Finance is changing dramatically. A new book explains how

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A farewell to cash

“The Future of Money” asks whether central banks can adapt to hold the ring

The Future of Money. By Eswar Prasad. *Belknap Press; 496 pages; $35 and £28.95*

FOR MOST people, money still means physical cash printed by a sole, public authority. Yet that is a surprisingly modern incarnation: only a century ago, private currencies competed with government-issued banknotes. It may be short-lived, too, as cash succumbs to the digitalisation of finance and new means of payment take over. This big bang will have huge implications for states, people and companies. Whether it does more good than harm, says Eswar Prasad, depends on the world’s dowdiest institutions—central banks—embracing change without losing control.

That cash is declining may not surprise readers. Many will bank from laptops and make payments on their phones. Financial innovation is old news, too. One of the first “fintech” breakthroughs happened centuries ago, when China helped engineer a boom in Asian commerce by introducing paper currency to replace metal coins, which were heavy and scarce. Yet this time is different, Mr Prasad insists. Previous overhauls mainly improved existing systems, he notes. The end of cash—likely within a decade or two—is revolutionary.

Three types of disruptive agents are involved, he says. The first are fintech firms, a varied group that all have a big online presence and a knack for crunching data. Their onslaught differs from previous, isolated breakthroughs—such as the debit card or the ATM—because it targets every facet of financial markets and institutions, from lending and payments to investment. By expanding the market for financial services, they help to democratise them. All the same, they are not imposing regime change. Banks remain dominant.

Bitcoin, and the many other digital monies it has inspired, could bring about a more fundamental shift. By enlisting a network of users to validate transactions, they make payments possible without the need for a trusted, central authority. Mr Prasad doubts decentralised money—less safe, stable and efficient—will ever trump its official cousin. But he warns that the technology involved is being co-opted by big corporations, such as Facebook; with their billions of users and financial clout, they could make private currencies an attractive means of exchange and store of value.

Fearing this could do them out of a job, many central banks are beginning to disrupt themselves by developing their own digital currencies—the third and most important shock. Done well, these "CBDCs" will upgrade the financial system. More efficient than cash for settling transactions, they could also provide a backstop to digital-payment systems managed by private firms, should those fail. They could offer "unbanked" communities access to digital payments and other financial products. And they may let central bankers experiment with new monetary-policy tools and more easily track illicit transactions.

Formerly at the IMF, Mr Prasad might have been expected to favour public solutions. Even if the pendulum swings back towards the private sector, he reckons central banks should and will remain at the heart of finance. But a strength of his analysis is his mastery of both technical details and big-picture trade-offs. He fears CBDCs may be vulnerable to hacking and bugs; they could crush private innovation and cause the instability they are meant to forestall. Meanwhile, central banks' new responsibilities may erode their independence. The privacy of transactions will be lost. Practising the balance he advocates, Mr Prasad is enthusiastic but nuanced.

He also manages to make the financial system intelligible and interesting without resorting to shortcuts and exaggeration. His patient description of how it works, peppered with well-researched examples and personal anecdotes, imposes a cosmic order on the constellation of institutions that determine how money flows. As it loses physical form, money's meaning will become ever harder to grasp. This book explores the economic and social effects of that upheaval, giving shape to this most abstract of concepts. ■

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