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Hyperbitcoinisation: Paying for your coffee in bitcoin?

Image source: iStock/ersinkisacik

Introduction

Hyperbitcoinisation is not just about the growing success of bitcoin. It is actually a scenario in which the digital token becomes the world's dominant currency. Overview.

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A currency must fulfil three main functions: medium of exchange, unit of account and store of value. Historically, money was backed by precious commodities such as gold, the production of which required labour and energy, until 1971, when the United States abandoned the gold standard, ushering in the era of fiat currency. Governments print money by issuing public debt without concrete limits, leading to inflation, exponential debt and what is known as currency depreciation, i.e., the gradual loss of its value. Since the 1970s, the dollar has lost around 4% of its purchasing power annually.

This phenomenon, known as currency debasement, is leading more and more investors, institutions, and individuals to turn to bitcoin as a store of value, without necessarily considering the first cryptocurrency as a genuine medium of exchange and unit of account.

Now imagine a scenario in which everyday exchanges, from drinking a cup of coffee to paying the rent, are made in bitcoins. This scenario, known as Hyperbitcoinszation, envisions bitcoin gradually replacing traditional currency to become the world's leading currency, fundamentally altering the way we perceive, spend and save our money.

This article offers a vision of what a world under Hyperbitcoinisation might look like.

Hyperbitcoinisation

Hyperbitcoinisation takes the idea of bitcoin as a digital currency and extends it to a scenario in which it becomes the primary medium of exchange, unit of account and store of value, eventually replacing traditional fiat currencies. This means that you could pay for your coffee, send money to your friend and even invest in the stock market with bitcoin.

Daniel Krawisz, research director at the Satoshi Nakamoto Institute, describes Hyperbitcoinisation as “a voluntary transition from an inferior currency to a superior one, and its adoption is a series of individual acts of entrepreneurship rather than a single monopolist that games the system.” Krawisz describes Hyperbitcoinisation as a revolutionary form of demonetisation, where bitcoin's superior characteristics (decentralised, transparent, immutable, secure, limited supply, digital) lead to the obsolescence of traditional currencies, gradually bringing their value to zero.

There are five possible scenarios for the trajectory of a bitcoin-based economy:

End of fiat currencies: bitcoin definitively replaces fiat currencies in the world's economies. The risk of holding a fiat currency that could rapidly lose value is driving people around the world to switch to cryptocurrencies.

Bitcoin and fiat currencies coexist: bitcoin is becoming as popular as fiat currencies for everyday transactions, without completely phasing them out. Bitcoin is also being adopted by financial institutions.

Semi-Hyperbitcoinisation: here, only certain regions or economies adopt bitcoin as their main currency, while others stick to their traditional national currencies. In 2021, El Salvador made history by becoming the first country to recognise bitcoin as an official currency. The IMF, which was in talks to grant a substantial loan to the financially struggling country, became one of its vocal opponents.

Digital gold: The least drastic change would be to make bitcoin a store of value, comparable to gold, and an efficient way of transferring money abroad rather than using it for everyday transactions. This means that bitcoin would not displace fiat currencies but would remain a store of value.

End of bitcoin: Governments stop Hyperbitcoinisation with a series of repressive measures, ranging from denying Internet access to rationing electricity consumption.

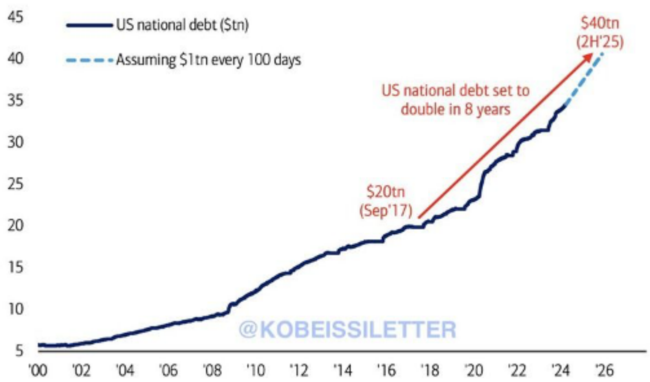
Drivers of Hyperbitcoinisation

1. Inflationary spiral and over-indebtedness precipitate the collapse of fiat currencies

The push towards Hyperbitcoinisation is increasingly fuelled by rising inflation in fiat-based economies. Economist Stephanie Kelton blames fiat currencies for becoming mere " points " that can be manipulated and lack real value. This situation is unsustainable, given current struggles with inflation and examples of hyperinflation in Venezuela (193% in 2023) and Argentina (160.9% in 2023). Against this backdrop, bitcoin offers a striking contrast: a decentralised network beyond the control of central banks, with a fixed supply limited to 21 million tokens. This scarcity makes bitcoin an inflation-resistant asset.

What's more, the United States faces a staggering level of debt, amounting to $34 trillion in 2024 and now increasing by $1 trillion every three months. The permanent cycle of borrowing and accumulating debt without a clear repayment strategy is a deep flaw in the fiduciary regime. This instability is reflected in the price of bitcoin, which is reaching new all-time highs across every currency in the world.

Chart 3: US national debt on course to double in just 8 years
US national debt ($tn) and projection assuming $1tn increase every 100 days



Source: The Kobeissi Letter, BofA

2. Mass adoption of bitcoin

Universal acceptance of bitcoin is accelerating, with over 15,000 global businesses, including giants such as Apple, Walmart, and Disney, accepting payments in cryptocurrency, either directly or via third-party apps. This trend continues as the benefits of bitcoin acceptance outweigh the costs.

The push towards Hyperbitcoinisation could also be accelerated by increased institutional adoption and bitcoin-derived products, such as ETFs, futures, and options, making cryptocurrencies more accessible to traditional investors.

Other countries might follow El Salvador's lead in adopting bitcoin as their official currency, particularly in regions in need of a stable currency. Since 2022, under the initiative of its president Nayib Bukele, El Salvador has pledged to buy one bitcoin a day. By 2024, they had accumulated 5,690 bitcoins (equivalent to around $400 million).

Source: Nayib Bukele on X

3. Central bank digital currencies (CBDCs)

Many politicians are now advocating the creation of CBDCs, government-controlled digital currencies, to maintain their influence on monetary policy. They believe that such a move could weaken cryptocurrencies. Yet it could have the opposite effect. The introduction of government-controlled digital currencies, such as the digital yuan, raises concerns about privacy and personal security, and could ironically drive people towards bitcoin, seeing it as the only true form of independent money.

If an account falls by 10%, for example from $100,000 to $90,000, traders proceed as if the account only had $80,000. Therefore, instead of risking 2% of $90,000 ($1,800), a trader would risk 2% of $80,000 ($1,600). This conservative strategy serves to control losses during adverse periods and keeps traders disciplined and focused on long-term goals.

Advantages of Hyperbitcoinisation

1. Redistribution of wealth

Under a Hyperbitcoinisation regime, the global economy would adopt bitcoin as its primary currency. Bitcoin would no longer be valued in fiat currency; 1 BTC would simply correspond to its own value. The prices of goods and services would be expressed solely in bitcoins, potentially creating a deflationary economic model.

However, for bitcoin to serve effectively as a daily currency, its volatility needs to be reduced, to facilitate day-to-day transactions. According to Willy Woo, a cryptocurrency on-chain analyst, with Hyperbitcoinisation, the bitcoin price will soar and then stabilise, potentially at a very high level.

Hyperbitcoinisation could turn traditional financial systems upside down, from banks to government monetary policies. The mass adoption of bitcoin will lead to a rapid devaluation of fiat currencies, resulting in a redistribution of wealth in favour of bitcoin's early adopters. This new economic framework would also strengthen the legitimacy of other cryptocurrencies, by integrating them into the circular economy.

2. Financial inclusion

The rise of bitcoin could facilitate access to financial services, especially in underbanked areas. Digital, borderless cryptocurrencies ensure transparent, secure transactions. Thanks to blockchain, those who were excluded from the traditional banking system can now participate in the global economy, without resorting to bank accounts expressed in local currency.

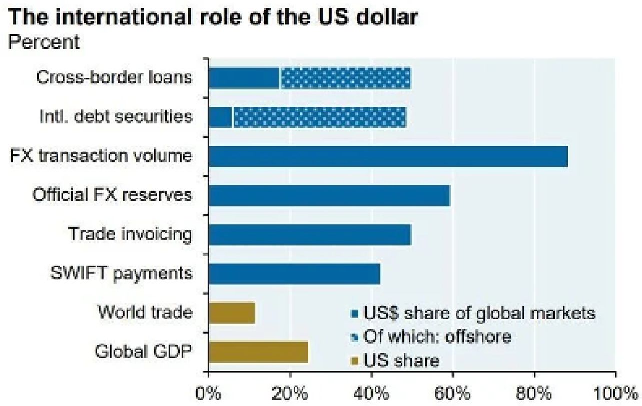
3. Enhanced security

Hyperbitcoinisation will rely on blockchain to offer greater confidentiality and security than traditional financial systems. All transactions are transparent and recorded on the blockchain, linking transactions to encrypted addresses rather than personal data. This reduces the risk of data breaches seen in traditional banks. In addition, the immutability of the blockchain ledger prevents fraud by making transactions irreversible and more secure.

Constraints associated with Hyperbitcoinisation

1. Status of fiat currencies

Investments and transactions in bitcoins are becoming increasingly popular, but their integration into everyday transactions is crucial to their mainstream adoption. According to Chainalysis, over 460 million bitcoin wallet addresses have been created. However, around 90% of these wallets are inactive, leaving just over 46 million wallets with at least $1. Daily bitcoin transactions currently stand at around 450,000, indicating a still limited use compared to global fiat currency transactions.



Source: JP Morgan

2. Volatility

Bitcoin is notorious for its wide price fluctuations, which poses a major problem for its use in everyday transactions. For bitcoin to be considered a unit of account, its value must be predictable and stable, like traditional currencies such as the dollar. Increased liquidity and adoption of bitcoin should reduce its volatility. Nevertheless, it is still difficult to reach a market maturity that would definitively stabilise bitcoin's price.

3. Technological obstacles

While Layer 2's Lightning Network has improved the speed and scalability of bitcoin transactions, also making the process more environmentally friendly, instant processing of billions of transactions remains out of reach for the time being. What's more, as the network grows and transaction volumes increase, so do transaction fees. In April 2024, the average transaction fee for bitcoin was $9.1, well below the 2021 peak of $60 per transaction. Imagine having to pay $60 just to buy a bottle of water. Challenges also include dependence on internet access, high energy consumption by miners and cybersecurity risks such as the double-spending problem or 51% attacks.

Source: Bitcoin Transaction fees, Blockchain.com

4. Governments' response

In a world marked by Hyperbitcoinisation, the traditional monetary policy powers of central banks would be significantly challenged. Governments could resist Hyperbitcoinisation by resorting to repressive measures, or they could adapt to integrate bitcoin into their regulatory frameworks.

Governing a decentralised financial system poses unique regulatory challenges. Governments will need to develop new laws or modify existing ones to manage a currency that transcends national borders and operates outside the traditional banking system. In particular, they will need to adapt tax, securities, and consumer protection laws. Global cooperation will be required to establish standardised regulatory frameworks

Conclusion

Whether bitcoin will become the universal currency remains uncertain, yet its enduring growth positions Hyperbitcoinisation as a plausible future. As the saying goes, "Necessity is the mother of invention", we find ourselves in the heart of a failing fiat experiment and a growing necessity to use bitcoin as a medium of exchange, store of value and potentially unit of account.

For further information

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