IEP@BU Working Paper Series

Whither Stablecoins?

Money in a Changing World Order

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1. Introduction[1]

Stablecoins have attracted a lot of attention in recent economic debates. Opinions are divided: according to some, they are the frontrunners of a new monetary system, freer, efficient and inclusive. For others, they are another example of financial madness, unnecessary and dangerous. This somewhat overstates the debate, but not by much.

Framed in these terms, however, the debate misses the point. The issue is not only whether stablecoins or crypto tokens improve the monetary system or not, performing a useful role from a technical viewpoint: it is fundamentally about who controls those instruments. Who sets the rules, governs the supply, controls and uses the information they generate. The matter is political at least as much as it is economic and financial.

As such, it cannot be separated from the broader geopolitical question of the day, namely, what new arrangements will emerge from the crisis of the rule-based international order that we have seen unfolding – gradually, then suddenly, as Hemingway would say – in recent years. Monetary developments are a sideshow to the main act and cannot be understood except in relation to it.

This essay discusses technical and political factors that shape the future of stablecoins as means of payment.

We start (section 2) by looking at the initiatives by the Trump administration which, at the outset, promoted stablecoins as an entirely new private form of money, potentially complementing, or even replacing, traditional payment means. In section 3 we examine whether stablecoins can be a “good” monetary instrument, in light of monetary theory and practice. We conclude that stablecoins perform this function only imperfectly, and only if properly regulated.

Section 4 compares stablecoin regulation in three jurisdictions: the US, the EU and the UK, highlighting their “regulatory philosophies”, strengths and weaknesses. Section 5 discusses political and economic influences driving current US policymaking in this domain, and their implications.

Section 6 concludes with a focus on Europe. After building advanced payment infrastructures in the early years of the ECB, more recently the EU has largely been a follower in digital payments. This may now change: new projects such as Pontes and Appia may result in another leap forward. While upholding its principles, the EU’s priorities are to strengthen its competitiveness and defend its monetary sovereignty. In this way it can also enhance the euro’s attractiveness as an international currency.

[1] This Working Paper was originally prepared as a chapter for the Institute for Law and Finance conference book, following the 14th ILF Conference on the Future of the Financial Sector, “Stablecoins, CBDCs, Tokenization – The New Frontiers of Money?”, held on 27 January 2026.

2. An unlikely actor on stage

Stablecoins have been around for several years, but became truly prominent only in early 2025, when the incoming Trump administration took several steps indicating its willingness to provide political support to that particular instrument. The first dates to 23 January 2025: the White House executive order titled “Strengthening American Leadership in Financial Technology” (The White House, 2025).

That document contained two surprising elements. The first was a shift of focus from Bitcoin, a highly volatile and speculative token, to an eminently “stable” one, the so-called stablecoin. In the preceding weeks and months, the Trump campaign had signalled political support for crypto, participating in Bitcoin conferences, launching tokens, and through other initiatives. The Bitcoin community supported political change in the hope of friendlier regulation. The new administration seemed inclined to return the favour: one of the campaign’s keywords was “the war on crypto is over”. In that context, all attention was, or appeared to be, on high-volatility speculative instruments offering holders and issuers the prospect of quick – albeit uncertain – gains.

It therefore came as a surprise that stablecoins featured repeatedly in the January document, while other crypto assets did not. Stablecoins are pegged to official currencies, the US dollar in particular; by construction they are suited for monetary transactions, not speculative gains. Their market capitalization remains small—at about one tenth of Bitcoin’s.

They are mainly held for operational convenience, to support transactions in and out of other speculative tokens, and were until then, and largely remain, ancillary to Bitcoin and its peers. Stablecoin capitalization has so far evolved closely in line with Bitcoin prices, rising during the Covid pandemic and then flattening or declining thereafter (more on this below).

Why, then, so much interest in this particular instrument?

The other surprise was in how the administration planned to pursue its stated goal of supporting “the development and growth of lawful and legitimate dollar-backed stablecoins worldwide”. Regulation was entrusted to a working group chaired by a Special Advisor for AI and Crypto (a tech entrepreneur associated with Elon Musk with no central banking background) and including members or appointees of the executive, but excluding the Federal Reserve. This was unusual. Not only does the Fed oversee the payment system and has unrivalled expertise in doing so, but a regulatory body with that mandate, including the Fed, already existed: the President’s Working Group on Financial Markets, already engaged, among other things, in stablecoin regulation (US Treasury, 2021).

The two surprises may plausibly be interpreted as expressing the intention to encourage the development of a new general-purpose payment instrument under the regulatory control of the executive, alternative to traditional forms of money issued and managed by an independent institution: the Federal Reserve. The subsequent attacks on the central bank, carried out at different times on various grounds or pretexts, are consistent with this interpretation. The legislation eventually approved, the Genius Act, moves in part in the same direction, as we will argue in section 4.

This raises two questions: How are things likely to develop? Behind the scenes, is politics indeed a main driver of much of the recent enthusiasm about stablecoins?

3. A 20th Century precedent: money market funds

To start, it is useful to revisit a historical experience that is in some respects comparable, namely that of money market funds (MMFs).

MMFs are an unprecedented success story in finance history. Virtually non-existent some fifty years ago, they grew into one of the most important instruments for asset and liquidity management in global finance. After a temporary setback in the financial crisis (Angeloni and Gros, 2025, provide an account), they surged again and now constitute about one third of the broadly defined money stock (M2) in the US.

MMF shares and stablecoins share several features. Both are “inside assets”, instruments that are both assets and liabilities of the private sector. Both are “private monies”: either usable for payments or close substitutes for such instruments. Supply is determined by market forces and not by the central bank. Both can be issued by banks but are more typically issued by non-bank intermediaries. Both stablecoins and MMF shares are redeemable on short notice and backed by liquid securities on the balance sheets of their issuers (banks and non-banks).

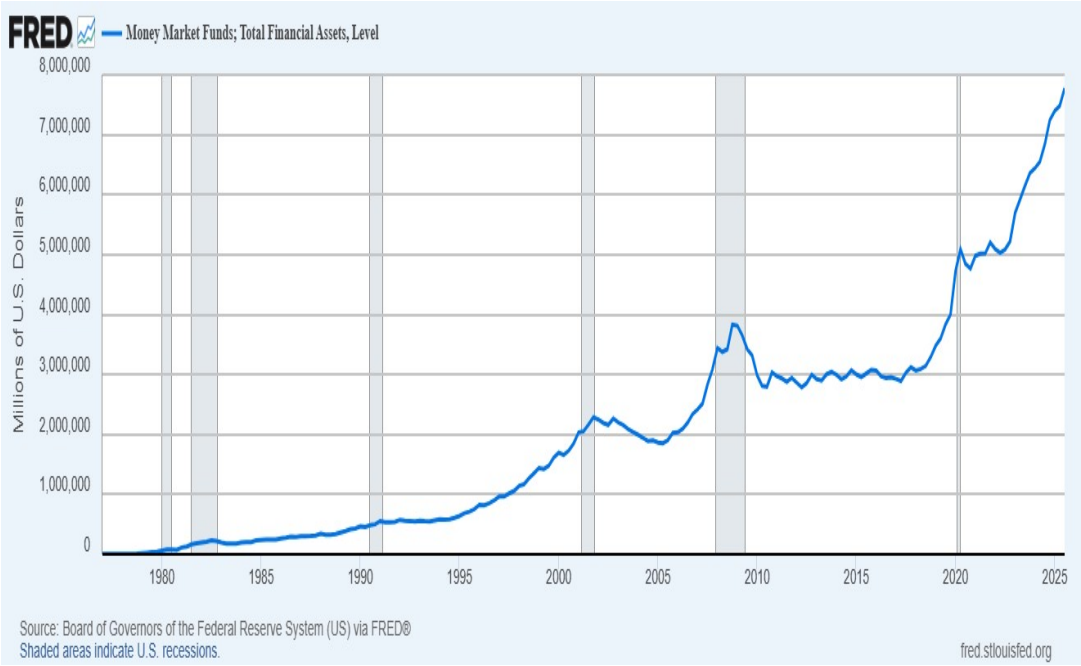
From a financial standpoint, stablecoins and MMF shares are essentially identical. They perform liquidity transformation (albeit to a lesser extent than banks) and hence are exposed to confidence shocks and runs, because their collateral is less liquid than their liabilities.

The rise of MMFs in the early 1980s in the US depended on a legal restriction: the ban on banks paying market-determined interest rates on deposits (by contrast, stablecoins are largely banned from remunerating holders, as explained below).

The novelty at the time was to issue shares in portfolios (a more modern term would be “tranching”), akin to payment instruments while yielding market returns. Their success persisted beyond the legal restriction: while the prohibition for banks to pay interest was lifted by the mid 1980s, MMFs accelerated right at that time, as seen in Chart 1.

The chart also shows that MMFs are cyclical: they slow down or even decline during recessions and accelerate thereafter, especially in the later stages of economic expansions when the general level of interest rates rises. This highlights their substitutability with bank deposits, which usually experience outflows at the later stages of economic expansions.

Chart 1: Money market funds in the US



Source: FRED.

Another distinguishing feature is that MMFs are (so far) largely handled through traditional centralized settlement systems, whereas stablecoins are created and traded on unconventional exchange platforms—namely, distributed ledgers. This makes stablecoins particularly useful in crypto exchanges. But not necessarily only: distributed ledger (DLT) technologies are increasingly used outside the crypto space. One can expect the role of stablecoins in the broader financial landscape to increase if distributed ledgers become more common in financial transactions more broadly. To some extent this is already happening; tokenized deposits are an example.

Will stablecoins replicate the success of MMFs? A decisive factor will be their returns. Unlike MMFs, stablecoin issuers cannot remunerate holders under existing legislation (section 4).

In practice, the legal prohibition is likely to be softened or removed altogether, and there are already signs that it is bypassed: exchange platforms enter into agreements with issuers whereby they remunerate holders and are in turn compensated by issuers. Competitive remuneration is likely to be crucial for the future evolution of stablecoins. Should restrictions persist, stablecoins would suffer a competitive disadvantage compared to banks, some of which already offer tokenized deposits traded on blockchains (Maechler, 2025).

JPM Coin, a deposit token issued by JPMorgan, combines the convenience of 24/7/365 DLT with the protection of the official safety net and the implicit guarantee of the bank's entire balance sheet. Tokenized deposits and tokenized MMF shares may be an ideal combination going forward, making

the singleness of money compatible with on-chain transactions and settlement (Garrath and Shin, 2023).

Remuneration is also relevant in relation to another potential competitor: CBDCs. The digital euro currently under development by the ECB is not supposed to pay interest. By contrast, China recently announced it will pay interest on eYuan, the People's Bank of China's CBDC, hence transforming this digital money from a "cash-like" instrument to a "deposit-like" one. One can only expect competition between CBDCs, stablecoins and tokenized banking products to intensify going forward, and remuneration to be a key factor in the competition.

Lately, the central banking community seems to be shifting attention from retail CBDCs to wholesale applications, possibly combining settlement in central bank money with transactions on permissioned distributed ledgers. Interesting avenues are being opened by the ECB with its projects Pontes (central bank money transacted on distributed ledger) and Appia (same concept applied to financial transactions in general; see European Central Bank, 2026).

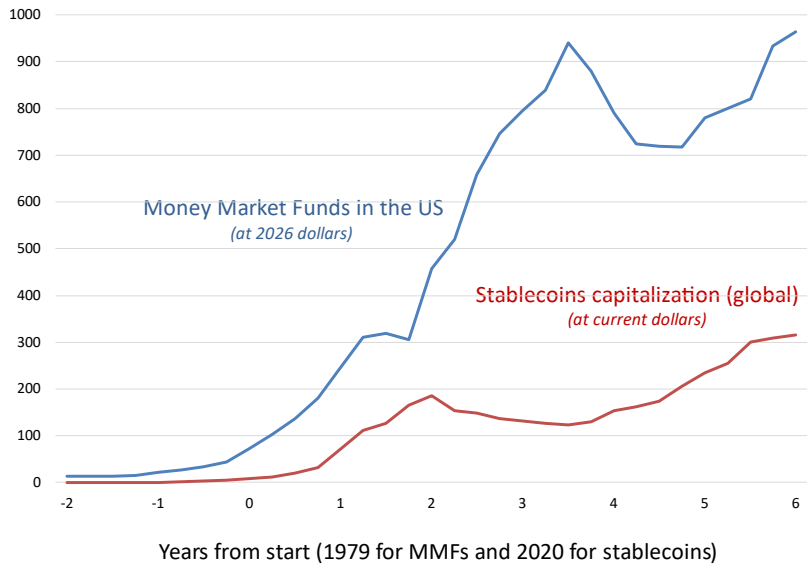
Contrary to what is often assumed, market traction of stablecoins has been modest so far. Outside the criminal world, most usage consists in supporting transactions in Bitcoin and other speculative tokens. This explains the close historical correlation between Bitcoin price and stablecoin market capitalization.

Stablecoin capitalization, virtually zero before 2020, rose with Bitcoin during 2021, benefiting from the Covid pandemic, then fell during the crypto-crisis. In late 2024 the two resumed growth. Today, stablecoins amount to just over $300 billion globally, a comparatively small amount. By comparison, Bitcoin amounts to about $2 trillion, while other crypto assets add a further $1 trillion.

Chart 2 compares the growth of stablecoins, over the few years since their inception, with that of MMFs in their early years. On the time axis, zero denotes the year in which the instruments started rising – 2020 for stablecoins and 1979 for MMFs. Market capitalization is measured in billions of US dollars, with MMF data rebased to account for cost-of-living changes (a ratio of 1:3.9).

In the first 6 years, the growth of MMFs was roughly three times that of stablecoins, once dollar values are adjusted for comparability. The two phases in which stablecoins grew most are 2021–22 and 2025, both special situations for different reasons: the first because of the pandemic, when stablecoins were driven by the surge in Bitcoin, and the second because of the favorable regulatory stance announced by the US administration. In other periods, stablecoin capitalization was either declining or stagnant.

Chart 2: Money market funds and stablecoins: early growth



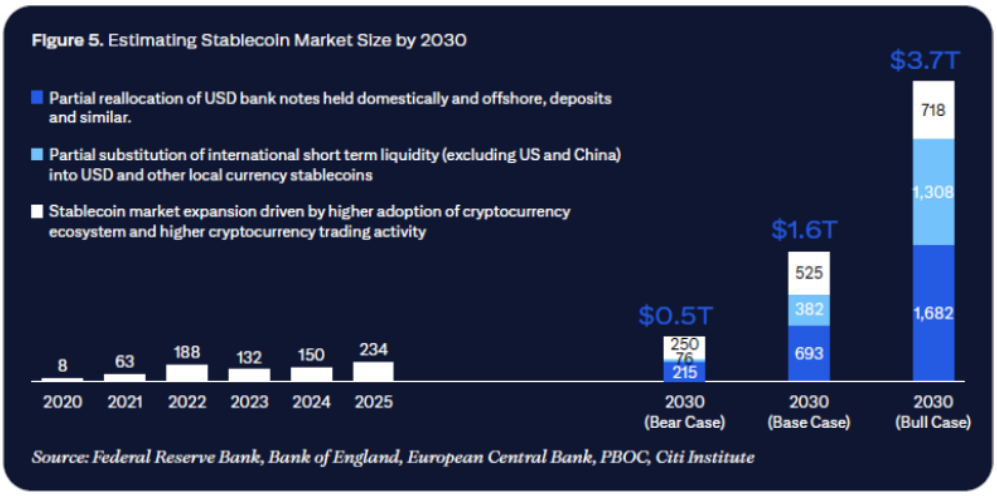
Source: FRED and DefiLlama.

Will stablecoins move beyond the narrow confines of crypto to become general-purpose payment instruments? Advocates point to the inefficiencies of traditional systems—slow transactions, high costs, limited innovation, and burdensome regulation.

Practitioners with a libertarian bent envision a future in which the system runs entirely on private monies, reminiscent of free banking of the mid-19th century. The recurrent crises that punctuated that period are forgotten, as are the reasons why free banking was abandoned and never seriously considered again except as a theoretical possibility. A “this time is different” mindset pervades much of current thinking.

The chart below, from a Citigroup report, presents three scenarios for how the stablecoin market may evolve, labelled “bear”, “base” and “bull”. The “bull case” – a tenfold expansion of market capitalization over five years – would exceed anything MMFs have experienced in their early years. Even in that case, however, stablecoins would not entirely crowd out mainstream instruments. By way of comparison, the M3 money stock in the US currently exceeds $20 trillion, roughly four times the size of the stablecoin market even under Citi’s “bull case”.

Chart 3: Estimates of future development of the global stablecoin market.



Source: Citigroup (2025).

4. Can stablecoins serve well as money?

According to standard monetary theory, certain requirements must be met for a financial asset to function as money (Cecchetti, 2026).

The most important is general acceptance: to accept a given instrument as a means of payment, people must be confident that it will be accepted by others in the future.

General acceptance is a self-fulfilling process. The more people use a form of money, the more others will accept it because they know it can be readily passed on. “Network externalities” favor incumbents: a new form of money may struggle to be accepted initially, but at some point a virtuous circle sets in whereby it becomes increasingly popular. Many digital payment instruments widely used today – payment cards, smartphone applications, online platforms such as PayPal – have gone through such a cycle.

Could stablecoins be undergoing a similar process, temporarily constrained because they have not yet reached a critical threshold? This is unlikely. There are other inherent characteristics a good money must possess, without which widespread use is not possible. Three are most important.

The first is “singleness”, the property whereby every unit of money is equivalent to any other, so as to provide an unambiguous measure of value. Official currencies have that property because they are convertible without limit into central bank money at a fixed rate.

Bank deposits, routinely used as money, maintain a constant value by contractual arrangements, and transactions are eventually settled in central bank money. Deposit contracts guarantee

conversion in central bank money, supported by deposit insurance backed by the government. Stablecoin value, by contrast, is backed by asset holdings whose value and liquidity are uncertain. Stablecoin issuers promise redemption on demand, but possibly with limits and subject to fees, depending on the agreement and regulation.

Reserve-backed stablecoin prices normally stay close to parity, with only minor oscillations above and below. Significant oscillations below parity do occur, however, in stressed market situations, as shown for example by USDC, the stablecoin issued by CIRCLE, during the March 2023 US banking crisis. The extent of the fluctuations depends on the amount and quality of their reserves, the transparency of disclosures, the frequency of audits, etc. (Standard and Poor's, 2023). All these factors are likely to depend crucially on how stablecoins are regulated.

A second characteristic of a good monetary instrument is transferability: the ease with which it can be moved across space and time. To serve as a means of payment, money must be transferable and be a good (albeit temporary) store of value. Again, official currencies possess that characteristic, while for stablecoins this is more uncertain. Transfers on the blockchain are more costly, slower and more cumbersome than transfers on traditional channels. Absent a safety net comparable to that accorded to the banking sector, stablecoins are also a less-than-fully reliable store of value.

A third desirable feature of money, from a collective interest perspective, is its elasticity and controllability. Money is also an instrument of economic policy. This implies a trade-off. Supply must adapt, in part spontaneously, to the needs of the economy.

At the same time it must be manageable by the central bank for influencing economic developments. Traditional monetary institutions provide both such flexibility and controllability through established channels. For stablecoins, as currently regulated, this property is doubtful. Stablecoin supply is constrained by the availability of reserves and does not predictably respond to monetary policy impulses. In a world where stablecoins were dominant, the elasticity-controllability of money would be compromised.

Judged against the three criteria – singleness, transferability and flexibility – stablecoins still fare worse than the traditional circuits. However, this is an interim judgment which partly depends on regulation. Regulation is still being shaped and is likely to evolve depending on market developments.

Furthermore, different considerations may apply depending on the segment of the payment system considered: retail or wholesale, domestic versus cross-border payments.

Retail users engage predominantly in low-value frequent transactions. They value safety, simplicity, speed and low costs. In all these dimensions, today's conventional payment systems have reached standards that can hardly be matched. The traditional banking and fintech systems in Europe today offer online transactions free of charge, domestically and across borders, on a multi-currency basis. By contrast, blockchain transactions are still slow, cumbersome and costly. Stablecoins suffer an efficiency gap which can hardly be expected to be overcome in the foreseeable future.

The situation is different for wholesale cross-border transactions. Traditional wholesale circuits rely on inefficient correspondent banking relationships among internationally active banks. Oligopolistic

banking structures keep transaction costs high and limit incentives to increase service quality. Distributed ledgers may help remedy long-standing problems in the large-value international payment system. Centralized settlement is not available in international payments, absent a global central bank. This environment could benefit from permissioned distributed ledgers among internationally active banks, supporting large-value payments across multiple countries and currencies, with appropriate legal provisions and currency conversion arrangements.

Alternatively, a comparable degree of efficiency and even greater safety would be offered by a multicountry, interoperable network of CBDCs, connected by a distributed ledger. Central bank money would be placed on-chain, with DLT transactions among participating central banks and selected counterparties, ultimately settled on central bank balance sheets. This solution, reminiscent of the international clearing union proposed by J. M. Keynes (1942) but not requiring an ad hoc international organization, would combine DLT transactions with the safety of settlement in central bank money. While the idea sounds promising, it is unlikely to be feasible today due to the fragmented international environment and the lack of convergence among central banks on payment system reform.

5. Stablecoin regulation across the Atlantic

Crypto regulation has been advancing rapidly in recent years. The European Union was the first to act: its “Markets in Crypto-Assets” (MiCA) regulation has been in force since 2023, even though a market for euro-denominated stablecoins barely exists. The Bank of England, after consulting the UK financial industry, has issued proposals outlining future regulatory guidelines. In the US, the “Guiding and Establishing National Innovation for U.S. Stablecoins Act”, or “GENIUS” Act, was approved by Congress in 2025 and is scheduled to enter into force in 2027. Japan and Canada are working on similar timelines.

Table 1 compares MiCA, the GENIUS Act and the Bank of England proposals (similar comparisons can be found in van t’ Klooster et al., 2025, Scotti, 2025, and Cecchetti, 2026). Entries for MiCA in the table refer only to E-Money Tokens (EMTs), the instruments most similar to stablecoins; other instruments covered by the regulation, such as the Asset Referenced Tokens (ARTs) referenced to assets other than official currencies, are not included in the table.

Table 1: Comparison between MiCA, GENIUS Act and the prospective UK regulation

	European Union (MiCAR)	United States (Genius Act)	United Kingdom (Bank of England proposal)
Regulated instrument	E-money tokens (EMTs): crypto-asset pegged to an official currency	Payment stablecoins: digital assets used for payments	Systemic stablecoins: crypto assets used for payments
Authorized issuers	Licensed banks; electronic money institutions authorized by NCAs	Licensed banks; federal and state authorized issuers	Authorized issuers
Redemption	Unlimited at par, no fees allowed	Unlimited at par, fees allowed	Unlimited at par, fees possible if fair and transparent
Interest payments	Prohibited	Prohibited for issuers, possible for service providers	Prohibited; other rewards may be allowed
Significant issuers	Thresholds set by EBA to define significant issuers	10 bn. US$ threshold with exceptions	All systemic issuers treated equally regardless of size
Reserve requirements	30% in a segregated bank accounts; the rest in highly liquid instruments	Liquid instruments under third-party custody	At least 40% in unremunerated central bank deposits; up to 60% in short term government securities
Reserve disclosure	Significant issuers: monthly disclosure and audit every 6 months	Monthly disclosure	Disclosure requirements to be set by the FCA
Capital requirements	Significant issuers: 3% CET1 plus possible 40% add-ons; others: 2% CET1 plus possible 20% add-ons	Ad-hoc decision by federal or state regulator	CET1 based on international standards
Central bank credit	Only for licensed banks	Only for licensed banks	Available to all stablecoi issuers
Supervision	Significant issuers: EBA; others: NCA plus EBA last resort intervention	Federal (OCC) above 10mn US$ threshold; otherwise state	Bank of England and FCA
Holding limits	None	None	£20,000 for individuals and £10 million for businesses

Sources: European Union (2023), US Congress (2025) and Bank of England (2025).

All in all, the three frameworks appear to differ in their sensitivity to risk and regulatory orientation.

The European rules appear more concerned with protecting individual investors. Redeemability at par must be guaranteed at all times, without limit or charge to the investor. Redemption fees are prohibited – by contrast, neither the GENIUS Act nor the UK proposed guidelines prohibit redemption fees as a matter of principle. Fees are critical for slowing down redemptions in times of stress, hence protecting financial stability and limiting contagion. However, they constrain individual holders who try to recover their investment.

Of the three, the GENIUS Act stands out for adopting the most decentralized and executive-dependent supervisory structure. A significant role is given to state supervisors and to the OCC. Reserves are required to be liquid; a general requirement, which leaves ample room for stablecoins to be backed by Treasury bills. By contrast, MiCA requires at least 30% of collateral to be deposited at licensed banks and the Bank of England sets a minimum of 40% to be deposited with the central bank. The stance of the GENIUS Act is relatively favorable to the Treasury, both as issuer of admissible collateral and as a regulator.

The UK framework is the most consistent with making stablecoins reliable means of payment. The key feature is the requirement that at least 40% of reserves be held in unremunerated central bank deposits. This effectively covers major redemptions, thereby avoiding knock-on effects on the rest of the financial system. Another important feature is that all stablecoin issuers can receive central bank credit, a benefit MiCA and the GENIUS Act reserve exclusively for licensed banks. Supervision is with the Bank of England (FCA for conduct issues), consistent with the existence of a lender of last resort.

MiCA is the only one requiring issuers to hold reserves with the banking sector. This has both advantages and disadvantages. On the one hand, it protects banks from disintermediation; for every euro lost to banks in favor of stablecoins, 30 cents must be redeposited with the banking sector. On the other hand, this requirement creates a structural link between stablecoins and banks that may lead to contagion in case of loss of confidence in stablecoins. The Bank of England requirement that funds be deposited with the central bank seems safer from a systemic stability perspective.

All three regulations impose capital requirements. Here again the GENIUS Act is more flexible, allowing for supervisory discretion, while MiCA prescribes specific ratios in terms of high-quality capital (CET1) and the UK, still requiring high-quality capital (CET1), aligns with global standards.

MiCA requires that no interest be paid, another element which protects banks from disintermediation. The GENIUS Act prohibits interest payments by issuers, but not by service providers. The latter can bypass the ban by entering into agreements with issuers and be compensated for interest payments. In the UK, the interest ban on issuers is foreseen but it can be mitigated in other forms of reward.

The UK provides for a comparatively simple and solid supervisory framework: all supervision is concentrated in the Bank of England. In the EU, issuers are supervised by the European Banking Authority. When the issuer is a bank, this means that the same intermediary would have two supervisors under its roof, for different activities, a possible complication. In the US, supervision is fragmented between federal and state authorities, depending on the $10 billion threshold. The explicit admission of “exceptions” to this criterion makes the demarcation potentially blurred.

6. Political support for stablecoins: influences and implications

As noted earlier, some signs from the US administration make it reasonable to suggest that political support for stablecoins may be part of a strategy to extend executive control over areas traditionally delegated to the central bank, such as payment system oversight and monetary policy. Here we discuss possible influences behind such a design and some consequences. The focus is on the US, though the dynamics described may have broader implications.

Four sources of influence, political and economic, seem relevant.

One comes from the legal doctrine known as the unitary executive theory, a judicial interpretation according to which executive power rests solely with the President and cannot be shared with other parts of the government.

The unitary executive concept finds support in the letter of the US Constitution but sits uneasily with the powers the Constitution itself assigns to Congress, in particular Art. 1, which assigns to the latter the power "to coin money and to regulate the value thereof". Based on this article, Congress in 1980 made the Fed independent in conducting monetary policy. Controversial among legal scholars, the unitary executive concept partly depends on how one defines an executive act. A strict reading implies that any decision producing an effect is executive, and hence belongs to the President. Such an interpretation, however, not only undermines central bank independence but contradicts the aforementioned Art. 1.

A second influence is political realism, a notion that sees political interactions as driven by self-interest and leadership by the most powerful actors. Political realism is incompatible with norms derived from consensus or democratic processes to which all political actors are subject. It is also incompatible with checks and balances, because an orderly interplay of balanced powers requires those norms. A government agenda marked by political realism stresses competition and conflict at the expense of cooperation, and regards negotiation and compromise as signs of weakness. Often applied to international relations, political realism is also relevant to domestic affairs.

The more these two notions take hold, the more they are likely to lead to regulatory capture. Superficially, it seems that an all-encompassing, discretionary executive, unchecked by norms, should be strongest against all counterparties. In practice, the opposite is likely to be true. The absence of principled, transparent, and commonly accepted rules makes it more difficult for public administrators to resist vested interests.

Weaker norms encourage administrative styles marked by transactional governance, crony capitalism, erratic decision-making, even kleptocracy. Likely victims are free and competitive markets, equal treatment, and transparency, replaced by opaqueness, conflict of interest, corruption and political favouritism.

Cronyism includes family capitalism, using government-derived influence to help family businesses and pressuring business leaders for donations and favours. This corrupts the economic fabric, eroding trust in the fairness of market mechanisms, official regulation and the judiciary behind it.

Another influence on the economic side comes from public debt constraints. Public debts have been rising almost everywhere in the world in recent years, with the US increasingly leading the way. Close to 50% of GDP at the turn of the century, the US federal debt now surpasses 120% and is expected to keep rising under all plausible assumptions.

The need to finance the public debt influences monetary and financial policies, encouraging financial repression (measures limiting capital mobility and encouraging or coercing investment in sovereign debt), limiting central bank independence, and complicating the pursuit of price stability. Fiscal constraints encourage the development of financial instruments that help fund the public debt, often at the expense of an efficient allocation of savings.

Monetary and payment system institutions are prime candidates to be impacted, and the consequences can be significant. Long-standing arrangements crucial for the stability and resilience of the financial system are endangered. Let us see how in some detail.

For the last half century, from the rise of global financial markets in the mid-1970s to now, monetary systems in Western democracies have rested on a few trusted pillars. Monetary transactions settle on bank accounts and, indirectly, on central bank balance sheets, where banks hold liquid reserves and settle their balances. To conduct monetary policy, central banks manage the supply and cost of those balances by means of transactions in which currency is exchanged for securities. In conducting open market operations, central banks are independent from the executive within boundaries set by their statutes. The effectiveness of this control mechanism depends on the central bank's monopoly provision of the ultimate settlement asset, central bank money.

Central bank cooperation extends the benefits of these arrangements, in terms of price and financial stability, at the international level. One example of how such cooperation is the currency swap arrangements put in place by central banks in times of crisis, which proved essential to preserve financial stability during the 2008 financial crisis.

Central bank cooperation does not depend on political relations. Central banks do not consult with their political masters before undertaking such actions, let alone seek authorization (this would be against their mandate). Central bank cooperation can even occur in opposition to executives; a recent example was the expression of support provided by global central bankers to Fed Chairman Powell when subjected to criminal investigation.

These examples illustrate the influence independently exercised, in each jurisdiction and collectively, by the community of central banks. Occasionally criticized as "unelected power", such initiatives, if consistent with their statutes, help make the financial system safe and resilient and are one of the "checks and balances" on which well-functioning democratic systems rest.

The digitalization of money has not fundamentally upset these arrangements so far. Since the 1990s, some 90% of global monetary assets are digital – mainly consisting of balances deposited in centralized ledgers of banks and other financial institutions. Payment cards, online commerce, smartphone applications, and digital wallets have not altered the payment system architecture except on the surface. All payments, retail and wholesale, domestic or international, continue to settle largely on bank accounts, and eventually on central bank balance sheets. The ability of central banks to exercise payment oversight and monetary control is unaffected.

Stablecoins are qualitatively different. They are ultimately settled outside central bank accounts, and their creation is not subject to the instruments and channels of control available to central banks. They are private money, issued by private entities (licensed stablecoin issuers), without linkage to central bank money. Moreover, US regulation largely frees stablecoins from central bank oversight, placing them under the purview of authorities with weaker statutory independence.

The consequences for monetary and financial stability are potentially serious. Under pressure from a unitary executive tainted by political realism, the central bank loses levers and authority to exercise effective independent monetary control, and with them influence and credibility. Under executive power, policy goals tend to be less clearly defined, politically influenced and subject to partisan cycles. A subordinate central bank is also less likely to cooperate internationally. To return to the example of currency swaps: a unitary executive may limit or outright ban such operations, with adverse implications for financial stability.

Large public debts compound the problem. Arm-twisting the central bank to conduct non-monetary-policy-related asset purchases is an obvious way to receive cheaper financing. But there are also other, indirect ways to achieve that result, to which stablecoins are instrumental. Collateralized stablecoins need to be backed, and Treasury paper fits that purpose. As asset holders shift into stablecoins, the demand for Treasury paper is likely to increase, helping finance the public debt. Short-term bills are usually traded in liquid markets, hence they can be easily sold in case of stablecoin redemption.

The recent movement by the US Treasury towards short-term financing makes stablecoins more suitable for financing the public debt.

A future scenario with a rise in private monies, shortening of public debt maturities, erosion of central bank independence, combining an erosion of the rule of law with loss of regulatory integrity and certainty, would all be signs that the US is moving toward a regime of “fiscal dominance”. Over time, this would likely have negative implications for the value of the dollar and erode its status as an international currency.

7. The European response

Often insufficiently acknowledged, Europe today has a highly efficient and user-friendly payment system, in many ways state of the art by international standards. In the retail segment, European consumers transact online, on an overnight or instant basis, free of charge, domestically and across borders, within the 21 countries using the euro, by means of online banking applications. The same facilities are available on handheld devices, though the latter typically rely on software designed by large US tech companies. The euro’s retail payment system has operated successfully for many years, consistently demonstrating high standards of reliability and resilience.

In the wholesale segment, TARGET, in its successive versions and developments, though not without scope for improvement, constitutes a solid infrastructure supporting both money market transactions and central bank monetary policy operations.

As global innovation and competition heat up, the question for Europe is how to build and further improve upon this already partially successful status quo.

In the crypto space, the EU has moved preemptively – some may say prematurely – on the regulatory side, introducing regulation on asset-referenced tokens, including stablecoins, already in 2023. Regulating a market that still does not exist risks biasing its development, even stifling it. That said, MiCA regulation contains useful elements, alongside others that, as discussed in section 4, may be reconsidered in future reviews. Adaptations of MiCA should be informed by market developments and experience in other, more advanced jurisdictions.

The ECB strategy on payment systems proceeds along two tracks.

In the retail segment, the central bank for many years now has pinned its strategy on the digital euro, a central bank digital currency offered to all citizens, in small amounts, for low-value transactions, settled directly on its books in central bank money. The actual launch date is still to be decided; the ECB envisages it potentially by 2029. Whether this application would add value and be well received in a market already overcrowded by private applications offering essentially the same service is an open and hotly debated question.

In the wholesale segment, the ECB has recently announced two new projects: Pontes, placing interbank and central bank transactions in central bank money on-chain; and Appia, essentially an extension of Pontes covering a broader range of financial market transactions, still with settlement in central bank money. Pontes and Appia are interesting concepts, the first being short-term and concrete, the second more ambitious and uncertain. Both imply a shift from the notion underlying the digital euro, providing a payment instrument to retailers, to building an infrastructure for wholesalers.

The future of Europe's payment systems is open and the opportunities are significant. What is needed is pragmatism and a firm focus on Europe's overriding priorities: strengthening competitiveness and upholding monetary sovereignty. Success on both fronts may also increase the attractiveness of the euro internationally.

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