

Alphaville's Libra cheat sheet | FT Alphaville

ftalphaville.ft.com

After months and months of speculation, Facebook [has finally revealed the details](#) of its would-be cryptocurrency challenger.

Spoiler alert: it's a glorified exchange traded fund which uses blockchain buzzwords to neutralise the regulatory impact of coming to market without a licence as well as to veil the disproportionate influence of Facebook in what it hopes will eventually become a global digital reserve system. (Boldness in business award incoming.)

Here in any case are the fast facts about Libra along with Alphaville's grounded analysis to help readers navigate through the media circus that is about to unfold in the wake of the release.

1) The currency they're issuing is called Libra.

Alphaville take: An obvious reference to scales and their etymological role in establishing the "pound" as a value unit. Possibly a nod to "balance of payments" and/or balance in general. But also -- given the number of coder geeks involved -- a possible inside joke about bringing balance to the force. (But whose side do they think they are on?!)

2) The Libra association will include any entity that operates a validator node and holds sufficient stake in Libra. At the offset all founder members have contributed \$10m to be part of the network. Founder members include Visa, Mastercard, Spotify, PayPal, Uber, Lyft and Vodafone.

Alphaville take: Don't focus on who is in the association, focus on who is out: notably Apple, Amazon, Google, and *all of the banks*. Don't presume the presence of the more successful payment incumbents necessarily means their interests are aligned with those of Facebook. \$10m isn't too hefty a price tag for insider information about what Facebook is planning and/or a vote at the table when the time comes to sabotage the system. Everyone else of any note is either a loss-leading company yet to make a profit, a VC, a blockchain company, or an actual non-profit.

3) The Association will be a not-for-profit based in Geneva, Switzerland but the assets backing the currency will be distributed across the global system.

Alphaville take: Switzerland isn't what it used to be.

4) To protect users from data-based conflicts of interest, Facebook has created a subsidiary called Calibra through which all its Libra related financial services will be offered.

Alphaville take: Calibra is the only part of the organisation seeking to be licensed, and the license it is going for is only a money transmission license. This is odd given the system's ETF-like structure and grander deposit taking aspirations. Calibra promises only to use users' personal financial data for cross selling purposes if users give them permission to do so. This possibly means Calibra will do everything in its power to incentivise that consent box is clicked.

5) The underlying assets of the Libra fund will be made up of bank deposits (representing a basket of currencies) and other low risk government securities. Customers who transfer value into the system will in effect give up their right to collect interest on their capital. Instead, the interest earned from their deposits and securities will be used to pay the system's operating costs and, if left over, dividend payments to founder members.

Alphaville take: This is hardly a novel strategy. PayPal [came to market](#) doing the same thing until it transpired a money transmission license wasn't enough to allow such operations. Under a money transmission license, entities are limited to keeping deposits in regulated banking institutions. From a regulatory standpoint, the fact Libra intends to use the deposits to purchase interest-yielding securities but only has a money transmission license would usually be considered a big no no.

Questions that need answering relatedly: who will Libra's bank deposit partners be? Will customers understand their interest rights are being given up? What sort of personnel will Libra hire to manage this system. Active security management is not easy, even if the intention is only to keep the fund low risk. This is especially the case in an environment where the safest government paper is often negative yielding.

6) Libra says its Founding Members are "committed to working with authorities to shape a regulatory environment that encourages technological innovation while maintaining the highest standards of consumer protection".

Alphaville take: Openly stating the intent is "to shape a regulatory environment" rather than comply with the existing regulatory environment is a veiled assertion that Facebook is more powerful than the state, and that

regulators should have to buckle to its will. While Facebook probably does have some sway over national bodies, to assume it can also sway international regulatory bodies like the BIS -- which happen [to have a bee in their bonnet](#) about the use and abuse of customer floats by non-banks -- is truly ambitious.

7) Founder members and others will be given the right to purchase Libra investment tokens in return for their capital pledges. These will entitle them to the cash flows derived from interest income in the long run, once the system is profitable.

Alphaville take: The Libra investment tokens sound like a preferential form of bank equity. In a normal banking structure, shareholders receive cash flows (effective rents) only after a share of interest-income is distributed to those funding the system (the depositors), and taxes as well as other expenses are paid. In Libra, the "token holders" strip all the interest income from the users. There is little to no mention of tax throughout all the documents -- but we do know the scheme will be based in Switzerland and the assets held all across the world to improve resilience.

8) Incentive allocations of Libra, funded by investors in private placements, will be distributed to founder members for the purpose of being given away in incentive programmes designed to kick-start the system.

Alphaville take: When it's free, you're the product. We're unclear on what's in it for the investors.

9) Libra will use a network of authorised resellers (a.k.a its version of the authorised participant/primary dealer) to manage the creation and redemption of Libra currency in line with customer demand.

Alphaville take: These resellers will be BBB-rated nonbank entities and will operate via the exchanges the Libra currency will be listed on. Would-be Libra users will also have to buy their Libra from such third parties. The authorised resellers will in effect be provided with privileged status entitling them to potentially very lucrative arbitrage windfalls. But it is unclear if the special arrangements will commit them to making markets even when liquidity conditions are poor. What we know from how ETFs and other NAV-based open-ended funds trade, and how HFT market-making entities behave, is that there are significant risks in over-relying on such third parties, not least because they don't tend to hang around when liquidity conditions get tough.

10) While the currency is pitched as a stable coin, Libra acknowledges that its basket-like nature will ensure the currency fluctuates vis-à-vis the value of domestic or international trade currencies. At the same time, Facebook is gearing this to the unbanked.

Alphaville take: The unbanked, especially in countries with volatile domestic currencies, will be most exposed to such fluctuations. It's hard, in that context, to understand how or why Libra thinks this will empower such sectors in the financial space. The assumption seems to be that because Libra is likely to be more stable than domestic equivalents, this will encourage a sort of Libraisation (*a la* dollarisation) of the respective economies. Except, ironically, the very act of encouraging people to invest in Libra en masse, may spark the sort of local currency depreciation that only worsens the load of poor people in the first instance.

11) The Libra blockchain aspires to be a permissionless system one day, but for now remains permissioned and quite centralised.

It's also unclear why the system technically needs a blockchain at all (though there is clearly PR and regulatory value in presenting the notion that because it's a blockchain system, it's decentralised and thus poses no antitrust issues).

12) While Libra expects that both users of its system and the businesses that service it will have to be bound by existing KYC and AML regulations, it offers little information about how it itself will meet such requirements.

Alphaville take: Libra has created a complex, legal, organisational and technical model that means Facebook and their associates receive deposits, manage money and process transactions without having to register as a bank or do any KYC/AML.

13) The release of the information was very carefully managed, and journalists were given a lot of time to crunch through the material -- a strategy clearly designed to maximise news headlines and impact.

Alphaville take: Watch out for who else might be using the release to bury bad blockchain news of their own. This release from [Digital Asset](#) (effectively [confirming the FT's scoop earlier this month](#) about their pivot out of blockchain and into the smart contract space) is probably worth your attention.

14) Libra reassures that customer privacy will be respected and, unlike Facebook profiles, the number of wallet addresses users can hold will be limitless. At the same time transaction chains will be based on pseudonymous not anonymous data, and made fully public.

Alphaville take: The Libra foundation will not know who the users are, however Facebook (through its Calibra entity and the wallet they provide) will have a reasonable (but not definitive) idea of who the users they are transacting with are because they will almost all be Facebook or WhatsApp users. This is very valuable information. Facebook promises that Calibra data will not be given to the core Facebook entity for advertising purposes. They do not say that Facebook data will not be given to Calibra (which possibly means it could?). A minor change of details of service could theoretically create a scenario where a user inadvertently allows Facebook to receive Calibra data by agreeing to some other minor service.

15) Libra admits that there are "currently unresolved research challenges" and other loose ends that need tying up.

Alphaville take: But there are a helluva lot of loose ends to tie up, including whether or not data will eventually be removed from the public ledger and archived (possibly for a fee). What's more, the Move language that aims to power the smart contract systems that ride atop of Libra is still in the process of being designed. A system-wide charter is also still to be finalised, meaning founder members haven't yet really committed to anything too concrete.

16) Libra says it is committed to transparency.

Alphaville take: And yet it is unclear who will be managing and executing Libra security purchases, what banks will be used to store customer deposits or who the auditors of the reserve system will be.

17) Facebook says as one member among many, its role in governance of the Libra Association will be equal to that of its peers.

Alphaville take: As we know, some members are more equal than others. In that regard, the Libra system will feature a council made up of the initial members who contributed \$10m to the project. Each \$10m investment entitles an entity to one vote in the council, but the same entity cannot present itself twice. But the Libra protocol is expected to have a limitation on the number of active validator nodes (and thus on the number of council members for several years). But there will also be a board and an executive team, with

significant input on distribution and raising of funds. Until we know how many Facebook people are represented in those positions, the jury's out on just how equal Facebook's role will really be.

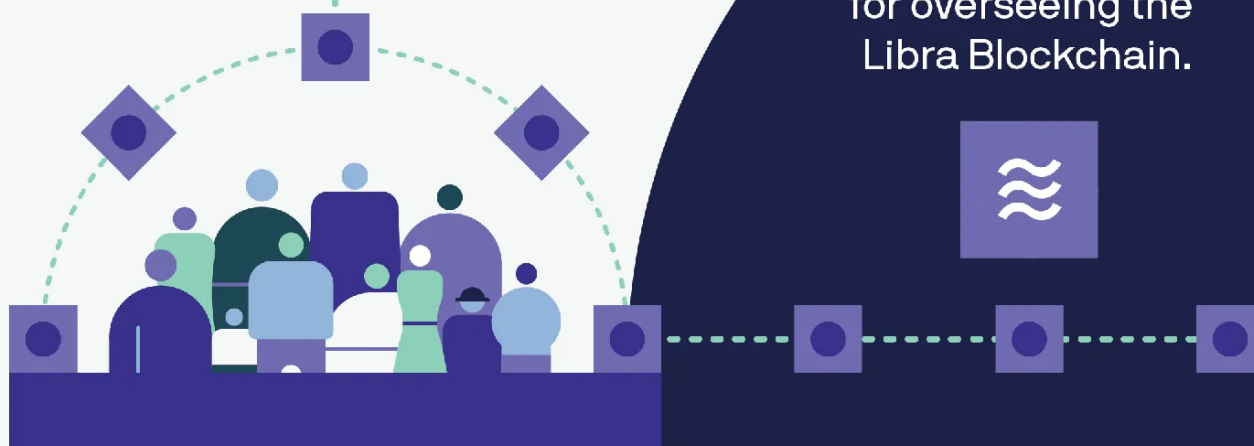
18) Is there a stupid meaningless graphic? Of course there is!

The Libra Association

An independent
not-for-profit organization.



It is responsible
for overseeing the
Libra Blockchain.



It manages the reserve
that keeps the value of
Libra stable.





And that folks, is about it for now.

[Copyright](#) The Financial Times Limited 2019. All rights reserved. You may share using our article tools. Please don't cut articles from FT.com and redistribute by email or post to the web.