Why the launch of a wCBDC is key

In light of the experiments in which it has participated, BNP Paribas strongly supports the launch of a wholesale Central Bank Digital Currency (wCBDC) by the European Central Bank. This support is based on well identified use cases that could offer significant benefits for operational efficiency, transaction security, and the economic sovereignty of Europe. In an era of rapid technological innovation and financial transformation, the implementation of a wCBDC would represent a crucial step to maintain the competitiveness and efficiency of the European financial system. Indeed, the absence of a wCBDC is an obstacle to the development of digital asset markets. Two use cases have already been identified as highly relevant: (i) the tokenization of financial markets and (ii) international payments. In particular, the wCBDC, leveraging underlying distributed ledger technology, would enable the transfer of asset ownership (or changes in the state of a digital representation of an asset) to occur against an instantaneous payment while eliminating delivery risk (both legs are executed, or none) and ensuring settlement finality.

Delivery versus Payment (DvP) for tokenized financial Instruments

One of the most promising use cases for a wCBDC lies in Delivery versus Payment (DvP) for tokenized traditional financial instruments. It should be a decisive tool to foster and accelerate the tokenization of financial markets. This tokenization is particularly promising for bonds, securitization, syndicated loans, trade finance, supply chain finance, repurchase agreements, and potentially embedded derivatives in smart contracts. The expected benefits include:

- Simplification and automation of processes: financial transactions would become smoother and more automated, reducing the number and role of intermediaries in standard cases. This would likely lower operational costs and improve overall transaction efficiency. The automated and transparent processes of the wCBDC would allow better lifecycle management of financial securities, such as dividends and coupon payments, and redemptions, thereby increasing payment efficiency and accuracy while reducing some operational risks by enabling greater reliance on shared golden sources (less reliance on reconciliations and confirmations).

- Speed and security of settlements/deliveries: reducing settlement, counterparty, and operational risks would improve transaction security and efficiency, while faster execution of transactions would minimize price volatility risk.

- Better liquidity management: a wCBDC could be beneficial for intraday liquidity management, including margin calls, repo, and reverse repo operations. The immediate availability of funds through the wCBDC would facilitate liquidity management for financial institutions, reducing the risk of liquidity shortages and improving financial stability. Improved collateral management would optimize asset use, reducing financing costs and enhancing the financial resilience of institutions.

- Improved collateral management and mobilization: a wCBDC would enable more dynamic and efficient collateral management, optimizing financial resources for institutions. It would also facilitate real-time tracking and adjustment of collateral, thus contributing to better risk management.

- Improved traceability of operations and reduction in regulatory reporting obligations : a better traceability would simplify compliance with regulatory requirements and reduce associated costs. Increased transparency of transactions, notably regarding ESG, would also allow for more effective market oversight.

International Payments and settlement of commercial bank money tokens

The introduction of a wCBDC could significantly enhance the efficiency of international payments. By simplifying and accelerating these transactions, the wCBDC would help bolster European sovereignty in the face of the rise of private alternative solutions and the dominance of the US dollar. It would be crucial to preserve Europe's monetary autonomy and ensure better competitiveness on the international stage. Cross-border payments, often requiring a serial intervention of different correspondent banks, could benefit from a drastic reduction in interactions, resulting in shorter delivery of funds and lower fees while increasing transaction transparency and traceability.

Additionally, a wCBDC would enable the settlement of commercial bank money tokens. Various initiatives are underway to develop tokenized commercial bank money/deposits[1] to provide client services, such as faster and seamless intra-group treasury management, programmable payments in supply chain management, and FX services for high-value transactions. Without a wCBDC, the elimination of counterparty risk - which is inherent in commercial bank money tokens is challenging to achieve, and significant interbank exposures are likely to persist. BNP Paribas welcomes the Agorá project, launched by the Bank for International Settlements (BIS), with participation from the Bank of France (representing the Eurosystem), Bank of Japan, Bank of Korea, Bank of Mexico, Swiss National Bank, Bank of England, and the Federal Reserve Bank of New York, which could lead the way toward an integration of tokenized commercial bank money and central bank money in the new digital economy, also leading to a harmonization of international standards on wCBDC and tokenized bank deposits.

Distributed Ledger Technology

A crucial aspect of the wCBDC is its integration with Distributed Ledger Technology (DLT). This integration is necessary to fully exploit the potential of new technologies, client services, and the needs of tokenizing traditional financial markets. DLT offers advantages in terms of security, transparency, and transaction efficiency. It allows for reduced transaction costs and better risk management, ensuring complete and immutable traceability of financial transactions. Moreover, DLT can facilitate interoperability between different financial systems, thereby enhancing international integration and cooperation.

Risks of the absence of a wCBDC

The absence of a European wCBDC is a major obstacle to the tokenization of European financial markets. The limited number of projects submitted by market infrastructures for authorization under the European pilot regime highlights this reality. This absence could encourage the rise of private alternative solutions, such as stablecoins, mainly issued by non-EU non-banking entities, introducing significant risks for financial stability. Even with the MiCA Regulation, since stablecoins are issued by private entities managing a reserve asset pool, they may present liquidity and solvency risks, unlike a wCBDC, which would benefit from central bank backing and ensure 1:1 convertibility to commercial bank money. It is both important and urgent to develop and implement a wCBDC, to circumvent the risk of disintermediation of both central and commercial banks, preserve the stability of the financial system, and avoid growing dependence on non-European payment solutions.

Continuity of the monetary system and financial stability

To ensure that this technological evolution respects the continuity and stability requirements of the monetary system, the issuance of a wCBDC must be complemented by the necessary instruments within the commercial banking system. A financial system embracing tokenization must ensure a balance between central bank money and commercial bank money, similar to the current monetary system. The wCBDC should not replace commercial bank money in areas such as payments between non-financial corporates, which are already well-served by existing payment systems. These systems provide essential functionalities to non-financial corporates, such as cash flow management and payment security, and it is crucial not to disrupt these services. Access to the wCBDC should be reserved, as is the case today, for regulated financial institutions to maintain control over the money supply, avoid potential disruptions to the monetary system, contain cybersecurity risks, and ensure the secure and controlled use of this new form of central bank money on new technology.

* *
*

Our support for the launch of a wCBDC is based on the substantial benefits expected for operational efficiency, transaction security, and economic sovereignty. The urgency to move forward in this direction is reinforced by the risks associated with the absence of a wCBDC, particularly in the face of the rise of stablecoins. Additionally, the renewed focus on the Capital Markets Union highlights the potential for high-quality DLT-based solutions to create new markets, improve efficiency, reduce costs, and mitigate certain risks. To succeed, the implementation of the wCBDC must rely on a careful balance between central bank and commercial bank money, while fully leveraging Distributed Ledger Technologies. By adopting a proactive and well-coordinated approach, the EU can not only strengthen its position in the global financial system but also ensure greater stability and efficiency in its financial markets.

[1] *A tokenised bank deposit is a digital representation on a blockchain or distributed ledger technology of a traditional bank deposit, i.e. commercial bank money. Like a traditional bank deposit, it is recorded as a liability on the issuing commercial bank's balance sheet. In other words, it is legally binding claim on the issuing commercial bank while stablecoins such as MiCA's e-money tokens (EMTs) are backed by a specific pool of assets and thus are comparable to units of money market funds, in some cases with a variable net asset value and in others with a constant net asset value.*