Central banks respond to decline in cash

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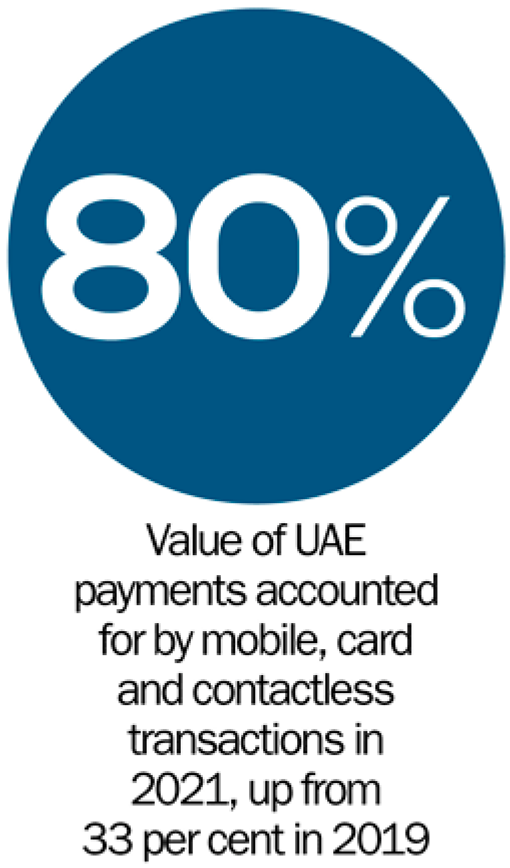
Cash use falls to less than 10 per cent of total value of payments among major economies

The pandemic has had **a profound impact on the global payments sector** (https://www.researchgate.net/publication/360114595_The_global_pandemic_laboratory_of_the_cashless_economy?channel=doi&linkId=626911618e6d637bd1022d6f&showFulltext=true). In many of the world's major economies, cash declined to less than 10 per cent of the total value of face-to-face payments in 2021.



In many emerging economies, too, more than 50 per cent of payments are now transacted through digital means, as reported in the **2022 Global Payments Report** (https://worldpay.globalpaymentsreport.com/en) by financial services company FIS.

Among developed markets, notable outliers are Germany and Japan, where the preference for cash remains strong for cultural and demographic reasons.

Advancing e-payment markets

The UAE and Italy, still largely cash-dependent three years ago despite their advanced banking and payment sectors, are now firmly in the e-payment camp (see the last chart below).

Digital payments accounted for 80 per cent of the total value of payments in the UAE in 2021, up from 33 per cent in 2019 – reflecting the increasing sophistication, diversity and competitiveness of the UAE's payment sector.

Among the most remarkable transformations is India, where e-payments have grown from 29 per cent to 63 per cent of the value of total payments.

This reflects the success of a massive financial inclusion drive integrated into the Digital India Programme, launched in 2015 to digitalise the full range of government services available to citizens, reduce the informal economy and strengthen social safety nets.

> **Concern for safeguarding money as a public good seems to have been missed in**

While most emerging economies share these objectives, few have pursued them at such a scale and in such a strategic manner.

The proportion of banked adults in India grew from 54 per cent in 2014 to 81 per cent in 2018 – a phenomenal leap among emerging economies that has firmly positioned India alongside China as a digital economy powerhouse.

cryptocurrency circles

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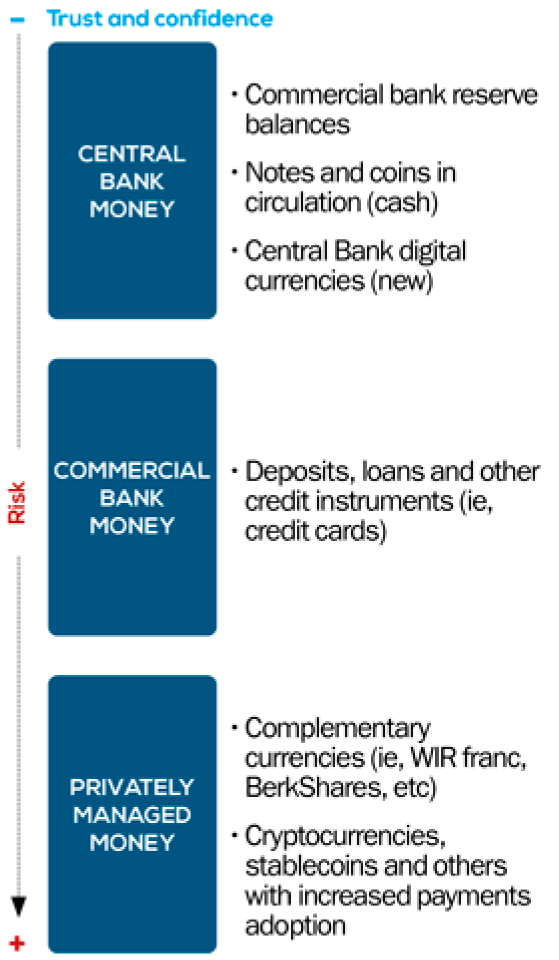
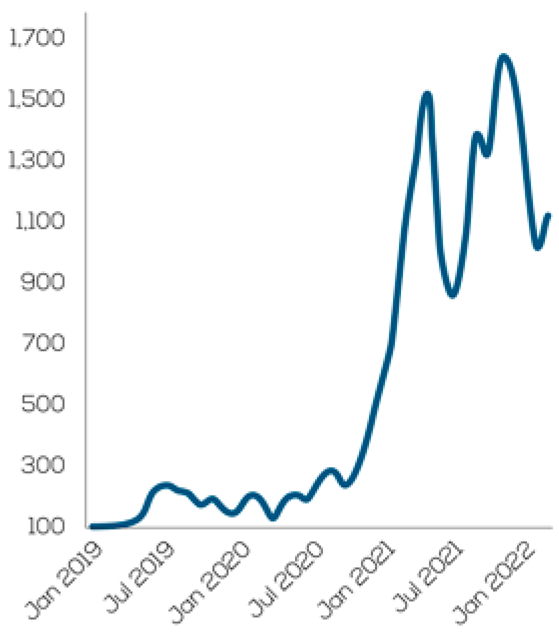
The two also lead the world in their progress towards issuing central bank digital currencies (CBDCs).

MONEY HIERARCHY IN AN EVOLVING PAYMENT LANDSCAPE



S&P CRYPTO BROAD MARKET INDEX
Jan 2019=100



Source: S&P Cryptocurrency Broad Digital Marketing Index, 9 March 2022

The risks of no cash

An unforeseen consequence of the boost in digital payments instigated by the pandemic is the new impetus to CBDC plans.

For several years, central banks in the major economies have been concerned that the declining use of cash by individuals and its acceptability by merchants could lead to a situation where payment systems end up entirely controlled by private entities, whether banks, card associations or privately managed digital currencies.

In Sweden, the e-krona project is seen as a necessary response to this scenario, allowing the central bank to replace cash with a digital national currency that is secure, efficient and accessible to all.

Japan’s central bank vice-governor expressed similar concerns in 2019, stating that as technological innovation evolves, “the retail payments market structure could suddenly change dramatically, pushing us toward a cashless society. In some cases, the need for CBDC issuance may suddenly increase”.

In its digital currency white paper issued in June 2021, the Bank of England stressed that any CBDC design needs to be compatible with offline payments, potentially using low-cost smartcards, to be accessible to those without smartphones or internet access.

A stabilising role

This concern for safeguarding money as a public good seems to have been lost on cryptocurrency circles, with claims that crypto-currencies threaten national currencies or should actively seek to replace them.

Beyond their headline-grabbing effect, these statements reflect a poor understanding of economics and the money hierarchy.

A century ago, British economist Ralph George Hawtrey, in his book Currency and Credit (1919), detailed how the cashless economy is unviable in the absence of central bank money.

Central bank money stabilises the value of commercial bank money, which otherwise would swing erratically, and guarantees that debt and credit instruments are ultimately convertible into a universally accepted means of payment: cash.

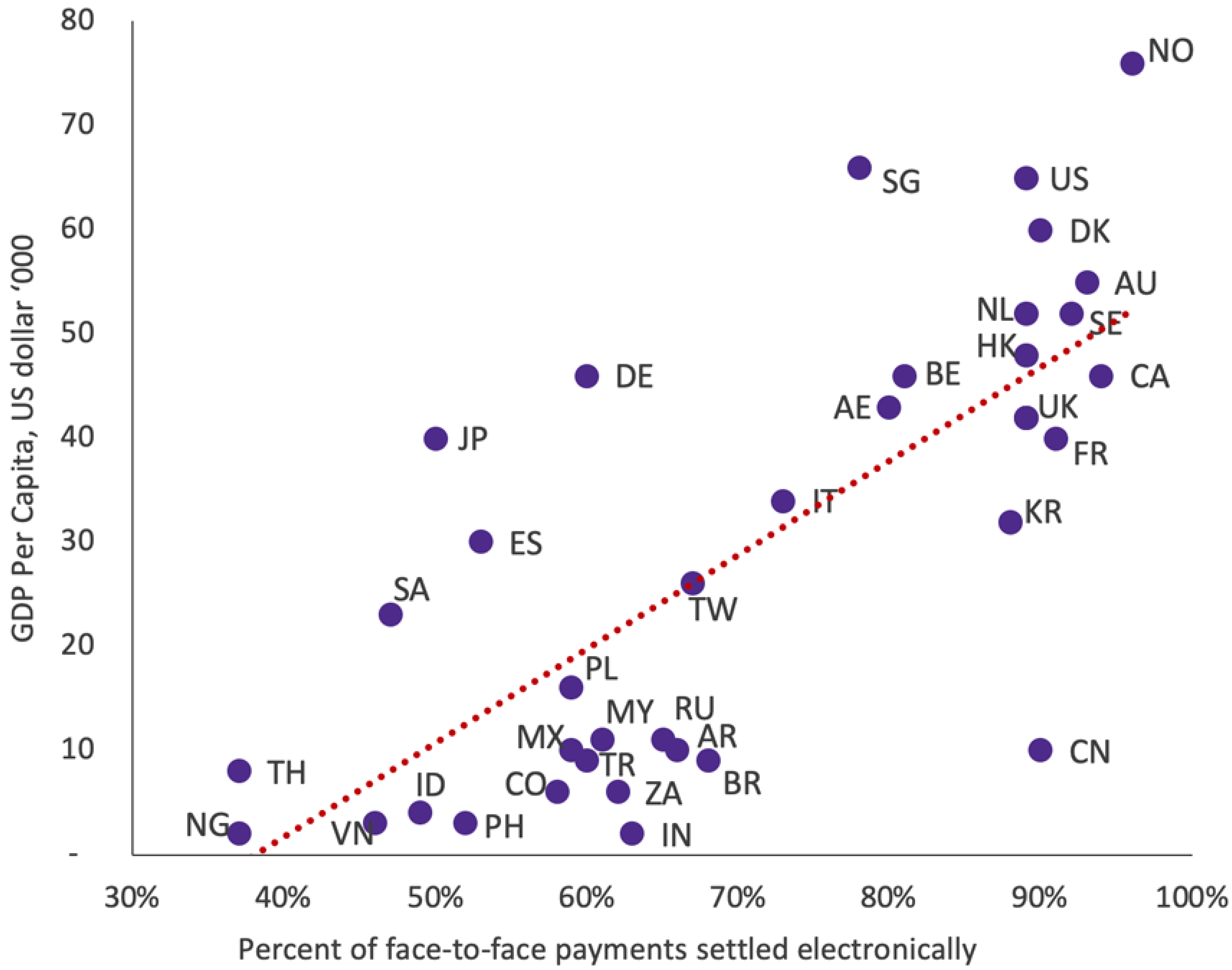
This underpins the credibility of modern banking and payment systems, including cryptos, which are only viable because they are priced in – and convertible into – national currencies.

As many economic sectors shifted into hibernation during the pandemic, much excess liquidity was directed to equities, commodity markets, real estate and cryptocurrencies.

These asset bubbles, along with broader supply-chain troubles and the war between Russia and Ukraine, increase the risks hanging over the global economy, and partly explain the surge of interest in crypto investments.

Nonetheless, as regulations strengthen, and as cryptocurrencies address scalability issues and achieve price stability, there is no reason why they cannot operate alongside national currencies or CBDCs, as many complementary currency schemes have done for decades.

GDP per capita and total value of payments settled by digital means in 37 countries in 2021



Source: FIS Global, The Global Payments Report, 2022; World Bank, WDI Database, 2022

ABOUT THE AUTHOR

Samer Srouji is a director at Tanmia Capital and a PhD researcher at the Université Côte d'Azur, CNRS, GREDEG in France

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