

Can a CBDC become a global currency?

Implementation would be challenging, as there must be a political will to reach a consensus.

BY GORDON CLARKE AND EMIR HRNJIC

WHILE blockchain-based cryptocurrencies like bitcoin have excessive volatility and dubious reputation, the blockchain technology is undoubtedly innovative and potentially greatly beneficial in circumstances where sensitive information needs to be efficiently and securely shared among large numbers of users such as in cross-border payments.

So, what would have to happen for one or more central bank digital currencies (CBDCs) to become an acceptable medium for settling international trade transactions?

Just like fiat currencies, CBDCs have a central bank's backing. They will be exchanged in FX markets, and via on-line exchanges such as Coinbase, and they can enable settlements between individuals and businesses.

They can be more secure, less volatile and more energy efficient than private cryptocurrencies.

Additionally, they can streamline trading via smart contracts whereby both information and payment travel together under the control of programmable governance rules.

If two parties to a transaction wish to use, say, the digital yuan as the medium for settling their transaction, the only constraints are whether the buyer has access to the currency and whether there's a mechanism for adding the transaction to the digital RMB blockchain.

That's where the constraints may arise

because a CBDC blockchain is controlled by the central bank and hence the central bank has to provide access to the mechanism that adds the transaction, either directly or via the domestic banking system.

If parties are in different countries, this will depend on the policies of central banks.

The cost of international funds transfers is another important factor. Using SWIFT for payments is increasingly efficient, but still expensive.

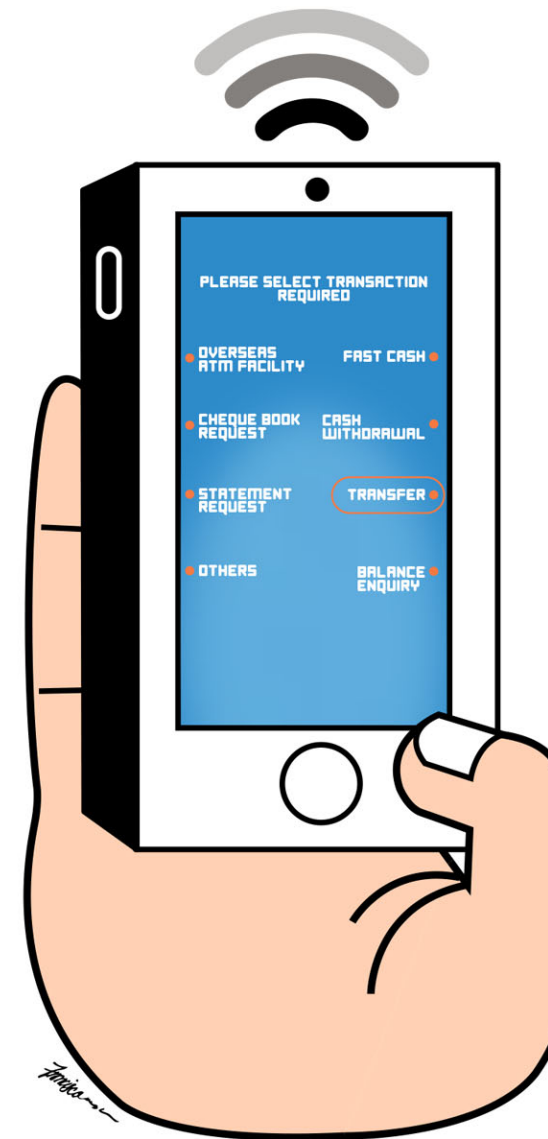
Since SWIFT only provides the messaging, transfers require correspondent banking relationships to manage settlements.

Once CBDCs are available as an alternative to SWIFT, however, we can expect major changes, even if SWIFT retains a messaging role.

Since CBDCs settle directly without a third party, they would enable faster transactions across the world at low cost, thus facilitating trade.

Small trading nations would be at less of a disadvantage as the global trade playing field could be levelled a little. So, the main requirements for global trading currencies can be met by blockchain-based CBDCs at lower cost, with quicker execution and less risk.

Cryptocurrencies of major trading nations could be trusted as they are transparent and exchangeable at a known stable rate that can be negotiated in advance. Moreover, trading via cryptocurrencies addresses the weaknesses discussed above.



It could remove the requirement for settlement using correspondent bank accounts.

This in turn removes some fiscal risks of a reserve currency nation as the issue of the global cryptocurrency can be controlled without requiring an adverse trade

balance.

Furthermore, appropriate blockchain technology can virtually eliminate the risk of forgery and various types of fraud.

Issue can be managed instantly to any central or commercial bank that needs it, so that small country physical shortages would no longer be a problem.

Finally, an arrangement between powerful CBDC issuers, perhaps via the Bank for International Settlements could avoid dominance of any one currency, while a standard basket of currencies could be used for global trade. This would avoid control by a single nation and facilitate open markets.

A CBDC based on the Singapore dollar, which already represents a basket of major global currencies, might be a good place to start.

Regardless of numerous benefits, actual implementation would be more challenging. There would have to be a political will among central banks and global commercial banks to reach a consensus. Rules which reduce the dominance of big players would give everyone a fairer chance, but at the moment, the big guys have too much power and prefer a skewed playing field.

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