Exercise walk-through

Definition, Measurement, and Functions of Money ▪ 4.3

eXercise

You must be able to

- state the three **functions of money 货币的职能**: medium of exchange, store of value, unit of account
- compare the money-supply measures **M1** and **M2** by liquidity
- distinguish **commodity money 商品货币** from **fiat money 法定货币**

Method — Three functions of money

- **Medium of exchange** — accepted in trade.
- **Store of value** — holds worth over time.
- **Unit of account** — a common measure of prices.

Method — M1 and M2

M1 is the most liquid (cash and chequing deposits); **M2** adds slightly less liquid savings and small time deposits.

Method — Commodity vs fiat

Commodity money has intrinsic value (e.g. gold); **fiat money** has value because the government declares it legal tender.

Practice 2.1 ▪ 2 marks

State the three functions of money.

Solution 2.1

Method: Three functions of money

Worked steps

medium of exchange, store of value, unit of account **B1** **B1** *for any two; for all three.*

Practice 2.2 ▪ 1 mark

State which is more liquid, M1 or M2.

Solution 2.2

Worked steps

M1 $\boxed{\textbf{B1}}$.

Practice 2.3 ▪ 2 marks

State the difference between commodity money and fiat money.

Solution 2.3

Method: Commodity vs fiat

Worked steps

commodity money has intrinsic value of its own; fiat money has value only because the government declares it legal tender **B1** **B1**.

Exam-style 3.1 ▪ 1 mark

Using money as a "unit of account" means it is used to

A store wealth over time

B measure and compare prices

C earn interest

D back the currency with gold

Solution 3.1

Method: Three functions of money

A store wealth over time

B measure and compare prices ✓

C earn interest

D back the currency with gold

Worked steps

B.

Exam-style 3.2 ▪ 1 mark

Fiat money has value because

A it is made of gold

B the government declares it legal tender

C it is naturally rare

D it earns interest

Solution 3.2

Method: Commodity vs fiat

A it is made of gold

B the government declares it legal tender ✓

C it is naturally rare

D it earns interest

Worked steps

B.

Exam-style 3.3 ▪ 1 mark

A shopkeeper prices goods, accepts cash for them, and keeps takings in a savings account.

(a) Name the money function used in **pricing** goods.

(b) Name the function used in **accepting cash**.

(c) Name the function used in **saving**.

Solution 3.3

Method: Three functions of money

Worked steps

(a) unit of account **B1**. (b) medium of exchange **B1**. (c) store of value **B1**.