Facebook “Libra” changes: A Structural Shift in the Business Model

--- A step towards possible “Public Capitalism”

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The Facebook’s Libra White Paper[1] was first released on 18th June 2019 and its business model was altered in October 2019. The House of Representatives Committee on Financial Services requested public testimony from Mark ZUCKERBERG, the Facebook CEO, regarding the Libra project on 23th October 2019[2][3]. Around the same time, the dividend payment system was removed from the Libra proposal but the change was not widely known until December 2019. We support the business model alteration as it advances its attribute of the public good and reduces its profit-making attribute.

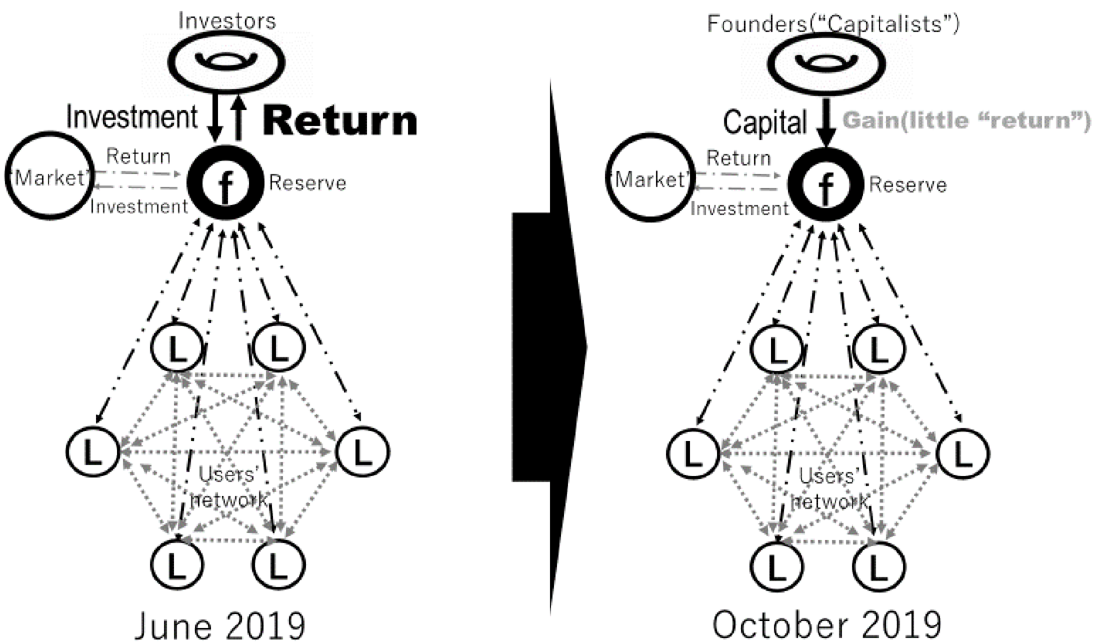

Figure: The change of Facebook “Libra” structure. Removing return from initial

investment,

“Investors” in the original model turn to be “Founders=Capitalists”.

The Libra White Paper was released on 18th June 2019 and it has faced criticism and opposition all over the world, especially in the United States. Most of the criticism was expressed from a political point of view and they didn’t enquire into Libra’s architecture. We revealed some essential problems with the architecture of Libra in our articles in early July 2019[4]. Those articles were early analyses of the Libra structure.
We pointed out 4 main issues on Libra below;

1) Concentration of profits exclusively towards investors
2) Domination of global digital economy = problem of single currency zone
3) Introduction of backing assets = devolution from managed currency to convertible currency
4) Administration of private companies = lack of a neutral mediator in the financial system

The issue which concerned us especially was the concentration of its profit towards its investors by paying dividends exclusively to them. Facebook claims that the Libra Association is a not-for-profit organization. However, funds from investors were to be used to back the stable coin and only investors would receive returns from Libra Reserve, which would be invested into financial markets, whereas Libra users wouldn’t receive any return from them. This original system has an asymmetrical profit distribution structure. In order to resolve the issue, we have developed “NAKOSO-IWAI’s Post Blockchain Neutrality Condition” [5] and pointed out blind spots in arguments by central bankers and government officials in the G20 and G7[6] since the end of June 2019.

1. Withdrawal of big credit card companies and Libra’s business model change

On 23th October, Mark ZUCKERBERG, Facebook CEO, were required to explain the Libra project to the House of Representatives Committee on Financial Services.
Before the hearing, 5 founding members, including Visa and Mastercard, left the Libra Association on 11th October 2019.
We can show these events in a timeline below;

Friday 4th October 2019
Paypal withdrew from the Libra project[7]

Friday 11th October 2019
Mastercard, Visa, eBay, Stripe and Mercado Pago withdrew from the Libra project[8]

By 13th October 2019, the Libra White Paper had been altered and the dividend payment system to its investors was removed. Its updated fundraising process is only from capital. This fact was not widely known until Chris BRUMMER, a law professor in Georgetown University Law Center, pointed it out[9]. Around the same time, the hearing of the House of Representatives Committee on Financial Services was held.

2. Removal of LIT and Shift to Public Capital

The original Libra plan had two separate ways of investing money in the Libra system; Purchasing the Stable Coin Libra or obtaining Libra Investment Tokens “LIT” [10]. The White Paper states that interest on the reserve assets would be used to cover the costs of the system, ensure low transaction fees, pay dividends to LIT holders who provided capital to jumpstart the ecosystem and support further growth and adoption. Therefore, the LIT is classified as an investment. However, the updated White Paper removed this LIT dividend payment system[7].

The right side of the diagram above shows this change from a network structural point of view.

The removal of LIT dividend payment system resolved the problem on concentration of profits exclusively towards investors. In other words, the removal can be interpreted as a one step closer to satisfy the “Nakoso-Iwai Post Blockchain Neutrality Condition”[5][6] . We support the change as it improves its attribute of public good and expect it to improve further.

3 Remaining Issues: Wealth Concentration in a Single Currency Zone

Once a global digital currency successfully starts to circulate, it may bring several changes to our society. If Libra provides financial services to 1.7 billion unbanked people (as of 2019) as Facebook claims, it would cause positive and negative impacts all over the world. One of them would be rapid economic growth in some areas. It would stimulate inflation but the stable coin would alleviate them. However, it would also be a cause of stagnation of local economy growth.

No matter how the stable coin exerts influence on the economy, we are concerned about possible secondary effects, such as an increase of inequity and immobilization of poverty, which would be caused by using a same currency between developed areas and developing areas without an exchange barrier.

According to the Euro criticism by Joseph STIGLITZ[12], wealth would leave a weak economy area and go to a strong one when a single currency is adopted in a wide area. In order to avoid this issue, several public network systems have been proposed. The BANKOR system in the Bretton Woods Proposal by J.M.KEYNES[13] and its theoretical origin, the Multilateral Clearing proposal by Ernst SCHUMACHER[14], are early examples of such system.

Based on analyses of Joseph STIGLITZ and Katsuhito IWAI, we will examine a stable economic growth model of a digital economy and an encrypted asset network in following papers.

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