BANCO DE ESPAÑA
Eurosistema

30.08.2022

Central bank money for the digital age: reflections on the new paradigm

Keynote address/ Central Bank Research Association (CEBRA) Annual Meeting

Margarita Delgado
Deputy Governor

Good evening and welcome to the Banco de España Office in Barcelona.

It is with great pleasure that I take up the opportunity of addressing such a distinguished audience with a topic that I very much feel falls within CEBRA's remit.

Yet, over and above the daunting challenges of inflation, climate change, macroeconomic stability and many others which you are touching upon in the conference, in the next few minutes I would like to turn my attention on to something very different. And it touches upon a very topical subject: central bank digital currencies. That is, the issuance of a new central bank liability, in digital format and accessible to all users.

The interest around this digital version of central bank money is increasing exponentially across the globe. According to the BIS, almost 90% of central banks are exploring the benefits and drawbacks of issuing CBDC, and in the last couple years we have seen a few of them either launching a pilot or actually going live.

While being a worldwide phenomenon, there is no doubt that the specific circumstances of each jurisdiction have a bearing on the analysis of its pros and cons. Nevertheless, when confronted with this topic, one question that inevitably arises in all cases is how a CBDC may impact the stability of the financial system.

Being digital in the financial industry means new opportunities for incumbents to acquire new clients, to expand their current share of the wallet and to obtain efficiencies unheard of. Nonetheless growing digitalization also entails the emergence of new competitors and value propositions that will likely erode their status quo in the industry.

Technology certainly holds a significant transformational power enabling promising developments but, per se, technology is by no means the ultimate answer to existing risks in economics and finance, as my colleague Sir Jon Cunliffe recently pointed out[1].

Against this light, it makes the more sense for central banks to consider the need for a speedy action. This action need to be based on the exploration of a wide set of tools that help to ensure the safeguarding of financial stability as well as the preservation of the critical role of money in the economy.

Let me mention three complementary perspectives from which this issue may be considered.

First of all, while there is a need to assess how a CBDC may impact the financial system, I also see the need to ask ourselves about how the absence of a CBDC could affect financial stability. In this context, it is important to bear in mind the recent developments in finance linked to the new technological advances and the digitalization. In other words, the status quo is unlikely to be an option.

In fact, one of the reasons why we, at the Eurosystem, are looking into CBDCs in depth is to evaluate their potential to ensure easy access to central bank money in the digital era as

[1] Cunliffe, J. (2022) "Some lessons from the Crypto Winter" (https://www.bankofengland.co.uk/speech/2022/july/jon-cunliffe-speech-on-crypto-market-developments-at-the-british-high-commission-singapore).

a foundation of our currency. In other words, a digital euro is seen as the best way to secure that public money remains an anchor for the whole payment system and, in achieving this goal, that trust is strengthened while further protecting the currency's function as a single unit of account.

The second one relates to CBDCs in normal times. When addressing the issue of CBDC and financial stability probably the first thing that comes to our minds is disintermediation. Indeed, a significant transfer of deposits and payments from commercial bank money to CBDC could be a major disruption of the banking system and as a result, a challenge to financial stability as we know it. Central banks must take this into account when designing a CBDC and find ways to strike a balance between the roles of the central bank and both, traditional and new, financial intermediaries.
(This leads to the issue of how to choose among the available features of a CBDC, including elements like limits on the holdings, specific remuneration policies or specific functionalities incorporated in CBDCs.)

The third perspective is the functioning of CBDCs in crisis times. Potential bank runs are a well-known weakness of bank-based financial systems, which justifies a significant amount of regulatory efforts. CBDCs offer to citizens and companies an option to move their deposits to a safer asset. Can design features cater for this risk without putting at risk the success of a CBDC? As a matter of fact, a too attractive and accessible digital euro could foster a significant migration of banks deposits, thus compromising their intermediation and lending capacity and likely destabilizing the entire banking system in times of financial stress.

There are also other considerations. A digital euro, however, exhibit a number of other non-trivial challenges as well. If, for example, anonymity was to be allowed as a means to provide the highest possible level of privacy, we would be compromising our commitment with fighting money laundering and the financing of criminal activity. In that respect, a balance needs to be struck between minimizing the Eurosystem's and intermediaries' involvement in the processing of users' data and still ensuring compliance with the law.

A digital euro is likely to increase as well the Eurosystem's general operational responsibilities over the payments channels. Thus, by promoting a digital euro we must acknowledge that the Eurosystem is potentially putting its reputation at stake as it remains liable for the overall functioning of the digital euro architecture whether it decides to rely on third parties (for its distribution) and or not.

To prevent these macroeconomic and financial stability consequences from happening, ongoing discussions are currently focusing on what potential safeguards could be built into the digital euro. Final decisions remain pretty much open at this stage. The main reason being they not only depend on the practical feasibility of the various available tools but also on the likelihood of different scenarios to materialize and the extent to which the latter may actually compromise banks' resilience. As such, the fine-tuning of design features of the digital euro calls for additional research which I strongly believe the members of CEBRA are best positioned to provide us with.

As of today, operational and legal considerations have been the bulk of our work. The digital euro project faces little chance of success unless it can prove to rely on a solid theoretical foundation. That means for instance, potential distortions of CBDCs to cross-border capital flows, the prospect of a displacement of international reserve currencies or the degree of fragmentation of capital markets they may introduce due to unresolved interoperability issues.

Hence, the time is ripe to ask and encourage you all to actively consider including CBDC-related topics in your respective research agendas as means to broadly support our efforts in landing at the best possible blueprint for a digital euro.

Well, I think it’s about time that we not only feed our minds and souls but our bodies, too.

So, thank you very much for listening and buen provecho. Enjoy the meal!