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CBDCs for Cross-Border Payments

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Most major economies and many emerging markets are conducting research or running pilot projects on central bank digital currencies (CBDCs). Digital central bank (CB) money has the potential to reduce costs and increase the speed and security of cross-border payments, but the pace of development is uneven. China is one of several markets that is piloting a CBDC but countries like the US and UK are unlikely to introduce their own CBDC for five to ten years. Greater dialogue, both between countries and between CBs and the private sector, can accelerate the development and successful use of CBDCs around the world. This note provides a summary of the key themes from the discussion, respecting that the conversation was conducted under the Chatham House Rule and comments are unattributed.

The opportunities of CBDCs are substantial. Companies around the world move more than $23 trillion across borders each year. They incur roughly $120 billion in transaction costs and wait two to three days, on average, for those deals to settle. According to a recent Oliver Wyman and JPMorgan Chase report, a multicurrency network of CBDCs could cut those costs by about $100 billion annually and eliminate delays, but that's just a first-order effect. CBDCs can catalyze innovation by the private sector to develop new offerings such as real-time payments services, intra-day swaps, and programmable payments. CBDCs may also become a tool for advancing national interests. China might use its e-CNY to promote wider use of the renminbi through trading partners in the Belt and Road initiative, while the European Central Bank has stated that a successful digital euro could increase the currency's global appeal. A variety of risks exists too, including cyber, political, reputational, and privacy.

Central banks should foster a broad dialogue to establish the right framework. Building a new cross-border payments infrastructure around CBDCs won't be quick or easy. The technology is developing rapidly, and the questions are myriad, ranging from how to govern the interaction of various national currencies to integrating CBDCs with private-sector stablecoins (SCs) to managing credit and liquidity risk. These all warrant active and broad-based dialogue across the public and private sectors. Policymakers should be looking to identify any no-regret moves that can make early progress without locking any undesired rigidities into the system.

Consider the function of commercial banks. Some CBs are reluctant to engage with the private sector or consider that it can provide related payments infrastructure, but that's short-sighted. It's unlikely that CB money will crowd commercial bank money out of the payments space, especially if CBs adopt low limits on CBDC transaction sizes. Commercial banks can play a major role in driving the adoption of CBDC cross-border payments among corporates, but they need to have a stake in developing the system and see real value in participating in it. The Bank of England offers omnibus accounts that allow commercial banks offering real-time gross settlement services to fund their customers' balances with CB money. Other CBs are considering allowing private firms to play a role as distributors of their CBDCs. Commercial banks can serve as market makers and liquidity providers, and drive innovation that continues to squeeze cost out of the system. Collaboration between the public and private sectors will produce the greatest benefits.

Assigning roles and responsibilities. The introduction of CBDCs will require clear coordination of the roles for both CBs and commercial banks and a system of governance that can address issues like who is responsible in the case of a cyberattack, and what's the minimum frequency of transactions you want to have as you transition to CBDC payments. Following a decentralized model like SWIFT's, where firms are responsible for their own infrastructure and onboarding processes, would build flexibility into the system.

Put interoperability at the center of efforts. Given the fragmented state of the current market, the uneven pace of CBDC adoption, and the plethora of private-sector instruments, the evolving payments system is likely to be very diverse. Wholesale CBDCs may dominate large cross-border transactions while SCs and other private instruments handle mostly retail transactions like remittances. Nothing is fixed yet, but the pace of development is expected to accelerate, with India's plan to launch a CBDC in 2023 likely to create critical mass alongside China. That makes it critical for public and private sector actors to make interoperability a key element of their design process so that all the pieces of the puzzle can work together. The more fragmented these systems, the less incentive for developed economies like the US and UK to speed up development.