Stablecoin Adoption in Australia: Implications for Financial Intermediation and Monetary Policy

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Abstract

This paper examines the macroeconomic and financial stability implications of stablecoin adoption within the Australian financial system. We develop a conceptual framework positioning stablecoins as a contemporary implementation of narrow banking that could drive transition from a traditional two-tiered system toward a three-tiered architecture incorporating specialised payment service providers. Our analysis focuses on how alternative collateral structures, i.e., government securities, bank deposit instruments, or central bank reserves, affect commercial bank liquidity management, high-quality liquid asset (HQLA) requirements, prudential ratios, and monetary policy transmission mechanisms. We demonstrate that stablecoin adoption outcomes are not determined by technology but rather constitute policy choices with significant implications for financial system structure, competition, and stability. We conclude that proactive and explicit regulatory engagement is essential to shape outcomes toward enhanced payment system efficiency and innovation while preserving financial stability and monetary sovereignty.

Keywords

Stablecoins; Narrow banking; Financial intermediation; Monetary policy transmission; Liquidity regulation; Collateral management; Australian financial system; Digital payments; Banking stability

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1. Introduction

The proliferation of stablecoins represents a significant innovation in digital payment instruments, with global market capitalisation exceeding $310 billion as of January 2026. While initially developed as settlement layers for cryptocurrency trading, stablecoins increasingly serve broader economic functions including cross-border remittances, treasury management, and integration with decentralised finance protocols. This expansion has attracted considerable attention from central banks and financial regulators. Australia faces distinctive policy challenges in integrating stablecoins into its financial system. Unlike major reserve currency jurisdictions, smaller open economies face potential dollarisation pressures if USD-denominated instruments lead adoption. Simultaneously, Australia's modern real-time payment infrastructure reduces domestic efficiency gains from stablecoin adoption near-term, concentrating benefits in cross-border cases and specialised applications. Understanding these dynamics requires examining not only technical innovation but also regulatory frameworks, institutional structures, and market forces that shape adoption patterns. For example, Tether (USDT) and Circle (USDC), the leading USD-denominated stablecoins, may create foreign currency exposure for Australian users if widely adopted. While domestic AUD stablecoins have started to emerge, their uptake hinges on regulatory clarity. This dynamic environment, ranging from outright bans to regulatory sandboxes globally, underscores the need for context-specific analysis for Australia.

This paper contributes to the emerging literature on digital currencies and financial intermediation in three ways. First, we develop a conceptual framework analysing stablecoins as a contemporary implementation of narrow banking proposals (Tobin, 1985; Kotlikoff, 2010). Second, we explore how alternative collateral structures affect commercial bank balance sheets, focusing on prudential frameworks rather than solely monetary aggregates. Third, we identify critical policy take-aways that determine whether stablecoin integration enhances or compromises financial stability, monetary sovereignty, and banking system resilience.

2. Conceptual Framework and Literature Review

The narrow banking concept has deep roots in monetary economics. Tobin (1985) proposed separating depository institutions providing payment services from those engaged in credit creation, arguing that combining these functions leads to fragility through maturity transformation and asset-liability mismatches. Kotlikoff (2010) advocated limited purpose banking with complete separation of depository and lending functions.

Contemporary literature explores various implementations of this principle (Pennacchi, 2012; Admati & Hellwig, 2013). Fiat-collateralised stablecoins can be viewed as a market-driven implementation of narrow banking. Stablecoin issuers accept customer funds and issue digital claims redeemable on demand, functionally equivalent to deposits. Unlike traditional banks, they back these liabilities entirely with liquid, low-risk assets and cannot engage in credit creation (Liao, 2022). This positions stablecoins as potential substitutes for traditional bank deposits and as shadow money operating outside traditional regulatory perimeters (Murau, 2017; Aramonte et al., 2021).

The literature on central bank digital currencies (CBDCs) and private stablecoins has expanded rapidly. Brunnermeier et al. (2019) examine how CBDCs could affect bank funding and policy transmission, identifying disintermediation risks if CBDC adoption drains deposits. Bindseil (2020) analyses tiered CBDC architectures to mitigate these concerns. Gorton and Zhang (2023) compare private stablecoins to CBDCs, arguing that private issuers may provide efficient payment services but require robust regulation. Meaning et al. (2018) examine regulatory approaches, emphasising backing asset quality and oversight. Auer et al. (2022) analyse international dimensions, identifying dollarisation risks in smaller economies (this, however, can be mitigated through tax obligations).

Bank liquidity management under Basel III introduced the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) (BCBS, 2013, 2014 and APS 210). These prudential frameworks require banks to hold high-quality liquid assets and stable funding. Bonner et al. (2015) and Gobat et al. (2014) considered impacts of HQLA holdings on funding structures. Stablecoin adoption affects these requirements. If customers migrate deposits to stablecoins, banks lose stable funding sources and must compete for short-dated HQLA with stablecoin issuers. The severity depends on regulatory frameworks governing backing assets. This is a policy choice, not a technical constraint.

Recent literature emphasises that stablecoin outcomes depend on regulatory design choices rather than technology (Bullmann et al., 2019; Adrian & Mancini-Griffoli, 2021).

Globally, the recent Bank of England's consultations on systemic stablecoin regulation (Bailey, 2025) and the Federal Reserve's exploration of specialised “skinny” payment accounts represent a shift toward explicit infrastructure decisions. This suggests a regulatory transition from viewing stablecoins as peripheral innovations to recognising them as potentially systemic components requiring proactive policy engagement.

Locally, Australia operates a floating exchange rate, shifting analytical focus from absolute capital flows to liability composition and stability across institutional types (Debelle, 2011; Kent, 2014). Kent (2014) examines bank funding dynamics, emphasising stable deposit bases. Price et al. (2015) analyse competition for deposits and policy transmission. Our analysis builds on this by examining how stablecoin adoption affects deposit composition and bank funding.

We develop a conceptual framework positioning stablecoins as a potential catalyst for structural transition from a two-tiered system (central bank and commercial banks) to a three-tiered architecture with specialised payment service providers. In this framework: Tier 1 is the central bank (RBA) providing settlement assets and monetary policy; Tier 2 is commercial banks engaging in credit intermediation and payment services; Tier 3 is stablecoin issuers providing payment services backed by safe assets without credit provision. This framework allows systematic analysis of how regulatory approaches and collateral structures affect each tier and their interactions (Figure 1). Additionally, stablecoins currently operate in a legal grey area, raising questions about issuer liability, redemption rights, and the adequacy of oversight. Studies on shadow banking (Pozsar et al., 2013) and systemic risk (Acharya et al., 2013) provide frameworks for analysing how entities like stablecoin issuers fit into broader financial stability considerations. The quality and liquidity of backing assets, such as commercial paper or government securities, and the operational resilience of stablecoin platforms, are key focus areas in the literature (FCA, 2020; IMF, 2021).

3. Australian Context and Adoption Dynamics

In Australia, the New Payments Platform (NPP), introduced in 2018, enables efficient real-time payments across banks, reducing the marginal utility of stablecoins for domestic transactions. Most current usage involves cryptocurrency trading, with emerging use cases including cross-border remittances and integration with decentralised finance protocols; both are focused on settlement efficiency and smart contract-based programmability. Corporate treasury management also increasingly considers stablecoins for specific applications. The empirical question of whether AUD or USD stablecoins will dominate depends on regulatory clarity, infrastructure development, and trust frameworks (Auer et al., 2022).

Several AUD digital currency programs have been recently completed or are underway, highlighting both opportunities and challenges in KYC/AML integration and global interoperability. This includes exploration of CBDCs and potential alternatives led by RBA and DFCRC (Project Acacia).

The Australian government and regulators support innovation, as evidenced by ASIC's regulatory sandbox and relief for pilot AUD stablecoin projects, indicating an openness to experimentation with proper risk management. Other policy responses already under consideration include ASIC's Information Sheet 225 and RG 282, Exposure Draft: Treasury Laws Amendment (Regulating Digital Asset, And Tokenised Custody, Platforms) Bill 2025, and payment reforms legislations.

Notably, stablecoins are not inherently exempt from the existing regulations:

- Regulatory oversight does not hinge on currency denomination of a stablecoin. USD-denominated stablecoins could come under Australian regulation if they are offering their product to Australians and ASIC determines that the issuers should hold financial services licenses, e.g., like Wise (that is also authorised and regulated by APRA as a purchased payment facility).
- APRA could also designate an issuer as a 'Registered Financial Corporation' if it is big enough and engages in borrowing and provision of finance (which stablecoins do by definition). This is not a regulatory designation but would result in stablecoins being included in the monetary aggregates.

Clear frameworks for AUD stablecoins can shape adoption toward domestic instruments, while ambiguity may lead to offshore USD instruments capturing market share, with implications for monetary sovereignty. Importantly, because Australia has a floating exchange rate regime, inflows and outflows to assets denominated in another currency cannot affect the domestic money supply. The capital flows affect the level of the exchange rate, but not domestic liquidity since the Australian banking system operates as a "closed loop" for domestic liabilities.

Successful retail adoption would likely require interest-bearing offerings. If regulations require stablecoins to pay zero interest (indicative direction rather than confirmed policy at present in Australia; existing e-money frameworks in EU and other jurisdictions), they will have limited appeal to retail customers compared with bank money, especially offset accounts, which effectively yield the mortgage rate in interest savings. Hence, retail adoption may concentrate in specific areas rather than broad displacement of deposits, unless there are compliant stablecoin yield products, e.g., offered by exchanges.

This has implications for monetary transmission, as proposed zero-interest products limit transmission to end users compared to interest-bearing deposits. On the other hand, if stablecoin issuers hold RBA reserves, the RBA's interest rate will also directly affect stablecoin conditions via interest paid on these reserves. Potential positive effects include payment system efficiency, reduced cross-border transaction costs, competitive discipline on banks, and potential financial inclusion. The policy challenge is capturing these benefits while managing risks to stability, requiring explicit regulatory design choices rather than passive approaches.

4. Policy Design and Collateral Structures

Regulatory frameworks must specify permissible backing assets for stablecoin issuers due to impacts on bank balance sheets and funding markets. We explore three models:

4.1 Government Securities Model

This model has two potential options: (1) reverse repo structure, where banks lend HQLAs to stablecoin issuers and receive cash in return, and (2) deposit-based structure, where issuers use deposits to purchase short-dated government securities directly in secondary markets and hold them as backing assets. The former creates short-term funding for banks while providing stablecoin issuers with the required HQLA backing. If structured appropriately, this can facilitate HQLA-to-HQLA swaps with potentially neutral LCR impact, as banks exchange one form of liquid asset (securities) for another (cash collateral). The latter may result in a scenario where a bank experiences deposit outflow with no offsetting inflow as the cash ultimately flows to a different institution; it then must replace lost deposits via wholesale funding or contract balance sheet. Regardless, domestic money supply does not contract as a result. The choice between repo and deposit structures represents a fundamental design decision related to how banks interact with stablecoin issuers.

Overall, this intensifies competition for comparatively limited short-dated HQLA supply, potentially tightening spreads, and yields (Debelle, 2011). Large-scale stablecoin adoption could recreate HQLA scarcity, that may be addressed by reinstating the Committed Liquidity Facility (CLF), or alternative arrangements if there were lasting supply issues.

A challenge for the Australian Office of Financial Management (AOFM) is whether to treat stablecoin collateral demand as a policy objective in debt management strategy or remain neutral and issue debt based solely on government funding needs.

This model aligns with narrow banking principles by using public debt as a safe collateral but raises questions about fiscal policy interactions and government debt management strategies.

4.2 Bank Deposit Instruments Model

This model includes NCDs and Interbank Deposits, Term Deposits and Client Money Accounts. In addition to existing term deposits and client money arrangements, regulations could permit stablecoin backing via portfolios of NCDs and interbank deposits. NCDs offer liquidity through secondary market tradability but create concentration risks. Banks gain wholesale funding but at higher costs than retail deposits. If stablecoin issuers liquidate NCD holdings during stress, funding runs may occur, introducing procyclical dynamics.

Term deposits have maturity mismatch concerns if used to back instantly redeemable stablecoins. Client money accounts have distinct legal treatment under Corporations Act frameworks, with implications for creditor priority and prudential classification.

All variants of this model keep funds circulating within the banking system, but have different instrument structure, including liquidity, stability, prudential treatment, and maturity transformation risk profiles.

4.3 Central Bank Reserve (Exchange Settlement Account) Model

Issuers could hold backing assets directly in central bank accounts, e.g., 40% unremunerated central bank deposits and other assets, as proposed by the BoE. Here, deposits migrate from banks to stablecoin issuers, draining bank deposits with no immediate offsetting inflow. Banks must replace lost deposits via wholesale funding or balance sheet contraction, affecting their prudential ratios. An often-overlooked consideration is how direct central bank access affects crisis behavior. If stablecoins are backed by central bank reserves, customers may perceive them as safer than commercial bank deposits during financial stress. Like retail CBDCs (Bidder et al., 2025), this could accelerate deposit flight from banks during crises, amplifying runs, and increasing systemic fragility (Diamond & Dybvig, 1983). The presence of a 'safe haven' accessible to retail customers through stablecoins may fundamentally alter crisis dynamics relative to traditional systems where only wholesale market participants can rapidly shift to central bank liabilities. This model offers strong safety signals to users but raises concerns about disintermediation and competitive equity.

4.4 Comparative Analysis

The impact of each model depends not just on the asset class, but on how funds circulate back to the banking system. The following table compares stablecoin collateral models.

Dimension	Government Securities	Bank Deposit Instruments	Central Bank Reserves (ESAs)
Bank Deposit Impact	Depends on structure: Reverse repo - minimal deposit loss; Deposit-based – deposits may be lost depending on flows	Deposits lost to stablecoins	Deposits lost to stablecoins
Offsetting Flows	Reverse repo: cash inflow to banks as collateral; Deposit-based: indirect (if cash recirculates)	Cash returns directly but as wholesale funding (NCDs, term deposits) or segregated as client money accounts	No immediate direct return flows to commercial banks
HQLA Competition	Yes - issuers compete for government securities	No - creates funding instruments rather than competing for assets	No

	(manageable e.g., via CLF)		
LCR Impact	Reverse repo: potentially neutral (HQLA swap); Deposit-based: moderate (potential 100% runoff risk)	Low to moderate (depends on instrument type and maturity)	Potentially high (permanent deposit loss)
NSFR Impact	Low (depends on structure and maturity)	Low (term deposits improve NSFR; NCDs less favorable than retail deposits)	Low (loss of stable retail funding)
Supply Constraints	Yes - limited government securities market (manageable via CLF)	No - banks can issue instruments as needed	Limited by RBA policy on ESA access
Systemic Concentration	Moderate (diversified securities market)	High (concentrated wholesale funding relationships, especially NCDs and term deposits)	Moderate (direct central bank exposure)
Liquidity Mismatch Risk	Low (securities are liquid)	Varies: NCDs - low (tradable); Term deposits - high (locked but instant stablecoin redemption); Client money - low	Low (reserves are most liquid)
Crisis Amplification	Reverse repo: low (stable funding structure); Deposit-based: low to moderate (depends on recirculation)	High - funding runs (NCDs most vulnerable); term deposits create redemption pressures; client money depends on legal treatment	High - deposit flight to "safer" central bank liability
Monetary Transmission	Indirect (depends on interest-bearing assets and structure)	Indirect (through wholesale funding costs, varies by instrument type)	Direct (interest on reserves, if pass-through permitted; zero-interest stablecoin adoption could weaken transmission)
Regulatory Complexity	Low (established securities market frameworks)	Low (established instruments)	High (requires new framework for non-bank ESA access)

Table 1: Comparison of Stablecoin Collateral Models

These considerations underscore the policy choice aspect, wherein regulators must balance trade-offs among safety, efficiency, and market integrity.

5. Financial Architecture and Monetary Policy Implications

Stablecoin proliferation could transition the system from two tiers to three tiers:

- Tier 1 (RBA): Ultimate settlement assets, monetary policy operations.

- Tier 2 (Commercial Banks): Traditional credit intermediation, payment services, with altered funding composition away from stable deposits.

- Tier 3 (Stablecoin Issuers): Specialised payment services, no credit creation, backed by safe assets.

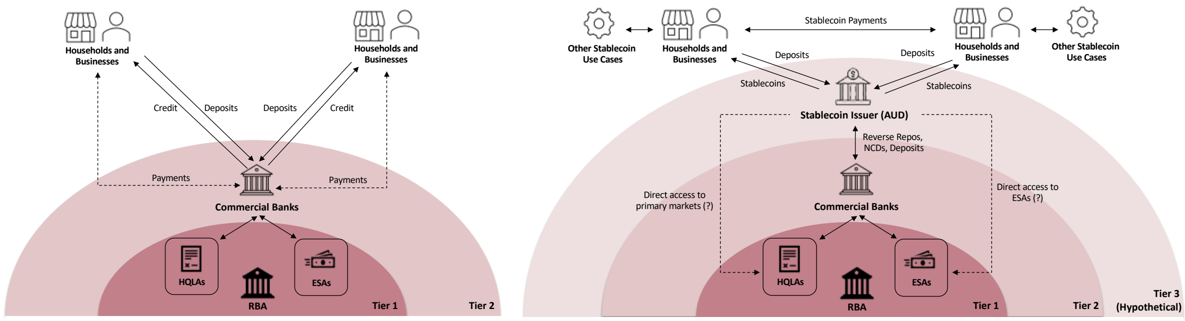

Figure 1: Simplified View of the Two- and Three-Tier Architectures

This structure offers efficiency gains through specialisation but introduces risks via interconnections, potential credit contraction, and altered monetary transmission. Traditional transmission through bank deposit rates may weaken if funds migrate to zero-interest stablecoins, requiring larger policy adjustments. Liquidity management becomes more complex with reserves distributed across new institution types, affecting interbank dynamics and liquidity demand. Systemic risks change: narrow banking reduces maturity transformation fragility, but new risks emerge, such as confidence-based runs on stablecoins, interconnection risks, and procyclical dynamics if stablecoins are perceived safer than deposits (Murau, 2017). Effective risk management must address these new vulnerabilities while preserving benefits.

Technical implementation questions arise if the RBA permits stablecoin issuers to hold backing assets in central bank accounts. Should issuers receive dedicated Exchange Settlement Accounts (ESAs) or use custodial arrangements through commercial bank ESAs? If the latter, do balances held in custody count toward the custodian bank's HQLA? How are custodial relationships treated for concentration risk and systemic importance assessments? These questions have no obvious technical answers but rather represent policy choices affecting competitive dynamics and risk distribution across the financial system.

Diminished transmission through deposit rates may necessitate alternative policy tools including CBDCs or reserve adjustments. New systemic risks span cybersecurity, cross-border coordination, and crypto-ecosystem interconnections. Effective frameworks require mandatory transparency (audits, reserve disclosure), consumer protections, and international coordination through FSB and BCBS to prevent regulatory arbitrage.

6. Conclusion and Policy Recommendations

Stablecoin adoption in Australia presents both opportunities and challenges. Well-regulated stablecoins could encourage innovation, improve the existing fast payment system and lead to cheaper cross border currency transactions (Dark, 2022).

The central finding of our research is that stablecoin outcomes reflect policy choices, not technological designs. Australia has several major levers:

- Collateral framework design is the most fundamental consideration.
- Transaction structure and return flows.
- Issuer licensing and prudential standards, inc. capital and other requirements.
- Access to RBA settlement infrastructure and implications of that.
- Interest-bearing vs. zero-interest products shaping retail adoption and monetary transmission.
- HQLA supply management.
- Proactive regulatory engagement that can shape outcomes toward domestic stablecoins, avoiding offshore dominance and preserving monetary sovereignty.

Our policy recommendations:

- Establish explicit collateral framework balancing safety, availability, and systemic implications. Consider tiered approach based on issuer scale.
- Coordinate AOFM debt management with stablecoin policy, formalise cross-agency coordination mechanism, e.g., by establishing a dedicated Digital Money Council with clear mandates.
- Implement comprehensive monitoring frameworks, track leading and crisis indicators and establish clear thresholds triggering policy review.
- Prepare contingent liquidity and stability tools.
- Foster domestic AUD stablecoins with strong prudential requirements.
- Address systemic importance and concentration risk.
- Engage internationally to share experiences and advocate for Australian economic interests in global standard-setting.

Stablecoin integration into financial system is fundamentally a policy choice. Australian policymakers can shape the outcomes via infrastructure development and regulatory frameworks. Recent actions, such as ASIC’s AUD stablecoin relief, demonstrate willingness to facilitate innovation. The challenge is building comprehensive frameworks for backing assets, prudential requirements, policy implications, and competition dynamics. As frameworks evolve, continued research, monitoring, and adaptive policy responses will be essential. Future research should monitor real-world experiments, such as central bank digital currency pilots and private stablecoin trials, to assess actual market behavior. Evaluating user adoption patterns, technology adoption hurdles, and regulatory impacts will provide empirical grounding to theoretical analyses. Additionally, cross-country comparative studies could elucidate how small open economies like Australia navigate stablecoin adoption compared to larger reserve currency jurisdictions. Thus, regulatory design must be iterative and include stakeholder consultation, adapting to technological developments, and user behaviors. Ensuring that the regulatory framework remains flexible, yet robust will help balance innovation with financial stability and consumer protection. Active engagement with international peers and continuous monitoring will enable Australia to navigate the evolving stablecoin landscape effectively.

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