

A Case for Preserving Anonymity in Payment Systems

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Abstract

This paper examines why individuals may value privacy in transactions for reasons other than identity theft or price discrimination. We develop a simple signaling model in which observable purchase records allow others to infer individuals' preferences and productivity. When transactions are anonymous ("full privacy"), individuals can consume according to their intrinsic preferences, yielding the first-best allocation. When transactions are non-anonymous ("no privacy"), individuals distort their consumption toward goods associated with higher productivity, generating signaling costs and welfare losses. When individuals can choose between anonymous and non-anonymous transactions, welfare is lower than under full privacy but higher than under no privacy. By associating anonymity in transactions with payment methods, this study shows that there may be benefits in maintaining anonymity in cash.