All the good things a digital euro could do - and all the bad things it will

10. 11. 2020 | Few other documents have been sent to me as often as the recent deliberations of the European Central Bank (ECB) on a digital euro. There is obviously a great deal of suspicion with regard to plans of a digital euro. The following analysis will try to answer the question if this suspicion is justified.

On 2 October, the ECB announced in a press release that it intends to intensify its work on a digital euro. The ECB enumerated three scenarios under which it might want to issue a digital euro: (i) a sharp decline in the use of cash, (ii) "he launch of global private means of payment that might raise regulatory concerns and pose risks for financial stability and consumer protection" (read: Libra), and (iii) a broad take-up of CBDCs issued by foreign central banks (read: digital yuan).

With a digital euro, also known as central bank digital currency or CBDC, one could, if one wanted and was allowed to, actually do some good, namely:

- create a supplement for cash that protects privacy almost as well but is more practical for some applications
- give citizens and companies an alternative to bank money that is threatened by bankruptcy, and thereby simultaneously curtail the power of banks,
- help prevent a private company such as Facebook, with its own globally accepted currency, from crowding out the euro in payment transactions,
- prevent China from using its digital yuan to replace the euro (or the dollar) as a transaction currency.

On the other hand, however, it is also possible to do rather underhanded things with it, especially:

- facilitate and accelerate the abolition of cash in order to perfect financial control over citizens,
- defend and expand the sanctioning power of the U.S. government, with which it enforces its own law worldwide, including in Europe, in violation of international law.

I will briefly explain what a digital euro is and how it works. Then it will deal with the all-important questions of who controls it and to what end.

What is a digital euro?

Deposits at banks that are denominated in euro and can be used for all sorts of digital payments are already in existence. However, these deposits legally are only loans to the banks which confer the right to be paid back with real money, i.e. euros issued by the central bank. These currently exist in the form of physical cash only. A genuine digital euro would be digital money from the central bank.

So far, only banks have access to digital central bank money. They have account balances at the central bank through which they effect payment transactions among themselves. The main innovation of digital central bank money (for everyone) would be that everyone would have direct or indirect access to such central bank money that can be used for digital payment transactions. There are two ways to achieve this:

1. Everyone gets an account at the central bank for payment transactions. The balances on this account are exchangeable on a one-to-one basis with balances at commercial banks or cash. Like cash, these balances are not at risk of insolvency because the central bank is behind them.

2. Alternatively, citizens would have special accounts at commercial banks for digital central bank money. Unlike normal bank deposits, the balance on these accounts is not a loan to the bank, but an escrow account. The account holder is the owner of the money on it, the bank only manages it as a service provider. If these accounts exist, the digital central bank money can be transfered from some commercial bank's central bank account to a private CBDC account at a commercial bank.

If the central bank would want to protect financial privacy of citizens, it could offer the possibility to load the digital euros onto anonymous electronic wallets or cards that can be used to make anonymous payments. That sounds good and it could be. But there is a big downside. It will not happen.

The real agenda

Anyone who believes that those same central bankers, which have been working together for ten years under US leadership to push back cash, would design central bank digital currencies in such a way that more than small amounts can be paid anonymously, is highly naive. Going beyond cash and looking, as an example, at the case of rechargeable credit cards, which one could use to shop on the Internet while maintaining privacy, the EU Commission and central bankers have acted to restrict the possibilities of use and the permitted amounts more and more, to the point that the option is hardly relevant any more. Why should those same people and working groups, who have done this, suddenly rediscover their respect for the value of people's financial privacy when it comes to central bank digital money?

And indeed, where the central bank's plans are already well advanced, in Sweden, there is only talk of small amounts of CBDC which might be allowed to be spent anonymously. And even that could be stopped at any time.

In Sweden, central bank digital money is recognizably intended to mitigate the disadvantages associated with the impending and intended complete elimination of cash. One of these disadvantages is that, without cash as the only central bank money, there is no longer a clear legal anchor for the monetary system. If bank money represents a claim to the legal tender cash, what is bank money when there is no more cash?

The Swedish central bank has already written a paper on this, in which it concluded that it would be quite complicated. If you declare central bank digital money another form of legal tender, this problem is solved.

Also, the problem of people without a bank account, which is currently impeding the removal of cash for legal reasons, can be solved more easily if the state can simply issue payment cards to everybody which can be loaded with central bank money.

Privacy and cash to be abolished

Just how much respect for privacy can be expected is shown by the fact that only a small paragraph in the long report of a working group of major central banks, including the ECB, together with the Bank for International Settlements (BIS), which was presented at the beginning of October, is devoted to this topic. It essentially only proclaims that a balance will have to be struck between privacy and governments' interest in monitoring citizens, and that it is not about the if of surveillance, but only about how much and by whom:

> For a CBDC and its system, payments data will exist, and a key national policy question will be deciding who can access which parts of it and under what circumstances.

The central banks proclaim that they will continue to offer cash as long as the citizens want it, but nothing more than that. There is no joint commitment to preserve the availability and usability of cash, so that citizens retain an interest in using it. There are recent commitments to that effect by individual central banks, including the ECB. We will have to see if they are meaning it or just paying lip service.

I do think, that the ECB or at least many at the ECB mean it. I doubt, though, that they will prevail against the powerful interests who want to see cash gone.

https://norberthaering.de/en/war-on-cash/ecb-cash-ceilings-mersch/

On the level of the Bank for International Settlements (BIS), which coordinated the group, the intention to get rid of cash is clear enough, though.

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Here is a quote from the secretary general of the BIS, Augustin Carstens, from a 2019 speech entitled "The future of money and payments". The former head of the Mexican central bank and a graduate of Chicago University is the man in Washington at the head of the BIS and a proven fighter against cash.

> Like cash, a CBDC could and would be available 24/7, 365 days a year. At first glance, not much changes for someone, say, stopping off at the supermarket on the way home from work. **He or she would no longer have the option of paying cash**. All purchases would be electronic. But from here, differences start to emerge. A CBDC is not necessarily anonymous, like cash. And unlike cash, it could pay or charge interest.

The report of the ECB working group published in October is also quite clear with regard to the chances of getting a digital Euro which would preserve privacy:

> Regulations do not allow anonymity in electronic payments and the digital euro must in principle comply with such regulations. Anonymity may have to be ruled out, not only because of legal obligations related to money laundering and terrorist financing, but also in order to limit the scope of users of the digital euro when necessary – for example to exclude some non-euro area users and prevent excessive capital flows

The users from outside the euro area who could be blocked are, of course, only one example. Anyone can be blocked and the money flows of the whole population can be controlled and limited if, thanks also to the digital euro, there is no more cash anymore.

The ECB seems only concerned about the banks

From the ranks of the ECB, the Director General for Payments, Ulrich Bindseil, presented a concept for a digital euro, which makes it quite clear that citizens should expect little good from it. His proposal is primarily aimed at ensuring that the banks can continue to play their old game, in which they create money by buying securities and granting loans, thereby boosting the economy, enabling them to put even more money into circulation, and so on until the whole thing collapses at some point and the banks are then rescued by governments and central banks.

To this end, Bindseil wants to discourage high CBDC-balances at the ECB by charging negative interest rates for CBDC-balances above 3,000 euros. The motto is: just don't let CBDC compete with the unsound bank money system.

The unfortunate thing is: such a castrated central bank money, which allows no or only small anonymous payments and limits the size of deposits, is quite unattractive, as economics professor Peter Bofinger pointed out in the German business daily Handelsblatt.

> The digital euro is therefore intended for retail customers. However, what good does an account at the central bank do those people, it there is no overdraft facility and deposits of over 3.000 euro are charged with a penalty interest rate. Any online bank can offer a better deal.

If central bankers are worried about cash disappearing, Bofinger says, it would be much better for them to ensure that the nationwide supply of cash remains guaranteed and that you can pay with it everywhere. After all, the digital euro cannot satisfy the growing demand for a secure and anonymous means of payment, which is evidenced by the increasing amount of cash in circulation in all major currencies, at least not in the expected and envisaged concept.

Fighting back against Libra and digital yuan

If it is not about the interests of the citizens, what is it all about? It's about what monetary policy and geopolitics are always about: power. It was the announcement of Facebook to issue a global money called Libra that scared the central bankers into action. A platform like Facebook, with over two billion users around the world, which issues its own money, could potentially undermine the power of central banks. US Treasury Secretary Mnukhin therefore described Libra as a threat to US national security.

What a private currency has to do with the national security of the USA is explained in the text of the tender of the Office of the Director of National Intelligence for a research project on the dangers for the global dollar dominance. It says:

> There are many advantages for U.S. national security to have the U.S. dollar as the world reserve currency. Any international transaction settled in US dollars, gives the U.S. jurisdiction over financial crimes associated with those transactions, to include support to terrorism and weapons-of-mass destruction (WMD) proliferation. In addition, the U.S. is able to effectively level sanctions against or designate entities that violate international laws or treaties, or that have the potential to cause financial instability in global markets. The U.S. maintains international dominance in no small part due to its financial power and authorities. However, there are many threats to the U.S. dollar maintaining its status as the world reserve currency. Countries such as China and India have large growing economies that could compete with U.S. economic growth. Many cryptocurrency enthusiasts predict that either a global cryptocurrency or a national digital currency could undermine the U.S. dollar. If either of these scenarios or others come to pass, the U.S. would lose both its status in the world and its global authorities.

That the U.S. government would have the power to domesticate Facebook and Libra was foreseeable. On May 6, 2020, Stuart Levey, former First Secretary of the Treasury and top financial sanctioner, was appointed head of the Libra Association. This appointment is likely to imply that Libra is destined to become a tool to assure the preservation of dollar domination rather than a potential threat to it.

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Of course, this is not really good news for the central banks of other countries, considering the unscrupulousness with which the US has recently been pursuing its political and economic interests with the sword of sanctions against everyone and everything. The sanctions against European companies that are involved in the perfectly legal Nordstream2 project and in the perfectly legal trade with Iran, sanctions which are contrary to international law, are only two examples of many.

For the rest of the world threatened by U.S. financial sanctions, a kind of Libra-dollar that could push back their own currency even on their domestic territory is therefore a great threat. It would make the US sanction sword cut even deeper.

If one was stubbornly optimistic, plans by European central banks to introduce digital central bank money could be interpreted as efforts to offer citizens a means of payment that is as attractive as US-based offerings such as Libra.

The fact that the ECB and the central banks of Japan, Sweden, Canada, Great Britain and Switzerland, together with the BIS, formed the above-mentioned working group on DBDC at the beginning of the year, without participation of the US, would seem to support this interpretation.

But that would be naive. As Peter Bofinger writes in his article, payment systems like Paypal's are much more attractive than an e-Euro castrated for the benefit of the banks - at least as long as the submissive EU Commission refrains from enforcing European data protection rules against large US-based global players like Paypal.

Paypal has recently expanded its offer to include payment transactions in Bitcoin. It will be easy for the company to also process transactions in e-Euro via its own system and thus keep them within the range controllable by the US services.

Teaming up against China

In the meantime, the US Federal Reserve has joined the central bank working group on CBDC as the seventh member. It seems to have succeeded in getting the six others to commit to cooperatively shape the development of digital central bank money, as it says in the report published in October entitled "Central bank digital currencies: foundational principles and core features".

The report also states that one of the basic principles must be the involvement of the private sector, i.e. de facto the large multinational U.S. corporations that dominate payment systems globally.

> The payment system upon which a CBDC exists and is transferred must involve the private sector to benefit from innovation and competition and support adoption and use.

In other words. There must not be a fully (national) government-controlled system that excludes US corporations.

Motions to break-free from dollar dominance and the US sanctioning power based on it are thus no longer possible. The only thing left to do now is to jointly avert the other threat to western and dollar dominance, the digital yuan.

China's central bank is further ahead with its digital currency. Since October, a field test with digital yuan has been underway in a district of the metropolis of Shenzen. The central bank raffled off digital yuan among the people who wanted to participate. At the start of the trial, 3,400 stores accepted the new currency.

To add to western concerns, Chinese smartphone manufacturer Huawai recently equipped its new Mate 40 top model with a pre-installed electronic purse that can be filled with digital yuan or crypto currencies.

It is expected that the same feature will soon be integrated into Huawai's low-cost models and those of other Chinese manufacturers such as Transsion, which has a large market share in Africa. Africa has close trade relations with China, so the yuan could significantly increase its market share in Africa in this way, at the expense of the dollar.

Conclusions

Anyone who wants to make the monetary system more stable and citizen-friendly, to preserve the privacy of citizens and the sovereignty of their country should oppose central bank digital money in general and a digital euro in particular.

This is, because a digital euro would most likely be used to speed up the demise of cash. And cash is the only means of payment that can preserve financial privacy and it is the only viable payment technology that can escape surveillance and control by the US-government. A digital euro cannot do this. I would expose citizens and companies of the euro area even more to the ever present threat of US financial sanctions.

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