Opinions

Bitcoin is big. But fedcoin is bigger.

By Campbell R. Harvey  December 18 at 3:51 PM

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Over the past few weeks, investors have been flocking to bitcoin, the digital currency whose value has soared by about 2,000 percent in the past year alone. And while many economists are cautioning against excitement about bitcoin — which is caught up in what may be one of the biggest speculative bubbles in history — it’s important to note just how revolutionary the technology may be.

Indeed, the technology underlying bitcoin could fundamentally change the way we think of money.

It is only a matter of time before paper money is phased out. Sweden, where about 2 percent of value of transactions are done in cash, may eliminate physical money within five years. Most central banks are working on technologies to power a future digital currency.

Bitcoin and other cryptocurrencies are based on a complicated technology known as blockchain, which acts like a digital ledger of all transactions completed with the currency. It’s somewhat similar to the serial number that you can find on every dollar bill, but it actually means something because it makes bitcoin nearly impossible to counterfeit.

The exploding value of bitcoin has many observers predicting the launch of a U.S.-backed digital cryptocurrency, colloquially known as fedcoin. And there are many reasons beyond fighting counterfeiting to switch to a digital dollar.

When was the last time you paid for anything with a $100 bill? Or even a $50? Many retailers won’t even take them. Most ATMs spit out twenties no matter how much you withdraw. And yet 79 percent of U.S. dollars in circulation are represented by $100 bills. Include the $50 notes, and it’s 85 percent.

So where are all these bills? In black markets. When police first captured infamous drug lord Joaquín “El Chapo” Guzmán, they also discovered a cash hoard including more than $200 million, mainly in $100 notes.

Cash has the distinct advantage of being anonymous. You can put cash under your mattress or in a vault, and no one knows about it except you. A national cryptocurrency would make it far more difficult for criminals to hoard money because all
transactions would be recorded in the government ledger. If a transaction was deemed illegal, the parties to the transaction could be identified. This is also true with bitcoin, whose ledger is viewable to anyone. 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.

There is another reason for governments to like the idea of a national cryptocurrency: strengthening the power of monetary policy to help manage the economy.

Currently, the Federal Reserve lowers interest rates during tough economic times, but the Fed is practically limited at the zero bound because it is difficult to impose negative interest rates (regardless of whether that would be good policy). Suppose bonds were issued with a negative interest rate of 2 percent, making it expensive for investors to hold them. Who would buy them? Why not hold cash, which has a zero percent interest rate? With a national cryptocurrency, whose supply is controlled by the central bank, rates can be negative.

Worried about deflation in a recession? No longer. A national cryptocurrency such as fedcoin would be able to operationalize Milton Friedman’s famous “helicopter cash” as an alternative strategy to stimulate the economy. A single line of code could instantly put $1,000 into every person’s wallet.

We are seeing an important proof of concept in real time — the meteoric rise in the popularity of bitcoin. Today, the technology is a niche product akin to gold. It is controlled by no one (in contrast to a central bank cryptocurrency) and has limited ability to process large numbers of transactions.

Fedcoin, by contrast, would be decentralized to various Federal Reserve banks. There would be central control over the money supply, just as we have today, but meanwhile, the technology would offer vast improvements in transaction efficiency. Digital transactions are quick, cheap and potentially a lot more secure than the system we have today.

If the Federal Reserve does 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 fedcoin would want that competition, and the Fed is in a position to impose a regulatory environment that tilts the playing field. So watch out, bitcoin.

As we increasingly move toward a cashless society, the idea of central banks taking advantage of cryptocurrency becomes far more plausible. While non-government-controlled cryptocurrencies will likely survive (gold is not centrally controlled, either), the big idea is blockchain technology. This innovation has applications that will likely soon affect every company and consumer.

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**cz_man**  11 minutes ago
Fedcoin would so lose to bitcoin for two reasons:

1) Anything on the blockchain is permanent, Fedcoin can be fiddled with at will
2) Bitcoins are created at a rate of 12.5 every 10 minutes, Fedcoin can debase your holdings in a second.

I guess you could pass laws requiring everyone to keep their value in something that can be debased in a second with no choice or option, but then it might be easier to just enslave everyone. So don't call it fedcoin, call it slavecoin.

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Jimzz 3 minutes ago
Bitcoin is controlled by Chinese miners. They could choose to triple the amount of Bitcoin in circulation tomorrow.
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cz_man 3 minutes ago (Edited)
No, they can't. They can try a hard fork, but that would be worthless as bitcoin trash and bitcoin gold have shown.
Then again bitcoin trash is over 2k at the moment. Antpool pump.
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halfbakedspuriousnationalism 20 minutes ago
Maybe I'll use it to buy electricity for my flying car.
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karfol 23 minutes ago
This is very "pollyannish." As noted below, think about a shutdown by government (or others) of the internet. Hard to believe? Look at our current politics. That is hard to believe too. In 2011 Egypt shut down most of it's internet and cellular services. If all your money is in the "cloud" that's an immediate return to a barter system. Also, think about EMP technologies. Also, EVERYTHING can be hacked -- look at Equifax. It's just a matter of time till bitcoin has a big loss. I use cash regularly and get $50 bills when I take cash. It's not all black market.
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rattus norvegicus 16 minutes ago
Bitcoin has already had a couple of exchanges hacked and coins stolen.
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john numbers 54 minutes ago
"When was the last time you paid for anything with a $100 bill? Or even a $50?"
Uh, yesterday? Very few places actually refuse to take large bills unless they're places like a mcdonalds or other fast food chains. I have never been to a store where I would likely spend 100 dollars and then they won't accept the bill. It's basically just little convenience stores and fast food restauraunt that won't take large bills.
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opinionated too 1 hour ago
Bitcoin offers one big advantage over fedcoin. The government generally can print or make as much money as they feel fit to. This has a general effect of devaluing currency over time. imho both are valuable for their own reasons.

**Jimr22** 9 minutes ago
Actually, the supply of Bitcoin could be increased also if 51% of Bitcoin miners agree to it. Almost all mining is being done in China now, so who knows what the future holds with the strings being pulled from there.

**fishybulb** 1 hour ago
I'm initially skeptical of going totally cashless, but then I think of the last time I used cash...ummm, 6 months ago when I bought a bagel sandwich in a place that doesn't take credit. I haven't carried around cash regularly in many, many months. I haven't carried more than $20 in cash in probably multiple years.

Still, I think there's some uneasiness about it. If the power goes out, you're basically broke. If the internet goes down, you got nothing. At least there's an analog ability with current currency. I would not bet against foreign adversaries targeting our infrastructure in the event of hostilities, so to add the fundamental societal element of currency to something they could completely eliminate from our lives is scary to think about. From gold to paper to crypto to...bartering.

**Jimr22** 1 hour ago
Those are all risks in the current system as well. As you noted, you rarely have more than $20 in your pocket. Unless you have the rest of your money stuffed in your mattress, it's being stored electronically.

**macdean** 9 minutes ago
The analog ability would be driving (or walking) to the bank and withdrawing cash.

**Jimr22** 2 minutes ago
If the electronic system collapsed, the bank would have no way to verify how much money you had in your account.

Even if they had a paper ledger, banks hold little cash in their vaults now. If there was a run for cash, the system would run out overnight.