Book Review

The Future of Money (2021)
Eswar Prasad

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In a world where advances in technology have disrupted and will continue to disrupt all basic human activities - work, communication, learning, governance, management- we should also expect similar changes to happen to the nature and scope of one of the oldest and most universal of human creations, namely money. There is reason to suppose that the ramifications and impact of these changes will be truly transformative because money and what it means for human life and economy is fundamental to the way the world works.

The future perspectives for money in terms of the unfolding of the forces and trends in its ongoing evolution is the theme of this book. Given the four proverbial functions of money - a medium, a measure, a standard, a store - the theme offers the challenge of its having to be addressed on different planes, from the operational and technological to the systemic and the philosophical. The last is not to be discounted by any means because money also has its place in the emotive areas of human life and a proper study of money's future has to include that aspect as well.

Eswar Prasad's "The Future of Money" rises well enough to that complex challenge of interpretation and prediction. It is a broad spectrum treatment of the future of money providing both enlightenment and insights in a vital subject area. Its author brings into his work impressive mastery of the discipline of monetary science and finance; that he does so while also managing to make it highly readable, somewhat in the manner of Thomas Picketty, is what invests it with a unique quality.

The future of money as Eswar Prasad tells it, is already here: its materiality being replaced by the digital, the shift away from cash and the trend towards decentralised finance. Fintech, " a catch-all neologism for novel financial technologies" in the words of the author, is the wellspring of these developments shaping the future and we can expect their currently estimated timeframes for further advance to only shorten as we go along, given their interface with market and government. Vast improvement in the financial system all round, not the least domestic and cross border payment systems, is assuredly a prospect, with major operational risks on the flip side. There would also be existential issues for traditional financial institutions like banks. Formidable challenges to regulation and financial stability would notably be part of what is in store for countries, as their central banks, with change in the stature of cash and the very functions of money parcelled out, could find themselves having

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to coexist with considerable as well as resourceful new private players, including payment systems and commercial platforms. Crypto currencies like Bitcoin pose a frontal threat to them; considerations of survival could well drive them to displace their cherished currencies through digital currencies of their own. (Witness our own government 's present moves in that department). And in regard to the central banks' indispensable function of pursuing key objectives such as low inflation and financial stability, the profound changes underway to money and financial markets would have a critical import.

Posing the question whether Fintech will make the world a better place, Eswar Prasad holds the view that in money and finance it has far more disruptive potential than technology in certain other areas as some of the fundamental elements of finance are being affected. Topping the list are payment systems in retail, wholesale and cross-border categories, determining the very role of money as the use of cash will eventually cease. From basic financial intermediation to insurance and payment systems Fintech will be a transforming influence. The changes resulting from the process have significant implications for financial markets and by extension to economic activity and monetary policy themselves. A part of the book devotes itself to a variety of examples to underline the transformative potential of Fintech across the entire financial sector. In this respect, emerging market economies, particularly China, have been sources of innovative developments, even to the extent of creating a level playing field in the domain of applications and yielding instructive lessons to advanced economies. Fintech as it emerges from this many-stranded narrative, so goes the argument of the book, “promises enormous potential benefits , but also seems vulnerable to enormous risks".

The sections of the book dealing with Bitcoin and "crypto mania" are the most informative, especially in view of the topical nature of the subject. The insights they provide into the nature and dynamics of crypto currencies constitute the prelude to one of the principal lines of enquiry of the book, which is the rationale as well as the implications of central banks of countries adopting their own digital currencies in a collective bow to the inevitable. With the prefatory observation that physical money, having taken in the past such various forms as cattle, beads, metal tokens and paper, the author states that central banks are now preparing the ground for the next wave of transformation which is the digital version of their currencies (Central Bank Digital Currencies or CBDCs in short). Going into details, he spells out that CBDC could take the forms of both wholesale, which already exists in the central bank money used in interbank transactions, and retail, where it would involve replacement or augmentation of retail money consisting of banknotes and coins with their digital versions, something which will mean a fundamental transformation. Such retail CBDC can take multiple forms: e- money wherein the central bank manages a centralised payment system linked to electronic wallets on prepaid cards, smartphones or other electronics devices. Another version of it is an account- based CBDC where individuals and businesses would have access to central bank accounts, with the central bank acting as the manager of a sophisticated payment system; alternatively, the digital wallets could be maintained and managed by commercial banks. The payment system would be based on a centralised verification mechanism consisting of Blockchains or any form of Distributed Ledger Technology DLT) rather than the decentralised, permissionless one of the sort used by Bitcoin. Another category of CBDC is official cryptocurrency issued and managed by a government or a specially designated private agency.

The two main motivations of the central banks in going in for CBDC are, firstly, its potential to serve as a support system to privately managed payment systems and secondly , as an instrument for promoting broader financial inclusion. Added to these is the stake governments have both in monetary sovereignty and in tax revenue on which the nature of central bank money can have an effect. CBDC's potential to enhance the central bank's monetary policy tool kit is also an important consideration. In weighing the pros and cons of CBDCs, the author points out that it has possible benefits such as greater transactional efficiency than cash, the possibility of serving as a backstop to private sector- managed payment systems thereby avoiding a breakdown of the payment infrastructure during a crisis of confidence, increased financial inclusion, the potential to add to the effectiveness of monetary policy while broadening the tax base and reducing tax evasion and greater immunity to use for illicit purposes. For advanced economies, its major benefits are that it would help maintain the relevance of central bank money as a payment system besides easing some constraints on monetary policy and increasing its effectiveness, especially in difficult times. On the side of risks are its technological vulnerabilities, including hacking, the likelihood of its putting the government in competition with the private sector, the chance of a CBDC precipitating financial instability in a counterintuitive sense and finally, the probable loss of independence and effectiveness by central banks under government pressure.

Prasad argues that even if in principle the benefits of a CBDC exceed the costs, a number of factors could militate against the desired favourable outcomes. Broadly speaking, CBDC will work better in countries with sensible government policies and sound regulatory frameworks. A well designed and managed CBDC can improve economic and financial outcomes, but is " hardly a panacea for a nation's deep-seated economic ills ". As for emerging market economies, there are important constraints on adoption of CBDC, imposing on them a need for a multitrack approach - embrace of new technologies, improvement of interbank payment systems and development of retail CBDC - to managing the fast-changing financial landscape.

The book cites the examples of a few central banks that have already launched their CBDC. Of particular interest to India is China's E-CNY which is a replacement for cash having equal status as legal tender and is stored in digital wallets provided by financial institutions and maintained on centralised digital ledgers verified by cryptography and consensus algorithms. Introduced in early 2020 supposedly in an effort to mitigate the increasing irrelevance of central bank -issued currency for retail payments in view of the high visibility of Alipay and WeChat Pay, it has other payoffs as well, notably promotion of internationalisation of renminbi " by extending its global reach into cross border payment systems at low cost and with faster transactions", to quote the author. The proposed e- rupee, the Indian version of CBDC, might find some features of E-CNY to be of interest to the project.

Eswar Prasad is definitely of the view that the rise of CBDC is a foregone conclusion, "although the demise of cash might not be imminent, as cash retains certain attributes such as privacy and anonymity in transactions that cannot be matched by digital currency". But he goes on to add, " With their greater convenience, however, along with their many benefits for consumers, businesses and governments, CBDC might prompt the disappearance of cash within a decade or two".

In the future of money as visualised by Eswar Prasad, there will be other possibilities to contemplate, some momentous, some remaining much the same as now. Central bank- issued currencies will retain their importance as stores of value; much as the dollar's dominance as a payment currency might erode, it will remain the dominant global safe haven currency for a long time to come. Prasad finds substantial and convincing reasons to make that assertion. Privately intermediated payment systems will acquire ascendancy; but central banks, while having to contend with these players as well as with private creators of money , will retain their indispensable role in monetary policy and in regulatory functions in the major economies, certainly in India. Fintech will increasingly mitigate the substantial frictions affecting cross border transactions at present, but part of that process will also inevitably add to the volatility of cross border financial flows, raising new challenges to regulators and governments. The changes on the global financial scene currently underway will not by themselves reorder the international monetary system or the balance of power among major currencies. The dream of decentralised finance fostered by new technologies will be a growing reality, with more financial inclusion coming to pass, but " technological innovations in finance could have double- edged implications for income and wealth inequality". On the other hand, there could be concentration of even more economic and financial power in larger economies and in major global corporations such as Alibaba and Amazon.

Eswar Prasad's book is a scholarly work on money which is robust in content and marked by the confidence and lucidity of its style, with gentle touches of humour livening up its narrative. In a wide sweep it provides what is arguably the definitive account of the direction that money and financial sector could take in the years to come. Readers comparing it with the best seller " The Ascent of Money " by Niall Ferguson will have little difficulty in deciding where a more rewarding experience was afforded.