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# What does the future hold for the Libra?

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Last May, Facebook officially announced its intention to launch Libra, an institutional crypto currency aimed at facilitating payments on the marketplaces of a certain number of websites affiliated with Facebook and its partners. The list of the Libra Association members, involved with the launch of the crypto currency, is impressive and demonstrates how serious this project is. It includes technology groups, notably marketplace websites such as Facebook, Booking, eBay, Uber, Spotify, etc.; or groups involved with Blockchain such as Coinbase, Anchorage, etc.; mobile telecom groups, such as Vodafone or Iliad; several venture capital groups; a few NGOs like Women's World Banking, Mercy Corps, etc. and finally and most importantly, major players in the payment industry: MasterCard, Visa, etc.

Will Libra be the first success of the libertarian ideology which backed the crypto-currency launch, and which ambitioned to create an alternative to State currencies? Will the institutional frame of this crypto currency be sufficient to ensure its success? Governments have been quick to express their scepticism towards this project, in a more or less vivid manner. To the extent that Paypal already announced its withdrawal from the project and that other Association members are pondering whether to distance themselves from the project. The debate is open. Stakes are huge. Without claiming to own a crystal ball, let's try and be more specific about them.

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The first crypto-currencies Bitcoin, Ethereum, etc. have met with real success: The Bitcoin market capitalization, total numbers of Bitcoins in circulation multiplied by the Bitcoin price, is estimated at \$205 billion, as of 2019 first quarter[1]. However, these crypto currencies have not demonstrated their usage as a traditional payment vehicle and are strongly suspected to be primarily used for speculation (on their own prices), laundering of criminal activities (ransomware and various trafficking activities) or tax evasion. The technology of these crypto currencies is "blockchain", a strange and complex technology, which validates and authenticates individual transactions through multiple confirmations of the IT block chains

which digitally define these transactions, through a network of independent computers. That network is open: any computer with available computation time can participate in this process. The transactions' anonymity and security are structurally built by this system.

Even stranger is how the crypto-currency is created: via a "mining" process. Computers which create this currency do it using computation time to solve ever more complex algorithms, therefore using ever increasing computation time. Not to mention the ethical question behind it – what is the justification for owners of these computers to be freely given crypto currencies? – the mining process uses considerable resources globally (computation time and IT infrastructures), consuming energy at a macro-economically significant level. As a result, the location of mining infrastructures is optimized to reduce the energy cost incurred. In Iceland, HS Orka, the local energy company, estimates the yearly consumption of electricity for currency mining purposes in the country at 840 gigawatts hour/ electricity, vs 700 gigawatts consumed by all country households[2].

The system is, by design, infallible, but the crypto currencies have fallen victim to numerous frauds, principally due to the poor ethical standards of some of its players: crypto currency brokers and depositaries mainly; as well as some computer bugs (?) which witnessed the disappearance of

1. Statista 2019. Statista is a German commercial markets data analysis company, owned by the Stroer group, German "out of home media" specialist, with circa \$ 4 billion market cap.

2. Interview of M Sigurbergsson, HS Orka, BBC News, Feb 12, 2018.

stacks of money. It should also be noted that the system's international dimension seems to be preventing any regulatory response to the various known system malfunctions.

Libra is however not designed under the Blockchain technology, at least not as it was originally intended. The Libra rate will not be freely floating, but pegged on a currency basket (50% US\$, 18% €, 14% ¥, 11% £, 7% Singapore \$[3]). As such, Libra is a "stablecoin", whose rate does not fluctuate in an intrinsic, hence erratic manner. Furthermore, Libra will not be created through a mining process, but will apparently be backed by a stock of monetary assets[4] owned by the entities authorized to process the Libra. The authenticators' network will not be open (at least at first [5]) but will be limited to the IT infrastructures owned by these authorized players.

Unsurprisingly, the public authorities' reactions are very negative. Let's specify the issues they have with Libra.

First, the system is built anonymously thereby facilitating crime, including the financing of terrorism. The project's founders have perfectly understood the issue since its inception and have indicated their commitment to making the crypto currency compliant with all regulations that the different jurisdictions will in all likelihood put in place. Will this imply restrictions in terms of transactions and owner anonymity? Most likely. But the stakes are higher. Like barter or cash, the use of crypto currencies, even if they are relatively non-anonymous, facilitates tax evasion (VAT non-payment, income dissimulation, etc.). The idea of a sanctioned crypto currency is especially iconoclastic in the countries that target complete control of payment transactions – notably through the progressive elimination of cash: prohibition of cash transactions above a certain threshold, elimination of large denomination bills, the digitisation of transactions – and drastically enhanced tax audits means, including fiscal laws with exemptions from common law, multiplication

of fiscal police departments, use of artificial intelligence to analyse semi-public individual data, etc. It does not therefore come as a surprise that France is particularly vocal in the matter. Bruno Le Maire, Minister for the Economy and Finances, for instance, declared that "*Libra is a danger for consumers and presents a systemic risk as well as a threat for France itself.*"[6] Furthermore, if the crypto currency were to allow credit transactions, which seems unavoidable even if the crypto currency founders indicate their opposition to it, it would raise monetary creation issues, implying inflation issues.

But the authorities do not respond unanimously. Although France, Germany[7] and India[8] reject the project globally, others limit their objections to demanding efficient and exhaustive regulations in terms of anti-laundering, the financing of terrorism, tax evasion, consumer protection, monetary policy, while expressing their doubts that Facebook and the crypto currency developers would be able to introduce a satisfactory framework. Not only is such an exercise difficult, but Facebook's reputation in terms of data security, user privacy and algorithm manipulation does nothing to reassure the authorities. The United States are particularly firm in their comments and have asked Facebook to suspend the development of Libra[9] or obtain a banking charter and agree to submit to all banking regulations[10]. The United Kingdom, according to the governor of the Bank of England, Mark Carney, has shown some pragmatism, declaring itself open to the crypto currency, but uncompromising with respect to its regulation[11]. Japan, according to Haruhiko Kuroda, governor of the Bank of Japan, has underlined the importance of having global coordinated regulations to regulate Libra and other crypto currencies[12]. He notably asked that political leaders ensure that the highest level of regulation applies to this type of asset. On the other hand, Switzerland, through one of the members of its Central bank advisory council, appears to have declared itself crypto currency friendly. The Swiss regulator (Finma) however, appears to disagree[13].

3. Facebook announcement, Sep 2019.
4. 100% backed? If not, "bank run and monetary creation issues will emerge as well."
5. Facebook appears to believe that today there is no technical solution which would make it possible to "deliver the scale, stability and security required to support billions of users and transactions across the world using a "permissionless network". Source: Libra White Paper 2019, on Libra.org.
6. Sep 13 2019 speech at the OECD Global Blockchain Policy Forum 2019.
7. Statement by Olaf Scholz, German Vice Chancellor and Minister of Finances: "We cannot accept a parallel currency. You have to reject that clearly. The Federal government will work at European and International level to ensure that stablecoins will not become an alternative to official currencies". Reuters Sep 17, 2019.
8. Subhash Gard, Indian Minister for economic Affairs: "the design of the Facebook currency has not been fully explained, but whatever it is, it would be a private cryptocurrency and that's not something we have been comfortable with." Bloomberg, July 2019.
9. Maxine Waters, President of the United States House Committee on Financial Services, Source: CNET.com, June 2019.
10. Donald Trump tweet, July 12, 2019, as reported by the Financial Times.
11. "The Bank of England approaches Libra with an open mind but not an open door. Unlike social media, the terms of engagement for innovations such as Libra must be adopted in advance of any launch." Pymnts.com, Sep 24, 2019.
12. Sep 23, 2019 conference, as reported by Reuters on Sep 24.
13. Coindesk.com, Sep 10, 2019. purchase of the steelworks of Smederovo and the creation of a tyre factory in Serbia.

Public objections are not the only difficulties that will impede the development of Libra. Implicit foreign exchange risk is, in my opinion, more problematic. Indeed, the constitution of a basket of currencies on which Libra will be pegged will reduce this risk, but it won't suppress it; notably in the non-US\$ jurisdictions, given the foreseen weight of the US\$ in the basket. This risk will remain significant, and incidents will happen. If one intends Libra to be used as a legitimate currency, beyond the current marginal uses of existing crypto currencies, households need to use it to make purchases. This is one of the currency's initial objectives which is meant to be used for purchases on the founder's merchant sites. But then, how will these households procure their Libras? Will they buy a stock that they will use progressively at the rhythm of their purchases? But then, during the period, that they own these Libras, these may lose value. Or else, will they buy Libras prior to any purchase? This will imply multiple transactions on small amounts, which is likely to lead to high Libra purchase costs. Incidentally, what about the purchase cost of Libras, the implicit foreign exchange rate? One can reasonably assume that, consistent with the practices of new economy companies, the purchase cost or FX spread, will be very low; these companies have indeed the habit of subsidizing the client acquisition process, sometimes to the cost of considerable losses, acceptable because of considerable amounts raised with devoted investors, fascinated by the new economy and in a desperate quest for yield, in a macro-economic context of low or negative rates and quantitative easing (QE). But, in time, the cost, the spread, will have to become economically sensible. It is also hard to imagine that Libra brokers provide hedging mechanisms to their clients, which would be very costly to them. The only efficient hedging approach, which would allow for the development of Libra in line with the founder's expectations, is what multinational groups call congruence: ensuring that revenues in each currency match the expenditure in that currency, i.e.: ensuring that salaries, as well as entrepreneurs and farmers'

income, are partially paid in Libras. Which seems quite complicated and unlikely to be imminent.

If the use of Libras for marginal activities is rendered difficult through rigorous regulation, professionally enforced within numerous national jurisdictions, if the use of Libras by households is rendered difficult by FX risk and costs, how will Libra grow? There is an initial lead. One can imagine that, , Libra could become a reserve currency even more so than the US dollar and the preferred payment for households in economies in which the currency is notoriously deficient, because of high inflation rates or restrictive foreign exchange controls (the best example being Zimbabwe, which forfeited the use of its national currency for 10 years and which is now trying to relaunch a Zimbabwean dollar[14]); or because of insufficient payment systems; or because the international currency exchanges are significant (personal remittances by immigrants toward their families, cross border purchases by frontier workers, etc.). The World Bank estimates that these personal remittances towards low to middle income countries, totalled \$ 529 billion in 2018[15]. The cost of these transfers is often huge: Western Union commissions, for instance, can represent up to 10% of the transferred amounts, in sub-Sahara countries notably. Of course, the relevant governments, as intended by India, will take restrictive measures, their sovereignty coming under an even greater challenge than that in developed countries. But one might suppose that, no more than Western governments, those in developing countries will not manage to prevent the use of these new crypto currencies. In the emerging countries, the need is real and compelling.

So, what does the future hold for the Libra? The instrument is profoundly disruptive, stakes are considerable, even involving challenges to some States' sovereignty. But the needs and the appetite on the part of many users will create a tidal wave. If current crypto currencies, which are fundamentally problematic, met with significant

14. BBC News: Editorial by Andile Masuku, July 7, 2019.  
15. Barron's July 11, 2019, The Street, June 23, 2019.

success, it is hard to imagine that current public response will be sufficient to kill off a Darwinian evolution of our societies such as this. This evolution will not be seamless; political, technical, cybercriminal, and fraudulent events will be numerous. But Libra or its successors, will most certainly be amongst the major evolutions of the

21st century, in an increasingly Schumpeterian world.

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