

Benoît Cœuré: Euro banknotes – a secure means of payment and a symbol of Europe

Speech by Mr Benoît Cœuré, Member of the Executive Board of the European Central Bank, at the conference “Preparations for the launch of the second series of euro banknotes: challenges and opportunities”, organised by the European Central Bank and the Central Bank of the Republic of Austria, Vienna, 22 April 2013.

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Ladies and Gentlemen,

I am very pleased to have been invited to speak at this conference, even though – because of my responsibilities for Payments and Market Infrastructures – my focus is more on policies concerned with cashless payments than with banknotes. I am, however, convinced that cash and electronic payments do not compete with each other, but complement each other. The existence of each is justified; the one needs the other.

As regards the role of cash in the Eurosystem, we should bear in mind that its importance for central banks goes beyond the issuance of banknotes. From a macroeconomic point of view we are especially interested in the share of euro cash in circulation, which is used for domestic transactions in the euro area, since this is a key variable for measuring economic activity and price developments. Furthermore, the demand for euro banknotes is one of the drivers of liquidity required by the banks, which is a relevant indicator for our monetary policy operations. I should add, though, that banknotes are currently less relevant for the liquidity required by banks due to the non-standard measures taken by the Eurosystem. That said, the profit made on banknotes in circulation, the so-called seigniorage, remains an important source of income for the Eurosystem.

However, even though seigniorage is an important part of the total income of the Eurosystem, the ECB has a neutral stance on the use of banknotes as opposed to other means of payment. In other words, we neither promote nor prevent the use of cash, and regard its use as a demand-driven process. But neutrality should not be mistaken for indifference. On the contrary, cash is fiduciary money, which comes from the Latin word “fiducia”, meaning confidence or trust. This means that its value depends on whether it is trusted as a means of exchange. This is a crucial point: maintaining trust is the fundamental principle underlying all the Eurosystem’s activities and decisions in the field of banknotes.

Fortunately, we can say that euro banknotes can be trusted if we look at the counterfeiting levels in recent years. In 2012 just over half a million counterfeits were detected and withdrawn – a very small proportion of the total average circulation of 14.9 billion banknotes. By the way, the fact that euro banknotes can be trusted is not only evident from the statistics, but also from everyday observation. In supermarkets, for example, you can see people carefully checking strawberries that cost less than €3. But the same people don’t seem to worry about checking the €10 banknote they receive as change when they buy those strawberries.

Also, the increase in euro banknote circulation itself shows that we have built and maintained trust in the banknotes. At the end of last month, there were 15.2 billion banknotes in circulation with a value of €396.4 billion; that’s around 150% more than at the end of 2002.

This increase can, however, only be explained to a very small extent by the growth in the use of cash for transaction purposes. We estimate that around one-third of the current circulation value is used for transactions in the euro area. Another 25% is estimated to be in use outside the euro area. This means that the remaining part – around 40% – is being used as store of

value in the euro area. The fact that around one-third of the circulation value is used for transactions in the euro area means that any change in this proportion will only affect a relatively small part of the banknote circulation. And even this relatively small share is only affected to a limited extent by changes in payment behaviour. This is because a banknote in circulation can be used for many transactions during a year. In other words, a 5% increase in card transactions does not mean a 5% fall in banknote circulation.

This is probably one reason why the circulation of euro banknotes, even of the denominations typically used for transactions, has not declined in the last ten years despite the strong increase in the number and value of card transactions. Indeed, the average number of card transactions in the euro area almost doubled between 2002 and 2011, from 36 transactions per inhabitant to 67. Also in terms of value, card payments saw a strong increase, from €600 billion in 2002 to €1.1 trillion in 2011.¹ Nevertheless, to judge by several studies, we estimate that in the euro area 70–80% of the number of transactions and 50–60% of the value of all transactions at the point of sale are still made in cash.²

However, despite the predominance of cash in daily payments there are indications that things are changing, although very gradually. One indication from surveys carried out by different central banks is that the share of cash payments in retail payments appears to be slowly diminishing. This decline seems to be somewhat more pronounced for the value than for the number of cash payments, meaning that the average value of a cash payment is also falling. A study on payments carried out by the ECB in eight euro area countries in 2008 revealed that cash is most often used for transactions below €20. On average 55% of the respondents said they normally paid cash for typical daily purchases of between €30 and €100. But on average 87% said they always or often used cash for purchases below €20. This behaviour is reflected in the average value of a cash payment, which in 2011 was around €20 in Germany and Austria, and only just over €12 in the Netherlands.³ In other words, cash is still the most common form of daily retail payment, but largely and increasingly because it is used for frequent small purchases.

However, this does not mean that cash is no longer used for high-value payments. Our 2008 survey showed that on average 20% of the interviewees in the eight countries said they used cash always or almost always for purchases of between €200 and €1,000. 4% even said they normally used cash for purchases above €10,000.

There is another function of banknotes, namely their function as store of value. Under normal circumstances low interest rates result in low opportunity costs of holding cash, and consequently in an increase in the demand for banknotes used for store of value purposes. However, as we have seen in recent years, extraordinary circumstances can create an additional demand for banknotes for store-of-value purposes. This became clear after the collapse of Lehman Brothers, when in a period of only three weeks euro banknote circulation increased by €35 billion. Also during the periods of high uncertainty in Greece banknote demand increased strongly in that country, although a backflow of banknotes to the central bank was also observed after the situation stabilised. Likewise, we saw a sharp increase in the demand for cash in Cyprus in March and at the beginning of April. Let me also add that

¹ ECB, Statistical Data Warehouse.

² Deutsche Bundesbank (2012) "Zahlungsverhalten in Deutschland 2011"; Jonker, N., Kosse, A. Hernández, L. (2012) "Cash usage in the Netherlands: How much, where, when, who and whenever one wants?", DNB Occasional Studies, Vol.10, No. 2; Mooslechner, P., Stix, H., Wagner, K. (2013) "The Use of Payment Instruments in Austria", Monetary Policy and the Economy, Q4/12, Oesterreichische Nationalbank. Schmiedel, H., Kostova, G., Ruttenberg, W. (2012) "The social costs of retail payment instruments: A European Perspective", ECB Occasional Paper Series, No 137.

³ De Nederlandsche Bank (2012) "Factsheet: Contante Betalingen Geteld 2011", available at <http://www.dnb.nl/en/news/news-and-archive/dnbulletin-2012/dnb274102.jsp>.

the Eurosystem stood ready to accommodate the resulting precautionary demand for banknotes to avoid further disruptions.

The situation in Cyprus has also reminded us that cash is both a means of payment and a store of value of last resort. If banks are closed, cheques are no longer accepted and even the payment cards of stressed banks are no longer trusted, so cash appears to be the only way to settle a transaction immediately and without credit risk. At the same time, it has to be said that while some retailers preferred cash, payment cards continued to be used for payments at point-of-sale and for cash withdrawals. This reminds us also of the interdependence of cash and payment cards. When banks are closed, ATMs are the only source of cash. But in order to withdraw cash from ATMs people need a payment card, and cards and ATM networks must be fully operational.

Now, how do all these developments influence the Eurosystem's perception of cash?

First, even though we do not expect a major changes any time soon, electronic payments will continue to grow. But it will be a gradual process and it will lead to a reduced need for banknotes for transaction purposes. And just for you to understand the possible implications: if the payment pattern in the whole of the euro area was like that in the Netherlands, where 62% of the number and 37% of the value of all retail payments were made in cash in 2011, the value of the cash withdrawals in the euro area would be only *half* the value of the current cash withdrawals. As a result, the social cost of making cash payments will continue to rise relative to the social cost of making an electronic payment. In one way or another, this will put pressure on the cash sector to become more efficient.

Second, we feel that because of national differences in the use of cash, and differences in geography and cultures, it is neither possible nor desirable to have one way of organising the cash cycle in the euro area. We should, however, at least move in the same direction and adopt a number of common rules and principles relating to the organisation of the cash cycle. A good example is the ECB Recirculation Decision, which lays down the rules under which third parties are allowed to re-circulate banknotes, and which applies to the whole of the euro area. This should ensure that in the whole of the euro area the public can be certain that banknotes provided by ATMs are genuine.

Third, while there can be no objections to a society with less cash, a cashless society is not possible in the foreseeable future. Decisions and initiatives taken in various countries to limit the value of cash payments by law are not incompatible with the legal tender status of euro banknotes and coins, provided that other lawful means of payments are available. Furthermore, limitations can be accepted if they are proportionate to the objectives pursued. But although it is understandable that merchants wish to reduce the amounts of cash they handle and hold for efficiency and security reasons, we feel that it is problematic that shops will become cashless on a large scale. It would ignore the will of a large share of the population, and it would also go against the principle of the legal tender status, and the universal acceptance, of cash.

Fourth, as the events of 2008 and the more recent developments in some countries have shown, there is a relationship between the demand for banknotes and public trust in the banking sector. Although people clearly trust euro banknotes, it would be much better if they did not feel the need to store banknotes because of concerns about the health of a bank or the banking sector. That is why we are working hard to establish a European banking supervisor, and why we should take all necessary measures as soon as possible to restore confidence in the banking sector.

Now, let me come back to the main purpose of our event today: the launch of the €5 banknote of the Europa series. The main reason for the new series is that the first euro banknotes were issued over 11 years ago and the technology in those banknotes is more than 15 years old. Even though the number of counterfeits is relatively low, it is important to maintain trust in euro banknotes and to stay ahead of developments. So on 2 May we are

launching the €5 banknote as the first denomination of the new series. The other denominations will follow in ascending order in the next few years.

Apart from the more vivid colour of the €5 banknotes, the most visible change in the banknotes is probably the emerald number on the front and the portrait of Europa in both the watermark and the hologram. However, maybe the most important changes are those which are invisible to the human eye. We have not only applied a special coating, which will make the banknotes more durable and should extend their life, but have also incorporated several new or enhanced security features which are used by banknote authenticity devices and banknote handling machines.

In most countries the €5 banknotes will be mainly brought into circulation via bank counters and the cash ordered as change by retailers. As a result, the new €5 banknotes will gradually arrive in everyone's wallets. Only in some countries will €5 banknotes also be issued via ATMs, but even in these countries banks seem to be reducing the availability of €5 banknotes in ATMs. We don't see this as a good development; banks should consider issuing more €5 banknotes via ATMs. It would be convenient both for the public, which tends to pay cash for small-ticket items, and for retailers, which would need less change. Additionally, it would also mean that the overall quality of the €5 banknotes in circulation would be higher in many countries.

In the presentations today and tomorrow you will learn more about the design and security features of the new euro banknotes and about the preparations for the introduction of the Europa series by central banks and the various stakeholders in the cash cycle. These presentations will make clear that the design, development and printing of a new banknote represent only half the work behind the issuance of a new series. The other half has to be done by the various stakeholders in the cash cycle.

When introducing a new banknote it is essential to inform the public about its security features and to encourage them to look at the banknotes. This is not easy for a product which the public has been using every day for the past 11 years. So, the public information campaign which we have launched aims to make people aware of the Europa series and its security features. In this respect, it is encouraging that after the unveiling of the new €5 on 10 January 2013 a public opinion survey showed that no fewer than 51% of people in the euro area were aware of the new series. This probably reflects the spontaneous interest that people and the media have in banknotes. But this survey also indicated that more efforts are needed to ensure the public not only knows about the new banknote series but also about the security features.

I have talked about euro banknotes as a means of payment and a store of value, but would like to conclude by mentioning the third Aristotelian function of money: as a unit of account⁴. Over the years the euro banknotes, as our unit of account, have become an important symbol of European integration. Just as a euro banknote is worth the same everywhere in the euro area, one euro of commercial money should be worth everywhere the same. The Single Supervisory Mechanism will contribute to restore the singleness of euro area banks' liabilities provided that it is complemented by a single mechanism, with a common financial backstop, to wind down failed banks. The ECB will not let trust in the euro as a standard of value be undermined by fears of a euro break-up and by financial fragmentation, and will continue to act appropriately within the limits of its mandate. Thank you for your attention.

⁴ Aristotle: Nicomachean Ethics, Book V, and Politics, Book I.