

Central banks versus private banks: what is the future ...

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The [FT included two articles](#) yesterday (the second [is here](#)) on a new report from the Bank for International Settlements (BIS) - which is the body that effectively represents the world's central bankers. Both related to a report from the BIS that effectively said that central banks should be very wary about setting up their own crypto currencies - as the central bank of Sweden has, for example, proposed doing - because if they did there was a real risk that in the event that there was a crisis of confidence in banking everyone would flee from private banks and their bank created money into the central bank and its crypto created currency.

The reporting is fascinating - and I should make clear that I have simply not had time to read the BIS and if anyone else has and can comment on it then that would be really useful. The implications are threefold.

The first is that it is entirely possible for a central bank to create such a currency. This is hardly a surprise. All fiat currency is essentially central bank money backed by the promise to pay from the government of a country that will accept the currency in question in settlement of tax.

The second is that such a currency may well prove more popular than that created by private banks now, acting under licence from the central bank. The argument is presented that because of this the crypto currency should not be created because this would reduce the role of private banks in the economy.

The third is that the reason why this role should be retained by private banks is, according to the BIS, that they might be better allocators of capital than central banks that might otherwise have to assume this role if it was apparent that the central bank was really the currency creator.

I do, of course, simplify the argument.

And I do, of course, put my spin on it.

But, assuming I have summarised appropriately (and I think I have) then there are

some pretty obvious implications.

The first is that there is only room for one currency in a country, and government created money will always be preferred.

The second is that the current role of private banking in money creation is wholly dependent on central bank support: by themselves they do not create this value.

Third, the value of banks is not then in loan creation: it is at best in loan portfolio management.

And fourth, depositors see this as an activity of little consequence to them when seeking security for their money. Income generation is, for them, vastly less important than asset security, which ultimately only the state can provide.

I am sure other points could be added. But the questions all this begs then are also numerous. Another list is needed.

First, why do we permit private banks such an important role in the economy in this case?

Second, why aren't we taxing the seigniorage that they enjoy now but which is very clearly not theirs?

Third, how do we know that the state might not be a better allocator of capital when there is little evidence in a country like the UK that banks do this at all well?

Fourth, this implies that there may be more to the Positive Money role for banks as allocators of capital provided to them by a central bank in the future than I might have expected. Thoughts?

Fifth, should we really shape policy on an issue as key as this purely on the basis of providing support to the private banking sector when it may well be that the ultimate arbiter on this issue - the cash holding public - think they are suboptimal?