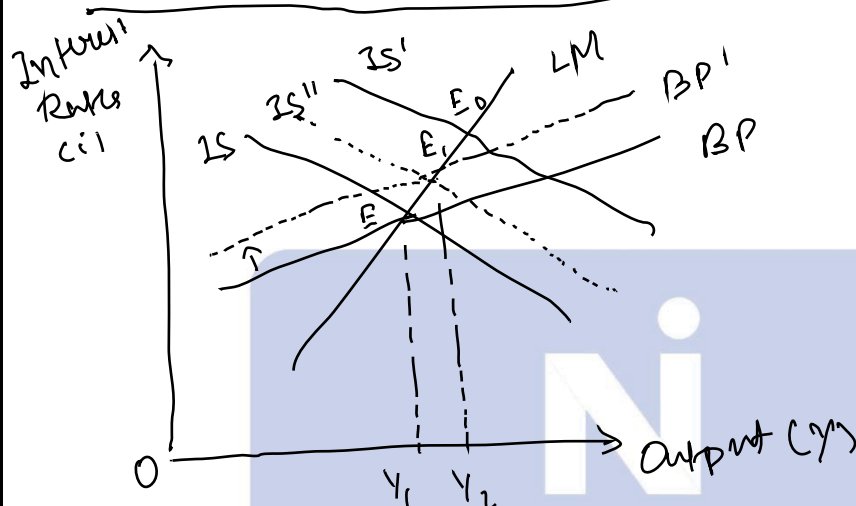
On an expansionary fiscal policy, IS shifts rightwards to IS'. The point E_0 reached now is a Balance of Payment Surplus point as for a given income, interest rates are higher $\Rightarrow$ Capital Inflows.

To maintain fixed exchange rate, central bank will buy foreign currency and sell domestic currency.

This will happen till LM shifts rightward to LM' to reach new equilibrium E₁.

The income has increased from Y_1 to Y_2 and thus fiscal policy is effective.

FLEXIBLE EXCHANGE RATES



On fiscal expansion and shift of IS rightwards from IS to IS' , a point of BoP surplus $\Rightarrow E_0$ is reached. The exchange rates will thus appreciate.

This will discourage exports & encourage imports. Thus NX will fall and both IS and BP will shift leftwards to reach E_1 .

At E_1 , income rises only little to Y_2 , while exchange rates appreciate. Also interest rates have risen to i_2 .

Fiscal Management is completely **INEFFECTIVE** only when **PERFECT** capital mobility along with **FLEXIBLE** exchange rate system is present.

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- (c) Devaluation of currency is a conditional policy instrument to increase exports. Analyse. (15)

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Deliberate Devaluation of Domestic currency is termed as 'Beggar-Thy-Neighbour' strategy to increase net exports and thereby increasing total output.

CONDITIONALITY OF EFFECTIVENESS

Following conditions need to be fulfilled if the policy is to yield desired results:

① Marshall-Lerner Condition

It states that the sum of Price Elasticities of Exports and Imports must be greater than 1. $E_p^x + E_p^I > 1$

This will ensure that Value of Exports rise and value of Imports fall.

This condition is generally not satisfied for countries like India whose exports are majorly Comd ore while exports are agriculture & services.

② Only if Business Cycles in different countries is not synchronised, recession in policy using country will not face COMPETITIVE DEVALUATION from other Trading Partners.

However, business cycles globally are very much synchronised now.

③ Time Lag

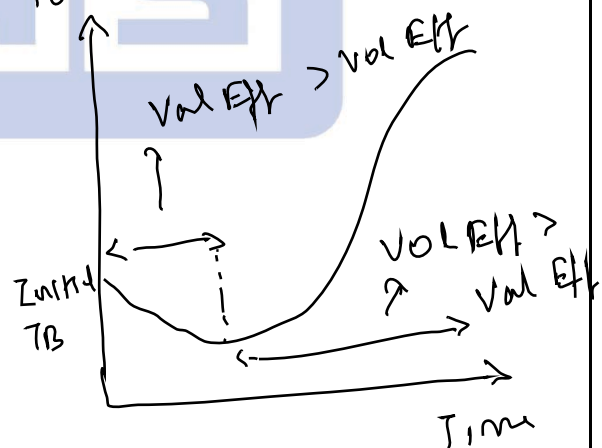
Even if above 2 conditions are met, the immediate effect of devaluation is worsening of Trade Balance as the

Value Effect dominates Volume Effect. After,

import demand and export demands have adjusted completely will Volume Effect

dominate Value Effect. This is depicted

by a J curve.



Devaluation is therefore a CONDITIONAL policy tool.

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3.

(a) Explain the concept of Optimum tariff in general equilibrium framework. (15)

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Optimum Tariff concept is a concept valid only for a large country. This is because only a large country experiences a POSITIVE Terms of Trade Effect on imposing a tariff.

OPTIMUM TARIFF

A tariff imposed has a negative wealth effect as trade goes down.

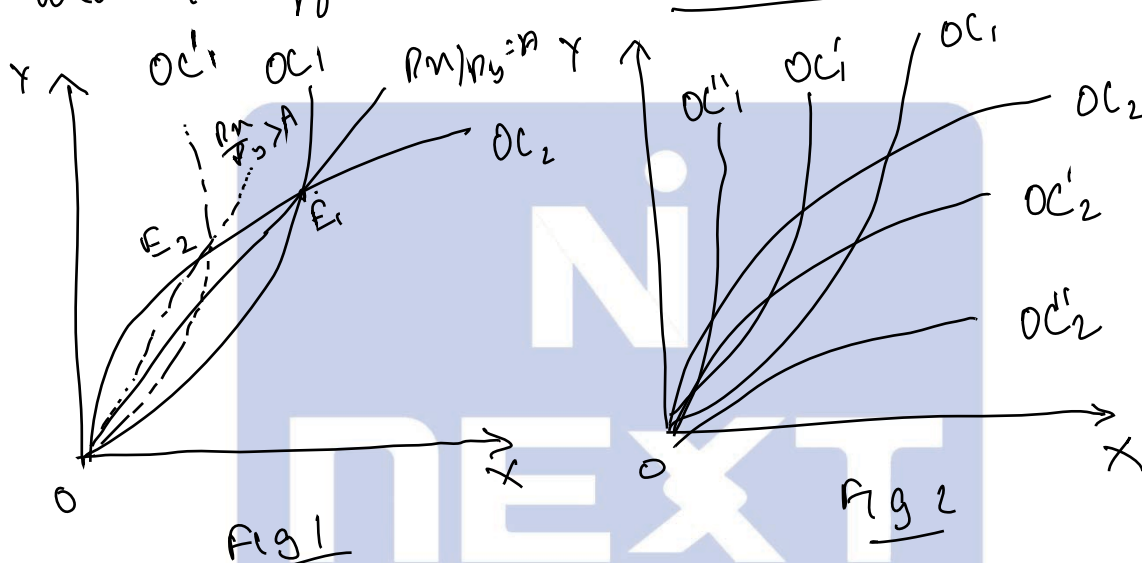
The welfare loss is in the form of consumption Distortion Loss as consumers pay higher price for imports and production Distortion Loss as some inefficient domestic producers now start producing.

However, not the complete tariff is passed on to consumers and some is borne by foreign producers. This has a favourable ToT effect.

When tariff is imposed for the first time, ToT effect dominates wealth effect and country's welfare enhances.

As tariff is subsequently increased, a point is reached, beyond which $To? \text{ effect} < \text{Wealth Effect}$.

At this point, $To? \text{ effect} = \text{Wealth Effect}$ and tariff is called OPTIMUM.



In Fig 1, E_2 is point of optimal tariff, where $To? \text{ effect} = \text{Wealth Effect}$.

However, if country 2 (trading partner) retaliates, as its welfare is lowered by tariff, offer curves subsequently shift away and finally intersect only at origin (OC'_2, OC'').

Therefore, optimum tariff is only applicable under the assumption of non retaliation and Large country.

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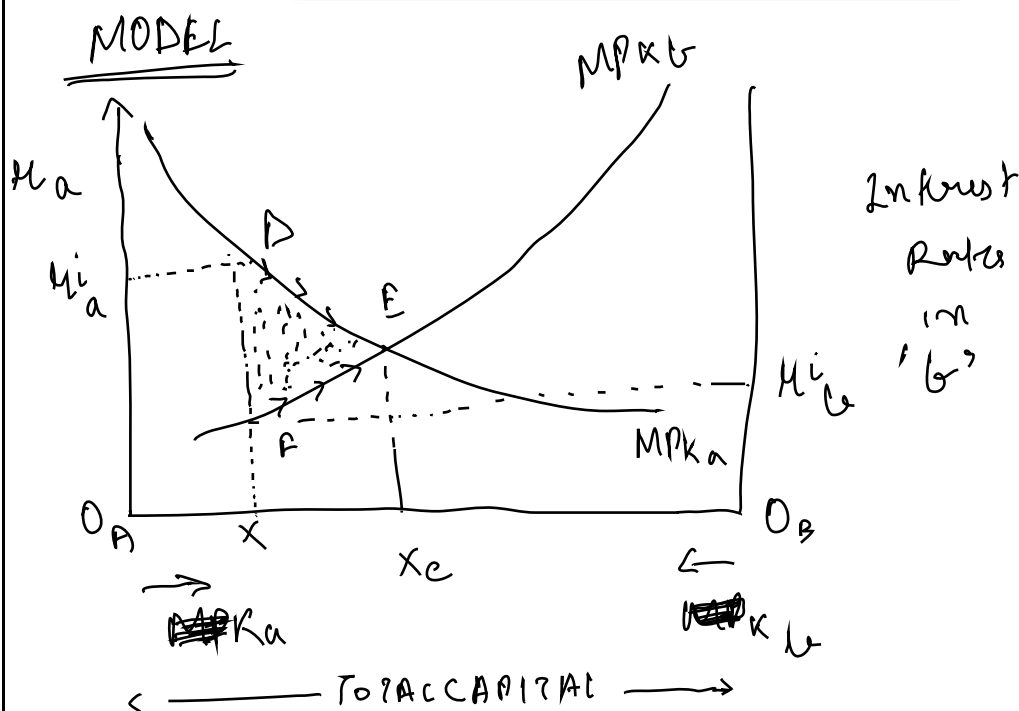
(b) Describe Classical Theory of FDI.

(20)

The Classical Theory of ADI uses perfect Capital mobility to show that capital is distributed in order to ensure maximisation of Overall Output.

ASSUMPTIONS

- ① Perfect Completion in Factor & Output markets & perfect Capital Mobility.
- ② Marginal Product of Capital diminishes in both countries.
- ③ Two countries A & B with perfectly flexible interest rates.
- ④ No barrier on Capital Mobility.



At initial situation 'x', MPK in B is less and interest rates are lower compared to interest rates in 'A'.

When capital mobility is allowed, Capital will flow from B to A, till x^e is reached and both nations have same interest rates.

This results in loss output of DEF area. However, output of B will decline while that in A rises.

IMPACT ON BALANCE OF PAYMENTS

Initially, BOP will worsen for country B while it will improve for country A, due to FDI inflows.

After some time, FDI in A will start reaping benefits and BOP of A will deteriorate as capital flows outwards while that in B improves.

The theory is however criticised for its strong assumptions.

CRITICISMS

- ① Perfect Capital Mobility does not exist in real world.
- ② Interest rates in many economies is highly regulated and not flexible.
- ③ Many economies have no Capital Account convertibility.
- ④ Initial BOP deficit faced by country B can force it to stop capital outflow.
- ⑤ Assets of different economies are not perfect substitutes.
- ⑥ The theory wishes away exchange rates fluctuation.

The theory can only explain, capital flows from capital abundant to capital scarce countries. It also holds good when long run data is observed. However, strong assumptions make it analytically useful.

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- (c) WTO has started losing its relevance, the result of which is protectionist tendencies across the world. Substantiate your arguments with proper reasons. (15)

World Trade Organisation (WTO) is a global consensus based organisation promoting international trade. It has 164 members and has off-late started losing relevance.

REASONS FOR LOSS OF EFFECTIVENESS

(1) Continuous dispute among Developed and Developing Nations:

(A) On Agreement on Agriculture, developing countries are calling for a permanent solution to issue of Public Stock holdings. For eg, India is asking for permission to export food from such exports to food insecure nations.

(B) TRIPS dispute:

Developing countries are lobbying for less stringent IPR standards, specially for pharma. But developed nations

are against it. For eg, COVID-19 therapeutics waiver is inadequate.

③ TRIMS:

The agreement is tilted heavily in favour of MNCs & developed countries and reduces policy space for developing nations.

② Dysfunctional Dispute Appellate Body

The left of USA has rendered the appellate body dysfunctional, making WTO an ineffective institution.

② COVID-19 crisis and the ensuing supply chain disruptions has forced countries to turn inwards and use protectionism for self-reliance.

④ The Consensus : It delays decision making.

If WTO wants to make itself effective again, majority rule must replace consensus and developing countries be made more powerful.

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4.

- (a) How does an economy reach full employment level of output if it is presently facing unemployment in a flexible exchange rate system and imperfect capital mobility? (15)

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- (b) Explain Salter Swan diagram. Define the zones of equilibrium and disequilibrium. What policy prescriptions would you suggest for the situations pertaining to unemployment and inflation vis a vis BOP deficit. (20)

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(c) Critically examine Hecksher Ohlin Model.

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SECTION 'B' : GROWTH AND DEVELOPMENT

5. Answer the following questions in about 150 words:

(10 × 5 = 50)

- (a) The rural areas in India have witnessed more of the centripetal effect than centrifugal effect of growth in India. Critically analyse. (10)
- (b) Environment degradation is also the result of low level of development along with absence of market. Explain. (10)
- (c) What is "Solow residual"? What are its implications? (10)
- (d) Analyse the role of linkages in Unbalanced growth theory. (10)
- (e) How can the problem of Harrod's instability be solved? (10)

(A) Myrdal's circular theory holds good for a dualistic economy like India which focus strong backwash effects and weak spread effects.

CENTRIPETAL FORCES

① With urban areas providing better employment opportunities, skilled labour has migrated from rural areas to urban areas leading to modernisation of Agriculture.

② Capital from rural areas in form of agricultural surplus has been invested in urban areas by rural

landlords for higher returns.

- ③ The manufacturing development in urban areas has throttled the small scale industries of rural areas.

CENTRIFUGAL FORCE:

- ① Remittances from urban areas have been the life blood of rural economy.
- ② Increased demand from urban areas for primary products like milk have generated employment in rural.
- ③ Some backward areas are now a source of raw material for urban industries.

Overall, backwash effect has dominated spread effects leading to low standard of living in rural areas.

The government can invest in social overheads & human capital to strengthen spread effects.

③ Environmental Degradation can be stopped only when incomes and output rise sufficiently to ensure surplus & technology development for environmental sustainability.

CAUSES OF DEGRADATION

① Under Development

Low Per Capita Incomes lead to use of poor & inefficient production methods which lead to pollution.

Eg, Fluorescent Disinfecting instruments have not been adopted in India yet.

② Small Market Size

Smaller markets in developing countries inhibit economies of scale.

The cost of production using cleaner technologies, thus increase.

Eg, High cost of Air Purifiers in India.

③ Poor Awareness

Under-development leads to poor and inefficient fuels like wood & cow dung, which again lead to environmental degradation.

Therefore, increasing economic growth is a must to protect environment. They are mutually reinforcers and not substitutes.

©) Solow gave the Growth Accounting Equation to show contribution of various sources to growth. Solow residues were the residue of this equation:

$$G = \frac{A'}{A} + w_k \times \frac{k'}{k} + w_n \times \frac{N'}{N}$$

where k = capital, N = Labour

G = Growth, A = Technology

and $'$ implies rate of change.

w_n & w_k are respective weights of labour & capital.

SOLOW RESIDUES

He used data from past and calculated the residues after plugging in values for Capital & Labour.

The residues came out to be 8.7% and Solow considered this as the contribution of Technology.

ISSUES

- ① He did not consider 'Human Capital', which may have inflated the residual term.
- ② Technology growth is not exogenously decided as Romer explained.
- ③ Human Capital increases productivity of both labour & capital.

Solow Residues, nevertheless were important in explaining the central role that technology plays in growth process.

⑤ Linkages between SOC & DPA play an important role in the unbalanced Growth Strategy. It thus recommends investing in industry with highest linkage scores.

STRATEGY

Disequilibriate the economy to induce demand & thus growth.

① SOC followed by DPA
Investment in education, infrastructure and skills reduce the cost of production activities and thus induce DPA.

② DPA first SOC follows

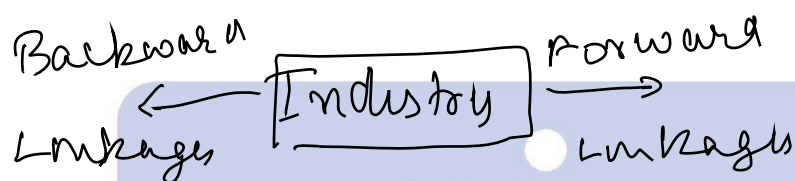
The DPA creates demands for SOC as demand for skilled people and physical infra like electricity etc.

LAST INDUSTRY FIRST

The development strategy recommends

investment in last stage of production first. This will be followed by further stages when sufficient demand for inputs is present.

Therefore, Import Substitution



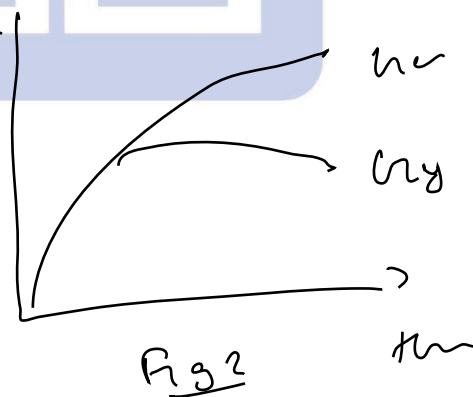
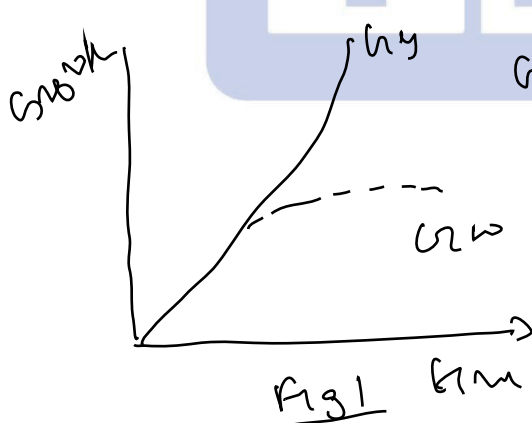
The industry with highest score is Steel & Iron.

Linkages therefore play a central role in UNBALANCED growth strategy.

- (E) Harrod's model is based on an unstable knife edge equilibrium where economy must run faster and faster to grow at a steady state.

KNIFE EDGE EQUILIBRIUM

- (1) When Actual growth (G_{ay}) exceeds warranted growth (G_{aw}), entrepreneurs are induced to invest more as profits are rising. Because investment will create more demand than supply the equilibrium will further diverge.



- (2) If $G_{aw} > G_{ay}$, entrepreneurs will reduce their investments. But because investment will lower supply by less than demand. DIVERGENCE

REASONS FOR KNIFE EDGE

- ① Rigidity of Interest rates, constant K/Y & K/L ratios.
- ② Rigidity in wages & prices

How to REMOVE?

① Kaldor's Solution

When $G_w > G_y$, share of profits will reduce and Total Savings will reduce as $s_p > s_w$. Thus savings will equal investment and G_y reduces to equal G_w

② Amartya Sen's Solution

If prices and wages are only sticky and not rigid.

(A) If $G_y > G_w \Rightarrow$ Prices increase

$G_w \downarrow$ $\leftarrow$ Rental cost of Capital Decrease $\leftarrow$ G_y decrease

(B) If $G_w > G_y \Rightarrow$ Wages lag Prices $\Rightarrow$

$G_w \downarrow$ $\leftarrow$ $G_y \uparrow$ $\leftarrow$ Real wage Rise

6.

- (a) Economic growth in underdeveloped and over populated countries is possible only when a sufficient minimum effort is made to transition from a state of backwardness to secular growth. Explain. (20)

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- (b) Examine the problem of free ridership in environment degradation. How can it be corrected? (20)

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(c) Explain the five stages of Rostow's growth model.

(10)

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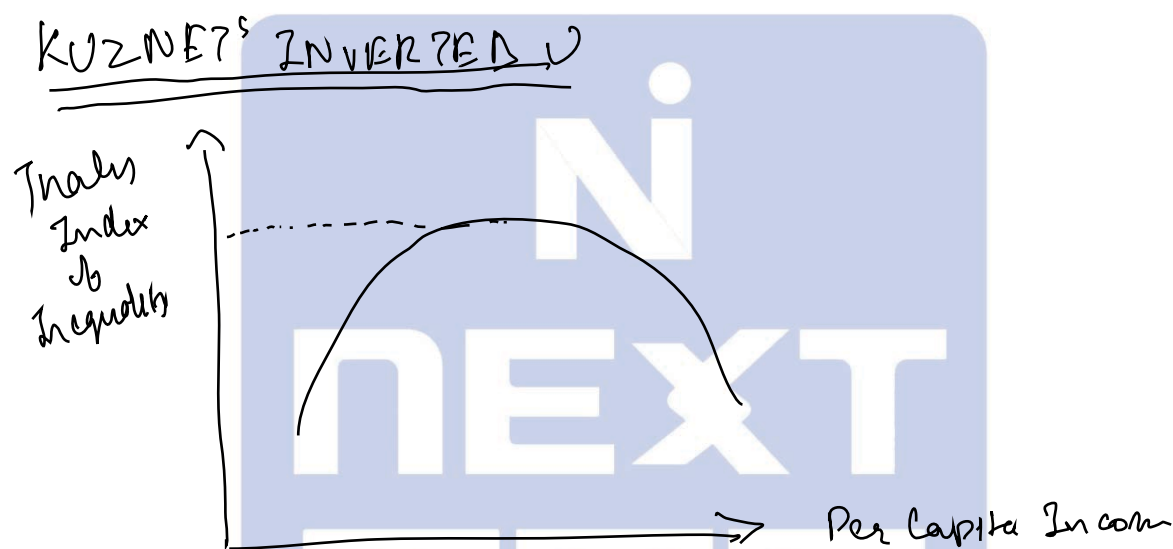


7.

- (a) The peak of the Kuznet's inequality curve can be reduced with proactive role of state in the economy. Do you agree? (20)

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Kuznets developed the Inverted-U theory of Inequality which says that initially development leads to rise in inequality and gradually it reduces:



CAUSES OF INCREASING INEQUALITY

- ① As labour shifts from agriculture to manufacturing sector, incomes in latter rise while incomes in former unchanged.
- ② Rural Property Owners flow their capital to urban areas in lieu of higher returns.
- ③ Government has an urban bias as more resources are diverted there.

- ④ Land reforms are politically difficult and state has low resources for social security as Income Tax is low to encourage savings & investments.

CAUSES OF FALLING INEQUALITY

- ① With development, state gathers resources for social security. For eg, MGNREGS, NPSA
- ② Rural areas start getting some benefits
- ③ Manufacturing sector matures and technological improvement in Agriculture.

COHORT EFFECT

Kuznets argued that inequality is lower in a fat cohort as more proportion of population is in middle ages (40-55). They have stable and higher incomes.

Inequality is higher in Narrow Cohort as more variability in age & income.

TRADE

As trade is opened, exporting sectors' income increases initially while that

of others remain unchanged. Gradually the benefits are spread and inequality reduces.

WAYS TO LOWER PEAK

Following Interventions by Govt can:

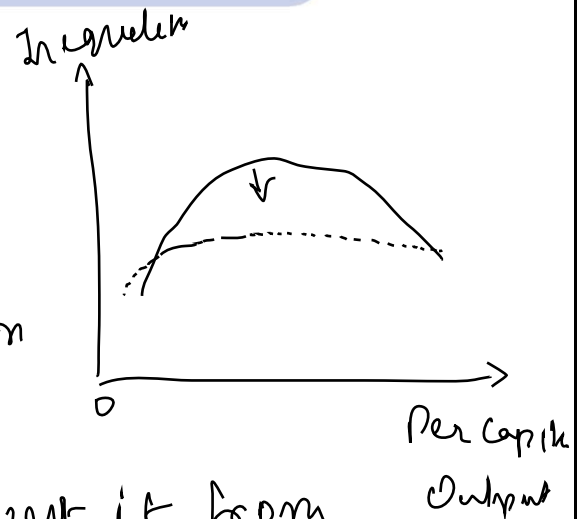
① Progressive Taxation: Higher taxes on rich people can be used to distribute to poor $\Rightarrow$ Inequality Reduces

② Targeted Poverty Reduction: State must not wait for high per capita income to start poverty alleviation.

③ Social security: Unemployment subsidy and food subsidies reduce inequality.

Therefore, suitable government policies aim at wealth redistribution can flatten Kuznet's

curve as well as prevent it from becoming N shaped.



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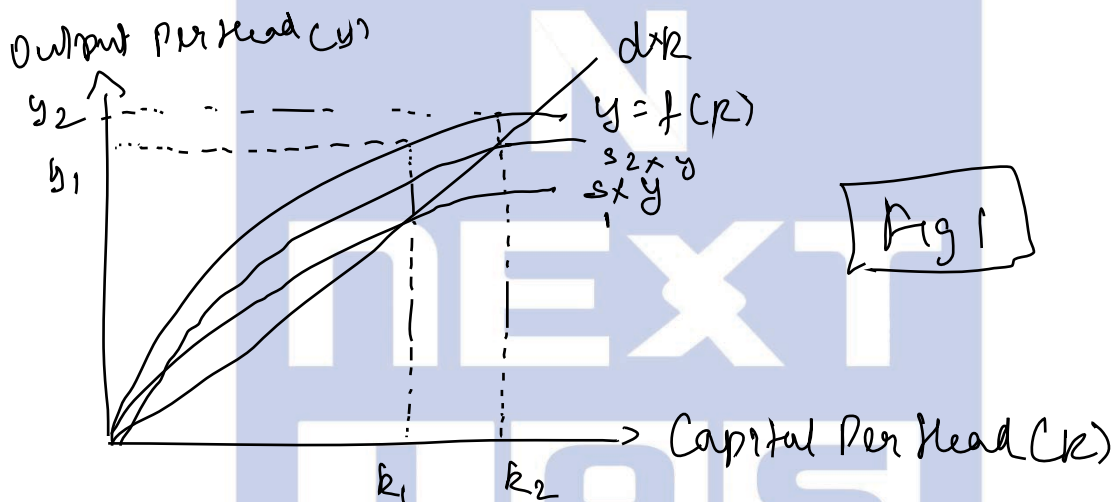


- (b) The impact of savings in Solow model differs from that in Harrod Domar Model. Analyse. (10)

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While savings rate only have a level effect under Solow growth model, it has a growth effect under Harrod Domar Growth models.

SAVINGS IN SOLLOW MODEL



It can be seen from Fig 1 that as savings rate increases from s_1 to s_2 , investment function shifts upwards.

For a temporary period, growth of output rises, but it is balanced by the need for extra output to compensate for higher depreciation.

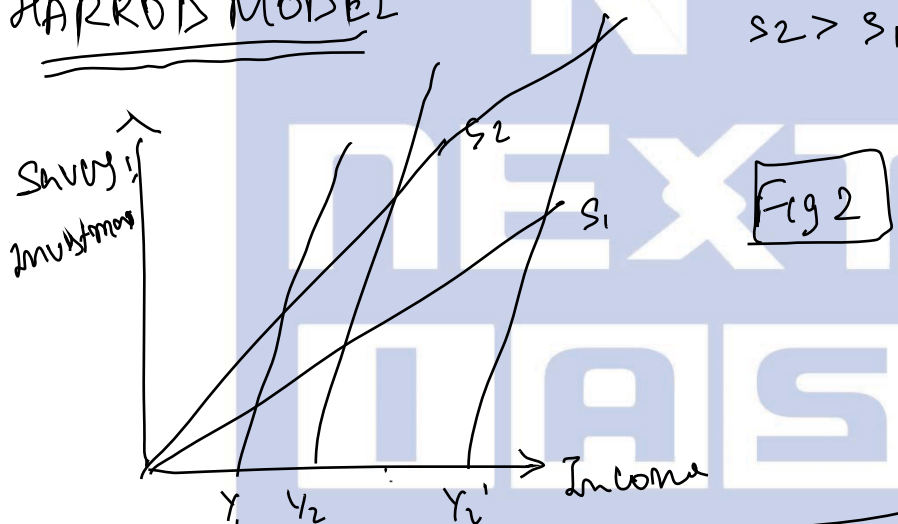
Per Capita Output thus rises from y_1

to y_2 and per Capita Capital also rise from k_1 to k_2 .

The labour thus has more machines to work with and standard of living has risen.

The Steady State Growth rate however remains equal to ZERO as no population increase is assumed.

HARROD MODEL



In Harrod's model $G_y = s/v$ where

v is the fixed Capital Output ratio. As savings rate increases, G_y increases to s_2/v . This is depicted in Fig 2.

Saving is a virtue in Harrod & as well as Solow model. But have different impacts.

- (c) "In view of resource constraints and economic uncertainties in developing economies, the Hirschman's Model makes more sense." Discuss in the background of limitations of Balanced growth theory. (20)

Hirschman propounded the Unbalanced strategy of Development that needs lesser resources at one go. It uses the linkages between SOC & DPA for growth.

UNBALANCED GROWTH

Assumptions

- ① There are investment projects that appropriate more economies of scale than they create. They are called convergent series of investments or Directly Productive Activities (DPA).
- ② Those projects that create more economies than they appropriate are called divergent series and Social Overhead Costs. Eg, Education, Infra.

Hirschman says that growth is a string of disequilibria which must not be culled, of which profits is a

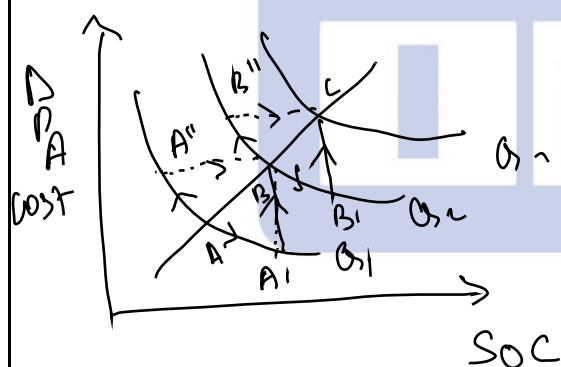
normal outcome.

TWO PATHS

The economy can be disequilibrated through 2 paths:

(1) SOC followed by DPA

Govt. can invest large resources in education, infrastructure and skill training. This will reduce input costs of DPA and thus induce DPA for GDP growth. This path is smooth.



Solid Path $AA'BB'C$
is SOC followed
by DPA

$Q_3 > Q_2 > Q_1$ are isoquants

(2) DPA followed by SOC

Initial investment in production will create demand for social overheads.

The Government will be forced to invest in SOC to avoid price inflation.

This is however dashed here $AA''BB''C$

BENEFITS OVER BALANCED

- ① Resources needed are much less compared to Balanced Strategy.
- ② Unbalanced Strategy uses Private enterprise economy and thus favours more realistic mixed economy
- ③ Balanced growth require entrepreneurial state, which is a harsh demand.

ISSUES OF UNBALANCED STRATEGY

- ① The shortages & bottlenecks created are beyond capacity of developing countries
- ② Inflation control is difficult.
- ③ Business Entrepreneurs will react adversely, knowing that bottlenecks are deliberately created.
- ④ Govt may not follow up with SOC after initial DPA injection.

India failed in implementing this strategy during 2nd FYP - 5th FYP as it was unable to control consumption. With Inflation Targeting, it is now possible.

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8.

- (a) The markets and state have complementary role to play in development of an economy. Critically analyse this statement in the light of Washington Consensus. (20)

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- (b) The Endogenous growth model on Technology is developed as an improvement over static understanding of the Solow Model. Explain. Analyse the conclusions drawn by the Romer's Model. (15)

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- (c) What are the core requirements of strategy of agricultural and rural development?
(15)

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SPACE FOR ROUGH WORK

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