

## STABLECOINS AND THE FORGOTTEN MERITS OF FRACTIONAL RESERVES

Modernity sometimes conceals, under new guises, a return to old precepts: a currency backed 100% by the safest assets, bank deposits guaranteed by tangible reserves, the search for unfailing financial stability. Stablecoins (digital tokens backed by highly safe and liquid assets) are part of this logic. However, in our modern economies, banks only keep a small fraction of deposits in reserve with the Central Bank: this is the principle of "fractional reserves" which gives them the ability to create money (the remaining deposits can be allocated to credit). Beyond the intellectual interest that they attract, stablecoins raise a broader question: if their use were to become widespread, would they not risk making it more difficult to finance the economy?

### AN ATTRACTIVE PROPOSITION THAT IS STILL ONLY marginally USED

Each token issued is backed by the same value of "reserve assets" in the form of bank deposits or short-term sovereign securities denominated in the currency to which the stablecoin is pegged (the dollar in 99% of cases). This fully backed architecture is appealingly simple and reassuring as it promises that each unit can be exchanged at any time for secure assets in official currency. In practice, stablecoins are rarely exchanged at exactly 1:1<sup>1</sup>.

These digital tokens, which circulate on public or private blockchains, offer instant borderless transferability, which explains their role in the crypto ecosystem. They are primarily a more stable alternative to first-generation crypto-assets (e.g. bitcoin) and a cross-platform settlement instrument facilitating the circulation of liquidity. Beyond cross-border payments or fund transfers, their adoption remains marginal<sup>2</sup>.

Their potential is nonetheless real: by reducing friction and costs, they are already streamlining some international payments and could quickly supplant, or at least compete with, traditional banking methods, and even the more recent alternatives offered by various fintech service providers.

Stablecoins are experiencing contrasting dynamics on either side of the Atlantic. In the United States, their outstanding amount has grown exponentially (from USD 1 billion at the beginning of 2019 to just over USD 300 billion today<sup>3</sup>), driven by global demand for dollar-backed instruments and the rise of an initially loosely regulated crypto ecosystem. The Genius Act<sup>4</sup>, adopted in July 2025, acted as a catalyst by establishing stablecoins as regulated payment instruments (and therefore, for example, acceptable as collateral for loans).

By contrast, in Europe, the market for euro-denominated stablecoins is still in its infancy (with an outstanding amount of less than EUR 350 million<sup>5</sup>), and most of those in circulation are denominated in US dollars. The entry into force of the provisions of the European MiCA Regulation<sup>6</sup> relating to stablecoins on 30 December 2024 led to the delisting of more than 140 billion of non-compliant stablecoins, mainly Tether's USDT, causing significant market disruption.

### AN OLD LOGIC IN NEW CLOTHES

Behind this apparent modernity lies an old logic: currency fully backed by reserves. Stablecoins are based on existing claims as they do not create new financing but instead recycle financial assets that are already available.

Conversely, when bank deposits increase, they are backed by new loans. Each loan granted by a bank corresponds to the creation of an additional deposit, which finances a new project. This project often creates wealth, is sometimes risky or has a long maturity, and contributes directly to the expansion of the real economy. This is a fundamental difference between banks and non-bank financial intermediaries, as banks do not simply act as intermediaries for existing savings, they create new monetary resources.

### THE PRECEDENT OF THE 'FRANC GERMINAL'

Monetary history provides an illuminating parallel. In 1803, the *franc germinal* was introduced in France as a metallic currency backed by gold and silver. It was completely stable, and embodied French monetary strength for nearly a century.

At that time, banks were already engaging a form of fractional reserve banking, as they did not hold all the gold or silver corresponding to their deposits in their vaults. However, this practice remained heavily constrained by the obligation to convert deposits into precious metals. This rigidity came at a cost: the money supply could not sustainably grow at a rate exceeding that of mining discoveries. It was only with the suspension of convertibility in 1914, followed by the gradual abandonment of the gold standard in the 20<sup>th</sup> century, that the fractional reserve system, increasingly consisting of reserves held at the Central Bank, became the bedrock of the contemporary banking system.

Similarly, stablecoins, which are 100% backed by reserve assets, carry this rigidity within them. They offer stability, but at the cost of a reduced ability to meet growing financing needs if they were to become widespread. The effect would be all the more significant given the important role played by money creation.

1 "(...) there is an inherent tension between their promise to always deliver par convertibility (i.e. be truly stable) and the need for a profitable business model that involves liquidity or credit risk", cf. BIS Annual Economic Report 2025, 23 June 2025, "III. The next-generation monetary and financial system", page 79.

2 "Currently issued mostly in US dollars, stablecoin circulation has doubled over the past 18 months but still facilitates only about \$30 billion of transactions daily—less than 1 per cent of global money flows" Source: Mac Kinsey (2025), "The stable door opens: How tokenised cash enables next-gen payments",

3 Source: DefiLlama

4 Acronym for the US federal law on stablecoins, "Guiding and Establishing National Innovation for US Stablecoins Act". For more information, see Choulet C., Quignon L. (2025) "United States: Will the Genius Act have the expected effects on demand for T-Bills?", *Charts Of The Week, BNP Paribas, 3 September 2025*.

5 Stable Insider – State of European Stablecoins, September 2025.

6 MiCA stands for Markets in Crypto-Assets. Regulation (EU) 2023/1114 of the European Parliament and of the Council of 31 May 2023 on markets in crypto-assets.



## EDITORIAL

4

## THE CONTROLLED RISK OF FRACTIONAL RESERVES

In modern economies, only a small fraction of bank deposits is backed by Central Bank reserves (reserve requirements) and, since 2015, by "high-quality liquid assets" (Liquidity Coverage Ratio – LCR requirements). This partial backing gives banks the ability to lend and create money (deposits) well beyond the reserves that they hold with the Central Bank. This role is regulated by monetary policy, prudential rules and banking supervision in order to prevent inflation and preserve financial stability. Depositors' confidence is reinforced by their ability to convert their deposits into coins and banknotes issued by the Central Bank at any time and at par value, and ultimately by deposit guarantees.

## EUROPE IS DEALING WITH AN URGENT FUNDING NEED

However, preserving money creation is a major challenge: the economy of the European Union must mobilise unprecedented levels of funding in order to remain competitive globally, ensure its defence sovereignty and respond to the challenge of energy and climate transition (see the Draghi and Letta reports). In the face of these challenges, no source of funding can be overlooked. Money creation, capital markets – particularly securitisation – which rely on private savings, and public funding are all complementary sources of funding and will be useful.

## WHEN STABLECOINS UPSET THE BALANCE – A LITTLE

The rise of stablecoins, if confirmed, could profoundly change the nature of bank deposits. If depositors "convert" their deposits into stablecoins and the issuers of these digital tokens buy sovereign securities in order to guarantee their value, retail deposits change in nature: they become deposits of securities sellers, often wholesale, which are more volatile (and to which the regulator logically requires more high-quality liquid assets to be backed up for the purposes of the LCR, which lowers the credit multiplier<sup>7</sup>). When securities are purchased from non-resident sellers, the funds simply leave the domestic banking sphere. This weakens banks' ability to create money and thus finance the real economy as a result. Broadly speaking, the development of stablecoins would increase the likelihood of deposits being converted into digital tokens and leaving the banking system, thereby undermining the stability of deposits that have not yet been arbitrated (but are arbitrable).

The European MiCA regulation and the Genius Act allow traditional banks to issue stablecoins. The monetary analysis remains unchanged when these instruments are pegged to the same currency as that in which the deposits are denominated. They would still be backed by secure assets held on bank balance sheets or ring-fenced in trusts ("fiducie" agreements under French law) and, as such, would still partially challenge the principle of fractional reserves, potentially reducing banks' money creation capacity. However, in the case of a bank issuer, the stablecoin wallet could easily be funded with the amount strictly necessary for payment transactions from the customer's bank account. Therefore, stablecoins' store-of-value function would be reduced to its simplest form, limiting their outstanding amount and their potential impact on banking resources. Furthermore, pegged to another international currency such as the dollar, they would enable European banks to offer their customers a competitive global payment solution without competing with domestic deposits.

## REGULATING WITHOUT STIFLING INNOVATION

According to Andrew Bailey, "*it would be wrong to oppose stablecoins on principle*"<sup>8</sup>. The Governor of the Bank of England believes that they can stimulate payment innovation, provided that they are subject to the same requirements for soundness and protection for their holders as existing currencies. Their future will depend in particular on their regulatory framework, covering aspects such as reserve transparency, resolution mechanisms and holder protection.

## EUROPEAN BANKS FACE THE CHALLENGE OF PAYMENTS

Banks are not standing by idly. In Europe, they have launched the European Payments Initiative (EPI), which has given rise to Wero, a digital wallet designed to offer a European alternative to American payment giants and, indirectly, to stablecoins. The objective is clear: offer instant, secure payments integrated into the European banking ecosystem.

However, this response remains focused on the European internal market and is still in its infancy in terms of penetration, particularly due to persistent barriers to cross-border transactions. Faced with borderless stablecoins, the question remains: how can traditional banks offer global, competitive, instant and interoperable payment solutions?

They have assets at their fingertips: a large customer base, a trusted infrastructure and a capacity for technological innovation. In order not to be left behind, they will need to invest more in international interoperability, user experience and reducing cross-border costs. They cannot be content with defending their turf: they must also invest in that of new entrants.

## CONCLUSION: REGULATE WITHOUT RESTRICTING

The promise of stablecoins in cross-border payments is seemingly attractive, but their 100% backing must not undermine a system that has long demonstrated its ability to finance the economy, particularly households and SMEs – a system whose foundations have been solidly reinforced since 2014 in the European Union through the strengthening of prudential regulation and the establishment of the Single Supervisory Mechanism.

European banks are not doomed to suffer from competition. The EPI/Wero initiative demonstrates their ability to modernise payments in Europe. However, in order to remain credible against global and instantaneous instruments, they will have to go further by strengthening international interoperability, improving the user experience, reducing cross-border costs and forging ambitious technological and strategic partnerships – including, where appropriate, around regulated stablecoins or interoperable banking tokens which would circulate, for example, on the future blockchain currently being developed by SWIFT, the global interbank network for secure payment instructions. However, they need to act quickly.

Laurent Quignon

laurent.quignon@bnpparibas.com

<sup>7</sup> The credit multiplier measures the banking system's ability to create money from a given amount of excess reserves (when there is sufficient demand for credit). Bank deposit outflows or an increase in the proportion of deposits backed by reserves automatically cause it to decrease.

<sup>8</sup> Andrew Bailey, "The new stablecoin regime", Financial Times, 1 October 2025.



BNP PARIBAS

The bank  
for a changing  
world