



14

MONEY AND ITS ROLE

The word “money” generates a lot of interest. In today’s busy life money has occupied a very important role. We need money to buy various types of goods in order to satisfy our wants. Similarly, we need money to avail various services such as- transport, communication, education, health, entertainment, home deliveries and so on. As a buyer, we pay money to buy goods and services and as a seller, we receive money by selling them. Normally, we pay or receive money in the form of paper currency and coins. But do you know that in ancient days people used to exchange good for good? This was called barter system. With passing of time, money replaced barter system. Why? To know all these continue reading this lesson.



OBJECTIVES

After completing this lesson, you will be able to:

- *understand the meaning of barter system;*
- *realize the need for money by the society;*
- *explain the functions of money;*
- *know paper currency and coins as types of money.*

14.1 BARTER SYSTEM

In the past when people were living in small societies and there was not much development as you see today, they were helping each other through barter system to mutually benefit one another. What is the meaning of barter system? **Barter system means exchange of one kind of goods and services for another kind of goods and services. There was no involvement of money in barter system.**

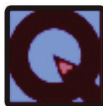


Notes

When one good is exchanged for another good without use of money, we call it trade through barter system. This was happening in ancient civilizations.

Some examples of Barter System are given below.

- (a) In the past traders from Europe used to trade goods such as fur and crafts in return for perfumes and silk from the Eastern part of the world.
- (b) In many tribal societies in India families used to exchange labour services in return for food and other labour services. For example, if a family needs labourers to harvest crop then another family would come to provide the service with the promise that it will get the same type of help in return either for harvesting crop or roofing house etc. This type of practice is still prevalent today in remote tribal areas of India.
- (c) People in various occupations, namely, farmers, artisans, cobblers, carpenters etc. used to exchange their products and services among themselves.



INTEXT QUESTIONS 14.1

1. Define barter system?
2. Give two examples of barter system?

14.2 NEED FOR MONEY

The barter system as described above is not prevalent now. In today's world nobody pays any good in exchange of another good. Everybody pays money to buy goods and services. So the following question arises - Why is the barter system not prevalent now? Why did the need for money arise? The answers to these questions lie in the fact that the barter system has many demerits as described below.

14.2.1 Demerits of barter System

The demerits of barter system are as follows.

1. A common problem with the barter system is **the lack of double coincidence of wants**. What does this mean? Double coincidence of wants mean that if one wants to exchange some good with another person then the latter must also be willing to exchange his good with the first person. Take for example, a person wants cloth and he has rice with him to offer in return. Then he can exchange rice for cloth with another person who has cloth and who also wants rice. In practical life, such situation may or may not arise. If the person who has cloth does not want rice, then exchange of rice for cloth will never take place and both the individuals cannot

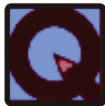


satisfy their wants. This is an example of lack of double coincidence of wants. So barter system will work when there is double coincident of wants, otherwise it will not work.

A related problem of barter system was that, one had to spend lot of time in searching for the person who was ready to exchange. However, in the early period of human civilization this was a very difficult task as there was no proper facility with regard to transport and communication.

2. **Lack of division of goods:** Certain goods are not physically divisible into small pieces. Suppose, a person possesses a cow and he wants items, such as cloth, food grains etc. Then how much of cow can be traded for cloth; how much of cow can be traded for food grains? It was very difficult to determine because, a cow cannot be divided into several pieces.
3. **Because of lack of divisibility of goods:** under barter system, it was difficult to equate the values of different goods which were traded because of **lack of common unit of measurement**. Taking the example in the previous paragraph, it will be very difficult to determine the amount of cow required to trade for some specific amount of food grains, or some yards of cloth. Also it sounds absurd. This happens because a cow can never become a common measure of value. This problem is same for all other goods.
4. Another problem of barter system is that a person must **store** a large volume of his own good in order to exchange for his/her desired goods with others on day to day basis.. Take the example of a farmer who has produced wheat. Obviously he will use some amount of wheat for his own consumption and keep some amount to get other necessary items by trading with others. If he wants furniture, then he will go to a carpenter who is willing to trade furniture in return of his wheat. Similarly, if he wants cloth, then he has to trade with a weaver who is ready to give cloth by receiving wheat and so on. So the farmer must construct a warehouse first to keep a stock of his wheat in order to carry out the transactions at the time of need for his desired good. But constructing and maintaining a warehouse was itself a very difficult task in early days of civilization.
5. Finally, a major problem of barter system is that, a good loses its original quality and value if it is stored for a long period. Many goods, such as salt, vegetables etc, are perishable. Hence, goods were never accepted for trading in future because they could not be used as store of value. This also implies that no good could be used for the purpose of lending and borrowing.

Due to above problems, the barter system could not continue for long. As human civilization progressed people realized that there has to be some common medium of exchange which can be easily carried, stored, and used to express value of a good. So money came into being. Hence the need for money arose due to the failure of barter system.



INTEXT QUESTIONS 14.2

1. Define double coincidence of wants?
2. Give two difficulties associated with barter system?

14.3 DEFINITION AND FUNCTIONS OF MONEY

Money is defined as something which is generally accepted by the society as a medium of exchange and which can act as unit of account, can store value and be used for repayment of debt.

The functions of money can be known from its definition. They are given below.

1. Medium of Exchange

The primary function of money is that it acts as a medium of exchange. This means that people can buy or sell goods and services with the help of money. Money is received by the seller who sells the good. Money is paid by the buyer who buys the good from the seller.

Example: You pay Rs. 10 to buy a pen. The seller receives Rs. 10 from you by selling the pen. So a pen is exchanged for Rs. 10.

2. Measure of Value

Another fundamental function of money is that it serves as unit of account or common measure of value. The value of a good is determined by multiplying its price with quantity sold in the market. Since the price is expressed in monetary units, the value of a good is also expressed in monetary term.

Example: Let price of rice be Rs. 20 per Kilogram. One bag full of rice weighs 25 Kilograms. Then the value of the bag of rice is Rs. $20 \times 25 =$ Rs. 500

3. Store of Value

Money also acts as store of value. How? As medium of exchange you can pay money to buy goods. This means if you have money, you have the power to purchase a good or a service. So money has purchasing power. The value of the good is contained in that purchasing power. Hence value of good is indirectly stored in money you hold. Similarly as a seller of good you receive the money which means value of good you sold comes back to you through money.

Example: Sushila has got some mangoes which she sells to a buyer for Rs. 250. This means a value of Rs. 250 was exchanged. The buyer, who purchased the mangoes, has the purchasing power to give Rs. 250 as value. Hence a value of



Rs. 250 was stored in the money received by Sushila as a seller. Sushila could not have stored mangoes but she can definitely store money which has stored the value of Rs. 250.

4. Making Payments in Future

We all indulge in lending and borrowing activities. Suppose, your friend requests you to give him Rs. 300 to purchase a book because he does not have any money at present. He promises to pay back the money after a week. If you agree with this and actually give him the money, then you will be called lender and your friend will be called borrower. As a lender, you can also charge some interest on the money you have lent to your friend. If you charge no interest, then your friend will pay you Rs.300 after a week. If you charge Re. 1 as interest, then your friend will have to give you Rs.301 after a week. Like your friend, there are many people who want to borrow money today to satisfy their present needs with the condition that they will settle the payment along with interest at some future date as agreed with the lender. This payment in future is acceptable in money only. We can also say that the borrower has deferred the payment under certain condition. So money has acted as a standard of deferred payment. Let us think for a while, that, your friend gives you the book which he purchased, instead of Rs.300 or 301. Then, will you accept this? Most probably not. Because after a week the book may have lost some value as it has not remained the same new book. But money will always be acceptable in a future date as it has stored the value.



INTEXT QUESTIONS 14.3

1. Define “medium of exchange”?
2. Give the meaning of value of good?

14.4 TYPES OF MONEY

14.4.1 Paper currency and coins

How money looks like? What is the form of money? Over the years the form of money has changed. You must have read in history that during the days of Kings, people used to trade by using gold coins, silver coins, copper coins etc. Before that, in the ancient days, in some places people used to hold money in the form of cattle, salt etc.

Now a days, no body holds cattle or salt to buy or sell goods and services. Keeping cattle is not feasible as it requires huge space and special environment. Salt is perishable and cannot be stored for a long time for the purpose of exchange. Hence after so many

MODULE - 5

Money, Banking and Insurance



Notes

Money and its Role

experiments over centuries, now people keep money in the form of paper notes and coins which are easy to carry. In India, we have paper notes in the denomination of 1, 2, 5, 10, 20, 50, 100, 500 and 1000. Normally they are called currency notes and named as Rupee (Singular) or Rupees (Plural). The symbol of Rupee is '₹'.

Money is paid by buyer or received by seller in the form of currency notes. For smaller denominations, we have coins called "Paisa", such as 50 paisa where 50 paisa is equal to half of one rupee. Now coins up to Rs. 10 denominations are in circulation in India.

You should know that the currency notes and coins which are in circulation are guaranteed by government of India. Otherwise anybody can make and misuse them.

Remember that currency notes and coins of India are valid only in India and not in other countries. Every country has its own currency. If you visit other countries, then you have to exchange Indian currency with the currency of the country you are visiting. The name of the currency of some of the countries of the world is given below.

- (a) Currency in USA is called dollar with symbol \$.
- (b) The European currency is called euro having symbol €.
- (c) Currency in United Kingdom is called pound having symbol £.
- (d) In Japan the currency is called Yen having symbol ¥.



INTEXT QUESTION 14.4

1. Give the meaning of currency note?



ACTIVITY

Make a list giving names of the currencies of France, Germany, China, Brazil.



WHAT YOU HAVE LEARNT

- Before money was invented people used to exchange goods for goods which was called barter system.

- There were many problems of barter system such as absence of a common measure of value, lack of double coincidence of wants, lack of space to store goods to exchange them for other goods etc. This prompted human society to discover money.
- The functions of money include medium of exchange, measure of value, store of value and used in making future payments.
- Money is exchanged in the form of paper currency notes and coins.



TERMINAL EXERCISE

1. Explain the working of barter system?
2. What are the main demerits of barter system?
3. Define money and state three of its functions?
4. Write a short note on currency notes in India?



ANSWERS TO INTEXT QUESTIONS

Intext Questions 14.1

1. Exchange of good for good is called barter system.
2. (i) 10 kg of wheat for 5 kg of sugar.
(ii) 8 kg of rice for a pair of shoes.

Intext Questions 14.2

1. Mutual exchange of goods between two persons.
2. (i) Lack of double coincident of wants (ii) lack of store of value.

Intext Questions 14.3

1. Anything which is generally acceptable for buying and selling goods and services.
2. Value of good = Price of the good × Quantity of the good.

Intext Questions 14.4

1. Currency note is a type of money.

