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INTRODUCTION

We are all familiar with money as we live in a monetary economy where money is used freely and widely in settlement of various economic transactions. We are so much accustomed to money now that it is difficult for us to imagine a modern society without money. It will be interesting to know why and how this money came into being. In this introductory unit, you will study how money came into being, its definition, role, importance, actions and defects.

PROBLEMS OF BARTER SYSTEM

Before the 'advent of money, the activity of exchange was carried out through barter system. In barter system people exchanged goods and services in their possession with goods and services available with others. For example, a farmer exchanged his surplus foodgrain (over and above his own needs) with the weaver for his surplus cloth. This activity helped both the farmer and weaver to satisfy their wants. The barter system of exchange worked well so long as human wants were simple and limited in number. However, in course of time human wants multiplied, which led to specialisation of occupations. This resulted in a lot of difficulties for exchange'through the barter system.

Consequently, need for a single and commonly acceptable medium of exchange was fell, This ultimately led to invention and evolution of money.

In the barter system people faced the following major problems :

I) **Lack of double coincidence or wants :** Barter requires double coincidence of wants. For instance, if 'A' has,a goat rind wants to exchange it for cloth. Then he must find some person who has surplus cloth to offer while, at the same time, needs the goat which is offered by a ‘A'. Such coincidences were easy when human wants were simple and number of goods produced were limited. But, as number of goods multiplied, such coincidences of,wants became both difficult and time-consuming. With the advent of money, this dificuity disappeared, as one can now sell product for money and then with the help of that money he/she can buy goods and services of his/her choice.

II) **Problem of a common measurement of value :** In the absence of money, value of every commodity was to be ascertained in terms of all other goods. For example, how much wheat or milk or salt or rice needs to be offered in exchange for one meter of cloth ? If there were, say, 10 goods in a society, people were required to determine and remember 45 values, while if there were 100 goods there would be 4950, such values. The number of exchange values required for transactions may be found by the expression, n(n - 1)/ 2 where 'n' is number of goods.

However, with money in circulation, vaiue of each commodity has to be expressed onIy in terms of money. Hence, in case of 100 goods, in a monetary economy people will have to know only 100 values.

III) **Loss due to sub-division of goods:** Many goods, if sub-divided, will lose their value partially or sometimes wholly. For example, a table or a refrigerator or a TV set cannot be sub-divided into parts as in doing so they will lose their value. In this situation, a person who wants to exchange his TV for five or six commodities, will find it difficult to get all these five or six desired goods from one perSon. Hence, he would need to sub-divide the TV into five or six parts, but by doing so TV will lose its vdue. On the other hand, if money is used as a medium of exchange, there would not be any such problem as money is perfectly divisible.

IV) **Difficulty in storage of wealth:** It is very difficult to save and create wealth in the absence of money as many of the goods lack durability, and all kinds of services are perishable and hence cannot be stored for future use. People could not think of storing something to provide against future cotltingencics as wealth stored in the form of goods like wheat, animal skin, etc., would not last long. However, money being durable has become a convenient form to save and store wealth.

EVOLUTION AND KINDS OF MONEY

As you know, at present money consists of coins, currency notes and deposit money. However, it has taken hundreds of years to acquire its present form. During the early part of civilisation, rnoney was in the form of commodity money like the cow. sheep, wheat, rice, tobacco, tiger teeth, elephant tusks, etc. The particular commodity chosen as money depended upon various factors like the climate, the level of cultural and economic development of the community, etc. In cold countries like Alaska and Siberia, animal skins and furs were used as money. In tropical countries elephant tusks and tiger jaws were used as money. In agricultural conmmunities domestic animals and goods of daily use took the form of money. However, with the passage of time their use as money was given up due. to lack of their durability, absence of a standard form, etc. The present day nroney has also passed through three stages : (i) metallic money, (ii) representative paper money, and (iii) credit money. The present inconvertible paper currency and other credit instruments acting as substitutes for legal money are only a recent development.

With progress of civilisation and economic advancement of societies, metallic coins made of gold, silver, copper etc., were used as money. These coins were of two types :

i) Standard coins or full-bodied coins, as they were called, because their face value aid intrinsic value were the same

ii) token coins, those coins whose face value was much higher than their intrinsic value.

Later on, currency notes were introduced to replace metallic coins primarily for two reasons :**firstly**, to economise the use of precious metals and avoid their wastage ; and **secondly**, for the sake of convenience of storage and transportation of paper vis-a-vis the coins. In order to build up the confidence of the public in paper currency, initially the currency notes took the form of representative notes. These rapresentative notes were simply substitutes for metallic money, i.e., convertible .into gold or silver coins on demand by the bearer. With increased use of paper money for transactions (due to expansion in production, population and monetized section of the economy) it became almost impossible to allow such convertibility. The present day currency notes are, therefore, no longer convertible into gold or silver coins and as such may be termed as flat money. Nowadays a sizeable portion of common money comprises this non-convertible paper currency.

Credit money is of more recent origin. People keep a part of their cash with baihks which they can withdraw at any time they like or can transfer to some other person through a bank cheque. The cheques and drafts, being mst convenient farm of transferring value, have come to be accepted as bmk manay, though they are not money proper as their acceptance is optional. However, they perform the most important function of money, viz. as a medium of payment.