



## **Berenberg/HWWI study: “The Future of Money – The Money of the Future”**

# **The market for digital payment systems is growing – Germany is in last place when it comes to mobile payment usage**

- Digital currencies like Bitcoin are not yet mature
- Cash is the most popular payment method in Germany

Hamburg. Payment systems are not immune to the increasing digitalisation of life in our time. Given the diverse range of digital possibilities, it is even possible to imagine a cashless economy today. “Despite all the technical alternatives, we do not believe that cash is on the verge of extinction”, said Berenberg economist Dr Jörn Quitzau in the recently published study “The Future of Money – The Money of the Future” of the Hamburg Institute of International Economics (HWWI) and private bank Berenberg. “We consider the complete abolition of cash in the coming years to be neither very probable nor desirable. Citizens should be able to freely decide whether they use cash or other payment systems.”

Blockchain, bitcoin, fintechs: The digital transformation is now shaking the very foundations of the financial sector. Given the diverse range of new payment possibilities, the continued existence of cash as the very symbol of the financial sector is at risk. The debate regarding a world without cash has already begun. However, technical innovations are not the only factor to consider in this debate, as monetary policy in particular has tarnished the image of cash in the

last few years. Some argue that monetary policy based on negative interest rates would be even more effective if economic actors were not able to escape negative interest rates by fleeing to cash. Without cash, it would be possible to better stimulate the economy, they argue. “However, we consider this argument to be hardly appropriate. It would be a dangerous experiment to react to a temporary economic problem with a profound structural alteration of our proven monetary system”, Quitzau said.

Despite all the criticism and all the technical alternatives, cash is not yet on the verge of extinction. “The great popularity of cash proves that it has prevailed in the competition of different payment systems, at least in Germany. Ultimately, cash confers a certain degree of liberty because in a cashless society the consumer would be completely transparent”, said Prof. Dr. Henning Vöpel, Director of the HWWI.

### **Digital payment systems are changing payment behaviour**

Nevertheless, payment behaviour in Germany and other countries will continue to change. Digital progress has made the payment process faster and simpler in many areas. Four innovations are particularly important: (1) *contactless payment*, (2) *mobile payment*, (3) *peer-to-peer (P2P) payment* and (4) *instant payment*. All four of these digital alternatives to cash rely on the existing infrastructure of commercial and central banks and credit card issuers. Security, transparency, low costs, and ease of use are especially important factors contributing to acceptance by consumers. Compared with other countries, Germany ranks last when it comes to the use of contactless and mobile payment methods. Moreover, the use of mobile payment apps is still in its infancy in Germany. Security concerns in particular stand in the way of widespread acceptance by consumers. “The possible risks associated with a completely “transparent” customer cannot yet be fully fathomed today”, Vöpel said.

### **Virtual currencies on the rise**

Innovative payment systems developing outside the sphere of existing monetary and currency structures (i.e. digital and cryptocurrencies) are making big headlines these days. Bitcoin is the most prominent representative of this new kind of money, with a market share of around 80 percent. This “new money” is

not created centrally by central banks, but decentrally by a network. However, virtually no one uses digital currencies in Germany today. Bitcoin has attracted the attention of the media as a result of its very impressive appreciation. “We consider the rapid price gains to be speculative and overblown, even though theoretically there is no predictable upper limit at this time; investor euphoria is fuelling the rise”, Quitzau said. Moreover, there are some inherent problems that cannot be easily solved. The importance of bitcoin as a payment method is still very limited today because hardly any merchants accept it. Digital currencies are also not well suited as a store of value or unit of account because they are still subject to substantial price volatility and cannot be said to have true value stability. “For the time being, digital currencies like bitcoin should be considered more of a gamble than an investment. The massive price fluctuations and the high hurdles that would need to be overcome before bitcoin and other digital currencies could become established as payment media can be considered prohibitive factors for now. The future development of bitcoin will depend very much on its acceptance, as well as transaction costs and risks”, Quitzau said.

### **Blockchain offers diverse application possibilities**

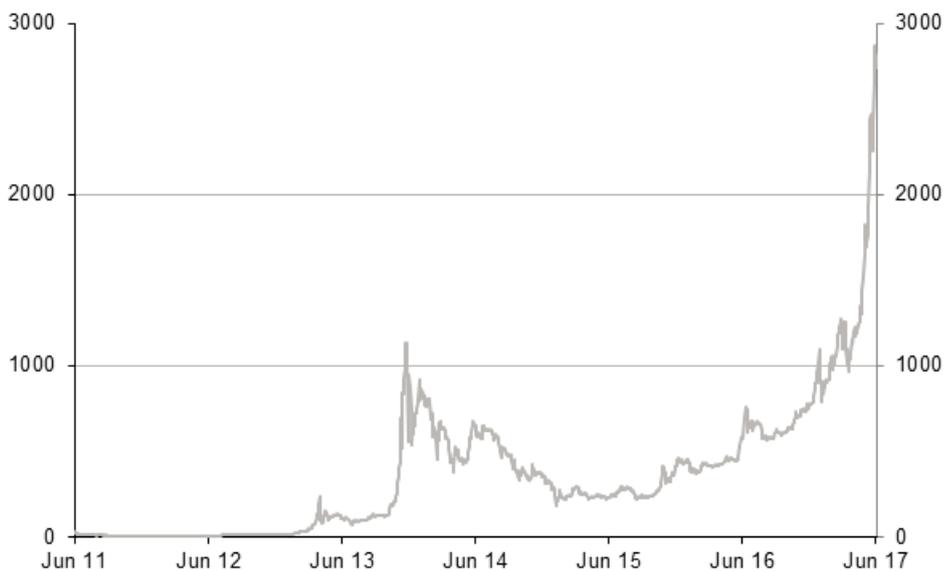
Blockchain as the technological innovation on which the cryptocurrencies are based offers a diverse range of application possibilities and will probably become established in our current economic system independently of the monetary and currency system. Blockchain offers great cost reduction potential. Information and performance flows will be executed decentrally. Work that was formerly done by humans will be processed by computers in seconds, free from errors and with complete reproducibility. Cost-intensive payment systems such as bank transfers and credit card payments will come under pressure. “Currently, those countries that do not yet have a mature financial infrastructure are benefitting the most”, Vöpel said.

### **Fintechs are modernising the financial industry**

Fintechs offer innovative financial services with the aid of new technologies and are mainly focused on making standardised processes of bank transactions simpler and faster. A transaction volume of EUR 17 billion was processed in the segment of payment services in 2015. “Fintechs can enhance the efficiency of the financial system by lowering the costs of financial transactions and

comprehensively analysing large quantities of digital information”, Vöpel said. There are supposedly more than 400 fintechs in Germany today. With their innovations, they not only challenge banks, but also cooperate with them. There are supposedly roughly 70 cooperation arrangements between major German banks and fintech enterprises today. “Fintechs are turning banks into leaner, platform-based technology enterprises whose capital will increasingly consist of data. Financial services will become hyper-individualised, i.e. increasingly tailored to individuals. This development, in turn, will bring new regulatory questions to the fore”, said HWWI Director Prof. Dr. Henning Vöpel.

### Bitcoin/US Dollar Exchange Rate



Source: Bloomberg

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#### **About Berenberg**

Founded in 1590, Berenberg is one of Europe's leading private banks today, with over 1,500 employees in its Wealth Management, Asset Management, Investment Banking and Corporate Banking divisions. Headquartered in Hamburg and led by managing partners, Berenberg maintains a strong presence in the financial centres of Frankfurt, London, New York, and Zurich.

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