What's Driving the Growth of Digital Assets **in Latin America?**

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PREFACE

Opening Statement from Paxos

WALTER HESSERT, HEAD OF STRATEGY AT PAXOS

I have been the Head of Strategy at Paxos for four and a half years. When I think about everything that has happened since 2018 – both in the world in general and within the cryptocurrency space – I am amazed at how fast things are moving. I feel fortunate and privileged to be working at the cutting edge of an evolving global financial system.

At Paxos, I am grateful to be a part of productive collaborations with some of Central and South America's foremost financial brands and platforms, such as Mercado Libre, Nubank, Prex and Impesa. All share our excitement about taking decisive steps to make our financial system more transparent, safer, faster and more accessible.

We have witnessed remarkable growth in the use of stablecoins and cryptocurrency in many regions of Latin America and wanted to take a closer look at what is motivating consumers to adopt digital assets. Some estimate that in 2021, the growth of cryptocurrency in Latin America in 2021 outpaced the rest of the world as a greater ratio of Brazilians – over 40%, tied with Indonesia – own more cryptocurrency than any other country in the world. We spoke with our boots-on-the-ground experts to determine the reasons behind widespread adoption, and to get a feel for how, or if, this trend will continue in the long term. Thanks to our extended family of partners, we were able to talk to several insightful professionals:

- **Bruno Balduccini**, partner at Pinheiro Neto Advogados, Brazil
- **Gloriana Carballo**, fintech consultant at Impesa, Costa Rica
- **Wences Casares**, chief executive officer of Xapo, Argentina
- **Dolores El Jaouhari**, product manager at Prex, Argentina
- **Florence Grassl**, regional product manager at Multimoney, El Salvador
- **Ernesto Leal**, payments and product head at Grupo Gente, Costa Rica
- **Agustin Paez de Robles**, growth marketing manager at Prex, Argentina
- **Michael Coscetta**, chief revenue officer at Paxos, United States

Decades of cumulative knowledge and experience gathered from these thought leaders allowed us to get a much clearer sense of cryptocurrency growth in Latin America. I am now proud to share the findings of this research. Some of the insights confirmed our hypotheses and some were enlightening.

In my role, it's important to temper my enthusiasm with facts and foresight, but there's no denying these are exciting times. With a burgeoning crypto landscape in Latin America growing and succeeding in real-time, we all have a stake in rooting them on.

INTRODUCTION

Cryptocurrency and blockchain technology adoption are ramping up in Latin America, with rapid growth acceleration projected for the remainder of 2022, into 2023 and beyond.

From El Salvador's official recognition of Bitcoin as legal tender to the tremendous growth of digital wallets in tech-savvy Brazil, major moves in 2022 have made it clear that crypto is in Latin America for good. However, the political, economic and cultural forces at work in Latin America are very different from those in the United States, comprising a complex patchwork of monetary, economic and regulatory policies which inform the advance of crypto differently from nation to nation. Yet, the opportunity for crypto and blockchain technology to revolutionize Latin America is undeniable, and the groundwork is quickly being established for mainstream adoption.

In this study, our focus is on the varied array of economic, regulatory, cultural and political factors that are catalyzing the growing adoption of cryptocurrency in Latin America, and on informed speculation of what the near future might hold for the industry. Latin American citizens are already using cryptocurrencies like stablecoins, accessing U.S. dollars to offset local currency depreciation and as a hedge against endemic inflation. The millions of breadwinners working in neighboring countries, as well as the U.S. and Europe, are marveling at the safety, ease, speed and low cost of using cryptocurrency to send money back home to their families. Many Latin Americans are cynical of centralized or government-backed institutions due to their historically high-risk nature, and are discovering that decentralized blockchain banking is a viable alternative to traditional banks.

The ongoing evolution of blockchain technology does not stop at the city limits of metropolitan areas. Citizens from all regions and socioeconomic backgrounds are playing a part in the explosive growth of cryptocurrency in Latin America, either out of necessity or opportunity. The continuing proliferation of hardware devices, like cell phones and gaming consoles – especially in underserved communities – is enabling internet access for previously disconnected or rurally-located populations and increasing their participation in fintech and cryptocurrency markets.

Future regulatory and monetary policy changes will continue to fortify the infrastructure for the expanding cryptocurrency markets in many Latin American countries. Cryptocurrency is poised to stimulate positive change for a legacy banking system that doesn't yet have the operational capacity for 24/7 functionality, and is slowed by expensive legacy systems and regulatory frameworks that restrict its ability to leverage new technologies. This financial system transformation is helping Latin America enterprises because it's creating the conditions needed to build new economies that didn't exist previously, thereby enabling connectivity for millions of people to new economic opportunities.

SECTION 01

Economic forces driving growth

As cryptocurrency and digital asset markets progress through their nascent stage with an assortment of expected growing pains in the U.S. and Europe, we have seen consumer use of digital assets grow enormously over the past two years in Latin American countries. That growth shows no signs of slowing – in fact it's accelerating. From July 2020 to May of 2021, the cryptocurrency value received by Latin America increased from under $10 billion to over $60 billion, with Brazil ranked 5th in the world in on-chain value received. Latin American crypto companies were busy raising more capital, as venture funding grew tenfold during 2021 from $68 million to $650 million. Most notably, the development of cryptocurrency is not confined to stable, prosperous economies such as Brazil's. Surprisingly, cryptocurrency adoption is proliferating in some of the more volatile Latin American economies. For example El Salvador was the first country in the world to adopt Bitcoin as legal tender, a move many experts regarded as a gamble – and it has proven to be a tenuous one at best. But after El Salvador established itself as a standard bearer, other economies wanted to capitalize on the opportunity and began to accept it – if not as legal tender, then as a vehicle for consumption. One might wonder why El Salvador beat the United States to the cryptocurrency frontier? The answer is, at least in part, that in 2022, economies in Latin America are strikingly different from that of the United States. Latin America is not a monolithic economic entity, and instead, represents a collection of divergent currencies, as well as monetary and economic policies.

Cryptocurrency as proxy for the mighty dollar

Currently, cryptocurrency is responding to the unique needs of many Latin Americans beginning with offering greater access to the U.S. dollar. Even though record inflation is adversely affecting U.S. consumers' buying power, the dollar remains the most reliable hedge against Latin America's own inflation challenges. The region is enduring the highest inflation in the world in 2021 and 2022 hovering around 12%, the highest inflation rate in 15 years. In Argentina, currency is so devalued that dollar inflation no longer matters. Latin America local currencies were frequently volatile even before the pandemic shook the world. In most Latin American countries, "an unstable macroeconomic environment has been a critical factor holding back financial system development" (Kohli, Harinder 2008). Decades of chronic inflation, periodic external crises and intermittent deposit freezes have imposed heavy losses on holders of financial assets. People are reevaluating where they keep their money – and how to keep it safe.

Latin Americans favor the U.S. dollar as their preferred currency to preserve stable stored value for long-term purchasing power. As of February 2020, the amount of transactions in dollars from all purchases stood at 64% in Venezuela. In 2013, Argentines held more than $50 billion in USD which amounts to more than 1 out of every 15 dollar-denominated cash assets in the world. In this way, cryptocurrency acts as a proxy for the U.S. dollar, offering some level of liquidity through the use of a cell phone without having to go to a bank, or worse yet – the black market, to get U.S. dollars at a discount. Crypto is proving an attractive alternative to traditional banks' foreign transaction fees and volatile exchange rates.

Stablecoins are naturally an excellent onramp for access to the U.S. dollar, with their liquid, secure 1:1 backing of the dollar. However, we should note that the May 2022 collapse of the Terra stablecoin exposed the important distinction between stablecoins backed by regulated reserves and more speculative algorithmic stablecoins, which use math and incentive mechanisms to maintain a fiat peg. Argentinians from middle or upper economic strata use cryptocurrency – and in large part stablecoins – to get access to the U.S. dollar as a hedge against high inflation.

> "The consumers in Latin America have suffered their currencies depreciation and capital controls for a long time, so they were quick to understand the advantages of crypto and embrace it... This demand is now gradually going to U.S. dollar stablecoins that are much easier to get."

WENCES CASARES, CEO OF XAPO

Mastercard recently reported that half of Latin American consumers have conducted at least one transaction with crypto assets, and over 33% of them have used stablecoins for everyday purchases – and with more access comes more usage. Consider a native Brazilian with relatives abroad during the pandemic. Perhaps they had to change jobs or received COVID-19 assistance, and were in need of banking they could do from home. They may have chosen Nubank, a popular fintech company, by using their mobile phone to deposit checks issued in Brazil's native currency, the real. In doing so, they discover the ability to buy, sell and receive cryptocurrency directly from their Nubank digital wallet.

Paxos Chief Revenue Officer Michael Coscetta observed, "The average user sees the stablecoin opportunity as a more accessible path to obtaining U.S. dollars, and they see cryptocurrencies and specifically Bitcoin as a means of building value and using that enhanced value to give themselves extra economic capabilities to buy and sell across their economies."

Latin America is adopting crypto out of necessity – and ambition

One of our more significant findings was that the drive toward digital currencies in Latin America is coming from consumers instead of institutions, regulators or national leaders. All socioeconomic groups are contributing to cryptocurrency's growth in Latin America -- but for distinctly different reasons and with differing levels of intensity. Perception and adoption can vary from country to country. Wealthier citizens in Uruguay are adopting more aspirationally, for luxury or curiosity, while retail investors, on the other hand, are seeking more flexible opportunities and the middle-class is using cryptocurrencies to diversify investment portfolios. But sophisticated investors are not necessarily the primary driving force of cryptocurrency adoption.

In fact, the more challenges a country's economy faces (e.g.,Venezuela), the larger the trend in cryptocurrency adoption. Lower economic populations are adopting out of necessity and some even assert that cryptocurrency is a potential solution for troubled Latin America economies because it enables competition and reduces transaction costs. Cryptocurrency is potentially a way for disadvantaged citizens to access loans, purchasing power, credit and cheaper remittances. "Crypto will also provide a different financial instrument and options for consumers for their day-to-day financial needs – specifically crypto lending, for instance, rather than a traditional bank personal loan," said Florence Grassl, regional product manager at Multimoney.

When the pandemic resulted in the widespread distribution of billions of dollars in stimulus checks, millions of Latin Americans entered the traditional banking system for the first time, and millions of others flocked to neo banks and fintech companies to deposit and use their funds. Investment in South America-based fintechs grew by 21% in 2020 while the total investments in fintechs fell by 2% worldwide. More fintech companies and digital wallets mean more access to cryptocurrency. The 2021 economic rebound that saw growth approach 7% across Latin America is expected to decrease significantly in 2022 and 2023 to under 3%, slowed by inflation, rising food and energy prices, currency depreciation and large increases in money supply. Despite these drawbacks and a forecasted crypto winter, cryptocurrency is forging ahead strongly, aided by the need for cheaper, faster and more efficient banking infrastructure. Incumbent financial institutions can leverage the current economic environment to reverse the decline they have been experiencing at the hands of fintechs. The rising interest rate environment is a good time for legacy banks to reorient their businesses toward a more customer-first approach, and one big tactic is to increase their interest and use of digital assets.

SECTION 02

Cultural and socioeconomic forces driving crypto markets

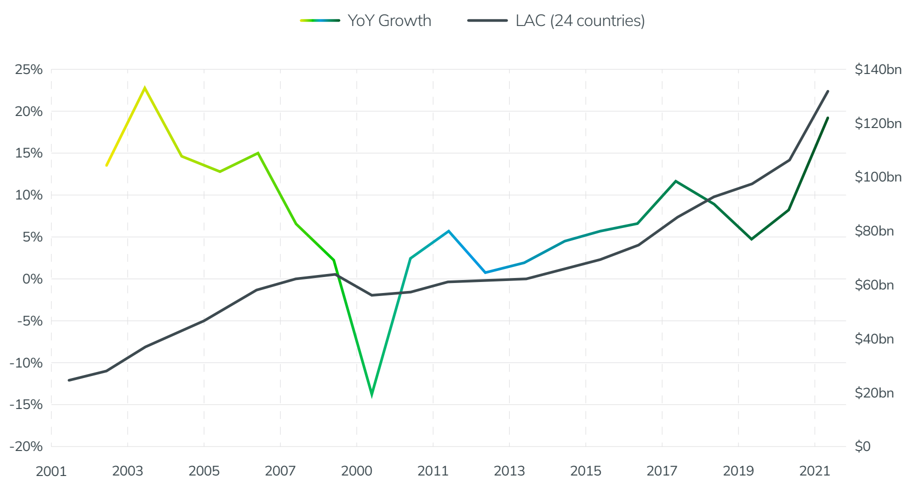
Digital transformation has just begun to impact our current financial systems in every conceivable way. Blockchain technology has the potential to be one of the great egalitarian tools for banking and personal finance if implemented properly. Instead of relying on traditional centralized banking entities, consumers can avoid the costly middleman, and transact on a decentralized peer-to-peer basis using digital currency on the blockchain. Consumers from all socioeconomic strata are moving away from traditional banks to alternative systems with access to cryptocurrency as a result of cultural and economic factors unique to Latin America.

The massive market for sending money across borders

One of the greatest driving forces of growth in digital assets is Latin Americans who work in the United States and Europe and send money home to family, known as remittances. These remittances are a significant part of Latin America's economic engine, with the World Bank estimating that $104 billion was sent to the Caribbean and Latin America in 2020. Remittances also vastly exceed U.S. aid and represent an enormous share of the recipient nations' GDPs; for example, the U.S. has pledged $4 billion over four years to Central

America, which represents only a fraction of the $11.4 billion in remittances received by Guatemalans in 2020 alone. That's equivalent to 15% of Guatemala's GDP. The global pandemic powered a one-year 23% surge in remittances, as over $134 billion was received in Latin America in 2021.

Family Remittances to Latin America and the Caribbean



Source: Inter-American Dialogue, 2021

For the average Latin American working abroad, the act of sending money back home represents an expensive necessity, as services like MoneyGram can charge as much as 5% on both sides of the transaction. Transfers also move very slowly, taking three days to a week. Further, people may not always feel secure transacting at wire service storefronts in person – whether it's discomfort with carrying around significant amounts of cash or limiting in-person interaction during local COVID surges. People are using cryptocurrency such as stablecoins to send money back home in a faster, easier, safer and less expensive manner. Beyond those that work abroad and send money home regularly, cryptocurrency technology is proving a lifeline for vulnerable citizens living in crisis-ravaged nations, helping them move money, or take it with them when emigrating, regardless of whether wire transfer services remain up and running. For example, millions of refugees have fled dire economic and institutional conditions in Venezuela to Colombia; some of the seven million left behind in need of humanitarian assistance rely on crypto remittances for survival. In an example of how legacy financial services are beginning to adapt, MoneyGram has responded to growing consumer demand for crypto, now preparing to launch a service which would leverage a stablecoin pegged to USD to carry out remittances.

The growing number of financially disenfranchised people using cryptocurrency for remittances has the cascading effect of opening up these populations to the advantages of blockchain technology for other banking products. People have clearly demonstrated they want payment mechanisms that are instant and borderless – which will lead to more merchant adoption. Securing remittances is just one compelling reason for crypto growth among the many ways consumer financial services can be utilized as an alternative to traditional banking.

Crypto lowers financial barriers to entry for the unbanked

Another population who may benefit from decentralized banking technologies are the unbanked and under-banked. Latin America has large numbers of people living in rural areas who have never had a bank account, perhaps due historically to the fact that traditional banks have found working with some consumers in Latin America to be unprofitable due to the costs of existing delivery models. Brazil is the sixth largest country by population but has an estimated 34 million people without access to banking services. About half of Latin America and the Caribbean's adult population are unbanked, but with cell phone penetration spurring internet access growth from 43% in 2012 to about 75% in 2021, those without traditional bank access increasingly have found a way into the system. The impact of the COVID-19 pandemic cannot be overemphasized as closures and lockdowns created an urgent demand for digital banking services, which both fintechs and traditional banks successfully addressed, as seen in 2020 when the banked population grew by an estimated 24%. In addition, literacy rates have been steadily climbing in Latin America from 79% in 1974 to over 95% today, and "the rural youth of Latin America are becoming hyper-educated, with literacy rates going over 95% in the majority of these countries," said Coscetta.

> "In Latin America there is a significant distrust of the central economy and the central government... But when you own something and in it's in your app and you can see it every day on a mobile phone, it makes it a little more stabilizing and secured."

MICHAEL COSETTA, CHIEF REVENUE OFFICER AT PAXOS

The number of unbanked people continues to shrink as neo banks, fintechs and blockchains proliferate, and this group is also one of the first to switch to cryptocurrency. Consumers are attracted to cryptocurrency's ease of use, lower fees and access to remittances. In addition, the unbanked and banked alike are becoming more frequently disenchanted with the traditional banks' cycle of numerous fees, onerous paperwork and poor customer experience, spurring a distrust exacerbated by the instability of their financial and government institutions, as well the ubiquity of fraud in the traditional banking world. Due to these and other factors, there will be a whole generation of Latin Americans who have digital wallets and fintech products, but will forgo ever having a traditional bank account. As of May 2021, Brazilian neo-bank Nubank had already brought five million Brazilians into the financial system. "Crypto is a great tool to cut the pain and foster competition – because banks will see they are losing control and must improve," said Pinheiro Neto Advogados Partner Bruno Balduccini, a 25-year veteran of banking and finance in Brazil.

Digital wallets and digital payments are a great force for economic inclusion

Cell phone market penetration is key to cryptocurrency growth because it's the easiest way to access the internet, especially in rural areas. Anyone with a cell phone can get access to the banking system and a cryptocurrency wallet today, which underscores the importance of educating people about cryptocurrency, digital wallets and stablecoins. Digital wallets are an effective way to bring the unbanked into the banking system, and naturally, more digital wallets means more exposure to cryptocurrency. One month after Brazilian fintech Mercado Libre chose Paxos to power its cryptocurrency offering, it had 1,000 people wanting to buy cryptocurrency – with absolutely no marketing. Mercado Libre eclipsed one million users of its cryptocurrency wallet in the first 60 days alone. Nubank sprinted to 1 million users on its crypto trading platform in a single month. Trailblazing American fintech PayPal has made a series of decisive moves to enable customers to buy, sell and hold cryptocurrencies, make payments to merchants and even send cryptocurrency to other wallets. When big names like PayPal expand investments in the cryptocurrency markets, the digital assets gain more and more credibility. Banks must adapt to compete with such fintechs, and are slowly recognizing that they're a permanent part of the financial ecosystem.

Payments is also an area helping to drive cryptocurrency growth and financial inclusion in Latin America; however, the rise of payment fintechs is in some ways undercutting cryptocurrency growth, with merchants remaining slow to accept cryptocurrencies as payment for goods. The central bank of Brazil launched the free payment platform Pix (similar to Zelle in the U.S.) to enable citizens to send and receive money on mobile phones. "The number of unbanked dropped to 5% in Brazil when they introduced Pix in 2020," said Balduccini. Venezuela sought out digital payment methods to alleviate shortages of its bolivar currency. The strategy has yielded some short-term success, with a modicum of price stability and inflation slowing to its lowest point in nearly a decade. As of June 2022, 95% of Latin Americans surveyed by Mastercard said they are planning to use a digital payment method in the coming year, and 51% of Latin American consumers have already made a transaction with crypto assets.

Latin America gamers are a growing segment of under-the-radar crypto users

One of the more interesting trends driving cryptocurrency adoption is the spread of mobile gaming across Latin America. Gamers are no longer a niche audience, and they are poised to become cryptocurrency natives, with Web3 game publishers and blockchain gaming platforms racing to topple barriers to entry for Latin American gamers and developers to help them jump into the metaverse. The growth of cryptocurrency in gaming is also bringing potential users into the financial fold earlier by appealing to a younger demographic – kids and teenagers. "There's a huge unrecognized population in Latin America in gaming: people use crypto to buy upgrades, accessories, they play the 'play to earn' games," said Gloriana Carballo, fintech consultant at Costa Rican payment solution provider Impesa. Play-to-earn gaming, referred to as GameFi, monetizes mobile gaming by combining it with cryptocurrencies and NFTs. Aided by the increase in mobile phone devices, data from a 2021 Newzoo study shows that Latin America is already the fastest growing region for gaming in the world.

> "What we're trying to do as a fintech is break stereotypes that crypto is just related to the dark web. I think it's going to keep growing."

GLORIANA CARBALLO, FINTECH CONSULTANT AT IMPESA

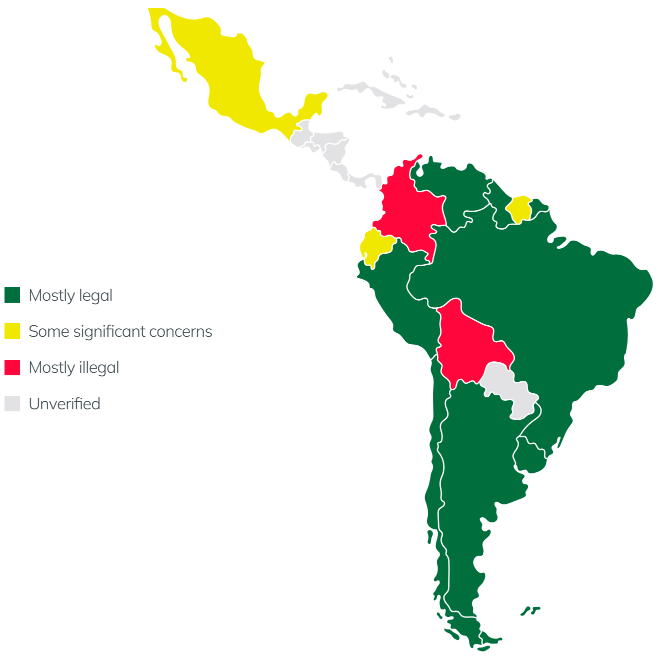
Financial inclusion is slowly improving and will likely accelerate as technological and educational advancements help overcome some of the challenges, creating connectivity for people who didn't have it before. "What we're trying to do as a fintech is break stereotypes that crypto is just related to the dark web. I think it's going to keep growing," said Carballo. Neo banks and fintech companies are leading the way in banking the unbanked. Traditional banks, hampered by traditional regulatory forces, as well as their lack of engineering resources, are generally not capable of, or have little interest in, building technological innovations to elevate the unbanked and under-banked populations. Traditional banks may try to compete in the future, but they will have to be willing to cut their own profit margins to do so.

SECTION 03

Regulatory & political forces are correlated with cryptocurrency growth

Almost daily, there seems to be more calls for regulatory oversight and talk of how to regulate the cryptocurrency sector in the United States, from U.S. Senators Kirsten Gillibrand and Cynthia Lummis' sweeping bipartisan proposal to set cryptocurrency standards, to the Security and Exchange Commission's recently announced crypto initiatives and its increased cryptocurrency unit hiring. The federal government has not settled on whether the tokens are securities, commodities or something else entirely. Meanwhile, in Latin America, regulations are a critical component of adoption trends. With no standard trend across the region, there is a direct relationship between individual nations' regulatory and monetary policies and cryptocurrency adoption.

Cryptocurrency regulations by country within Latin America



Source: Thomson Reuters, 2022

Nobody wants to operate in a regulatory limbo

While regulation can be onerous, and compliance costly and resource-intensive, it is essential to protect consumers and thereby earn their trust. "Many crypto traders want regulations because they protect against money laundering and other illicit activities and enable access to greater capital from bigger institutions," said Balduccini. At the same time, many traditional banks are waiting for a regulatory framework before they fully get on board with offering cryptocurrency capabilities within their platforms – after all, it would be a tremendous waste of resources to implement a new capability, only to have to scrap or redesign it to meet new regulatory requirements.

Many in the cryptocurrency and fintech industries see an opportunity to win the confidence of consumers who have lived with a distrust of institutions almost at the cellular level. Over the past few years, cryptocurrency exchanges and fintechs worked hard to earn trust by meeting consumers' needs and providing reliable services when they needed it most. When an event like the Terra collapse demonstrates instability, it's a one step forward two steps back scenario. As governments and central banks race to build regulatory frameworks to protect consumers, many cryptocurrency businesses and fintech startups are not as eager for regulation. Payments and products head at Grupo Gente Ernesto Leal noted, "The mindset has been, 'Let's just push this through as fast as we can and let's complain about the regulators and let's complain about why the law doesn't permit it. And let's say that it's a ridiculous law,' which it might be!" The fintech app provider Multimoney is the only crypto-regulated financial institution currently available in El Salvador and Costa Rica, used by millions to safely get access to revolving credit, savings accounts and the opportunity to invest in cryptocurrency. While some companies are turning to marketing and advertising to rebuild trust with consumers, other companies who take the proactive steps to collaborate with regulatory agencies and offer transparency in their operations may be doing more to build a trustworthy, open financial system.

Brazil and El Salvador want to lead the way in Latin America

In Brazil, the central bank is writing legislation with the U.S. Senate, large banks, and fintechs to pave the way to introduce crypto in the most regulated, transparent way. Said Coscetta, "They've been doing this in a very open way because the reality is, if they do it in a closed way that's not transparent, crypto would then become counter to its ideal of being fully transparent and decentralized." In Brazil, the current regulations allow for the sending of money abroad using the local currency, the real, which must be exchanged through a regulated counterparty – a gatekeeper instead of a cryptocurrency exchange – to guard against money laundering or other crimes. Because Brazilians have the legal ability to send remittances through the gatekeepers of the central bank, they have no need to turn to cryptocurrency to send money abroad. However, Brazil enacted no regulations against investing in cryptocurrency, so over 34 million tech-savvy Brazilians leapt at the investment opportunity, even eclipsing the U.S. percentage of cryptocurrency investors 16% to 13%.

But other countries have sought to take steps to protect their own fiat currencies by enabling cryptocurrency remittances. Argentina, for example, has prohibited remittances out of the country unless they are first converted to crypto assets and then changed to dollars abroad. Consequently, the cryptocurrency market grew substantially for remittances, but not for investments. In 2021, Argentina recorded the 10th highest rate of cryptocurrency adoption anywhere in the world and the third highest in the Americas behind the U.S. and Venezuela, according to the Chainanalysis index. Venezuela is high on this list because it is using cryptocurrency to fill the gaps in an economy muted by sanctions and hyperinflation.

Appraising the Bitcoin and CBDC options

El Salvador famously declared Bitcoin a legal tender in September 2021, but most countries will not follow its example because their economies are not dollarized. On the heels of Bitcoin's price collapse, El Salvador's Bitcoin gamble has cost the government around $374 million – in a $29 billion economy. The country's economy had already been headed for the brink, and the current crypto winter has exacerbated the issue. "I don't see a lot of countries in Latin America adopting crypto as the legal tender. But you will see crypto being used as a payment method – not as an investment – in countries where the actual payment system is expensive or inefficient," said Balduccini. Although El Salvador's adoption of Bitcoin hasn't solved its problems, it has earned more visibility for cryptocurrency.

One potential obstacle to cryptocurrency adoption could occur if a country doesn't peg the asset to the U.S. dollar in any way, it can have a disjointed effect, as economies may experience accelerated deflation or inflation of the currency. Brazil, Mexico and Venezuela's central banks are making plans to implement Central Bank Digital Currency (CBDC), a digital version of a country's legal tender, as a way for countries to make their currencies fully convertible, cheaper and faster, instead of physically sending cash – something we may see happen in other Latin America countries in just a few years. While a CBDC is not truly cryptocurrency (by definition), a well-designed CBDC could offer "more resilience, more safety, greater availability and lower costs" than unbacked cryptocurrency assets that are inherently volatile. The Pax Dollar (USDP) stablecoin is a privately intermediated digital dollar that is centralized, open, unconstrained, digital and most importantly, truly stable in the face of crypto market fluctuations. A Pax dollar always represents a dollar.

The potential for money laundering and other crimes financed by digital assets

Another important regulatory effort focuses on stifling the spread of criminal activity such as money laundering. As one might expect, the more troubled the country's economy, the more extensive the use of cryptocurrency assets – and the more likely it is that cryptocurrency may be used in crimes like corruption, money laundering and financing of illegal activities. Most central banks are moving to set up strict controls over criminal activity in cryptocurrency because if a country is considered under-effective on anti-money laundering controls, they tend to be punished by the international economy, losing the faith of foreign entities reluctant to invest. The Brazilian Senate passed the first bill to regulate its cryptocurrency market. Now the Bill has to be approved by Congress and then subject to final Presidential sanction. There is an expectation that the bill will become law by the end of 2022 after completion of the Presidential election process.

> "Regulations basically bring more security to the system itself. We will be able to access better quality capital for our financing, for our equity or for growing the business. Therefore, we welcome regulations.' The trend in Latin America is you're going to see the regulation of crypto exchanges."

BRUNO BALDUCCINI, PARTNER AT PINHEIRO NETO AVOGADOS, BRAZIL

Cryptocurrency cannot make the long-term impact that many hope for in struggling Latin America economies until at least some controls, regulations and taxes are implemented. Banks are currently in wait-and-see-mode while waiting for AML protections and to see how they must treat cryptocurrency assets on balance sheets. Banks will enter the picture once there are exchange regulations, and it will all start to evolve as a singular effort with exponential growth. The success of stablecoins is critical because crypto hasn't hit a point of equilibrium yet. "One of the regulatory things we hope we end up seeing is that all digital currency must be registered somewhere. It has to be backed one to one, it can't be levered, it can't be hidden. Stablecoins will provide additional stability inside these economies," says Coscetta. He also believes there is a desire for openness, transparency and a standardized set of parameters for how stablecoins operate to ensure that they function just like dollars. Millions of Latin American consumers are already finding new paths to financial freedom and inclusion through regulated stablecoins and secure, stable cryptocurrency markets that bypass the distrusted centralized middlemen. The advancing regulations can only help to fortify the faith consumers have in these new financial platforms and products as an exciting alternative to traditional banks they have long avoided.

SECTION 04

Conclusion and the Future

Crypto collapse or market correction?

Cryptocurrency has made tremendous strides in gaining adoption and acceptance in Latin America in the past few years and may be poised to enter a new stage of growth as nations begin to establish regulatory frameworks, and most importantly, as citizens gain greater awareness of the new technology. But the recent fall of the Terra stablecoin and the subsequent impact to the broader cryptocurrency market has shaken the industry, leading to several firms failing, while raising an assortment of questions as to the permanent viability of cryptocurrency and stablecoin. For many, the losses demonstrate that there was more leverage built into the system than previously understood. However, for those seeing a more nuanced picture, the crash is more likely a market correction, an opportunity for maturation and a clarion call for regulatory oversight. This is similar to how internet technology's new markets of commerce in the 1990s dot-com boom and Web2 outpaced our protection of personal data and other consumer regulations – likewise, blockchain and cryptocurrency entrepreneurs have sprinted into a unregulated frontier. Exchanges should be cautious and exercise more due diligence when listing certain tokens, and all consumers, exchanges, merchants, investors and central banks need to be aware of the risks. Terra and El Salvador's daring miscalculations are cautionary tales that the financial industry and governments are applying to crypto's next evolutionary step occurring right now.

How cryptocurrency could rescue troubled Latin America economies

The future appears promising for continued growth of Latin America cryptocurrency markets, propelled by expanding awareness of cryptocurrency, the desire to break from traditional banks, the popularity of digital wallets, the continuing advancement of internet access and persistent economic instability. According to the Global System for Mobile Communications Association, the number of mobile internet users in Latin America will increase by 422 million within 2025, and CAGR is forecasted at 4% during this period. As in the rest of the world, when more consumers become educated about the benefits of cryptocurrency and the stereotypes about cryptocurrency and blockchain and otherwise nefarious reputations fade, then digital assets will find legitimacy and reach the mainstream. Given the complex dynamic at play in Latin America, the proliferation of the digital dollars across the region promises to alleviate economic pain points and increase the spending and saving power of millions, thus helping drive innovation and market development. Digital dollars will prove an important mechanism for unlocking Latin American economies. Further, once government regulations catch up and traditional banking institutions see that they must adapt to compete with fintechs, cryptocurrency markets will find a permanent foothold in our financial systems.

Cryptocurrency and fintechs are well-positioned to effect positive change on Latin American economies and people, helping isolated, unbanked consumers merge onto the economic freeway, and thus aid the growth of struggling economies. Everyday people are finally discovering a remedy for the endemic mistrust of financial institutions. Whether it's through investment opportunities, avoiding the hefty fees of traditional remittances, or enabling faster payments transactions, cryptocurrency and blockchain technologies ultimately put more power and assets into the hands of everyday consumers in Latin America – an essential component of growth.

> "I don't think merchant adoption is the number one problem to be solved. Cryptocurrencies solve a very important problem. They make a store of value to defend against inflation, the ability to make an investment in a digital asset or stablecoin that in the future may give a yield, or more sophisticated access to something that banks cannot provide right now. So that's a huge value."

DANIEL RABINOVICH, CHIEF OPERATING OFFICER OF MERCADO LIBRE, from Bitcoin 2022 Conference - Global Bitcoin Adoption fireside chat

In addition to this positive, democratizing effect on underserved consumers, the growth of blockchain products, digital wallets, fintechs, cryptocurrency and other digital assets have the potential to open Latin America economies up to become participating global economies. Many smaller countries could potentially create their own regional economies, not unlike countries in Europe did with the Euro. The creation of this regional economic zone could cultivate more financial freedom and more economic growth.

Worldwide, cryptocurrency is influencing the establishment of a new financial system to replace a legacy banking system which operates on traditional bankers' hours and simply does not have the infrastructure to accommodate consumers from all socioeconomic backgrounds, many of whom are especially in need of instant, borderless, real-time transacting to keep pace with the modern global economy. The blockchain is creating financial connectivity for people who didn't have it before and it is well-positioned to assume its place as the foundation of the global financial system in the Web3 era.

It may be hard to believe, but it has only been 14 years since an anonymous white paper about a futuristic peer-to-peer electronic cash system was published, and just a decade since the launch of Bitcoin. Today, the mainstream is calling, as cryptocurrency markets are becoming inextricably connected with other components of the established financial sector.

Perhaps the greatest single impediment to cryptocurrency achieving its enormous potential in Latin America – not unlike in the U.S. – is skepticism and a lack of easy-to-understand information about how cryptocurrency works – and what the benefits are to end-users. If the industry can demystify digital assets and the associated technologies, then millions of people of all socioeconomic means could expand their opportunities with access to digital assets. And once the regulatory guardrails are in place to prevent ecstatic ups and cavernous downs, cryptocurrency could become the egalitarian force it was intended to be.

About Paxos

By providing blockchain infrastructure for PayPal, Impesa, Interactive Brokers, Mercado Libre, Mastercard, Nubank and more, Paxos is helping them to bring hundreds of millions of people closer to a more inclusive financial system, while also ensuring customer assets are safeguarded by the leading regulated Trust for digital assets globally. Paxos is redefining financial infrastructure. Our blockchain solutions tokenize, custody, trade and settle assets for enterprise clients, enabling the trustworthy and instantaneous movement of any asset at any time. As the economy evolves more rapidly than ever before, we are committed to the innovation that will make its new financial system a reality – and by working within regulatory frameworks, we're creating an ecosystem built with integrity. If you're interested in adding crypto to your platform, reach out to us today.