

# A DIGITAL EURO FOR THE PEOPLE

POSITION PAPER



# TABLE OF CONTENTS

<b>Executive summary</b>	<b>3</b>
<b>Introduction</b>	<b>4</b>
<b>1. The ECB's proposal on the digital euro misses its full potential</b>	<b>6</b>
<b>2. A digital euro designed for the benefit of people and society</b>	<b>8</b>
2.1. Be universally accessible	8
2.2. Be free of cost for users	9
2.3. Offer a high level of privacy and data protection	9
2.4. Have a clear European Central Bank branding	10
2.5. Bring resilience to the payment system	10
<b>3. Long-term benefits of an attractive digital euro</b>	<b>11</b>
3.1. A long-term vision to improve financial stability	11
3.2. More effective and fairer monetary policy	12

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# EXECUTIVE SUMMARY

The recent bank collapses and bailouts highlight the fragility of the banking system and our bank deposits. The digital euro is an **opportunity to reconfigure our monetary system** to serve the interests of people and society, by making money safer and more inclusive. **However**, the European Central Bank's (ECB) **current proposal for a digital euro falls short of this potential**. The current plan relies heavily on private financial intermediaries and envisions putting important limitations on the use of digital euros, thereby impacting its capacity to be a universally accessible public good and risking undermining the uptake of the digital euro. By heeding to the bank lobby and baking their interests into the design of the digital euro, the ECB is missing an opportunity to develop an appealing and public digital alternative to private bank deposits.

The digital euro must be developed with the aim of benefiting people and society over private interests, and these considerations should guide its design. In the **short term**, the digital euro should:

- 1. Be universally accessible.** People should be able to access digital euros through a diverse range of intermediaries, which include non-profit and public entities. Implementing a tiered identification system for account-based digital euros, and introducing a value-based option, would ensure the availability of digital euros to the most vulnerable segments of society.
- 2. Be free of cost for users.** Any future legislative framework on the digital euro should include a list of basic services that should be provided for free to users, such as opening and managing an account and the provision of a payment instrument (e.g. a card).
- 3. Offer a high level of privacy and data protection.** Cash, which is fully anonymous, should be used as the baseline when developing the digital euro. A value-based option should be introduced alongside an account-based one, and it should be designed to be fully anonymous. For the account-based option, a 'privacy threshold' can ensure that users' data for small transactions is protected.
- 4. Have a clear European Central Bank branding.** Clear branding will help to differentiate public digital euros from private bank deposits.
- 5. Bring resilience to the payment system.** By providing an offline value-based option, and by ensuring that the digital euro's legal and technical core infrastructure is public and works independently of any private system, we can offer an alternative to existing payment rails and increase resiliency in case of outages.

The digital euro is also an opportunity to **improve financial stability** by transforming the banking system, and helping central banks to **more effectively carry out their monetary policy**. The design of the digital euro should be flexible enough to allow for the achievement of these **long-term** goals, and more research should be conducted to explore how different features could help achieve them. For instance, a digital euro without any holding limit could reduce moral hazard in the banking sector, and the adjustment of interest rates on digital euro deposits and direct monetary transfers could improve the transmission of monetary policy.

# INTRODUCTION

The recent bank collapses in the US and the bailout of Credit Suisse show once again that banking crises can, and will, recur, and that when they do, governments have to step in to ensure that our bank deposits are safe. The underlying problem is that the money that we use on a daily basis, namely bank deposits, is inherently fragile due to a number of reasons, including the banks' risky investments, the lack of separation between their lending and payment services, and the consequences that bank runs can have on their sources of funding, among other things. The banking crisis rekindled the conversation about how a digital form of public money could reduce our reliance on profit-seeking banks.<sup>1</sup> This would, among other benefits, improve the stability of the financial system as a whole, and the resilience of our payments system, by providing a public alternative.

**In contrast** to the private bank money created by the commercial banks, **public money** issued by central banks **is an inherently stable form of money**. Physical cash is currently the only form of public money that people can use.<sup>2</sup> It is the most liquid and risk-free asset that people have access to in an economy today because it is a liability of the central bank, which, unlike commercial banks, cannot go bankrupt. However, people continue to rely on private money because physical banknotes and coins are not convenient for keeping large sums of money and making high-value transactions, and cannot be used to pay digitally.<sup>3</sup> Today, **privately issued money represents 86% of the total money** in circulation in the real economy.<sup>4</sup>

The digitisation of money and the decline of physical cash in payments has led to an increased privatisation of money and payments. This poses at least three concerns in terms of data protection, financial inclusion and cost of payments. First, with cash no longer being accepted everywhere, people are losing access to an anonymous means of payment, which means even more transfer of personal data into the hands of payment service providers, and this at a time when trust in these actors is already low.<sup>5</sup> Second, **13% of eurozone residents** do not have or use a debit or credit card, meaning that they **are financially excluded**. Among the 40% of people with the lowest income, this number is estimated to be between 16% and 22%.<sup>6</sup> Third, payment services are not getting cheaper, despite competition between firms. In Europe, Visa and Mastercard scheme fees are estimated to have increased by €876 million from 2016 to 2021.<sup>7</sup>

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1. Sandbu, M (March 2023): [www.ft.com/content/c66e6980-2d64-407a-ad79-2d85c3e32e69](https://www.ft.com/content/c66e6980-2d64-407a-ad79-2d85c3e32e69).

2. In practice, however, people mostly do have to possess bank accounts and pay corresponding fees in order to access physical cash: in that sense the digital euro could restore the original meaning of costless means of payment.

3. The ECB's 'Study on the payment attitudes of consumers in the euro area' (SPACE) found that while cash is still the most frequently used payment method at the point of sale in the euro area, its use overall has declined. It was used in 59% of transactions in 2022, down from 79% in 2016 and 72% in 2019: [www.ecb.europa.eu/stats/ecb\\_surveys/space/html/](https://www.ecb.europa.eu/stats/ecb_surveys/space/html/)

[ecb.spacereport202212-783ffdf46e.en.html](https://www.ecb.europa.eu/press/pr/spacereport202212-783ffdf46e.en.html).

4. Own calculation as of February 2023. Money in circulation is defined as M1, meaning currency in circulation (cash) and overnight deposits (bank deposits): [www.ecb.europa.eu/pub/pdf/annex/ecb.md2302\\_annex.en.pdf](https://www.ecb.europa.eu/pub/pdf/annex/ecb.md2302_annex.en.pdf).

5. According to OMFIF, net trust in commercial banks among 'advanced economies' is negative. OMFIF (2020), Digital Currencies: A question of trust: [www.omfif.org/wp-content/uploads/2020/02/Digital-currencies-A-question-of-trust-1.pdf](https://www.omfif.org/wp-content/uploads/2020/02/Digital-currencies-A-question-of-trust-1.pdf).

6. Estimate based on extrapolation of available data from The Global Findex Database 2021: [www.worldbank.org/en/publication/globalfindex](https://www.worldbank.org/en/publication/globalfindex).

7. CMSPI & Zephyre, commissioned by Eurocommerce (2020), Scheme Fee Study. Available upon request to the authors.

Other developments risk further displacing public money, and even the euro as a currency. These include the development of cryptocurrencies by Big Tech, such as Meta's now abandoned Libra project,<sup>8</sup> and the development of central bank digital currencies (CBDC) by other jurisdictions. Included in the latter is China's digital yuan, which could become widely used at the international level, including in Europe. Both of these developments are seen by the European Central Bank (ECB) as a threat to the euro,<sup>9</sup> and together with the decline of cash, were strong catalysts for the ECB to start researching its own digital currency project in 2021 — the digital euro.

The digital euro is an **opportunity to provide a universally accessible and safe electronic form of public money**, offering people a real alternative to private bank money. It would also provide all residents with a state-of-the-art digital payment infrastructure that is standardised throughout the euro area. It is an opportunity to re-establish money as a truly public good that serves the interests of people and society. Unfortunately, the ECB is currently considering putting important limitations on the digital euro to protect the interests of private financial intermediaries, such as commercial banks. These considerations, which will be discussed in the next section, would make the digital euro unattractive to users, and would risk undermining the project before it even takes off.

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8. The Libra project put central bankers on edge in 2019: Mersch, Yves (2019), Money and private currencies: reflections on Libra: [www.ecb.europa.eu/press/key/date/2019/html/ecb.sp190902-aedded9219.en.html](https://www.ecb.europa.eu/press/key/date/2019/html/ecb.sp190902-aedded9219.en.html).

9. Blitz, R (2019): [www.ft.com/content/46312412-e469-11e9-b8e0-026e07cbe5b4](https://www.ft.com/content/46312412-e469-11e9-b8e0-026e07cbe5b4).

# 1. THE ECB'S PROPOSAL ON THE DIGITAL EURO MISSES ITS FULL POTENTIAL

The ECB has the task to promote the smooth operation of the payment system.<sup>10</sup> As mentioned above, the increasing digitisation of payments, the decline of cash, and the emergence of Big Tech and foreign digital currencies prompted the central bank to start studying and developing a digital alternative to cash.

The ECB plans to create a digital euro infrastructure whereby supervised intermediaries (primarily commercial banks) play a central role in its distribution, by opening accounts and providing payment services to consumers. In this organisational structure, the ECB's role will be limited to issuing the currency and settling transactions between commercial banks and other intermediaries. ECB Executive Board Member Fabio Panetta has clearly highlighted that the digital euro is only meant to be a 'raw material',<sup>11</sup> to be handed over to financial intermediaries so that they can integrate it into their services and supply it to their customers. The digital euro project is then **reduced to a simple 'payment scheme'**,<sup>12</sup> in other words, a platform for intermediaries to build their own services on.

Recent communications from the ECB seem to open the door to public entities being able to distribute digital euros along with private intermediaries.<sup>13</sup> **However, it has not been made explicit** by Fabio Panetta or other ECB staff. In his speech presenting the third report to the European Parliament, Fabio Panetta primarily referred to the commercial banks as the main distributors of the digital currency.<sup>14</sup> If the digital euro is primarily intended to be distributed through private financial intermediaries, the **cost and accessibility of the digital euro risk being influenced by their primary goal of profit-making**, rather than ensuring access to public money.<sup>15</sup> A parallel can be drawn with the example of cash today, where banks have closed bank branches and ATMs because they see them as unprofitable. As mentioned above, this reliance on banks to provide the public good of payment systems ultimately results in large numbers of people being financially excluded.

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10. Article 3 of the Statute of the European System of Central Banks and the ECB, and Article 127.2 of the TFEU.

11. Panetta, F (June 2021), Interview with Financial Times: [www.ecb.europa.eu/press/inter/date/2021/html/ecb.in210620-c8acf4bc2b.en.html](https://www.ecb.europa.eu/press/inter/date/2021/html/ecb.in210620-c8acf4bc2b.en.html). This is the same terminology used by the European Banking Federation's position paper on the digital euro: [www.ebf.eu/wp-content/uploads/2023/03/EBF-Digital-Euro-paper-2023\\_final.pdf](https://www.ebf.eu/wp-content/uploads/2023/03/EBF-Digital-Euro-paper-2023_final.pdf).

12. ECB (6 July 2022), 5th Digital Euro MAG meeting: [www.ecb.europa.eu/paym/digital\\_euro/investigation/governance/shared/files/ecb.degov220706\\_distrib.en.pdf?cd246b972ac841930de2a970f2eaa3a7](https://www.ecb.europa.eu/paym/digital_euro/investigation/governance/shared/files/ecb.degov220706_distrib.en.pdf?cd246b972ac841930de2a970f2eaa3a7).

13. In its third report progress report, the ECB explicitly says that payments service providers, as defined under the Payment Services Directive (PSD2), will be responsible for distributing digital euros. This definition includes Member States or their regional or local authorities, post office giro institutions and even the ECB and national central banks themselves:

ECB (April 2023), Eurosystem third progress report on the investigation phase of the digital euro:

[www.ecb.europa.eu/paym/digital\\_euro/investigation/governance/shared/files/ecb.degov230424\\_progress.en.pdf](https://www.ecb.europa.eu/paym/digital_euro/investigation/governance/shared/files/ecb.degov230424_progress.en.pdf)

14. In footnote 12 to the speech, Fabio Panetta (2023) only mentions "credit institutions, electronic money institutions and payment institutions" as examples of PSP2: [www.ecb.europa.eu/press/key/date/2023/html/ecb.sp230424\\_1-f44c7ac164.en.html](https://www.ecb.europa.eu/press/key/date/2023/html/ecb.sp230424_1-f44c7ac164.en.html)

15. The banking sector also expects to be compensated by the ECB for the digital euro payment services that it would supply. See: European Banking Federation (2023), Vision on a Digital Euro Ecosystem: [www.ebf.eu/wp-content/uploads/2023/03/EBF-Digital-Euro-paper-2023\\_final.pdf](https://www.ebf.eu/wp-content/uploads/2023/03/EBF-Digital-Euro-paper-2023_final.pdf).

Moreover, this approach would make the digital euro very similar to existing bank deposits. **People are unlikely to take up digital euros if they perceive them as being no different to the private money** already offered by commercial banks. The digital euro would then bring little added value, and would not represent a true alternative to bank deposits, thus missing its full potential.

These risks would be further exacerbated by the enforcement of a cap on digital euro accounts. The ECB is currently discussing a limit of €3,000 to address financial instability concerns raised by the banking sector. According to Fabio Panetta, an unrestricted digital euro could trigger a flight from bank deposits to digital euros, thereby affecting the profitability of the commercial banks and their capacity to attract cheap funding, and ultimately their ability to lend to the real economy.<sup>16</sup> On the other hand, **limiting the amount of digital euros that people can hold** would prevent the digital currency from becoming an effective safe store of value,<sup>17</sup> which **would discourage people from using it**.

However, the fear of flights from bank deposits to digital euro accounts has to be put into perspective. A recent report commissioned by the European Parliament says that the ECB's narrow position on the digital euro cannot be fully justified by existing literature, which does not come to a definitive conclusion on the effects of the introduction of an unrestricted CBDC on the stability of the banking sector.<sup>18</sup> In fact, research shows that there is **no unique answer to the macroeconomic implications of the introduction of a CBDC**, and that commercial banks with high liquidity and diversified funding portfolios can deal with potential deposit flights.<sup>19</sup> And even in the event that this would be insufficient, commercial banks could find alternative sources of funding. The central bank could, for instance, use its refinancing operations to reallocate the liquidity it collects in digital euros to the commercial banks.<sup>20</sup>

**Keeping the financial system stable is in everyone's interest**, whether it is the ordinary person on the street or the commercial banks. A well-designed digital euro has the potential to serve people's interest and improve financial stability in the long run (see Section 3.1). At the moment, the ECB heeds too much to the concerns of the commercial bank industry,<sup>21</sup> rather than making sure that it develops an attractive digital equivalent to cash.<sup>22</sup>

Ultimately, the digital euro project will be the **result of political choices that will determine its policy objectives**. Ahead of the upcoming legislative proposal, policymakers need to make sure they consult with a wide range of stakeholders including ordinary people, civil society, academia and financial institutions. This paper aims to provide a civil society perspective. In the following sections, we propose short- and long-term policy goals, as well as associated design features that we believe the digital euro should have in order to fulfil its function as a true public good.

16. Panetta, F (2021), The present and future of money in the digital age. In: Lecture for FederCasse (Federation of Italian Cooperative Credit Banks), Rome, 10 December 2021.

17. Cash and bank deposits perform both as a means of payment and a store of value. That means they are accepted widely as a currency, they retain their value over time and they can be stored to be reused for future payments.

18. Hofmann, C (2023), Digital Euro: An assessment of the first two progress reports. The case for unlimited holdings of digital euros: [www.europarl.europa.eu/RegData/etudes/IDAN/2023/741511/IPOL\\_IDA\(2023\)741511\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/IDAN/2023/741511/IPOL_IDA(2023)741511_EN.pdf).

19. Infante S, Kim K, Orlík A, et al. (2022), The Macroeconomic Implications of CBDC: A Review of the Literature. Federal Reserve Board Finance and Economics Discussion Series (2022–076): [www.federalreserve.gov/econres/feds/files/2022076pap.pdf](http://www.federalreserve.gov/econres/feds/files/2022076pap.pdf). Gorelova A, Lands B and teNyenhuys M (2022) Resilience of bank liquidity ratios in the presence of a central bank digital currency. Bank of Canada Staff Analytical Notes (2022–5). Bank of Canada: [www.bankofcanada.ca/2022/05/staff-analytical-note-2022-5/](http://www.bankofcanada.ca/2022/05/staff-analytical-note-2022-5/).

20. Dissaux T, Kalinowski W (eds.) (2023), A digital euro for a better monetary system, Veblen Institute for economic

reforms: [www.veblen-institute.org/IMG/pdf/veblen\\_study\\_digital\\_euro\\_the\\_case\\_for\\_a\\_public\\_option\\_jan\\_2023.pdf](http://www.veblen-institute.org/IMG/pdf/veblen_study_digital_euro_the_case_for_a_public_option_jan_2023.pdf). Brunnermeier M. and Niepelt D. (2019), On the equivalence of private and public money: [www.sciencedirect.com/science/article/abs/pii/S0304393219301229](http://www.sciencedirect.com/science/article/abs/pii/S0304393219301229).

21. The Digital Euro Market Advisory Group (MAG) is mandated to advise the Eurosystem 'on the design and distribution of a potential digital euro from an industry perspective'. It is composed of 30 senior business professionals appointed by the High-Level Task Force on Central Bank Digital Currency. ECB (2021): [www.ecb.europa.eu/press/pr/date/2021/html/ecb.pr211025-08af93ada7.en.html](http://www.ecb.europa.eu/press/pr/date/2021/html/ecb.pr211025-08af93ada7.en.html). Following its announcement, more than 100 scholars and NGOs called for greater involvement of civil society in the design of the digital euro: [www.euractiv.com/section/economy-jobs/opinion/the-digital-euro-concerns-the-whole-society-not-only-finance/](http://www.euractiv.com/section/economy-jobs/opinion/the-digital-euro-concerns-the-whole-society-not-only-finance/).

22. It should be noted that in his first speech on the digital euro, Fabio Panetta (2020) described the digital euro as 'a digital equivalent of euro banknotes', underlying that it would fulfil both payment and store of value functions: [www.ecb.europa.eu/press/key/date/2020/html/ecb.sp201012\\_1-1d14637163.en.html](http://www.ecb.europa.eu/press/key/date/2020/html/ecb.sp201012_1-1d14637163.en.html).

## 2. A DIGITAL EURO DESIGNED FOR THE BENEFIT OF PEOPLE AND SOCIETY

There are various ways of implementing a central bank digital currency, and policy objectives should guide technical design choices. To serve the public interest, the digital euro should not be designed only as a 'raw material' for financial intermediaries to build services on, but also be a viable alternative to private bank deposits.<sup>23</sup> For these reasons, in the short term a digital euro should:

### 2.1. Be universally accessible

To be truly universally accessible to all residents of the eurozone, digital euro services should be **provided by a diversified range of intermediaries**, which include non-profits and public entities. These could include public banks, postal networks, public digital spaces, local administrations and even the ECB itself, through its own digital euro app, or national central bank branches,<sup>24</sup> among others. Banks and other financial institutions are selective towards their customer base, and with the increased digitisation of payments, marginalised groups, such as low income households, refugees or elderly people, increasingly risk becoming victims of financial exclusion. We cannot expect the market to meet all needs, nor can we rely solely on it to fulfil public policy objectives.

Digital euro accounts **should be more accessible than bank accounts**. Currently, strong Know Your Customer (KYC) rules lead to the financial exclusion of people who do not have all the required documentation, such as refugees with valid residence cards. For the digital euro, a **tiered identification system** could be put in place to allow anyone to be able to open a digital euro account with a simple identification element, such as an email address or a phone number. These accounts would hold a limited amount of money and allow for a limited transaction value over a certain period of time. The more KYC steps the user is able or willing to take, the further these limitations could expand.<sup>25</sup> This approach also ensures transparency for higher amounts of holdings and higher values of transactions, addressing Anti-Money Laundering (AML) and Countering the Financing of Terrorism (CFT) considerations.

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23. Dissaux T, Kalinowski W (eds.) (2023), A digital euro for a better monetary system, Veblen Institute for economic reforms: [www.veblen-institute.org/IMG/pdf/veblen\\_study\\_digital\\_euro\\_the\\_case\\_for\\_a\\_public\\_option\\_jan\\_2023.pdf](https://www.veblen-institute.org/IMG/pdf/veblen_study_digital_euro_the_case_for_a_public_option_jan_2023.pdf).

24. Dissaux, Kalinowski et al. (2023) argue that the functioning of TARGET2 and the recent past show central banks can have customer-facing activities; therefore, this option should be further studied.

25. This approach is in place with the digital yuan; Xu J (2022), Developments and Implications of Central Bank Digital Currency: The Case of China e-CNY. Asian Economic Policy Review 17(2): 235–250: <https://onlinelibrary.wiley.com/doi/10.1111/aep.12396>.

A value-based digital euro, which could have **no identification requirements**, should complement an account-based digital euro for those who do not qualify for or do not wish to use it. While the account-based digital euro requires an intermediary to transfer money from one user's account to another, value-based systems consist of peer-to-peer digital tokens that can be considered as a digital version of cash. Acting as wallets for the digital euro, universal access devices<sup>26</sup> such as smartcards should be provided by the Eurosystem, so that anyone can access digital euros.<sup>27</sup> AML and CFT regulations must be taken into account and limitations could apply in the same way to the digital euro as they do to cash.

## 2.2. Be free of cost for users

In order for the digital euro to be a truly public good, it needs to be free of charge for users. Future legislation relating to the digital euro should include a list of **basic services that should be provided for free** to users, such as opening and managing an account, and the provision of a payment instrument (e.g. a card). If digital euro services are to be provided by profit-making financial intermediaries, and legislation does not oblige them to offer cost-free basic services, then there is a risk they will pass on the cost to users. Costs could also be indirect if private providers cross-sell digital euro services with their other services.

## 2.3. Offer a high level of privacy and data protection

A truly public digital euro would need to address the concerns of privacy that were raised by the public in the ECB's public consultation on the digital euro.<sup>28</sup> Anonymity in payments offers the strongest protection against mass surveillance by both private and public actors.<sup>29</sup> **Cash**, which is fully anonymous, and not private payment solutions, **should therefore be used as the baseline when developing the digital euro**. This position is echoed by the European Data Protection Board (EDPB),<sup>30</sup> who recommends a value-based model over an account-based model. A value-based option should be introduced alongside an account-based one, and it should be designed to be fully anonymous, with no identity associated with digital euro wallets, allowing peer-to-peer exchanges without the involvement of a third party.

When it comes to account-based digital euros, a '**privacy threshold**' under which no tracing of the transactions can occur could be introduced, as recommended by the EDPB. The tiered identification, discussed in Section 2.1, could in this way balance important security concerns (such as AML and CFT) with the protection of the fundamental rights to privacy and data protection: an increasing value of transactions would be associated with higher levels of KYC requirements and a lower level of privacy. Tiered identification would allow for less concentration of data in the hands of the intermediaries offering digital euros.

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26. Miedema J et al. (2020), Designing a CBDC for universal access, Bank of Canada Staff Analytical Notes: [www.bankofcanada.ca/2020/06/staff-analytical-note-2020-10/](https://www.bankofcanada.ca/2020/06/staff-analytical-note-2020-10/).

27. On the downside, similarly to cash, losing a digital token also means losing money, without the possibility to block or retrieve funds.

28. Eurosystem report on the public consultation on a digital euro (April, 2021), Frankfurt am Main: European Central Bank: [www.ecb.europa.eu/pub/pdf/other/Eurosystem\\_report\\_on\\_the\\_public\\_consultation\\_on\\_a\\_digital\\_euro-539fa8cd8d.en.pdf](https://www.ecb.europa.eu/pub/pdf/other/Eurosystem_report_on_the_public_consultation_on_a_digital_euro-539fa8cd8d.en.pdf).

29. A pertinent example of this is the Canadian Government's invocation of the Emergency Act to end the Freedom Convoy's anti-vaccine protests in 2022. These emergency powers allowed the government to freeze the organisers' bank accounts, showing public entities can access people's accounts at private financial institutions (even in the absence of any CBDC).

30. EDPB (2022), [https://edpb.europa.eu/system/files/2022-10/edpb\\_statement\\_20221010\\_digital\\_euro\\_en.pdf](https://edpb.europa.eu/system/files/2022-10/edpb_statement_20221010_digital_euro_en.pdf)

## 2.4. Have a clear European Central Bank branding

In the same way that physical cash issued by a central bank can be easily identified through the symbols and images on bank notes and coins, digital euros should also have a clear European Central Bank branding. This is crucial to ensuring that people can **tell the difference** between public digital euros issued by the central bank, and private money (that also carries the euro symbol), which is created by the commercial banks. As a new form of public money, the digital euro should clearly convey its public function and its public ownership.

## 2.5. Bring resilience to the payment system

The ECB's 'digital euro scheme'<sup>31</sup> would offer an alternative to existing card schemes, but it would still depend on commercial banks and acquirers at both ends of every transaction.<sup>32</sup> In order to bring resilience to the payment system, **the digital euro's legal and technical core infrastructure should be public** and work independently of any private system. This, together with a value-based digital euro, which would allow for offline transactions using a digital euro app or a universal access device such as a smart card, would offer a fully independent public fall-back system in case of outages due to cybersecurity attacks or extreme weather events.

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31. According to the ECB, the digital euro would be a platform on which private intermediaries can build their own services.

32. Today, we rely entirely on private service providers for settling our digital financial transactions. Besides commercial banks, the main actors of our payment systems are the card payment schemes (mainly Visa and Mastercard, who handle around 70% of European payments) and the acquirers (Worldline and Nexi being the main ones in Europe). Each digital payment we make involves our own bank, the acquirer to which the merchant is connected, a card payment scheme and the merchant's bank.

### 3. LONG-TERM BENEFITS OF AN ATTRACTIVE DIGITAL EURO

The digital euro is an opportunity to improve financial stability in the long run by transforming the money and banking system, and helping central banks to more effectively carry out their monetary policy. The design of the digital euro should be flexible enough to allow for the achievement of these **long-term** goals. More research may be needed to explore how different design features could achieve them.

#### 3.1. A long-term vision to improve financial stability

The ECB needs to switch from the short-term lens through which it is looking at the digital euro as a limited means of payment, and welcome the **improvements that a successful CBDC can bring** in the long run, such as helping to build a more resilient and fair monetary system. Bank deposits are currently not only the dominant digital means of payment, but also the dominant digital store of value available. However, as we have witnessed during the multiple banking crises over the last 20 years, they are inherently fragile, and people risk losing their money in cases of a bank collapse. For this reason, bank deposits are protected by legally-required deposit guarantee schemes and there is often an implicit guarantee by the state to safeguard deposits. However, there is a paradox here. The very fact that banks benefit from these guarantees means that they can continue to pursue additional risks in their search for more profit — a phenomenon known as 'moral hazard'. And despite continuously expanding bank regulation, the vulnerability of bank deposits continues to threaten financial stability.

The digital euro, on the contrary, would be inherently safe, even in the case of a bank run or financial tremors, because it is a liability of the central bank. It **does not require any state protection**, such as deposit guarantee schemes, because central banks cannot go bankrupt. Therefore, higher uptake of the digital euro should be seen as an opportunity to reduce moral hazard in the banking sector and improve the overall financial stability of the system, rather than as a threat to it.

For that to happen, on top of its function as a means of payment, the digital euro **needs to become a store of value for the public**, meaning that there should be no cap on the amount of digital euros people can hold. This might incentivise users to move considerably more of their funds from bank deposits to digital euro accounts. In response, banks would have to seek out alternative funding sources, including long-term debt issuance and own equity, that could make them more stable and resilient in the long run.

In the eventuality in which evidence of financial instability emerges from the absence of holding limits, a 'second best' scenario should be considered: limits can be applied in the short term as an adjustment period for all actors in the financial sector, but they should be gradually removed with time. This stepwise increase of caps should go hand in hand with a stepwise reduction of deposit guarantee schemes in correspondence to the increased storing capacity for all residents of digital euro accounts. This approach would support a gradual transition to a safer monetary system that would allow banks to adjust their business models.

Starting to reduce government protections of the banking sector and levelling the playing field could see some alternative payment and lending institutions emerging. This could further **reduce our over-reliance on too-big-to-fail banks**, and the problems that such banks entail for financial stability.

### 3.2. More effective and fairer monetary policy

Experts are divided on whether the digital euro can, and should be, used as a monetary policy tool, but the ECB has clearly dismissed this possibility. The debate should be open and constructive, and more research should be conducted to explore whether the digital euro could improve the effectiveness and fairness of monetary policy. The digital euro could, for instance, **improve the transmission of monetary policy by adjusting interest rates directly** (rather than relying on the banking system as an intermediary). In times of restrictive monetary policy, remuneration on digital euro accounts would push banks to pass on higher interest rates to users and incentivise people to save, or see their customers moving their deposits away. Conversely, in an expansionary environment, and especially in the case of negative interest rates, where banks may decide to pass on their costs to their customers, the ECB could implement a tiered remuneration approach to protect small depositors from these penalties.<sup>33</sup>

The digital euro could also facilitate direct monetary transfers to people (so-called helicopter money).<sup>34</sup> This instrument would be particularly effective for **stimulating the economy** in times of economic downturn, **by transferring money directly to people to spend in the real economy, rather than injecting it into the financial markets**, as has been the case with quantitative easing. The digital euro could support ECB monetary policy operations, and these options should be better explored to leave no stone unturned.

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33. Hofmann, C (2023), Digital Euro: An assessment of the first two progress reports: [www.europarl.europa.eu/RegData/etudes/IDAN/2023/741511/IPOL\\_IDA\(2023\)741511\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/IDAN/2023/741511/IPOL_IDA(2023)741511_EN.pdf).

34. More has been written in: Dissaux T, Kalinowski W (eds.) (2023), A digital euro for a better monetary system, Veblen Institute for economic reforms: [www.veblen-institute.org/IMG/pdf/veblen\\_study\\_digital\\_euro\\_the\\_case\\_for\\_a\\_public\\_option\\_jan\\_2023.pdf](http://www.veblen-institute.org/IMG/pdf/veblen_study_digital_euro_the_case_for_a_public_option_jan_2023.pdf).



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