

Not repaying our debt: risk of a loss of trust in money and risks for society

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Budgetary and monetary policies are vital to limiting the damage wrought by the pandemic and lowering our guard precipitously would be a serious mistake. But given the substantial debt resulting from the crisis, what is likely to occur once the situation returns to normal?

The failure to repay public debt to private creditors would have considerable consequences for both the economy and society, impacting household savings and pensions. Even supposing that the law allowed us to not repay the debt to the central bank alone, then given that the Governments are its shareholders, we would be playing a zero-sum game. And even if a part of the additional debt resulting from the pandemic were to be financed on a near-perpetual basis by the central bank at a rate close to zero, could this possibility be extended to the debt and its future increases?

How to avoid succumbing to the idea of a magic money tree and that, ultimately, since we have found the financial resources for what previously appeared impossible to finance, there is no reason for not continuing in this manner?

A policy of endless quantitative easing would not work and should be rejected. Allowing the state to spend limitlessly and private players to amass debt indefinitely with no constraints would have substantial consequences on the financial instability thus triggered. With the economy returning to more normal growth, maintaining excessively low interest rates for too long would be tantamount to encouraging and even engendering financial cycles. This would create ever larger speculative bubbles and their inevitable bursts. These well-known phenomena give rise to major crises.

Lastly, in the longer term, people could end up shunning the currency altogether. The lack of payment constraints could lead to a crisis in our trust in money, as the monetary system is essentially a system of debt payments conferring consistency to trade and vital to economic efficiency. The entire system is based on that trust. If you buy something, you must pay for it; if you sell something, you must be paid for it. And we borrow because we bet that the income generated by the investment will enable us to repay what we borrowed.

Trust essentially is the ability to rely on someone's word, or on a signed contract. In this case, contracts for debts and receivables, which underpin the entire system, must be respected. Trust in banks themselves is also crucial, as they create money out of nothing by offering credit. The same applies to trust in the central bank. Not only because it is the bank's bank, but above all because it is in charge of monetary regulation, regulating the growth rate of money, the linchpin that holds everything together.

If the central bank were to emit too much money for too long and with no limits, a major crisis could arise, similar to the collapse of the assignat currency in revolutionary France. Beyond a theoretically undetermined threshold, there is a risk that the official currency will be spurned, resulting in the

disintegration of the system of debts and receivables, and, in turn, the potential disintegration of our entire society.

This trust must be protected, otherwise people may decamp to a foreign currency. And even if all the central banks were to do the same thing at the same time, people could potentially take refuge in gold or physical assets such as real estate. The day could even come when we take refuge in a cryptocurrency issued by a GAFA having become more solvent than states. The cryptocurrency would become a private currency, and a way to circumvent official systems.

Money is an institution, and must be managed as such, as an entirety founded on trust and rules. By rules, I mean the repayment of debt, i.e. monetary restrictions. In other words, while company and government debts are generally repaid by the introduction of new loans, by the obligation to maintain a sustainable debt trajectory. Keeping interest rates extremely low will not suffice alone to ensure this requisite sustainability, as there are no assurances over the long term, and incomes can also contract during a recession, even in an environment of extremely low interest rates. It is thus possible to suspend monetary restrictions temporarily, as is the case today, but not on a lasting basis.

The legitimacy of central banks thus hinges on their being above private and state interests alike by guarding against fiscal dominance and financial market dominance. They must be dominated neither by states, which would oblige them to maintain excessively low interest rates on a lasting basis, nor by the financial markets and their ongoing calls for more monetary injections.

The duty of central banks, then, is to defend the general interest and safeguard their credibility. Failing this, they will be powerless to make valid use of monetary policy in the event of a further need, for the economy and its effectiveness, and for social order itself.