

MODULE ONE

Money: Its Functions and Characteristics

1.1

The Economy: Its Role

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Specialization, Trade, and the Barter System: Setting the Stage for Money

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The Role of Money

1.4

The Characteristics of Money

Many People Think Economics Is All About The Study Of Money, But ...

Many people think that the study of economics is all about money – but that is not the case. The job of our economy is primarily to enable the efficient production, distribution, and consumption

of goods and services that are wanted by people in our society. The primary job of money is to serve as a tool to help the economy do its job. Therefore, to understand the role of money, we first need to understand the role of an economy. Let's begin there.

1.1 The Economy: Its Role

The Drivers of Production – Peoples' Needs and Wants

People have many needs and wants – cars, tables, taxi rides, medical services, computers, doors, pens, tires, theatres, and on and on and on. A “need” is something you feel you *must have*. A “want” is something you would *like to have* to make life easier, more comfortable, more enjoyable.

Needs and wants will differ from person to person. You may *want* a smartphone. Someone else may feel they *need* a smartphone. What's the difference? Why does the distinction matter? One reason it matters is because your feelings, and the intensity of your feelings, will affect your money decisions. If you feel that you *need* something you are more likely to commit to buying it – and it is likely you will be more willing to pay a higher price for it. You are also likely to be willing to trade-off other things to get it.

Box 2:

Economic Insight: Needs and wants differ from person to person



Businesses Particularly Like It When You Feel You NEED Their Product or Service

Businesses therefore like it when you feel you *need* what they are selling. Advertising is a means by which businesses aim to inform you of their product or service – and encourage you to buy it. But they often use advertising to aim at consumers' emotions – and how they feel about their product or service – to try and move consumers perspectives or their good or service from being a want to being a need. If that happens, consumers are most likely to buy – and possibly buy on a regular basis.

The Economy's Job is to Respond to Needs and Wants

People need and want goods and services for two primary reasons: (i) to survive – which involves such necessities as food, clothing, and shelter, and (ii) to enhance the enjoyment and

Box 1:

Economic Insight: Money is a tool to help the economy do its job

Box 3:

Economic Insight: Businesses like it when you feel you *need* what they

comfort of life – which involves things that simply make life better. The economy's job is to try to respond to these desires – people's needs and wants – with goods and services. At the same time, by producing goods and services, the economy creates opportunities for people to work and be employed by businesses, governments, and other organizations involved in production. Opportunities exist and evolve for entrepreneurs to see the potential to start and operate businesses to respond to changing or expanding needs and wants.

BOX 4

In Using Resources to Produce Goods and Services, Opportunities are Created to Earn Incomes

Many of the resources used in production – land, natural resources and raw materials, capital equipment, and labour – are owned by individuals and companies. In return for the use of their resources, people are able to earn incomes. The incomes earned from production then enable people to buy the goods and services that are produced. If you are getting the impression of somewhat of a “circular flow” here, you are right. Resources flow into the business sector to produce goods and services. In return, incomes are paid for using the resources and this enables people to buy the goods and services produced.

Growth is Important for an Economy to Create Jobs and Incomes

BOX 5

Over time, the hope is that the economy will grow and produce more goods and services, create more opportunity, more jobs, more incomes and help Canadians achieve a higher level of well-being. A key role of the Bank of Canada, as we will see, is to try and support economic growth and the improved well-being of Canadians.

But There Are Other Things That Are Important Too

At the same time, as efforts are made to achieve economic growth, there are a number of other concerns that also have to be addressed and assigned priority. One is fairness. As production occurs, what will affect and determine who gets those goods and services? Is distribution, and access to the goods and services, equitable and fair? That's one concern.

There is also the consideration of the environment. Is the current production of goods and services negatively affecting the environment? If so, can production methods be changed so that does not occur? Better yet, can the means and methods of producing goods and services actually help improve the environment? These are just two of the factors that have to be considered when it comes to economic activity.

Why Can't We Have Everything in Life We Want?

BOX 6

As we noted, an economy's job is to respond to people's needs and wants with goods and services. But although people's needs and wants may seem unlimited, people learn very early in life that they can't have everything they want. The economy does not satisfy everyone's needs and wants. Why?

The main reason is that, unlike the potential for peoples' needs and wants, the resources available to use in production are limited. Our resources – our available natural resources, labour and capital (plants, factories, equipment), along with existing technology – are limited. If our resources weren't limited, every society could produce everything that everyone wanted. We could all have ten computers, five houses, twelve cars, three boats, and so on. But there are only so many trees, so many minerals, so many people.

Our Limited Resources Generate the Basic Economic Problem ...

The limitations imposed by our resources pose an economic challenge to our society. We have to decide how to use our available resources in the best way possible to produce goods and services in response to peoples' needs and wants. That is the "basic economic problem." Since we can't have everything we want, what will be produced? And, in making those decisions, we have to consider the tradeoffs that will be made. After all, if a resource is used for one purpose, it can't be used for another. Each decision made about the use of a resource has an "opportunity cost" – the loss of the next best thing that we could have produced with that resource. Options. Decisions. Choices. Tradeoffs. That is what economics is about.

BOX 7

... and the Three Basic Economic Questions

All of us face economic choices, decisions, and trade-offs. But what are the key decisions facing an economy? The key decisions are:

1. Given the available resources and options, what goods and services will be produced?
2. Which resources will be used and how will they be combined to produce goods and services?
3. How will the goods and services produced be distributed to those who need and want them?

These three decisions are sometimes summarized as "What? How? And for whom?" – and these are the key questions and challenges facing any economy.

BOX 8

How Do We Measure An Economy's Success? Standard of Living and Quality of Life

Knowing the challenge faced by an economy, there is another question. How do we measure

how well an economy is doing its job? There are two common ways of looking at that. One way is to look at our *standard of living*. The other is to consider our *quality of life*.

To arrive at a measure of our standard of living, we use math and make a calculation. We add up the total value of all the goods and services produced and divide that total by the number of people to get the output per person. That gives you a sense of how much wealth, on average, is being produced, per person, by the economy. The following shows the dollar value of output per person produced in the Canadian economy in 2015 and 2016:

2015 GDP per capita: \$??

2016 GDP per capita: \$??

BOX 9

This shows us that the total dollar value of output produced in Canada in 2016 was higher than that in 2015. Does this mean Canadians were better off in 2016 and was Canada's standard of living higher? The reality is, we need more information to know. Why?

BOX 10

Prices Have to Be Considered – And Factored Out to Compare *Real Information*

When we add up the value of all the goods and services produced by our economy, we tend to add them up according to their monetary value, that is, their price. That's where we have to be careful. Suppose in 2015 a hockey stick cost \$60. Then suppose that in 2016 that same hockey stick cost \$65. If we add up the value of hockey sticks produced in 2016 and compared that with the value of sticks produced in 2015, and get a higher value, that figure may be partly due to higher prices – not that more hockey sticks were produced.



That creates a challenge for us if we want to learn whether more hockey sticks were actually produced from one year to the next. Why do we want to know that? Well, if more sticks were actually produced, that means more resources were used. That could mean more labour was used – and that means possibly more jobs – and more income to Canadians. It could mean more wood was purchased – helping the wood manufacturers. It could mean more fibreglass was purchased – helping the manufacturers of fibreglass. And so on.

So it is important to know if more hockey sticks were produced – or whether the higher value was primarily, or totally, a result of higher prices. Let's use our example for further illustration with some bigger numbers. Suppose in 2015, 500,000 hockey sticks were produced and sold at an average of \$60 each. The total value of hockey sticks produced is:

$$500,000 \times \$60 = \$30,000,000$$

Then, suppose that 490,000 hockey sticks were produced and sold at an average price of \$65

in 2016. The total value of hockey sticks produced is:

$$490,000 \times \$65 = \$31,850,000$$

If you simply looked at the total value of hockey sticks produced, you might think that more hockey sticks were produced in 2016 – when, in fact, fewer were produced. The higher number was due to the higher average price. To know whether more hockey sticks were produced, you would have to factor out the change in price.

We aren't going to do that at this point – but it is very important to know that one has to do that if you want to compare production and output from one year to another. And that applies to trying to measure the output of all goods and services in an economy – which we want to do if we want to measure whether an economy has actually grown from one year to another.

Measuring and Comparing An Economy's Output Over Time is Important – Here's Two Reasons Why

Measuring whether an economy has actually grown from one year to another, and over time, is something we want to determine whether a society's "standard of living" is changing – and whether it is improving over time.

Real GDP in Canada over time

<http://www.statcan.gc.ca/tables-tableaux/sum-som/l01/cst01/econ05-eng.htm>

2016	1,796,178
2015	1,770,196
2014	1,753,683
2013	1,709,820
2012	1,668,524
2011	1,273,984
2010	1,248,739
2009	1,209,948
2008	1,201,030
2007	1,164,057

Measuring the changes over time in output in an economy can also provide policymakers with information that can affect their policies. How well is the economy doing compared with its overall ability? Over time, is more slack showing up in the economy with more and more room to grow? Or is the economy moving closer to the limits of its productive capacity? That kind of information is very important to those who make policy decisions that can affect spending and output in the economy – as we will see.

So measuring an economy's level of output over time is important to policymakers. And measuring an economy's level of output, and dividing that by the population, and factoring out the effect of price changes, provides a measure our "standard of living" – and that is one way to measure how well an economy is doing its job. Is our standard of living improving over time – or is it declining?

The following shows the measurement of Canada's standard of living over recent decades.

CHART HERE

Standard of Living Tells Us Nothing About Distribution – or Fairness

It is important to remember that when we calculate the standard of living in a nation, that doesn't tell us anything about how the wealth generated by the economy is distributed to people. In 2016, the average household income in Canada was \$30,474 a year. But what does that tell us? It doesn't mean every household earned \$30,474 last year. It tells us that, on average, a Canadian household earned that amount.

BOX 12

It is interesting to note that, according to the Organizations for Economic Cooperation and Development (OECD), in 2016, the top 20% of income earners in Canada earned about five times more than those in the lower 20%. The distribution of wealth and income is certainly not equal in Canada. Nor is it equal in other countries around the world. The other question to consider is – is the distribution fair and “equitable?” Societies – and the people in those societies – can face choice and decisions as to whether the distribution is equitable – or whether efforts and policies would be put in place to make the distribution more equitable. This is particularly the case in democracies where people can exercise their views by voting and choosing among policies and parties. In some nations, the people do not have a say in the distribution of wealth.

BOX 13

Standard of Living Gives Us a Measure of Material Well-Being – But There is More to Life Than That

So measuring standard of living gives us a picture of an “average” – and it can be used to measure how “on average” an economy is doing over time. But how income is distributed is important – and something that all societies need to consider – and address as they deem appropriate.

There is another way of measuring how well an economy is doing. You've probably heard the expression: “Money can't buy happiness.” This phrase is saying that there are other considerations in life besides material well-being. These other things in life include such things as peace, freedom, happiness, environmental quality, and so on. To assess a society's well-being in this broader sense, we need to look at something else – something that gives us a measure of overall “quality of life.”

BOX 14

Measuring Quality of Life is More Difficult

Measuring the quality of life in a society is much more difficult than measuring the standard of living. Measuring standard of life is a mathematical calculation. But how do we measure the value of feeling free, having good health, having a good education, being at peace, breathing clean air, drinking clean water, enjoying parkland, and feeling happy? Efforts are made to do so [see box 

Refer to Box  to see what the statistics show in terms of our quality of life. Certainly compared to other countries around the world, Canadians enjoy a very high quality of life – perhaps, in some ways, the highest quality of life. That is something which we can enjoy – and in which we can take pride – and is something we need to work to protect.

The primary challenge for any economy, then, is to decide how to use available resources to produce and distribute goods and services in response to needs and wants. And that's where money can help. Let's see how.

1.2 Specialization, Trade, and the Barter System – Setting the Stage for Money

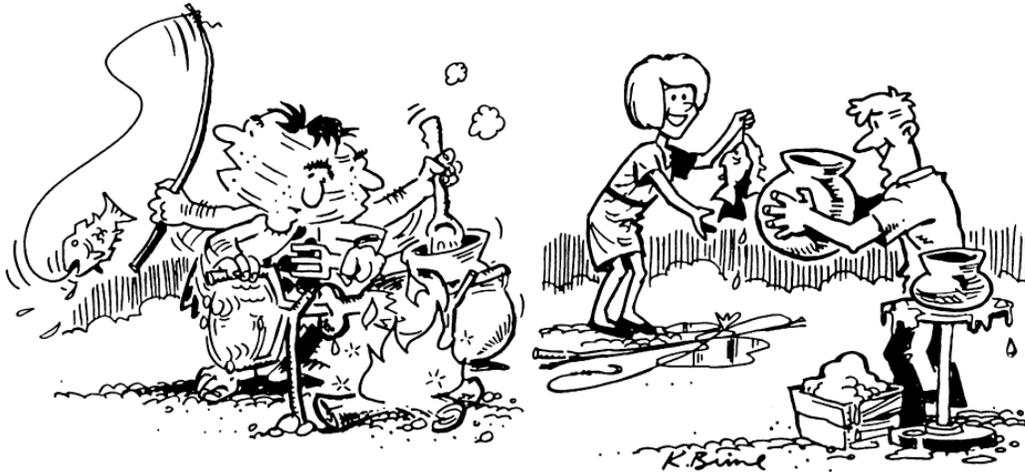
In Early Societies, Needs Were the Focus and Priority

People in early civilizations were not particularly concerned with thoughts about money. They were too busy worrying about survival and dealing with their basic needs of food, clothing, and shelter. But, over time, societies advanced and became more developed. The initiative of people led to new discoveries, new technology, new resources – and the opportunity to develop and provide new products and services. Increasingly, people benefitted from these changes and were able to think about things they might want – above and beyond what was needed.

Then “Specialization of Labour” Helped to Change Everything

As a result of these changes, a major evolution occurred that helped to increase the production of goods and services – in quality, quantity, and variety – and improve the efficient use of our resources. That development was specialization.

What does that mean? With specialization, rather than trying to do everything independently, people began to become interdependent – to cooperate, collaborate, work together – and specialize in certain skills, talents, jobs, and careers. Rather than trying to be a “jack of all trades,” people began to develop specialized skills and used those skills to produce particular goods and services.



As people specialized, they became better at what they did. More and better products could be produced. More and better services could be offered. This helped societies to achieve improved economic development and progress.

With Specialization Came a Challenge – and an Answer – Trade!

However, as specialization occurred, a challenge arose. If individuals specialized in one or a few areas of production, how were they to acquire the other things that they needed and wanted – the other things that they didn't produce?

BOX 15

For example, suppose a person decided to specialize in farming and thereby was able to provide food for one's own use – and also enough so that there was additional food beyond their own needs – a “surplus” amount of food that could be made available to others. Farming provided food – but what about all the other things that the farmer would need to acquire beyond food?

The answer was to trade with others – others who were able to produce a surplus of the other things the farmer needed and wanted.

If everyone who specialized in an area of economic activity was able to produce a surplus beyond their own needs, the surpluses produced were available for trade. A consequence of specialization, therefore, is the need for trade. The farmer produces surplus food – beyond the needs of the farmer's family. The farmer can then trade the surplus food with those who need food and have other things in surplus that the farmer needs – e.g. clothing, dishes, tools, and so on.

BOX 16

Specialization Helped to Improve Productivity

The more *productive* the farmer – that is, the more the farmer is able to produce using the available resources – the greater the surplus that the farmer can produce for trade and the more the farmer can acquire from others. Specialization usually leads to people becoming more skilled and able to produce more wealth for the economy. The wheels of economic progress begin to turn. Innovation. Invention. Creativity. Hard work. Productivity. Progress.

Through specialization and trade then, more can be produced, better goods and services can be produced, and the standard of living in a society can improve.

Specialization is associated with the concept of the division of labour, that is, labour becomes specialized and concentrated on certain activities. Rather than trying to do everything, or many things, a person concentrates his or her labour skills on one activity or on just a few activities.

As Economies Progress, More Opportunity is Generated

In our early history, the degree of division of labour was limited because there were still relatively few producers with a limited number of goods and services being produced. Over time, though, more and more producers, and more and more goods and services, have enabled more opportunities for different careers, different jobs, and more areas of specialization. Our economy has grown and evolved so that, in today's economy, we have a vast array of jobs, careers, and occupations from which people can choose to focus upon for their area of specialty.

The Benefits of Trade Preceded the European Arrival in North America

The economic advantages of specialization and trade have been recognized for a long period of time. Indeed, when the Europeans first came to North America, they discovered that the Indigenous people were already very adept and skillful at trading. The Indigenous people were particularly good at hunting and trapping and were able to obtain furs beyond their needs. They could, therefore, provide furs for trade with the Europeans. The Europeans were anxious to trade for furs as they were valuable back home in Europe. In return for furs, the Indigenous people received goods from the Europeans, often goods they had never seen or known of before.

There are many issues discussed today regarding the interaction of European explorers and settlers with the Indigenous peoples of North America. There were some benefits that came to North America with the arrival of the Europeans – but there were also some problems. We aren't going to go into a discussion here on the benefits and problems. That would require a whole other book. We do know, though, that the fur trade was very significant to the early development of Canada.

BOX 17

The Early Barter System in Canada

In those early economic days, exchange took place by trading one or more items directly for another, that is, through barter. An economy based on this method of exchange is referred to, not surprisingly, as a *barter system*. As long as the output of the economy is made up of relatively few goods and services, this type of system can function successfully.

However, as a society advances, and a much greater volume and diversity of output is produced, bartering becomes very complicated and cumbersome. Calculating the value or cost of each item in terms of every other item becomes very difficult. Making the trades becomes difficult. The economic system becomes costly and cumbersome. It doesn't take very many items before this happens. Bartering, as the basis for an economy's system of exchange and transaction, just doesn't suit the needs of a modern, diversified economy, with so many trades occurring. Note though that even though bartering is not used as the basis for our system of exchange, some bartering still goes on in the world today.

BOX 18

More Goods and Services, and More Exchanges, Led to a Need for a New System of Exchange

So, as more and more goods and services were produced in our economy, the exchange process became much more complicated. An alternative system for trading one good or service for another was needed. Something had to replace the complexities and complications of a direct barter system. Did I hear someone mention money?

1.3 The Role of Money

Bartering Requires a *Coincidence of Wants* – Very Difficult for a Modern Economy

In a barter system, a farmer who wants a television has to find someone with an extra television who also wants food. Simply finding someone who has a television available isn't sufficient. The person with the television has to have a "coincident want," that is, the person with the television has to want the food that the farmer has to trade.

BOX 19

In today's world, finding people with coincident wants for all the exchanges we make would be a monumental task. Suppose your chosen profession was to be an electrician. Think about how difficult it would be if you had to trade the output of your electrician skills for a pen, a milkshake, a car, an apartment, a pair of shoes, and so on.

BOX 20

Money Provided a Solution to the Problem – A Common "Unit of Account"

To avoid this chaos, an alternative system of exchanging goods and services evolved. It became apparent that exchanging one good or service for another would be much simpler if everyone was willing to accept some common item in a trade, that is, each person could trade whatever he or she produced for one, common thing. Something like money.

Money overcomes the problems of a barter system and the need for a “coincidence of wants.” With money, a set of common prices can be established. In this way, one of the roles of money is to serve as a “unit of account.” People can be paid for their services in money – and earn an income paid in money. People can then use their money for spending to buy the things they need and want.

BOX 21

Money Also Served as a “Medium of Exchange”

In that way, money has another function – serving as a “medium of exchange.” The farmer can provide food to those wanting food and receive money from them in exchange. The farmer then exchanges the money for a TV at a price the farmer is willing to pay. Such a process is much simpler and saves a great deal of travel, searching, and time.

BOX 22

Money, therefore, eliminates the need for a “coincidence of wants.” Money helps bring simplicity and organization to our economy. It is something people are willing to accept in exchange for the output they have produced. Money is our “medium of exchange.”

Many Things Have Served as Money in the Past

Throughout history, societies have used various items as a medium of exchange, everything from playing cards to shells to furs to gold. For one reason or another, these items became acceptable in some societies as forms of payment for goods and services. As soon as something is readily accepted in a society as money, and people will accept it in exchange for goods and services, it can serve as a medium of exchange. That is the most important criterion for anything to serve as money – it must be readily acceptable.

Another function of money we noted was that it serves as a *standard of value* or a *unit of account*. In this role, money serves as a common item in which the prices of all goods and services can be set. If a person wants a computer, he or she doesn't have to calculate how many loaves of bread will be necessary in order to buy it, how many painted houses, how many rocking chairs, how many rakes, or how many taxi rides. Instead of setting millions of prices for a television in terms of all other goods and services produced, one price is set. And the prices of all other goods and services are set in the same unit of account. So much simpler.

BOX 23

Money Also Serves as a Store of Value

Money has also to serve a third function – that is, as a “store of value.” Rather than using money for spending today, you can store (save) it for use in the future. If what we use as money is going to serve as a store of value, this can further limit what can serve as money. For example, suppose your income was paid in apples, but you didn't want to spend all your income right away. You wanted to save some of it to spend later. You're going to have some difficulty saving some of your “apple income.” The apples will eventually rot, and no one is going to want rotten apples. And you don't want this to happen to your money. You don't want it to lose its acceptability because you saved it.

We want our money to enable us to postpone using some of our current income today to be able to use it in the future. One of our goals in saving is usually to ensure that the value of our savings doesn't decrease over time. In fact, we usually hope that the value of our saved funds will increase. Later on, we will look at the value of money and how the value of money can potentially erode over time due to the influence of inflation. We will also learn how the value of savings can increase over time through wise investment and the earning of interest.

There Are a Variety of Ways to Store the Value of Money for Use in the Future

BOX 24

If you decide to save some of your money for use in the future, you might decide to acquire other things of value – other “assets” – such as bonds or stocks. Or you might invest in a house. People invest in such assets with the goal/hope that they will retain or increase their value over time. Eventually these assets will be sold and converted back to money to use for spending. When you sell an asset such as a bond, stock, or real estate, this is referred to as “liquidating” an asset – that is, converting it back to money.

To summarize, money serves three key roles: (1) a medium of exchange, (2) a unit of account, and (3) a store of value for future use.

Money simplifies the exchange of goods and services and enables us to save for the future. That's what money does for us – but what enables something to serve as money?

1.4 The Characteristics of Money

Today, something like shells or furs wouldn't work particularly well as money in Canada. At an earlier time, in a simpler economy, they could and did.

There are some characteristics for whatever serves as money in a modern economy.

BOX 25

Characteristic of Money: Durable

First, to serve as an effective medium of exchange, money must be durable. Drawing upon our earlier example, we could have chosen to use apples as money and pay for everything in apples. But problems arise when the apples rot. Who wants to carry around rotten apples? In addition, apples can be eaten, and nothing could erode the value of your money more quickly than having it end up in your stomach.

Characteristic of Money: Not Easily Reproduced, Relatively Scarce

BOX 26

Second, what serves as money must not be easily reproduced by people. It should be relatively scarce. We could use chestnuts as money. They're relatively scarce and last a long time. But, if, we did, people would start growing chestnut trees, and we wouldn't be able to control the supply. Soon there would be so many chestnuts available that prices would be bid up higher and higher. It could get to the point where you'd need a truck to carry the chestnuts you'd need to pay for bread and milk.

Characteristic of Money: Not too Scarce

BOX 27

Third, although what serves as money must be relatively scarce, it can't be too scarce. Whatever serves as money has to be available in sufficient quantity to enable all the exchanges in our economy to take place. We could use whooping cranes. But there wouldn't be enough of them to enable all the exchanges that have to take place. We would very quickly run out of money – to say nothing of the poor birds.

Characteristic of Money: Easy to Transport

BOX 28

Fourth, money has to be easy to transport. We could use elephants. But just think of all the problems at payday if elephant money was used to provide your wage or salary. Pocket money would take on a whole, or should we say hole, new meaning.

Characteristic of Money: Divisible Into Fractions

BOX 29

And last, money must be divisible into usable quantities or fractions. Imagine the difficulties you would face when you went to purchase something that had a price of 1/50th of an elephant. Not a pleasant thought.

So money needs to be (1) durable, (2) not easily reproduced by people, (3) relatively scarce, (4) not too scarce, (5) easily transported, and (6) divisible. But, as we emphasized earlier, the most essential attribute of anything that serves as money is its acceptability. It must be readily accepted by people in the economy in the exchange of goods and services.

Apples, rocks, chestnuts, elephants, or whooping cranes don't satisfy the above criteria, and they aren't readily acceptable by people in return for goods and services. So what is accepted today, and what we do use for money?

Two Forms of Money in Our Economy – Cash and Bank Accounts

Money, as a medium of exchange in our economy, takes two primary forms – cash (coins and paper notes) and bank accounts where we put our money on deposit with a financial institution – and where we can access that money in accounts in different ways.

Our money in Canada is measured in dollars and cents. These are what we use as our unit of account. Everything in our economy has a price in terms of dollars and cents and we use our money to acquire goods or services.



Carrying our money as cash – coins and paper currency – is becoming less and less common over time. There is the risk of losing the cash or having it stolen. And, because cash is all the same, your cash is no different than anyone else's. As a result, if someone takes your cash, or finds your cash, it is easy for them to use it.

But many people do still carry some cash with them. To get cash, one can go to the financial institution where their money is on deposit and withdraw it. This can be done through a person – a teller – or through an ATM (Automatic Teller Machine) or ABM (Automatic Banking Machine) – two names used for the same thing.

Cheques – A Means by Which to Access Your Money and Make a Payment

Another way to use your money is to write a cheque. By using a cheque you instruct your financial institution to transfer money from your account into the account of another person, company, or



government.

As it is, the person or organization to which you are transferring your money may or may not have their money on deposit at the same financial institution. At the end of the day, all the money transferred by cheques will have to be settled among the different financial institutions. More on this later.

Debit Card – A Means by Which to Access Your Money and Make a Payment

BOX 30

Another common way of accessing your money is by using a debit card. Like a cheque, when you use your debit card you are telling your financial institution to transfer money from your account to someone else's account. Debit cards, though, do this electronically and makes the transfer more quickly than by using a cheque.

BOX 31

Important – Have the Money in Your Account to Cover the Payment – However It Is Made

The important thing about using a cheque or a debit card is that you have to have enough money in your account at the financial institution to cover the payment. If you don't, a debit card transaction won't be approved – and you will learn that right away when your payment is not accepted.

With a cheque, the process can take longer. Your cheques will have to be “cleared” at the end of the day when financial institutions settle up all the payments that have been made that day. If you don't have enough money in your account to cover the payment you made, your cheque will “bounce” – that is, it will not be cleared. The person or organization to which you wrote the cheque will not receive your money. They likely won't be happy about that. They will be looking for their payment and you will likely be charged a fee by your financial institution.

Needless to say, it is best to avoid “bouncing cheques” since that can affect your financial reputation and credibility.

So there are three primary ways we use or access our money to pay for goods and services – cash, debit cards, and cheques.

Credit Cards – A Means by Which to Access Someone Else's Money to Make a Payment

There is one other form of payment that is used to acquire goods and services – credit cards. This brings us to an important distinction. By using a cheque or a debit card, we are using a *process* to access and transfer our money. Therefore, the deposits are the money. A cheque or debit card is a process by which to access money.

Credit cards are another process by which to make a payment. In using a credit card though, you are not accessing and transferring *your* money. Rather, when you use a credit card, you are drawing on a pre-arranged loan you have with your financial institution. Your institution will have approved “credit” for you to use – up to a set limit. When you use a credit card, you are using all or part of that loan the institution is willing to give you. You are, though, borrowing funds to make the purchase. The credit card is the process by which you borrow the money.

BOX 32

The borrowed funds, not the credit card, are the money. Eventually, you must use your own funds to pay back those that were borrowed by using the credit card. A credit card is a process of payment that enables you to use the financial institution’s money now that you will pay back later.

Quick Summary

We have seen that the primary challenge of an economy is to use relatively scarce resources to produce goods and services to satisfy the needs and wants of people in a society. The primary roles of money are to serve as a medium of exchange, a unit of account, and a store of value. We have also identified the characteristics of money and what we tend to use as money in Canada.

Before we examine the economy and the financial system in more detail, let's take a little journey back into history to look at the evolution of money in general and particularly in Canada.