Q. 1. What is meant for demand for money?

The total amount of money demanded in an economy is thus the total amount of money demanded by all individuals in that economy.

Q.2. what is the meaning of money supply?

The supply of money in an economy at any point in time refers to the amount of money held by households and businesses for transactions and debt settlement.

Determinants of Money Supply

Following are the main determinants of money supply----

1. The Required Reserve Ratio:

The required reserve ratio (or the minimum cash reserve ratio or the reserve deposit ratio) is an important determinant of the money supply. An increase in the required reserve ratio reduces the supply of money with commercial banks and a decrease in required reserve ratio increases the money supply.

2. The Level of Bank Reserves:

The level of bank reserves is another determinant of the money supply. Commercial bank reserves consist of reserves on deposits with the central bank and currency in their tills or vaults. It is the central bank of the country that influences the reserves of commercial banks in order to determine the supply of money. The central bank requires all commercial banks to hold reserves equal to a fixed percentage of both time and demand deposits.

3. Public's Desire to Hold Currency and Deposits:

People's desire to hold currency (or cash) relative to deposit in commercial banks also determines the money supply. If people are in the habit of keeping less in cash and more in deposits with the commercial banks, the money supply will be large.

This is because banks can create more money with larger deposits. On the contrary, if people do not have banking habits and prefers to keep their money holdings in cash, credit creation by banks will be less and the money supply will be at a low level.

4. High Powered Money and the Money Multiplier:

High-powered money is the sum of commercial bank reserves and currency (notes and coins) held by the public. High-powered money is the base for the expansion of bank deposits and creation of the money supply.

5. Other Factors:

The money supply is a function not only of the high-powered money determined by the monetary authorities, but of interest rates, income and other factors. The latter factors change the proportion of money balances that the public holds as cash. Changes in business activity can change the behaviour of banks and the public and thus affect the money supply

Q. Determinants of demand for money.

Some of the key determinants of demand for money specified by Friedman are:

1. Total wealth: It is the total that must be divided among various forms of assets. Due to difficulty of getting estimates of total wealth, Friedman substituted permanent income (Y) for wealth in his demand- for-money function. Permanent income is the expected income flow from total wealth.

2. Human and Non-Human Wealth:

Total wealth includes both human and non-human wealth, but there exist legal and institutional constraints in converting human into non-human wealth. Therefore, Friedman introduces the ratio of non-human to human wealth (w) as a variable in the demand function.

3. Money:

The nominal rate of return on money may be zero as on currency, or positive as on saving deposits or even negative if current account deposits are subject to net service charges. But money is demanded for the services it yields and these services arise because of money's command over goods and services.

4. Bond:

Bond is considered to be a perpetual security, or consol, which yields an income stream whose value, is fixed in nominal terms. Thus, the yield on bond (r) consists of the sum of its coupon plus any anticipated capital gain due to an expected fall in the market interest rate or less any anticipated capital loss due to an expected rise in the market rate.

5. Equity:

The equity is identical to the bond except that it contains a cost- of-living escalator so that its income stream always maintains constant purchasing power. The yield on equity (r) is composed of three elements: (a) its coupon yield, (b) any expected capital gains or losses due to changes in interest rates, and (c) any expected changes in the general price level.

6. Commodities:

Physical goods held by wealth-owners yield income in kind (i.e., utility) which cannot be measured by an explicit interest rate. However, their real return is affected by the changes in the price level. Friedman uses the nominal yield on commodities (r) to consist of their expected rate of price change per unit of time.