Are Crypto-Currencies About to Replace Fiat as National Currency and the Key to Anti-Money Laundering?

In his bestselling book The Brief History of Mankind, historian Yuval Noah Harari discusses the origins of money. He describes how around 3000 B.C., Sumerian Barley money was first introduced as a mean for trading. Half a millennium later, humans in Mesopotamia developed enough trust in each other to use the Silver Shekel, probably one of the earliest forms of cash known to date. Harari concludes, "*Money is accordingly a system of mutual trust, and not just any system of mutual trust: Money is the most universal and most efficient system of mutual trust ever devised. Even people who do not believe in the same god or obey the same king are more than willing to use the same money. Osama bin-Laden, for all his hatred of American culture, American religion, and American politics, was very fond of American dollars*."

Five millennia later humankind is on the precipice of making a dramatic shift from traditional fiat currency to digital money, by using Blockchain based crypto currencies. Thus, raising the question whether crypto-currency proves trustworthy enough to be considered for integration as a national currency by sovereign states? The answer may very well be: if it's cost- effective, in crypto-currency they will trust.

The key to crypto-currency's widespread use is not so different from what the Silver Shekel had been used for successfully: trust. Through its core technology, Blockchain, crypto-transactions are validated by other computers, run by 'miners', who account for every element of the transaction. Once a miner's computer solves the algorithm and publishes the verification results on a public ledger, multiple computers "check the math" and validate the transaction as well. In this sense, the element of trust is compounded upon within the system. And that's good news, as the world is faced with a number of hard-cash challenges that crypto-currency might help overcome.

Where fiat currency once played a dominant role in the world's economy, today its function has not only shrunk, it has become expensive to maintain. Aside from the significant funds governments spend fighting cash-counterfeit vis-à- vis watermarks and other paper-based improvements, printing money, counting it, guarding it, etc. can cost countries up to 1% of their GDP a year. Cash in circulation also increases the costs of enforcing Anti-Money Laundering (AML) and Anti-Terrorist Financing regulation because it is barely traceable, and therein, by default, funds most illegal activity. Due to these aspects and the fact that around 90% of fiscal transactions today are already in electronic-network form (for example, SWIFT), countries like Sweden, Denmark, Spain, Italy and France, and their respective central banks, have declared a silent war on cash, discouraging its use by capping the legal amount at which a transaction can be made in hard-currency, withholding banking services for increasingly smaller amounts of money or limiting the branches where cash deposits can be made.

The advantages and potential solutions which crypto-currency offers these centralized-fiat issues necessitate the possibility of integrating a nationalized crypto-currency. The decentralized structure of crypto-currency eliminates the need of a middleman and therefore diminishes transaction costs. In parallel, it protects the privacy of its users through end-to- end e-wallet transactions that do not compromise personal information. Yet, it still enhances AML-purposed surveillance due to Blockchain's public ledger and validation mechanism, which is subject to an enforceable protocol. On a grander scale, crypto-tech is simply more fitting for a globalized economy. A trend towards multi-nationalized crypto-currency could reduce transaction time and eradicate foreign exchange rates. With the free flow of digital currency across state lines smaller and developing economies may also find it easier and cheaper to be part of the global financial economy, and their citizens would not be barred from participation simply because they cannot afford to keep a bank account or lack the infrastructure to do so.

As such, it comes as no surprise that governments are seriously considering the benefits of national crypto-alternatives. Tunisia already picked up the gauntlet, being the first to launch a nationalized digital-currency, the eDinar, which it recently announced will be replaced with a Blockchain-based improvement. The Central Bank of China (People's China Bank) announced their intention to introduce a prototype state-crypto currency to compete alongside their national hard-currency, the Renmibi or Yuan. Canada has been experimenting with a blockchain-backed version of its national currency, called CAD-Coin. And other central banks, such as that of Russia and South Africa, have released similar statements about testing nationalized crypto-currencies.

However, this upswing in multi-national interest does not mean the road to nationalized crypto-currency is free of its own challenges. To start, there is an inherent tension between the decentralized feature of crypto currencies and the authoritarian nature of governments. If trust is at the heart of using currencies, distrust of how authorities may take advantage of Blockchain technology could become an obstacle to its adaption. Furthermore, governments would have to invest in educating citizens on how to use digital currency, and also clean up the bad reputation the primary crypto-currency, Bitcoin, has earned thanks to fiascos like Mt. Gox, The DAO, Bitfinex cyber-attack and others. These public education and branding campaigns would have to be backed by developing tangible increased cyber security capabilities and advanced standards to increase consumer confidence.

The road to novelty is never free. However, as the globe gets more interconnected, traditional fiat currency loses its justification and costs countries, and citizens alike, a pretty penny. Governments would do well to curb transition costs now, by focusing on built-in crypto-issues and solving them on a nationalized or even internationalized level, such as AML standards and increasing tradability capabilities of crypto-currencies. Predicting that 5000 years of using coins and bank notes is about to end is hardly a revelation, it's pure logic. Figuring out how to make it the most cost-effective transition for humankind is genius.

By Roy Keidar and Tal-Or Cohen of Yigal Arnon & Co.