

# No Cash, no Banks!

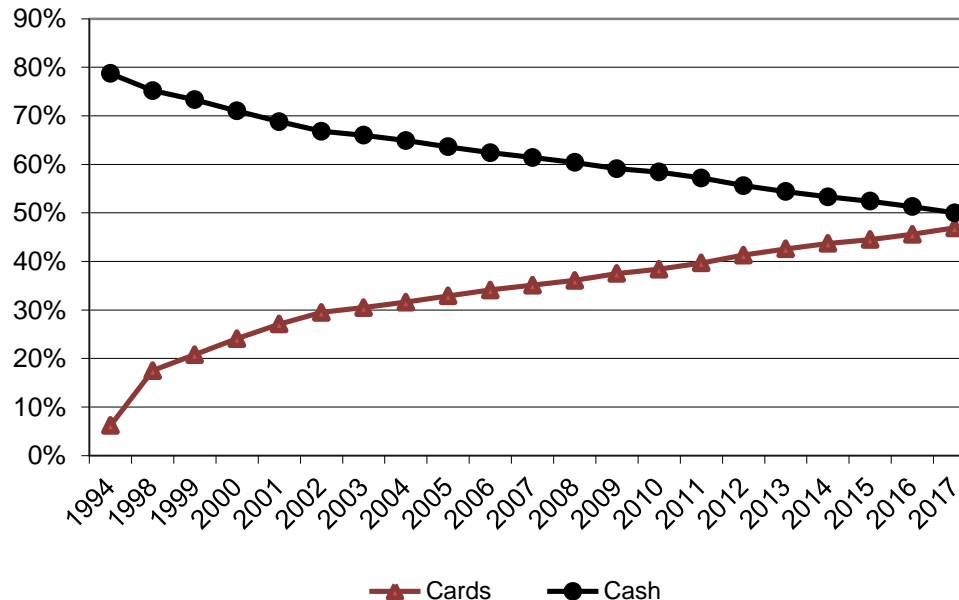
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Germany)

## Cash transactions at the POS

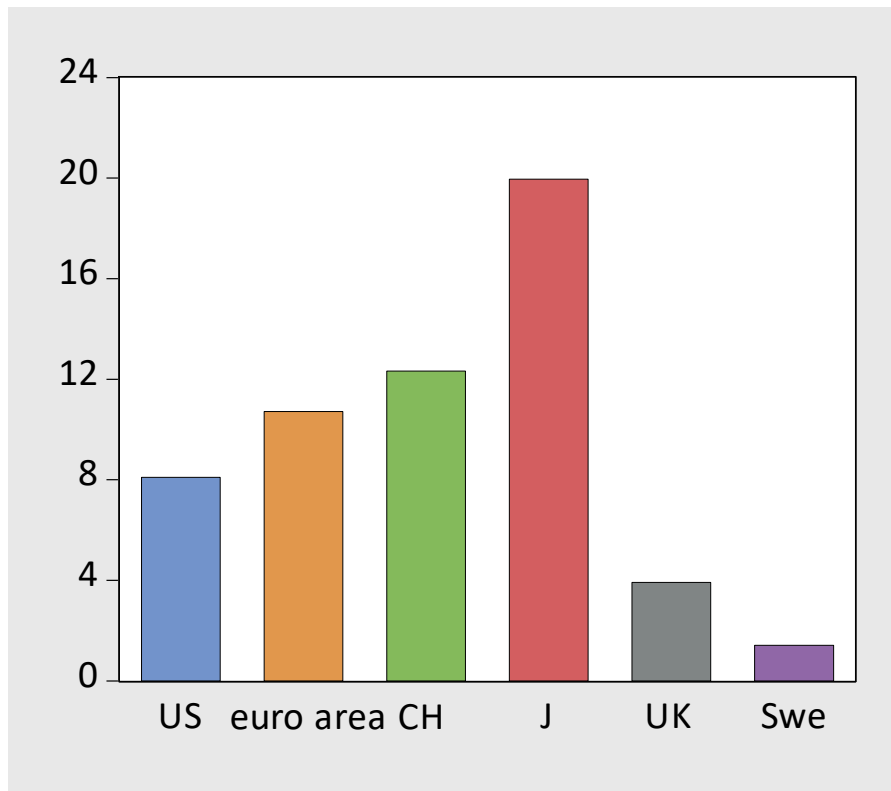
- ▶ Declining volumes
- ▶ Regulatory limits of cash usage
- ▶ Spread of cashless payments instruments

### Germany: Cards and cash at the POS (share in retail turnover)

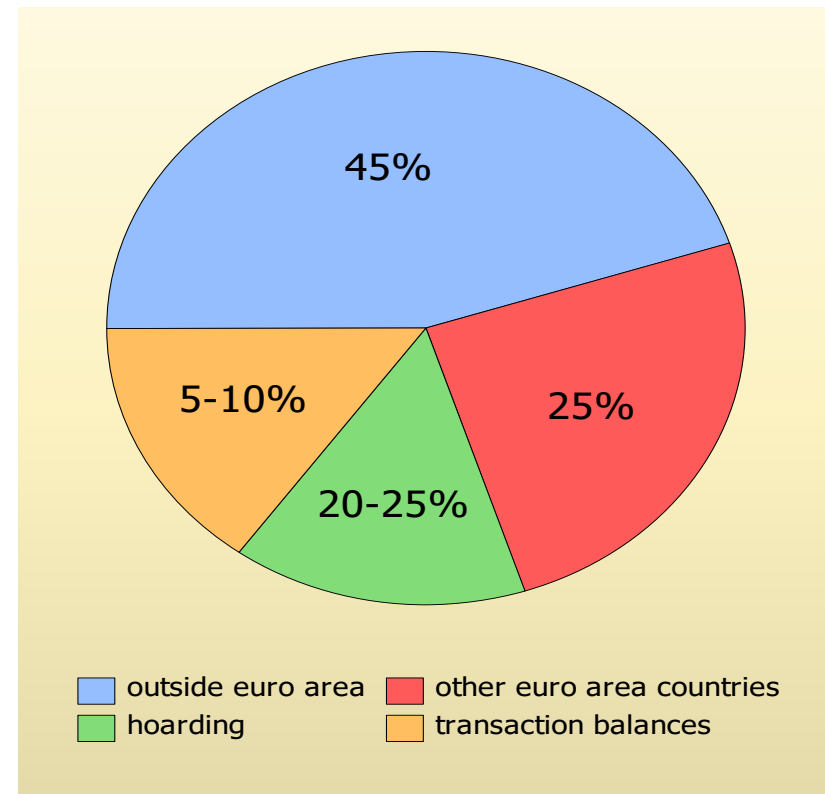


# Cash: different countries, different motives

## Cash relative to GDP (% , 2016)



## GE: Cash demand motives



## Banks' statements

- ▶ "Cash is expensive and inefficient. Cash will disappear in the next 10 years." (J. Cryan, CEO Deutsche Bank, 2016)
- ▶ "The provision of cash represents an enormous challenge to the banks. This, in turn, means that it is expensive" (H.-W. Peters, President of the Federal Association of German Banks, 2018)
- ▶ "However, it is no secret that the cash services represent a considerable cost factor for the banks. That was already true in the past. And it is even more so in the present and future." (M. Kemmer, bank representative, 2016)
- ▶ ....
- ▶ However: Cash (and the payments system in general) also generates revenues

# Two studies

Malte Krüger and Franz Seitz

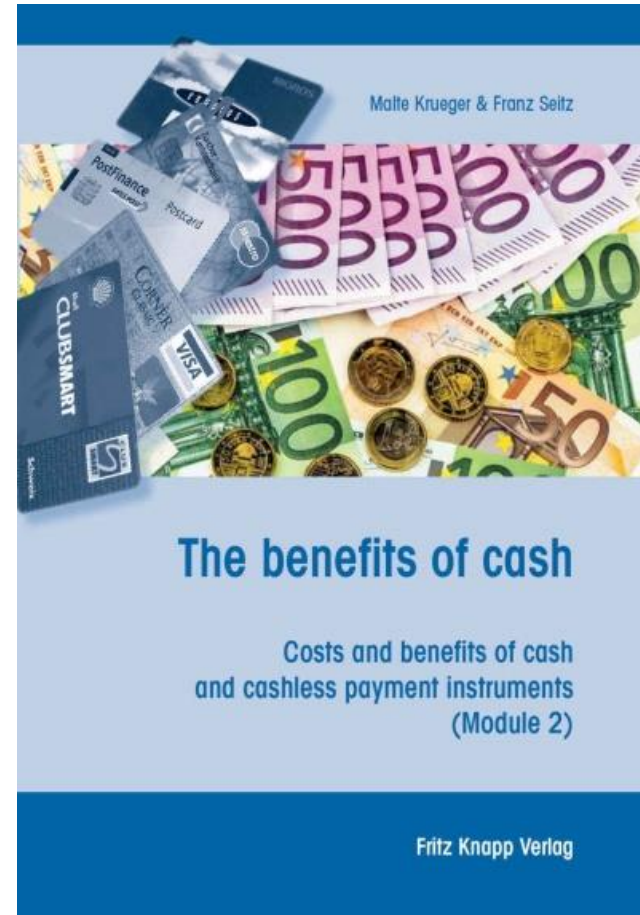
Study commissioned by the Deutsche Bundesbank

## Costs and Benefits of Cash and Cashless Payment Instruments

Overview and initial estimates



## Module 1



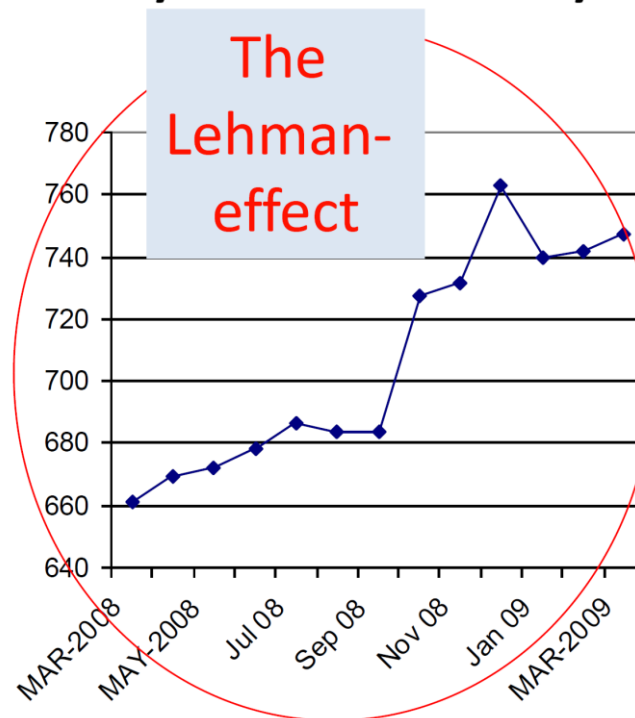
## Cash and the banking system

- ▶ Cash is an important **means of settlement** in the relation between **banks** and **non-banks**
  - Non-banks as a whole can withdraw "their money" from the banking system
  - Cashless world: non-banks are "**prisoners**" of the **banking system**
- ▶ Example: financial market / economic crises
  - Cash is an important store of value
  - Availability of cash may stop the panic

## Cash and the banking system

- ▶ October 2008: after the Lehman bankruptcy cash withdrawals increased drastically

They want their money back



Oct. 2008:  
EUR43.7 billion  
(app. €150 p.c.)

## Cash and the banking system

- ▶ What can replace cash as legal tender – directly accessible to non-banks?
- ▶ Potential structural changes
  - Central bank issued digital (virtual, electronic) money
  - Non-bank access to central bank accounts
  - 100% reserve backing ("Chicago Plan", "Vollgeldinitiative")
- ▶ Many central banks have task forces or working groups on digital money; Fed St. Louis Research: "...there is a strong case for central bank money in electronic form, and it would be easy to implement."
- ▶ Germany: Insurer Talanx asked for access to central bank accounts and sued the Bundesbank



## Cash and the banking system

- ▶ Three different systems,...
  - Central bank issued digital money
  - Non-bank access to central bank accounts
  - 100% reserve backing
- ▶ ...**but**: similar consequences
  - Significant growth of central banks' balance sheets
  - Banks lose capability to create money and credit
  - Banks are becoming mere "financial service providers"
  - "A bank is no longer where the money is" (Sutton's Law")

# Cash and the banking system

## ► Potential central bank balance sheet growth

<b>Deposits of enterprises and households</b>	<b>11,616</b>
<b>- Overnight deposits</b>	<b>6,348</b>
Memo item: Eurosystem liability items	
Cash	1,123
Deposits of credit institutions held with the Eurosystem	1,882
Liabilities to euro area non-banks	288

Notes: Euro area, € billion. December 2017

- **Asset side** of balance sheet?
- Risk of "**politicization**" of monetary policy

## Cash and the banking system

- ▶ Banks seem to regard cash mainly as a cost factor
- ▶ In the eyes of bank customers, cash may be the decisive point that distinguishes a bank from non-bank competitors
- ▶ See Sutton's Law which refers to cash
- ▶ For most people "money" is equivalent to cash
- ▶ If "money" is not in the bank anymore - is a "bank" still a "bank"?
- ▶ See the term "**bank**notes"

## Cash and the banking system

- ▶ In a cashless world, banks will resemble other intermediaries (e.g. mutual funds, money market funds)
- ▶ Banks' potential to create credit will be significantly reduced
- ▶ The profit-generating business model of issuing zero interest rate liabilities will come to an end
- ▶ The potential increase in central banks' balance sheets will be mirrored by a parallel decline in commercial banks' balance sheets
- ▶ Financial stability considerations
  - What, if the electronic payment system is down?
  - What, if its security is compromised?
  - .....

## The payments market and cash

- ▶ Is there **inefficient pricing** of cash?
  - payment market is a two-sided market
  - cost-based pricing not necessarily efficient
  - business models for cash and payment cards are not too different
  - Why is there no surcharge on cash payments?
  
- ▶ Is cash **subsidized** by **central banks**?
  - Issuing cash generates seigniorage revenues
  - Current fee structure in payment transactions works against cash: as banks are allowed to levy only few direct charges on cash services, they have an incentive to promote cash substitutes

## Cash abolition

- ▶ Arguments (e.g., shadow economy, enhancing the scope of monetary policy via deeply negative interest rates) not convincing
- ▶ Often based on **sectoral** (especially banks) **cost** studies
- ▶ Neglect of **benefits** of cash (microeconomic, macroeconomic, societal)
- ▶ **Essential:** economy-wide cost-benefit analysis by taking into account all stakeholders

# Summary, conclusion

- ▶ Cashless society not in sight
- ▶ Importance: distinguishing different **motives** of holding cash
  - Diminishing role of transactions motive
  - Increasing role of other motives
- ▶ In the long run possibly extremely negative implications of cash abolition for the (two-tier) **banking system**
- ▶ Digital **legal tender** as a case of "disruptive innovation"?
- ▶ Fostering cash abolition socioeconomic experiment with not only uncertain, but probably unexpected negative consequences
- ▶ Supporters would have to establish that the benefits they postulate – better crisis management of central banks, containment of illegal cash-based activities – are significantly larger than the associated private and social welfare losses

**Cash. I just am not happy  
when I don't have it.  
(Andy Warhol)**



# Thank you very much for your attention!

## Any questions?



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