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1st Home Assignment
ECO307 Fundamentals of Economics

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CLASS: B. Tech (IT) VI Sem

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PAGE NO: 03

DATE: 25-01-2022

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Q1. We all know the issues of excessive debt & how it harms in the long-run. India currently has a debt of approx. 75% of its GDP. You have been appointed as an economic advisor to the Govt of India. Pls detail why do you think this is harmful for our country & suggest any 10 measures should we adopt to reduce it?

Sol: Excessive public debt results in high-risk premium in interest rates, which causes reduction of private investment and contraction of GDP in the long run. Excessive public demand stimulates demand and shows desired result, but it will be not for a greater period of time. After a period, the economic growth will turn negative if the debt-GDP ratio exceeds 90 per cent.

10 measures to reduce excessive debt are:

1. The government may think of privatising loss-making public sector undertakings (PSUs) such as Air India. Further, 'minimum government and maximum governance' principle may be adopted in privatising any PSU.
2. By maintain Lower interest rates, the government make it easier for individuals and businesses to borrow money. These borrowers can spend that money on goods and services, which will create jobs and tax revenues, thus, reducing public debt.
3. Government can also raise taxes like federal, state, local, business tax, etc, to pay for expenditures.
4. The government can also consider Public Private Partnership in social schemes.
5. India has abundance of Renewable Energy, Thus, saving money on foreign exchange for fossil fuels, and relying on India's Renewable energy can make India a very large economy.
6. Public Financial Management System should be leveraged to the maximum possible through real-time. consolidated and granular data on advances, transfer of funds and utilisation.
7. Under the banner of co-operative federalism, the Central and State governments should undertake robust expenditure planning to address the socio-economic challenges without diluting the goals of fiscal consolidation.
8. The government should to focus on investment in infrastructure and human capital for realising the multiplier effect.
9. Rather than raise taxes, governments should issue debt in the form of bonds to raise money. This stimulates the economy by generating additional tax income from prosperous businesses and taxpayers.
10. There are examples throughout history where spending cuts and tax hikes together have helped lower the deficit.

Q2. Capitalism, Socialism, Mixed economy all have their pros & cons. In your opinion, what type of economic system will suit India as of today & justify your answers with any 10 reasons for the same.

Sol: In my opinion mixed economy is the most suitable for India even now. A mixed economy is variously defined as an economic system blending elements of market economies with

elements of planned economies, free markets with state interventionism, or private enterprise with public enterprise. Mixed Economy is neither pure capitalism nor pure socialism but a mixture of the two systems.

10 reasons to support my answer are:

1. Mixed economy provides freedom to Businesses, Consumers on their decisions. Monopolies, market structures that are the only producer of a certain product, are allowed under government watch so they do not make it impossible for entrepreneurs in the same industry to succeed. Thus, Mixed economies provide adequate freedom to certain economic units.
2. India with its 1.38 billion(approx.) population that is still growing, requires a living where from rich to poor all can coexist, therefore the Government encourages free economic activities while taking necessary measures to control them simultaneously.
3. Various fiscal and monetary policies introduced by Governments urge private entities to contribute towards economic welfare at a larger level. In contrast, India's public sector provides employment opportunities to the masses and avoids regional inequalities. Furthermore, its price policies are guided by economic welfare instead of profit maximisation.
4. The Government of India has the authority to exercise price control and its regulation. However, it usually does not interfere with the prevailing price system, thus allowing industries to freely determine the prices of goods and services.
5. Heavy industries like atomic energy and defence equipment come under the purview of the public sector. The private sector includes agriculture, smaller enterprises, cottage industries, and consumer goods. Moreover, the Government of India also assists in the operations and growth of this private sector.
6. Capitalism enhances economic inequalities but under mixed economy, inequalities can be easily controlled by the efforts of government.
7. The most important advantage of mixed economy is that it provides encouragement to private sector and it gets proper opportunity to grow. It leads to increase in capital formation within the country.
8. Under this system, both private and public sectors work for the efficient use of resources. Public sector works for social benefit while private sector makes the optimum use of these resources for maximisation of profit.
9. Due to competition between both private and public sectors, the level of efficiency remains, high. All factors of production work efficiently in the hope of profit.
10. The Government takes measure to battle inflation and devises measures to control economic fluctuations.