Libra, Weltwährung des 21. Jahrhunderts?

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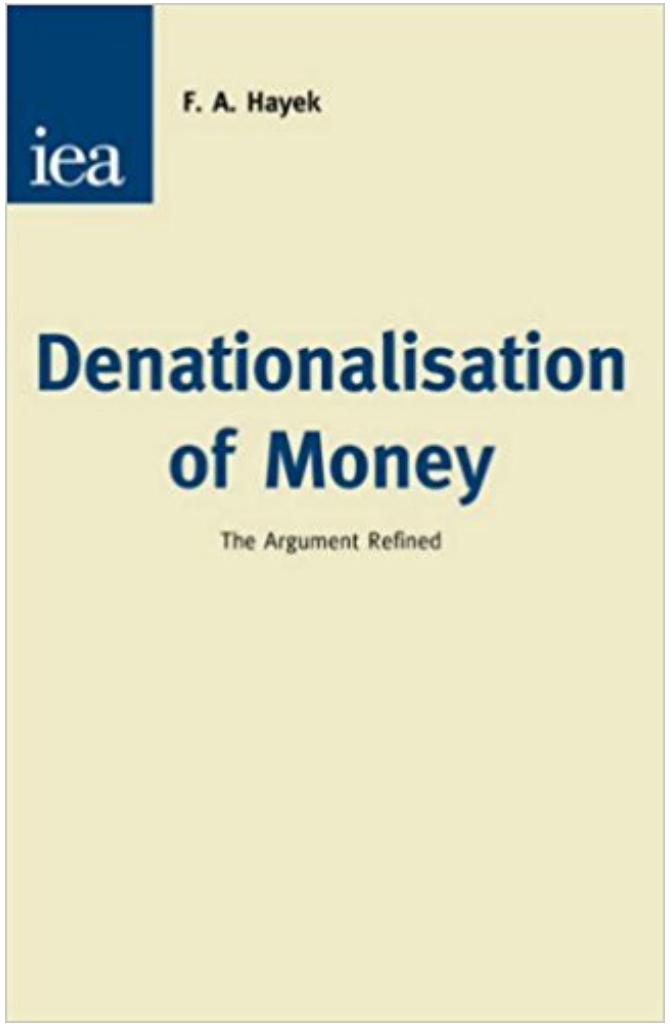
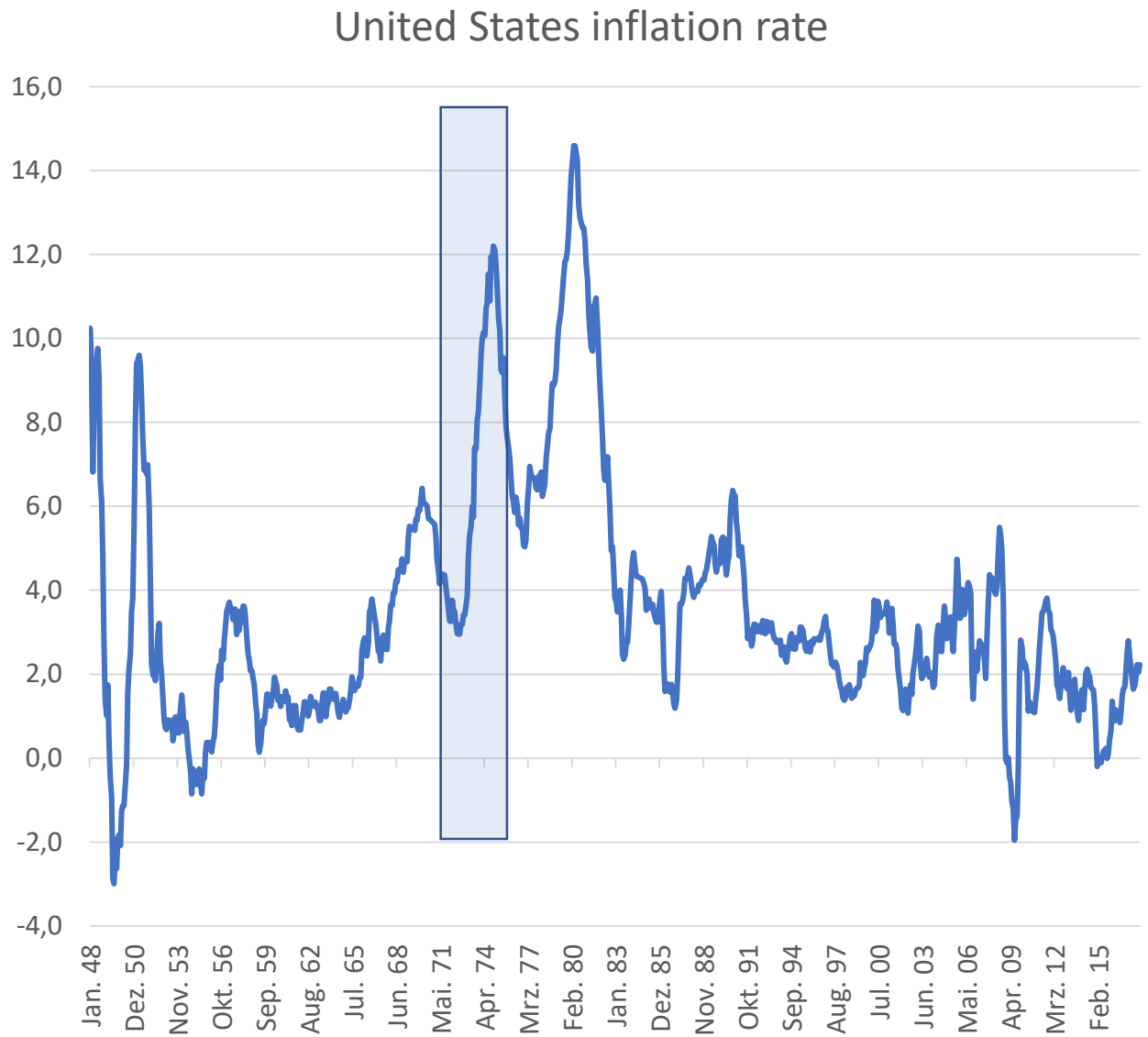
The vision of Friedrich A. von Hayek (1899-1992)

“Neither a general increase nor a general decrease of prices appears to be possible in normal circumstances so long as several issuers of different currencies are allowed freely to compete without the interference of government.”



Hayek: “A single monopolistic governmental agency can neither possess the information which should govern the supply of money nor would it, if it knew what it ought to do in the general interest, usually be in a position to act in that manner.“



Hayek‘s money: an early version of Libra?

- “I would announce the issue of non-interest bearing certificates or notes, and the readiness to open current cheque accounts, in terms of a unit with a distinct registered trade name such as 'ducat’.
- The only legal obligation I would assume would be to redeem these notes and deposits on demand with, at the option of the holder, either 5 Swiss francs or 5 D-marks or 2 dollars per ducat.
- This redemption value would however be intended only as a floor below which the value of the unit could not fall because I would announce at the same time my intention (…) to keep their (precisely defined) purchasing power as nearly as possible constant.
- “ (…) it seems neither necessary nor desirable that the issuing bank legally commits itself to maintain the value of its unit.”

Core insights by Hayek

"It seems to me to be fairly certain that

(a) money generally expected to preserve its purchasing power approximately constant would be in continuous demand so long as the people were free to use it,

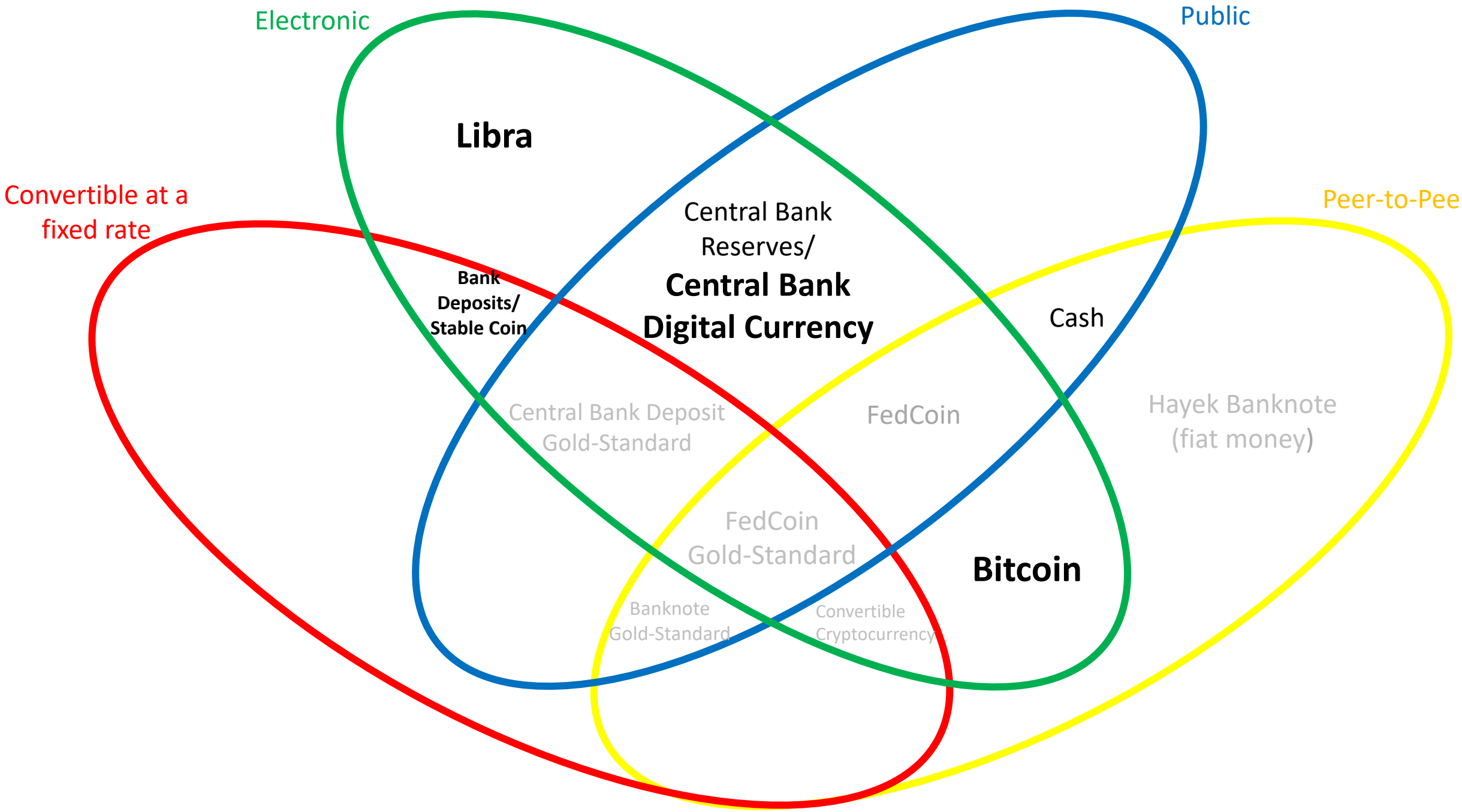
(b) with such a continuing demand depending on success in keeping the value of the currency constant one could trust the issuing banks to make every effort to achieve this better than would any monopolist who runs no risk by depreciating his money,

(c) the issuing institution could achieve this result by regulating the quantity of its issue, and

(d) such a regulation of the quantity of each currency would constitute the best of all practicable methods of regulating the quantity of media of exchange for all possible purposes

A taxonomy with four dimensions of „money“

- Privately issued money versus money issued by government
- Electronic money versus physical money
- Money with fixed-rate convertibility guaranteed by the issuer versus „fiat money“ with no convertibility commitment by the issuer
- Centralized accounting mechanism versus decentralized accounting mechanism (peer-to-peer)


Electronic
Public
Libra
Convertible at a fixed rate
Peer-to-Peer
Central Bank Reserves/
Central Bank Digital Currency
Bank Deposits/ Stable Coin
Cash
Central Bank Deposit Gold-Standard
FedCoin
Hayek Banknote (fiat money)
FedCoin Gold-Standard
Bitcoin
Banknote Gold-Standard
Convertible Cryptocurrency

What kind of money is Libra?

- Inconvertible: „**Fiat money**“ like bank notes and central bank digital currencies
- **Electronic** like bank deposits and central bank reserves held by commercial banks
- **Private** like deposits held with a commercial banks
- **Centralized accounting mechanism** like bank deposits

- Libra and also Bitcoin can be regarded as „base money“, as they do not provide a legal obligation of the issuer(s) to exchange them at a fixed rate into another asset

How is Libra created?

- Monetary base is typically created in transactions, i.e. by
  - Purchase of foreign assets (fx interventions)
  - Purchase of domestic assets (government or corporate bonds)
  - Loans to banks (refinancing policy)
- Libra is created by the purchase of established currencis („foreign assets“)
- Bitcoin and other cryptocurrencies are created in a mining process, i.e. without transactions. They can be regarded as a form of helicopter money

Is Libra a „stable“ currency?

- Libra is defined as a currency basket
- The currency basket of the Special Drawing Right

Currencies defining the basket	Fixed amounts of basket currencies (x)	USD exchange rate (on 25 June 2019) (y)	USD value of basket components (xy)	Relative weight of components (xy as % of USD basket value)
US-Dollar	0.58252	1	0.58	41.91
Euro	0.38671	1.14	0.44	31.61
Chinese Yuan	1.0174	0.15	0.15	10.64
Japanese Yen	11.9	0.01	0.11	8.01
Pound Sterling	0.085946	1.27	0.11	7.83
USD value of basket (25 June 2019)			1.39	100

Is Libra a „stable currency“?

- Exchange rate risk: Libra deposits are to a large degree FX-deposits
- Liquidity risk:
  - Libra holds its reserves in bank deposits (risk of bail-on in major banking crisis) and in government bonds (risk of losses in case of high sales
  - Risk that Libra is not accepted by stores in case of a „run“. It is not legal tender.
- Convertibility risk: Libra gives no binding commitment to convert its assets back into the public monies

Main areas of currency competition

- Functions of money
  - Money as an object
    - Means of payment
    - Store of value („safe asset“)
  - Money as a unit of account/unit of measurement
    - Numéraire: Unit in which absolute prices of goods are measured (temporal and intertemporal comparisons)
    - Standard of deferred payments: Unit in which the intertemporal value of a debt is measured
    - Standard for accounting: Unit in which the increase of the net value of a firm is measured

What makes currencies attractive?

- **Libra as global means of payment:**
  - Most payments are made within countries
  - With **electronic payments systems** the liquidity dimension becomes less relevant.
- **Libra as a safe asset:**
  - Stability in terms of the basket does not guarantee stability in terms of the national unit account. Inconvertibilty and liquidity risk
- **Libra as unit of account:**
  - **Hayek**: “I believe it would prove that **suitability as a unit of account** would rule the roost.”
  - It is unlikely that Libra will outcompete established currencies as unit of account
  - Some potential in developing countries. But in countries with unstable monetary systems the dollar is already well established as parallel currency.

Stability guarantees for the store of value function

	Libra	Euro bank deposits	Euro bank notes issued by ECB	Euro reserves held with the ECB
Convertibility obligation by issuer	No: fiat money	Convertible in euro bank notes	No: fiat money	No: fiat money
Legal Tender	No	No	Yes	No
Mechanisms to guarantee the stability of value	• Reserve holdings of the Libra association	• Banking supervision • Capital buffers	• Article 127(1) TFEU defines the ECB's primary objective to maintain price stability. • ECB has the monopoly over the issuance of euro monetary base • ECB is actively engaged to control the value of the euro with its monetary policy instruments and so far quite successful	
Risk of a total loss	High. No stabilization mechanism in a crisís of confidence	Limited by deposit insurance and lender of last resort function of ECB	Hyperinflation is very unlikely	

How a stable Libra would look like

- Libra gives a legally binding convertibility commitment for Libra deposits
- Libra holds its reserves in the form of central bank deposits (synthetic CBDC): model of Alipay
- Libra issues $-Libra, €-Libra, ¥-Libra, £-Libra. A global currency is not required for an efficient global payments system

Summary: Potential for Libra is limited

- Libra is a great business model for Facebook: It is neither equity nor debt.
- For users in advanced economies Libra is not very attractive:
  - Inconvertibility: No intrinsic value
  - Stability: As a currency basket Libra cannot be targeted to national price indices
  - No legal tender: Risk of full implosion impairs store of value function
  - Fundamental flaw: An effective global payments system doesn not need a global currency
- For developing countries with unstable domestic monetary systems Libra could be attractive.
- A truly stable Libra would be much less attractive for Facebook

Libra versus Bitcoin and traditional bank deposits

	Libra	Bitcoin	Traditional bank deposits (Money stock M1)
Issuing process	Purchase of established currencies	Mining	Credit creation
Supply	Fully elastic: Demand determined	Inelastic: Supply determined	Determined by supply (banks) and demand (borrowers)
Convertibility	Unclear	Inconvertible	Full convertibility into bank notes
Stability (store of value, safe asset)	Stable in terms of currency basket	High volatility	Stable in terms of the domestic unit of account
Liquidity	Facebook Community	Very limited	