POLICY

Central Bank Digital Currencies And Freedom Are Incompatible

Norbert Michel Contributor
I follow the evolution and devolution of monetary and financial policy

Follow

Jul 15, 2022, 11:39am EDT

Listen to article 6 minutes

Eswar Prasad, professor of trade policy at Cornell University, arrives for dinner during the Jackson ... [+] © 2019 BLOOMBERG FINANCE LP

In a recent interview, former International Monetary Fund (IMF) official Eswar Prasad discussed his new book, *The Future of Money: How the Digital Revolution is Transforming*

Currencies and Finance. Naturally, Prasad talked about central bank digital currencies (CBDCs).

Prasad, now a professor of trade policy and economics at Cornell University, gave a blunt assessment of how CBDCs will affect monetary policy:

One should recognize that the CBDC creates new opportunity for monetary policy. If we all had CBDC accounts instead of cash, in principle it might be possible to implement negative interest rates simply by shrinking balances in CBDC accounts. It will become a lot easier to undertake helicopter drops of money. If everybody had a CBDC account you could easily increase the balance in those accounts.

Prasad's "helicopter drops of money" informed the article title, but the flip side of CBDC helicopter money is the real attention getter. It's right there in plain sight: shrinking balances in CBDC accounts to implement negative interest rates.

In other words, central banks will take money *out* of people's accounts to conduct monetary policy.

It is possible, of course, that a mere threat would suffice. If, for example, the Fed believes demand is lacking and people should spend more, the mere threat of taking people's money away might be enough to get them to spend it. But that's not really a free society.

MORE FROM FORBES VETTED

The Absolute Best Panama Hat To Wear On Vacations And At Home, According To A Luxury Travel Expert

By **Zoe Schaeffer** Contributor

The Nordstrom Anniversary Sale Opens To Everyone Today—Shop These 24 Deals Before They Sell Out

By **Kara Cuzzone** Forbes Staff

At its core, this brave new world of monetary policy equates to the government saying that your money isn't really *your* money. Your property rights are subservient to the "public good" and the supposed necessity of "managing the national economy."

Prasad doesn't really discuss this fundamental issue. He focuses, instead, on how the CBDC helicopter drops might impact the central bank's independence. He warns that:

There is a risk because helicopter money on one level really is fiscal policy and if the central bank starts being seen as the agent of the government in terms of implementing fiscal policy, that poses risks to the central bank's independence which ultimately might not be great.

Of course, he is right about this risk and about helicopter money being fiscal policy. But central banks *are* fiscal agents of the government. The Fed, for instance, supports the market for U.S. Treasury securities and now holds approximately 27 percent of outstanding federal debt held by the public (up from 21 percent in May 2020).

The blending of fiscal and monetary policy is a concern regardless of CBDCs and helicopter money. It is an inherent structural issue for all central banks.

Yet, few economists ever discuss this issue in any substantive way, and even fewer central bankers tackle the issue as it relates to CBDCs. The central banker that favors *private* solutions to

payments system problems over CBDCs is even rarer.

A perfect example of the norm for central bankers is the new Bank for International Settlements (BIS) report, *The Future Monetary System*. It proclaims that "the metaphor for the future monetary system is a tree whose solid trunk is the central bank." And while it claims that this future system, one that must be based on central banking, "supports a diverse and multilayered vibrant ecosystem of participants and functions," it must do so only after the central bankers set the rules.

So, while central banks are nominally happy to see innovation and competition in the private sector, such competition can only be helpful if it "serves the public interest." Naturally, the central bankers define those interests.

As most government CBDC reports, this BIS report takes great care to list all the advantages *and* disadvantages of cryptocurrencies. It then claims that a CBDC can provide all the same advantages as crypto while uniquely protecting against the disadvantages of crypto. It concludes that "fundamentally, crypto and stable coins lead to a fragmented and fragile monetary system."

It is difficult to take this conclusion at face value, even if one ignores the tattered history of central banking *and* the fact that central banks could easily improve the crypto monetary system by granting non-bank crypto firms access to central bank master accounts. Virtually all its criticisms of crypto are exceedingly superficial. (My colleague Nick Anthony dissects the "crypto suffers from high fees" claim here.)

The report essentially says that few people will ever adopt

crypto for regular use because it has so many inherent weaknesses and "mutual incompatibilities." Yet, it argues that it is critical for governments to regulate crypto because of the risks it poses to financial stability–even among non-banks–*and* to address the "immediate risks in the crypto monetary system." They can't have it both ways.

The truth is CBDCs are government's attempt to protect its privileged position and exert more control over people's money.

But money itself is *not* a public good. The fact that its production has been increasingly encroached upon by the government does not make it a public good. And the fact that something called a CBDC even exists is owed only to payment innovations that occurred in the private market.

The real danger in CBDCs is that there is no limit to the level of control that the government could exert over people if money is purely electronic and provided directly by the government. A CBDC would give federal officials full control over the money going into–and coming out of–every person's account.

This level of government control is not compatible with economic or political freedom.

Governments should foster more access to financial markets and ensure more innovation in financial services by supporting more private innovation and competition. They should reduce government monopoly and regulation and forgo issuing retail CBDCs.

Follow me on Twitter.

Norbert Michel

I am Vice President and Director of the Cato Institute's Center for Monetary and Financial Alternatives.

Editorial Standards Reprints & Permissions

ADVERTISEMENT