PUBLIC FINANCE. ACCOUNTING EXPERIMENTS AND INTERNATIONAL CREDIBILITY

The excessive risks of the fiscal currency

A parallel currency for civil servants and suppliers would lead to a financial crisis
Fiscal currency: why we say no to a fiscal currency

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When two-thirds of the political forces, at least on paper, are in favour of introducing a parallel currency, this can only be worrying. When a detailed economic "point of view" of the Bank of Italy breaks down this idea and no newspaper reports it, this worries even more.

What did the Bank of Italy say? With a wealth of normative references, the Bank of Italy has made various considerations. (1) The fiscal currency would not be legal tender but have only a function of reserve of value, and therefore would be very similar to a government bond (someone calls it mini-BOT). (2) If a state decides to make its payments in a currency other than the legal tender, it would be a violation of the European Treaties. (3) It would probably have "negative reputational repercussions on potential underwriters of public debt securities". To use less cautious and careful words, a financial crisis would arise.

The central bank also clearly stated that the fiscal currency "would have a lower degree of liquidity in transactions other than paying taxes" and thus would be exchanged at "a discount on face value" and would entail "additional costs on top of those paid for the issuance of government bonds". As a result, if suppliers and employees "were forced to accept payment of the fiscal currency, they would suffer a reduction in their income, being paid with an instrument of lower value than the legal tender in subsequent transactions." Also, the fiscal currency represents "a liability from the moment it is issued, in line with government bonds". Therefore, "since they are all liabilities of the State, these instruments could only be issued respecting the constraints on the deficit and public debt imposed by the Stability and Growth Pact".

We dare to raise some additional points, much more fundamental and not said by the Bank of Italy. Even if on a small scale (but this would be all to be seen), it would produce the same effects of an exit from the euro, that is Italexit.

With the immediate depreciation of the new fiscal currency, firms would either increase prices or their revenues would suffer, and therefore the ratio between their revenues and their euro-denominated debt would deteriorate. Even the State would still have to repay the existing public debt in euros against revenue denominated in the new fiscal currency (which according to some should be given for free to citizens). Even if a debt redenomination could theoretically be possible, it would be a de-facto default. Major companies would not be able to do so for their debt and, if they did, foreign creditors could seize their assets, at least those abroad. Many businesses would end up bankrupt.

And the banks? The existing deposits are denominated in euros. With the adoption of a parallel currency, any attempt by the government to change the denomination of the public debt or the debt of the residents towards the banks would bring the value of the assets in euros well below that of the liabilities and then lead to a potential insolvency. Recording these developments, depositors would not waste time and thus move their deposits abroad, causing capital flight and panic.

The bleeding could be contained only with the introduction of restrictions on capital movements, but this, outside a European assistance programme, would not be consistent with full participation in the European Monetary Union. Alternatively, it could be limited if the European Central Bank were willing to act as a lender of last resort for the banks. Alternatively, if there was adequate national and/or European deposit insurance. To put it slightly differently, in the European context the ECB/SSM and European authorities would, in practice, have a veto power. Any attempt to adopt a dual currency would rapidly transform into a forced ejection from the single currency. Therefore, the fiscal currency would not even serve as a bargaining chip in Brussels or as a "Plan B".

Even the idea of making quantitatively limited double circulation does not hold. If the circulation were for small amounts, it would not be worthwhile to take all these risks, and the limit beyond which the above effects would emerge is not quantifiable ex-ante.

For these reasons, the idea of adopting unilaterally a fiscal currency in a vulnerable country like Italy is simply not a sustainable proposition.

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