

# Why restrict stablecoins?

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## **Abstract:**

Competition among unrestricted stablecoins has been compared to antebellum US episodes of “wildcat banking” fraud as a rationale for restricting stablecoins. Fraud in minimally restricted banknote issue was in fact historically rare, and fraud in stablecoin issue has also been rare. It is important to distinguish how stablecoin issuers are like historical banknote issuers in some respects and different in other respects. Proponents of the US “Genius Act” for restricting dollar stablecoins (signed into law July 2025) predict that it will make stablecoins more popular globally. But the market-leading stablecoin (Tether USD) does not owe its global popularity to legal restrictions, so that prediction is doubtful. The Genius Act does not remedy any apparent market failure, and can be seen instead in part as a fiscal measure.

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## **Why restrict stablecoins?**

### *Some background information*

A “stablecoin” is a cryptocurrency whose value is pegged to a fiat currency, to gold, or (conceivably) to another potential money. The leading stablecoins are tokenized IOUs, issued on Ethereum and other platforms, and traded on crypto exchanges. On 1 September 2025, stablecoins in circulation totaled \$284 billion, with US dollar-denominated stablecoins comprising about 99 percent of the total. (Gold and euros back most of the remaining 1 percent.) On that date USD Tether was the largest issuer (59 percent market share), followed by USDC. Tether was established in 2014 and is now legally based in El Salvador, having moved from the British Virgin Islands in January 2025. USDC (25 percent share) was established 2018 and is domiciled in the United States. All the leading dollar stablecoins (see Table 1) are managed by their issuers to maintain a price centered on and close to \$1.00 (usually between 0.999 and 1.001).

Like bank deposits and historical banknotes, stablecoins are the liabilities of their issuers. On the other side of their balance sheets, Tether and USDC promise to hold safe and liquid USD-denominated assets, including US Treasuries and other bonds, equal or greater in value to their liabilities. They bought their current assets by issuing the stablecoins now in circulation; on any day they (or speculators) will buy back or issue enough coins to maintain their \$1.00 pegs.

The third, fourth, and fifth largest stablecoins listed, Ethena USDe (launched 2024), USDS (2025; an upgrade of DAI), and DAI (2019), are over-collateralized mostly by on-chain cryptocurrency assets rather than off-chain USD-denominated assets. They similarly buy and sell assets (issue and withdraw coins) as needed to maintain their \$1.00 pegs. Stablecoins

collateralized by crypto assets will no longer be legal within the United States when the 2025 GENIUS Act (discussed below) becomes effective in 2027.

**Table 1: Top 10 stablecoins by market cap (value in circulation)**

Source: <https://www.coingecko.com/en/categories/stablecoins>, taken 13:21 EST, 16 Sept. 2025.  
Note: The listed tokens and figures at Coinmarketcap.com differ in some respects.

| ▲ #  | Coin                                                                                                 | Market Cap        | Price      | 24h Volume       |
|------|------------------------------------------------------------------------------------------------------|-------------------|------------|------------------|
| ☆ 4  |  Tether USDT        | \$170,843,358,087 | \$1.00     | \$81,967,094,520 |
| ☆ 7  |  USDC USDC          | \$73,210,633,137  | \$0.9998   | \$12,116,380,324 |
| ☆ 17 |  Ethena USDe USDe   | \$13,718,532,786  | \$0.9985   | \$199,460,080    |
| ☆ 30 |  USDS USDS          | \$8,018,908,761   | \$0.9994   | \$8,975,168      |
| ☆ 43 |  Dai DAI           | \$4,601,899,607   | \$0.9996   | \$90,181,927     |
| ☆ 62 |  USD1 USD1        | \$2,668,667,292   | \$1.00     | \$275,786,875    |
| ☆ 83 |  Falcon USD USDF  | \$1,843,139,251   | \$1.00     | \$85,533,295     |
| ☆ 85 |  USDtb USDtb      | \$1,817,511,169   | \$0.9997   | \$2,832,755      |
| ☆ 90 |  BFUSD BFUSD      | \$1,699,239,613   | \$0.9996   | \$9,223,566      |
| ☆ 99 |  Tether Gold XAUT | \$1,390,106,975   | \$3,700.41 | \$182,405,413    |

Stablecoins first became popular among cryptocurrency traders and exchanges, and have displaced Bitcoin (BTC) from the role of commonly accepted medium of exchange in crypto markets. Before 2020, cryptocurrencies were mostly priced in BTC and paid for with BTC. Today USD Tether is the predominant pricing unit and medium of payment. The volume of the top two stablecoins (USDT + USDC) in circulation grew dramatically from less than \$5 billion

at the start of 2020 to more than \$130 billion two years later. Tether USD in September 2025 had less than 1/10<sup>th</sup> of Bitcoin’s market cap, but approximately twice its daily transaction volume. Being pegged to the US dollar, Tether and other stablecoins spare traders the high daily purchasing-power volatility (average dollar price movement of about 3.5 percent per day between September 2024 and September 2025)<sup>1</sup> that characterizes BTC. By contrast to using bank dollars as a medium of exchange, a trader can sell Ether for USD Tether on one exchange, then buy a different coin with the USD Tether on another exchange, without the hassle, delay, and non-privacy involved in moving funds into a bank account and back out. Nic Carter (2024) estimates that “[a]round 60–80% of all value settled on blockchains is done with stablecoins, and over 99 percent of stablecoins reference the USD as their unit of account.”

Lately, stablecoins issuers are promoting their usefulness for business-to-business transactions. The selling points are simple: Payment by stablecoin transfer is just as fast, more private, and cheaper than wiring money from bank account to bank account.

#### *Stablecoin balance sheets and “reserves”*

The following t-account reproduces the latest available figures reported on Tether USD’s website (<https://tether.to/en/transparency/>) regarding its assets and liabilities:

#### **Tether Issuer Assets and Liabilities as of 30 June 2025**

|              |                   |                   |                   |
|--------------|-------------------|-------------------|-------------------|
| Total Assets | \$162,574,933,798 | Total Liabilities | \$157,108,000,474 |
|              |                   | Net Equity        | \$5,466,933,324   |

<sup>1</sup> Source: <https://marketmilk.babypips.com/symbols/BTCUSD/volatility?source=coinbase>.

These figures give Tether USD a capital-to-assets ratio of 3.36 percent, low by historical banking standards. Alternatively stated, Tether USD is leveraged approximately 30:1.

An “independent auditor’s report” (LBDO 2025) subdivides the assets as follows:

| <b>Asset Category</b>                                  | <b>Amount in USD</b>   |
|--------------------------------------------------------|------------------------|
| 1. Cash & Cash Equivalent & Other Short-Term Deposits: |                        |
| U.S. Treasury Bills <sup>4</sup>                       | 105,518,993,610        |
| Overnight Reverse Repurchase Agreements <sup>5</sup>   | 16,341,965,339         |
| Term Reverse Repurchase Agreements <sup>6</sup>        | 1,666,870,344          |
| Money Market Funds <sup>7</sup>                        | 6,345,999,587          |
| Cash & Bank Deposits <sup>8</sup>                      | 32,430,726             |
| Non-U.S. Treasury Bills <sup>9</sup>                   | 48,169,774             |
| <b>Subtotal</b>                                        | <b>129,954,429,380</b> |
| 2. Corporate Bonds <sup>10</sup>                       | 14,605,090             |
| 3. Precious Metals <sup>11</sup>                       | 8,725,417,224          |
| 4. Bitcoin <sup>12</sup>                               | 8,928,174,931          |
| 5. Other Investments <sup>13</sup>                     | 4,815,162,084          |
| 6. Secured Loans <sup>14</sup>                         | 10,137,145,089         |
| <b>Total (1+2+3+4+5+6)</b>                             | <b>162,574,933,798</b> |

Using the traditional banking concept of reserves (vault cash plus demandable deposits), Tether USD’s reserves (cash and bank deposits, assuming that its deposits are all redeemable on demand) give it a 0.02 percent cash reserves to liabilities ratio, extremely low by traditional banking standards. If we add its money market funds, the figure is 4.06 percent, within the normal historical range for a bank without imposed reserve requirements. In October 2018

Tether briefly de-pegged to 88 cents, reportedly on worries about the solvency of its affiliated firm Bitfinex, but it recovered.

The latest reported figures for USDC's balance sheet (<https://www.circle.com/transparency>) are as follows:

**USDC Issuer Assets and Liabilities as of 31 July 2025**

|              |                  |                   |                  |
|--------------|------------------|-------------------|------------------|
| Total Assets | \$64,000,903,241 | Total Liabilities | \$63,935,611,557 |
|              |                  | Net Equity        | \$65,291,684     |

These figures give USDC a capital-to-assets ratio of 0.10 percent (one-tenth of one percent, or one-thousandth). Alternatively stated, USDC is leveraged approximately 1000:1. USDC thus has an extremely thin cushion to absorb asset losses before it becomes insolvent. This cushion was depleted in the failure of Silicon Valley Bank in March 2023. USDC's issuer (called Circle) had uninsured deposits in SVB that made up around 8 percent of its assets, far exceeding its net equity, so USDC became insolvent when SVB failed. The coin de-pegged, falling to around 88 cents, until the FDIC announced that it would exercise its discretion to make all uninsured SVB depositors whole.<sup>2</sup>

Of its \$64,000,903,241 in total assets on 31 July 2025, USDC held a reported \$9,596,056,073 in net cash assets. Its cash reserve ratio was thus 15.0 percent. The remainder of its assets were in a proprietary mutual fund holding only US Treasuries. Circle refers to all of USDC's assets as "reserves," not only its cash assets.

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<sup>2</sup> For an analysis of this event see Watsky et al. (2024).

## **Run-proneness and non-par pricing as rationales for restricting stablecoins**

The leading argument for restricting stablecoins rests on a negative reading of the history of private payments systems, emphasizing the problems of bank runs and non-par circulation, and the belief that stablecoins are similarly vulnerable. This emphasis, however, distorts the actual historical record. In a 2021 speech, Federal Reserve Governor Lael Brainard (2021) gave a concise statement of the argument:

A predominance of private monies may introduce consumer protection and financial stability risks because of their potential volatility and the risk of run-like behavior. Indeed, the period in the nineteenth century when there was active competition among issuers of private paper banknotes in the United States is now notorious for inefficiency, fraud, and instability in the payments system.

Gary B. Gorton & Jeffery Y. Zhang (2024) offer a more academic version of the argument. They summarize it as follows (p. 909):

... new technology has recreated circulating private money in the form of stablecoins, which are similar to the banknotes that circulated in many countries during the nineteenth century. The implication is that stablecoin issuers are unregulated banks. Based on lessons learned from economic theory and financial history, we argue that circulating private money is not an effective medium of exchange because it is not always accepted at par and its issuers are vulnerable to destabilizing bank runs.

While the first two sentences of this statement are unobjectionable, the third rests on a one-sided picture of economic theory and financial history.

Gorton and Zhang argue that private money is inherently “not an effective medium of exchange.” To be effective, they write (pp. 911-12), a “money must also satisfy the no-questions-asked (NQA) principle, which requires that the money be accepted in a transaction without due diligence on its value.” In their view private banknotes in the nineteenth century did not, and stablecoins today do not, satisfy the NQA principle: “[S]tablecoins are not yet money because they do not satisfy the NQA principle and so cannot be efficiently used as a medium of exchange.” Their criticism has been echoed by Hyun Song Shin (2025) of the Bank for International Settlements, who similarly claims that stablecoins fail to provide “singleness”:

Stablecoin holdings are tagged with the name of the issuer, much like private banknotes circulating in the 19th century Free Banking era in the United States. As such, stablecoins often trade at varying exchange rates, undermining singleness. They are also unable to fulfil the no-questions-asked principle of bank-issued money.

There are serious theoretical and empirical problems with the NQA principle. Theoretically, the claim that a candidate medium “must” satisfy the NQA principle to be money, or to be an effective or efficient money, is completely made up.<sup>3</sup> It is not derived from any

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<sup>3</sup> Gorton and Zhang do not explicitly distinguish among the terms “inefficient,” “ineffective,” and “not money,” but seem to use them interchangeably.



fundamental principle or standard taxonomy of monetary theory. Empirically, the claim has been repeatedly falsified. It is contradicted by the nearly universal voluntary use of banknotes in the nineteenth century, and the significant voluntary use of stablecoins today, as seen in the greater than \$93 billion in daily transaction volume reported in Table 1. Crypto analyst Nic Carter wryly tweeted in response to Gorton's and Chang's working paper that "central bankers 'proving' that stablecoins don't work in theory because they violate some obscure econ principle, meanwhile, us hapless practitioners use stablecoins as money to the tune of \$10-30b/day."<sup>4</sup> Today the volume of the tune is many times greater. But NQA is not even an obscure principle of monetary economics.

The leading stablecoins are widely accepted (with effectively no questions asked) by a sizable set of users. Those who accept USD Tether or USDC or another stablecoin do not first check the current price on CoinMarketCap or Coin Gecko. They know that the price is seldom more than \$0.0005 away from \$1.00.

When Gorton and Zhang (p. 912) write that "The most economically efficient forms of money are ones that maintain a uniform price at par," they misuse the term "economically efficient" because they fail to consider other costs and benefits of using various forms of money. It is reasonable to say that uniform par valuation ( $\pm 0.0000$ ) is preferred to minor deviations from par ( $\pm 0.0001$ ), other things equal, but that preference is not the only thing that matters when other things are not equal. Consider a head-to-head comparison of USDT transfers with bank wire transfers. Both methods provide near-instantaneous settlement. During the week ending 19 September 2025, the difference between Tether's momentarily highest traded value and its lowest value, as recorded on Coinmarketcap.com, was \$0.0009. The greatest possible loss from

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<sup>4</sup> [https://x.com/nic\\_\\_carter/status/1416801282317332481](https://x.com/nic__carter/status/1416801282317332481)

buying \$1000 USDT with USD, and later spending it, would have been 90 cents. Because the trend in the price of USDT is completely flat, the expected loss is zero. “Gas” fees for transferring USDT tokens (according to <https://gasfeesnow.com/>) on 19 September 2025 under 1 cent on the platforms Aptos, Avalanche, Binance, Polkadot, Polygon, and Solana, and were under 3 cents on Ethereum. Meanwhile, the wire transfer fees charged by Bank of America, Chase, and Wells Fargo, as surveyed by Nerdwallet (Tierney 2025), were \$15 for incoming domestic or international wire transfers in USD, \$25-45 for outgoing domestic wire transfers, and \$40-45 for outgoing international wire transfers.

Tether is presumptively privately efficient, all things considered, because it is demonstrably the preferred medium, for a large volume of payments even though not for all payments. There are transactors outside its usual range of circulation who are unfamiliar with it. They would ask questions or simply not accept it if it were offered to them. While it is therefore true that Tether USD is not *universally* accepted in dollar transactions, universal acceptance has never been a defining characteristic of money. The textbook definition of money is an item that serves as a *commonly* accepted medium of exchange. Neither Federal Reserve Notes, nor insured deposits, nor any other form of dollars is universally accepted in all transactions. The fact that ordinary offline retailers do not commonly accept Tether does not make it an ineffective or inefficient medium of exchange in other uses, any more than the fact that some retailers do not accept deposit transfers via cheque (they might bounce), or via debit card (the required hardware is too costly), or do not accept \$100 bills (they might be counterfeit), means that those forms of dollars are not money. To say (p. 912) that efficiency or moneyness requires “*no* questions asked” (where “NQA means that both parties to a transaction must agree that the money be accepted at par—a ten-dollar bill should be accepted as being worth ten dollars, not a penny

less”) inappropriately imposes a discrete 0/1 criterion on the costs of using a medium of exchange, costs that in practice are a matter of degree.

Gorton and Zhang employ the NQA principle to argue that historical private banknotes and present-day stablecoins are volatile in value and thus inefficient as media of exchange. In their view the past use of private banknotes that did not circulate at par was a problem that governments efficiently eliminated; likewise the present use of stablecoins is supposed to be a problem to be eliminated. Only the national government, they indicate, can provide NQA money. According to their Table 1 (p. 913) the only ways to achieve NQA status for stablecoins are (1) have them fully guaranteed by the national government, like FDIC-guaranteed bank deposits today, (2) require them to be backed 1:1 by short-term Treasury or central bank liabilities, like \$1-per-share government money-market funds today, or (3) replace them with a central bank digital currency.

The view that that non-government-guaranteed private money systems are typically and were historically prone to serious volatility is contrary to the banking history research of the last 50 years. Minimally restricted banking systems—free banking in the sense of nearly unrestricted banking—were usually more stable (and more competitive) than more heavily restricted systems. To cite two common head-to-head contrasts from the nineteenth century: (1) Scottish banking was less restricted and more successful than English banking at delivering safety (and competitive pricing), and (2) Canadian banking was less restricted and similarly more successful than United States banking. It is not necessary to review the evidence in detail here. Kevin Dowd (2023) collects a wide-ranging set of case studies of free banking systems. Ignacio Briones and Hugh Rockoff (2005) and Lawrence H. White (2015) survey the literature on these historical cases, and find less restricted banking systems more successful on the whole than more restricted

systems. The comparison of stablecoins to the private banknotes of the 19<sup>th</sup> century therefore does *not* make a prima facie case for legally restricting stablecoins.

Gorton and Zhang's banking history (pp. 939-49) unfortunately ignores the wide range of international evidence, focuses entirely on the antebellum banking systems of the United States, and blurs the distinction between free banking in the near-laissez-faire sense and so-called "free banking" in the sense of the highly restricted antebellum systems in some of the United States. They make zero reference to Scotland's free banking experience.<sup>5</sup> Gorton (1985) was once aware of its importance, having written that "the Scottish free banking experience seems to have been dramatically different from the American free banking experience, which is generally viewed as a failure." But Gorton and Zhang would have had a hard time squaring their argument with a successful near-laissez-faire banking system in which banknotes from many private issuers circulated widely at par.

In the antebellum US experience, each bank was confined to the single state where it was chartered (no interstate branching), and in "unit banking" states to one office only. Each state had its own system of restrictions. Banking systems in the New England states of the northeast had relatively free entry (legislatures were least restrictive of the number of bank charters) and were the most successful at achieving regional par circulation under the clearing system administered by the Suffolk Bank of Boston. Other states' legislatures used chartering to restrict competition for the benefit of incumbent banks. "Free banking laws" in that context were a reform that granted a charter to any comer who met the legal requirements. The most important

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<sup>5</sup> They offer a single footnote reference (p. 959 n. 166) to Canadian free banking experience, in which they write that "the private money did not achieve the NQA principle." They cite a Bank of Canada working paper (Fung, Hendry, and Weber 2017). For a detailed critique of the Fung et al. working paper see Selgin (2017).

requirement was to hold state-approved assets as collateral against their banknote liabilities. Some “free banking” states for fiscal reasons compelled the “free banks” to buy the state government’s own bonds as collateral. (This model was later adopted by the Union government during the Civil War.) Others allowed the bonds issued by other state governments, and sometimes valued them at par for collateral purposes. The result was that their banks held poorly diversified portfolios of bonds they could buy well below par, with the knock-on effect that the banks failed in large numbers when those bonds dropped in value. For example, Rolnick and Weber (1985, pp. 7-8) find that 52 of 107 Wisconsin banks failed or closed in the period June 1860 to June 1861. The failed banks held 84 percent of their note-backing collateral in the bonds of five Southern states. Southern bond prices fell sharply with the approach of the US Civil War.

George Selgin (2021) spells out the story of the US “free banking era” and its largely mythical “wildcat banks” in greater detail, drawing especially on the work of economic historians Hugh Rockoff (1974; 1985), Arthur Rolnick and Warren Weber (1983), Gerald P. Dwyer (1996), and Matthew Jaremski (2010). The moral of the story is that banking instability and the failure of banknotes to circulate widely at par (outside of New England) in the antebellum US was due to legal restrictions on their issuers, not due to the issuers being private. It is not a basis for arguing that private stablecoins should be restricted.

To their credit Gorton and Zhang, unlike Brainard, do not advance the wildcat banking myth. They write (p. 944) that in the antebellum period, “Bank failures were not due to wildcat banking as has often been alleged.” Their concern instead is with the “varying discounts” on banknotes that “made actual transactions (and legal contracting) very difficult. In other words, it was not economically efficient. There was constant haggling and arguing over the value of notes in transactions. Private banknotes were hard to use in transactions.” They do not, however, place

the blame for discounts squarely where it belongs, on anti-branching restrictions that made it impossible for banks to set up branches to redeem their notes at par away from their home cities.

### **How stablecoins are like and unlike free banknotes**

Like banknotes in nineteenth-century Canada or Scotland, stablecoins are issued competitively. They typically do not bear interest when held in a personal wallet (and this will be illegal when the Genius Act comes into effect), which means that issuers compete on non-price dimensions to attract users. USDC held in a Coinbase account, by contrast, pays interest-like “rewards” at a rate that rises and falls with short-term US Treasury rates. In the nineteenth-century United States, with limited-liability banks, issuers used to advertise the dollar amount their capital—the cushion for absorbing asset losses—to convince customers that their notes and deposits were trustworthy. In Scotland, with unlimited shareholder liability, new banks would sometimes advertise the names of their wealthiest shareholders. Before deposit insurance, capital ratios of 20 percent were typical. For reasons not fully understood, Tether and USDC do not hold ample capital (nor of course do they make a selling point of the size of their capital or ratio of capital to assets). To be fair, extreme leverage was the only way for a stablecoin issuer to earn a normal rate of return on capital during the period of near-zero short-term interest rates, while holding a portfolio of short-term assets and imposing no fees on stablecoin holders. While Tether’s reported capital ratio has normalized with the normalization of short-term interest rates, USDCs remain extremely low. To reassure customers, both issuers emphasize that their liabilities are fully backed by safe assets. Tether’s portfolio listed above, devoting about 20 percent to the asset set {corporate bonds, precious metals, bitcoin, other investments, and secured loans}, is clearly not risk-free (which would mean holding only deposit accounts at the Federal

Reserve, or other fully insured deposits, or overnight Treasury obligations). USDC's is closer to risk-free, now that it has reduced its holdings of uninsured bank deposits.

For the typical private banknote issuer, notes in circulation were around half of liabilities (deposits were the other half, not all of them redeemable on demand). For Tether and USDC, tokens in circulation are 99.9 percent of liabilities. Understandably, given their commitments to keep their tokens at \$1.00, which requires the ability to immediately buy back all unwanted tokens whenever demand to hold them declines, their portfolios are dominated by easily liquidated assets. Note-issuing banks, by contrast, could safely hold illiquid assets like loans in proportion to their time deposit liabilities.

Both Tether and USDC speak of *redeeming* their tokens at \$1 each. This indicates a debt-type obligation similar to the obligation stated on the face of a typical \$1 banknote, "Will pay the bearer \$1 on demand at our offices." In their user agreements, however, both Tether and USDC include escape clauses. Tether's (at [tether.to/en/legal/](https://tether.to/en/legal/)) reads as follows:

Tether reserves the right to delay the redemption or withdrawal of Tether Tokens if such delay is necessitated by the illiquidity or unavailability or loss of any Reserves held by Tether to back the Tether Tokens, and Tether reserves the right to redeem Tether Tokens by in-kind redemptions of securities and other assets held in the Reserves.

This is an emergency option clause, never yet invoked, not a statement of daily procedure. Because its business depends on maintaining continuous \$1.00 valuation within a fraction of a tenth of a cent, Tether tokens in everyday practice are debt claims redeemable at par. Gorton and Zhang (pp. 923, 965), citing the emergency clause, incorrectly categorize USD Tether as an

equity claim, “similar to money market funds” with a fixed \$1 share price, although they correctly categorize USDC and other stablecoins as debt claims.

Gorton and Zhang worry that stablecoins are run-prone:

During times of heightened economic uncertainty, the quantity [of a money in circulation] can adjust very quickly to zero in a bank run, a situation in which the backing of the money becomes suspect. Stablecoin issuers are vulnerable to these bank runs, which can spill over into the broader economy.

The wording that “in a run ... the backing of the money *becomes* suspect” [emphasis added] suggests the Diamond-Dybvig (1983) model depicting a bank run as randomly sparked and self-validating (because hasty asset sales deplete the bank’s net worth), rather than sparked by news that the bank may already be insolvent, or in other words that its assets are suspect before the run begins. Gorton (1988, p. 752) previously advanced the latter view, the “bad news” theory of historical runs: “Banking panics during the U.S. National Banking Era were systematic responses by depositors to changing perceptions of risk, based on the arrival of new information rather than random events.”

Are stablecoins run-prone? It does not seem so to date. The de-pegging of USDC in 2023 was due to its pre-run insolvency, caused by the failure of Silicon Valley Bank in which USDC imprudently held uninsured deposits in excess of its net worth, not to its assets becoming suspect due to a run. The thin capitalization of USDC and some other coins is bound to make their holders alert to news, however. That any buyer of a non-interest-bearing claim prefers low



default risk, other things equal, suggests that stablecoin users should prefer an issuer who provides greater evidence of net worth sufficient to absorb all but the most improbable asset losses. The stablecoin market is still young. It may be that new entrants will attract customers by offering better capitalization and better diversification. Competition for users may compel better asset disclosures and higher capital ratios than we have seen so far. But perhaps not. There may be some explanation yet to be uncovered for why users haven't demanded greater evidence of capital adequacy so far.

A major contrast between banknotes and stablecoins is that banknotes were held by almost everyone. Workers could receive their wages in banknotes, and could spend them on rent and groceries, without having bank accounts. Stablecoins, by contrast, are held mostly by participants in cryptoasset markets. Tether's website (<https://tether.io/news/tether-reopens-account-verification-and-direct-redemption-of-fiat-from-its-platform/>) speaks of its policies, "[d]esigned with Tether's professional investor audience in mind." In this respect Brainard's concern about stablecoins being "widely adopted" seems premature.

Promotional copy currently on the website (<https://www.circle.com/usdc>) of USDC's parent company Circle ("USDC enables businesses to offer payment connectivity and dollar-backed financial services to more people in more places"), however, suggests that Circle seeks to attract a wider business clientele who want faster-settling global dollar payments. As previously noted, the exchange platform Coinbase offers reward-bearing USDC account balances. Stablecoin issuers are hoping that clients are willing to leave the mainstream banking system, sacrificing FDIC coverage, for competitive returns and better payment services. Until the Genius Act, the attitude of regulators to stablecoin users seemed to be "caveat emptor." There is now a

non-profit stablecoin rating agency, Bluechip.org, that aids stablecoin users by providing online at zero cost its rating of various stablecoins' safety and soundness.

### **Network effects as a rationale for restricting stablecoins<sup>6</sup>**

In the same speech quoted above, Brainard (2021) worried about the growing circulation of stablecoins pegged to the US dollar, and about digital private money more generally. Part of her worry was expressed in an unclear description of what stablecoins offer. She warned: "If widely adopted, stablecoins could serve as the basis of an alternative payments system oriented around new private forms of money." To be clear, while US dollar stablecoins do offer alternative payment rails, wallet-to-wallet transfers via blockchains rather than account transfers cleared through the central bank, they do not offer a new unit of account or monetary standard. The US dollar to which they are pegged remains the basis, or medium of redemption, for payment media.

In explaining her concern about an alternative to the status-quo payment rails, Brainard seemed to conflate network economies with scale economies:

Given the network externalities associated with achieving scale in payments, there is a risk that the widespread use of private monies for consumer payments could fragment parts of the U.S. payment system in ways that impose burdens and raise costs for households and businesses.

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<sup>6</sup> This section draws heavily on White (2021).

To be clear, although stablecoins and Bitcoin can both be considered “private monies,” their implications are different. Greater use of Bitcoin rather than dollars in payments would reduce the scale of the dollar network, but greater use of dollar stablecoins in place of dollar bank accounts has no such consequence. Network effects of a common *monetary standard* (more users make adopting that standard more beneficial for each user) and economies of scale in payment processing are distinct phenomena.<sup>7</sup> Network effects in payments are associated with the widespread adoption of a common monetary standard or unit of account. Scale economies (declining marginal production cost) *up to a point* characterize clearing and settlement systems. These economies need not be so extensive that a single national clearinghouse is most efficient. The huge volume of daily transactions in the New York foreign exchange market—nearly equal to the daily volume on Fedwire—continues to be cleared efficiently (to all appearances) on the CHIPS system by the private consortium The Clearing House (formerly the New York Clearing House Association). No informed observer, to my knowledge, suggests that moving forex clearing to the Fedwire system would better achieve efficient scale.

The US already has “the widespread use of private monies for consumer payments,” of course, in the sense that transferable bank account balances are monies issued by private commercial banks. (Brainard’s language seems to suggest that only stablecoins and cryptocurrencies are private monies.) Just as there is no fragmentation of the dollar unit-of-account network from the issue of dollar-denominated checking accounts by thousands of banks, there is none from the proliferation of dollar stablecoins.

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<sup>7</sup> Although Brainard spoke of “externalities,” network effects need not involve uncaptured or *external* effects. There are no externalities at the margin once everybody who it is socially efficient to have join *has* joined the network (because social and private network benefits coincide), or if the network is proprietary and the proprietor appropriately subsidizes marginal joiners.

Dollar-denominated stablecoins can in fact be expected to enlarge the dollar unit-of-account network by enabling dollar-denominated payments outside the US where dollar checking accounts are inaccessible. (In this respect they enlarge the dollar network much as offshore dollar banking systems do.) The use of dollar stablecoins outside the US is in this respect similar to the current use of Zelle, the inter-depositor transfer system provided by a consortium of US banks, for dollar-denominated transactions in Venezuela. The use of dollar stablecoins by traders in cryptoasset markets, or offshore, does not in any evident way impose burdens or raise transaction costs for US households and businesses.

### **The GENIUS Act's restrictions**

The “Guiding and Establishing National Innovation for U.S. Stablecoins” Act, or GENIUS Act, was signed into law in July 2025. Its provisions become effective in January 2027. The main provisions can be summarized (Anonymous 2025) as follows:

1. Only subsidiaries of federal or state-chartered banks, or federally supervised non-bank institutions, may issue stablecoins. State supervision is sufficient only if the state framework is federally certified.
2. Non-financial firms are prohibited from issuing stablecoins unless they receive special dispensation.
3. Foreign stablecoin issuers are permitted to issue payment stablecoins in the United States only if they meet the licensing and compliance requirements.
4. US trading platforms may not list non-compliant stablecoins.

5. Stablecoins must same-day redeemable at par, and fully backed with approved safe and liquid assets (such as Treasury bills, Treasury bond collateralized repos, reserve balances at the Fed).
6. Issuers must certify monthly that they hold full backing and meet capital and liquidity requirements to be established by federal and state regulators.

The legislative history of the Act is beyond the scope of discussion here, but two factors motivating its passage can be noted. First, many supporters of the Act have embraced the argument, mentioned above, that the global spread of dollar stablecoins will enhance the benefits the US receives from the international dominance of the US dollar as a medium of exchange. These include fiscal benefits, discussed below. Second, the leaders of Circle, issuer of the second-largest USD stablecoin, have for years emphasized their own compliance (by contrast to Tether) with existing legal restrictions on money transmitters, and lobbied for federal restrictions on stablecoins, presumably to increase their market share at the expense of Tether.

Supporters of the Act expect it to encourage growth in the holdings of dollar stablecoins, which combined with rules to require domestic issuers hold US Treasuries or deposits at the Fed as backing will increase the demand for US Treasuries, enabling greater debt financing of federal government spending. For example, Treasury Secretary Scott Bessent tweeted on 18 August 2025 that “Stablecoins will expand dollar access for billions across the globe and lead to a surge in demand for US Treasuries, which back stablecoins. It’s a win-win-win for everyone involved: stablecoin users, stablecoin issuers, and the US Treasury Department.”<sup>8</sup> Like the National

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<sup>8</sup> <https://x.com/SecScottBessent/status/1957489664870302091>

Banking Acts passed during the US Civil War, the GENIUS Act is partly a fiscal measure, compelling a class of intermediaries to buy federal debt, in the guise of a regulatory reform.

It is doubtful that the GENIUS Act will increase the uptake of dollar stablecoins across the globe. Stablecoins are already available across the globe to anyone with internet access. Tether has attained market leadership because it has proven itself reliable and easy to use despite—or because of—its history of minimal compliance with US legal restrictions. If most global users wanted a stablecoin more transparently backed by low-risk assets, based in the United States, and with the imprimatur of US regulatory authorities, USDC would be doing a larger business than Tether. If there is no increase in the global holding of dollar stablecoins, then there is no increase in the demand for US Treasury debt.

Proponents of the Act's provision to have all dollar stablecoins backed by the same set of US government liabilities think that such uniformity, eliminating stablecoins over-collateralized with crypto assets, will increase potential users' confidence in stablecoins. Creating a stablecoin monoculture, however, increases the danger of a systemic crisis. A negative shock to the value of US Treasuries will endanger all stablecoins, rather than some less than others. When all coins have the same backing, any exodus from one stablecoin implies an exodus from all, rather than a switch from some coins to others. An exodus from all raises the possibility of a deviation-amplifying feedback loop, where liquidation of stablecoin issuers further depresses the price of Treasuries, and so on.

### **The Bank of England's proposal to restrict stablecoin use in the UK**

In September 2025 the Bank of England circulated a proposal to cap the value of stablecoins that an individual or business in the UK is allowed to hold at £10,000 to £20,000.

The BoE is said to be concerned that outflows from banks into stablecoins would shrink bank intermediation and could be destabilizing. Critics have called the plan unenforceable, and noted that neither the US nor the Eurozone imposes such a cap. Nor is there a cap on the value of bank deposits allowed (Masnavi 2025). A more fundamental criticism is that the authorities should not try to preserve the status-quo payment system from losing its clientele when the public prefers an alternative system. To do so limits personal liberty and economic efficiency.

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