Will the World Soon Be Ready for Central Bank Digital Currencies? The IMF Seems to Think So

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The move towards central bank digital currencies (CBDCs) "is gaining momentum, driven by the ingenuity of Central Banks."

As a barrage of Western sanctions visit all manner of pain upon Russia's economy, attention is turning in some quarters to potential ways of circumventing U.S. economic sanctions in the future. One potential weapon for defanging future sanctions is central bank digital currency (CBDC) networks, according to Lewis McLellan, the digital editor of the Digital Monetary Institute of the Official Monetary and Financial Institutions Forum (OMFIF):

Cross-border central bank digital currency networks are in development across Asia (like the mCBDC Bridge, which involves Thailand, Hong Kong, China and the United Arab Emirates). Russia's central bank is working on a digital rouble and Governor Elvira Nabiullina has expressed interest in its value as a means of facilitating cross-border payments, particularly with China.

The digital yuan could also be pressed into service. It is widely usable within China and is likely to be accepted by anyone with costs or liabilities in China. Even dollar stablecoins, which are growing in scale and importance, could help form the backbone of a payments network that cannot be curtailed by revoking access to Swift or the Fed's clearing system. There is no evidence that China intends to help Russian businesses circumvent sanctions — they are likely to face their own sanctions if they do — but if the dollar payments network is becoming a tool of foreign policy, it adds a new sense of urgency for some to develop an alternative.

Beijing Expands Public Testing of Digital Yuan

The digital renminbi is the first CBDC to be issued by the central bank of a major economy and has been undergoing public testing since April 2021. China's testing of CBDCs has so far taken place in ten cities and regions (Shenzhen, Suzhou, Chengdu, Xiong'an, Shanghai, Hainan, Changsha, Xi'an, Qingdao and Dalian). According to Chinese state-backed financial media outlet *Securities Times*, Beijing is on the verge of launching trials of its digital yuan currency in a third batch of localities, which could include Henan, Fujian and Heilongjiang provinces, and the cities of Guangzhou, Chongqing, Fuzhou and Xiamen.

China's central bank has been exploring the possibilities offered by digital currencies since 2014. Those possibilities include reduced operating costs, increased efficiency and "a wide range of new applications," said Fan Yifei, a deputy governor of the PBOC, in 2016. A year later, the State Council of the People's Republic of China gave its blessing to the development of the digital RMB. Commercial banks were invited to participate in the project, as too were Chinese tech giants Tencent, Alibaba, Huawei, JD.com and UnionPay.

The digital renminbi has since been flagged as a “national security issue” threatening the U.S. dollar by Josh Lipsky, a former IMF staffer who is now at the Atlantic Council, an influential U.S. think tank. Yet the People’s Bank of China is hardly what you would call an outlier when it comes to experimenting with or piloting a digital upgrade of its national currency.

In total, 87 central banks in economies representing 90% of global GDP are currently at it, including the Federal Reserve, the European Central Bank, the Bank of Japan and the Bank of England. The Reserve Bank of India recently announced that it will introduce a digital rupee in the coming financial year (April 2022 to March 2023). Three CBDCs have actually gone fully live in the past two years: the so-called DCash in the Eastern Caribbean, the Sand Dollar in the Bahamas and the eNaira in Nigeria, whose impact so far has been pretty underwhelming, as the technology news website Tech Monitor reports:

Almost as soon as it was launched, users complained of poor functionality and the app was briefly withdrawn from the Google Play Store for improvements. By January, only 694,000 eNaira wallets had been downloaded (the e-Yuan, by contrast, remains in its pilot stage but boasts some 260 million users). Spending also remained low, with $450,000 worth of transactions recorded.

IMF Firmly on Board

As one might expect, the International Monetary Fund (IMF), the world’s most important supranational financial institution, is deeply involved in this process, including by providing technical assistance to many of its members. Speaking at an event organized by the Atlantic Council last month, the IMF’s President Kristalina Georgieva outlined the potential benefits of CBDCs while heaping praise on the “ingenuity” of central banks:

> We have moved beyond conceptual discussions of CBDCs and we are now in the phase of experimentation. Central banks are rolling up their sleeves and familiarizing themselves with the bits and bytes of *digital* money.
>
> These are still early days for CBDCs and we don't quite know how far and how fast they will go. What we know is that central banks *are* building capacity to harness new technologies—to be ready for what may lie ahead.
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> If CBDCs are designed prudently, they can potentially offer more resilience, more safety, greater availability, and lower costs than private forms of digital money. That is clearly the case when compared to unbacked crypto assets that are inherently volatile. And even the better managed and regulated stablecoins may not be quite a match against a stable and well-designed central bank digital currency.
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> We know that the move towards CBDCs is gaining momentum, driven by the ingenuity of Central Banks.
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> All told, around 100 countries are exploring CBDCs at one level or another. Some researching, some testing, and a few already distributing CBDC to the public.
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> In the Bahamas, the Sand Dollar—the local CBDC—has been in circulation for more than a year.
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> Sweden's Riksbank has developed a proof of concept and is exploring the technology and policy implications of CBDC.
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> In China, the digital renminbi [called e-CNY,] continues to progress with more than a hundred million individual users and billions of yuan in transactions.
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> And, just last month, the Federal Reserve issued a report that noted that "a CBDC could fundamentally change the structure of the U.S. financial system."[i]
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> As you might expect, the IMF is deeply involved in this issue, including through providing technical assistance to many members. An important role for the Fund is to promote exchange of experience and support the interoperability of CBDCs.

A Digital Peso?

Even countries where cash is still the undisputed king of the payments landscape are frantically trying to roll out a CBDC. Three days ago, *El País* published an article (in Spanish) titled "Is Mexico Ready for a Central Bank Digital Currency?" The article begins by looking at recent moves by Mexico's central bank, Banco de Mexico (Banxico), to explore the possibility of rolling out a digital peso, which Banxico believes could be ready as early as 2024:

> Othón Moreno, director of policy and studies of payment systems and market infrastructure of the central bank, recently said in a seminar on cryptocurrencies that there is a demand for stable currencies (known as stablecoins), and that several central banks are currently analyzing the issuance process. "Central banks have historically successfully issued their legal tender currencies. We have limited ourselves to doing it physically, but I think it shows that the technology is there, and that the demand is there to be able to issue the same functionalities of legal tender, in a digital version", he mentioned.

Obviously most Mexicans are not even aware that Banxico is exploring the possibility of launching a CBDC, or even what a CBDC is, let alone how it may impact their lives, so just how Moreno can claim that the "demand is there" for a digital peso is hard to fathom. It is even harder to fathom when you consider that 86% of Mexicans still use cash while just 4% use mobile payment platforms or the country's interbank electronic payments system (SPEI).

Zero Public Debate

As with the vaccine passports and digital identity programs that have been or are being rolled out by governments across the world, there is virtually no attempt made to even inform let alone consult the general public on the matter. One of the few attempts was a POLITICO survey of 2,500 Brits conducted in 2021, which found that "British people harbor more suspicion about central bank digital currencies (CBDCs) than excitement":

The poll found only 24 percent of those surveyed believed the digital pound would bring more benefits than harm — 30 percent said the opposite. The rest couldn't decide one way or the other.

Concerns among the U.K. public vary. The threat of cyberattacks and hackers left 73 percent of poll participants reluctant to hold Britcoins. The prospect of losing payment privacy worried 70 percent, while 45 percent were mindful of Britcoin's potential environmental impact — a debate that enveloped other cryptocurrencies.

Fear of government power was also widespread, with 62 percent saying they feared the idea of public authorities being able to seize Britcoins from their digital wallets.

The benefits CBDCs offer central banks are likely to be significant, including far greater control over the money supply as well as the possibility of going much deeper into negative interest rate territory. The benefits for the general public are a lot less clear while the risks, including loss of anonymity and privacy, are potentially huge. The ability to track and trace spending in real time is one of the major attractions (for central banks) of having CBDCs, as Agustín Carstens, the president of the Bank of International Settlements, the central bank of central banks, and former chairman of Banco de Mexico, said in a recent interview:

> "We don't know who's using a $100 bill today and we don't know who's using a 1,000 peso bill today. The key difference with the CBDC is the central bank will have absolute control on the rules and regulations that will determine the use of that expression of central bank digital liability, and also we will have technology to enforce that."

One way central banks could use its expanded powers is to exert control over people's spending habits, as Etienne Luquet, a Mexican lawyer specialized in cryptocurrency, tells *El País*. "Imagine that central banks would become a kind of all-powerful Financial Intelligence Unit that can audit or block accounts, or ensure that money can only be spent on certain items."

This is not beyond the realms of possibility. In June 2021, the *Daily Telegraph* reported that the Bank of England had asked Government ministers to decide whether a central bank digital currency should be "programmable":

> Tom Mutton, a director at the Bank of England, said during a conference on Monday that programming could become a key feature of any future central bank digital currency, in which the money would be programmed to be released only when something happened.
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> He said: "You could introduce programmability – what happens if one of the participants in a transaction puts a restriction on [future use of the money]?
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> "There could be some socially beneficial outcomes from that, preventing activity which is seen to be socially harmful in some way. But at the same time it could be a restriction on people's freedoms."
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> He warned that the Government would be required to intervene and make the final decision.

Another huge possible consequence of CBDCs, whether intended or not, is the disintermediation of commercial banks, which will suddenly face unfair competition from their senior market regulator, which has unlimited ability to create money. According to Luquet, commercial banks could disappear altogether (though one can imagine certain well-placed institutions finding a new role in the emerging paradigm). This is an issue NC contributor Clive discusses in greater detail in his 2019 piece, "Mark Carney's Trojan Unicorn — Are Central Banks Considering Stealth Nationalization in Sovereign Digital Currencies?"

In a speech at the China Europe Finance Summit, in Octobe 2020, Burkhard Balz, a member of the Executive Board of the Deutsche Bundesbank, posited: "What if, in times of crisis, bank deposits were rapidly withdrawn and converted into a digital euro? We call this scenario a 'digital bank run.' The result could be the destabilisation of the entire financial system."

Another major risk posed by CBDCs is they could grant central banks the power to deprive people exhibiting the wrong sorts of views or behavior of the ability to transact altogether. It would be similar to what happened in the Trudeau government's recent money heist in Canada, just a lot less visible and messy. This, of course, would only be possible if governments and central banks completely eliminated physical cash once the CBDCs were fully established — something many central banks swear they won't do. But central banks are not exactly known for keeping their word.