Europe: Towards Digital Dollarization?

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"You will unleash an explosion of economic growth and with the dollar-backed stablecoins, you will help expand the dominance of the U.S. dollar in many, many years to come."

– Donald Trump, Blockworks Digital Asset Summit, March 20, 2025

Digital Money Landscape

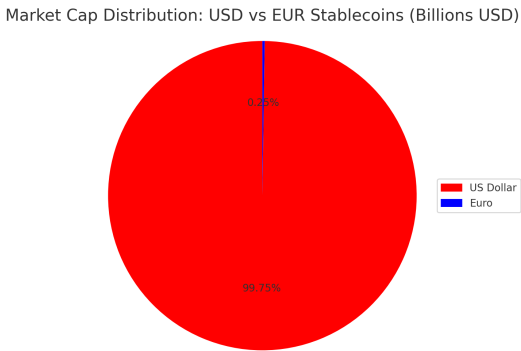
	US	**Europe**
Private Digital Money	Lightly regulated stablecoins (Legislation in progress, STABLE and GENIUS)	MiCA-compliant stablecoins (EU-level laws, e.g., MiCA effective from June 2024 for stablecoins)
Public Digital Money	No CBDC allowed	Digital Euro (CBDC) (Legislation facing challenges)

Distinct US vs. EU Stablecoin Regulatory Approaches

Aspect	US (Proposed)	EU (MiCA - In Force)
1. Issuer Scope	Primarily US-based; potential gaps for offshore.	Broad: EU presence/currency peg.
2. AML	limited new powers beyond.	Can block non-compliant.
3. Level	Mix state/federal licensing.	Single EU rulebook; EBA.
4. Conglomerates	Fewer specific rules on parent companies/affiliates.	'Significant' issuers (e.g., Big Tech) tougher oversight.
5. Insolvency	Tweaks bankruptcy laws; no special resolution fund.	Pre-failure safeguards (reserves, wind-down).
6. Cons. Prot.	Ensures backing; less detail.	Disclosure, redemption, liability.
7. Interest	Debated.	No

Table: Source for US: Atlantic Council, Massad, Jackson, and Awrey (Apr. 2025).

Stable Coin USD Share



The Appeal of USD Stablecoins in Europe

Despite currency risk, dollar stablecoins offer advantages:

- **Market Dominance:** USD stablecoins vastly larger ($>$\$200B vs. 0.6B for EUR stablecoins) $\rightarrow$ higher liquidity, lower transaction costs.
- **Regulatory Environment (US):** Currently less restrictive, potentially allowing faster innovation and expansion (though with higher risk).
- **Network Effects:** Dominant in crypto trading, DeFi, and increasingly for international B2B payments priced in USD.

However, MiCA hurdles and currency risk make EUR options more practical for many Eurozone users.

The Specter of Digital Dollarization in Europe

ECB fear that widespread adoption of USD stablecoins in Europe would mean:

- **Weakened Monetary Policy:** ECB's ability to manage Eurozone economy diminished if transactions bypass the euro system.
- **Financial Stability Risks:**
  - Currency mismatches for households/businesses (earn EUR, pay in USD stablecoins).
  - ECB cannot be lender of last resort for USD instruments.
- **Erosion of Monetary Sovereignty:** Reduced control over payments, increased dependence on US financial infrastructure.

Proposed Solution: Digital Euro

The Digital Euro: Goal vs. Reality

Ambition: Monetary Autonomy

- Essential for Europe's sovereignty.
- A public, safe, efficient digital payment method.
- Counterbalance to private digital currencies and foreign CBDCs.

Reality: A Compromised Design

- Intense bank lobbying $\rightarrow$ fear of deposit disintermediation.
- Result: Severe functional limitations imposed.
- *Designed to be weak*

Like designing a new car but limiting it to 30 mph to protect existing taxis.

Key Limitations Imposed on the Digital Euro:

- No interest on holdings (*unlike bank reserves at ECB*).
- Strict holding caps for individuals (e.g., 500-€3,000 suggested).
- Mandatory linkage to bank accounts for funding/overflow.
- Merchant can process, but not hold Digital Euros.

ECB's Rationale Preserve "Financial stability, "Economic function of commercial banks.","Corporate deposit base."

But historically, central banks accepted private deposits.

- Why are citizens different now?

The Core Question

Are these limitations proportionate, or do they render the Digital Euro uncompetitive by design to shield incumbent banks from disruption?

Is the System Worth Such Protection?

Traditional Bank Justification: Maturity Transformation

Functions Increasingly Unbundled

- Non-banks: 55% of U.S. mortgages.
- Private credit funds: \$2T+ AUM.
- Fintech (e.g., Stripe) leads payments.
- Specialized funds in corporate lending.

Enduring Feature: Fragility and Runs

- High leverage (90% debt financed).
- Susceptibility to runs (SVB...).
- Ever-larger state guarantees & bailouts.
- E.g. current CRE exposure masks significant risks for many banks.

ECB/EC Choice

Digital Euro could offer stability, but current design defers to a fragile system.

The Digital Euro's Impossible Dilemma

The ECB is trying to:

1. Make Digital Euro restrictions tough enough to protect banks.
2. Make Digital Euro attractive enough for public adoption.

This is likely an unwinnable trade-off:

- A heavily restricted Digital Euro $\rightarrow$ Low adoption.
- May struggle against MiCA-compliant EUR stablecoins and dominant USD stablecoins (offering remuneration, no caps).
- Result: Preserving weaknesses of the old system without gaining benefits of the new.