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Cryptos and CBDC

Why in news?

The central bank must note that a Central Bank Digital Currency (CBDC) can only be a fiat currency and not a crypto.

What are crypto assets?

- A crypto asset is a digital asset; but not all digital assets are crypto assets.
- The distinguish features of crypto assets:
  - uses cryptography
  - depends on distributed ledger technology
  - no need for a third party such as a bank to issue crypto assets
  - have three primary uses: as an investment, a medium of exchange, and to access goods and services.
- Crypto assets are commonly known as cryptocurrencies such as Litecoin, Ripple, Bitcoin, and Ethereum.

What is CBDC?

- A CBDC is a legal tender issued by a bank in a digital format.
- Also known as digital base money or digital fiat currencies, a CBDC is no different from hard cash, apart from the fact that they are in a digital or virtual form.
- It is not meant to replace hard cash but coexist as an additional form of payment method.

What were the different stands taken on cryptos?

- **Finance minister**- In the Budget session, it was said that Cryptocurrency will be discouraged via taxation and capital gains provisions.
- **RBI Governor**- The Governor of the RBI highlighted that private cryptocurrencies are a big threat to our financial and macroeconomic stability.
- Also he said that these cryptocurrencies have no underlying asset.
- **Deputy Governor of RBI**- A Deputy Governor of the RBI called cryptos worse than a Ponzi scheme and argued against legitimizing them.
- **Supreme Court**- The Supreme Court of India has asked the Government whether or not cryptos are legal.

How do cryptos become acceptable as tokens for exchange?

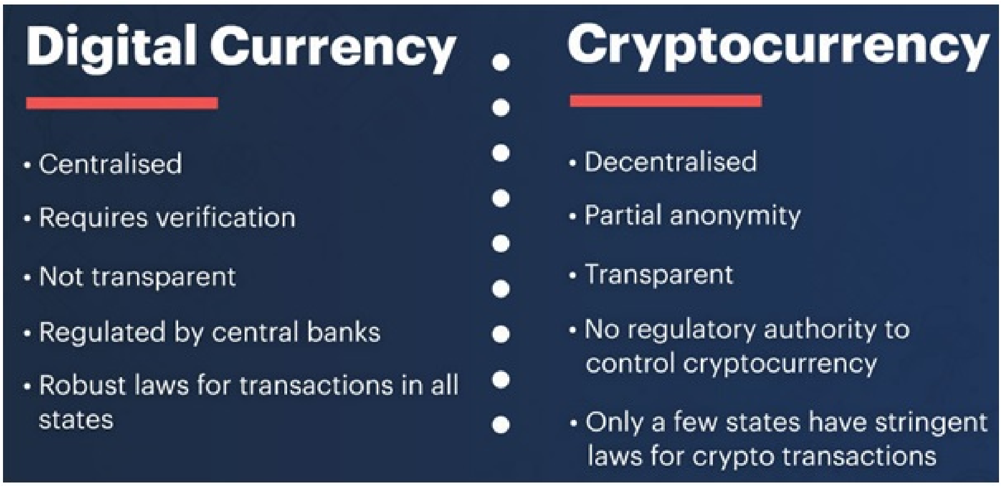
- A currency is a token used in market transactions.
- Historically, commodities (copper coins) have been used as tokens since they themselves are valuable.
- But paper currency is useless till the government declares it to be a fiat currency as it derives its value from state backing.

- Cryptos are a string of numbers in a computer programme and there is no state backing.
- Cryptos acquire value and can be transacted via the net which enables them to function as money.

Is it possible to ban cryptos?

- The total valuation of cryptos recently was upward of 2 trillion dollars which is more than the value of gold held globally.
- Cryptos which operate via the net can be banned only if all nations come together.
- Even then, tax havens may allow cryptos to function, defying the global agreement.

What is the difference between CBDC and cryptocurrencies?



What are the concerns of CBDC?

- Blockchain enables decentralisation where everyone on the crypto platform has a say but, central banks want a fiat currency to be exclusively issued and controlled by them.
- Theoretically everyone can 'mine' and create crypto unlike the centrally controlled CBDC.
- Solving the 'double spending' problem and being a crypto (not just a digital version of currency) seems impossible.
- A centralised CBDC will require the RBI to validate each transaction.
- CBDCs at present cannot be a substitute for cryptos that will soon begin to be used as money. This will impact the functioning of central banks and commercial banks.

Double-spending is the risk that a cryptocurrency can be used twice or more. It occurs when someone alters a blockchain network and inserts a special one that allows them to reacquire a cryptocurrency.

References

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