ESTA
The cost of cash in an evolving cash cycle

Position paper by the European Security Transport Association in response to the Commission (DG Markt) consultation on the Impact Assessment study on the New Legal Framework for Payments (NLF)
31 March 2005

Cash is a natural form of payment and the most preferred one of consumers and users. ESTA supports the Commission's objective of improving the efficiency of payment systems and markets.

The purpose of this paper is to respond to the consultation organised by the Commission on the Impact Assessment and to address false perceptions, namely that:

- "*Cash is more expensive than other (notably electronic) means of payment*": in reality, cash is less expensive than electronic means, particularly if one looks at withdrawal; cash inflows can be improved substantially to reduce the related cost.

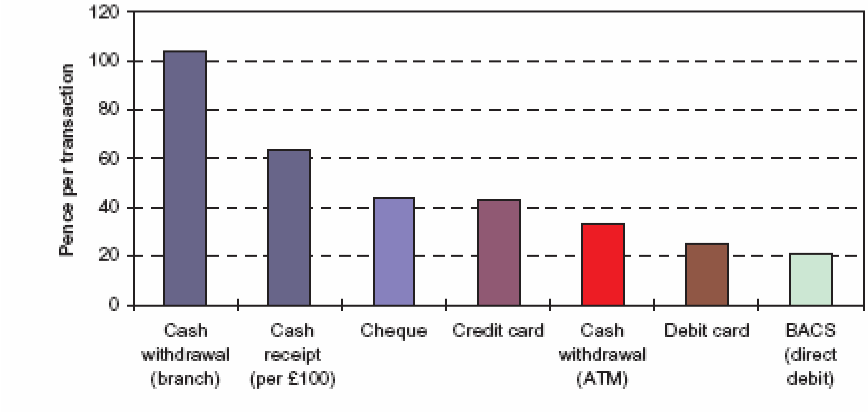
Cash should not be disadvantaged

The aim of the NLF is to improve the efficiency of payment systems, and the Commission has expressed its view that there is a strong business case for this efficiency improvement. Because the issue is precisely that of improving payment markets, it is up to the market to decide which payment is competitive and which is not, and up to users to decide which payment system they want to use. Nothing, however, should be done to disadvantage or disincentive the use of cash.

Particularly, the Impact Assessment does not substantiate its claim that for each 10% increase in electronic payments, GDP is stimulated by "as much as half a percent".

What is the cost of cash?

The wholesale cost of cash to the European banking industry is estimated at €32bn per annum (EPC sources). It is of interest that the incoming processing cost is twice that of outgoing process cost (€21bn vs. €11bn). When cash processing is automated, like in outflows in ATMs, the cost of cash is very low. The inflows of cash could be substantially improved in different ways, such as through automation, and its cost reduced by 30%, i.e. €10bn. It is therefore necessary to consider a change in the cost structure of cash.



Source: "Competition in UK Banking, a Report to the Chancellor of the Exchequer" by Don Cruickshank, Chairman of Banking Review, 2000

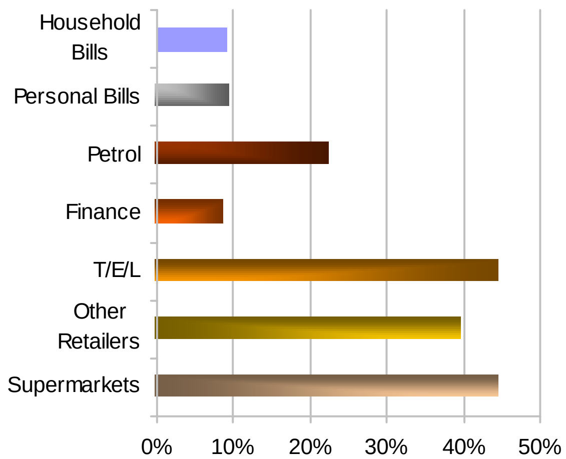
When one considers the net cost of cash (i.e. including its contribution to public revenue, or "seignorage") the cost of cash is 0.5% of GDP.

The effective cost of cash in comparison with other means of payment has been assessed independently in the UK in Don Cruickshank's banking review (see graph above). This concludes that a cash withdrawal at an ATM approaches the cost of direct debit or debit cards, and is cheaper than a payment by a credit card or a cheque. Only cash receipts and cash withdrawals in branches remain expensive, but the scope for efficiency gains is huge.

<u>Consumers prefer to use cash</u>

Gallup Eurobarometer sources, also referred to in BEUC's documents[1], show that even for the payment of large sums, consumers prefer cash. Preference is very strong for payments under €100. The reason for the success of cash amongst consumers is that cash is cheap, simple, reliable, readily available and highly popular, particularly for lower-value transactions. It is also the only payment system which allows for anonymous transactions.

Consumers use cash for transactions such as:



Source: APACS 2004: Use of Cash in a Developed Economy *T/E/L = Tobacco, Entertainment and Leisure sectors

Finland is, on occasion, referred to as a model of best practice due to its low use of cash. However, it should be noted that this is a consequence of the reduction of bank branches and ATMs, and therefore results from a constraint of supply rather than a diminution of consumer demand.

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[1] See for example "E – Payments: the consumer perspective", by D. Forest, Senior Economic Adviser of BEUC.

There are limited benefits to a cashless society

- Retailers would still have to deal with the costs of other payment systems. It is likely that the unit costs of card-based transactions will actually rise as a result of migration, due to the lower average payment value.
- Consumers would be deprived of their main tool of payment.
- In any alternative payment system to cash, there is no state-produced token of value involved and therefore no seignorage benefit to the state.

Conclusion

The EU policy in the context of the NLF should not be to attempt to re-engineer consumer preference for cash or alternative payment modes, but to improve efficiency and competition between payment systems while users would choose which one to use for which circumstances. The Impact Assessment proposed by the Commission should reflect this and be neutral as regards cash.