



# THE CASE FOR STRINGENT REGULATIONS OF STABLECOINS



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### THE CASE FOR STRINGENT REGULATIONS OF STABLECOINS

By David S. Evans

Decisions on how to regulate stablecoins, and other parts of the crypto industry, should be based on what we know about crypto's past and present and discount starry-eyed forecasts of its future. The past demonstrates public blockchains cryptocurrencies are highly volatile; main blockchains have no mechanisms for ensuring stability; and that after 13 years there are unfulfilled promises and no widespread use of cryptocurrencies for productive purposes. The present shows that speculation is the main use case for currencies with the leading exchanges investing in feeding hype with celebrity-studded ads among other things. Crypto exchanges and other participants with a stake in the continued trading of currencies are now selling the "vision thing": a vague and distant future of a decentralized internet and financial system. Now we also have hard evidence that lax regulations of stablecoins, combined with the inherent volatility of the native cryptocurrencies have resulted in the classic systemic financial risks from runs and contagion. This article advocates for stringent regulation of stablecoins: fully backed with cash and short-term instruments, with a trustee, and in a regulated bank. It also argues for regulators going further to ensure stablecoins are not used to support unsafe applications.

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# 01

## INTRODUCTION

Fortunately, despite all the hype, cryptocurrencies are a small part of the financial system.<sup>2</sup> At the peak value in October 2021 the market cap of crypto was about \$2.7 trillion.<sup>3</sup> The total value of physical money (“M0”) was about \$40 trillion that year and the broader money supply (“M3”) was about \$90 trillion.<sup>4</sup> And crypto is largely confined to its own ecosystem.

Thus, when the prices of cryptocurrencies plunged, a large stablecoin issuer collapsed in early May 2022, and crypto investors started pulling funds in classic runs, nothing happened to the traditional financial system. There was no material contagion. The crypto world became a case study, however, of what can go wrong in the absence of the banking-type supervision. The answer, which we’ve known for better than a century, is just about everything.

There is now increased interest in regulating crypto in case it gets so big and intertwined with our financial system that it does pose systemic risk to the economy.<sup>5</sup> This article explores striking the balance between regulation and innovation by focusing on a key part of the crypto business — stablecoins — and drawing some comparisons with an almost contemporaneous money innovation, mobile money. It concludes there should be stringent regulation of stablecoins but not an outright ban at this point in time.

# 02

## STABLECOINS AND THE HOT POTATO PROBLEM

Stablecoins show how far crypto has come from its early promises. Cryptocurrencies were supposed to replace fiat currencies. This was just not possible because bitcoin and the other currencies are inherently unstable and cannot function as money. There is no mechanism — human or algorithmic — for ensuring that the major cryptocurrencies have stable value, and they don’t. Between 2012 and 2021, for example, the average annual volatility of bitcoin was 16 times higher than the dollar.<sup>6</sup> Crypto prices tend to move in tandem and high volatility is endemic.

As a payment method, crypto is a hot potato. Gambling aside, businesses don’t want to be paid with currency that could plummet in value. An early example of this involved Ross Ulbricht, the founder of Silk Road, who negotiated a contract for a hitman on the dark web. He paid the hitman, who was an undercover agent, \$90,000 in bitcoin but pledged to send more if the bitcoin price tanked.<sup>7</sup> Today, wallet providers that enable consumers to pay merchants with crypto solve the hot potato problem by almost immediately converting the crypto that the consumer has paid to fiat currency. El Salvador’s experiment in making bitcoin a national currency has failed largely because of the hot potato problem. Businesses and people avoid it since they cannot manage their budgets with it.

Crypto volatility even made it risky to trade cryptos for other cryptos or with fiat. The prices were volatile even in short windows. The volatility also made it problematic to develop financial services applications on the public blockchain. Ethereum was supposed to be a platform for smart contracts with decentralized finance the main use case. There is little appetite for contracts, particu-

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2 For the purposes of this paper, I use the term “cryptocurrencies” to refer to the crypto currency native to public blockchains (such as ether for Ethereum) and not to stablecoins. I use the shorthand “crypto” to refer to the public blockchains and related entities.

3 ConDesk, “Crypto Market Cap Surges to Record \$2.7T,” October 21, 2021. <https://www.coindesk.com/markets/2021/10/21/crypto-market-cap-surges-to-new-record-27-trillion/>.

4 Go BankingRates, “How Much Money Is In the World Right Now,” June 8, 2022. <https://www.gobankingrates.com/money/economy/how-much-money-is-in-the-world/>.

5 Kim shows that cryptocurrencies and traditional financial markets are linked through stablecoins which lead to fluctuations in the demand for commercial paper and this could pose systemic risks absent regulation if stablecoins became a larger part of the financial system. Sang Rae Kim, “How the Cryptocurrency Market is Connected to the Financial Market,” May 7, 2022. At <https://ssrn.com/abstract=4106815>.

6 David S. Evans, “Can Crypto Fix Itself in Time,” *CPI TechREG Chronicle*, February 2022. At [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4031977](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4031977).

7 PYMNTS, “The Alleged Bitcoin Silk Road Hitman Operation,” February 6, 2015. At <https://www.pymnts.com/in-depth/2015/the-alleged-bitcoin-silk-road-hitman-operation/>.

larly long-term ones, when the money involved has highly uncertain value.

Stablecoins were the solution to these problems. They are tokens typically relying on Ethereum's ERC-20 protocol but usable across other public blockchains. As of July 16, 2022 Tether's USDT, Circle's USDC, and Binance's BUSD accounted for 90.6 percent of the market cap of stablecoins. As the initials suggest they are all pegged to US\$1.00. Each of the sponsors claims to keep full liquid dollar-denominated collateral (such as cash and short-term treasuries) for their stablecoins. Terra's Luna stablecoin, which collapsed following a classic run, was pegged to the U.S. dollar but relied on algorithmic trading to maintain the peg.

Stablecoins do not replace the native cryptocurrencies for the public blockchains. Those public ledgers are recording transactions in their native currencies. Transaction processing is based on incentive schemes — whether proof of work or proof of stake — tied to those native currencies. In fact, Terra's collapse was precipitated by massive rapid decline in the value of cryptocurrencies — by about half in the roughly six months from their November 2021 peak to the when Luna started deviating from the peg in early May 2022. Then the well-known knock-on effects of the resulting runs led to crypto currencies plummeting further. Stablecoins can alleviate the hot potato problem in exchange but not the fundamental crypto volatility problem.

Regulators are looking at how to balance systemic risk versus systemic innovation in considering regulations and have a heightened concern over stablecoins following what looks like classic bank runs and financial contagion. In considering that, a trip to Kenya is helpful.

## 03

### M-PESA AND THE REGULATION OF MOBILE MONEY

In many lower and middle-income countries people can load money onto a mobile phone, often paying cash at agents (typically small shops), and send that money to other

people, who take cash out at agents. Increasingly, mobile money stays in the system as it is used to pay for goods and services directly rather than being converted to cash. The mobile money platforms support other financial services such as saving and borrowing.

As of 2021, according to GMSA, 98 countries had live mobile money deployments, there were 1.35 billion accounts of which 518 million had been active in last 90 days, and around \$1 trillion was processed that year by mobile money schemes. That's a lot of money since many of the people are dirt poor. About half of the users in are in Sub-Saharan Africa.<sup>8</sup> There, mobile money brought banking and other financial services to large portions of the population, particularly the poor, and those living outside urban centers.

Decisions on how to regulate mobile money have important effects on the success of mobile money schemes — whether they take hold at all and how rapidly they grow. Key considerations concern the role of banks in mobile money schemes and the extent to which traditional banking regulation should apply to the new schemes. Some countries decided to insist that banks take the lead role in operating new schemes or imposed burdensome KYC and agent regulations. Banks lobbied for policies since they viewed the new schemes as competitors. Other countries adopted light regulations and a wait-and-see approach as the schemes evolved.

My paper with Alexis Pirchio studied the first wave of mobile money schemes from the mid 2000s to 2014.<sup>9</sup> In practice, the choice was between lightly regulated schemes operated by mobile carriers, or heavily regulated schemes with significant bank involvement. We found that all the successful ones (there were eight) had light regulatory regimes — they didn't have to be run by banks and the other restrictions were not onerous. Almost all the ones that failed (seven of eight) had heavy regulatory regimes that required that banks take the lead role in the scheme or had heavy KYC and agent regulations.

The launch and regulation of M-PESA, which established the pioneering and most successful mobile money scheme illustrates the issues. In 2005, Safaricom, the dominant mobile carrier in Kenya, together with Vodafone Group and the Commercial Bank of Africa, asked the Central Bank of Kenya ("CBK") to authorize what became M-PESA. The CBK could have just denied the application. But, as a study sponsored by the Gates Foundation noted, the CBK chose to "navigate the necessary risks to find a regulatory solution that would foster greater financial inclusion."<sup>10</sup>

8 GMSA, *State of the Industry Report on Mobile Money*, 2022. At [https://www.gsma.com/sotir/wp-content/uploads/2022/03/GSMA\\_State\\_of\\_the\\_Industry\\_2022\\_English.pdf](https://www.gsma.com/sotir/wp-content/uploads/2022/03/GSMA_State_of_the_Industry_2022_English.pdf).

9 David S. Evans & Alexis Pirchio, "An Empirical Examination of Why Mobile Schemes Ignite in Some Developing Countries but Flounder in Most," *Review of Network Economics*, 2014, vol. 13, issue 4, 397-451. At [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2578312](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2578312).

10 Brian Muthiora, *Enabling Mobile Money Policies in Kenya: Fostering a Digital Financial Revolution*, GMSA, January 2015. [https://www.gsma.com/mobilefordevelopment/wp-content/uploads/2015/02/2015\\_MMU\\_Enabling-Mobile-Money-Policies-in-Kenya.pdf](https://www.gsma.com/mobilefordevelopment/wp-content/uploads/2015/02/2015_MMU_Enabling-Mobile-Money-Policies-in-Kenya.pdf) p. 9.

# 04

## REGULATION, INNOVATION, AND RISK

The CBK insisted that mobile money exchange at par with fiat and that the consumer retain ownership in that mobile money. When a consumer gave 100 Kenyan shillings (“KES”) to an agent to put mobile money on their SIM card, the value of the mobile money on the SIM card was pegged at 100 KES. That money belonged to the consumer and not M-PESA or the agent. M-PESA and the agent could not, like a bank, lend or invest those deposits. The mobile money was extinguished when it was converted back into cash by an agent. The cash backing the mobile money went into a trust under the custody of a trustee and deposited into a bank. Safaricom and its partners had no access to these funds. In February 2007 the CBK authorized the launch of M-PESA, which happened in a few days, but put M-PESA into a sandbox where the CBK oversaw the mobile money scheme while considering a complete regulatory framework.<sup>11</sup>

M-PESA grew quickly in part because it met an enormous need in Kenya.<sup>12</sup> There were few banks. Family members often left villages for the cities to earn money which they wanted to get back to relatives back home. The countryside was dangerous, at the time torn by civil war. M-PESA was an alternative to giving cash to drivers and hoping it would make successful journey to its intended recipient. There were 5 million registered users by April 2009, among about 39.6 million adults, and 25 million registered users by February 2015. As a share of GDP, M-PESA transactions increased from 7 percent in 2008 to 45 percent in 2014. As of 2022 most adults in Kenya use M-PESA. It has expanded from money transmittal to bill payment, credit and savings, and paying at merchants.<sup>13</sup>

Not surprisingly, as M-PESA use exploded after 2007, Kenyan banks were unhappy. They lobbied the government to shut it down on the grounds that it would cause a financial crisis. A Kenyan newspaper reported that the banks approach the Minister of Finance and claimed that M-PESA was “similar to a ‘pyramid scheme’ and that ‘people could lose their money if it collapsed.’”<sup>14</sup> The bank lobbying ultimately failed in Kenya. Other countries were not as lucky, as Pirchio and I showed.

Without sound regulation, however, the bankers might have been proved right. M-PESA eventually became the main financial system for Kenya. People trusted it to put their money. And eventually to borrow and invest money. A large number of agents — small shop owners — in Kenya trusted it too. They had to keep funds on hand to redeem mobile money. Merchants also took mobile money payment. A lot could go wrong here in the usual ways for banking systems. There could be runs, contagion effects, waves of personal and business bankruptcies, dragging the economy down into recession or worse.

The CBK recognized all this. It had to make a tradeoff between heavier regulation that could reduce these risks but also dampen, if not kill, innovation and lighter regulation that could promote innovation but pose some risks. It could have put more trust in Safaricom and let it hold on to the funds and even invest them like a bank. After all, Safaricom was a large regulated mobile carrier, not a start-up. Alternatively, it could also have concluded that mobile money schemes should be reserved for banks. It had to strike the balance in the face of great uncertainty, with the risks and costs in both directions.<sup>15</sup>

M-PESA, and the experience of mobile money schemes, highlights three important points for regulators. First, it is better to nurture innovation even if it could be harmful. It is hard to know for sure just how important innovation could be to an economy. Second, it makes sense to retain flexibility in the face of uncertainty. If regulation can kill an innovation it is better to take a lighter touch at first until the risks and rewards are better known. That is the premise behind the use of regulatory sandboxes. Third, it is important to guard against incumbents seeking to use regulation to preserve their own rents, and to be skeptical of claims that innovation will lead to the end of the world.

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11 *Id.*

12 David S. Evans & Richard Schmalensee, *Matchmakers: The New Economics of Multisided Platforms* (Cambridge, MA: Harvard Business Review Press, 2016).

13 See <https://www.safaricom.co.ke/personal/m-pesa/m-pesa-home>.

14 Mwangi S. Kimenyi, “Mobile Wars and Political Barriers to Entry: Safaricom vs. Equity Bank,” Brookings, October 29, 2014. At <https://www.brookings.edu/blog/africa-in-focus/2014/10/29/mobile-wars-and-political-barriers-to-entry-safaricom-vs-equity-bank/>.

15 Decision theory, which is the basis for error-cost analysis, provides the analytic framework for this sort of problem. For an introduction in the context of antitrust see David S. Evans, “Why Different Jurisdictions Do Not (and Should Not) Adopt the Same Antitrust Rules,” *Chicago Journal of International Law*, Vol. 10, No. 1. At <https://chicagounbound.uchicago.edu/cjil/vol10/iss1/9/>.

Regulators, however, also need to avoid reasoning by analogy. Striking that balance is a fact-dependent, context-specific, exercise. There may be cases where initiatives should be stopped dead cold or ruled with a heavy hand. That light regulation was the right solution for mobile money, particularly as done in Kenya, doesn't mean that it is for other different initiatives, in different situations, elsewhere.<sup>16</sup>

# 05

## SELLING CRYPTO'S FUTURE

The current consideration of regulation for stablecoins and other aspects of crypto occurs in a vastly different environment than mobile money, FinTechs, or many other new financial services innovations. Bitcoin launched more than 13 years ago. We've had the chance to learn a lot about public blockchains and their cryptocurrencies

As the Silk Road example illustrates, in bitcoin's first few years, its main use case was for illegal trading activity that took place on the dark web. The convenience of using a difficult to trace digital currency — rather than say credit cards — was worth the price of bearing the volatility. It still is. Bitcoin is the currency of choice for the cybercriminals behind ransomware. When I first starting writing about crypto, in 2014, hardly any legitimate merchant accepted bitcoin.<sup>17</sup>

Crypto advocates and their backers, however, insisted that it was going to replace traditional payments. In May 2014, Brian Armstrong, the founder of a two-year old startup, Coinbase, claimed, according to Andy Kessler of the Wall Street Journal, that his company wanted “to be the Visa and Mastercard of Bitcoin payment processing, taking those behemoths out of the picture as merchants and customers move to virtual transactions” and as these giants had to drop their fees “to match cheaper technology.”<sup>18</sup>

This was nonsense. Bitcoin couldn't be a currency that people used for payment because experience had shown that it was too volatile, and it was clearly incapable of solving this problem. It also turns out that Bitcoin couldn't be like Visa or Mastercard, because it wasn't capable handling anything remotely close to their transaction volumes.<sup>19</sup> Eight years later, in July 2022, the major public blockchain still are not scalable and rely on volatile cryptocurrencies.<sup>20</sup>

No killer app for public blockchains has emerged for which there has been widescale adoption. There are apps such as remittances and lending but there is no evidence than any of these are in widespread use. The major new competition to incumbent remittance and lending business have come from FinTechs and Neo-Banks who do not rely on public blockchains for the bulk of their services. There is no success story remotely close to M-PESA in its first few years much less its first thirteen, or to FinTech Wise for remittances.

For the last decade, cryptocurrencies have mainly been used for trading by people betting on the value of the coins. Crypto businesses have made money largely by supporting this trading activity directly (as is the case for exchanges) or indirectly through processing these trades (as is the case for miners). Coinbase, for example, never put a dent in the card networks. It makes its money mainly from trading which is stoked by greater volatility.<sup>21</sup>

In fact, speculation has become the main use case for crypto. The exchanges have gotten increasingly aggressive at persuading retail investors to buy crypto. The recent Superbowl in the U.S. had ads promoting crypto. FTX's ad had comedian Larry David telling Thomas Edison that the light bulb stinks, with the commercial closing with “Don't be like Larry. Don't miss out on the next big thing.” Crypto.com, featuring LeBron James, said “Fortune favors the brave.” Coinbase had a rotating QR code that took people to a page giving them \$15 of free bitcoin to sign up for its wallet and entry into a \$3 million lottery.

The July 4 issue of the *New Yorker* features a two-page spread with Gisele Bündchen, the Brazilian supermodel, boosting FTX. She's “In” because she “share[s] a passion

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16 *Id.*

17 David S. Evans, “Economic Aspects of Bitcoin and Other Decentralized Public-Ledger Currency Platforms,” Coase-Sandor Institute for Law and Economics, University of Chicago, May 2014. At [https://chicagounbound.uchicago.edu/law\\_and\\_economics/680/](https://chicagounbound.uchicago.edu/law_and_economics/680/).

18 Andy Kessler, “Angling to Be the MasterCard of Bitcoin,” *Wall Street Journal*, May 16, 2014. At <https://www.wsj.com/articles/SB10001424052702303908804579563951822782842>.

19 David S Evans, “Can Crypto Fix Itself in Time,” *op. cit.*

20 Ethereum promises to ameliorate the scalability problem by switching to from proof of work to proof of stake — possibly in the next few months.

21 Khristopher J. Brooks, “Coinbase to cut workforce by 18% amid wide crypto sell-off,” CBS News, June 15, 2022. At <https://www.cbsnews.com/news/coinbase-layoffs-cryptocurrency-sell-off-brian-armstrong/>. Coinbase, *Annual Report 2021*. At <https://d18rn0p25nwr6d.cloudfront.net/CIK-0001679788/8e5e0508-da75-434d-9505-cba99fa00147.pdf>.

for creating positive change.” That’s followed by with a two-page spread with FTX founder Sam Bankman-Fried who is “in on crypto because [he] want[s] to make the biggest global impact for good.” The “You In” campaign has run in other magazines. Seven-time Superbowl winner Tom Brady, Ms. Bündchen’s husband, is also promoting crypto for FTX,<sup>22</sup> and the couple reportedly have an equity stake in the exchange.<sup>23</sup>

The ads do not disclose the extraordinary historical volatility of cryptocurrencies. The celebrity promotions started occurring during 2021. Over the last 12 months bitcoin had a high of close to \$68,991 in November 2021 and a low of \$17,602 in June 2022. Between Superbowl (February 13) and Independence Day (July 4) it fell from \$42,068 to \$20,260. The ads also do not disclose the fact that after 13 years, and many promises, cryptocurrencies are not in widespread use for any productive purpose, or the abject failure of El Salvador’s decision to make crypto a national currency.

Crypto promotions are backed by claims that it is “the future”. The blockchain will be the basis for web3 (often described as a decentralized internet based on blockchain) or financial nirvana (often described as lacking intermediaries and promoting financial equality). That future is distant, uncertain, and vague. The latest promises beg the question why the future, the next big thing, which crypto enthusiasts have promised for the last 13 years, isn’t here already.

The actual present, with exchanges paying celebrities to encourage people to speculate on crypto, in the face huge historic volatility, and great uncertainty that latest visions will ever be realized, isn’t very attractive.

## 06 STRIKING THE RIGHT BALANCE

Regulators considering where to strike the balance between innovation and regulation for crypto are working with a far different set of knowledge in which to form expectations of benefits, costs, and risks compared to what regulators

had for mobile money or more recently for FinTechs. Mobile money schemes and FinTechs came to regulators with a clean slate. They could pose problems, but there wasn’t any evidence that they had or would. They were also nascent, so it was possible to put guardrails in place to limit risk while regulators collected data from actual use.

There was no certainty at first that these were significant innovations that could help society. But they all had immediate constructive use cases. Also, within a couple of years from the start it was apparent that mobile money was a powerful force for economic progress by layering the country with an inexpensive banking and payments system that, in fact, helped large numbers of poor people.

By contrast, crypto comes to regulators today with a problematic past, a dubious present, and a concerning future. The past is filled with unlawful activity, volatility, and failed promises. The present is based on speculation and celebrity-fueled hype. Recent events demonstrate that crypto volatility combined with lax supervision can result in financial calamity and contagion. The future is one where there appears to be no solution for the underlying volatility of native cryptocurrencies which could be long-run source of systemic risk for the economy. And these are just the highlights.

Regulators should also have different priors on the likelihood that crypto will result in important innovations than a new FinTech business. Crypto has a credibility problem. For many years, crypto supporters claimed it was going to displace fiat money and traditional payments rails. Many economists, including me, explained that was just not possible and years went by, predictably, with no mass adoption. Other promises, involving various applications, came and went. Important ones, such as smart contracts, went on hiatus when, in 2017, Ethereum recognized it had to go back to the drawing board to develop a scalable efficient platform. The credibility of crypto defenders is not helped by silly similes that crypto is just like the internet and some people said the internet wouldn’t amount to anything.<sup>24</sup> Regulators should therefore view current claims about web3 with a healthy dose of skepticism.

Regulators cannot discount the possibility that overly onerous crypto regulations could prevent the realization of valuable innovations. Crypto is a vast, heavily-funded enterprise and it could lead to disruptive innovation that would be socially valuable. Ethereum is close to moving to proof of stake and taking other steps that could improve the scalability of this blockchain. It has invested in developing a

<sup>22</sup> You should not watch this if you are a Tom Brady fan but here is one of his ads: [https://www.instagram.com/reel/Cfl\\_fCEAmO9?igshid=M-DJmNzVkJMjY%3D](https://www.instagram.com/reel/Cfl_fCEAmO9?igshid=M-DJmNzVkJMjY%3D).

<sup>23</sup> Vildana Hajric, “Tom Brady and Gisele Bündchen Take Equity Stake in Crypto Firm FTX,” Bloomberg, June 29, 2021. At <https://www.bloomberg.com/news/articles/2021-06-29/tom-brady-gisele-b-ndchen-take-equity-stake-in-crypto-firm-ftx>.

<sup>24</sup> Crypto is just like alchemy. People said you couldn’t turn lead into gold. They were right. QED!

platform for smart contracts which could lead to innovations. That wouldn't solve the inherent volatility of existing cryptocurrencies. It is possible, however, that new solutions — based on or inspired by the work that has gone on — could emerge that would not be based on volatile cryptocurrencies.<sup>25</sup>

Nevertheless, when it comes to stablecoins, it is time for regulators to err on the side of caution. The risks posed are too high and immediate while the likelihood of valuable innovation too uncertain and remote. To begin with, regulators should consider imposing the firmest guarantee possible that people will be able to redeem their stablecoins at par for fiat. In practice that means 100 percent reserves of fiat for stablecoins, in cash or very short-term instruments, held by an independent trustee, in a regulated bank.

Regulators should consider doing more. There is not simply a bank solvency issue for stablecoins. There are an increasing number of crypto apps that are unregulated, and pose substantial financial risks themselves, based on stablecoins.<sup>26</sup> When crypto prices collapsed, many investors lost the stablecoins they had deposited in return for high interest rates in entities such as Celsius. More of these dangerous crypto apps will arise.<sup>27</sup> Eventually, those entities should be subject to regulation too. That may be difficult given the ability of crypto apps to locate in places — or nowhere at all in theory — where there is little regulation or operate as decentralized autonomous organizations for which there is no one to regulate.

Regulators could deal with this problem by limiting the use of stablecoins in unsafe applications. There are two potential ways to do this, helped by the fact that stablecoins are programmable. First, the regulator could approve stablecoins only for use on approved applications. It could approve applications directly or ones that have been approved by another reputable regulator. Second, the regulator could require the stablecoin issuer to have an application review process and allow its stablecoins only to be used a approved application. In either case, the stablecoin issuer should be subject to penalties, including a possible halt in activities, if it failed to limit the use of its stablecoins with the designated safe applications.

These proposed regulations ignore the elephant in the crypto room: the use of stablecoins to facilitate speculative trading, which results in increased volatility and systemic risk as well as harm to hype-fed consumer investors. That is worth serious attention by banking, exchange, and consumer protection regulators. ■

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**“Regulators cannot discount the possibility that overly onerous crypto regulations could prevent the realization of valuable innovations**

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25 It is also possible that completely different technologies could emerge, without the problems of crypto, that could result in similar innovations.

26 Rachel Louise Ensign, “They Thought ‘Crypto Banks’ Were Safe, and Then Came the Crash,” *Wall Street Journal*, July 23, 2022. At <https://www.wsj.com/articles/they-thought-crypto-banks-were-safe-and-then-came-the-crash-11658568780>.

27 For a recent example see, Scott Chipolina and Stefania Palma, “SEC charges 11 in ‘massive’ crypto Ponzi scheme,” *Financial Times*, August 1, 2022. At <https://www.ft.com/content/c011817f-7f1f-4462-95b5-d4e0fec9004>.



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