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Fedcoin Could Be Coming Soon, But Would It Really Challenge Bitcoin?

by **Giulio Prisco** Dec 22, 2017 5:36 PM EST

The idea of "Fedcoin," a cryptocurrency sponsored by the U.S. government and managed by the Federal Reserve, has been around for quite some time. "Imagine that the Fed, as the core developer, makes available an open-source Bitcoin-like protocol (suitably modified) called Fedcoin," a Federal Reserve VP speculated already in 2015. The idea gained traction also in Europe in connection with the financial crisis in Greece, and was notably discussed in a "Eurocoin" context by former Greek Minister of Finance Yanis Varoufakis.

Earlier this year, Nobel Prize–winning economist Joseph Stiglitz said he believes

by Giulio Prisco Tweet

"The technology underlying bitcoin could fundamentally change the way we think of money," said Campbell R. Harvey, a finance professor at Duke University's Fuqua School of Business, in the *Washington Post*. "It is only a matter of time before paper money is phased out."

Phasing out physical cash — the reserve of drug dealers and black marketers — would be one of the main advantages of a national cryptocurrency, according to Harvey, since it would make it far more difficult for criminals to hide and launder money if all transactions could be recorded on the government's blockchain.

The potential for privacy isn't considered a desirable feature for state-owned cryptocurrencies. On the contrary, as Harvey argues, the introduction of digital currencies would be partly motivated by the desire to eliminate the anonymity of cash. On the other hand, even in a future Fedcoin-like, all-electronic economy, it's easy to predict that there would be a strong black economy on the side, powered by privacy-oriented cryptocurrencies, including bitcoin, ether, Monero and other emerging alternatives able to offer stronger privacy.

"Despite the negative press about bitcoin being used for illegal transactions, bitcoin is not anonymous, and criminals who use it often do not understand that their transactions are being recorded," notes Harvey. In fact, while a Bitcoin address isn't explicitly associated with its owner, blockchain network analysis can often de-anonymize Bitcoin users. To support law enforcement, companies like Chainalysis and Elliptic offer sophisticated blockchain network analysis tools and services to trace Bitcoin transactions back to their participants and de-anonymize users.

In a recent presentation, Harvey defined Fedcoin as "a digital USD currency where the complete history of all transactions is visible to the Fed via a Fed blockchain." That blockchain technology, initially thought of as a libertarian means to escape government control, could become a killer app for governments to have complete control over the citizens, and enforce compliance and tax collection, seems surreal to say the least.

Indeed, as Saifedean Ammous, an economics professor at the Lebanese American

flows.”

In the presentation, Harvey cited economist Kenneth Rogoff’s 2016 book “The Curse of Cash,” which proposes to gradually phase out cash, eventually leaving only small notes and coins in circulation, and move to electronic money, perhaps “a government-run version of the virtual currency Bitcoin.”

While Rogoff is not persuaded that the “potentially disruptive” technology of today’s cryptocurrencies is sufficiently mature, he thinks a next-generation “Bitcoin 3.0” could be a precursor to a government-controlled digital currency. “If the private sector comes up with a much better way of doing things, the government will eventually adapt and regulate as necessary to eventually win out,” says Rogoff.

Ammous disagrees with this sort of argument. “The only thing central banks can do with Bitcoin is accumulate it as a monetary reserve asset. At some point, central banks around the world will start asking themselves if they might be better off holding Bitcoin, with its apolitical monetary policy, than other countries’ national currencies.”

> “ Central banks have as much to learn from Bitcoin’s operation as horses have to learn from car engines. It’s a technology meant to displace central control of money.

“The Fedcoin idea was presented by David Andolfatto, Vice President, Federal Reserve Bank of St. Louis, at the first P2PFISY workshop that I organized at the Bundesbank in Frankfurt, 2015,” Paolo Tasca, executive director of the University College London Centre for Blockchain Technologies, told *Bitcoin Magazine*.

“The idea of dispensing with cash in favor of alternative, more efficient means of payments is not new. Pre-1900 utopian thinkers devoted a lot of effort to finding a way to allow people to get rid of what Robert Owen called the ‘insane money-mystery.’ In more recent years, economists have also begun to study the implications of living in cashless societies, especially referring to the role of central banks and to

introduce a purely digital form of government-backed money, perhaps using distributed ledger technology (DLT). The proposed e-krona would be a digital complement to cash guaranteed by the state, and work as a means of payment, unit of account and store of value. It's worth noting that usage of cash in Sweden is declining, and there are indications that the country could go entirely cashless in five years.

The Riksbank isn't the only central bank to consider issuing its own digital currency. The central banks of Singapore, Papua New Guinea, Canada and others are considering similar moves. A recent research paper issued by the Bank of Canada, which considers a possible Bitcoin standard similar to the gold standard, is especially interesting. A discussion paper published by the Bank of Finland, which describes Bitcoin as a revolutionary, marvelous economic system, could indicate that the bank is considering with interest the possibility to someday launch its own digital currency. Even China's central bank is cautiously testing a digital currency.

"Other central banks (Bank of England, Bank of Canada and European Central Bank, among others) are studying the idea of a Central Bank Digital Currency (CBDC) as a non-ordinary monetary tool that could improve the central banks' ability to stabilize inflation and the business cycle, and as a new payment channel that could permit tracing the network of payments and record the payment history of each individual," added Tasca.

Another reason for governments to like the idea of a national cryptocurrency, according to both Harvey and Rogoff, is the possibility to strengthen the power of monetary policy to help manage the economy, for example by making it easier to impose negative interest rates.

Harvey notes that, were the Federal Reserve to adopt its own cryptocurrency someday, it will become a major (and far less volatile) competitor to bitcoin and other digital currencies. "In fact, it's not clear whether [F]edcoin would want that competition, and the Fed is in a position to impose a regulatory environment that tilts the playing field," warns Harvey.

"So watch out, bitcoin."

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