

## STABLECOINS AND THEIR SPECIFIC FEATURES

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### ABSTRACT

The study provides an in-depth analysis of the nature of virtual currencies and the distinguishing features and types of stablecoins as one of them, as well as the factors that distinguish them from other virtual currencies. Then the similarities and differences between stablecoins and traditional currencies has been shown and the essence has been explained with examples. At the same time, the essence of the Central Bank Virtual Currency (CBDC) has been explained, its differences with stablecoins have been shown, and the possibility of using stablecoins in the banking system has been identified. In addition, the experience on stablecoins in United States, the United Kingdom, China and Thailand, as well as the international card organization VISA, has been studied, and it has been determined whether stablecoins should be regulated by the state. At the end, the final findings of the research and our conclusions have been reflected in the results section of the research.

**Key word:** stablecoins, traditional currencies, banking system, digitalization, virtual currencies

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### INTRODUCTION

Over the past few decades, global trends in digitalization and the transfer of databases to the financial sector have led to the joint development of finance and technology. There have been significant changes in digital innovation in the financial sector, driven by rapidly evolving technologies, especially information and communication technologies in the 2010s.

These innovations have affected not only financial services such as payments, credit, investment and insurance, but also money itself, which is the basis of the financial system (BIS, 2018; 2020). The Covid-19 crisis has accelerated the transition to digital payments. It has raised public concern about the transmission of the virus in cash and led to an increase in the use of digital payments. For central banks and regulators, these challenges are particularly important in achieving their financial and monetary stability. Today, authorities around the world are struggling with the rise of digital currencies and decentralized finance based on emerging technologies, especially various combinations of distributed ledger technology (DLT) and blockchain, and advances in traditional centralized financial support systems. Many claim that there has been a technological revolution in money and payment systems (Arner et al., 2020).

In current policy discussions, stablecoin can be defined as a cryptocurrency that aims to maintain a fixed value relative to a particular asset or asset pool or basket (FSB, 2020). Stablecoins based in the same space as bitcoin and other cryptocurrencies because they are electronic, can be exchanged between peers, and are not issued by central banks. Stable coins are token-based; their validity is verified based on the token itself, not on the identity of the other party, as in account-based payments (Kahn, 2016).

The idea of stablecoins is not entirely new. Prepaid cards and money market funds also offer some similarities, such as various forms of mobile money, with electronic or “electronic money” discussions dating back to the 1990s. However, DLT has enabled the creation of new digital money forms and payment systems that can serve new purposes and expand some well-known economic and regulatory issues related to past innovations into the digital world. Existing stablecoins such as Tether, USD Coin and Maker’s Dai aim to serve as a means of settlement for automated financial products. They also offer “smart” contracts, ie self-executing code and “programmable money” opportunities.

The main focus of the article will be on the objectives of creating stablecoins as a virtual currency, its differences with traditional currencies, the characteristics that combine stablecoins with central bank virtual currency, the possibilities of its use as a means of payment and its regulation by government in international practice.

## **WHAT ARE STABLECOINS?**

There are different types of virtual currencies in the world today. One of them is a stablecoin. Before looking at the nature of stablecoins, let's look at the essence of virtual currency in general. Virtual currencies are available in two types of schemes: centralized and decentralized.

Centralized currency schemes preceded decentralized currencies. Centralized currencies have a central depository and are usually managed and controlled by a single entity. Decentralized currencies do not have a single depository center and are issued and operate in a decentralized manner. Centralized virtual currencies rely on third parties to create new virtual currencies, verify transactions, and manage the accounting of the account. Decentralized systems refer to systems that do not have a central governing body (for example, the Central Bank) and virtual currencies are not issued from a single center (Khayaladdin Tagiyev and Aysel Hasanli: 2018, BIS November 2020: Stablecoins-risks, potential and regulation).

Decentralized virtual currencies operate on the basis of blockchain or distributed ledger technology (DLT). Blockchain technology is an innovative platform that enables transactions in payment systems, clearing and settlement, especially in e-Government systems, using procedures and protocols. DLT is an architecturally decentralized network environment that does not require the involvement of intermediaries to verify and authorize transactions. All payment transactions are crypto-protected, and as they enter the DLT network, a direct (Peer-to-Peer) connection is established between the beneficiary and the issuer without intermediaries.

Stablecoin is a type of cryptocurrency that is backed by assets such as any country's national currency or gold and is designed to provide more stability than other cryptocurrencies. There are several types of stablecoins (European Central Bank November 2021, BIS November 2020: Stablecoins-risks, potential and regulation):

1. Fiat-backed stablecoins;
2. Crypto-backed stablecoins;
3. Commodity-backed stablecoins;
4. Algorithmic stablecoins.

Stablecoins backed by the national currency are the most common type. Unlike other cryptocurrencies with sharp fluctuations in value, stablecoins supported by the national currency are subject to very small price fluctuations. However, this does not mean that these types of stablecoins are completely safe, they are relatively new in the market and caution must be exercised in investing because there is not enough information about the risks.

Volatility is high in crypto-backed stablecoins. For example, a \$1 crypto-backed stablecoin may be tied to an underlying crypto asset worth \$2, so if the underlying crypto loses value, the stablecoin has a built-in cushion and can remain at \$1.

Stablecoins backed by precious metals maintain their value, relying mainly on gold and other precious metals. These stablecoins are centralized, and some crypto users may see this as a drawback, but this feature protects them from volatility in the crypto market.

Algorithmic stablecoins are not supported by any asset, which makes it difficult to accept it as a stablecoin. These types of stablecoins use a computer algorithm to keep the coin's value from fluctuating too much. If the price of an algorithmic stablecoin is pegged to \$ 1, but the value of the stablecoin rises higher, the algorithm would automatically release more coins into circulation to lower the price. If the price falls below \$ 1, the algorithm would reduce the supply and bring the price to the previous level.

### **WHAT IS THE DIFFERENCE BETWEEN STABLECOINS AND TRADITIONAL CURRENCIES?**

Cryptocurrencies and traditional currencies have two main features: they provide unimpeded payments between the two parties and act as an expression of value. Traditional currencies, are straightforward. You can spend the traditional money in cash or transfer it to your debit or credit card. Traditional currencies can be used for direct purchases, money transfers, payment of invoices, taxes, etc. Most of the existing traditional currencies are used only for domestic payments. When spending abroad, you need to convert them into other currencies. In these transactions, an exchange fee is usually applied. Although the commission for the exchange is not specified, there is always an exchange rate margin, which is the difference between the rate at which banks and currency exchange services trade and the rate offered to consumers (Pay Space Magazine July 2021, Nikkei Asia July 2021, Bank of Thailand: Press Release No. 16/2021).

As for cryptocurrencies, they also offer features that the traditional monetary system cannot currently offer: cryptocurrencies can be spent and received by anyone, anytime, anywhere in the world, and without the need for a bank or government. This is the most revolutionary aspect of cryptocurrencies. Stablecoins can also be used for daily shopping at traditional outlets.

With multi-currency wallets, you can quickly convert crypto into traditional money. For example, Trust Wallet, one of the most popular multi-active crypto wallet, allows you to spend your stablecoins by converting them into traditional money and cashing them out. In 2019, the BitPay wallet program announced the introduction of stablecoin payments for traders and consumers around the world. Some crypto ATMs, such as Instacoin in Canada, support cashing out of the most popular stablecoins in selected locations.

On the other hand, stablecoins are not accepted everywhere. The possibility of using them depends on national policies and regulations. Some countries completely ban cryptocurrency, while others promote its use regularly.

In addition to using it for daily trading, stablecoins can be traded on crypto exchanges. Some exchanges allow you to lend your stablecoins and earn interest. There are both fixed and flexible lending models, as well as person-to-person (P2P) crypto credit markets. Stablecoins currently offer the highest interest rates on most exchanges between 5% and 25%. There are many opportunities to earn income on fixed assets, and they will expand as the DeFi (Decentralized finance) system continues to grow (Romain Dillet March 2021).

### **WHAT IS THE DIFFERENCE BETWEEN STABLECOIN AND CENTRAL BANK DIGITAL CURRENCY (CBDC)?**

The Central Bank Digital Currency (CBDC) is a digital expression of the official currency of any country. The CBDC facilitates the implementation of monetary and fiscal policies and promotes financial inclusion in the economy. The main difference between CBDC and stablecoin is that the CBDC is issued by the country's monetary policy-making body or the central bank, while the stablecoin is issued by a private organization (Business Insider India December 2021, European Central Bank November 2021).

Digital currencies backed by the central bank, such as the potential digital euro and the digital yuan, could become a reality in the coming years. Unlike cryptocurrencies like Bitcoin and Ethereum, these currencies promise less volatility and more security. In addition, they will have the support of relevant monetary institutions responsible for ensuring financial stability.

### **INTERNATIONAL EXPERIENCE WITH STABLECOINS**

The experiences of the UK, China, the United States, Thailand and the international card organization VISA on stablecoins have been studied (Berkshire Hathaway Company March 2021, Bank of Thailand Press Release No. 16/2021, Central Bank of France 2019, Bank of England 2021, Romain Dillet March 2021).

Bank of England's Financial Policy Committee's stablecoin expectations inform the design of regulation for stablecoins. The expectations aim to ensure the safety of stablecoins as an alternative to both existing payment systems and commercial bank money. To meet these expectations, a regulatory framework would need to be clearly established before a stablecoin could safely operate in the UK.

Establishing a secure and clear regulatory environment for stablecoins to operate within the UK would also lay a clear foundation for sustainable innovation and allow consumers to safely realise the benefits they may offer.

Her Majesty's Treasury propose to bring systemic stablecoins into the Bank's regulatory remit, in line with its responsibilities for systemic payments systems under the Banking Act of 2009. This is outlined in HMT's recent consultation on the UK regulatory approach to cryptoassets and stablecoin. The legislative changes to be made by Parliament in order to implement the outcomes of this consultation are vital to ensure the Bank and other UK authorities have the necessary remit and powers to fully regulate stablecoins both in line with the risks they pose and under the principle of 'same risk – same regulatory outcome'.

China's central bank warned that digital coins, a stable currency, pose a serious risk to global financial systems, and that China's digital yuan has no problems. Officials of the People's Bank of China say digital currencies issued by private entities, including stablecoins, have been used as speculative tools threatening financial security and social stability as payment for illegal activities and money laundering. Officials say the Chinese government has already taken some steps to limit the expansion of global stablecoins in the country.

Stablecoins are also used in the United States. Examples include USD coin and Tether. However, as their activities are not regulated by any legislation, the US government, especially financial regulators, have stated that they are preparing to take appropriate steps to prevent the risks that the use of stablecoins could pose to the financial system. But before all these steps, they would urge Congress to pass comprehensive legislation that would control the form of the digital currency. Bank of Thailand is taking steps to legalize illegal foreign currency-backed stablecoins, asset-backed stablecoins and algorithmic stablecoins.

The BOT oversees risks associated with e-Money, such as settlement, money laundering cybersecurity and consumer protection risks. Therefore, those wishing to provide services involving Baht-backed stablecoins are required to consult with the BOT for consideration before beginning any operations. This policy is in line with the regulatory guidelines in many countries, such as the United Kingdom, Singapore, and Japan.

As for other forms of stablecoins including foreign currency-backed stablecoins, asset-backed stablecoins, and algorithmic stablecoins that are not illegal, the BOT is open to receive comments and feedback before considering regulatory guidelines as appropriate.

On March 29, 2021, Visa International Card Organization announced that it will allow customers to make transactions with USD Coin (USDC), a stablecoin fixed at 1:1, and became the first large payment network to use cryptocurrency to make payments. This step is a bigger step in bringing cryptocurrencies into the main financial position.

Visa is partnering with Anchorage, a digitally active bank, and Crypto.com, a cryptocurrency exchange platform, to conduct transactions over the Ethereum network for the pilot program. The payment giant plans to add more partners later this year. The project is the result of an 18-month project launched in 2019.

The move aims to facilitate transfers between digital assets and fiat currencies without incurring any extra fees, reflecting increased interest in the crypto space, especially from crypto-native FinTechs. Cuy Sheffield, Head of Crypto at Visa, said: “we see increasing demand from consumers across the world to be able to access, hold and use digital currencies”.

Visa’s pilot program eliminates the need for cryptocurrency platforms to convert digital currencies into traditional fiat currency before settling transactions with Visa. The fiat-denominated cryptocurrency USDC will, as such, be treated like any other the other 160 fiat currencies Visa clears and settles. This enables crypto-native companies to settle transactions with Visa without having to maintain a traditional bank account. This reduces complexity, speeds up the process, and reduce transaction costs. Visa is already partnering with around 35 digital platforms, including Coinbase, Bitpanda, and Crypto.com, all of which have more than 50 million active users.

Bridging the gap between digital and traditional fiat currency payment networks is essential for cryptocurrencies to become a widely accepted payment method used by consumers. Visa’s pilot program will facilitate a more widespread use of digital currencies.

The value of Bitcoin, Ethereum, and other cryptocurrencies rose after Visa said its payment network would use USDC to settle transactions.

## CONCLUSION

Stablecoin is a type of cryptocurrency that is backed by assets such as country's national currency or gold and is designed to provide more stability than other cryptocurrencies. There are types of stablecoins that are backed by the national currency of any country, supported by crypto assets, backed by precious metals, and algorithmically. Each of them has specific features. Stablecoins can also be used for daily shopping at traditional outlets.

With multi-currency wallets, one can quickly convert crypto into traditional money. For example, Trust Wallet, one of the most popular multi-active crypto wallet, allows to spend your stablecoins by converting them into traditional money and cashing them out. On the other hand, stablecoins are not accepted everywhere. The possibility of using them depends on national policies and regulations. Some countries completely ban cryptocurrency, while others continue to promote its use. In addition to using it for daily trading, stablecoins can also be traded on crypto exchanges. Some exchanges allow you to lend your stablecoins and earn interest.

The main difference between the CBDC and the stablecoin is that the CBDC is issued by the country's monetary policy body or the central bank, while the stablecoin is issued by a private organization.

The experiences of the UK, China, the United States, Thailand and the international card organization VISA on stablecoins have been studied.

The UK Treasury is proposing to include stablecoins in the Bank of England's regulatory framework in line with its obligations under the Banking Law regarding systematic payment systems. This is stated in the last consultation of the Ministry of Finance on the regulatory approach to cryptocurrencies and stablecoins in the UK. People's Bank of China states that digital currencies issued by private entities, including stablecoins, have been used as speculative tools threatening financial security and social stability, and serve as payment for illegal activities and money laundering.

Stablecoins are also used in the United States. Examples include USD coin and Tether. However, as their activities are not regulated by any legislation, the US government, especially financial regulators, have stated that they are preparing to take appropriate steps to prevent the risks that the use of stablecoins could pose to the financial system. The Central Bank of Thailand is taking steps to legalize illegal foreign currency-backed stablecoins, asset-backed stablecoins and algorithmic stablecoins. On March 29, 2021, Visa International Card Organization announced that it will allow customers to make transactions with USD Coin (USDC), a stablecoin fixed at 1:1, and became the first large payment network to use cryptocurrency to make payments.



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