



# Will Bitcoin's Fixed Money Supply Be Its Downfall?

## Inflation Proofing Could Be Too Much of a Good Thing

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Unless you know what terms like “blockchain” and “public ledger” mean, you will find the many aspects of bitcoin hard to fathom. But one thing that’s straightforward is the rule governing the total quantity of bitcoin in existence.

According to that rule, the number of bitcoins in circulation, now just shy of 14.2 million, will grow at an ever-diminishing rate as it approaches its ultimate limit of 21 million coins. By 2030, new coin output will be reduced to a mere trickle. By 2050, it will have practically ceased.

To suggest that bitcoin is doomed for any reason at all, let alone for some specific reason, is to go way out on a flimsy limb. So I hope I’ll be forgiven for saying that the fixed long-run quantity of bitcoin will doom it only in one particular but important respect: namely, by ruling out the possibility of it becoming a more stable exchange medium, let alone a more popular one, than the US dollar.

Don’t get me wrong: I’m not particularly crazy about the dollar. In fact, I think it’s a lousy currency, except when compared to most other government-supplied currencies, which are even worse. (If you want to see a really crazy money supply “protocol,” just have a look at how the supply of dollars has evolved since the Federal Reserve took charge of it in 1914).

Nevertheless, the dollar has at least one tremendous advantage over bitcoin, which is its huge and well-established network of users. The dollar’s big head start means that if any new currency is going to challenge it, it has to be not just a little better, but far better.

In at least one way bitcoins are better than dollars: they can be transferred at practically no cost, and with a degree of anonymity unmatched by any other sort of electronic money. But for a

currency to make big inroads against an established, official money, it has to offer the further advantage of a stable and predictable purchasing power.

Next to its large network of users, the relative stability of the dollar's purchasing power has been the main reason for its popularity abroad, both officially (in "dollarized" economies like Panama and Ecuador) and unofficially. Although dollars tend to depreciate, they do so less rapidly than many other currencies.

With bitcoin's ultimately fixed supply, the long-run risk is the danger, not of depreciation, but of unpredictable and excessively rapid depreciation. As economies grow, so does their real demand for money. Consequently, either the quantity of money units must keep up, or prices must decline to make existing units worth more.

Mild deflation may not be a problem. But if the demand for money grows rapidly, it might not prove possible to reduce prices — and especially wages — rapidly enough to keep up with it without encountering serious resistance. Even under the gold standard the supply of money tended to keep up with demand, especially in the long run, as gold output responded to falling prices (which meant a higher relative price of gold).

A fixed-quantity monetary standard, on the other hand, isn't likely to prove consistent with either short- or long-run price level stability. Indeed, and perhaps paradoxically, the more popular bitcoin becomes, the more likely it is to appreciate rapidly, and the less attractive it will seem as a primary means of exchange, meaning one in which contracts are written and accounts are kept.

To say this isn't, I hasten to add, to suggest that bitcoin can play no important part in our monetary future. First of all, it may long continue to play a part, and perhaps an increasingly important one, as a secondary or "parallel" one, without ever displacing dollars as primary or "standard" money. As a means of making foreign remittances, for example, its superiority is already well established. More importantly, though bitcoin is thus far the most successful cryptocurrency, it is hardly the last word.

The ingenious technology behind it is fully capable of being modified, and of otherwise pointing the way toward alternatives that may prove superior, not only to bitcoin, but to any bureaucratically managed money.

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