The Swiss vote on the monetary system

Switzerland will vote on the “Vollgeld Initiative” - a sovereign money system where only the central bank can issue money. While the proposal is unlikely to be adopted, we cannot exclude some nervousness, as a yes vote is likely to have a negative impact on Swiss GDP

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What is the Vollgeld Initiative?

First, a bit of context. Switzerland's political system is based on a form of “direct democracy”, which means citizens can propose changes to the constitution (popular initiative), or ask for a referendum to be held on any law voted by the government.

Now on 10 June, Swiss citizens will be asked to give their opinion on the “Vollgeld initiative”. The promoters of the initiative want to reform the monetary system and transform all existing money in Switzerland to sovereign money and enable the Swiss National Bank (SNB) alone to create both bank notes and electronic money (scriptural money). Banks would no longer have the ability to create money. Instead, they would only be able to lend the money they receive from savers, other banks or from the SNB.

The goal of this initiative is to transform money on current accounts into completely safe money as promoters believe it would avoid bank runs, which we believe is highly debatable, resolve "too big to fail" problems as well as prevent the creation of financial bubbles. Moreover, they think Switzerland will be able to benefit from seigniorage on scriptural money creation, which is an unused resource in today's system. These additional resources would then be used following some yet-to-be-decided rules, for example redistributing to the Confederation, the cantons or directly to the citizens.

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In practice, the initiators of this reform imagine a system where banks would continue to offer all current financial services such as offering credit, enabling transactions, wealth management, etc., but without creating money. They would still grant credits to clients, assess implied risk and set interest rates accordingly, but the number of credits would be limited by the quantity of money created by the SNB.

Moreover, only central bank money would be on current accounts, and they wouldn't generate any interest because they are completely risk-free. Alongside current accounts, saving accounts would still exist at the commercial banks but as a form of investment solution, bearing risk and yielding interest. The SNB would be solely responsible for determining the quantity of money needed by the economy under its price stability mandate, so it has direct control over 100% of the money supply.

For the system to work, the central bank is required to be completely independent in estimating the quantity of money needed to ensure price stability and determine financing conditions in function of the economic situation.

Consequences of the initiative

The referendum will allow the Swiss press to cover the pros and cons of this initiative, but the sheer technicality of the topic will make it hard for supporters and opponents to explain their arguments simply. But we believe that this initiative Without a doubt, this initiative has the merit of asking interesting questions about the modern monetary system and highlighting systems that are not well known to the public.

But for now, it seems almost all political parties, institutional bodies and economic circles are opposed. The SNB itself is not in favour as it believes this would not increase the stability of the financial system and fears there would be an increased risk of politicisation of the monetary policy, which threatens the independence of the SNB.

An academic paper[1] studied the impact of the reform and estimated the possible qualitative implications which show that the overall impact would be negative for the Swiss economy[2] and more specifically for depositors.

Moreover, the reform is likely to lead to high uncertainty because the text of the initiative is not precise and the way to implement it is not defined. Secondly, the system has never been achieved anywhere else, which means that we would not know how economic agents would react. The initiative could, therefore, have a clear destabilising impact.

[1] http://people.unil.ch/philippebacchetta/files/2017/08/Vollgeld_6.pdf

[2] More precisely, in a normal interest rate environment it would have an annual cost to the economy of 0.8% of GDP.

Our baseline scenario

We believe that abstention will be the major winner of the referendum, but the majority will still reject the proposal.

Thus, our baseline scenario is that the monetary system won't change any time soon. However, both the majority of cantons and votes is required, but no minimum participation rate is required. A low turnout might yield unexpected results.

As we have learnt from Brexit, leaving something with so many possible consequences at the mercy of a single referendum is a risk worth flagging. Indeed, a "yes" would require a complete overhaul of the current monetary system and would cause insecurity and could harm the financial centre and, thus, Switzerland as a whole. It is almost impossible to anticipate the consequences of such an experience on the Swiss economy for now.

All in all, even though we don't believe the initiative will get enough public support, the referendum remains a risk for the Swiss economy, potentially creating turbulence for Swiss financial markets especially if opinions polls suggest a close result. This is likely to put downward pressure on the Swiss franc.

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