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Abolition of Cash or Loss of Anchor

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Summary

The squeezing-out of cash means, in essence, the elimination of government money for the public. We know that this process has been going on since the 18th century and could not be reversed even by the gold standard, which applied only to central bank notes. It was not the 'War on Cash' that dealt cash the final blow: it was merchants' refusal to accept national currencies in banknotes and coins. In a cashless society, ***only private money exists****. The fundamental problem is that the disappearance of central bank notes means the end of risk-free money for the public, the only money with a stable nominal value. Without banknotes, £10 will not always be £10, €10 will not always remain €10, nor will $10 always stay $10. The end of cash will remove the final line of defence against monetary policy without constraint and corporate money issuers.*

Key words: *cash, banknotes, government money, private money, the course of cash, war on cash, legal tender status, payment tigers.*

The gradual expulsion of government money

Coins are government money and so is, ultimately, central bank money. Since non-cash central bank money is not available to the general public, ***government money for the public*** is comprised of coins and central bank notes, in other words, of cash. So the expulsion of cash is, essentially, the abolition of government money.[1]

We know that this process has been going on since the 1750s, when the bankers of London concluded that issuing banknotes was not as profitable as doing business with non-cash money on account. This initial squeeze-out of cash was not halted by the introduction of large-denomination banknotes (the minimum being £10), which were readily used by businesspeople and the wealthy. Simply, non-cash money on account proved superior for wholesale payments. The lowering of banknote denominations throughout the 19th century did not slow the process down but merely meant increasingly fewer coins were used for daily retail payments.

In a seeming paradox, the ousting of cash could not be stopped even by the gold standard, which applied to central bank notes of most countries in Europe and further afield but not to households' and firms' deposits with commercial banks. Moreover, before the 1930s, the convertibility of bank deposits into banknotes was not assured by the government, but depended on the liquidity and solvency of the saver's bank. The explanation for this lies in the efficiency of account-to-account wholesale payments and interest returns on deposits.

The final exodus

The final exodus of cash from retail payments, its last stronghold, began with the introduction of payment (credit and debit) cards, followed by ATMs and PoS terminals. Understandably, the innovations were broadly accepted by most money holders: they facilitated payment services, and money in banks was convertible into banknotes at face value.

Over the past decade, contactless payments by card and smartphone have meant cash has increasingly been 'out', with its legal tender status reduced to nothing but a myth. The cashless economy ignores central bank notes, or government money. 'When people come across a cashless café, restaurant or pub for the first time they can be surprised that they don't have a right to use cash in the UK, and that cash acceptance is determined by the party offering the service.'[2] It would be interesting to see whether the UK Government and the Bank of England would react if *the party offering the service* in London posted a note announcing it only accepted euros, bitcoins, or libras. New York and many other cities throughout the world are facing the same issue. Stockholm has taken this absurdity to new heights: there, krona notes are not accepted by nearly anyone, except the Riksbank, and, perforce, hospitals.[3]

Central banks will continue to supply cash until the last *café, restaurant or pub* stop accepting it. Faced with the threat of the Covid-19 pandemic, most countries' national banks re-affirmed this position, with the Bank of England being one of the first to do so: 'The provision of secure physical cash is a core part of our mission. The Bank has made clear its commitment to *continuing to produce cash for as long as people want to use it*. … Acceptability requires not just that banks distribute and "bank" cash. It also requires that **merchants accept it.**'[4] Only days earlier, on 19 February 2020, BBC News reported that the *UK's cash system 'will collapse without new laws'.*

So, it turns out, acceptance of a nation's currency in banknotes and coins depends not on their legal tender status, the government, or the central bank, but on merchants and their payment policies. The US has nearly identical rules in place: 'Private businesses are **free** to develop their own policies on whether or not to accept cash unless there is a state law which says otherwise.'[5]

With the global exodus of cash from payment systems and economies in full force, cash was put on two symbolic trials, one in 2015 in Zurich and another in 2019 in Frankfurt. The principal organiser was SUERF, the European Money and Finance Forum, seemingly guided by the honourable intention of provocatively presenting and thoroughly discussing issues that are set to determine the fate of cash. Given the arguments for and against, as advanced by *witnesses for the **prosecution*** and *witnesses for the **defence***, and the turbulent events that took place between 2015 and 2019, it will be useful to look at the conclusions of these two events.

Cash on trial

The first conference, held in November 2015, saw simultaneous presentation of both indictments against and evidence in favour of cash. ‘Cash has been accused of three sins: First, cash is inefficient and costly to use and society would be better off without it. Second, it promotes crime, and facilitates money laundering and tax evasion. Third, it makes negative nominal interest rates infeasible.’[6]

One of the main arguments in defence of cash was that it was *fast and easy to use*. Also highlighted were its privacy, anonymity, role in preventing central banks’ extreme interest rates, the fact that the state earns income from seigneurage, and so on. The defence focused on rebutting specific accusations, but other benefits of cash were advanced as well. ‘Cash provides an insurance against very bad outcomes, such as economic crises, hyperinflation, or the failure of computer or electricity networks. The costs of cash can therefore be viewed as an insurance premium.’[7]

The *Cash on Trial* conference, which took place in May 2019, recorded fewer accusations against cash, with its inefficiency in payment being the most serious one. The principal indictments are condensed in the title of a speech made by one of the witnesses for the prosecution: ‘Cash – an inefficient and outdated means of payment’.[8] The evidence and arguments in favour of cash once again prevailed over the accusations, even when it came to crime and terrorism.[9] It was especially emphasised that *the tangible nature of cash contributes to the liberty and autonomy of members of society*, allowing them to ***live off the grid.***[10]

Between the two conferences, Kenneth Rogoff published his *The Curse of Cash*, with the gruesome title matched by equally gruesome content. The weight of the accusations laid at the feet of banknotes (the author is a supporter of coins, provided they are made of gold) requires a detailed look, before we move on to the *war on cash*, of which Rogoff is an enthusiastic supporter and proponent.

The Curse of Cash

The author contradicts himself from the very outset. He admits to having devoted an entire book to a ‘sideshow’: ‘Indeed, most academic and policy academics tend to think of physical paper currency as an irrelevant sideshow in today’s world of high-tech banking and finance.’ (*Preface*) The titles of the three sections reveal his preferences and intentions: Part 1, *The Dark Side of Paper Currency*; Part II, *Negative Interest Rates*; and Part III, *International Dimensions and Digital Currencies*.

On the first page of *The Dark Side*, having referenced Goethe’s *Faust*, Rogoff rolls out an outrageous charge: ‘Goethe, writing early in the nineteenth century, was nothing if not prescient. Without paper money, there might have been no German hyperinflation, and perhaps no World War II’.[11] Goethe indeed knew of the collapse of John Law’s bubble, and read Adam Smith and even Henry Thornton (he even revised the German edition of Thornton’s *Paper Credit*),[12] but could not have been so far-sighted as to envisage a global conflict caused by the hyperinflation of banknotes, which Rogoff disparagingly calls *paper money.* On the contrary, it was banknotes that allowed Germany to burn off the greatest part of its World War I reparations in the fire of hyperinflation while its citizens rejected the Reichsbank's worthless paper. Goethe was ultimately unable to convince his fellow Germans that cash was *cursed*, and they continue to rank amongst the world's greatest adherents of banknotes. Finally, associating World War II with banknotes is mockery of this most tragic event in human history.

Rogoff illustrates the unreliability of coins, the oldest form of cash, by citing their debasement during the decline of the Roman Empire. 'In Rome, coin debasement produced cumulative inflation of 19,900% over the period 151-301 AD, a period that saw major revolts and plague' (p. 19). Over these 150 years, this seemingly terrifying rate of inflation works out at ***no more than 3.6% annually,*** an unattainable goal from the 1960s to the 1990s for many developed countries, the UK and US included. The effects of plague are now plainly visible from our own perspective, tinged as it is by Covid-19. Rogoff has thus slandered ancient Rome's monetary policy unprovoked. The table showing *Selected peak debasement years for European coinage, 1300-1812* (p. 20) is similarly erroneous, as the peaks indicate cumulative debasement over the course of decades. Reducing the values to average annual growth rates would have revealed the true pace of coinage debasement.

Even though he considers it cursed, Rogoff does not dispute the importance of *'paper money'* for his own nation's independence: 'Paper currency also played a major role in the American War of Independence from 1775 to 1783, financing the vast majority of the colonists' expenditures.' (p. 27). It is questionable whether the colonists saw the 'paper' as money or as war bonds, but the author would have to admit that no other means of issuing money would have given as much help to his ancestors in gaining liberty.

After thoroughly enlarging on all the evils and disasters caused by *'paper money'*, Rogoff proposes a most cunning ***Plan for Phasing Out Most Paper Currency***. His proposal is based on *three guiding principles: first, make it more difficult to engage in anonymous untraceable transactions; second, the speed of transition needs to be slow; and, third, that* **poor and unbanked individuals** *have access to free basic debit-accounts and possibly also basic smartphones*.[13] The key oversight of his concept of a ***total banked regime*** is the likely disobedience of these poor and unbanked individuals, who may refuse to take up the *free basic debit-accounts* and *basic smartphones*. Perhaps this promoter of social engineering worthy of any totalitarian regime ought to think about obligatory ***basic microchip implants*** for the *poor and unbanked individuals*.

To date, the proposals Rogoff suggests *for phasing out most paper currency* have not helped bring about his desired banishment of cash, unlike the fluidity of *legal tender status* banknotes, which the author fails to recognise as an option for swift *de-cashing*.

The rapid phasing out of cash from most of the world in the latter half of the 2010s nevertheless proved too slow for the interests of the banking sector and many non-bank companies and institutions. Financial inclusion for all (see G-20 – *High-level Principles of* ***Digital*** *Financial Inclusion*, September 2016) and a cashless society were the rallying cries for both governments and the payment industry. Analysts at Germany's largest bank concur: '***Governments, banks and card providers share at least a goal: the elimination of cash***'.[14] This is why a global war on cash had to be declared.

War on cash

A relatively comprehensive definition of this conflict and its objectives was given by Lawrence White: '[t]he "war on cash" refers to a set of policies, in the United States and around the world, deploying the power of government agencies to suppress the use of paper currency. The principal aim is to shift transactions to credit card and bank account media that leave an electronic data trail for law enforcement and tax authorities. A secondary aim is to raise the cost of cash storage so as to allow the central bank to push nominal interest rates further below zero'.[15]

Government agencies include the Fed, the Treasury Department, FDIC, and other public authorities whose decisions directly or indirectly affect the use of cash, here US dollar notes and coins. Similar government agencies are also employed in most other countries to eliminate cash. Yet the government is not the only stakeholder mobilised to combat cash. The 'war effort' receives robust support from banks and other financial institutions, as well as consulting firms, universities, research institutes, social media networks, non-profit foundations, and a host of other related entities.

Ensuring a means of payment that *leaves an electronic data trail for law enforcement and tax authorities* is a key focus of the conflict, yet not its primary goal. The primary and ultimate outcome is to abolish government money and transfer money issuing power from the public to the private sector. This makes banknotes only a tactical target, with central bank reserves remaining the strategic objective. The public have never fully understood the nature of these reserves, making them much easier to take over under the veil of a public-*private* partnership. Obviously, before this can happen, banknotes and coins must be abolished as evidence of erstwhile issuing power. Cash is here only collateral damage, and the private sector may reissue it at some point in the future in the guise of digital notes and coins.

Many central banks are in favour of the abolition of their own products, citing their technological obsolescence – an issue they hardly gave any thought to until recently. This is probably the only recorded case in economic history of a monopolist advocating the removal of its monopoly to the benefit of a technologically more advanced competitor. Perhaps absurdly, cash is being defended from central bankers by supporters of *free banking*, *currency competition* and *new private monies.* One of the most courageous of these cash defenders is Kevin Dowd:

‘One of the most significant developments in economic policy in recent years has been a gradually escalating government war against cash. … The abolition of cash threatens to destroy what is left of our privacy and our freedom … Quite simply, the government’s war against cash is the state’s war against us. Andy Haldane, the chief economist of the Bank of England – announced that he too was in favour of abolishing cash.’[16]

Policy tactics involve various restrictions and monitoring requirements that hinder the holding of cash, suppress cash transactions, and generally make cash more expensive to use.[17] However, none of these tactics is as effective at squeezing cash out as the ephemeral nature of cash’s *legal tender* status. Merchants’ freedom to set their own payment policies, as described above, has been accelerating the disappearance of banknotes and coins.

How the war can end

At the war’s end, the merchants will lead us into a cashless society. The Swedish central bank has an answer as to what that society will look like: ‘In a cashless society, a restricted group of financial corporations has access to risk-free central bank money. The general public, in contrast, does not.’[18] By being denied to the public, central bank money would lose its risk-free status, whereas reserves would remain private bank money. Soon after, a public-private venture would take over the issue of reserves, which would then comprise all of base money (without cash). Global payment corporations, encouraged by the full control they already exercise over payment systems, have no reason to refrain from reaching after the power to issue money. Monetary sovereignty, lost in the intricate interpretations of legal tender status, would be replaced by the sovereignty of the corporate issuers of reserves, i.e. of money.

Public-private issue of reserves will serve as an overture to the abolition of central banks and the fully private issuance of base money. The government would retain its deposit insurance function that employs taxpayer (our) money, whereas regulation and oversight would be the remit of independent agencies created from remnants of the former central bank. ‘In a cashless society, a financial crisis could arise in a situation where ***only private money exists***’ (Riksbank, *Petition*, p. 8). The function of *lender of last resort* would have to be assumed by the new money issue masters, as it is inseparable from issuing authority, but is nonetheless difficult to reconcile with their private interests.

The incompatibility between the power of issue and private interests of corporate money issuers ultimately limits the feasibility of this new monetary order sketched out in the preceding paragraphs. The pretenders to the sovereign right to issue money are the same private banks whose business policies have caused so many financial and economic crises. The transformation of banks and payment providers from payment intermediators to money issuers will not do away with their genetic vulnerability. By definition, a money issuer cannot be illiquid, but it may still devalue its own product. No formal definition of a *unit of account* by the government will allay this danger, and corporate money issuance will inevitably lead to monetary chaos.

The new monetary order of the cashless economy hides a built-in construction error: the abolition of cash, which guarantees the stable nominal value of money. The absence of stable nominal value removes two of money's fundamental functions, unit of account and measure of value. This structural weakness will bring the planned monetary system crashing down soon after central bank money for the public is scrapped. The abolition of cash will ultimately prove to be a Pyrrhic victory for the cashless armada.

Loss of anchor

Banknotes are the nominal anchor of the economy due to their stability of denomination, meaning that their denominated face value does not change. They anchor the nominal prices of goods and assets and relative price ratios, which is a precondition for the operation of product and financial markets. The nominal certainty of factor incomes (salaries, profits, rents, interest payments, dividends) underlies all our decisions to produce, sell, consume, save, lend, borrow, and invest. Without banknotes to serve as their anchor, the certainty of nominal values in the economy will inevitably be lost.

Their unchanging nominal value and transferability lend banknotes another unique characteristic: they ***discipline*** banks and other financial intermediaries, including the very central banks that issue them. Of all the forms of money, banknotes are the easiest to withdraw and dispose of, which sends a clear signal to their issuers and depositaries about how much we trust them. In a cashless economy, we would not be able to take out our money from the bank – *all we could do is move to a different bank.*

Immediate settlement is another characteristic of banknotes that sets them apart from other means of payment, which cannot function without payment providers. 'A banknote is the payment instrument by which the ***highest settlement finality*** can be achieved'.[19] This *highest settlement finality* is clearly the reason why, according to Milton Friedman and Anna Schwartz, 'there is no pressure by banks or other groups to gain that **privilege**'.[20]

Apart from all the advantages cited above, which are derived from the intrinsic nature of banknotes and the credibility of their central bank issuers, other prerequisites exist that have long been completely ignored. Conclusions of the Swedish *Committee of Inquiry of **1881*** can serve as a reminder: 'The inquiry's three main reasons for a banknote monopoly were: 1) banknotes should be entirely free of risk, 2) banknotes must be issued without a short-term profit motive, and 3) revenues from the issue of banknotes are necessary to fund a central bank's function in society so that it does not have to act according to a profit motive.' (Riksbank, *Petition*, p. 9). These past findings clearly indicate that what makes banknotes unique is their absence of *a short-term profit motive* and private profit from their issue, or seigniorage.

The re-introduction of the gold standard, which not even Kenneth Rogoff believes to be far-fetched, is also impossible without banknotes. Banknotes were the only form of money that allowed the gold standard to operate. Gold coins and gold certificates are not viable in practice as means of payment.

There is no reason to invoke the costs of payment in the retail sector as an argument against cash, as data indicate it is competitive in comparison with other means of payment. [21] Of course, if it continues to be squeezed out of everyday transactions, cash will lose its cost competitiveness.

In spite of all their exceptional qualities, banknotes are disappearing, and their passing marks the end not only of physical central bank money, but also of risk-free government money for the public. Its technological development neglected by its issuers, no longer accepted as *legal tender*, lacking an heir in the form of central bank digital notes, this authentic money has no chance of survival in the payment market. And so the precious heritage of Sir Robert Peel will be irrevocably lost in today's world in which the banishment of cash has become a sign of progress, and where those the furthest advanced on that road are held up as paragons. 'An emerging group of ***"payment tigers"*** have also made especially rapid progress – Poland, Ghana, Malawi, and Rwanda. Rwanda aims to become a cashless economy by 2024.'[22]

Technologically superior payment methods will obviously replace traditional banknotes permanently. Most consumers and merchants now rightly want to use these vastly more efficient means of payment. The fundamental problem here is that the disappearance of banknotes means the end of risk-free money for the public, the only money that has stable nominal value. Without banknotes, £10 will not always be £10, €10 will not always stay €10, nor will $10 always remain $10. This will remove the final line of defence against *monetary policy without constraint* and corporate money issuers.

STRENGTHEN THE NOMINAL ANCHOR OF YOUR INCOMES AND ASSETS

KEEP YOUR CASH IN YOUR HANDS

[1] The term *government money* is more precise and modern than *sovereign money*, but not exclusive.
[2] Access to Cash Review, *Final Report*, London, March 2019, p. 86.
[3] *See:* V.V. Lepin (2020), How Money Disappears, CBM *Research*, Paper 1, April 2020.
[4] John Cunliffe, Deputy Governor (2020), It's time to talk about money, *Speech*, 28 February 2020, p.6, 7.
[5] U.S. Department of the Treasury – *Legal Tender Status* (Resource Center).
[6] Aleksander Berentsen and Fabian Schar (2016), The fallacy of a cashless society, In: Cash on Trial, *SUERF Conference Proceedings 2016/1*, February 2016, p. 14.
[7] Christian Beer et al (2015), Cash on Trial, *Findings from a conference*, SUERF.
[8] McKinsey&Company (2019), Cash – an inefficient and outdated means of payment, *Witnesses for the Prosecution*, Cash on Trial Mk II, SUERF Conference, 20 May 2019.
[9] Frederich Schneider (2019), Restricting or abolishing cash: An effective instrument for eliminating the shadow economy, corruption and terrorism? In: Urs Birchler et al (eds.), Cash on Trial Mk II, *Conference Proceedings 2019/1*, SUERF, p. 53-66.
[10] Morten Bech and Amber Wadsworth (2019), What is money? Comparing cash and central bank digital currencies, In: Urs Birchler et al (eds.), Cash on Trial Mk II, *Conference Proceedings 2019/1*, SUERF, p. 24-31.
[11] Kenneth Rogoff (2016), *The Curse of Cash*, Princeton University Press, p. 15.
[12] Hans Binswanger (1994), *Money and magic: a critique of the modern economy in the light of Goethe's "Faust*", The University of Chicago Press.
[13] 'The proposal here is driven by three guiding principles. First, the ultimate goal is to make it more difficult to engage in anonymous untraceable transactions repeatedly and on a large scale. … Second, the speed of transition needs to be slow, stretching changes out over at least 10-15 years. Gradualism helps avoid excessive disruption and gives institutions and individuals time to adapt. (p. 92) Third, it is essential that ***poor and unbanked*** individuals have access to free basic debit accounts (or the future equivalent), and possibly also basic smartphones, as several countries have already done or are contemplating.' (p. 93). (Kenneth Rogoff (2016), *The Curse of Cash*).
[14] Marion Laboure (2019), Cryptocurrencies: the 21st century cash, *Imagine 2030*, Konzept # 17, Deutsche Bank Research, December 2019, p. 58.
[15] Lawrence White (2018), The Course of the War on Cash, *Cato Journal*, Vol. 38, No. 2, p. 477.
[16] Kevin Dowd (2017), Killing the cash cow: Why Andy Haldane is wrong about demonetisation, *Briefing Paper*, Adam Smith Institute, London, April 2017, p. 1.
[17] 'The main policy tactics in the war on cash are currently four: 1. Abolishing high-denomination banknotes. 2. Place a maximum legal value on cash payments. 3. Require declarations from any party carrying a cash amount above a specified value across the national border. 4. Require banks to report to authorities any cash deposits or withdrawals in amounts above (or suspiciously near) a specified value.' Lawrence White (2018), The Course of the War on Cash, p. 478-9.
[18] Sveriges Riksbank (2019), Petition to the Riksdag – *The state's role on the payment market*, Summary, p. 9.
[19] Wataru Takahashi (ed.) (2012), *Functions and Operations of the Bank of Japan*, Institute for Monetary and Economic Studies, Bank of Japan, p. 55.
[20] 'While we therefore see no reason currently to prohibit banks from issuing hand-to-hand currency, there is no pressure by banks or other groups to gain that privilege.' Milton Friedman and Anna Schwartz (1987), Has Government Any Role in Money, In: Anna Schwartz (ed.), *Money in Historical Perspective*, NBER & University of Chicago Press.
[21] 'As a result of the low fixed costs, cash payments up to an average payment amount of just under €20 are the most cost-efficiency for the retail sector.' Deutsche Bundesbank (2019), The costs of payment methods in the retail sector, *Monthly Report*, June 2019, p. 107.
[22] Markus Massi et al. (2019), How Cashless Payments Help Economies Grow, BCG: Boston Consulting Group, May 28, 2019.