

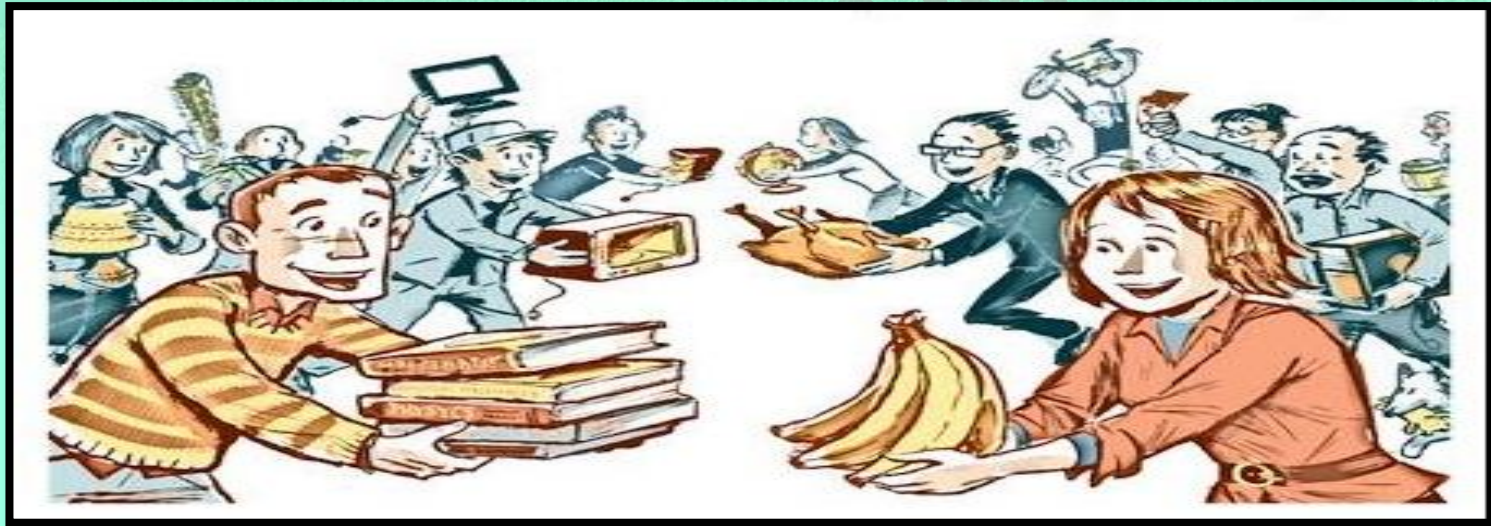
CHAPTER-3

MONEY AND CREDIT



BARTER SYSTEM

- A barter system is an old method of exchange. This system has been used for centuries and long before money was invented. People exchanged services and goods for other services and goods in return.

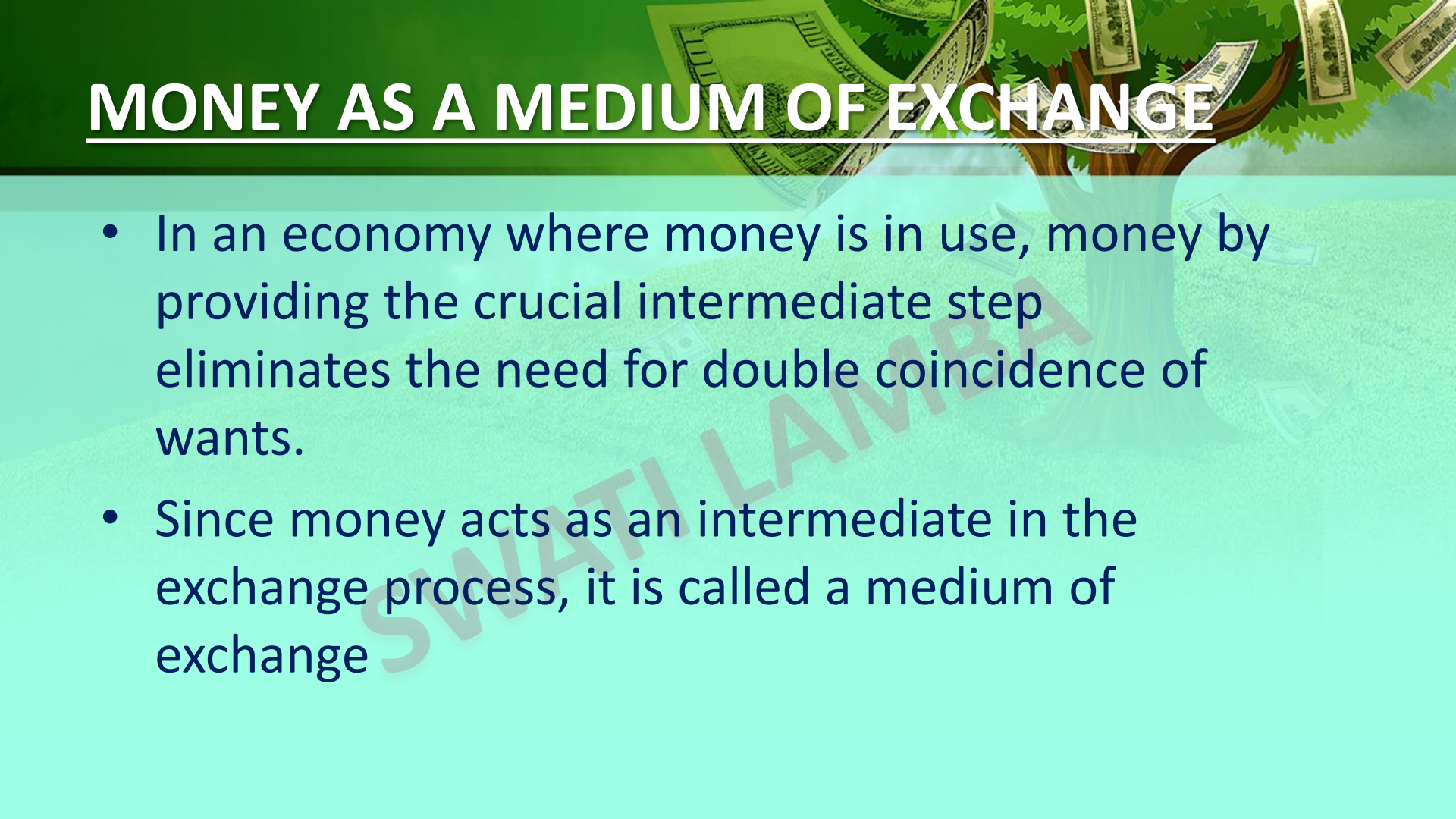


ESSENTIAL FEATURE OF BARTER SYSTEM

- **DOUBLE COINCIDENCE OF WANTS**
- When both parties have to agree to sell and buy each others commodities. This is known as double coincidence of wants.
- What a person desires to sell is exactly what the other wishes to buy.
- In a barter system where goods are directly exchanged without the use of money, double coincidence of wants is an essential feature.

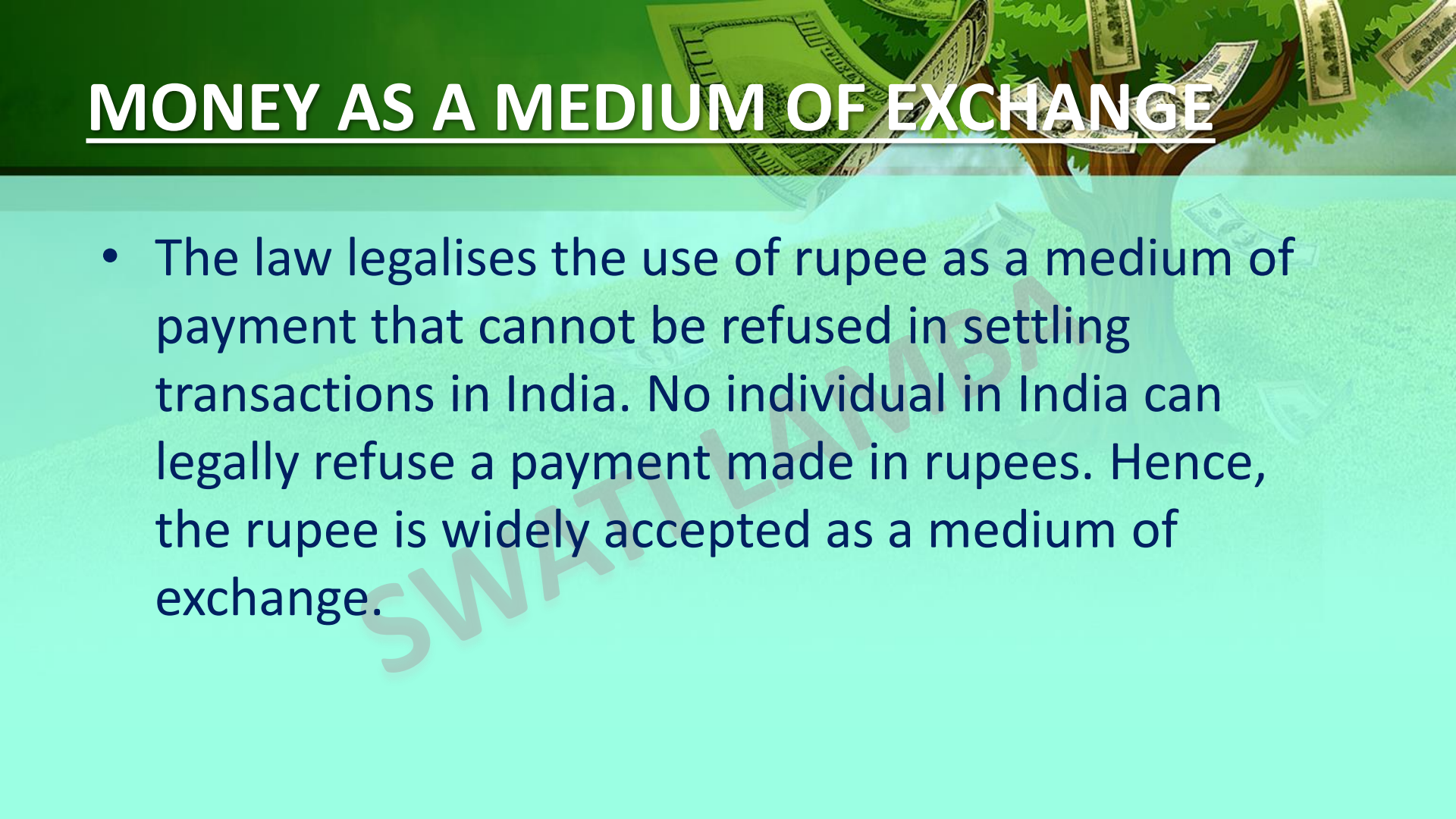


MONEY AS A MEDIUM OF EXCHANGE

A stylized illustration of a tree where the leaves are replaced by various US dollar bills. More dollar bills are shown falling from the branches, creating a sense of money being dispensed or circulating. The background is a solid green color.

- In an economy where money is in use, money by providing the crucial intermediate step eliminates the need for double coincidence of wants.
- Since money acts as an intermediate in the exchange process, it is called a medium of exchange

MONEY AS A MEDIUM OF EXCHANGE



- The law legalises the use of rupee as a medium of payment that cannot be refused in settling transactions in India. No individual in India can legally refuse a payment made in rupees. Hence, the rupee is widely accepted as a medium of exchange.

WHY MONEY IS ACCEPTED AS A MEDIUM OF EXCHANGE?

An illustration of a tree with green foliage. Several US dollar bills are shown falling from the branches and floating in the air around the tree. The bills include \$100 and \$50 denominations.

- It is accepted as a medium of exchange because the currency is authorised by the government of the country.
- In India, the Reserve Bank of India issues currency notes on behalf of the central government. As per Indian law, no other individual or

WHY MONEY IS ACCEPTED AS A MEDIUM OF EXCHANGE?



- organisation is allowed to issue currency. Moreover, the law legalises the use of rupee as a medium of payment that cannot be refused in settling transactions in India.
 - No individual in India can legally refuse a payment made in rupees. Hence, the rupee is widely accepted as a medium of exchange.
- SWATI LAMBA

WHY PEOPLE DEPOSITS WITH BANKS

- People deposit with the banks by opening a bank account in their name.
- Banks accept the deposits and also pay an amount as interest on the deposits.
- In this way people's money is safe with the banks and it earns an amount as interest.



DEMAND DEPOSITS

- People also have the provision to withdraw the money as and when they require.
- Since the deposits in the bank accounts can be withdrawn on demand, these deposits are called demand deposits.



DEMAND DEPOSITS

- demand deposits share the essential features of money.
- The facility of cheques against demand deposits makes it possible to directly settle payments without the use of cash.



WHAT IS CHEQUE?

- A cheque is a paper instructing the bank to pay a specific amount from the person's account to the person in whose name the cheque has been issued.

Date on which you wish to issue the cheque → DATE _____

PAY ← _____ *Name of person you wish to pay*

_____ *if you want to let anyone holding the cheque get the payment* → OR BEARER

RUPEES ← _____ *Amount of money in words*

_____ *Amount of money in numbers* → ₹ _____

SB A/C No.	1234 4321 0123
------------	----------------

← *Cheque issuers account number*

SUM BANK
Bank Road, Bank Town
Bank complex - 000 012
BK ID IFSC 0001 2312 3412

← *Where the cheque issuer needs to sign* →

Authorized Signatory

Cheque Number → ⑈ 00000000 ⑆ 000000000000 : 00000000 ⑆ 00

← MICR Code

MICR Band



LOAN ACTIVITIES OF BANKS

- Bank holds about 15 per cent of their deposits as cash.
- **Why banks hold deposits as cash?**
- This is kept as provision to pay the depositors who might come to withdraw money from the bank on any given day.



LOAN ACTIVITIES OF BANKS

- Banks make use of the deposits to meet the loan requirements of the people.
- In this way, banks mediate between those who have surplus funds (the depositors) and those who are in need of these funds (the borrowers).



LOAN ACTIVITIES OF BANKS

- Banks charge a higher interest rate on loans than what they offer on deposits.
- **Bank's main source of income:**
- The difference between what is charged from borrowers and what is paid to depositors is their main source of income.



CREDIT

- Credit (loan) refers to an agreement in which the lender supplies the borrower with money, goods or services in return for the promise of future payment.

SWATI LAMBA



DEBT-TRAP



- A debt trap is a situation in which a borrower is led into a cycle of re-borrowing, or rolling over, their loan payments because they are unable to afford the scheduled payments on the principal of a loan.
- SWATI LAMBA

TERMS OF CREDIT

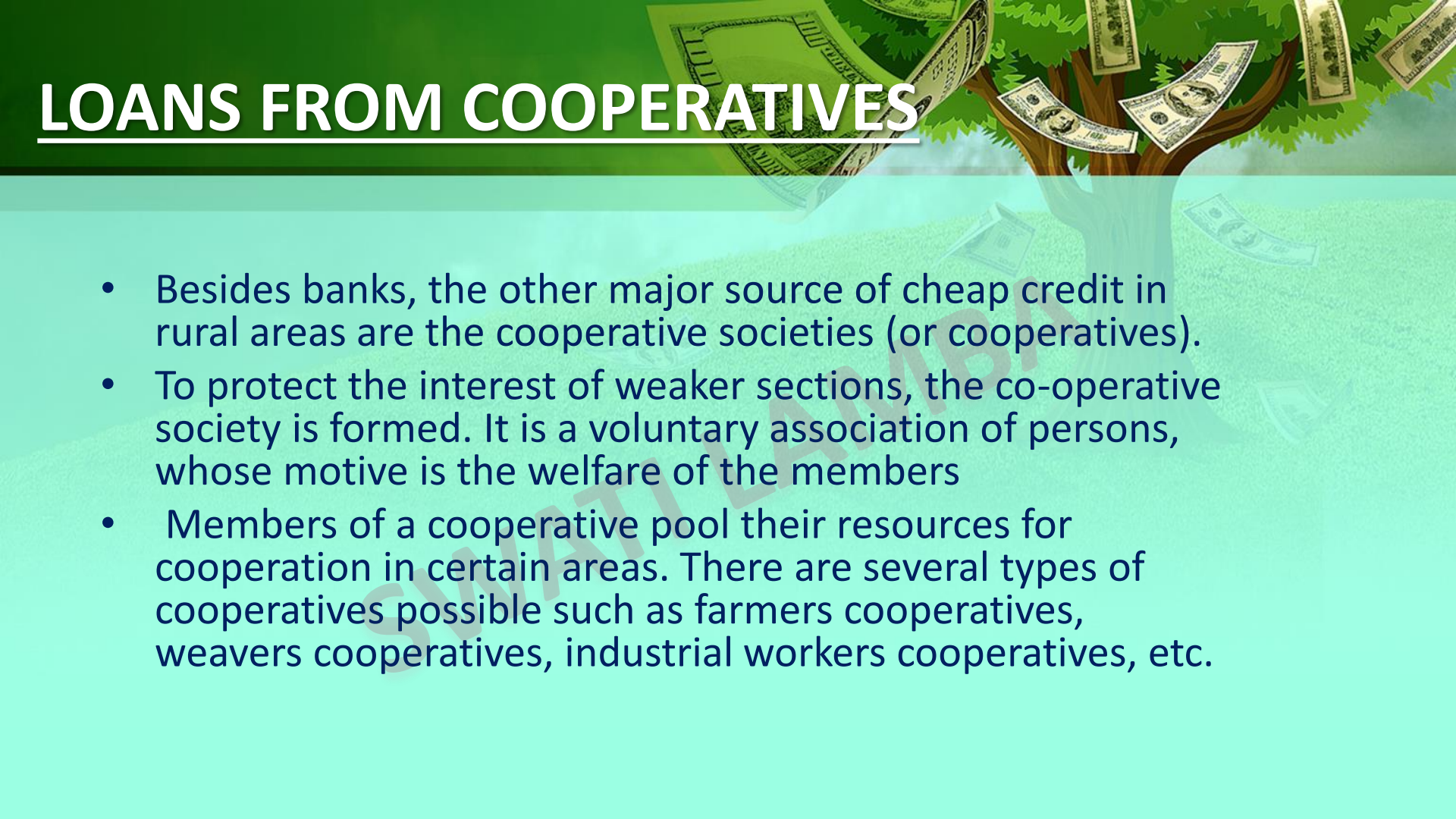
A stylized illustration of a tree where the leaves are replaced by various US dollar bills (100, 50, and 20). Several dollar bills are shown falling from the branches, floating in the air around the tree. The background is a solid green color.

- Interest rate,
- collateral and documentation requirement and
- the mode of repayment together comprise what is called the **terms of credit**.

➤ **COLLATERAL**

- **Collateral** is an asset that the borrower owns (such as land, building, vehicle, live stocks, deposits with banks) and uses this as a guarantee to a lender until the loan is repaid.

LOANS FROM COOPERATIVES



- Besides banks, the other major source of cheap credit in rural areas are the cooperative societies (or cooperatives).
- To protect the interest of weaker sections, the co-operative society is formed. It is a voluntary association of persons, whose motive is the welfare of the members
- Members of a cooperative pool their resources for cooperation in certain areas. There are several types of cooperatives possible such as farmers cooperatives, weavers cooperatives, industrial workers cooperatives, etc.

FEATURES OF COOPERATIVE SOCITIES

- It is a voluntary association, the membership is also voluntary.
- A person is free to join a cooperative society, and can also leave anytime as per his desire. Irrespective of their religion, gender & caste, membership is open to all.
- It is compulsory for the co-operative society to get registration. The co-operative society is a separate legal identity to the society. It does not get affected by the entry or exit of its members.



FEATURES OF COOPERATIVE SOCIETIES

- There is limited liability of the members of co-operative society. Liability is limited to the extent of the amount contributed by members as capital.
- The cooperative society works on the principle of mutual help & welfare.
- Hence, the principal of service dominates it's working. If any surplus is generated, it is distributed amongst the members as a dividend in conformity with the bye-laws of the society



SECTORS OF CREDIT IN INDIA

- The various types of loans can be conveniently grouped as formal sector loans and informal sector loans.
- Among the former (Formal Sector) are loans from banks and cooperatives.
- The informal lenders include moneylenders, traders, employers, relatives and friends, etc.

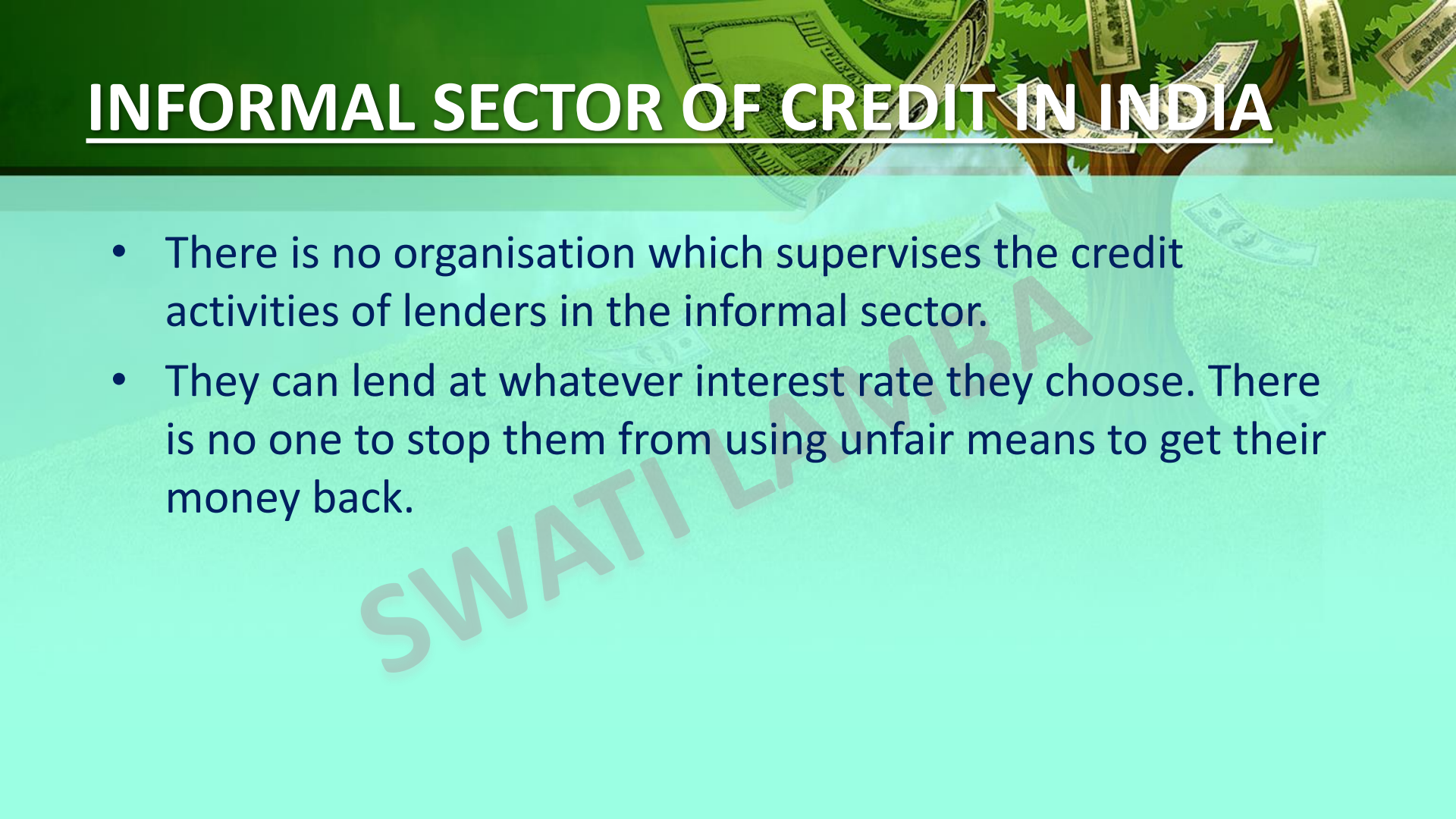


FORMAL SECTOR OF CREDIT IN INDIA



- The Reserve Bank of India supervises the functioning of formal sources of loans.
- The RBI monitors the banks in actually maintaining cash balance. Similarly, the RBI sees that the banks give loans not just to profit-making businesses and traders but also to small cultivators, small scale industries, to small borrowers etc.
- Periodically, banks have to submit information to the RBI on how much they are lending, to whom, at what interest rate, etc.

INFORMAL SECTOR OF CREDIT IN INDIA



- There is no organisation which supervises the credit activities of lenders in the informal sector.
 - They can lend at whatever interest rate they choose. There is no one to stop them from using unfair means to get their money back.
- SWATI LAMBA

DIFFERENCE BETWEEN FORMAL AND INFORMAL SECTORS OF CREDIT IN INDIA

FORMAL

- They follow those sources of credit, which are registered by the government and have to follow its rules and regulations.
- RBI supervises the functioning of formal sources of credit
- They generally charge lower rates of interest.
- Their main motive is social welfare.
- Example: Banks and cooperatives

INFORMAL

- These include those small and scattered units which are largely outside the control of the government.
- There is no organisation which supervises the credit activities.
- They charge much higher rates of interest.
- Their main motive is profit-making.
- Example: Moneylenders, traders, employees, relatives and friends, etc.

SELF-HELP GROUPS FOR THE POOR

- In the previous section we have seen that poor households are still dependent on informal sources of credit. Why is it so?
- Banks are not present everywhere in rural India. Even when they are present, getting a loan from a bank is much more difficult than taking a loan from informal sources. As we saw for Megha, bank loans require proper
- documents and collateral. Absence of collateral is one of the major reasons which prevents the poor from getting bank loans



SELF-HELP GROUPS FOR THE POOR

- In recent years, people have tried out some newer ways of providing loans to the poor.
- The idea is to organise rural poor, in particular women, into small Self Help Groups (SHGs) and pool (collect) their savings.
- A typical SHG has 15-20 members, usually belonging to one neighbourhood, who meet and save regularly.



SELF-HELP GROUPS FOR THE POOR

- Saving per member varies from Rs 25 to Rs. 100 or more, depending on the ability of the people to save.
- Members can take small loans from the group itself to meet their needs. The group charges interest on these loans but this is still less than what the moneylender charges.



SELF-HELP GROUPS FOR THE POOR

- After a year or two, if the group is regular in savings, it becomes eligible for availing loan from the bank. Loan is sanctioned in the name of the group .
- Moreover, SHGs are the building blocks of organisation of the rural poor.
- ❖ Not only does it help women to become financially self-reliant, the regular meetings of the group provide a platform to discuss and act on a variety of social issues such as health, nutrition, domestic violence, etc.



QUESTIONS

A stylized illustration of a tree where the leaves are replaced by various US dollar bills. Several more dollar bills are shown falling from the tree and scattered on the ground below. The background is a gradient of green and blue.

Q1.What are Demand Deposits?

Q2. What is a cheque?

Q3. What is a Collateral?

Q4.How do cooperatives function?

Q5.Why money is accepted as a medium of exchange?

Q6. Who issues currency in India and on behalf of whom?

Q7.What are the terms of credit?

Q8.Differentiate between formal and informal sectors of credit in India?

Q9.Why does people take more loan from Informal sectors ?

Q10.Explain SHG's.

THANK YOU

BY: SWATI LAMBA

