

America's Future Depends on the Blockchain

di Jay Clayton

Bitcoin and other novel “tokenized” assets—so called because ownership is documented as a unique digital token on a ledger such as blockchain—recently reached more than \$3 trillion in total value. The race is now on to tokenize all types of assets. Embodying ownership, rights and obligations in blockchain-based tokens is in many ways superior to our legacy financial infrastructure.

Tens of billions of dollars of tokenized assets change hands daily on markets that operate seamlessly around the clock. The nascent cryptocurrency market is the tip of the financial-information technology iceberg. Below the water's surface lie vast, interconnected payment networks and credit and securities markets that exceed hundreds of trillions of dollars in asset value. We all use these markets and depend on them, but they are ripe for functional change.

While securities trading and other financial transactions may appear instantaneous, many back-end processes still move at a snail's pace in rigid sequences set decades ago. A mortgage payment isn't completed when the funds leave the homeowner's bank account. Those funds have many hands to go through before they come to rest, days or weeks later. Through tokenization, many of these cumbersome and costly processes can be streamlined with better market information, greater certainty and enhanced security.

The potential efficiency improvements to the current system are enormous, including billions of dollars annually in reduced frictions and increased consumer choice. End-to-end tokenization of sovereign currencies, securities, loans, real estate, mortgages, pledges, and related payments and credit is a once-in-a-generation opportunity for both entrepreneurs and nimble incumbents. It is also an existential threat to those who are slow to adapt.

What is government's role? Regulation is essential to our financial markets, and there is no doubt that tokenized financial assets should be regulated to ensure financial stability, promote capital formation, prevent illicit activity, and protect consumers. But there is more the U.S. government must do. Innovators must have assurances that if they follow time-tested regulatory principles, they will be free to pursue the market opportunities provided by better functionality. The government should actively facilitate the adoption of technology in core U.S. dollar funding and payments markets. This is a matter of national security and financial stability.

The most important financial market in the world, the U.S. Treasury market, is a government market. Virtually all other financial markets, at home and abroad, have some tie to the U.S. Treasury market, including the cash in our wallets and the entries in our bank

accounts. A central bank's digital currency, or "digital dollar" is the tail of the dog. Financial regulators, in tandem with the private sector, should be focusing on the dog.

Dollar primacy and stability are critical to global economic development, financial stability and U.S. national security. In the face of broad technological change, primacy of the U.S. dollar is by no means certain. China views this technological shift as an opportunity not only to achieve operational efficiencies but to extend the reach and influence of yuan-based payments and lending. Chinese authorities are driving digitization and tokenization in their core payment and credit markets, allowing greater government monitoring and control. And there is no doubt Chinese leadership plans to extend similar practices to international trade and finance, expanding their influence over global commerce. The U.S. must recognize the reserve currency race is on, and winning is the only rational objective.

We have a head start in both traditional markets and new tokenized markets. More than 95% of stablecoins by value are based on the U.S. dollar. In other words, at the incipient stages of this global shift in financial technology, dollars—actually U.S. Treasury securities—have remained the preferred liquid store of value for new and traditional markets. But stability and leadership can erode quickly in times of technological change. Another nation seizing control of global credit and payment systems would not only affect our global standing but also could destabilize the global financial system.

Time is of the essence. Emerging as the standard-setter in any technological shift has great and one-time-only multiplier effects. Investment capital and ingenuity flow quickly to the emerging standard, further enhancing its acceptance and related economies of scale. The U.S. should use its head start to set the standard for tomorrow's marketplace.

One potential path is an open public-private effort to explore the tokenization of the U.S. Treasury market and related funding processes. Imagine the efficiencies and regulatory enhancements provided by real-time trading, clearing and settlement in the U.S. Treasury market. How about the many efficiencies and welfare-enhancing products that could be built off tokenized interoperability among the Federal Reserve, regulated financial institutions, other financial services providers, investors, savers and consumers? Imagine the benefits to the U.S. from modernizing current payment markets rather than waiting for new ones to develop. Imagine the investment and human capital that would flow in the direction of U.S. ingenuity, virtually immediately, if such an effort were announced.

The iceberg, above and below the surface, is much bigger than we saw just a few years ago. It's time for a public-private partnership to ensure that it floats in the direction of our long-term commitment to free and fair markets, global financial stability and consumer welfare in every country.