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CRYPTO · BEGINNER · LESSON 1 OF 15

What Makes Something Money

The jobs money has to do, the qualities that make it work, and where crypto fits in a story that is thousands of years old

9 min read 7 quiz questions with answer key

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What Makes Something Money

IN ONE SENTENCE

Money is whatever people widely accept in exchange because it does three jobs well: it buys things, it measures prices and it keeps value over time. Gold, paper notes and bank balances have all done those jobs, and crypto is the newest attempt.

Life before money: the barter problem

Imagine a village with no money at all. A fisher wants bread, so she walks to the baker with a basket of fish. But the baker does not want fish today. He wants a new coat. So the fisher has to find a tailor who wants fish, trade the fish for a coat, and then bring the coat to the baker. Every trade only works if both sides happen to want exactly what the other one has.

Economists call this the **double coincidence of wants**, and it is the core weakness of **barter**. The more people and goods there are, the harder it becomes to find a match. Some trades never happen at all, and a great deal of time is spent searching instead of producing.

Now add one item that everyone in the village accepts, even if they do not need it themselves, because they know someone else will take it later. The fisher sells her fish for that item and pays the baker with it. Nobody has to find a perfect match anymore. That item is **money**.

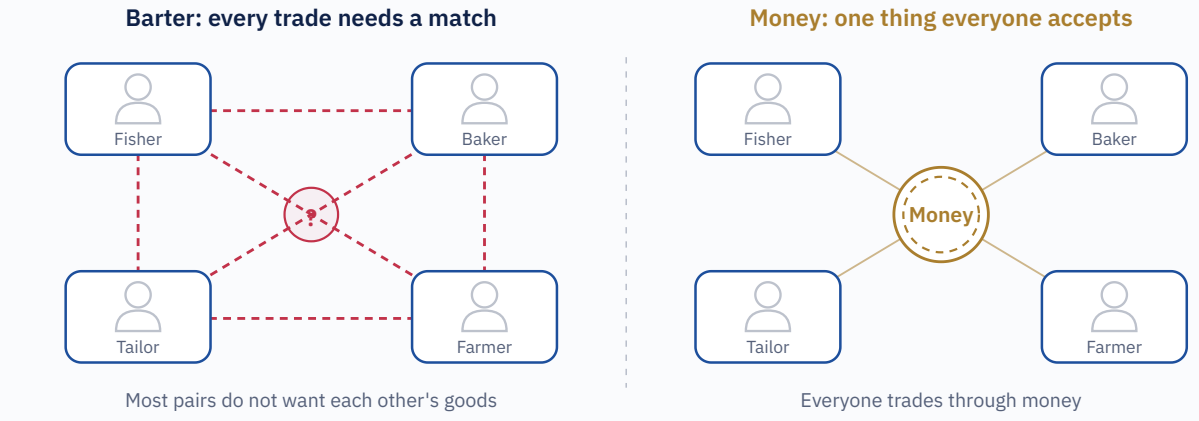


Figure 1. Without money, every pair of traders must find a match, and most cannot. With money, each trader deals with one thing that everyone accepts.

EXAMPLE: COUNTING THE MATCHES

With 4 traders and no money, there are 6 possible pairs, and each pair has to find its own match. With 50 traders there are 1,225 pairs. With money, each trader only needs one relationship: with the money itself. That is why every growing society, sooner or later, has settled on something to use as money.

The three jobs money has to do

Whatever form it takes, money is judged by how well it does three jobs:

- **Medium of exchange.** You can use it to pay for things, and the other side accepts it without fuss. This is the job that solves the barter problem.
- **Unit of account.** Prices are written in it. When a coffee costs 4 and a book costs 20, you instantly know the book is worth five coffees. A shared measuring stick makes comparing, planning and keeping accounts possible.
- **Store of value.** It still buys roughly as much next year as it does today, so you can earn now and spend later.

These jobs support each other. People are happy to accept something in payment if they trust it will hold its value, and prices are only useful in a unit that does not change size every day. When a form of money starts failing at one job, the others usually suffer too.



Figure 2. The three jobs of money. Each one supports the others, so a weakness in one usually hurts the rest.

The qualities of good money

To do those three jobs, a form of money needs certain physical and practical qualities. Over the centuries, six have stood out:

- **Durable.** It does not rot, rust or fall apart.
- **Portable.** Large values are easy to carry or send.

- **Divisible.** It can be split into small amounts for small purchases, and combined for large ones.
- **Uniform.** One unit is the same as any other, so nobody has to inspect each piece. Economists call this being **fungible**.
- **Scarce.** Nobody can create more of it easily or cheaply. If they could, it would lose its value.
- **Widely accepted.** Other people will take it. In the end this is the quality that matters most, and it grows out of the other five.

No form of money has ever scored perfectly on every point. Each one has been a trade-off, and the history of money is largely the story of people swapping one set of trade-offs for a better one.

> **ANALOGY: WHY TOMATOES NEVER BECAME MONEY**
>
> Try using tomatoes as money. They rot within days, so they are not durable. They come in every size, so they are not uniform. Anyone with a garden can grow more, so they are not scarce. Now try gold: it lasts for thousands of years, every ounce of pure gold is the same, and the world's supply grows only slowly. It is no accident that one ended up in vaults and the other in salads.

From shells to screens: a short history

Early societies used goods that were valued in themselves, such as shells, salt, grain or cattle. This is called **commodity money**. Metals slowly took over because they score better on almost every quality above.

The first known coins were struck in **Lydia**, in today's western Turkey, in the late seventh century BC, from electrum, a natural mix of gold and silver. A stamped coin was a big step: its weight and purity were guaranteed by the issuer, so people no longer had to weigh and test metal at every sale.

Paper came next. In Sichuan, China, merchants first issued paper notes called **jiaozi**, and in 1024 the Song government issued its own official series. Paper was far easier to carry than strings of coins. It also brought a new risk: printing more is cheap, and later Song governments issued so many notes that their value collapsed.

For much of the nineteenth and twentieth centuries, many currencies were tied to gold. A note was a promise that you could exchange it for a fixed amount of metal. That link ended for the US dollar on **15 August 1971**, when President Nixon announced that foreign governments could no longer exchange their dollars for gold. From then on, the world's main currencies were backed by trust in the governments and central banks that issue them, and nothing else.



Figure 3. A short history of money, from goods valued in themselves, to coins and paper backed by an issuer, to bitcoin, which is backed by open rules instead of an issuer.

What backs money today

Today's dollars, euros, won and yen are **fiat money**. "Fiat" is Latin for "let it be done": the money has value because a government declares it legal tender, requires taxes to be paid in it, and a central bank manages how much of it exists. It works because people trust that system.

Most of it is not even paper. According to the Bank of England, notes and coins make up only about 3% of the money in the UK economy. Most of the rest is bank deposits, the numbers in accounts that we saw in Blockchain Lesson 1.

Fiat money has real strengths. Central banks can add money to calm a financial panic or support the economy in a deep recession. The trade-off is that the supply can grow year after year, and when money grows faster than the goods and services it buys, prices rise. This is **inflation**, and it slowly reduces the **purchasing power** of every unit you hold.

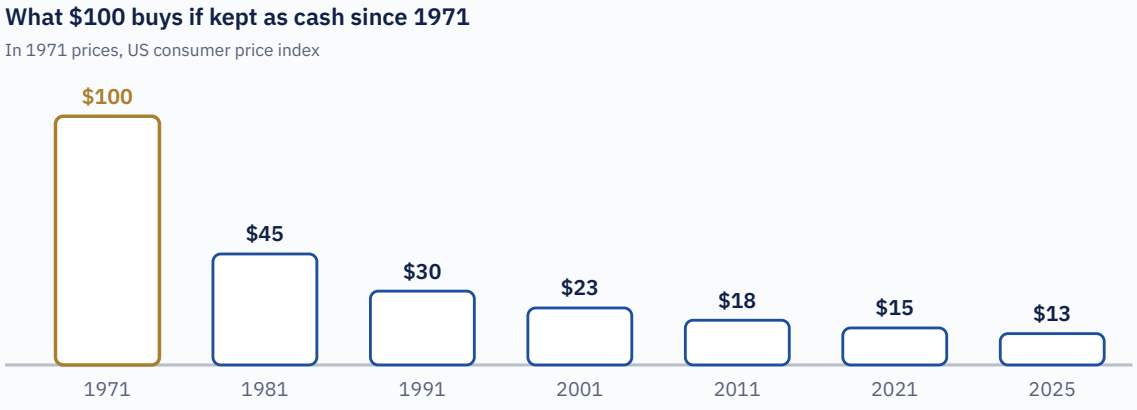


Figure 4. The buying power of $100 held as cash since 1971, based on the annual average US consumer price index. By 2025 it buys about $13 worth of the same goods.

EXAMPLE: $100 SINCE 1971

Using the US consumer price index, a basket of goods that cost $100 on average in 1971 cost about $795 in 2025. Put the other way round, $100 kept in a drawer since 1971 would buy only around $13 worth of those same goods today. Prices did not rise because the goods got better. Each dollar simply buys less.

Where crypto fits

Bitcoin, launched in January 2009, was designed as money with **no issuer**. Nobody can print more than the rules allow: the supply is capped at 21 million bitcoin, and new coins are released on a fixed schedule that slows down over time. The 20 millionth bitcoin was mined in March 2026, and the last is expected around the year 2140. Instead of trusting a government or a bank, users trust open rules that anyone can check, which is the idea the whole Blockchain track was built around.

Measured against the qualities of good money, the picture is mixed:

- **Strong:** it is scarce by design, can be sent across the world in minutes, divides into 100 million units called satoshis, and does not wear out.
- **Debated:** every coin's history is public, so some coins linked to crime can be refused, which makes units slightly less uniform than cash.
- **Weak so far:** its price swings a lot. Within a year of its November 2021 record of about $69,000, bitcoin had fallen more than 70%. A coffee priced in bitcoin would need a new price tag every day, which makes it a poor unit of account for now. Acceptance is also limited: El Salvador made bitcoin legal tender in 2021, but in January 2025 it made accepting bitcoin voluntary.

So most people today treat bitcoin less as everyday cash and more as a possible **store of value**, often compared to digital gold. Whether it will keep that role over the long term is one of the big open questions in finance, and serious people disagree.



Figure 5. A simplified scorecard of three forms of money against the qualities of good money. Fiat means government money such as the dollar, including bank balances. Several ratings are debated.

Two different answers from the crypto world

Crypto has produced two quite different responses to the qualities of money, and you will meet both throughout this track:

- **Scarce assets such as bitcoin** focus on a fixed or predictable supply and freedom from any issuer, accepting large price swings as the cost. Lesson 2 looks at how bitcoin's supply and its halvings work.
- **Stablecoins** do the opposite. They aim for a steady price, usually one US dollar, by holding reserves or other assets behind each coin. They are good at being a medium of exchange and unit of account inside crypto, but they bring back an issuer that you have to trust. Lesson 6 explains how they work and when they fail.

Neither is the complete answer. Each one chooses a different set of trade-offs, just as shells, gold and paper did before them.

Why this matters for traders

- **The money story moves prices.** When inflation worries grow or central banks add money, the scarce money argument for bitcoin and gold tends to draw more attention and buyers. When central banks tighten and money becomes harder to borrow, crypto has often come under pressure, as it did in 2022.
- **Every price has two sides.** BTC/USD is bitcoin measured in dollars. A rise can mean bitcoin is getting stronger, the dollar is getting weaker, or both. Watching the dollar helps you read moves in bitcoin and gold.
- **Stablecoins are the unit of account of crypto markets.** Most crypto trading pairs, and the profit and loss on many futures contracts, are counted in dollar stablecoins such as USDT and USDC, not in bitcoin.
- **Volatility cuts both ways.** The large swings that make bitcoin a weak unit of account are the same swings that attract traders. They also mean position size and risk deserve more care than in calmer markets.

Key terms

Barter	Trading goods directly for other goods, without money. It only works when both sides want what the other has.
Medium of exchange	Something people accept as payment for goods and services, even if they do not need it themselves.
Unit of account	The measure in which prices are written, so that different things can be compared.
Store of value	Something that keeps its purchasing power over time, so you can earn now and spend later.
Fungible	Interchangeable: every unit is equal to every other unit of the same kind.
Fiat money	Money issued by a government and managed by a central bank, valued because of trust in that system rather than a link to gold or another commodity.
Inflation	A general rise in prices over time, which means each unit of money buys less.
Purchasing power	How much a unit of money can actually buy.

Key takeaways

1. Money exists to solve the barter problem: without it, every trade needs both sides to want exactly what the other has.
2. Good money does three jobs: medium of exchange, unit of account and store of value.
3. It needs to be durable, portable, divisible, uniform, scarce and widely accepted, and every form of money has been a trade-off among these.
4. Since 1971 the world's main currencies have been fiat money, backed by trust in governments and central banks, and their purchasing power tends to fall over time.
5. Bitcoin scores well on scarcity, portability and divisibility, but is still weak as a unit of account because of its volatility, while stablecoins make the opposite trade-off.

Test yourself

Circle one answer for each question. The answer key with explanations is on the next page. You can also take this quiz online at markettalks.info and see your score instantly.

1. What is the main problem with barter?

- A Goods lose their value too quickly
- B Both sides must want exactly what the other has
- C Governments do not allow it
- D It requires a bank account

2. Prices in a shop are written in won. Which job of money is the won doing?

- A Store of value
- B Medium of exchange
- C Unit of account
- D Collateral

3. Why would tomatoes make poor money?

A They are too valuable
B They are hard to divide
C They rot, vary in size and anyone can grow more
D Nobody likes tomatoes

4. What changed on 15 August 1971?

A The first paper money was printed
B Foreign governments could no longer exchange US dollars for gold
C Bitcoin was launched
D The euro replaced national currencies

5. According to the Bank of England, roughly how much of the money in the UK economy is notes and coins?

A About 3%
B About 25%
C About 50%
D About 90%

6. What does inflation do to money you keep as cash?

A It increases its purchasing power
B It has no effect on cash
C It reduces what each unit can buy
D It converts it into gold

7. Which job of money is bitcoin currently weakest at?

A Being scarce
B Being sent across borders
C Being divided into small units
D Being a stable unit of account

Answer key

1 B

Both sides must want exactly what the other has

This is the double coincidence of wants. Money removes it, because everyone accepts money even when they do not need what the other person is offering.

2 C

Unit of account

Writing prices in one shared unit is the unit of account job. It lets you compare the value of very different things at a glance.

3 C

They rot, vary in size and anyone can grow more

Tomatoes fail on durability, uniformity and scarcity. Good money has to last, every unit has to be the same, and it must be hard to create more.

4 B

Foreign governments could no longer exchange US dollars for gold

President Nixon closed the gold window. After that, the world's main currencies were fiat money, backed by trust in their issuers rather than by gold.

5 A

About 3%

Only about 3%. Most money today is bank deposits: records in bank databases rather than physical cash.

6 C

It reduces what each unit can buy

When prices rise, each unit of money buys less. $100 kept since 1971 buys only around $13 worth of the same goods today.

7 D

Being a stable unit of account

Bitcoin's large price swings make it hard to use for writing prices. It does well on scarcity, portability and divisibility, which is why many people treat it as a possible store of value instead.

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Up next: Lesson 2 Bitcoin as Money: Fixed Supply and Halvings

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