

# ECON 112

## INTRODUCTION TO ECONOMICS II

### Session 10 – Money



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# Session overview

- This session focuses on introduction to money which is used by every citizen in an economy for various purposes. The session essentially deals with the evolution of money, qualities of good money as well as the functions of money in an economy.

## **Goals and Objectives**

- At the end of the session, the student will
- Be able to explain the barter system of trade.
- Be able to define money
- Be able to outline the qualities of good money.
- Be able to describe the functions of money in the economy.
- Examine how the ability of money to perform its function can be affected by high inflation.

# The Barter Trade System

## What is the barter system?

**Barter** is a method of exchange by which goods or services are directly exchanged for other goods or services without using a medium of exchange

- Example:
- A horse may be exchange for a cow
- A lecturing service may be exchange for a root of cassava
- Concert show may be exchange for a bow of cola or two pieces of plantain.

# Problems of the Barter system

- **Double Coincidence of Wants:** It is necessary for a person who wishes to trade his good to find someone who is not only willing to buy good, but also possesses that good which the former wants.
- **Lack of Common Measure of Value:** This relates to the unavailability of a common unit in which the value of goods and services should be measured.
- **Indivisibility of Certain Goods:** Indivisibility of certain goods say a cow or sheep makes it difficult to operate.
- **Difficulty in Storing Value:** In this system trying to save an item or real capital as an asset for future consumption or use is likely to face the difficulty that during the intervening period the stored commodity may deteriorate or go bad.
- **Difficulty in making Deferred Payments:** Transferring payments that has to be made now to the future was inexistence.

# What is Money?

## What is Money: Definitions

1. **Money** is the stock of assets that can be readily used to make transactions.

2. **Money** is anything that is generally accepted in payment for goods and services



# The functions of Money

## ...a Medium of Exchange



- By definition, a Medium of Exchange is *anything that is used to determine value during the exchange of goods and services.*
- Money allows us to use systems of trade beyond the Barter System.
  - Bartering is *directly trading one good or service for another.*
- Your money acts as a common ground for determining value.

# Functions of Money cont'd...

## ...a Unit of Account



- Money can be used as a means to compare the values of goods and services.
- You can use the monetary value assigned to a specific good or service to compare it to one offered by a different provider.
- Money allows us to compare similar offers for goods and services to determine the best value.

# Functions of Money cont'd...

## ...a Store of Value



- Money is used to maintain the value of a transaction over time.
- If you receive monetary compensation for a good or service, the actual amount that you received does not change if you do not use it immediately.
  - You can spend, or exchange, your money at a later time without penalty.
- However, the functional value of the stored money may change over time due to other factors.



# Characteristics of Money

## What then is Money?

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- An item must have six key characteristics to be considered as “Money”.
- These Characteristics are:
  - Durability
  - Portability
  - Divisibility
  - Uniformity
  - Limited Supply
  - Acceptability

# Characteristics of money cont'd..

## Durability

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- Durability means that the item must be able to withstand being used repeatedly.
- Items that are considered Currency, *coins and paper bills used as money* meet this requirement.



# Characteristics of money cont'd...

## Portability

- Portability means that individuals are able to carry money with them and transfer it easily to other individuals.
- This is why coins and paper money have historically proved popular.



# Characteristics of money cont'd...

## Divisibility

- Divisibility means that the money can easily be divided into smaller units of value.
- Today, different coins and notes convey these fractional values.



# Characteristics of money cont'd...

## Uniformity

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- Uniformity means that all versions of the same denomination of currency must have the purchasing power.
- As an example, a 1928 \$2 bill will still buy \$2 worth of goods or services today.

