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From: Peter MacKenzie and Mark Zelmer
To: Stablecoin Watchers
Re: THE STABLECOIN REGULATORY CHALLENGE

Stablecoins are often framed as a niche innovation, something for crypto enthusiasts or a problem best left to market forces. That framing is increasingly outdated. As stablecoins move closer to the financial mainstream, they raise fundamental questions about payments, monetary sovereignty, and financial stability that policymakers can no longer afford to treat as theoretical.

At their core, stablecoins promise something deceptively simple: A digital instrument that behaves like money. They aim to combine the speed and programmability of crypto assets with the price stability of sovereign currencies. That promise explains their appeal, particularly for cross-border payments and settlement. But it also explains why they matter to governments. Anything that functions like money, at scale, inevitably becomes a public policy issue.

Canada's regulatory system has so far approached stablecoins cautiously, and rightly so. Unlike traditional bank deposits, most stablecoins do not come with deposit insurance, lender-of-last-resort support, or clear resolution regimes. Yet many users interact with them as if they were cash equivalents. That mismatch between perception and reality is where systemic risk begins.

It's important to remember that stablecoins are not a single, uniform category. Their risk profile depends heavily on how they are structured, what assets back them, and who governs them. Some are fully backed by high-quality liquid assets and subject to regular audits. Others are opaque, lightly governed, or dependent on complex financial engineering. Treating all stablecoins the same—harmless innovation or uniformly dangerous—misses the point.

For policymakers, the challenge is not whether stablecoins should exist, but under what conditions they should be allowed to scale. History offers a clear lesson: Private money can function effectively, but only when it operates within a robust regulatory framework. Free banking experiments and lightly regulated money substitutes have repeatedly ended in instability, often requiring public intervention. Stablecoins should not be allowed to repeat that cycle.

Payments are a public good. They underpin commerce, trust, and economic efficiency. Allowing large-scale payment instruments to develop outside prudential oversight risks fragmenting the system and weakening confidence. This is particularly true if stablecoins begin to compete directly with bank deposits or are widely used for everyday transactions. At that point, their failure would not be a niche event—it would have economy-wide implications.

Meanwhile, there is also a sequencing problem in current policy debates. Too often, stablecoins are discussed alongside broader crypto innovation, as if they rise or fall together. In reality, stablecoins deserve separate treatment because of their monetary characteristics. Policymakers need to decide first what role, if any, stablecoins should play in the payment system, and then design regulation accordingly. Leaving that role undefined invites regulatory arbitrage.

Some argue that heavy regulation will stifle innovation or drive activity offshore. That concern is not trivial, but it is frequently overstated. Financial innovation has always operated within guardrails. The most successful innovations—credit cards, electronic payments, online banking—scaled because they earned public trust through regulation, not because they avoided it. Stability is not the enemy of innovation; it is often its precondition.

Another critical issue is the relationship between stablecoins and central bank digital currencies. Stablecoins are sometimes portrayed as a private alternative to a digital Canadian dollar. But this risks creating a false dichotomy. A well-designed regulatory framework could allow stablecoins to coexist with public money. The question is not public versus private, but accountability versus opacity.

Transparency is key. Policymakers should require clear disclosure of reserve assets, governance structures, and redemption rights. They should also ensure that stablecoin issuers are subject to ongoing oversight, not just one-time approval.

These are not radical ideas; they are baseline expectations in any system that handles money at scale.

Waiting for stablecoins to become “systemic” before acting would be a mistake. Early, proportionate regulation allows policymakers to shape market development rather than react to crises.

Canada has an opportunity to be deliberate rather than reactive. Other jurisdictions are moving quickly, and regulatory fragmentation will create pressure points regardless of domestic policy choices.

Stablecoins test an old question in a new form: Who gets to issue money-like instruments, and under what conditions? That question has never had a purely market answer. It has always been resolved through public policy, grounded in the recognition that trust in money is a collective asset.

Treating stablecoins as merely another tech trend understates their significance. They sit at the intersection of payments, banking, and monetary policy. Policymakers do not need to rush, but they do need to decide. The cost of clarity now is far lower than the cost of crisis management later.

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