Central Bank Digital Currency

Anchor: Vishal Dahiya

Guests:

1. Ashok Nag, Former Advisor, RBI
2. A.K. Bhattacharya, Editorial Director, Business Standard

Context

The discussion highlights the concept of 'Central Bank Digital Currency and its impact on the banking system and monetary policy framework.

Currency: Properties

- A currency is a bearer note for which no authorization is required i.e. the person having the currency becomes the automatic beneficiary of it.
- The transaction between the two parties through currency is a complete transaction.
- There is no third-party verification for currency-settled transactions, unlike Bitcoins.

Central Bank Digital Currency (CBDC)

- CBDC is the same as currency issued by a central bank but takes a different form than paper.
- It is the sovereign currency in an electronic form and it would appear as a liability (currency in circulation) on a central bank's balance sheet.
- The underlying technology, form, and use of a CBDC can be molded for specific requirements. CBDCs should be exchangeable at par with cash.
- The idea of "Central Bank Digital Currencies" (CBDC) is not a recent development. Some attribute the origins of CBDCs to Nobel laureate James Tobin, an American economist, who in the 1980s suggested that Federal Reserve Banks in the United States could make available to the public a widely accessible 'medium with the convenience of deposits and the safety of currency'.

What is the need for a CBDC?

- While interest in CBDCs is universal now, very few countries have reached even the pilot stage of launching their CBDCs.
- The adoption of CBDC has been justified for the following reasons:-
    - Central banks, faced with dwindling usage of paper currency, seek to popularize a more acceptable electronic form of currency (like Sweden).
    - Jurisdictions with significant physical cash usage seeking to make issuance more efficient (like Denmark, Germany, or Japan, or even the US).
    - Central banks seek to meet the public's need for digital currencies, manifested in the increasing use of private virtual currencies, and thereby avoid the more damaging consequences of such private currencies.

Also read: **Cryptocurrency**

CBDC vs Other Digital Payments systems

- CBDCs are not just different from digital payments, they are in fact, not digital payments.
- CBDCs are digital currencies that would not have any underlying physical aspect when there is any transaction between two parties via CBDC.
- CBDCs can become the common currency for a nation but that depends on the choices of the nation's Central Bank for the preferred CBDC type. For example, what kind of ledger (centralized or distributed) is used by the Central Bank for the launch of CBDC.

Direct Cost of Physical Currency

- The RBI bears a very huge cost – supply-side cost and logistics of the entire currency management.
- Cash has several cost factors like printing cost, transportation cost, storage cost which would not incur in the case of CBDC.

CBDC and Monetary Policy Paradigm

- The leakage from the commercial banks through cash can be largely controlled through CBDC.
- The central bank will have larger control over the withdrawal of money, further resulting in better control of the liquidity in the economy.

Conclusion

- The CBDC has many advantages to offer like reduced cost, and better central control over the paper currency.
- The present banking system needs to be part of the CBDC Pilot projects in the Indian context.
- The acceptance and anonymity of paper currency can be attained with CBDC only with time and gradual acceptance.

Read all the RSTV articles in the link.