NON COLLEGIATE WOMEN'S EDUCATION BOARD

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By – ANUJ KUMAR (ECONOMICS)
anuj1990srcc@gmail.com

PAPER – ECONOMICS

UNIT – 6 MONEY IN A MODERN ECONOMY

Definition of Money -

"Money can be defined as anything that is generally accepted as a medium of exchange and at the same time acts as a measure and as a store of value."

- Crowther

"The means of valuation and of payment as both the unit of account and the generally acceptable medium of exchange."

- Coulborn

"Money is a highly liquid financial asset that makes the real economy function smoothly by serving as a medium of exchange, a unit of account, a store of wealth and a standard for deferred payments."

- David Colander

Crowther has defined money on the basis of its medium of exchange functions which says that money can be anything that can be used for purchasing goods and services. Here, money is not defined in terms of what it is, like a piece of paper with specific instructions or like some specific metal. It is defined in terms of what it does or in terms of its specific functions like a medium of exchange or store of value.

John Hicks says that money is defined by its functions – "Money is what money does." i.e. anything is money which is used as money. Money must also possess general acceptability and has the legal power to discharge debts. Keynes in his General Theory followed the traditional view and defined money as currency and demand deposits.

Characteristics of Money –

In every economy money possess certain common characteristics. These may broadly be defined as follows –

1) Medium of Exchange –

Anything that is used as money must be accepted as a medium for exchanging goods and services. This characteristic of money facilitates sale-purchase of goods among people within an economy.

2) General Acceptability –

All people must accept money as means of payment of transactions and repayment of debts. No one must deny to take money for his/her goods and services.

3) Liquid Asset –

One of the most important characteristics of money is that it is always the most liquid asset. Here the liquidity of money means that it is the most rapid source to pay for any transaction.

4) Unit of account –

Means that the value of each good or service can easily be measured in the monetary unit. It acts as a yardstick of standard measure of value to which all goods can be compared.

Meaning of Near Money -

"Near money refers to those assets which cannot be used immediately to buy goods and services, but which can be converted into money very easily and without much loss in their values."

It means all the financial assets that can be used to buy goods and services after being converted into cash without any loss. Thus near money assets serve the store of value function of money and are convertible into a medium of exchange in a short time without loss in their face value. The following assets are treated as near money –

1) Time or Fixed Deposits –

Time deposits refers to those amount which are deposited in the banks for a fixed period. However in case of emergency FD can be withdrawn before the expiry of the maturity period but with loss in value.

2) Bill of Exchange –

It is an instrument of credit in which an individual is to pay a stated sum of money on a specified date which is never more than 90 days. A bill of exchange is not money by itself but is certainly money on the due date.

3) Treasury Bills -

Treasury bills are those instruments of credit on the basis of which government gets loans loan from the public for a short period. These bills can also be converted into money easily.

5) Shares and Debentures –

These are issued by firms and companies to the public to obtain loan for a long period. Holders of them can encash their shares easily by selling the same in the share market.

6) Life Insurance Policy -

A holder of a policy can obtain cash in the form of loan on his policy from the Life Insurance Company. Thus a policy is form of liquid asset which can be regarded as near money.

Functions of Money –

David Kinley classifies functions of money into following three categories –

1) Primary Functions, 2) Secondary Functions and 3) Contingent Functions.

1) Primary Functions –

Primary functions means the basic functions performed by money.

a) Medium of Exchange – It means that money acts as an intermediary for the goods and services in an exchange transaction. Double coincidence of wants was a major difficulty under the barter system. With the advent of money exchange has become well convenient. This function of money also separates the transactions in time and place because the sellers and buyers of a commodity are not required to perform the transactions at the same time and place.

b) Measure of Value –

Money is the standard for measuring value just as the metre is the standard for measuring length. The monetary unit measures and expresses the value of all goods and services in terms of price. Unlike barter, the prices of commodities are expressed in terms of so many units of rupees, dollars, francs , pounds etc. depending upon the nature of monetary units prevalent in a country. Further, money as a unit of account helps in calculation of economic units such as cost and revenues and profitability of business firms, gross national product, aggregate consumption and savings etc.