MAY 27
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The Fed's plans for a CBDC raise concerns among trade groups that banks will lose their edge

Article

The news: The **Federal Reserve Bank** (Fed) made a case for a **central bank digital currency** (CBDC) in Congress, but trade groups see more harm than good, per Banking Dive.

The Fed testifies: In a speech to Congress on Thursday, Fed Vice Chair Lael Brainard spoke about the benefits and risks of a CBDC in testimony favorable to the digital asset.

- She acknowledged that the chaos in the crypto market was unsettling, but said this was primarily due to a lack of regulation.
- The Fed is the right entity to oversee a CBDC because it's been entrusted with currency issuance and it has worked with the private sector to build a stable currency in the US through the security of deposit insurance, central bank liquidity, and regulation and supervision.
- A US CBDC should coexist with crypto and other digital assets as a form of stability and safety in an otherwise unregulated space. To encourage disintermediation of banks, she said, the CBDC should be non-interest bearing and accounts would be capped at a certain amount per user.
- Private banks could offer digital wallets, allowing CDBC to tap into anti-money laundering (AML) technology in the private sector.

Her testimony also pointed out that a CBDC is necessary for the US to stay relevant as a world banking power, as other countries such as China and Russia are developing their own CBDCs.

The industry rebuttal: Prior to this testimony, when the Fed released a report in January discussing the development of a CBDC, it invited comments from industry players and trade groups. Multiple trade groups submitted comments rebutting a CBDC, including the American Bankers Association and the Bank Policy Institution.

- Even with account limits, retail banks would lose major deposits. The groups estimated upward of **$720 billion in deposits** would exit the banking system.
- **95% of money** is held at private institutions, which in turn generates economic output through bank lending.
- The lack of deposits will affect banks' ability to offer credit, and the cost of credit will unsustainably increase.
- Instead, the trade groups believe the Fed should focus on private sector innovation.

In support of their views, the groups also pointed out that private sector innovation in banking established the US dollar as the world's reserve currency, and that further innovation would solidify its position in the future.

CBDCs around the world: Currently **91 countries** have considered or are considering the launch of a CBDC, per Atlantic Council.

- **Nine** countries have already **launched** a CBDC, including Nigeria and the Bahamas.
- **15** countries are running a CBDC **pilot**, such as China and Russia
- **16** countries are **developing** a CBDC, like Canada and Brazil
- Most of the remaining countries are **researching** the possibility of a CBDC.

Notably, China's pilot currently spans **28 major cities**, and it reports that more than **260 million digital wallets** have been opened. Earlier this year, during the Olympic Games, foreign visitors could use the CBDC, called **e-CNY**, at venues in Beijing and Zhangjiakou.

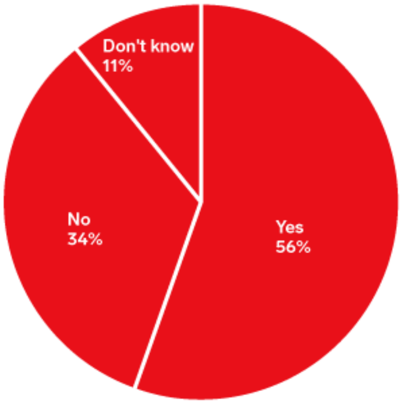
The Bank of Russia is piloting a digital ruble program in partnership with **12 banks**. Earlier this year, it reported that two partner banks had successfully completed a full cycle of digital ruble transfers through mobile banking applications. The Bank of Russia claims that **83% of the feedback it received during a feedback period supported the initiative.** Nevertheless, as in the US, some Russian banks and fintechs fear the CBDC is excessively centralized and could harm private banks' business.

The big takeaway: Worldwide development of CBDCs will push the US to develop its own digital currency if it aspires to remain a world banking leader, especially as younger generations move away from the use of cash.

But execution will be key, as regulation, liquidity, and some form of deposit insurance will be necessary to quell the fears associated with a digital currency. Implementation will also require further planning, as the Securities and Exchange Commission (SEC) has already indicated it needs to bulk up staff in its crypto division. Private banks have an opportunity to step in and help out with CBDC operations. The Fed has hinted at private bank wallets, but whatever course it follows, private banks should expect to play a role in the development and rollout of a CBDC.

Likelihood of Central Bank Digital Currencies (CBDCs) to Replace Physical/Fiat National Currencies in Their Country According to Institutional Investors Worldwide, March 2021

% of respondents



Note: numbers may not add up to 100% due to rounding
Source: The Economist Intelligence Unit, "Digimentality 2021: Digital Currency From Fear to Inflection," May 27, 2021

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