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R&R Weekly Column
By Brunello Rosa

CBDCs Are Inevitable. The Sooner Reluctant Central Banks Understand That, The Better

Last week, Money 20/20, the largest FinTech conference in Europe, was held in Amsterdam. One of the headline events at the conference was a panel discussion in which the project called a "New Era for Money" was presented. The project aims at developing and implementing the first Digital Sterling (dSterling) pilot. As we discussed on our website, Project New Era is a privately-led initiative evaluating the path towards a retail Central Bank Digital Currency (CBDC) in the UK. A CBDC would be the digital version of a banknote, with still the liability of a central bank. The project proposes that there be closer public-private collaboration in order to address key challenges and open questions relating to CBDC development.

Project New Era will form the Digital Financial Market Infrastructure (FMI) Consortium, with the aim of keeping central banks, regulators, and government informed of progress. The consortium will issue Sterling, a digital settlement asset similar to a CBDC, to drive the pilot, which will focus on core design issues. Rosa & Roubini Associates are an independent advisor of the Project and the associated Consortium.

The panel discussion in Amsterdam brought to the fore the technical, regulatory, policy and political challenges that lie ahead for the formal introduction of a CBDC in the UK. They mirror the challenges faced by all private and public sector actors in other jurisdictions on the introduction of a CBDC. In future reports we may discuss all this in more detail. In this column, we want to highlight one specific aspect of the adoption process: the reluctance felt by so many central banks in even engaging with the issue.

Just to give an example, the Reserve Bank of Australia (RBA), in September 2020 declared that "the Bank's view is that there is currently *no strong public policy case* to introduce a CBDC for retail use," for various reasons including the still-strong demand for AUD banknotes, the availability of an electronic payments system and the cost of the exercise. Since then, the RBA has introduced a number of projects to study the potential adoption of a retail CBDC, but officially their position has not changed.

It is estimated however that around 80% of central banks are studying the introduction of a CBDC, and some of them have already begun issuing it. First and foremost, the People's Bank of China (PBoC), which issued its e-CNY on the occasion of the Winter Olympics in Beijing. After this event, the US Federal Reserve speeded up its project for the introduction of a digital dollar in the US, following President Biden's executive order on a Responsible Development of Digital Assets on March 9th. In particular, Rep. Lynch introduced legislation to develop an electronic version of the U.S. Dollar, in a pilot program.

In the UK, there seems to be a gap between what the Treasury wants to do, namely to make the UK become a global hub for crypto assets, and what the Bank of England is prepared to do. The BoE's approach seems more cautious than that of the Treasury, at this stage. In Europe, while the Riksbank is in the forefront for the introduction of its e-Krona, the ECB has just launched a 2-year investigation period for its own CBDC.

Several industries have of coure already been disrupted by the introduction of digitalisation. We used to write letters, now we write e-mails; instead of phone calls on a landline, we now make video-calls on mobile phones. In the digital era, in which payments are made electronically and new forms of digital payments are introduced through crypto-assets and stablecoins, central banks will have to introduce the digital version of coins and banknotes, i.e. CBDCs. The PBoC has understood this before anyone else. It started its projects in 2014, and has already issued its digital renminbi. By doing so, it is gaining a massive competitive advantage on other central banks, including from a geopolitical perspective. So, the sooner reluctant central banks will realise introducing CBDCs is an inevitable process, the better. Put in simpler terms, regarding CBDCs, it's not a question of IF, but of WHEN, and maybe, HOW.

Our Recent Publications

- *Deep Dive Into The Near-Term Future Part 2: What Lies Ahead For Policy And Financial Markets, by Brunello Rosa, 10 June 2022*
- *Flash Preview: Yet Another Rate Hike From the BoE In June, by Brunello Rosa and Nato Balavadze, 10 June 2022*
- *Flash Review: The ECB Signals The Beginning of Rate Normalisation in July, by Brunello Rosa and Nato Balavadze, 9 June 2022*
- *Deep Dive Into The Near-Term Future Part 1: What Lies Ahead For Geopolitics and the Global Macroeconomy, by Brunello Rosa 8 June 2022*
- *Ukraine War To Impact Tourism in the GCC, by Gulf State Analytics, 7 June 2022*
- *Flash Preview: ECB Prepares The Ground For The Rates Liftoff , by Brunello Rosa, Nouriel Roubini and Nato Balavadze, 2 June 202*

Looking Ahead

The Week Ahead: Inflation To Reach Other Record Highs In The EZ and EZ Economies; UK Unemployment To Fall; CBs Turn Hawkish

In the US, May's PPI is expected to raise by 10.9% (*p:* 11.0%).

In the EZ, in May, final data for inflation is expected to show: *i)* CPI inflation surging to 8.1% y-o-y and 0.8% m-o-m (*p:* 0.6%); and *ii)* core-inflation rising to 3.8% (*p:* 3.5%). Among largest EZ economies, in May inflation is expected to: *i)* accelerate to 7.9% y-o-y (*p:* 7.4%) in Germany; *ii)* increase to 5.2% y-o-y (*p:* 4.8%) in France; and *iii)* reach 6.9% y-o-y (*p:* 6.0%) in Italy. EZ April's IP is seen shrinking further to -1.1% y-o-y (*p:* -0.8%).

In the UK, in April, the unemployment rate is expected to fall to 3.6% (*p:* 3.7%). April's IP is likely to accelerate to 1.7% y-o-y (*p:* 0.7%)

CBs are expected to turn hawkish. In the US, the Fed is likely to increase its policy rate by 50 bps to 1.25-1.50%. In the UK, BoE is expected to increase its Bank Rate by 25 bps to 1.25%, the fifth increase in a row.

The Quarter Ahead: OECD Projects Global Growth To Decelerate; World Bank: "The Risk Of Stagflation Are Hammering Growth"

According to the latest OECD Economic Outlook, the war in Ukraine weighs on global economic prospects. The global economy may decelerate to 3.0% this year and 2.8% in 2023. It says: 'When coupled with China's zero-COVID policy, the war has set the global economy on a course of slower growth and rising inflation - a situation not seen since the 1970s.' Amid unseen the cost-of-living crisis, OECD warns Governments to combat inflation in order to protect low-income households. The organization also pointed on targeted direct aid to help and most vulnerable ones.

World Bank reports that stagflation is very real economic risk. World Bank also downgraded global growth from 5.7% in 2021 to 2.9% (vs 4.1% as forecast in January) in 2022. Growth in advanced economies is also revised down from 5.1% in 2021 to 2.6% in 2022.

On 6 June 2022 a vote of confidence was held on U.K.'s PM Boris Johnson. The government was criticized over parties and gatherings, also known as 'partygate', held during the COVID-19 pandemic in 2020 and 2021. Amid increasing dissatisfaction with his leadership, last month a report into lockdown parties in and around Downing Street was published in full.

Last Week's Review

Real Economy: US Inflation Rose; EZ Q1 GDP Advanced; ECB Kept Interest Rates Unchanged; UK PMIs Fell But Less-Than-Expected

In the US, May's inflation accelerated to 8.6% y-o-y (*c:* 8.3%; *p:* 8.3%), whereas core-inflation cooled off slightly to 6.0% (*c:* 5.9%; *p:* 6.2%). On a monthly basis, inflation rose by 1.0% (*c:* 0.7%; *p:* 0.3%). In June, according to a preliminary estimate, Michigan consumer sentiment decreased to 50.2 (*c:* 58; *p:* 58.4).

In the EZ, in Q1, GDP growth rose to 0.6% q-o-q (*c:* 0.3%; *p:* 0.2%) and 5.4% y-o-y (*c:* 5.1%; *p:* 4.7%).

Still in the EZ, the ECB kept its policy stance unchanged with the main refi rate at 0%, the depo rate at -0.5% and the marginal refinancing rate at 0.25%. The ECB pre-announced rate hikes in July (+25 bps) and September (either +25 or +50 bps).

In the UK, the final data for S&P Global/CIPS in May showed: *i)* services PMI fell to 53.4 (*c:* 51.8; *p:* 58.9); manufacturing PMI also fell to 54.6 (*c:* 54.6; *p:* 55.8) and *iii)* composite PMI decreased to 53.1 (*c:* 51.8; *p:* 58.2).

Financial Markets: Stock Markets Are Down And Yields Rose As Inflation Soars; Dollar Index Surged; Oil And Gold Are Up

Market Drivers: Investors digest two important readings for the U.S. Economy: *i)* consumer prices rose the most since 1982; and *ii)* consumer sentiment data came in at a record low. As a result, major U.S. stock index finished the week with steep losses. In the immediate aftermath of CPI release, U.S. Treasury yields surged and curve flattened. With ECB suggesting that the Bank may raise interest rates by a larger increment after July, European shares fell and government bond yields jumped.

Global Equities: Decreased *w-o-w* (MSCI ACWI, -4.4%, to 620.3). The US S&P 500 index fell (-5.1% w-o-w, to 3,900.9), as the Wall Street suffered the worst week since January. the EZ, shares were down (Eurostoxx 50, -4.9% w-o-w, to 3,599.2). In EMs, equities declined (MSCI EMs, -0.6%, to 1,055). Volatility rose to 28.2 (VIX S&P 500, 52w avg.: 22.3; 10y avg.: 18.1).

Fixed Income: *w-o-w*, 10-year US treasury yields increased (+22 bps to 3.2%). The 2-year US Treasury yields were up too (+41 bps to 3.07%). German 10-year bund yield increased (+23 bps to 1.50%).

FX: *w-o-w,* the US Dollar Index was up (DXY, +2%, to 104.2; EUR/USD -1.9%, to 1.052) over hotter-than-expected inflation data. In EMs, currencies weakened (MSCI EM Currency Index, -0.9% w-o-w, to 1,683.5).

Commodities: *w-o-w,* oil prices rose (Brent, 1.8% to 121.9 USD/b). Gold prices increased w-o-w (1.4% to 1,875.2 USD/Oz).

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The picture in the front page comes from this website

Abbreviations, Acronyms and Definitions

a	*Actual*
AKP	*Justice and Development Party, Turkey*
ann.	*annualized*
ARS	*Argentinian Peso*
avg.	*Average*
bn	*Billion*
BoC	*Bank of Canada*
BoE	*Bank of England*
BoJ	*Bank of Japan*
bpd	*Barrels per day*
bps	*Basis points*
BS	*Balance sheet*
c	*Consensus*
C/A	*Current account*
CB	*Central bank*
CBB	*Central Bank of Bahrain*
CBK	*Central Bank of Kuwait*
CBT	*Central Bank of Turkey*
CDU	*Christian Democratic Union, Germany*
CNY	*Chinese Yuan*
CPI	*Consumer Price Index*
DJIA	*Dow Jones Industrial Average Index*
DJEM	*Dow Jones Emerging Markets Index*
d-o-d	*Day-on-day*
DXY	*US Dollar Index*
EC	*European Commission*
ECB	*European Central Bank*
ECJ	*European Court of Justice*
EIA	*US Energy Information Agency*
EM	*Emerging Markets*
EP	*European Parliament*
EPS	*Earnings per share*
EU	*European Union*
EUR	*Euro*
EZ	*Eurozone*
Fed	*US Federal Reserve*
FOMC	*US Federal Open Market Committee*
FRB	*US Federal Reserve Board*
FX	*Foreign exchange*
FY	*Fiscal Year*
GCC	*Gulf Cooperation Council*
GBP	*British pound*
GDP	*Gross domestic product*
IMF	*International Monetary Fund*
INR	*Indian Rupee*
IPO	*Initial public offering*
IRR	*Iranian Rial*
JPY	*Japanese yen*
k	thousand
KSA	*Kingdom of Saudi Arabia*
LN	*Northern League, Italy*
M5S	*Five Star Movement, Italy*
m-o-m	*Month-on-month*
mb	*Million barrels*
mb/d	*Million barrels per day*
MENA	*Middle East and North Africa*
MHP	*Nationalist Movement Party, Turkey*
mn	*Million*
MPC	*Monetary Policy Committee*
NAFTA	*North-American Free Trade Agreement*
NATO	*North Atlantic Treaty Organization*
OECD	*Organization for Economic Cooperation and Development*
Opec	*Organization of Petroleum Exporting Countries*
p	*Previous*
P2P	*Peer-to-peer*
PBoC	*People's Bank of China*
PCE	*Personal Consumption Expenditures*
PE	*Price to earnings ratio*
PM	*Prime minister*
PMI	*Purchasing managers' index*
pps	*Percentage points*
pw	*Previous week*
QCB	*Qatar Central Bank*
QAR	*Qatari Riyal*
QE	*Quantitative easing*
q-o-q	*Quarter-on-quarter*
RE	*Real estate*
RBA	*Reserve Bank of Australia*
RRR	*Reserve Requirement Ratio*
RUB	*Russian Rouble*
SWF	*Sovereign Wealth Fund*
tn	*Trillion*
TRY	*Turkish Lira*
UAE	*United Arab Emirates*
UK	*United Kingdom*
US	*United States*
USD	*United States Dollar*
USD/b	*USD per barrel*
UST	*US Treasury bills/bonds*
VAT	*Value added tax*
VIX	*Chicago Board Options Exchange Volatility Index*
WTI	*West Texas Intermediate*
WTO	*World Trade Organisation*
w	*Week*
w-o-w	*Week-on-week*
y	*Year*
y-o-y	*Year-on-year*
y-t-d	*Year-to-date*
ZAR	*South African Rand*
2y; 10y	*2-year; 10-year*