

CHAPTER-4

MONEY

Definition- money as “anything that is generally acceptable as a means of exchange and at the same time acts as a measure and store of value”.

The functions of money can be classified under three main heads:

A. Primary Functions or Original Functio

B. Secondary Functions

The main functions performed by money are called primary or original function.

The primary functions of money are as follows:-

Medium of Exchange: The most important function of money is to serve as a means of payment. To be a successful medium of exchange, money must be commonly accepted by people in exchange for goods and services. While functioning as a medium of exchange, money benefits the society in a number of ways: (a) It overcomes the inconvenience of barter system (i.e., the need for double coincidence of wants) by splitting the act of barter into two acts of exchange, i.e., sales and purchases through money.

It promotes transactional efficiency in exchange by facilitating the multiple exchanges of goods and services with minimum effort and time. (c) It promotes allocative efficiency by facilitating specialisation in production and trade (d) It allows freedom of choice in the sense that a person can use his money to buy the things he wants most, from the people who offer the best bargain and at a time he considers the most advantageous.

Measure of Value: Money serves as a common measure of value in terms of which the value of all goods and services is measured and expressed. By acting as a common denominator or numeraire, money has provided a language of economic communication. It has made transactions easy and simplified the problem of

measuring and comparing the prices of goods and services in the market. Prices are but values expressed in terms of money.

Money also acts as a unit of account. In India, the unit of account is the 'Rupee', in USA the 'Dollar', in Japan the 'Yen' etc. As a unit of account, it helps in developing an efficient accounting system because the values of a variety of goods and services which are physically measured in different units (e.g. quintals, metres, litres, etc.) can be added up. This makes possible the comparisons of various kinds, both over time and across regions. It provides a basis for keeping accounts, estimating national income, cost of a project, sale proceeds, profit and loss of a firm, etc.

To be satisfactory measure of value, the monetary units must be invariable. In other words, it must maintain a stable value. A fluctuating monetary unit creates a number of socio-economic problems. Normally, the value of money, i.e., its purchasing power, does not remain constant; it rises during periods of falling prices and falls during periods of rising prices.

The secondary Functions are-

The relatively less important functions of money are called secondary functions. Since, these functions originates from primary functions, these are also called derived functions. The secondary functions of money are as follows: -

Standard of Deferred Payment: Money serves as the standard of deferred payment or units in which future or deferred payments are made. This function applies to interests, rents, salaries, pensions, insurance premium etc. The lending and borrowing acts are easily expressed in money. Due to the qualities of stability in value, general acceptability and durability, money is regarded best for these transactions.

Thus, money not only helps current transactions by functioning as a medium of exchange, but facilitates credit transaction (i.e., exchanging present goods on credit)

through its function of standard of deferred payments. But, to become a satisfactory standard of deferred payments, money must maintain a stable value over time.

Store of Value: The fourth function of money is to serve as a store of value because it is easy to spend and easy to store. Money serves as a store of value in the short run as well as long run. By performing the function of store of value, the money provides security to individuals to meet unpredictable expenditures and to pay debt that are in terms of money. In barter exchange system, all commodities could not be stored for a longer period of time. Money has a unique nature of durability and stability in value; thus it can be stored for a long time. This has introduced in people, a trend of making savings from the incomes for future purposes.

This function of money i.e. a store of value is necessary but not sufficient condition to term anything as money. Although, money functions as a store of value, but all things functioning as store of value cannot be termed as money. For instance, things like diamond, jewellery work as a store of value. But, these do not serve the primary functions of money, hence are not termed as money; therefore not used as money.

Transfer of Value: Money has general acceptability as a means of exchange. So it is easier to transfer value from one place to another. At present, money is stored in the form of bank deposits. Depositor can transfer the amount of money deposited in his bank account to the account of another person. It means it is easier to transfer value in the form of money. Money is a means through which transfer of value from one place to another has become easier and quicker. So transfer of value in the form of money through space continues to be important. For example, a businessman of Orissa who sells his property and goes to Delhi and settles down there is a case of transfer of value through space. Further, money serves as the function of transfer of value or purchasing power. People transfer value by selling commodities or property to others and by buying commodities and property from others. Money has facilitated the transaction of goods in distant places. For example, it is much easier to transfer one

lakh rupees through bank draft from person A in Amritsar to person B in Mumbai than remitting the same value in commodity terms, say wheat.

CONCEPTUAL QUESTION

Q. what is the meaning of maney?

Q. Explain Barter system?

Q. explain the benefit of store of value function of money?

Q. How sale and purchase activity became easy with the help of money?

Q. how deferred payment function of money helpful in growth of financial market?