SECTION 11.1 WHAT IS MONEY?

- **Money** is anything that is generally accepted in exchange for goods or services.
- Many things, including tobacco, furs, playing cards, cigarettes, and whiskey have been used as money. But commodities have several disadvantages when used as money, the most important of which is that they deteriorate easily after a few trades. Precious metal coins have for millennia been used for money, partly because of their durability.
- Money has four functions: it is a **medium of exchange**, to facilitate transactions
- **Barter** is expensive and inefficient and generally prevails only where limited trade is carried out over short distances, which generally means in relatively primitive economies. The more complex the economy is (e.g., the higher the real per capita GDP), the greater the economic interactions between people, and, consequently, the greater the need for one or more universally accepted assets serving as money.
- Besides serving as a medium of exchange, money is also a **measure of value**. With money, a common "yardstick" exists so that the values of diverse goods and services can be very precisely compared. By providing a universally understood measure of value, money serves to lower the information costs involved in making transactions. Without money, a person might not know what a good price for a particular good is, because so many different commodities can be bartered for it. With money, there is but one price of a particular good, and that price is readily available as information to the potential consumer.
- Money serves as a **store of value**. It can provide a means of saving or "storing" things of value in an efficient manner. It is both cheaper and safer to store paper rather than wheat.
- Money is also a **means of deferred payment**. Money makes it much easier to borrow and to repay loans. With barter, lending is cumbersome and riskier. Fluctuations in the value of money can occur, and indeed, inflation has been a major problem. But the value of money fluctuates far less than the value of many individual commodities, so lending in money imposes fewer risks on buyers and sellers than lending in commodities.