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market notes: Once Upon a Time… There Was e-Gold

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Marcel Kasumovich
Coinbase Asset Management

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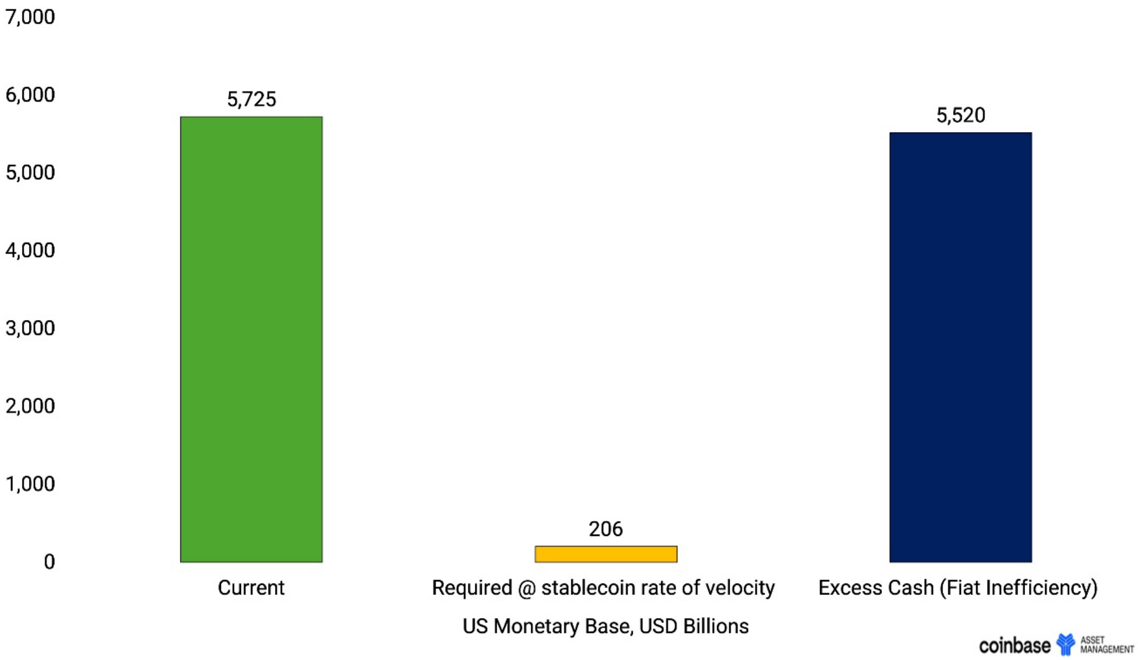
Figure 1: The Faster Money Moves...the Less You Need to Hold



Source: Federal Reserve Board of Governors. Coinmarketcap.com. CBAM Calculations. Velocity is transactions over the stock of money. Stablecoin is the trading volume of the top five fiat-based US dollar assets in the 24-hour period ending June 28, 08:00ET. The velocity of the US monetary base is 4.94-times ($28,269 billion in annualized nominal GDP divided by $5,723 billion monetary base). The velocity of US dollar stablecoin is 137.5-times ($20,400 billion in annualized transaction volumes divided by $148 billion in top-five fiat stablecoin assets).

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6/28/24 - Marcel Kasumovich, Deputy CIO, Coinbase Asset Management

1. "Make the numbers dance on the page, dammit." It's my inner voice of frustration when my fingers hit the keyboard to the old habit of academic mumbo jumbo. Start over, old friend. Guarav, a security guard, inspires me, endearingly questioning whether the person in the passport is the one standing before him. He suggests that precious metals may be better for my welfare. Precious! e-gold is a precious story...and a highly relevant one. (Thank you for listening, Gaurav.)

2. Moving financial value at internet speeds became patently obvious as the world moved online. e-gold was the brainchild of Douglas Jackson, a doctor by trade and a passionate student of monetary history. In his mind, the inability of central banks to achieve financial stability argued for a "Free Banking" world, where money is preserved by a real asset—like gold. After all, there are plenty of instances where people discard paper money like tissue. No one leaves gold curbside.

3. The idea was obvious, but somebody had to do it. Douglas Jackson was Mr. Somebody. And e-gold worked, delivering a 24/7 payment system that transcended borders and time zones. Its chief rival in the mid-2000s was PayPal. But like many first movers, its success was also its failure. e-gold claimed it was neither a money transmitter nor a bank. Its users were also anonymous, features that precluded it from entering the mainstream. But it also inspired Bitcoin.

4. Bitcoin avoided many of the challenges faced by e-gold chiefly through its decentralized nature. However, a different challenge is emerging. Bitcoin's asset value is increasingly seen as a version of digital gold, which greatly reduces its circulation and discourages its use for payments. Bitcoin Pizza Day celebrates the 10,000 Bitcoin payment, a transaction that no one aspires to repeat. So, Bitcoin is playing the role of reserve to the digital economy, much like gold does for central banks.

5. Unlike gold, however, the Bitcoin protocol has a technological upside. It can dynamically adjust to user demands. The world wants tokenized assets? The Taproot Asset Protocol, built on Bitcoin, is designed to deliver them. And the first asset of choice? It seems there's no escaping the fiat system of equations—US dollar stablecoin. It's also a competitive arena, as evidenced by Solana's recent integration of stablecoin payments into Web2 platforms—a leap in user experience.

6. These crypto innovations are learning from the history of e-gold. Scaling requires entry into the regulatory mainstream. Once a close competitor to e-gold, PayPal now holds more than 80 US money transmitter licenses and

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follows FinCEN regulatory requirements for reporting and recording transactions—two areas of deficiency for e-gold. Crypto isn't sure what rules to follow, and the lack of clarity is slowing progress into practical applications. But this, too, is changing.

7. Regulatory clarity does not guarantee ideal outcomes. Rather, it means the rules will be clear for assessing capital investments. Europe's clarity around stablecoin has put a digital euro at the forefront of payments, aiming to regulate euro stablecoins into existence. This week, the UAE offered a similar path, with a digital dirham regulated as the primary payment tool to springboard local banks into the digital era. The model is clear—local currency for local payments.

8. It should not be surprising to see sovereign countries guard their currency independence. Monetary sovereignty is at the heart of any financial system. When in doubt, you can print—an inherent instability that led to the birth of e-gold in the first place. Nearly every country is likely to introduce its own central bank digital currency (CBDC) to keep monetary sovereignty alive, even if private payment protocols dominate. On point, Switzerland extended its CBDC trial last week.

9. Crypto has come a long way in a short period. And it's for the right reasons—it's better, cheaper and faster. Take the tokenized asset of choice these days—the US dollar. Measured by velocity, stablecoin is nearly 30-times more efficient than fiat (Figure 1). To put that into context, there is $5.7 trillion of US base money in circulation. At the velocity of stablecoin, you would need around $200 billion to support the same transaction volume as the current $5.7 trillion of circulating fiat.

10. It's not a comparison to take literally. After all, stablecoin transactions are overstated and they are tied mostly to financial trading where velocity demand is inherently higher. Fair. And irrelevant, too. Crypto is the first payment and settlement rail built into one. As efficiency gains in crypto technologies become apparent, they demand regulatory clarity and scale into the mainstream. Philosophies like e-gold started the story. But all great ideas live and die by their economics.

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