CRYPTOCURRENCY

A NEWLY MINTED MARKET

Is blockchain-backed money ready for prime time?

BY PAUL GILLIN

For investors, cryptocurrency has become a byword for high risk. Bitcoin, the world's most recognized cryptocurrency, is a prime example. In 2018, the currency's value plummeted more than 80% while nearly $1 billion worth of bitcoins was stolen. And last year, a handful of major cryptocurrency exchange platforms were attacked, with hackers making off with millions. Quite a bit of drama for a currency format that touts its reliability and security.

So why are banks, merchants and even government agencies pushing forward with cryptocurrency initiatives?

"Banking systems in this country are archaic," says Kevin Lehtiniitty, chief product officer at Prime Trust, a U.S. financial services firm that specializes in alternative assets that include digital instruments. Traditional non-cash transactions like credit cards, checks and wire transfers all introduce delay, risk and fees to the payments process. "Retail adoption of crypto is going to modernize our systems," he says, decreasing settlement times, reducing overhead and enhancing functionality.

Momentum seems to be building. In February 2019, JP Morgan launched its prototype JPM Coin, a dollar-backed virtual currency designed to support instantaneous payments between institutional clients. In June, a consortium of prominent banks, including UBS and HSBC, announced the latest plans to move forward with the Utility Settlement Coin project—a $63 million cryptocurrency investment intended to reduce the time and complexity of post-trade settlements. Days later, Facebook announced its own plans for Libra, a private digital coin designed to facilitate monetary transactions within the social media giant's network and by rival ones as well. By distinguishing their currencies from

"The legacy banks are still trying to get their head around it."

—**Stefan Rust**, CEO of Bitcoin.com

“Banking systems in this country are archaic. Retail adoption of crypto is going to modernize our systems.”

—**Kevin Lehtiniitty**, chief product officer, Prime Trust

the more than 1,000 open-source alternatives, these well-known companies hope to gain first-mover advantage.

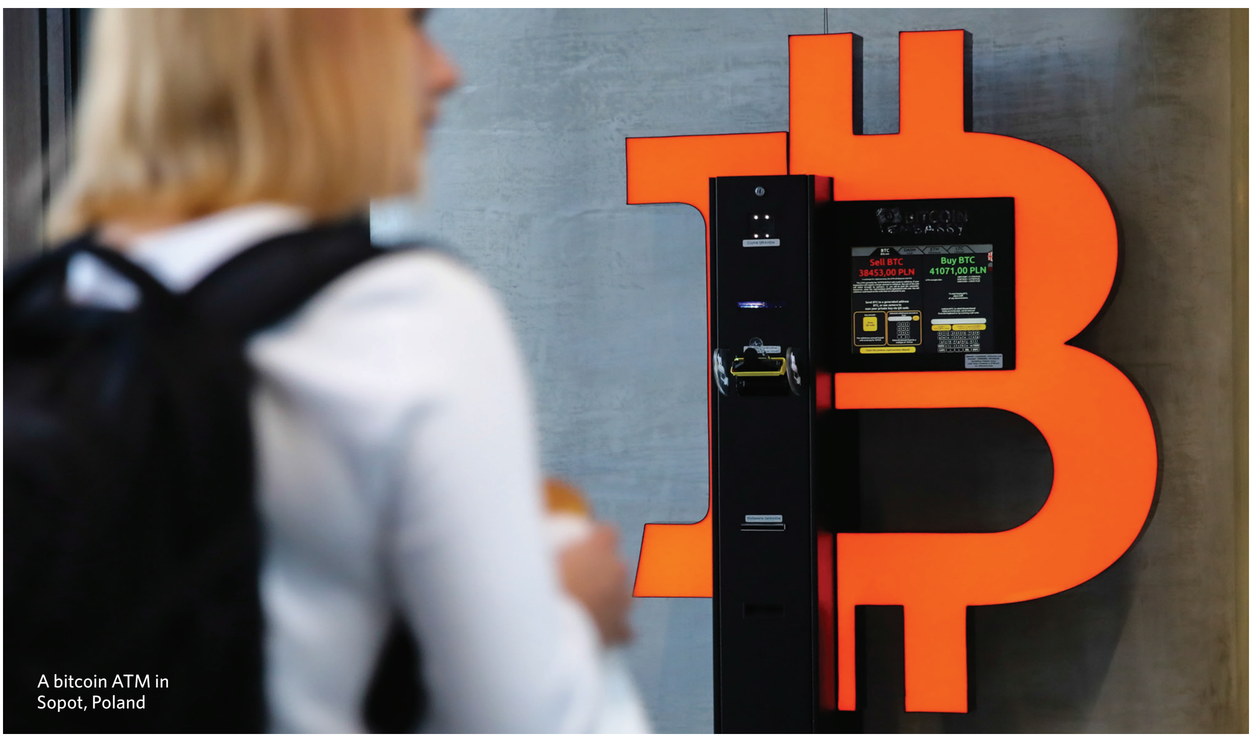
Multidimensional Potential

Even with recent hacks in mind, most experts continue to tout the fundamental security of blockchain, the technology that backs these cryptocurrencies. “The technology is sound,” says David Deputy, director of strategic development and emerging markets at tax software provider Vertex Inc. “The exchanges have been the weak point.”

Using blockchain, virtual currencies like Bitcoin are decentralized, meaning that the record of each person’s transaction—whether a buyer or seller—is cut up into fragments and stored locally over the entire network of users. It negates the need for third-party authentication. Blockchain can record more payments, and contract terms, supply chain history and other data shared between parties can also be handled.

Stefan Rust, CEO of the Bitcoin.com exchange, says ubiquitous customer loyalty points—from airline miles to grocery store rewards—can be encoded within a blockchain to enable point-holders to “swap and trade those points not just at one retailer but across retailers.” The blockchain guarantees that ownership and transactions are legitimate, he says.

Blockchain can also be programmable, meaning that one transaction can replace traditionally complicated procedures. For example, a smart contract for a real estate purchase can



A bitcoin ATM in Sopot, Poland

PHOTO BY JAKUB PORZYCKI/NURPHOTO VIA GETTY IMAGES

“The genie is out of the bottle. Do businesses want to be Netflix, which successfully adapted to the digital era, or Blockbuster Video?”

—Jimmy Nguyen, founding president, Bitcoin Association

PHOTO BY FABRICE COFFRINI/AFP VIA GETTY IMAGES

include all the additional closing documents necessary for sale, eliminating the need for signatures, title searches, settlement delays or legal reviews. Virtual currencies like JPM Coin could also potentially reduce rampant credit card fraud while eliminating transaction fees.

And because they are borderless, cryptocurrencies do not incur foreign-exchange charges and are not subject to the strengths and weaknesses of local currencies. This can be especially valuable to fight the inflationary tendencies of sovereign currencies, says Jimmy Nguyen, founding president of the Bitcoin Association. He also points out that crypto exchanges could offer a secure payment system to the unbanked of the world.

Challenges Ahead

Given all these advantages, why has it taken a decade for cryptocurrencies to begin to catch on?

One reason is that the technology remains intimidating to many. “The legacy banks are still trying to get their head around it,” Mr. Rust says. The average customer is even further behind. Virtual wallets, passwords and exchanges are more complex than merely swiping a card. And the growing number of cryptocurrency options—over 1,000 as of October—can be overwhelming. Add to that an overall lack of clear regulation, and it is easy to understand a person’s hesitancy.

Yet the biggest risk for many is the volatility of virtual currencies. To address this problem, many currency exchanges are developing stablecoins, currencies whose value is pegged to conservative assets. After a rocky start, the Coinbase exchange recently rolled out its U.S. dollar-pegged USD Coin in 85 countries. Going one step further, JP Morgan’s JPM Coin is guaranteed to be redeemable by any standard currency that the bank holds, such as the dollar.

“Acceptance will be gradual, and then suddenly it’ll be all around us,” Mr. Rust says. Drawing an analogy to the early commercial internet, he adds that, “All of a sudden we’re doing everything on it.”

What this means is that it might be time for many businesses to jump into the pool. “Right now, it’s a great opportunity to engage with millennials as a marketing play,” says Mr. Deputy. Bitcoin.com now partners with 15,000 merchant customers through its network, Mr. Rust explains. His advice to businesses? “Start now, start small and learn.”

The same is especially true for banks, where anxiety and inexperience are often stumbling blocks to adoption. Mr. Deputy recommends that bank executives start working with distributed finance companies now before they become real competition.

“But business leaders must be wary of cryptocurrency hype and find a solid business case that can reduce inefficiencies,” Mr. Nguyen says. “The genie is out of the bottle. Do businesses want to be Netflix, which successfully adapted to the digital era, or Blockbuster Video?” **IQ**

THE TAKEAWAY

Bitcoin got the buzz—and the high-risk reputation. But it is an emerging class of stablecoins—virtual currencies backed by conventional assets—that has leaders finally taking a serious look at cryptocurrencies. By exploring still-nascent blockchain technologies, organizations can connect with unbanked populations as well as engage with digital natives.