Negative Interest Rates, and Abolishing Cash Money

[This is a letter I sent to friends on April 26, 2015.]

Hi everybody,

For those of us following the U.S. & world economy, and keeping an eye on the still developing and extremely serious world overproduction crisis, *BusinessWeek* magazine is generally of little use these days. After Bloomberg took it over the new "millennial" editors essentially destroyed what was left of the magazine. Even the layout stinks and seems to be designed to make the magazine impossible to read. However, once in a while there is still an interesting article or two in it.

A case in point is the article by Peter Coy, entitled "Welcome to Less than Zero", in the current issue (April 27-May 3, 2015). This article is also available online at:
http://www.bloomberg.com/news/articles/2015-04-23/negative-interest-rates-may-spark-existential-crisis-for-cash

This 2-page article describes the move by banks and monetary authorities around the world to try to bring about negative interest rates on the money they borrow from customers, not only from ordinary small scale depositors but even more so from major corporations and other banks!

There is even growing discussion about how it may be necessary to entirely abolish cash—i.e., physical currency—in order to be able to force much more strongly negative interest rates. (Of course governments would also like to abolish cash in order to collect more taxes and put an end to the underground economy.)

That's right—bourgeois economists and banking officials are now becoming more serious in their proposals that the government should entirely abolish cash and force *all* monetary transactions to take the form of digital transactions between bank accounts.

It is easy to see why banks and monetary authorities want to get rid of cash money in order to enforce negative interest rates. After all, if the bank is *charging you* interest to hold your money, then why not just take the cash out of the bank and hide it under your mattress?! (But that may not be such a good idea if you have millions of dollars in the bank, and fear that the money might be stolen.)

However, if there is *no such thing as cash anymore*, then you *can't* take your money out of the bank; all you can do is move it to a different bank account. And if all bank accounts have negative interest rates, then there will be nothing you can do about it. Your money will be gradually, but steadily, stolen from you by the banks.

Coy says that JPMorgan Chase bank is now charging negative interest (in the form of "balance sheet utilization fees") for many of its largest customers. And he says that the bank is doing this in order to increase its profit, which would otherwise suffer a bit because of government regulatory rules.

So the question then is *why* has the government established such regulations? It has been done totally on purpose to try to "foil cash hoarders"—that is to say, to try to force companies and individuals not to sit on their money (mostly actually in the form of bank deposits), *but rather to invest or spend it.*

And this is the fascinating part of it all! (And the part that Peter Coy either can't or won't fully explain.)

Traditional bourgeois economic theory has always maintained that capitalists will not hoard money, and that—as David Ricardo put it—any amount of capital can be profitably employed in any country. And even if one capitalist doesn't know how to spend or invest his excess cash, by putting it in the bank he makes it available for some other capitalist to borrow it and build new factories.

This central dogma of bourgeois economic theory, that more capital can always be profitably employed and that there cannot be any such thing as general gluts or overproduction, is what is known as "Say's Law".

But while this so-called "law" is still accepted as gospel by most bourgeois economists, some of them have developed some doubts over the past century. Keynes and his followers thought that once in a while things would (rather inexplicably) get out of kilter, and the government would have to step in with its own deficit financing for a little while to get the economy humming again. (See "Priming the Pump".)

More recently, and due to the continuing weakness of the U.S. and world economies in the aftermath of the financial crisis of 2008-2009, the Federal Reserve and other important central banks have been engaged in what they call "quantitative easing". What this amounts to is creating vast amounts of money by the central bank and loaning it to banks at little or no interest. The justification for this move has been that surely the banks would lend out this money at fairly low interest rates to companies to expand production and get the economy moving again.

But quite mysteriously (to bourgeois economists) this has not happened to any significant extent. Instead, those hundreds of billions in new money are just sitting in these vaults of the big banks (or more precisely, in their own financial accounts with the Fed) and are NOT being borrowed by corporations to invest in new factories. Why not? Because these corporations already have more than enough factories to produce all the goods which they can sell.

So while "Say's Law" says that capitalists will jump at the chance to borrow money for little or no interest and expand production with it, this has not been happening despite the vast mountain of such money available. This deeply puzzles the ruling class financial authorities, but they can't help but see that it is the actual situation. So what then to do about it?

What they are trying to do is to find ways to *force* companies (and individuals) to spend or invest their money. And their method of doing that is to take part of the corporation's (or individual's) money away from them if they don't spend it.

There are actually several ways of taking away part of their money from companies and individuals:

1) Money hoards could be taxed. (I.e., not just interest income, but also principal. Such as say a 3% tax on the balance of all checking and savings accounts every year.) But this won't work at all well if money can be hidden (as cash can). And this method is not politically practical in the U.S., at least, where taxation is anathema, especially to Republicans.

2) Through inflation. The problem here though, for the ruling class, is that inflation is surprisingly hard to arrange for in an economic crisis. (Well, actually it would be very easy to accomplish, if the government just handed out huge amounts of money to ordinary people, who would then spend it. But that is also anathema to the bourgeoisie.)

The Fed actually has a current target of inflation of 2% per year, but is falling short of that (in their own skewed measurements) for a variety of reasons including the falling costs of goods imported from China, etc. Moreover, even if they could raise the inflation rates to 2 or 3%, this would still not be sufficient to force big corporations to invest in new factories they simply do not need. On top of this, high inflation rates are also politically impossible over a long period.

3) That leaves negative interest rates. If the government can arrange things so that banks charge companies and people to hold their money, and if companies and individuals see their money disappearing when it is left in bank accounts, they will definitely be more inclined to invest or spend. This, at least, is the new thinking on the part of a section of the ruling class.

There are, however, several big questions about all this.

First, is it really feasible politically? I think you will find people (and even more so many corporations!) raising total hell about any actual concrete proposal to abolish currency. Even if most people don't really understand why the government would want to do such a thing, the vast majority of them would instinctively fear and oppose the move.

There would also be various methods developed for getting around it, such as employing various commodities as ersatz cash. (This is historically how gold came to be money in the first place.) Gold itself, would almost certainly boom in value if this abolition of cash is ever actually tried. If the government tried to make private ownership of gold illegal again (as FDR did), then some other commodities would take its place.

Second, even if significantly negative interest rates are established on money (and there is no cash anymore), would this really have the desired effect? And if so, to what degree? And for how long? I think the effect would be much less than the rulers hope for, and would become less and less effective over time.

Suppose, for example, that a corporation was forced by this method to double the number of factories it had even though the market for its goods was little increased. That would in effect mean that its profits would be severely cut because of the doubled overhead. It would at some early point prove to be more profitable to suffer the negative interest rates than it would be to build yet more unused factories.

The results for consumers would also be much less than hoped for. A huge fraction of the American population already has little or no savings, so they cannot be "forced" to spend more unless they are granted more credit. And credit levels are already obviously dangerously high.

So the consumer market cannot be greatly expanded by "forcing" people to spend, when most of them already have little extra money to spend in the first place.

As for the rich, they do have lots of extra money, and are desperately looking for places to invest it. If negative interest rates force them even more to look for places to invest, when there are so few good places, then they will turn even more to financial derivatives and gimmicks. In other words, establishing negative interest rates will promote to even a greater degree than already exists the financial bubbles and casino economy. This would be one of the many unintended consequences of abolishing cash, and would make ensuing financial crashes much worse.

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What we see with proposals like this (to abolish cash and enforce negative interest rates) is actually sort of a growing desperation on the part of the ruling class to find a way to get capitalism to work again.

Their own theory ("Say’s Law") says that this should not be necessary. But their system is not working "the way it is supposed to do!" So they feel that pragmatically they have to resort to all kinds of unwise schemes. It would all be hilarious, if—as is always the case—the working class was not the biggest victim of all this foolishness.

The bottom line is that capitalism is in the still relatively early stages of what will be an ever more serious and disastrous economic crisis, and the ruling class has no idea what to do about it. At least no *good* idea, because there simply isn’t one.

Scott