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Central bank digital euro

Should central banks issue digital currency to households and businesses, as a supplement to cash and deposits with commercial banks? This is an issue that is currently being debated internationally. Latest, the European Central Bank published a report on a digital euro issued by the central bank and addressed to the public (therefore, in the following referred to as CBDE, i.e. central bank digital euro).

The debate is primarily caused by the transformation that is taking place in the payments landscape. The share of electronic payments is increasing, and the use of cash is declining. This tendency has taken place over many years but has accelerated during the pandemic. Furthermore, the arrival of foreign central bank digital currencies and private actors, including large technology firms, developing payment solutions not denominated in euro, means the Eurosystem considers options to increase the relevance of our currency, maintain monetary sovereignty and safeguard financial stability. In general, central bank digital currencies may also be seen as a way to foster the digitalization of the broader economy.

The European banks are acknowledging the European authorities' attention to this transformation and the resulting consequences for the European financial system. Money is the primary and pivotal 'raw material' for banks and bank services. Consequently, a policy debate on the very nature and characteristics of this basic commodity is of utmost importance for the future of banks, the banking system and banking activities, at the service of the economy and society. Depending on its design, a CBDE could have considerable monetary impact. Hence, it is fundamental to acknowledge and secure the role of banks as reliable, trusted and supervised intermediaries when considering any possible future provision of a CBDE. The following reasoning picks up on the ECB's identified scenarios for a digital euro issuance and supports the discussion by reference to essential design principles, aiming to protect the Eurosystem, citizens and financial stability.

Reasons to issue a central bank digital euro should be clear

The EBF takes note of the work that is done by the Eurosystem to investigate a CBDE, that could be aimed at a retail audience, should the need arise. A central bank digital euro should first and foremost be a viable and optimal solution to a clearly defined unserved need in the market, for which no other more efficient solution exists. In addition, it should benefit private individuals and corporates and the economy as a whole, while avoiding destabilizing the financial system. Therefore, before the ECB decides to issue a CBDE, it should be very clear what a CBDE can contribute that is not already covered or can be covered by private payment and deposit solutions.

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ECB and others have identified different scenarios which could induce the Eurosystem to issue a central bank digital euro:

CBDE as a European alternative to global stablecoins or foreign central banks' digital currencies

The Eurosystem wants to ensure that the euro will not be displaced by non-euro-denominated or foreign-operated digital currencies. This would require the CBDE to be at least as attractive from a retail perspective as the mentioned alternatives. However, it should also be considered how private payment solutions in commercial bank money, together with strong regulation and oversight of all digital currencies, can respond to this objective.

CBDE to support the international role of the euro

Developing a CBDE to support the international role of the euro would require opening it up for non-domestic users. If a central bank digital euro is to be used internationally for e.g. trade transactions, it would need to be open for wholesale use too. That is difficult to square with domestic financial stability needs (see below) and would need to be further investigated.

CBDE as a complement to cash

It is unlikely that physical cash will completely disappear anytime soon in the Eurozone. And even so, it seems that a central bank digital currency is not required to have an efficient payment market. This is backed by experiences from the recent Covid crisis and the Nordic countries, where cash usage is very low. CBDE as a complement to cash would impose specific design demands which may not completely replicate those of cash. It would require the possibility to use the CBDE anonymously to a limited extent. Offline use would also need to be possible.

CBDE to improve cross-currency transactions

Cross-currency transactions can be improved upon in terms of speed and costs. However, it is difficult to see how a single-currency digital euro infrastructure can solve this issue. In that respect, ECB and other central banks would have to agree on global minimum standards to ensure the interoperability of different central bank digital currencies. Furthermore, wholesale multi-currency digital currency projects may play a role here but are beyond the scope of a retail digital euro.

CBDE to enable programmable money

Setting up a totally new infrastructure could enable programmable features from the ground up. While it would be possible to build some of these features on top of existing private infrastructures, a CBDE could add to programmability and the introduction of business logic into money, considering also applications for wholesale purposes. It needs to be thoroughly explored how conditionality, being at the heart of smart contracts and programmability, can interact with the CBDE role as legal tender and unconditional acceptance of payments.

CBDE as backup for existing infrastructure

Designing a central bank digital euro as backup would require it to be fully separate from existing infrastructures, and to be able to work offline as well because existing digital infrastructure going down is often not caused by payment processor issues, but by a telecoms breakdown. The CBDE would be vulnerable to the same most common disturbances that affect also private market payments, for example electricity outage.

CBDE to improve financial inclusion

Lack of financial inclusion is a serious problem in many parts of the world, and a central bank digital currency could be part of the answer. However, it is less of an issue in the Eurozone / EEA countries. Moreover, it is doubtful whether introducing a new digital means of payment would address the lack of financial inclusion – especially within the Eurozone, where the risks to financial exclusion are increasingly related to digital exclusion. Would the underbanked really benefit from a digital euro and give them access to financial services they cannot access today?

High-level design principles that must be adhered to

A central bank digital euro can be designed in several ways in terms of who is to have access, how it can be used, distributed and managed, the degree of privacy and whether it is to accrue interest. The way it is designed could affect financial stability and the division of labor between the public and private sector and the extent to which it contributes to future potential economic growth and welfare. It therefore requires thorough assessments at a technical, economic, societal and political level before issuing a CBDE. European banks have in-depth experience with digital transformation and possess the competences on relevant IT and governance structures such as eID solutions and Anti-Money Laundering (AML)/Counter-Terrorism Financing (CTF). Many of them own also specific know-how developed in already implemented solutions based on DLT, distributed infrastructure and related governance. The EBF stands ready to engage in the ECB's considerations of a CBDE if there is a clear analysis that the benefits overcome the risks of destabilisation.

Issues are very different if a CBDE concerns relations between banks and central banks or retail and corporate banking, if it concerns the creation of money or only payments, if it deals with scriptural money or digital banknotes in dedicated wallets.

Should the need for a central bank digital euro to the general public be confirmed, the EBF would like to stress the importance of ensuring that the following high-level principles are incorporated in its design:

Financial stability should be preserved

It is vital that a CBDE does not undermine the robustness of the financial system. In case a CBDE would provide the public with an alternative to bank deposits, this could challenge banks' intermediation capacity. This, in turn, could deprive banks of an important source of stable funding and therefore reduce their ability to provide credit to the economy, i.e. their capacity to support and finance present and future economic growth and welfare. If the banks' deposit base becomes less stable because of a CBDE, this will impair the funding management and make liquidity planning less predictable. There should be appropriate planning and control over the pace at which funds move towards digital currency in order to avoid disruptions in the business model of banks, which could, ultimately, have repercussions on the level of lending. Furthermore, households and businesses could – even given the existence of deposit insurance and bank resolution frameworks – arguably transfer massively their bank deposits to central bank digital euro in a systemic crisis, increasing the risk of bank runs. To preserve financial stability, if a retail CBDE were to be issued, an indirect model should be used whereby banks have access to the central CBDE infrastructure, but then provide access to retail users via accounts and wallets.

A CBDE should therefore be designed as a means of payment only and its usage as a savings or investment instrument should be disincentivised. This could be ensured, for example, by a cap on a CBDE wallet.

Complement and stimulate innovation in payments

The payment landscape is evolving rapidly. European citizens and businesses already benefit from efficient and innovative digital payment solutions, including instant payments. The payments infrastructure is continuously developing and new private initiatives are planned to deliver faster, more efficient, and secure payment solutions in a competitive European market.

The appropriate role of the public and private sector needs to be identified, and the synergies exploited, so that a central bank digital euro will not crowd-out private solutions nor discourage new initiatives in the payment market, some of which are also intended to increase European autonomy in the payment space. We wonder how would a digital euro be aligned with or compare to existing and planned payment solutions and what would be the benefits to the end-user of one over the other. Further down the road, for instance, commercial bank solutions based on a distributed ledger technology could also play an important role in the future of the EU economy to support digital industry processes involving smart contracts and machine-to-machine payments.

Provide a clear governance framework

A CBDE could fundamentally change the role of the European Central Bank, private banks and non-bank service providers in the financial system. The division of labor hence needs to be very transparent and a clear governance framework needs to be agreed on, e.g. who owns, administers, develops and is liable for which part of the infrastructure. The central bank should not provide end-to-end payment solutions but instead rely on supervised private institutions in the distribution and provision of user-facing services, as is currently the case. Caution would be needed so that central banks do not become a direct competitor of private banks in the offering of payment services to the public. Further, to ensure a level playing field, all participants (public and private) must be governed by the same regulatory framework.

Should be cost-efficient and provide incentives for private sector involvement

In general, before issuing a CBDE, the costs (for set-up, integration and running operation) should be estimated and compared with the expected benefits, considering alternative private solutions and effects on existing ones. Any costs associated with the development should be borne by the Eurosystem. Furthermore, there must be viable opportunities for the private sector to develop value-added services and generate revenues, operating on a level playing field between public and private initiatives.

The infrastructure should be secure and resilient

As cybersururity and resilience are the indispensable foundation for any successful and sustainable digital innovation, a state of the art, secure and resilient infrastructure is needed. A central bank digital euro would need to meet the highest security requirements and fully respect the European regulatory framework, with particular attention to the protection of personal data of our citizens (privacy, GDPR) and the AML/CFT requirements.

The way forward

Taking into account their crucial position in the financial and payment systems, and for the financing of the economy, European banks welcome a continuous exchange with the ECB on the digital euro project. The underlying needs, possible – effective – alternatives under these objectives as well as the design principles should be further explored with representatives of the European society at large. We welcome detailed discussions with sufficient time prior to a decision on a project launch.

It is advisable to collect further insights for this complex debate. **We stand ready to engage with the ECB in conducting additional assessments and applying investigative tools beyond the launched public consultation.** The resulting analysis should look, for example, at citizens' and corporates' distinction between central bank money and commercial bank money. It should be understood if there are possible unintended consequences for the citizens' and investors' trust in the banking system, in case this distinction is further highlighted. It should be investigated what could be the potential impact on financial intermediation and stability as well as monetary and prudential policies.

Furthermore, the scope and costs of the project should be quantified by the ECB, in order to compare this solution with possible alternatives, as presented above. Any development towards a CBDE should include an in-depth assessment of the impact on the existing regulatory framework and include a full cost-benefit analysis. We encourage a broader policy debate, given the systemic nature of the considered project and its possible fundamental impact.

Considering the project's potential impact on the Eurosystem's stability, only the result of a thorough debate – while taking into consideration market developments – will add value to Europe's readiness for the future, European financial sovereignty, and citizens' safe access to money in a digital world.

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About the EBF

The European Banking Federation is the voice of the European banking sector, bringing together 32 national banking associations in Europe that together represent a significant majority of all banking assets in Europe, with 3,500 banks - large and small, wholesale and retail, local and international - while employing approximately two million people. EBF members represent banks that make available loans to the European economy in excess of €20 trillion and that reliably handle more than 400 million payment transactions per day. Launched in 1960, the EBF is committed to a single market for financial services in the European Union and to supporting policies that foster economic growth.

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