Introduction to Economics

Topic 8 (Macroeconomics):
Financing the economy

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Overview

1. Money: concept, kinds and functions

Goal: The various roles money plays and the many forms it takes in the economy.

1. Money: concept, kinds and functions

Household’s wealth

A household’s wealth is the value of its accumulated savings.

The economist’s definition of money doesn’t include all forms of wealth.

The cash in your wallet is money; other forms of wealth – such as cars, houses, and stock certificates – aren’t money.

Household’s wealth

Forms of wealth…

Real assets: Physical or identifiable assets such as gold, land, equipment, patents, etc.

Financial assets: An asset that derives value because of a contractual claim. Stocks, bonds, bank deposits, and the like are all examples of financial assets (financial assets do not necessarily have physical worth).

What distinguishes money from others forms of wealth?

What is money?

Money is any asset that can easily be used to purchase goods and services.

Note that an asset is liquid if it can easily be converted into cash. Money consists either of cash itself, which is liquid by definition, or of other assets that are highly liquid.

Some definitions…

Currency in circulation is cash held by the public.

Checkable bank deposits are bank accounts on which people can write checks.

Electronic (plastic) money: MasterCard, Visa,…

Roles of money

[1] Medium of Exchange

[2] Store of Value

[3] Unit of account

Types of money

Today money is pure **fiat money**; so coins and notes (currency in circulation).

Quiz – *lawful money? – legal tender? – commercial bank money?*

Quiz - *What about the money supply?*

The money supply

$$\boxed{\mathbf{M = EMP + Deposits}}$$

EMP: liquid assets held by the public

Quiz – *Do you know any other monetary aggregate?*

The money supply

A) **Fiat money** (currency)
Paper + Coins

- Currency (cash) in banks
- Liquid assets held by the public / Currency in circulation(EMP)

B) **Bank Money**
Deposits

- Demand deposits
- Saving deposits
- Time deposits

D

Money Supply

(M)

Money supply (M)- quantity of money in circulation in an economy (EMP + D)

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