



Module: English

Branch: Commercial Sciences

Level: Second year Bachelor

Lecture 02: The History and Evolution of Money

To understand the effects of money on the economy, we must understand exactly the origin and evolution of the money.

Objectives

After reading this unit, you should be able to:

- Elaborate the origin of money
- Discuss the evolution of money
- Identify the meaning and inconveniences of barter system

1- Origin of Money

Money is a human invention to overcome the inconveniences of barter system. In the words of Geoffrey Crowther in his book *An Outline of Money*, money is one of the fundamentals of all man's inventions. Every branch of knowledge has its fundamental discovery. In mechanics, it is the wheel; in science, fire; in politics, the vote; and similarly, in economics, money is the essential invention on which all the rest is based. The word *Money* has been derived from the Latin word *Moneta* which refers to the name of the Roman Goddess Juno, in whose temple at Rome coins were being minted. Money plays an important economic role in all societies. It renders invaluable economic services without which the development of modern industrial societies would hardly be possible. According to P.F. Drucker, in modern industrial society, money influences, moulds and directs economic life; changes in the money sphere cause changes in the real economy. In modern societies, nearly all aspects of economic life involve the use of money. The purchase of goods, services and claims; the settlement of debts; and payment of taxes are generally effected with the agency of money. Our individual economic well-being depends upon the amount of money income we receive for the goods we produce; or the services we render and the goods and services our money income will buy. For payment purposes, we always carry with us some money in the form of coins and notes, or cheque books with which we can order the transfer of deposit money that we have in commercial banks. Money is indeed familiar to every one of us. The complex economies of the modern world would be unable to function without the use of money. If money is not employed, production or distribution must be completely planned by the State or all transactions must be carried on by barter, i.e. goods or services must be exchanged for other goods or services. Money is a commodity the primary function of which is to facilitate the exchange of goods and services.

2- The Evolution of Money

The development of economic relations (production, consumption, distribution...) contributed to the emergence of money as an economic phenomenon, from the stage of self-production linked to

the phenomenon of self-satisfaction to the stage of specialized production linked to the need for exchange.

A-The stage of the self-sufficiency economy (non-exchange economy):

At this stage, individuals produce a set of goods and services that are relatively sufficient to satisfy their needs, regardless of the existence of economic relationships with other individuals. As for the distribution process, it was carried out automatically and internally according to the prevailing social systems, so that the individual resorted either to picking fruits and hunting animals sufficient for his consumption, or the individual lived in a group that adhered to a set of organizational rules agreed upon regarding the process of production and distribution among members of one group. This exchange took place occasionally and at intermittent times, as members of the group gathered in one place for long periods of time on religious occasions, for example. Exchange also occurs on some special occasions (marriage, funerals), which require the participation of others on the basis of mutual aid, and such a type of deferred exchange includes a kind of commitment to return the favor or help.

B- Exchange stage based on the barter system:

After the end of the first primitive state of man in which he lived by collecting and reaping fruits, individuals formed into groups that had a minimum level of organization that ensured a kind of need satisfaction, and with the diversity of individuals' needs, a kind of specialization in production was necessary. As development continued, exchanges began little by little.

C- Money swap stage:

Money did not appear directly, but rather barter developed until it was divided into buying and selling. This gradual development led to the emergence of money as a means of exchange, and the bartering process was divided into two processes: selling for money and then using the money in the purchase process.

In the first stage, individuals resorted to using one of the commodities as a measure of values. Some individuals, for example, chose livestock to attribute the values of other commodities to them. In general, the measure of values is usually something widespread. Here it can be said that something of the nature of money has appeared. With the persistence of the basic problem of barter, which is the difficulty of achieving double compatibility of desires, individuals resorted to exchanging their commodity for this commodity (the widespread commodity) and then using this commodity to get what they want. Thus, widespread commodities as money intervened in the exchange process, mediating the barter process and dividing it into two processes: exchanging the first commodity for commodity money and then using the commodity money to obtain the second commodity (buying and selling). Thus, money recognized a new function, which is that it is an intermediary for exchanges. At a later stage, the need to store values helped choose money from storable materials, which is available in gold and silver metals. The form that this instrument took has evolved according to the development of the swap system.

3- Barter System:

A- Meaning:

By barter we mean direct exchange of one commodity for another commodity. In other words, barter means the direct exchange of goods for goods without any mediation of money. Under the barter system, the exchange process is very simple and direct. For example, rice may be exchanged for wheat; scooter may be exchanged for bike; cloth may be exchanged for chair and so on. In the early stages of civilization, human needs were simple and every individual was able to produce all that he needed to maintain himself. This was followed by specialization, whereby people settled down in different occupations, depending on their skills and the availability of

resources. Against this backdrop if we look at the barter system, a person having plenty of one commodity, say, food, exchanging it with another person having plenty of another commodity, say, cotton, seems to be an uncomplicated process. However, barter system is not an unmixed blessing. The barter system has its inconveniences or defects or difficulties or shortcomings as well

B- Inconveniences of Barter System:

The following are the inconveniences of barter system:

- Lack of Double Coincidence of Wants

Under the barter system, no exchange can take place unless the wants of two persons coincide. In other words, double coincidence of wants is a necessary condition for the exchange of commodities under barter system. A man must find another person who has what he wants and wants what he has. This is not easy. For example, a carpenter has a chair and he wants cloth. He must go in search of weaver who has cloth and he who wants chair. Suppose the carpenter meets the weaver who has cloth, but the weaver does not want chair and he wanted again food grains, then the carpenter cannot exchange his chair with the weaver. Here, wants of the carpenter and the weaver do not coincide. Lack of coincidence of wants between the carpenter and the weaver will hinder the exchange of chair for cloth. This involves wastage of time, cost and energy. Thus the lack of double coincidence of wants is the first and the foremost inconvenience of barter system.

- Lack of Common Measure of Value

Another inconvenience of barter system is that there is no common measure of value of commodities. In the primitive society, there was no common commodity to measure the value of commodities. Then the people measured the value of commodities in commodities only. Suppose that a carpenter and a weaver wanted to exchange chair against cloth, they must first of all decide in what proportion the two goods should be exchanged. This was not easy as the transactions were isolated. Since there was no common measure of value, the exchange ratio would be fixed in an arbitrary manner. It was clear that where each exchange was an isolated transaction, one party should suffer.

- Lack of Divisibility of Goods

Some commodities cannot be divided into parts without reduction in their value. Examples are cows, horses, goats and camels. All commodities are not of equal value. Suppose that a person has a cow and wants one cotton saree. Let us further assume that one cow is equal in value to 50 sarees. It is not easy to cut the cow to secure one saree. If he gives a cow for one saree, he will lose heavily. So exchange is not possible. Thus lack of divisibility of goods is another inconvenience of barter system.

- Lack of Common Store of Value

Under the barter system, it is very difficult to store wealth for future use since wealth consists of perishable commodities. People also have no means to store their wealth. Moreover, the store of value in terms of real wealth involves cost and, further, the problem of storing the commodities sometimes also involves a heavy loss. Thus lack of common store of value is another inconvenience of barter system.

-Lack of Deferred Payments

Under the barter system, it is very difficult to make payments in the future. Debt contracts may not be possible due to disagreements between the two parties involved in the exchange process because of several reasons. Deferred future payments are impossible under barter system because of the following reasons:

- The quality of goods and services to be repaid.
- The two parties would be unable to agree on the specific commodity to be used for repayment.
- Both parties would run the risk that the commodity to be repaid would increase or decrease the value of the commodity over the duration of the contract.

- Lack of Specialization

Under the barter system, a high degree of specialization cannot be achieved as the production system is such that each person is a jack-of-all trades and master of none.

- Difficulty of Exchanging Services

Under the barter system, the exchange of services would be far more difficult than the exchange of goods. For example, how much would be the services of a teacher, a priest, a doctor or a lawyer paid? How would these persons be paid?

-Difficulty of Transporting Goods

Under the barter system, it is inconvenient to carry bulky goods from one place to another for exchange purposes.

- Inconveniences of Borrowing and Lending

The barter system is inconvenient as regards borrowing and lending. For example, if a person borrows a pair of goats for a year to two, he cannot return the same pair of goats, because by that time, they would either become old, slim or even die. Therefore, it is not possible to return the same pair of goats in original form after lapse of time. So borrowing and lending become extremely difficult under barter system.

References:

- E.Narayanan Nadar. Money and Banking. Asoke K. Ghosh, PHI Learning Private Limited, Rimjhim House 2013