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Bank of Japan

What to Know about Central Bank Digital Currency

Remarks at the FIN/SUM 2024

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(English translation based on the Japanese original)

Introduction

I am delighted to be given this opportunity to speak to you at the FIN/SUM 2024.

Today I will be talking about Central Bank Digital Currency, often abbreviated as CBDC. CBDC is a pivotal topic for central banks. Regardless, the results of the Bank of Japan's *Opinion Survey on the General Public's Views and Behavior* for September 2023 show that when asked about their familiarity with the term CBDC, less than 20 percent of respondents answered "have read or heard of it, but do not know much about it" while merely 3.1 percent responded "know about it." While I am aware that many of those present today may already have a thorough grasp of this subject, I will walk you through the topic in everyday language.

Differences between CBDC and Existing Digital Payment Instruments

In Japan, a wide array of cashless payment instruments, including credit cards, e-money, and QR code payment, are in use. How do CBDCs differ from such existing digital payment instruments? Retail CBDC, assuming a wide range of users, which include individuals and firms, has been explored in many countries, including Japan, on the premise that this would align with cash -- in other words, banknotes and coins -- in terms of their roles and functions as a means of payment. The key features of cash would therefore serve as a gateway for considering the differences between CBDC and existing digital payment methods. Broadly speaking, there are three such features.

First, cash is a direct liability of the central bank. This is in sharp contrast to existing digital payment methods, for which payment is made with liabilities issued by private entities, including banks and payment service providers.

Second, a cash payment becomes final at the point in time where the payee receives the cash from the payer. Put differently, immediately upon receipt of cash the payee can reuse it for other payments. For most digital payment instruments used for consumer-to-business payments, on the other hand, there is a time lag of days before merchants receive the money through a bank transfer or other means.

These features bring us to the third point, that is, we use cash on a daily basis and with a sense of confidence. Cash is available for anyone to use, whenever and wherever it is needed.

Differences between CBDC and Cash

While CBDC is being explored on the assumption that it will possess the features of cash that I have just described, there is, in fact, a stark difference between the two, namely, in terms of tangibility. Specifically, whereas cash is a tangible asset and comes in physical form, such as paper and metal, CBDC is intangible, with information on the amount and holder provided in the form of electronic data. This intangible feature is a crucial point in considering the differences between CBDC and cash. Let me raise three key characteristics of data in this regard.

First, the use of data transcends space. While cash requires the payer and payee to physically coexist in the same place, no such restrictions are placed on data usage, allowing for the use of CBDC in a wider variety of settings, such as online shopping.

Second, data does not take up any physical space. Storing a large amount of cash requires securing enough storage space; this is never the case when it comes to data. While this may appear convenient in the eyes of the user, it is also important to take into account how digitalization's removal of such inconvenience in handling cash could affect the relationship between money issued by the central bank and money issued by private entities.

Money has evolved over the course of history. The modern era has seen the establishment of a two-tiered system with regard to the supply of money. The central bank, underpinned by its confidence, exclusively provides the public with base money -- in other words, banknotes and central bank deposits. Commercial banks then provide individuals and firms with deposits through credit creation based on central bank money. As part of this process, developments in the banking supervisory mechanism and the framework of protection provided by deposit insurance, for example, have helped secure a system in which the values of various forms of money, such as bank deposits, and cash are equal -- in other words, a situation where "one yen is one yen" is maintained. While such a system serves as an effective means of supplying money widely throughout society, the advantage of commercial banks --

skilled in gathering and analyzing information on borrowers -- lending and providing deposits to individuals and firms, is that financial resources are efficiently allocated through private-led initiatives.

In many countries, including Japan, the idea prevails that securing a two-tiered system with the kind of advantages that I have just mentioned is also preferable when implementing CBDC. At the same time, because CBDC, unlike cash, does not take up any physical space, there is concern that a sudden and large-scale flow of funds from deposits to CBDC could have an excessive impact on the two-tiered system. As a preemptive measure, many countries have been considering putting in place a safeguard, for example, by imposing a ceiling on users' CBDC holdings.

Third, the use of data leaves digital footprints. This feature generates opportunities to leverage data, a characteristic not observed in cash. Such opportunities carry the potential of bringing about enhanced convenience for consumers and growth through creation of new values. This has also shed light on the growing importance of networks that coexist with payment services, such as e-commerce and social networking sites.

At the same time, we must be aware of privacy-related concerns that this would give rise to. Of course, being able to effortlessly conduct payment that transcends space -- which I touched upon earlier -- means that this could increase room for illicit financing such as money laundering. This calls for the need to consider countermeasures. With this in mind, it is essential to design a framework in which privacy protection is ensured through such measures as minimizing the amount of data accessible to the Bank of Japan.

Points Considered in Exploring CBDC

Whether to issue a retail CBDC in Japan should be decided by discussions among the public. To facilitate such discussions, the Bank has been proceeding with technical experiments and explorations into institutional arrangements. In doing so, the following three points are borne in mind at all times.

The first is to visualize and shape our future. While CBDC continues to be explored by many countries as one of the realistic options being laid out, the goal of these future discussions is to design payment and settlement systems that are suitable for a digital society, taking into account external factors such as the introduction of novel technologies and new forms of money including stablecoins. In doing so, it is necessary to consider, with a well-balanced perspective that takes into account both global and domestic circumstances, potential problems that could eventually arise even if we do not face an immediate problem at the moment.

Second, there is a need to respect the various functions that cash and the two-tiered system, which I have mentioned, have provided society with. To give an example, it is vital for CBDC to be designed in such a way that users' privacy would be preserved, showing respect for their lives as people. Similarly, the sharing of roles between central bank money and private money as well as private firms' capacity for resource allocation and innovation should also be valued.

Last but not least, the digital features of CBDC carry the potential to create diverse values. How should we utilize CBDC to empower people and firms, and ultimately establish a new ecosystem, which would be brought about by CBDC adoption? Exploring CBDC from such a perspective is equally important.

Closing Remarks

The main theme of this year's FIN/SUM is "Building a Bright Future: Fintech for Happy Growth." Underlying this is said to be the hope for and determination to build a better future by striking the right balance between (1) stable and sustainable economic growth and (2) people's happiness, while effectively utilizing novel technologies.

The Bank of Japan has been proceeding with the pilot program for CBDC -- my topic today -- since 2023. We continue to engage in various efforts to envision the future of the overall payment system, including a panel discussion on the future landscape of wholesale payments scheduled to take place here tomorrow. For these efforts to serve as channels to "happy growth," it is essential that we continue with our dialogue, as drawing on your experiences and wisdom is key to this bright future. We therefore kindly ask for your support as we pave

the way forward.

Thank you for your attention.