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B.A. Economics

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Paper- MJC 3

Topic : The Demand for Money

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The Demand for Money.

09 The study of the equilibrium of the money market
 10 is essential to analyse the effects of the changes
 11 in the stock of money. "Money is an asset of the
 holding public." And it must have demand for
 it and supply of it and also have market for it.

12 The demand for money → derived by the general public

13 The supply for money → it comes from its producers,
 14 the govt. and the banking system.

15 The stock of money refers to its quantity at a given
 point of time.

16 Money is an asset i.e., demanded by the public
 17 in order to hold it, whatever the motive for
 18 holding it and whatever the length of the time
period for which it is held.

19 Demand for money is the sum of all money
 20 demanded by individual members of the public,
 whether households or firms.

• The Theory of the demand for money is mainly
 concerned with the following questions:

i) What are the determinants of the public's demand
for money and why?

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08 ii). Why does the public demand money?

09 • Nominal versus Real Cash Balances :-

10 → Nominal cash balances are money of the current
11 purchasing power of a unit of money (say,
a rupee). A nominal rupee is normally
12 always a rupee. It is simply monetary value of a rupee.

13 → Real cash balances are money of some base-year
14 purchasing power. The purchasing power of a
15 nominal rupee in terms of real goods and
16 services can vary from time to time with change
17 in the general price level. Then it is said that
18 real value (purchasing power) of a (nominal)
19 rupee has been changing over time.

16

$$\text{Real cash Balance} = \frac{M}{P}$$

17

18 where, $M =$ nominal money
 $P =$ price level

19 → Monetary Theory

20 These are two main streams of monetary Theory.

i) the neoclassical

ii). the Keynesian.

08 → The Neo-classical Theory :

09 The neo-classical theory of the demand for
10 money was put forward by the Cambridge
economists "Marshall" and "Pigou".

11 In Cambridge approach, the following demand
12 for money function was hypothesised:

$$\boxed{M^d = kY} \quad \dots (i)$$

13 where, M^d = amount of money demanded

14 Y = money value of national income

15 k = constant

16 Since,

$$Y = Py \quad \dots (ii)$$

18 where, P = general price level

19 y = real national income

20 therefore,

$$\boxed{M^d = k.Py}$$

(from eqn (i) & (ii))
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... (iii)

where, k = Cambridge " k "
↑

It gives us the demand for money per rupee of
"income per unit time". since, from eqn (iii) i.e.

$$K = \frac{Md}{Y}$$

- K = shows the proportion of money income public likes to hold in the form of money.
- Y = flow of money income per unit of time.
- Md = stock of money at a point of time.

By: afana