The Blessings of Cash

Eliminating cash would deprive us of blessings. The problems with cash such as for tax evasion can be cured by taxing what cannot be evaded: land.

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#banks #federalreserve #drugwar #publicfinance

Paper money offers the benefits of anonymity, immediate payment, no identity theft, and no transaction charges. Government also benefits by printing notes with much greater value than the cost of the paper. However, some economists argue that cash has social costs that outweigh these blessings, and advocate the reduction and eventual elimination of paper cash. Several countries are planning to discontinue their largest currency notes. The European Central Bank is phasing out its 500-euro note; it will stop issuing new ones in 2018. The Scandinavian countries are reducing their paper cash.

Kenneth Rogoff, professor at Harvard University, has written a book, *The Curse of Cash*, in which he argues that the elimination of large-denominations of paper money would be good for society. Cash is a curse, he says, because criminals use the large bills, and because it limits the ability of central banks to have negative interest rates.

The use of cash by the underground economy is a symptom of bad policy, and the elimination of cash treats the effects rather than the causes. The reason economic activity goes underground is that governments have prohibited economic transactions.

Although some U.S. states have decriminalized medical marijuana, the substance remains illegal in federal law, which prevents the sellers from using the normal banking system. Therefore they use paper money. The prohibition of drugs generally drives the industry towards the use of large denominations, especially "Benjamins," the US $100 bill depicting Benjamin Franklin. The elimination of Benjamins would make it less convenient to sell illegal drugs. The higher cost would raise the price of illegal drugs, but since the quantity demanded by addicts is not very responsive to a change in price, the drug dealers would find ways to do their transactions.

The legalization of drugs would eliminate the cause of the high demand for paper cash. Just as with alcohol, producers would then use the normal banking system.

The underground economy uses cash also for activities that are legal if taxes are paid on the income and sales. Again, the elimination of cash would make tax evasion less convenient, but not eliminate the incentives to evade having substantial amounts of gains taxed away. Rogoff thinks that if the government prohibits the legal use of Benjamins, the remaining notes would lose value, as they would no longer be legally convertible into small denominations and not be legally payable for goods. But large notes could circulate as a medium of exchange within the underground economy as an alternative currency. Moreover, there are underground currency traders in all countries with artificial currency exchange rates.

The problem originates in evadable taxation. The remedy that eliminates the cause is to make taxation unevadable. The main resource that cannot hide is land. The taxation of land value, based on its best possible use regardless of current use, cannot be evaded. The elimination of all other taxes would bring production, trade, and consumption above ground and eliminate the current high demand for paper cash.

Another "curse of cash" argued by Rogoff is that paper money prevents central banks from lowering the transaction rate of "interest" much below zero. Suppose a bank has a negative 5 percent , so that the depositor has to pay $5 per year per $100 deposited. Many people would withdraw the money and hold it in paper cash. Companies would offer to securely store your cash in insured vaults. If all notes above $10 were made illegal, the storage and insurance costs would rise substantially, and the banking system would be better able to have the negative rates.

The alleged benefit of negative rates is that, because the banks also pay negative rates on their deposits with central banks, financial institutions would scramble to loan out the money to investors who would pay a positive rate, or become partners in ventures.

It is bad enough now that savers, especially retired folks, are getting close to a zero return on their retirement savings. Negative returns on, say, large certificates of deposit would further ruin those who depend on income from savings. Again, the artificial device of pushing the nominal rate of interest below zero is an attempt to treat the symptoms rather than cure the causes.

Some blame a glut of global savings for the low rates of interest. But technology is marching forward, to artificial intelligence, robots, medical advances, better batteries, and many other frontiers. There is no shortage of possible investment projects. But governments world-wide stifle investment with taxes and restrictions. The USA, for example, has choked investment since 2008 with tighter banking restrictions and higher costs such as medical mandates.

What is needed is the ultimate supply-side policy, cutting marginal tax rates on labor and investment yields to zero, with a prosperity tax shift, replacing all other taxes with a single tax on land value. The land-value tax would also push land to its most productive use, stimulating productive investment and employment.

As to money, attempts to skew markets almost always fail, so it would be best to eliminate central banks and their manipulations of nominal interest rates. Let markets set the money supply and restore the positive natural rate of interest based on the human-nature tendency to prefer to have goods sooner rather than later.

Controlled market manipulations are failing, and so statist advocates propose even more artificial controls such as eliminating paper money and pushing interest rates below zero. But the further we get from economic freedom, the worse the outcome. Interest rates and money evolved in markets; let them return to their natural base.

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"Let markets set the money supply.."?

You are arguing against elimination of cash.

What other forms of money do you have in mind? We need to identify money. Money as means of payments for purchase, investments, taxes and debts is cash and deposit on demand. When you look at the Fed numbers as of end of 2016, UD dollar in circulation was around 3.3 trillions with 30 % of it was cash. More importantly, if you look at the historic number you will find a sharp increase after 2008. How and who made and took advantage of these net increase of money? Money supply should benefit the gemeral public. Money should be democratized.

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FRED E. FOLDVARY, Ph.D., (May 11, 1946 — June 5, 2021) was an economist who wrote weekly editorials for Progress.org since 1997. Foldvary's commentaries are well respected for their currency, sound logic, wit, and consistent devotion to human freedom. He received his B.A. in economics from the University of California at Berkeley, and his M.A. and Ph.D. in economics from George Mason University. He taught economics at Virginia Tech, John F. Kennedy University, Santa Clara University, and San Jose State University.

Foldvary is the author of *The Soul of Liberty*, *Public Goods and Private Communities*, and *Dictionary of Free Market Economics*. He edited and contributed to *Beyond Neoclassical Economics* and, with Dan Klein, *The Half-Life of Policy Rationales*. Foldvary's areas of research included public finance, governance, ethical philosophy, and land economics.

Foldvary is notably known for going on record in the *American Journal of Economics and Sociology* in 1997 to predict the exact timing of the 2008 economic depression—eleven years before the event occurred. He was able to do so due to his extensive knowledge of the real-estate cycle.