# Money: Meaning, Forms and Functions

Money is a concept which we all understand but which is difficult to define in exact terms. This is because it fulfills many functions and comes in many forms each of them providing a criterion of moneyness. For this reason, Prof. Walker defines money as ‘‘Money is what money does’’. Since general acceptability is the fundamental characteristic of money, in simple words, money may be defined as anything which is generally acceptable by the people in exchange of goods and services or in repayment of debts.

One of the traditional definitions of Money calls it “a unit of account, a means of payment and a store of value”. Professor Coulborn defines money as “the means of valuation and of payment; as both the unit of account and the generally acceptable medium of exchange.” These are the functional definitions of money because they define money in terms of the functions. Some economists define money in legal terms saying that “anything which the state declares as money is money.”

## Forms of money

There are many forms of money. Following are the main forms of money.

**1. Metallic Money**: The money made of any metal such as gold, silver etc is called metallic money. It exists in the form of coins. Metallic money has the following two types:

**a) Full Bodied Coins:** When the face value of the coin is equal to the value of metal contained in the coin, the coin is called a full bodied coin. The gold and silver coins of old times are examples of full bodied coins.

**b) Token Money:** When the face value of a coin is greater than the value of the metal it contains, it is called token money. In our country, all the coins are token money.

**2. Paper Money:** Paper money refers to notes of different value made of paper which is issued by the central bank or government of the country. The paper money can be classified into following types:

**a) Representative Money:** Representative money is that money which is fully backed by equal metallic reserve. The holder of a bank note can easily get it converted into metallic (gold & silver) form on demand.

**b) Convertible Money:** It is the form of money which can be converted into gold, silver i.e. metallic reserves. But all these notes issued by the government are not fully backed by gold. The amount of gold kept by the government is a particular proportion of the notes issued.

**c) Inconvertible Money/fiat Money:** Inconvertible or fiat money is one that we have in our pocket and use in daily business. The face value of such money is more than the value of the paper. For Example, the value of the paper of 100 rupee note is almost nil but its purchasing power is equal to Rs.100. it has this value because it has been declared as legal money by the government. So it is generally accepted as a medium of exchange.

**3. Bank Money**: This is the most modern form of money this money is also called credit. It only consists of the following:

**a) Cheques**: A cheque is an unconditional order by the client on his bank to pay a certain sum of money to him or to any other party.

**a) Bills of Exchange**: A bill of exchange is an order by the drawer to the drawee to pay a sum of money to the drawer or to any other party.

**c) Draft:** Draft is a cheque drawn by a bank on its own branch or the branches of another bank requesting it to pay on demand a specific amount to a person named on it.

**4. Legal Tender Money:** The money that a person accepts as a means of payment and in discharge of debt is called legal tender notice. All the notes and coins issued by the government and the central bank are legal tender money. Legal tender money is of two types:

**a) Limited Legal Tender Money**: The money which can be used a means of payment up to a certain limit is called limited tender money.

**b) Un-limited Legal Tender Money**: The money that can be used a means of payment up to any limit or amount.

**c) Non legal tender money:** Non legal tender money implies optional money which a person may or may not accept as a means of payment. Bank money in the form of cheques, bills of exchange, promissory notes is not legal tender money therefore they represent Non legal tender money.

**5. Plastic Money**: Plastic money means the credit cards, smart cards. Plastic cards which have specially printed set of characters. Recently the use of this money has increase.

**6. Standard Money:** Standard money is that in which the value of goods as well as all other forms of money are measured. Thus, in India all prices of goods are measured in terms of rupees. Moreover, the other forms of money such as two-rupee notes, ten rupee notes, hundred rupee notes and one half rupee coin are expressed in terms of rupees. Thus rupee is the standard money of India. Standard money is always made the unlimited legal tender money.

**7. Near Money**: A type of money which can easily be converted into money. It included deposits, government bonds, printed bonds etc.

**8. Fiduciary Money:** Fiduciary money depends for its value on the confidence that it will be generally accepted as a medium of exchange. Unlike fiat money, it is not declared legal tender by the government, which means people are not required by law to accept it as a means of payment. Instead, the issuer of fiduciary money promises to exchange it back for a commodity or fiat money if requested by the bearer. Examples of fiduciary money include cheques, banknotes, or drafts

**9. Commodity money:** Commodity money is a commodity that has intrinsic value and is used as a medium of exchange. Salt, animal, gems, beads, gold, silver etc. are examples of commodity money.

## Functions of Money

In general terms, the main function of money in an economic system is to facilitate the exchange of goods and services and help in carrying out trade smoothly. Money performs a number of primary, secondary, contingent and other functions which not only remove the difficulties of barter but also oils the wheels of trade and industry in the present day world. We discuss these functions one by one.

### 1. Primary Functions:

The two primary functions of money are to act as a medium of exchange and as a unit of value.

**a) Money as a Medium of Exchange:** By serving as a medium of exchange, money removes the need for double coincidence of wants and the inconveniences and difficulties associated with barter. The introduction of money as a medium of exchange decomposes the single transaction of barter into separate transactions of sale and purchase thereby eliminating the double coincidence of wants. Thus money gives us a good deal of economic independence and also perfects the market mechanism by increasing competition and widening the market.

As a medium of exchange, money acts as an intermediary. It facilitates exchange. When acting as the intermediary, it helps one good or service to be traded indirectly for others. It helps production indirectly through specialization and division of labor which, in turn, increase efficiency and output.

**b). Money as a Unit of Account or Measure of Value:** Money serves as a unit of account or a measure of value. Money is the measuring rod, i.e., it is the units in terms of which the values of other goods and services are measured in money terms and expressed accordingly Different goods produced in the country are measured in different units like cloth m meters, milk in liters and sugar in kilograms.

Without a common unit, exchange of goods becomes very difficult Values of all goods and services can be expressed easily in a single unit called money Again without a measure of value, there can be no pricing process. Without a pricing process organized marketing and production is not possible. Thus, the use of money as a measure of value is the basis of specialized production.

**2. Secondary Functions:** Money performs the following three secondary functions which are as follows**:**

**a) Money as a Store of Value:** As a secondary function, money acts as a store of value. Wealth can be stored in terms of money for future. It serves as a store value of goods in liquid form. By spending it, we can get any commodity in future. People therefore normally wish to keep a part of their wealth in the form of money because savings in terms of goods is very difficult. Clearly money is the best form of store of value. Wheat or any other product which will command a value cannot be stored for a long period.

**b) Money as the Standard of Deferred Payments:** Deferred payments are payments which are made some time in the future. The use of money as the standard of deterred or delayed payments immensely simplifies borrowing and lending operations because money generally maintains a constant value through time. Thus, money facilitates the formation of capital markets and the work of financial intermediaries like Stock Exchange, Investment Trust and Banks. Money is the link which connects the values of today with those of the future.

**c) Money as a Transfer of Value:** Since money is a generally acceptable means of payment and acts as a store of value, it keeps on transferring values from person to person and place to place. A person who holds money in cash or assets can transfer that to any places.

**3. Contingent Functions:** Money also performs certain contingent or incidental functions which are as follows:

**4. Other Functions:** Money also performs such functions which affect the decisions of consumers and governments.

**a) Helpful in making decisions:** Money is a means of store of value and the consumer meets his daily requirements on the basis of money held by him. In this way, money helps in taking decisions.

**b) Money as a Basis of Adjustment:** To carry on trade in a proper manner, the adjustment between money market and capital market is done through money. Similarly, adjustments in foreign exchange are also made through money.