Tomorrow's Affairs
Analysis of today
Assessment of tomorrow

By: Daniel Lacalle

Central Banks Only Want to Ban Bitcoin Because They Will Destroy Money

If a government or central bank had the unequivocal objective of maintaining or strengthening the purchasing power of the currency they issue, they would never fear bitcoin or any other competition. It would make no sense.

Government money has all the qualities to win people's favor and increase demand if its economic value is strong through time.

However, when central banks and governments express fear of bitcoin and demand its ban, they are revealing their lack of commitment to upholding the value of their currency.

A strong currency welcomes competition. A weak currency fears it.

This week, the ECB and the Federal Reserve of Minneapolis have published papers that should instill a great deal of fear in us.

The two papers unashamedly call for fiscal repression and direct banning of Bitcoin because it may pose a threat to the endless desire of governments to run elevated deficits and destroy the purchasing power of the currency they issue.

The ever-rising debt

The Minneapolis Federal Reserve paper (Unique Implementation of Permanent Primary Deficits?, Working Paper 807, October 17, 2024) says that the government can use nominal debt and continuous Markov strategies for primary deficits and payments to debtholders to set up a permanent primary deficit.

But this result fails if there are also useless pieces of paper (bitcoin for short) that can be traded. It goes on to conclude that "there is a balanced budget trap: continuous government policies designed for a permanent primary deficit cannot eliminate an alternative steady state in which $r - g = 0$ and the government is forced to balance its budget. A legal prohibition against bitcoin can restore unique implementation of permanent primary deficits, and so can a tax on bitcoin at the rate $(r - g) > 0$."

Allow me to translate and summarize. According to the writers of the paper, the government can run eternal deficits and force citizens to accept the ever-rising debt if the currency issued is imposed and cannot be exchanged for an alternative.

Given its control over the game's rules, this would empower the government to arbitrarily impoverish citizens and drive debt out of control.

It is scary to read the paper's unashamed defense of repression, coercion, and political use of money to increase the size of government

However, the government would be forced to run a balanced budget if there is a store of value alternative, like Bitcoin, which they call a useless piece of paper because it does not serve the government in its quest to dissolve its financial commitments in real terms.

It is scary to read the paper's unashamed defense of repression, coercion, and political use of money to increase the size of government.

The writers clearly admit that governments will be pleased running eternal deficits and using the currency to enforce inflationist policies, but an independent asset like Bitcoin puts this strategy in danger.

Hence, they demand "a legal prohibition against bitcoin" to restore the "unique implementation of permanent primary deficits."

Bitcoin may be banned, but...

The paper is simply delusional. Bitcoin may be banned, but if governments continue to destroy confidence in their solvency and fiscal responsibility, the currency they issue will be demolished and its use will vanish sooner or later.

If it is not Bitcoin, it will be gold or any other means of payment that remains a reserve of value. They despise Bitcoin because it exposes the fallacy of Modern Monetary Theory (MMT) and the unrealistic expectations of a perpetual expansion of government in the economy.

The ECB paper (The distributional consequences of Bitcoin, 2 Oct 2024, Bindseil et al.) follows a similar train of thought.

Similar to the Minneapolis Fed paper, it leads one to believe that the social use of fiat money is solely related to the government's budget expansion strategy.

They assume that currency must be imposed, or the government will be forced to be fiscally prudent. With it, they admit that they have no intention of maintaining the value of the euro and therefore want to ban Bitcoin using the ridiculous excuse that early adopters got rich.

> If you purchased Amazon shares during the IPO, you should face penalties due to their dramatic price rise, which current buyers are not receiving

Imagine a supposedly serious paper suggesting that if you purchased Amazon shares during the IPO, you should face penalties due to their dramatic price rise, which current buyers are not receiving. Similarly, if you invested in gold a decade ago, you should face steep taxes.

This is a clear example of socialist repression, disguised as a seemingly serious study. Moreover, it fails to acknowledge the fact that Bitcoin capital gains are subject to standard taxes.

Ludicrous scenario

They state that Bitcoin is not a global digital currency that facilitates transactions, eliminating intermediaries. For them, Bitcoin is not a common means of payment due to its design limitations, high volatility, and slow, costly transactions.

Therefore, the authors describe Bitcoin as a speculative investment that promises high returns rather than a practical currency. As such, they say that Bitcoin’s value increase does not contribute to economic productivity, potentially leading to wealth redistribution from non-holders to holders.

“The scenario where Bitcoin's price continuously rises could impoverish those outside or late to the Bitcoin economy, creating social and economic disparities."

This scenario is so ludicrous that it defies comprehension. How can an alleged ECB expert assume that there will be no productive use, no lending, or no investment in Bitcoin? I am sure they are not that silly.

> They are admitting that Bitcoin puts the mirage of eternal government money printing and imposed currency devaluation at risk

They simply perceive the potential threat to the increasing amounts of government bonds in the commercial banks' asset base should Bitcoin be incorporated into the financing of mortgages and loans.

They see no contribution to economic productivity in Bitcoin, but they hail “perennial” unproductive government debt and constant currency debasement as "social."

In essence, they are only admitting that Bitcoin puts the mirage of eternal government money printing and imposed currency devaluation at risk. Nothing else.

Statism and socialism

Both papers want to ban or tax Bitcoin because they see that governments may lose the monopoly of money and the power to erode the purchasing power of their currencies, and in the case of the ECB, the writers try to warn of an evil world where the first buyers of Bitcoin profit and the rest lose, something so ridiculous that would imply that the economy is a zero-sum game and it is not.

People are not impoverished today because shares issued years ago are at all-time highs. The opposite happens.

Guess what? I am confident that the authors of both papers understand the absurdity of these excuses. If Bitcoin rises in value and generates its own liquidity, it will benefit everyone involved because it is designed to maintain its status as a reserve of value.

The idea that you must ban or tax an asset because it may rise substantially is pure statism and socialism.

What I find intriguing about these two pieces of interventionism committed to paper is that both indirectly acknowledge that governments have no intention to defend the purchasing power of the currency they issue.

Furthermore, they admit that the cracks are beginning to show and that confidence in sovereign issuers and their currency is declining.

No leader worries about a worthless competitor unless the leader's objective is to issue a weak currency and, therefore, wants to maintain its leadership by imposition - Daniel Lacalle

If Bitcoin was a useless piece of paper, as the Minneapolis Fed paper states, they should not worry. Some investors would lose their money and learn from the experience, as happens every day in markets.

If Bitcoin had no productive contribution, they should not worry about it either, because it would never achieve status as a world currency, as no one would take loans or make investments in it.

If Bitcoin is a useless speculative investment asset and holds no productive capabilities, it should not worry anyone at the Fed or the ECB.

If the ECB and the Fed were serious about following their mandate and defending the currency's status as a reserve of value and generalized means of payment, they would not have to worry at all about Bitcoin.

No leader worries about a worthless competitor unless the leader's objective is to issue a weak currency and, therefore, wants to maintain its leadership by imposition.

Propaganda pieces of a monetary dictatorship

When both papers advocate for the prohibition of Bitcoin, they are essentially advocating for the prohibition of any alternative to fiat currencies, as this could potentially compel governments to exercise fiscal prudence and uphold the currency's value.

Both papers are appalling propaganda pieces of a monetary dictatorship where governments can do what they want and citizens must obey and swallow the demolition of their real wages and deposit savings.

> If the reasons for perceiving Bitcoin as a risky asset were accurate, then it would never pose a threat to traditional currencies. It would be irrelevant

The premise of both papers is that Bitcoin poses a threat because it has the potential to challenge fiat currencies. However, if the reasons for perceiving Bitcoin as a risky asset were accurate, then it would never pose a threat to traditional currencies. It would be irrelevant.

The only way in which the premise and the conclusion of both papers can be tied together is if the ECB and the Fed writers want to destroy the purchasing power of the currency and bloat the size of government through a de facto nationalization of the productive sector via public debt accumulation, generating currency debasement.

This is not the Fed and the ECB waging a war on Bitcoin. The authors are waging a war on free markets and your money.