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Stablecoins: The cryptocurrency Holy Grail?

Singapore Management University

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Cryptocurrencies such as Tether were built with the aim of eliminating wild price fluctuations but it is still a work in progress

May 22 is known as Pizza Day amongst cryptocurrency enthusiasts. In 2010, computer programmer Laszlo Hanyecz paid for two pizzas with 10,000 Bitcoins (BTC), marking the first known use of BTC to buy a physical item. Those BTC, if they had not since been sold, would be worth about US$80 million right now.

They would have fetched an even higher price during the Bitcoin craze around Christmas 2017 when one BTC went for nearly US$20,000 – $200 million for two pizzas. Exactly a year later in December 2018, one BTC was worth less than US$4,000.

These wild price swings prompted former PayPal CEO Bill Harris to label Bitcoin “a scam”, likening it to a pump-and-dump scheme. JPMorgan CEO Jamie Dimon called it a “scam”.

But what if there was a cryptocurrency whose price does not fluctuate so wildly?

A STABLE COIN

“Here in Asia, people don't care about Bitcoin,” claims **Joshua Ho**, Managing Partner of digital asset traders QCP Capital. “[Most of the action] is in stablecoin.”

Some of these are dollar-backed, such as Tether, which is “1-to-1 pegged to the dollar, so 1 USD₮ is always valued at 1 USD” and gives “customers the ability to transact with traditional currencies across the blockchain”. Other popular stablecoins include USDC and TrueUSD (TUSD), just two of the various stablecoins that Ho says are gaining popularity with his high-net-worth clients.

“People use this to have self-sovereign control over value so they can transfer, 10, 20, 30 million dollars, however much they want,” he says. “We have many clients who after that eighth phone call to the bank and being transferred 10 times, they say ‘Screw this’ and move half their net worth into stablecoin.”

He adds: “In many cases it's value transfer, it's money movement, it's capital flow. A lot of it is Renminbi, Hong Kong dollar, a lot of it is Indonesian Rupiah to USD₮. Every country seems to have its own flavour. Even though all the dollar-backed stable coins are pretty similar in scope, there are very small intricacies and differences.

“For some reason, Korea loves TUSD, which is called TrustToken. Indonesia for some reason likes USDC, which is the stable coin created by Circle and Coinbase, but the rest of Asia is still very bullish on USD₮.”

Once the stablecoins have been moved, it is then possible to cash out to fiat currencies. Tether charges a maximum of three percent for fiat withdrawals while Coinbase charges different rates for different countries and withdrawal methods. While they are not free, these charges are generally much lower than those levied by traditional banks and financial institutions.

KYC: KNOW YOUR CUSTOMER…AND KEEP YOUR COIN

That is not to say stablecoins are the holy grail of cryptocurrencies. Just last month Tether’s US$2.8 billion market capitalisation was found to be backed by only 74 percent in cash and “short-term securites” that happened to be shares in cryptocurrency trading platform iFinex, Tether’s holding company.

It was bad enough that each Tether token was not backed 1-for-1 with fiat reserves as advertised. To make things even murkier, the shares were secured as collateral for a line of credit to cryptocurrencies exchange Bitfinex, which was also part of iFinex. To make a long story short, Bitfinex borrowed money – as much as US$900 million – from a sister company (Tether) to cover losses without informing anybody.

BitFinex got into this mess in the first place after having US$850 million frozen when Portuguese and American authorities seized the funds. Bitfinex had sent the money to a payment processor called Crypto Capital, the crypto banker of the infamous QuadrigaCX. At the end of last month, two people with alleged ties to Crypto Capital were charged with money laundering.

Given cryptocurrencies' sometimes shadowy reputation, Ho insists on strict KYC (Know Your Customer) procedures to maintain a competitive edge.

"The most valuable thing in this space right now is fiat to crypto access," Ho says, referring to the ability to buy cryptocurrencies with cash or credit cards – the most popular way for investors to trade. "We're probably one of two groups out here that have very reliable fiat backing with every single bank. [Our KYC procedure] is very strict because we don't want to lose our fiat access."

CRYPTOCURRENCY IN THE REAL WORLD

For most people, the ultimate value of cryptocurrencies is measured in the things it can buy i.e. Pizza Day. Microsoft accepts Bitcoin for its online Xbox Store – Bill Gates: "Bitcoin is better than currency." – while small brick-and-mortar retailers worldwide are accepting crypto payments in varying degrees from one country to another.

Ho, who started his business with arbitrage, got into the cryptocurrency space following numerous projects. He observes that those "trying to figure out how that next crypto token is going to become a form of currency" has gotten it the other way around.

"We believe that many of the projects we received in this space were putting the cart before the horse. In our opinion, crypto can behave a lot more like FX (foreign exchange). We've got the whole world trying to figure out how that next crypto token is going to become a form of currency that people will use for value exchange.

"In reality it's more like FX and fiat are becoming more like crypto, taking on the aspects of crypto into its value transfer."

Joshua Ho was a member of the discussion panel "Digital Assets in Asia" at the SMU SKBI event, Digital Assets Working Group (DAWG): APAC Readout 2019 held on May 22, 2019.

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