AT A GLANCE

Monetary Dialogue July 2018

European Parliament

Virtual currencies and central banks' monetary policy: challenges

Background

Speculation on Bitcoin and other virtual currencies appears to have subsided in recent months, yet the evolution of money in the digital age and the underlying block-chain technology are attracting growing interest. Not a week passes without financial institutions, including central banks, making statements or providing analysis on how to deal with this matter and the associated risks. Some believe that virtual currencies are the currencies of the future and are deemed to be economically significant. Others claim that virtual currencies are not money, nor will they be for the foreseeable future. As well summarised in a recent lecture of an ECB Executive Board Member, virtual currencies have certain shortcomings compared to traditional money: as a medium of exchange they are far inferior to existing payment options; they lack of widespread recognition as virtual currencies are not legal tender and are not backed by a central bank; and they cannot work as a safe and effective store of value due to their intrinsic wild volatility. Against this background, what is the potential impact of virtual currencies on the financial system? What are their implications for central banks' monetary policy? Could virtual currencies potentially disrupt the monopoly issuance of money by central banks?

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The publications are prepared by Policy Department A of the European Parliament and are available in the relevant section (**Monetary Dialogue**) of the ECON Committee website.

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For the July 2018 session of the Monetary Dialogue, the Committee on Economic and Monetary Affairs (ECON) of the European Parliament has asked monetary experts to analyse the challenges related to the virtual currencies and central banks' monetary policy. References to the relevant in-depth analyses are provided below.

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Directorate-General for Internal Policies
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In-depth analyses of the July 2018 Monetary Dialogue

Virtual currencies and central banks' monetary policy: challenges ahead by Marek Dabrowski and Lukasz Janikowski (Center for Social and Economic Research)

Virtual currencies are a contemporary form of private money. Thanks to their technological properties, their global transaction networks are relatively safe, transparent, and fast. This gives them good prospects for development. However, they remain unlikely to challenge the dominant position of sovereign currencies and central banks, especially those in major currency areas. As with other innovations, virtual currencies pose a challenge to financial regulators, in particular because of their anonymity and trans-border character.

Should central banks be concerned about virtual currencies? by Karl WHELAN (University College Dublin)

Virtual currencies have generated much discussion over the past few years with some believing they are an improvement on state-issued currencies and will end up replacing them. This paper argues this is extremely unlikely. Cryptocurrencies such as Bitcoin do not work well as money because of security weaknesses and the volatility of their price relative to traditional currencies. The theory that the private sector will choose to replace a state-backed currency with privately-issued currency also has little historical backing.

Virtual Currencies by Salomon FIEDLER, Klaus-Jürgen GERN, Dennis HERLE, Stefan KOOTHS, Ulrich STOLZENBURG and Lucie STOPPOK (Kiel Institute for the World Economy)

The paper provides an overview of virtual currencies describing relevant technological aspects and different use cases. Based on this the authors derive implications for financial market regulations and monetary policy (with a focus on the possibility of central bank digital currencies).

Cryptocurrencies and monetary policy by Grégory CLAEYS, Maria DEMERTZIS and Konstantinos EFSTATHIOU (Bruegel)

Cryptocurrencies became a new form of money. However, the current volume of transactions in such cryptocurrencies is too small to make them serious contenders to replace official currencies. Underlying this are two factors: (i) cryptocurrencies do not perform the role of money well, because their value is very volatile and (ii) cryptocurrencies are not managed in modern ways. To replace official money, cryptocurrencies would have to conform to the institutional set up that monitors those who manage money.

Virtual Currencies in the Eurosystem: challenges ahead by Rosa María LASTRA (Queen Mary University of London) and Jason Grant ALLEN (Humboldt-Universität Berlin)

Speculation on Bitcoin, the evolution of money in the digital age, and the underlying block chain technology are attracting growing interest. In the context of the Eurosystem, this briefing paper analyses the legal nature of privately issued virtual currencies (VCs), the implications of VCs for central bank's monetary policy and monopoly of note issue, and the risks for the financial system at large. The paper also considers some of the proposals concerning central bank issued virtual currencies.

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