VIXIO PAYMENTS COMPLIANCE

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LatAm Governments To Turn Eye To CBDCs Rather Than Bitcoin

Mexico's recent announcement to adopt a central bank digital currency (CBDC) shows that Latin American countries are more likely to adopt their own digital currencies than follow suit with El Salvador's controversial Bitcoin experiment.

On December 30, Mexico's government announced on Twitter that Banxico, the country's central bank, will have the digital currency in circulation by 2024.

The government said it considers "of utmost importance these new technologies and the latest generation payments infrastructure as options of great value to advance financial inclusion in the country".

Although the news has not yet been confirmed by Banxico itself, Victoria Rodriguez Ceja, recently approved governor of Banxico, told the Senate that the central bank is examining the possibility of introducing a digital currency.

With such a decision, Mexico would join the likes of Brazil and Peru, highlighting a trend that Central and South American countries are turning to CBDCs rather than private virtual currencies.

"At a high level, it does seem these developments align with what we would expect based on the El Salvador case study," David Martinez, an attorney at Clifford Chance, told VIXIO.

Last September, Bitcoin became the second official currency in El Salvador, next to the U.S. dollar, enabling citizens to use Bitcoin as a legal means of payment.

The so-called "Bitcoin experiment" has been the brainchild of 40-year old President Nayib Bukele, who argues it "will improve lives and the future of millions".

Since September, the country has purchased more than 1,100 Bitcoins (worth more than $50m at end 2021 prices) and Bukele has revealed grandiose plans to build the world's first-ever Bitcoin city, on a volcano, and issue Bitcoin bonds worth $1bn.

However, El Salvador is relatively unique insofar as it did not have its own fiat currency in circulation at the time it adopted Bitcoin as an official legal tender, Martinez explained.

In the case of other countries in Latin America that have their own fiat currencies, it is reasonable to expect them to implement a CBDC system rather than the El Salvador model for digital payments, he noted.

In October 2021, it was widely reported that Brazil was following El Salvador by making Bitcoin a legal tender. These rumours circulated based on an interview given by federal deputy Aureo Ribeiro discussing a proposed bill to regulate virtual currencies.

Ribero said that the regulations will bring Bitcoin under regulatory supervision, which will eventually help Brazilians to buy a house, a car or a hamburger in McDonald's in Bitcoin.

However, as reported by VIXIO, Ribeiro never said that Bitcoin would become a legal tender in the country. He expressed his personal view that the regulations will eventually ease the use of Bitcoin, as well as any other cryptocurrencies, in the country.

In fact, Brazil looks to be pursuing its own path to a CBDC. In December, Roberto Campos Neto, the president of the Brazilian Central Bank (BCB), announced a new partnership aimed at testing potential use cases for CBDC.

Financial inclusion a key driver

Many governments and central banks in the region are looking at digital currencies and weighing whether a CBDC or a private virtual currency could help reach the millions of people that remain outside the scope of the traditional banking system.

This was a stated aim of El Salvador at the time of adopting Bitcoin. Similar to many Latin American countries, El Salvador had an unbanked population of around 70 percent.

However, just one month after the adoption of Bitcoin, 3m people, equivalent to two thirds of the country's adult population, had already downloaded the new Chivo e-wallet developed for the use of Bitcoins. Chivo was heavily promoted by the government, who incentivised adoption by depositing $30 worth of Bitcoin in the account of every citizen that downloaded it.

Despite this positive development in terms of financial inclusion, Bukele’s experiment has faced serious and continuous criticism from economists and international organisations who argue that the highly volatile currency poses numerous risks to consumer protection, financial stability and integrity.

In November, the International Monetary Fund warned El Salvador that Bitcoin should not be used as a legal tender and recommended narrowing the scope of the Bitcoin law and strengthening the regulation of the new payment ecosystem.

Meanwhile, end users were facing numerous and repeated issues with their Chivo wallets. An increasing number of people complained that their funds had disappeared from their wallets, while others reported the loss of their unspent $30 sign-up bonus.

The volatility of the virtual currency could pose a bigger challenge for the country. On December 31, the virtual currency closed the year on $46,200, more than 10 percent lower in price ($51,000) than when the country purchased its first 200 Bitcoins in September.