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Money

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Money

Money is an officially-issued legal tender generally consisting of notes and coin, and is the circulating medium of exchange as defined by a government. Money is often synonymous with cash and includes various negotiable instruments such as checks



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Definitions

something generally accepted as a medium of exchange, a measure of value, or a means of payment

Anything of value that serves as a

- (1) generally accepted medium of financial exchange,
- (2) legal tender for repayment of debt,
- (3) standard of value,
- (4) unit of accounting measure, and
- (5) means to save or store purchasing power



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Functions of Money

Money is often defined in terms of the three **functions** or services that it provides.

Money serves as a medium of exchange, as a store of value, and as a unit of account.

Money's most important **function** is as a medium of exchange to facilitate transactions.



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The following points highlight the top six functions of money

A Medium of Exchange

A Measure of Value

A Store of Value (Purchasing Power)

The Basis of Credit

A Unit of Account

A Standard of Postponed Payment



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Barter System

A **barter system** is an old method of exchange. This **system** has been used for centuries and long before **money** was invented. People exchanged services and goods for other services and goods in return. ... The value of **bartering** items can be negotiated with the other party.



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History of Barter System

The history of bartering dates all the way back to 6000 BC. Introduced by Mesopotamia tribes, bartering was adopted by Phoenicians. Phoenicians bartered goods to those located in various other cities across oceans

Goods were exchanged for food, tea, weapons, and spices. At times, human skulls were used as well. Salt was another popular item exchanged. Salt was so valuable that Roman soldiers' salaries were paid with it.



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Problems

No Proof

No warranty/protection

No Fixed rate of Exchange

Wastage of Time and Effort

Problems of Indivisibility

No Room for Deferred Payment

It Discourages Borrowing and Lending

Difficulty in Storing Wealth

It Discourages Large Scale Production



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Differences between money and barter

Money is generally acceptable while other commodities are not.

Money is portable while some of the other commodities may be bulky.

Money is relatively scarce while other commodities are available.

Money is homogeneous while other commodities are heterogeneous (difference in color, shapes and sizes).

Money is durable while some other commodities are perishable e. g. fresh tomato.

Money is stable while other commodities are not.

Money is divisible into small units while other commodities are not.

Money has no intrinsic value but other commodities have.

Money can function as a standard of deferred payment while other commodities require immediate payment.

Money serves as a unit of account, other commodities cannot.



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Classification of Money

Legal Tender Money

It is that money which is accepted as a means of payment both by the Govt as well as the people. This type of money has legal sanction behind it. No one refuse to accept it as a means of payment.

Optional money

It is that money, which ordinarily accepted by the people, but has no legal sanction behind it. No one can be forced to accept this type of money against his wishes. It is optioned money



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Metallic Money

This money is made of a particular metal (i.e., Gold, Silver, Copper, Nickel, etc.,)

Paper money

has along history to its credit. China was the first in the world to make use of this in the 9th century and it began in India in the 19th century.



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Fiat Money

This is only a variety of in convertible fiat money and is issued generally at a time of crisis. That is why it's sometimes referred to as emergency currency

- a) Fiat money is issued in limited quantities
- b) Fiat money is issued at a time of crisis
- c) There is no-cover (metallic or fiduciary) behind it



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Money Supply

The total stock of money circulating in an economy is the money supply. The circulating money involves the currency, printed notes, money in the deposit accounts and in the form of other liquid assets.



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The supply of money means the total stock of money (paper notes, coins and demand deposits of bank) in circulation which is held by the public at any particular point of time.

Briefly money supply is the stock of money in circulation on a specific day. Thus two components of money supply are

Currency (Paper notes and coins)

Demand deposits of commercial banks



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Sources of Money Supply:

Government (which Issues one-rupee notes and all other coins)

RBI (which issues paper currency)

Commercial banks (which create credit on the basis of demand deposits).



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Price Index

A **price index** (plural: “**price indices**” or “**price indexes**”) is a normalized average (typically a weighted average) of **price** relatives for a given class of goods or services in a given region, during a given interval of time. ...
Consumer **price index**. Producer **price index**.



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Price Index

A general price index is an economic measurement that assesses the change in prices for goods and services. This index often measures the inflation in a market that artificially increases prices for goods and services at both the wholesale and consumer level.



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A **consumer price index (CPI)** measures changes in the price level of market basket of consumer goods and services purchased by households.

A **Producer Price Index (PPI)** is a price index that measures the average changes in prices received by domestic producers for their output.



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Inflation/Deflation

A: Inflation occurs when the price of goods and services rise, while **deflation** occurs when those prices decrease.

The balance between the two economic conditions is delicate, and an economy can quickly swing from one situation to the other.



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Inflation is when prices rise, and deflation is when prices fall. You can have both inflation and deflation at the same time in various asset classes.

When taken to their extremes, both are bad for economic growth, but for different reasons



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Inflation

It is defined as a sustained increase in the general level of prices for goods and services in a country, and is measured as an annual percentage change. Under conditions of inflation, the prices of things rise over time.

inflation is a sustained increase in the general price level of goods and services in an economy over a period of time.



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Types of Inflation

Hyperinflation: The worst is *hyperinflation*. That's when prices rise more than 50 percent a month. Fortunately, it's rare. That's because it's only caused by massive military spending.

Asset inflation: which occurs somewhere nearly all the time. For example, each spring oil and gas prices spike because commodities traders bid up oil prices. They anticipate rising demand at the pump thanks to the summer vacation driving season.



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Creeping inflation is when prices rise 3 percent a year or less. It's somewhat common. It occurs when the economy is doing well. The last time it happened was in 2007.

The fourth type is *walking*, or *pernicious*, *inflation*. Prices increase 3-10 percent a year, enough for people to stock up now to avoid higher prices later. Suppliers and wages can't keep up, which leads to shortages or prices so high that most people can't afford the basics.



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The fifth type, galloping inflation, is when prices rise 10 percent or more a year. It can destabilize the economy, drive out foreign investors, and topple government leaders. It's a result of exchange rate fluctuations.



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Causes of Inflation

There are three causes of inflation.

The first, demand-pull inflation, occurs when demand outstrips supply.

The second is cost-push inflation, which is when the supply of goods or services is restricted, while demand stays the same.

For example, since there is a shortage of highly skilled software engineers, their wages skyrocket.

The third, overexpansion of the nation's money supply, is when too much capital chases too few goods and services. It's caused by too-expansive fiscal or monetary policy, creating too much liquidity.



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Deflation

Definition: When the overall price level decreases so that inflation rate becomes negative, it is called deflation. It is the opposite of the often-encountered inflation.



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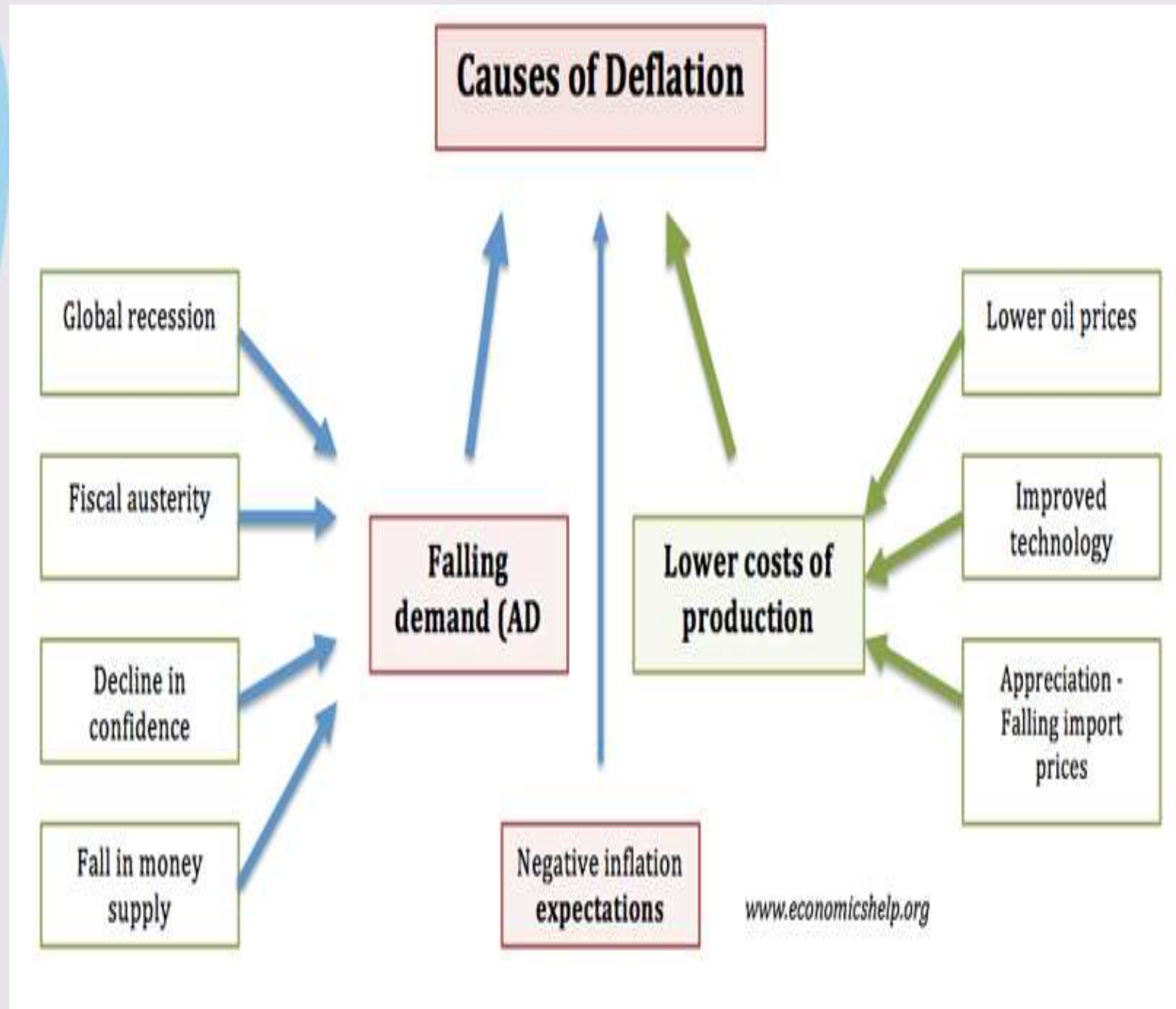
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Causes

Deflation, or negative inflation, happens when prices fall because the supply of goods is higher than the demand for those goods. This is usually because of a reduction in money, credit or consumer spending.



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