Modern Money Theories

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Abstract*: This article analyses the historical stages of money and their theoretical dimensions, and comments on the works and views created by scientists. The article also examined the theories of money and analyzed the activities of new schools based on the work of previous representatives of schools. As we explore the historical stages of the economy, we have come to see different approaches to money circulation, different schools and trends that interpret its importance to the economy. In the process of studying some of the similar and distinctive aspects of classical and neoclassical economists' views on money, the necessary conclusions are drawn. At present, economic reforms are one of the important factors in ensuring the stability of national currency, development of international monetary relations, increasing the export potential of the country, and satisfying the needs of the population in foreign currency. The tasks that are to be accomplished in this process are very complicated, and their solution has had a significant impact not only on the economic situation, but also on the development of our society. Continuous study of this issue requires simultaneous alteration of the economic situation and introduction of changes and additions to the measures to ensure stability of the sum[1].

***Index Terms*: Crisis, economics, inflation, monetary system, neoclassical economist.**

I. INTRODUCTION

According to the research, the level of implementation of programs aimed at raising the value of monetary assessments, the consequences of its implementation, the causes of the negative consequences, and measures to overcome them and the search for effective ways of doing business are considered appropriate. It is clear from research that money is the main tool that affects people's labor, giving vital energy to the movement of revenues and expenses, which reflects the entire economy of the country. A well-functioning monetary system helps the full enjoyment of the full potential of society, and the bad monetary system has a major impact on the state of the country's production and price system. Thus, money plays a strategic role in the economic system: it is an important factor in the formation of investment demand, and the level of price dependence depends on the amount of money.

The debate between the economists, though much has passed since the beginning of money, requires a step-by-step analysis of its origins to the present day. More precisely, after the natural transformation system, the role of money in the economy with the task of performing the "medium of exchange" as gold in "monometallic theory"[2] is continuing to be a matter of economics. Then, in the "bimetallism"[3], the appearance of the "Gresham's Law" [4] with the accomplishment of silver and gold, and then the "fictitious monetary system" and the appearance of "quantity theory of money"[5] in the "paper money" system as a result of the cancellation of the Breton Woods[6] system in 1973 and today emerging "plural theory of money"[7] is the continuation and the consequence of the debate on the role of money in the economy.

Classical economists have explained that money is "neutral" in the process of economic governance, while money was considered to have no value in managing the economy according to Keynes theory of money. However, "monetarists" led by M. Friedman have reckoned that the root of economic problems stems from the problems with money and mass management of money. For that reason, monetarists consider economic management as the optimal control of this money mass."The rational assumptions theory"[8] institute, led by R. Lucas, attempted to explain the role of money in the economy on the basis of "skill-based" or "rational" assumptions about the future of economic entities.

D. Hume, A. Smith, D. Ricardo, J. Mille, and others have studied the theory of money in different ways. Some of their views and opinions have coincided, while others have played an important role in the development of the economy.

John Keynes' theory, including the role of money in the economy, was formed in the first half of the 20th century. At that time the whole capitalist world was experiencing a major economic crisis of reproduction.

Crisis and wars during 1929th and 1933th years had a positive impact on the development of capitalist economy and raised

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[2]Monometallism – the economic term for a monetary standard where the use of the only one metal (gold or silver) in the standard currency of a country or as a standard of monetary value.

[3]Bimetallism – the economic term for a monetary standard which the value of the monetary unit is defined as equivalent to certain quantities of two metal, typically gold and silver creating a fixed rate of exchange between them.

[4]In economics, Gresham's law is a monetary principle stating that "bad money drives out good". For example, if there are two forms of commodity money in circulation, which are accepted by law as having similar face value, the more valuable commodity will gradually disappear from circulation.

[5] Фридман М. "Количественная теория денег". Эльфпресс. М., 1996.

[6] The Bretton Woods Monetary System (Gold and Two Replacement Currencies Gold Exchange Standards - US Dollars and Pounds Sterling) .1973.

[7]Зелизер В. Создание множественных денег // Западная экономическая социология: Хрестоматия современной классики / Сост. и науч. ред. В.В. Радаев; Пер. М.С. Добряковой и др. — М.: Российская политическая энциклопедия (РОССПЭН), 2004. — С. 413-430.

[8] Lucas R. "Rational assumptions theory".

[8]Sum – national currency of Uzbekistan.

the issue of prospects and ways of further development of the countries. Several states followed the principle of keeping the budgetary instrument-budgetary stability and stable exchange rate, which was the traditional tool of neo-classical theory in emergency situations of this period, and the remaining problems were automatically resolved by the market. However, the economic situation deteriorated.

For example, in the context of "great depression", the fundamental shortcomings of the traditional economic theory have demonstrated that it is incapable to realize the causes of chronic diseases of the old system, and not in correcting serious misbalances in the economy, but of inability to offer effective solutions to their equalization.

At that time, significant changes took place in the monetary circulation of all the capitalist countries. In 1931, Britain abandoned the gold standard. The Bank of England did not attend other international currencies in order to keep the fixed value of the pound. Following the Great Britain, almost all the countries of the British Empire, almost all European and Japanese countries rejected the gold standard. In 1934, the United States banned the exchange of dollars to gold for private individuals. By 1936, the gold-blocking countries under the French leadership rejected the gold standard. As a result, there grew up a need for a new economic approach.

Before proceeding with a detailed study of the concept of Keynes, it is important to point out that he proposed a new methodological approach in the process of economic analysis. The peculiarity of this technique is, firstly, the emphasis on the overall set of indicators (macroeconomic, aggregated) across the whole society, and second, renouncing functional approach to the Cambridge school and short-term analysis, and focusing on macroeconomic relationships. The central idea of the theory of the so-called theory is that the emerging market economy is not an ideal system of self-regulation, a mechanism of reverse relations. He pointed out that full and rational use of material and human resources would ensure economic growth, which would be confirmed by the scale of the crisis.

Keynes criticizes Say's law, and shows that the economy is not merely the basis for conversion of goods into commodities but also by the exchange of money. Here, however, the first difference between Keynes theory and classical quantum theory appears that money is not just a "veil" but it also takes part in barter deals. Monetary factor plays an active role in the context of the uncertainty of the economic prospects and the interdependence of the risk.

As a result, theoretical perspectives such as "Functional", "Liquidity", "Portfolio" and "Quantity" theories about the role and importance of money in the economy have been created, but nowadays it is on the threshold of "Plural theory of money". Perhaps, in the future, theories like "Square money theory" or "Quantum theory of Money" may appear. However, economists have not been able to give conclusion on the role and importance of money in the economy.

This can be compared to astronomical scientists' efforts to explain the creation of the universe. To exemplify this comparison, centuries ago Ptolemy stated, "the Sun is turning around the earth", but our Abu al-Raykhon Beruniy proved that the earth is rotating around the sun. Later on, Newton created the "Gravity law of the whole universe", while Einstein discovered the theory of relativity. So far, S. Hawking has tried to unite the gravitation and quantum mechanics to explain the creation of the entire universe, with the theory of Great Explosion. Even though astronomers have not yet commented on the creation of the entire universe, the science of astronomy has evolved far and wide. Even economists do not give a complete conclusion about the role and importance of money in the economy, no matter how many new theories, like astronomical scientists. Yet, the theory of money has developed and improved in comparison with the classical economists' time.

In particular, the "Functional theory" considers the function of money as "medium of exchange" as the main function. According to the aforementioned theory, all assets may have value-added characteristic, but can not be a substitute for money in terms of the function of money as "medium of exchange". That is why money is the means to establish relationships between the consumers and producers. Taking this theory into account, the central bank should focus on controlling the functional amount of money. Thus, the optimal money supply for the economy should include coins, cash money, and fixed-term deposits of enterprises. This theory believes that the time deposits must not be included in the total cash flow, rather than the payment, but rather for earning money, and suggests withdrawing the amount from the control object.

According to "Liquidity theory", the main feature of money is that it is a liquid asset. Therefore, in the case of every active liquidity, asset can perform the function of money in the economy, and consequently, assets can be grouped into liquid assets, financial and real assets from the liquidity point of view. Supporters of this theory allocate their liquidity to their ability to convert to cash in the short term and at no cost. The theory of liquidity more widely emphasizes total money mass differing from the functional theory. Money mass is even more widely considered in "Portfolio theory".

According to "Portfolio Theory", issued by Nobel Prize laureate Thomas Sargent in 2011, there is an "investment portfolio" of economic entities in every economy, which consists of liquid, financial and real assets. Providing that the share of these assets in the capital portfolio does not change and the amount does not change then the economy is considered to be in balance. Portfolio theory broadly describes the overall mass of money in the economy, but also suggests the criteria in terms of money mass balance.

The quantity theory of money is directed at controlling money supply and ensuring the balance of demand and supply. According to this theory, the problem of the economy is the quantity and variability of the goods, which substitute money, not the nature or appearance of the goods. The quantity theory of money emphasizes the importance of monetary policy tools and money management tools in detail.

$$MV \equiv PT$$

The quantity theory of money suggests that the change in the value of money is explained by the change in the amount of money, that is, changes in the amount of money directly and in the same amount will cause changes in the overall value of money. This theory is regarded as an instrument of simplifying the function of money as a medium of exchange in the economy. Nevertheless, this theory does not confirm the same laws in all economies due to different levels of economic development of countries. For instance, in

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developing countries, due to high unemployment rate, the increase in money mass positively affects not only on the growth of prices like in the developed counties, but also on the rise of GDP as a result of high goods turnover, providing that there is no change in the rate of money circulation. In developed countries, GDP growth can stem from by population demography and modernization in the manufacturing. Therefore, the increase in money supply in the developed countries contributes directly to the increase of total price.

According to the quantity money theory, the desire of the population to save money firstly influences the speed of the money circulation. As a result, the increase in the rate of money circulation turns into an increase in the goods turnover in the economy. However, due to the high stages of economic knowledge, acquisition and the high level of deception of money in developing countries, the increase in money supply simultaneously leads to an increase in the general level of prices and goods turnover.

Thirdly, the fact that the real, relative and general level of prices in the economies of the developed countries has been fully implemented, there is little probability of deception of money phenomena. As a consequence, the increase in money supply leads to an increase in the level of direct public spending, rather than an increase in GDP. In developing countries, the relatively low standard of living than the developed economies leads to the increase in the total value of money and the increase of goods turnover in the economy[9].

With regard to the role of money in the economy, all including from the requirements to goods substituted money, the concept of monetary functions and the explanation of money also are changing and improving in line with the requirements of today's modern economic system. In the period of classical economics, monetary functions had been defined as the medium of exchange, the unit of account, the substitute instrument, the savings instrument and the world's money. Today, the appearance of money has become an electronic form of money and has been enhanced by means of money and power, capital and production. This is inevitably an impetus for the technological advancement of the economy and the improvement of the payment system, as well as development of economic entities, the sudden changes in their future expectations.

As a result, psychological, material, legal, and economic explanations of money are improved, and the social and political features of money are emphasized due to the monetary outcome in the economic processes.

As far as the psychological nature of money is concerned, it is understood that each commodity should have the ability to repay its debts first and should be recognized by all economic entities in order to perform the function of money. The intrinsic nature of the money is, of course, the fact that it has a material appearance and, at the same time, directly involved in the payment process, has a per-per-item value and the requirements for maintaining it. To explain the legal nature of money, it is understood that money is legally secured by the state and that these safeguards are guaranteed to be in the national economy. From the above, the economic characteristics of money can be summarized as follows: money must fulfill all its functions in economic activity.

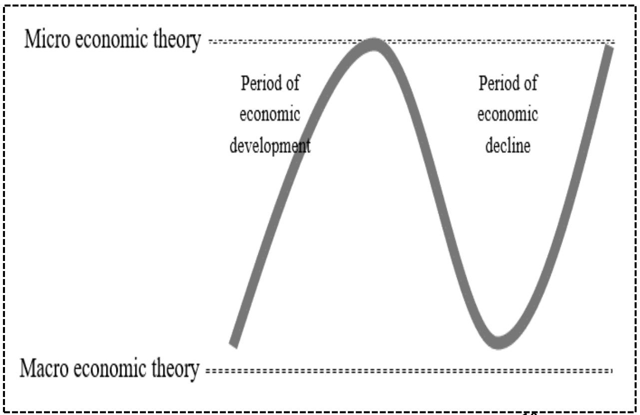

Fig. 1. Economic changes in trends[10]

In today's sophisticated monetary system, the political nature of money has been dealt with, where from the point of view of the central bank, money must have the power to regulate the payment system, while the government emphasizes the nature of collecting tax of money.

The social feature of money is that money is a function of capital for well-off people, whereas it is a lively asset for the poor. Therefore, the confidence of economic entities in the national economy towards the national currency as to "payment" and "debt" is higher than for foreign currency (if the foreign currency profitability level is unchangeable).

Moreover, improving the social norms and rules of financial institutions involved in money circulation (commercial banks and technological armament of payment systems, credit and microcredit organizations, savings, exchanges and insurance companies) are changing the needs and views of economic entities.

According to the research conducted by economists, the reliability of the money plays a key role in the value of it, rather than its material security and protection. Of course, both the technological armament of monetary institutions and the payment system are crucial in shaping that reliability. As a result, today, the "quantity theory of money" is at the edge of being replaced by "plural theory of money".

As evidence of this, as far as scientific researches in economics awarded by the Nobel Prize are considered, the Nobel Prize awarded John Nash [11](California University) in 1995 for his "Game theory". The theory of game has been proven a contradictory solution to conflicts, meaning that to make a profit from competition (contradiction) in the economy has been proven. According to him, competition in the economy is a complex of conflicting actions, and the factor determining profits is the intellectual capacity of economic entities and the commonality of interests. Thus, the measure and the size of profit in the economy are regulated by economic entities.

In 2003, Nobel Prize winners, Daniel Kahneman (Princeton University) and Vernon Smith (University of Mason), promoted macroeconomic issues in their research on the

[9]The existence of "norms" and demand for culture in the consumption is the antipathy of every economic decision. Due to the "imitation", "boasting" tendency in consumption, high levels of consumption and difficulty in controlling the entire P of the population spent on T and increase in R.

[10]By author

[11]http://italife.ru/obo-vsem/628-teoriya-igr-dzhona-nesha

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topic of "Experimental and fundamental economic theory: alternative market economy."

In 2006, the Nobel Prize winners, Thomas Schelling (Israel University) and Robert Aumann (Maryland University), devoted their research on "Natural conflicts and mutual assistance theory" to microeconomic problems.

In 2010, the Nobel Prize winners, Oliver Williamson and Eleanor Ostrom (New York University), focused on macroeconomic measures in managing microeconomic issues on their "Theory of transactions in management institutions and complex economic processes", which emerged as a solution to the international financial crisis. In this study, which includes the theory of monopolistic profits because of the oligopolistic combination of cognitive (contrasting) forces, macroeconomic measures are emerging as a solution to the development of competition and crisis prevention.

Laureates of the Nobel Prize in 2011 were awarded for their suggestions on resolving macroeconomic problems in their research at Thomas Sargent (University of New York) and Christopher Sims (Princeton University).

As the “Plural money theory”[12]proposed by the American sociologist Zelizer is considered this is based on the idea that there is an alternative to the purpose and source of spending, even though the same objective and aspirations are in the interest of accumulating money. Accordingly, monetary income generated by the same source of funds has a significant impact on the living standards of the population, based on different goals and social conditions. In the United Kingdom, for example, a substantial proportion of money incomes is spent on children's clothing and commodities, whereas private consuming goods occupy large proportion of money spent, which serves to improve the livelihoods of households in Canada and Sweden. According to research on distribution of money in Russia, the population is paying attention to durable goods used for household needs, while trying to save money in the period of economic difficulties.

Moreover, according to the results of research it appeared that the share of women’s income in the structure of household income is higher. In Bangladesh, it has been established that the majority of bank loans allocated to women are spent on family needs rather than to men. In Brazil, government spending on mothers has increased dramatically for family health and child nutrition compared to fathers' spending.

As a result, modern functions of money such as medium of exchange and cash flow, savings and capital, calculations and measurements, incentives and interests, value and redistribution, confidence and pride are emerging today. Money is generally regarded as a reliable medium of exchange for individuals, families, firms and the state in all economic activity and needs.

Monetary circulation in the economy does not occur if monetary circulation is not convinced of the future fate and value of the money that is involved in the exchange of goods and services. The basis of this confidence lies in the following factors:

1. The participant of the money circulation shall meet his / her needs via exchange of money on his / her hand;
2. The participant believes that other participants in the same way act with money as the exchange of goods;
3. At least the participant knows that the currency has the value of exchange for another currency. Therefore, economic entities do not lose their desire for money even during inflation.

Hence, the “plural money theory” describes socially structured debt obligations in the economy. According to this theory, participants in money circulation believe in the future value of money and have rational assumption about it. Thus, not only to pay for a one-time payment, each participant believes that he will act in such a way that the spent money will be returned, at least to the equivalent of the currency on his hand.

This confidence issue can be seen in the case of Monetary Policy in Argentina during 1991 and 2001 years. In 1991, Argentina issued a “peso” to its currency reserves to keep the parity of its currency at the rate of 1: 1 for the dollar. As a result, the exchange rate of peso to the dollar was strengthened and inflation expectations were lost in the economy. As time went by, the volume of capital imports to Argentina increased, exports declined and the budget deficit began to increase. The recession started in the Argentine economy, due to the slowdown in economic growth due to the budget deficit. As a result, the confidence in the parity rate of “peso” and the dollar at 1: 1 ratio diminished, and the banks began to recover their savings due to the economic downturn. In contrast, the Argentine government imposed a limit of "max. $ 1,000" in withdrawal from banks. As a result, the rate of “peso” to the dollar was raised to 1 dollar = 2.3 peso. After that, the Argentine government cancelled the "Funds Restriction Order" and introduced a free converting system. As a result, the rate of the peso / dollar increased several times and the domestic and foreign debt of the country increased. In 2001, the Argentine state faced in default.

Economic theorists have also explored intermediate goals in the process of achieving the major goals of monetary policy. In particular, M. Friedman begins studying the impact of nominal earnings on prices and production levels after examining the nominal earnings and its impact on production. That is why the inflation issue is the subject of research. The main issue of interest here was the increase in nominal earnings and the change of interest rates on it. Studying the stagflation process, he examines the effects of the famous Philips curve and the prices. According to M. Friedman, the main reason for the increase in inflation, that is, the amount of money in circulation. Accordingly, inflation is always a matter of money and is a kind of tax that can be sneaky from the economic subtleties. M. Friedman considers that inflation is continually repeated in the same way. There are three reasons for this:

- Inflation is the result of an increase in nominal money. An increase in the amount of money compared to the amount of production is higher. That is why economists believe that the rise in prices is exhaustive and quickly absorbed;
- Economical subgroups are directly involved in the rise in prices and increase the costs by moving them to the desired amount of money. As a result, the increase in the rate of increase in the value of money increases;

[12] Зелизер В. Создание множественных денег // Западная экономическая социология: Хрестоматия современной классики / Сост. и науч. ред. В.В. Радаев; Пер. М.С. Добряковой и др. — М.: Российская политическая энциклопедия (РОССПЭН), 2004. — С. 413-430

- Finally, with the increase in the rate of money and the rate of increase in prices, one begins with a period of infinite inflation. In hypertension, the rate of increase in prices will be several times higher than the rate of increase.

According to M. Friedman, the idea of the supply inflation rate is not true, that is, the increase in the burden on the producers will increase the amount of money. According to him, the increase in the cost can lead to a short-term rise in prices. This is because of a rise in the price of a network will be covered by the increase in production in the second sector, and the fall in prices. In particular, M. Friedman does not accept the concept of industrial syndicates and monopolistic firms as an inflation factor. At the same time, he does not accept direct "salary-to-inflation" chain either. In addition, strong anti-inflation measures can have a detrimental impact on mutual agreements between firms and overrun economic activity, because economic entities have suppositions and expectations. Therefore, M. Friedman recommends acting according to rational inflation. In addition, M. Friedman believes that a person respected and trusted in the society, famous political parties and organizations should accept the decision against inflation, which makes it with a «credibility» label. This idea is supported by both W. F. Eller and Garbert Stain, representatives of the rational theory of evolution. Statements below should be taken into consideration when deciding on such a decision;

- a combination of several activities and a good relationship between the government and the central bank;
- mutual agreement on specific issues between political parties;
- a clear explanation of the intended targets and the vulnerabilities and expected risks at each stage;
- an uncompromising program of fighting against unemployment and denials of control.

Only then people can believe this decision and dedicate to fight against inflation. M. Friedman doubts the positive aspects of inflation like redistribution of earnings, reducing unemployment, providing flexibility for employment. He fully believes in the issue of the hidden taxation for the government, but explains that it will lead to catastrophic consequences. This is because the level of the tax base's real money and the level of depreciation of real monetary resources are the same as the increase in the real value of the tax with the increase in the value of real money. That is why M. Friedman opposed inflation.

He also opposes the anti-inflationary policy of the government and the central bank's intervention in inflation, as well as against the inflationary measures. He is somehow a known inflationist. It affects the rational development of the economy, the decline in unemployment, the inability to maintain relative prices, and the economic suppositions and expectations of economic growth. M. Friedman considers relative prices as a free source of information for people. Indeed, he says that, as a matter of fact, the measures taken by the government based on the situation will lead to high inflation in the future. For example, he said: "closing the budget deficit at the expense of money emissions is a government's anti-inflationary policy compared to issuing securities."[13]

An untimely and unplanned response to inflation results in bad consequences, which explains the stagflation in the field of development of the economy. In particular, the expansion of monetary policy to reduce unemployment results in inflation. The demand for labor will increase, as the real wages and the offer of labor decrease as the nominal wage increases. As a consequence, prices will increase and producing will decrease, arising stagflation. In the meantime, the sharp decline in inflation will result in the fact that in real firms, the real wage is higher than the productivity of the workforce, resulting in a decrease in production due to increased product cost. As a result of these processes, M. Friedman has studied the relationships between money and interest rates and unemployment and pricing, and explains that the most important issue in the economy is the amount of money and the issue that needs to be monitored is money offer. After that, he analyses monetarism's views on economic policy.

At the same time, the theorists are asking for a central bank's monetary policy to target its intermediate goals, meaning that there should be protecting the targeted intermediate target in the basis of monetary policy.

According to M. Friedman, the notion of "high production-high prices" is different, with the notion "production-based evaluation". He thinks that only in the second case there is an inflationary shadow. According to M. Friedman, there are two reasons for the inflations, which are due to the increase in cost price:

First; with the increase in the amount of money, people increase the cost of reducing the amount of true cash in their hands, which means the demand increases. In this way, the prices will increase. This process takes place in production facilities and in the network of services. As a result, this network begins to cost a second line that uses the services of production facilities. This is not an increase in the overall cost, but the rise in prime cost in some sectors due to the increase in demand.

Second; in fact, the decisions of money makers (central banks and commercial banks) on the basis of the increase in money supply. Only monetary authorities state the increase in cost price as a cause of inflation, in order not to take responsibility over inflation and workers and firms are claimed the cause of inflation.[14]

M. Friedman answers the question, "Is it necessary to reduce the money emission for anti-inflation or to use monetary control instruments?" According to M. Friedman, the only way to fight against inflation is to control the amount of money. No other measures will be effective. In particular, price controls and organizational arrangements are only a temporary measure, which means that prices can only be increased, but cannot stop the increase in the amount of money that is the main cause of inflation. Breaking the

[13] **Friedman M.,** "Monetary Policy" Journal of Money credit and Banking. USA. Chicago. 1982. p – 31.

[14] **Friedman M.,** "Monetary Policy" Journal of Money credit and Banking. USA. Chicago. 1982. p – 28.

thermometer is not a cure for thermal reduction. Even price controls can also be overestimated. Nevertheless, it does not cover the overall rating.
Controlling the monopoly prices of the firms is necessary to eliminate barriers to the implementation of free pricing, but rather to control the overall rating. In addition, the need to control the price level causes the contract to fall and the optimal allocation of resources.
The most optimal and strategic interim objectives for the Central Bank are the nominal interest rate and the nominal money supply. First, we will analyze the targeting of nominal interest rates in monetary policy.

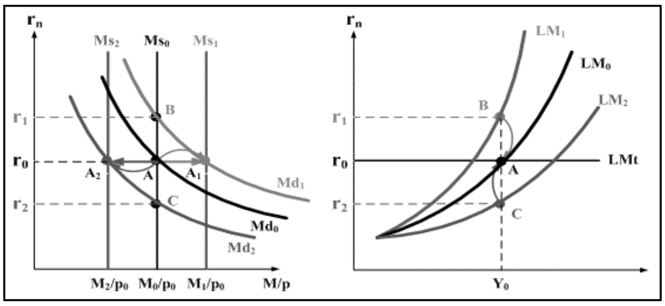

Fig. 2.1. Targeting nominal interest rate[15]

There are two reasons why the nominal interest rates are chosen by the central bank as an interim objective of monetary policy:

1. The nominal interest rate is an indicator that is under constant control by the central bank. If the nominal money quantity is raised by the central bank, the nominal interest rates will decline, and vice versa.
2. The nominal interest rate is consistent with the major monetary policy instruments at the central bank's disposal, that is, the nominal interest rates can be adjusted using the major monetary policy instruments. If the central bank purchases government short-term bonds through an open market transaction, the money supply in the economy will increase, the nominal interest rate will fall and the level of pricing will be increased his process also occurs at the expense of the increase in the nominal money supply in the real sector (with no change in demand for money) and an increase in the value of securities market securities. Meanwhile, the increase in nominal money will lead to an increase in consumption in the economy, a rise in prices, a decrease in interest rates, and an increase in investment. Therefore, nominal interest rates are one of the strategic objectives of the Central Bank as an intermediate objective.

There are also several advantages of targeting nominal interest rates by the central bank. These are:

1. The central bank has the ability to automatically correct nominal interest rates during monetary policy conduct, because the change in the nominal interest rate is proportional to the change in nominal money supply.
2. It is the easiest and fastest way to target nominal interest rates in achieving the ultimate outcome of monetary policy. For example, suppose that the main goal is to reduce the unemployment rate. At that time, in order to increase the investment activity in the economy, the nominal interest rate should be reduced. This is done by increasing nominal money supply. This ultimately affects the growth of national income in the economy.

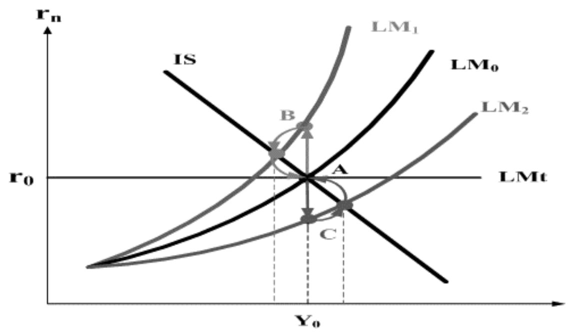

Fig. 2.1. Advantage of the nominal interest rate targeting[16]

There are some problematic aspects of choosing the nominal interest rates as an intermediate target. These are as follows:

1. Changing the macroeconomic demand in the economy can lead to severe consequences by targeting nominal interest rates, because the change in the nominal interest rates will ultimately take place by the change in nominal money supply. The increase in nominal money supply, on the one hand, can lead to the rise in prices and the rise in tax burden due to an increase in the overall demand in the economy, and, on the other hand, the activation of investment activity through savings, and the rise in the overall level of the national income.
2. Often, the central bank seeks to overcome the main objective as a result of an intermediate target in the form of targeted nominal interest rates. This tactic, which has easy and effective indicators, can be the main target of the Central Bank in monetary policy. This is the optimal indicator for short notice of the results of the event;
3. Determining the nominal interest rate that is acceptable for the economy to target a nominal interest rate is also a major problem, because the nominal interest rate also affects the formation of the stock market and asset price movements, without affecting the investment activation in the economy.
4. According to some newcomers, the indicator that activates the investment process in the economy is a real interest rate rather than nominal interest rate. There is a very short circle between real interest rates and inflation, i.e. the difference

[15] **Parasiz I.M.,** “Para ve banka: teorik ve politik uygulamalar” Turkiye – Bursa: Ezgi, 1995–64 s

[16] **Parasiz I.M.,** “Para ve banka: teorik ve politik uygulamalar” Turkiye – Bursa: Ezgi, 1995–78 s

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between nominal interest and inflation is the real interest rate. Accordingly, these economists say that real interest rates appear on the real net, rather than the nominal money supply. In this case, targeting the nominal interest rates can lead to erroneous results;

The use of open market operations to target nominal interest rates could trigger the 1998 "reverse pyramid" event in the Russian economy. That is why M. Friedman says: “closing budget deficit by means of nominal money emissions an anti-inflationary program rather than closing by means of security emissions. This is because the principal and interest payments on securities can double their cash outflows.”

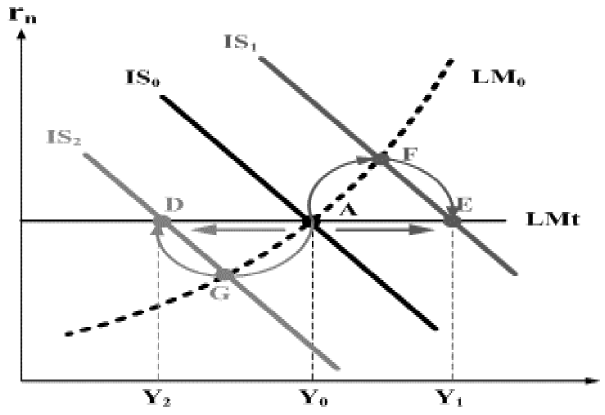


Fig. 2.3. Defects of targeting nominal interest rates[17]

In the 50-60's of the last century, all central banks chose to target nominal interest rates as an intermediate objective. As a result, there are some economists, who claim that stagflation, i.e. the state of increase in unemployment rate and decrease in national gross income, occurred in 1970-1975’s years was the indicator of the central bank's misbehavior in misplaced targeting.

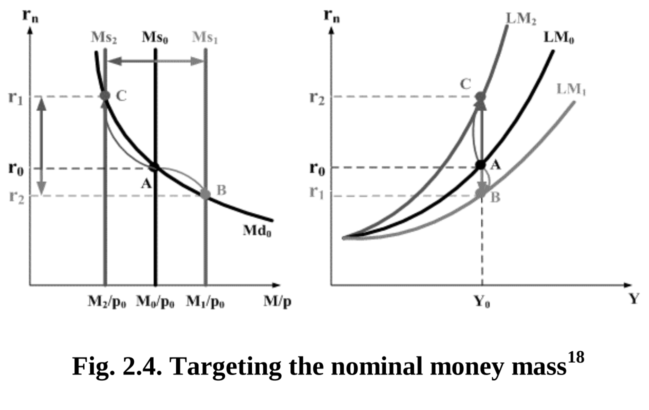


Fig. 2.4. Targeting the nominal money mass[18]

The second strategic intermediate objective of monetary policy is, of course, the nominal amount of money. The central bank should select the monetary aggregate M1 and M2 as the nominal money is accepted as an intermediate target. Because, when the M1 money aggregate is selected, the total cash money can be increased to M2 through the "money multiplier". Therefore, when the nominal money mass by the central bank is selected as an interim objective of monetary policy, M2 will have to choose the currency aggregate as the maximum amount of money. This intermediate goal could have been the main intermediate goal of central banks in the 1970s and 1980s with the influence of the theory of monetarism.

There are several reasons why the Central Bank has chosen the nominal amount as an intermediate target. These are:

1. If the nominal amount of money is the object of the Central Bank, then the nominal amount of money is the basis of all macroeconomic indicators, based on monetarism, new classic and new keywords.

2. Nominal cash money means multiplication of money by multiplying the probability that the money mass M1 will be converted into money mass M2;

3. When the Central Bank chooses nominal cash money as an intermediate target, it should first examine the state of macroeconomic demand, i.e. it should have full knowledge of the macroeconomic situation in the real sector. Because the increase in nominal money will have an impact not only on the interest rate cuts in the financial sector, but also on the growth of the overall macroeconomic demand, which promotes growth in the real sector;

At the same time, the advantage of the Central Bank's nominal cash money supply as a strategic intermediary is the following:

1. The nominal interest rate has the ability to automatically resolve problems that may arise in the targeting. Because targeting the nominal interest rate only affects the economy on the surface by balancing the financial sector, the targeting of the nominal money mass will include the balance of the financial sector and the real sector balance. For example, targeting the nominal money mass causes a decrease in the nominal interest rate in the financial sector, which leads to an increase in consumer demand in the real sector, i.e. an increase in automated costs and activation of savings tendencies and investment. It also increases the overall macroeconomic demand;
2. When the nominal interest rate target by the Central Bank is targeted, the nominal interest rate is negatively less than the targeting process. For example, the decline in the nominal money supply will result in a reduction in the total demand due to the reduction in the cost of the automated consumption, investment, state and taxation. However, the macroeconomic consequences, which will result from the reduction of the total demand, are less than the negative consequences of the crisis in the financial sector due to the decrease in the nominal interest rate, i.e.:$(M\downarrow \rightarrow IS\downarrow) < (r\downarrow \rightarrow LM\downarrow)$$

[17] **Parasiz I.M.,** “Para ve banka: teorik ve politik uygulamalar” Turkiye – Bursa: Ezgi, 1995–86 s

[18] **Parasiz I.M.,** “Para ve banka: teorik ve politik uygulamalar” Turkiye – Bursa: Ezgi, 1995–88 s

3. According to monetarism theory, "if the demand for money is not elastic to the change in interest rate, the actual production of the nominal money target will not change. Therefore, by targeting the nominal money mass, the overall level of prices can be controlled, that is, inflation can be controlled ".

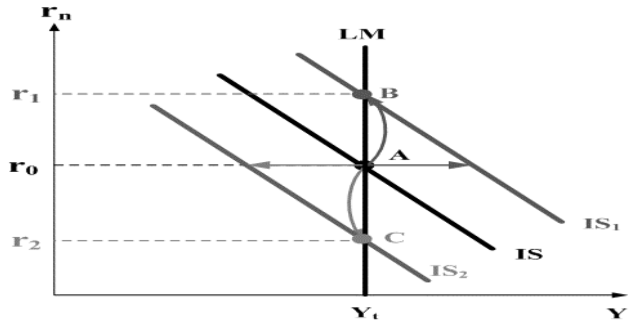


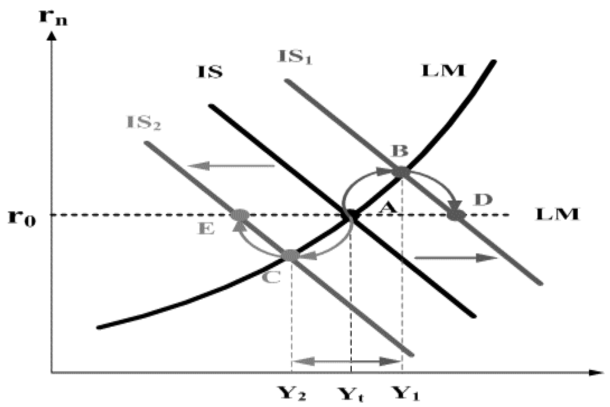
Fig. 2.5. Targeting the nominal money supply when it is inelastic for changes in demand for money[19]

According to the above assumptions, targeting, i.e. protection of nominal money mass, is relative to targeting of nominal interest rates. Because the factor influencing the change in the nominal interest rate is the nominal money supply.
The targeting of nominal interest rates as well as the nominal interest rates is also negatively relevant:
1. First of all, there is a problem with determining the optimal money supply that serves as a functional payment or transaction in the economy. Because some economists, including classics, view money as a "dealing tool" (transact), the latter view the money as a "liquid", that is, a "financial asset", and monetarists look like "capital" - a profitable asset. These three ideas are right for their era. Because money is doing business as a "hedge" for both value-added and value-savvy producers. Accordingly, it is difficult for the central bank to identify the "optimal cash money", which is a control object for the economy on the basis of monetary aggregates M1 and M2.
2. The Central Bank sometimes has to resort to the nominal interest rate targeting process to ensure the economic balance of the nominal money mass or its targeting. Because the target of the nominal amount falls in the balance of the financial sector. In order to re-balance the financial gap, the Central Bank will be forced to take targeted interest rates. This implies the need for a second intermediate goal to achieve an interim goal;

If the demand for money in the economy is stable, then the target money nominal monetary aggregate will have a more realistic net effect than targeted rate. Therefore, targeting the nominal money mass requires a complete set of data from the central bank and a thorough analysis;

[19]**Parasiz I.M.,** "Para ve banka: teorik ve politik uygulamalar" Turkiye – Bursa: Ezgi, 1995–91 s

Figure 2.7. The advantage of the nominal money



mass targeting[20]

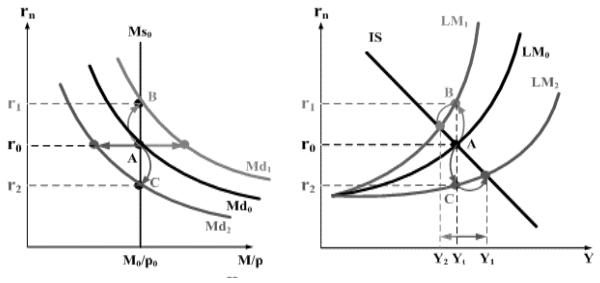


Figure 2.8. The disadvantage of nominal money mass targeting[21]

Based on these analyses, it is crucial for policymakers to properly select interim goals and use impressive monetary instruments. While the nominal interest rate and targeted nominal cash mass are the strategic intermediate target of the central bank, taking these measures requires the "weaponry" to be followed. According to some economists, such as Theodore Lewis[22], nominal earnings and commodity pricing for intermediate purposes of monetary policy after the 1990s will help prevent the above negative moments. Particularly, T. Lewis is based on long-term analysis of the theory of monetarism as the target of monetary policy as an intermediate goal of monetary policy.
The advantage of this is that the increase in the nominal monetary aggregate at the lowering of the general macroeconomic demand prevents the decline in national income. With a decline in macroeconomic demand, the increase in the nominal money supply has led to an increase in national income. Another advantage of this type of monetary policy is that when the Central Bank monetized monetary policy and targeted nominal interest rates, it only affects the increase in macroeconomic expectations and prices, such as inflation. If nominal revenues are selected as a target, the increase in macroeconomic demand is in line with the growth of macroeconomic offers and no further action is needed.

[20]**Parasiz I.M.,** "Para ve banka: teorik ve politik uygulamalar" Turkiye – Bursa: Ezgi, 1995–93 s
[21]**Parasiz I.M.,** "Para ve banka: teorik ve politik uygulamalar" Turkiye – Bursa: Ezgi, 1995–103 s
[22]**Friedman M.,** "Monetary Policy" Jornal of Money credit and Banking. USA,.Chicago. 1982. p – 38.

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On the other hand, the increase in national income is attributable to the investment activity, which is the decline in the nominal interest rates, and also the general macroeconomic demand, while targeting nominal income yields positive results. However, there are some difficulties in these activities, as the author of money is the problem that can not be solved by the central bank. There monthly nominal earnings information can be obtained, but monthly information about nominal interest rates is available on the nominal interest rate.

When T. Lewis offers brand value as a targeted asset, the brand value only reflects the gold price and the overall price index. On the one hand, the fall in the value of the value of the "Brute Woods" in the form of the gold value, and on the other hand, given that the general price index is calculated within the framework of consumer goods, the "index of macroeconomic indices", the effectiveness of monetary policy in these indicators is not so high.

SUMMARY

1. Theoretical bases of monetary policy are mainly related to monetary theory, and monetary policy is the result of theoretical ideas. However, due to delays in the decision-making process in the implementation of monetary policy, the cyclical periodic fluctuations in the context may not produce results from monetary policy.
2. Monetary policy can often have a monopoly policy effect that expands its work directly on labour, capital and commodity markets, and sometimes substitutes for narrow monetary policy;
3. Monetary policy, its instrumentalities, and object and purpose of monetarism are liberal in relation to the theory of Keynes and are based on encouraging market relations.
4. The main objective of monetary policy is to target the nominal interest rates and nominal interest rates to slack the main goals, such as increasing the rate of economic development, maintaining inflation and balancing the prices, ensuring unemployment and equilibrium in the market.
5. Effective use of monetary instruments. The optimal management of cash money in the economy reduces the demand for cash. It is important not to reduce the amount of money, but to reduce the demand for money.
6. In the process of targeting nominal money and interest rates as monetary targets, it is important to keep in mind that shortening the mass of money does not require great measures, but the mass of money requires deep and clear analysis.

The conclusion is that the new theory suggests not only theoretical suggestions on the place of money in the economy but also the practical suggestions at the end of the research. A new look at this monetary theory suggests a deep analysis of the state of monetary institutions and the degree of technological armament, the trust of money-based economic entities, and the alternative ways of monetary spending on the economy in implementing monetary policy. Although these views have little to do with methodological, theoretical, psychological, and ideological foundations, the theory is raising the interest of economists on monetary policy.

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