Olli Rehn: Central Bank issued digital cash

Speech by Mr Olli Rehn, Governor of the Bank of Finland (at time of speaking Deputy Governor of the Bank of Finland), at the seminar on "Central Bank Issued Digital Cash", Helsinki, 13 June 2018.

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Ladies and Gentlemen, Dear Colleagues,

It is a pleasure for me to open the second session of the seminar on Central Bank Issued Digital Cash. This session asks what would be a rational and justified reason for central banks to pursue digital cash.

Today’s seminar is part of a trio of events this week, partly academic and partly for a wider audience in the financial sector. This seminar is for central bankers only, since we wanted to facilitate open and possibly frank discussions, with no any need for official statements.

We have also chosen different colour codes for the three events.

I’m not sure if the yellow colour of our badges has been deliberately chosen to indicate a yellow card, i.e. to be warned due to a foul. Maybe some people see that even a discussion about a digital central bank currency is dangerous play. But here today we won’t be afraid of discussion.

In fact, virtual currencies or crypto assets, as we prefer to call them today, already emerged on central banks’ radar screen many years ago. Since then, central banks, other authorities and academics have studied the phenomenon and published analyses on it. When the market turned into a highly speculative one, both financial supervisors and central banks issued warnings. In our view, virtual asset creation and trade should be regulated in the same way as other tradeable assets. It is important to protect consumers and prevent fraud.

Originally, promoters of virtual assets like Bitcoin claimed they would provide an alternative to banks’ payment systems and change the whole financial system. Even if virtual assets currently don’t have the capacity to fulfil the original vision, they did bring to the surface two very interesting issues: the potential of blockchain technology, and the future role of central bank money in the modern financial infrastructure.

The discussion on the future use of central bank money, whether physical cash or digital, has emerged and even intensified recently, especially in countries where the role of cash in society has been declining.

This raises several pertinent and difficult questions:

What would happen if physical cash really vanished? How would it affect central banks, the financial industry and society as a whole? What will legal tender mean in the future? How will monetary policy and financial stability change if perfectly safe central bank cash were to disappear? If physical cash were to become obsolete, should central banks still be involved in providing central bank money to the public – perhaps in a digital form?

These are indeed relevant questions, even if the issuance of euro cash still continues to grow. This seminar aims to contribute to the contemporary debate and increase our understanding of these questions.

Against this background, let me focus on three topics that the central banks must in my view carefully analyse.

1. What is **the role and meaning of legal tender** and the need for some form of generally

available and usable central bank money for members of the public?

The historical background of legal tender lies in times when different monies circulated and, for the sake of stability, one of them had to be classed as legal. That gave central banks the power to create unlimited liquidity in their own currency, useful for financial stability. However, as the Bank of Finland Legal Unit concluded in its survey, this concept is surprisingly vague today, at least in retail payments.

There are several reasons for this. In some countries, legal tender stands for the common fall-back, if no other payment instrument is agreed upon. In some countries legal tender means the mandatory acceptance of cash for payment e.g. in retail. In the U.S., where it reads on dollar bills that they are "legal tender for all debts", there is no mandatory requirement to accept them in the purchase of goods and services.

2. How can we maintain the ability of official oversight to ensure the safety and – under the dual threats of fragmentation and monopolization – the efficiency of payment systems?

As I mentioned earlier, the payments market is in turmoil with all the new initiatives. Some of them are just user interfaces, but also completely new transmission mechanisms are being introduced to the market.

This development entails some potential problems for the oversight of payment systems. First, while consumer choice is a positive thing, fragmentation may increase uncertainty about trustworthy services. It may become impossible for supervisors to monitor all players, and for the overseers to ensure the robustness of the overall payment system.

Another problem may arise from the fact that more and more service providers are non-banks that are not accustomed to regulatory requirements and may prefer to stay outside the oversight domain. The end-game may look like the free banking era, when competing private banks were printing their own banknotes, and it was hard to keep track of their value. In such a situation, at least, the reintroduction of legal tender in the form of digital cash might become a serious issue.

Robust payment systems are a crucial backbone of modern economies. We must be able to safeguard their functioning also in the future.

About a week ago, Europe experienced a short hiccup in the Visa payment card network. Even if the technical problem was solved in less than 10 hours, it showed how vulnerable our daily lives have become. When 75% of payments are not working, a lot of uncertainty and losses are created. The event reminded us that, to ensure resilience, we need parallel safe infrastructures that can be scaled up, if the normal network is failing.

Today, we still have cash. If or when cash is no longer used to the extent that it can be easily scaled up, other alternatives will be needed. One line of analysis contemplates whether some alternative means of payment could or should be provided by central banks.

3. How are the efficiency of monetary policy and the objectives of macroeconomic and financial stability to be maintained, if all money is issued by private parties, all of which are not necessarily even banks?

Central bankers are often considered conservative. But work in central banks has had to continuously adapt to meet the challenges of a changing environment. The tasks of price stability, financial stability and oversight of payment and settlement systems tend to change and take on new forms, but the core content endures.

This capability to adapt has been evident since 2008, when, during the financial crises, central banks were able to think 'out of the box' and create new monetary policy tools to fulfil their task. The outcome was not just new monetary policy tools, but also stronger macroprudential supervision and, in Europe, the creation of Banking Union.

Bearing that in mind, it is entirely reasonable to expect that the central banks will be able to adapt to the changing financial and payment landscape also when the driver is not a recession, but a technological revolution.

Dear Friends,

I trust your discussions today will be interesting and substantive, and that you will have new insights with you when travelling back home. Sharing both understanding and open questions, being able to work together in the future and take action jointly, all these will be ever more vital when our common field of work is transformed in so many ways.

I wish you a successful seminar.