



Blueprint for a timely idea

The economic and social benefits of less cash

Danae Kyriakopoulou

Indian Prime Minister Narendra Modi and Venezuelan President Nicolás Maduro would have benefited from reading Kenneth Rogoff's book *The Curse of Cash* before embarking on their demonetisation efforts at the end of 2016.

Their ill-planned actions have caused chaos, ranging from queues at ATMs and protests, to deaths from heart attacks and suicides. Worryingly for economists, they also risk putting a black mark against an idea which is fundamentally good and – as Rogoff convincingly argues – whose time has come.

The dark side of cash

Rogoff, Harvard's pre-eminent monetary economist and former chief economist of the International Monetary Fund, devotes a large part of his book to introducing readers to 'the dark side of paper currency'. The examples he analyses range from the obvious, like its use in the black economy and facilitation of illegal activities, to the more sophisticated, such as monetary policy effectiveness at the zero lower bound, to the more obscure such as the public health risk of bacteria living on banknotes.

The statistics are impressive. Surveys reveal individuals in the US carry around \$46 of cash on their person and just over \$200 at home, yet an average of \$4,200 per capita circulates in the economy. Of the \$1.3tn floating outside banks, 80% is in \$100 bills, yet the fraction of consumers who report having a \$100 bill in their possession is close to zero. This hints at the huge role of the underground economy.

It would be easy to get carried away by these statistics. Commendably, Rogoff's response is measured, and his policy recommendations are soundly based on the empirical evidence he uncovers. Though the title might suggest otherwise, he is not inciting a witch-hunt against cash. As he makes clear from the introduction, he advocates a 'less cash' society, not a 'cashless' one.

He recognises that cash is a necessary medium of exchange for the unbanked

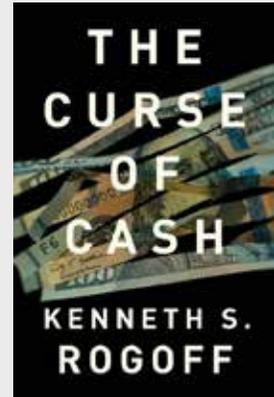
population, a sizeable demographic factor in developing economies. His proposal for phasing out cash includes a clause on financial inclusion: governments should provide free debit or smartphone-linked accounts. Timing is important, and implementing one without the other could damage the economy in the short run, as the experience of India will probably show. Another key benefit is privacy. Fyodor Dostoyevsky called money 'coined liberty', nodding to the freedom, security, and simplicity it offers. But while it is not cash itself that is cursed, some of its users are. Thankfully, data reveal which sorts of cash are cursed.

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Large-denomination bills dominate cash, but hardly feature in the average person's wallet. Based on this diagnosis, Rogoff's proposed treatment is to start with these, allowing access to lower-denominations and to limited private accounts indefinitely.

Cash and the zero bound

It is not just individuals who benefit from cash. Governments also gain from paper currency, or, more precisely, from their monopoly over its issuance. Seigniorage revenue, linked to governments' ability to monetise debts, is constrained in economies with independent central banks and is less relevant in a low-rate environment. But it is not trivial, generally ranging between 0 and 1% of GDP. This would be given up along with paper currency, but higher tax revenues raised through increased compliance and a weakened underground economy would more than make up for this foregone benefit. Central banks would also benefit from escaping the zero bound constraint on interest rates, given that cash allows individuals to escape negative rates by storing savings in cash.



The key question is where to draw the line. Rogoff's proposal to allow only small bills and surrender more privacy to the government will make some readers uncomfortable. And phasing out cash is not the only alternative. One example is lottery prizes for consumers who send in sales tax receipts, an idea introduced in Greece and later practised in Portugal and Slovakia, resulting in increased tax compliance. Legalising some drugs would constrain the underground economy and increase the government's tax coffers, but these measures would only go a small way. Legalisation may work with marijuana, but it is unlikely to be extended to hard drugs or other illicit activities such as human trafficking. The beauty of Rogoff's proposal is that it can achieve multiple goals with a single action.

The book ends with a postscript: as it went to press, the European Central Bank announced its decision phase out the €500 note. An analysis of Google trends suggests that this measure attracted far less attention than India and Venezuela's demonetisations. But it is probably the most relevant and tangible test of ideas explored in *The Curse of Cash*. The implementation and subsequent medium-term impact on corruption, crime and tax evasion may demonstrate the merits of Rogoff's policy proposals. ■

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