

# Review of Chinese Policy Against Cryptocurrency Growth

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## Abstract

The development of financial technology arrived at a new form, namely cryptocurrency. The development of cryptocurrency with an increasingly widespread network and its autonomous nature cannot be controlled by the state, which makes China implement policies to block all domestic cryptocurrency activities. The policy becomes unnatural when China occupies the top position in the developing global digital currency market. This anomaly is interesting to study further to find reasons that motivate China to take firm policy when in a safe position as a center of production and global crypto currency transactions. To explain this reason, national interest theory and rational choice are used as the main tools in analyzing this problem. The national interest theory and rational choice explain that the policies taken by China are motivated by economic and security interests, as well as rational calculations of the advantages and disadvantages of those policies.

**Keywords:** Advantages, Autonomy, China, Cryptocurrency, Disadvantages, National Interest, Policy, Rational Choice.



## A. INTRODUCTION

The development of technology in the modern era brought major changes in human life, including the economic and financial systems. The international financial system in 2008 experienced a disruption due to the global crisis felt in almost all countries. New ideas emerged along with the format of the international financial system, namely the birth of the cryptocurrency system which is the use of digital currencies with the concept of cryptography as a security system. Bitcoin as the first form of cryptocurrency that emerged, has evolved amid the existence of conventional financial systems. The emergence of cryptocurrency then increases the pros and cons of state control of the currency in circulation.

This has become a controversial problem because cryptocurrency is basically decentralized, and there are no institutions that can regulate all of its activities including large countries like China. China is one of the countries with the largest population at present, reaching 1.3 billion inhabitants (World Bank, 2019). With a large population, China is one of the pivots of the world's power to balance other countries

such as the United States, Russia, and Japan in the economic, technological and military fields. In the economic field, China is one of the countries with the largest gross domestic product (GDP), ranking second below the US with a value of US \$ 14 trillion. The strength of the Chinese economy is motivated by the rapid development of industry and technology in the domestic field, as well as good management from the Chinese government (International Monetary Fund, 2018).

The economic and technological strength of China, which is one of the biggest powers in the world and able to rival the US, China can easily handle the development of the domestic currency cryptocurrency. Strong and well-established economic and technological advancements can make China a leader in the field of digital currencies. In 2015-2016 China ranked first as the country with the highest cryptocurrency activity in the world, even reaching 70% of the cryptocurrency circulating in the Chinese domain, both from mining, initial coin offering (ICO), and trading (Bitcoin.com, 2018).

In 2017 China took a decisive step by making a policy on banning the use of cryptocurrency in the domestic realm, including mining, ICO, and trade. Peoples Bank of China (PBOC) issued regulations containing higher standards regarding cryptocurrency related to anti-money laundering and banned all banks from serving cryptocurrency disbursement transactions (Zhang, 2018). This step is an unusual policy, if we consider that China itself is a country with the highest cryptocurrency activity, but instead it blocks all activities of its domestic cryptocurrency. Technology resources and cryptocurrency markets owned by China can be put to good use to become the center of world cryptocurrency, where the US and Japan strive to achieve that position by facilitating and legalizing the domestic cryptocurrency market.

With its strength and resources, China actually blocks the activities of the digital currency industry in this country. This is an interesting problem to be studied more deeply, regarding the reasons that influenced China in taking the policy of blocking the activities of the domestic currency.

## **B. RESULT AND DISCUSSION**

China's National Interest in Blocking Domestic Cryptocurrency Activities  
Cryptocurrency in the Chinese perspective has an autonomous nature on its ecosystem, it does not require the intervention of state institutions. it gives rise to dualism in Chinese economic activity, which can be a lucrative opportunity, or it can be a trap and ultimately detrimental to innovation. The economic threat is one of the reasons why China implements the policy. In the field of cryptocurrency, China has implemented policies gradually through PBOC blocking all domestic cryptocurrency activities. Starting to issue rules on the prohibition of cryptocurrency transactions in the domestic sphere, forbidding banks to carry out activities related to cryptocurrency, closing cryptocurrency payment systems, and finally legalizing the use of cryptocurrency as a

payment system (Zhang, 2018).

China is the country with the highest cryptocurrency activity in the world, and is a country that produces 70% of cryptocurrency circulating in the global market (Bambrough, 2018). The strength of China in the field of cryptocurrency is supported by the number of domestic users to reach 90% of the world's cryptocurrency activities (Bitcoin.com, 2018) making domestic cryptocurrency difficult to control. Isolation carried out against cryptocurrency is not a new strategy, seen in the history of China that had done the same thing when implementing a closed economic system and reopened when it was able (Hilman & Rauchs, 2017). A similar strategy was applied to cryptocurrency, China implemented a complete blocking of all activities related to ICO, mining and trading precisely when it became a country with the most crypto currency activities and production.

One of China's responses in blocking cryptocurrency is motivated by the interests of the domestic economy. First is the currency monopoly by the state. Countries such as China, currently have a structured domestic economy, such as having a central bank, ministries and other institutions that strengthen one another. One of the most important institutions for the Chinese economy is the PBOC. The strong development of cryptocurrency in China is considered by the PBOC to be a monopolistic threat to the domestic currency which in this case has a legal currency according to law, and China's interest in regulating its monetary system is carried out through central bank policy with the Renminbi or Chinese Yuan (Hilman) currency & Rauchs, 2017). The risk of cryptocurrency for the Chinese government is when the Yuan is being abandoned and shifted to cryptocurrency like Bitcoin, Litecoin, Ethereum and so on. If the Chinese population prefers to use cryptocurrency rather than Yuan, the value of the Yuan exchange rate against currencies from other countries will drop significantly, so that the stability of the Chinese economy can be threatened.

Security is the second challenge of cryptocurrency against China, because of the nature of cryptocurrency. The large number of individuals who invest in cryptocurrency and the lack of regulation raises many threats, such as data theft and fraud. This threat is a risk with great value for cryptocurrency owners, both individuals and institutions selling service providers. China has a large focus on domestic security from the threat of developing cryptocurrency. The anonymous and unlimited transaction is a real threat to the security of Chinese cyber, because China is a country with the highest number of cryptocurrency users, and is the country with the second most cybercrime cases in the world (Cook, 2017).

Cybercrime is one of the reasons why China blocks cryptocurrency, many cases of data theft, malware, hacking, and cracking can be dangerous for the cryptocurrency ecosystem in China. When the Chinese government provides rules that allow the use of cryptocurrency and levies taxes from its use, the Chinese government has an obligation

to overcome all forms of threats to users, and also ensure the safety of the cryptocurrency ecosystem. China has several major cases related to cryptocurrency, such as the theft of mining equipment which reached 600 units with a value reaching £ 1.5 million from Iceland which was later found to be in China (Khan, 2018). In addition, there is also the largest case of theft of bitcoin in China which reached a loss of up to US \$ 87 million, by cracking several computers that have access to cryptocurrency in large numbers (Yan, 2018). In 2017, China was listed as a country with The highest cybercrime loss was recorded at US \$ 66.3 Billion (Norton By Symantec, 2018). This proves that China is still vulnerable to cybercrime threats to internet users. The big threat makes the Chinese government choose a safe strategy to block all activities related to cryptocurrency in the domestic sphere, because the risks that arise for individual and national security can reach dangerous levels.

In relation to International Relations, cryptocurrency also influences the actions of China involved in trade wars with the US. In recent years, the Chinese economy has remained stable, although in 2017 China has a new focus on economic relations with the US which are hostile in trade wars. The trade war between China and the US is the background of the country's policy. Such as when applying tariffs on imported goods, limiting quotas, to blocking a commodity (Goncalvez, 2018). In the field of cryptocurrency, China has implemented policies gradually through PBOC blocking all domestic cryptocurrency activities. Starting to issue rules on the prohibition of cryptocurrency transactions in the domestic sphere, forbidding banks to carry out activities related to cryptocurrency, closing the cryptocurrency payment system, and finally legalizing the use of cryptocurrency as a payment system (Library of Congress, 2018).

### **Chinese Rationality in Domestic Cryptocurrency Policy**

The Chinese government through the PBOC provides definite rules regarding the banning of all activities related to cryptocurrency and encourages cryptocurrency owners to immediately sell the digital assets. Chinese policy on the issue of cryptocurrency is motivated by a rational calculation of the costs and benefits of each element that influences the development of cryptocurrency in China. First is ICO which dominates the global market, it is considered by the Chinese government as a threat. Chinese cryptocurrency users such as the use of Bitcoin, are one of the factors that influence value fluctuations in the global market, and in some time can be said to be the center of world cryptocurrency transactions. The rising trend of bitcoin prices in China affects the level of value of the domestic currency issued by the PBOC, so that indirectly, when there is a trend of rising global bitcoin prices, the central bank of the PBOC will be affected primarily in the Yuan exchange rate.

Secondly, China is one of the countries with the highest development of digital

and ecommerce industries today, such as Taobao.com, Baidu.Inc's, Jiasule, has begun to accept cryptocurrency as a legal payment tool in all of its transactions. Cryptocurrency entered into the Chinese payment system integration, but was outside the control of the PBOC central bank. This is a detrimental effect on the central bank in maintaining economic stability and Yuan exchange. This is a matter of concern to the PBOC in relation to maintaining the level of the economy as explained in the previous section on China's national interests. Cryptocurrency is considered a threat to the economy and the Yuan, the development of payment technology from several retail companies that support cryptocurrency certainly affects the stability of the economy and Yuan. The correlation between cryptocurrency value and Yuan exchange rate becomes an important consideration. The PBOC keeps the yuan exchange rate strong compared to other currencies, such as the US dollar and Yen, which are widely used as a liquidity currency from cryptocurrency that is developing in the Chinese domestic market.

In addition, China is one of the countries with the largest online gaming community in the world, this has also pushed most to become crypto miners, with a number of players reaching 55.5 million, and there are about 100,000 crypto miners. This is also a concern related to excessive electricity consumption in China, because the mining process is a chain reaction that does not stop for 24 hours or even more, it is certainly burdensome and a concern for the government to regulate wasted energy consumption associated with cryptocurrency even is not a profitable domestic Chinese product. Costs incurred by China to provide cheap energy are used by miners to get maximum results, on the other hand consumption due to the many activities becomes difficult to control.

### **The Impact of the Domestic Cryptocurrency Blocking Policy on China**

China's policy towards domestic cryptocurrency has various impacts, both direct and indirect. From an economic standpoint, blocking by China has both positive and negative sides. The positive side of the policy is that China can prepare itself to have strong control over cryptocurrency, it is known that China is currently developing domestic cryptocurrency products (Ehrlich, 2018). The strategy certainly has a positive impact when China enters the industry and the financial economic system by utilizing cryptocurrency technology, compared to the present which would have a fatal impact if forced. With a large number of consumers, cryptocurrency developed by PBOC has good potential, seen from the high interest of domestic consumers in cryptocurrency products. Moreover, China has many retail websites that can adopt the cryptocurrency payment system, so that it will expand PBOC crypto currency products.

In the field of security, China also benefits more, as explained in the previous section that cybercrime is a major threat to the cryptocurrency industry in China. By temporarily blocking domestic cryptocurrency activities, and at the same time China is

building a new system that is more efficient and secure for certain individuals and entities when transacting or storing cryptocurrency. If China takes another step to legalize cryptocurrency when it is not ready in the security field, it will jeopardize China's security, especially with the world's largest number of cryptocurrency production and transactions (Mourdoukoutas, 2017). Calculations in the field of security will be an important consideration, because the obligation to maintain security will incur a large cost in accordance with the amount of cryptocurrency activity in China. The economy which is also the main objective in blocking cryptocurrency has both positive and negative sides. The positive side of the policy is that China can focus on maintaining economic growth, and securing the value of the Yuan currency in conditions of economic conflict with the US. If China prefers to legalize cryptocurrency, it is feared that it will affect economic stability, especially the Yuan exchange rate because many cryptocurrency users in China make purchases using the dollar.

Even so, China suffered losses when it did not legalize cryptocurrency for the time being, that is, it could not receive taxes from all cryptocurrency activities which were worth up to 90% of global activity (Bitcoin.org, 2018). Furthermore, China will lose the confidence of speculator and cryptocurrency investors because of its closed nature, unlike the US or Japan which chose to open themselves to attract global markets that are centered in China. The blocking policy also affects China's cryptocurrency ecosystem, especially in mining and ICO. Cryptocurrency miners who carry out their activities in China are very large in number, due to the cost of production, namely computer equipment and electrical energy, which is cheaper than other countries. With this regulation, many miners in China have closed down their businesses due to licenses that were not obtained or accusations of illegal activities by the authorities (Hsu, 2018).

China has positive and negative impacts from the cryptocurrency blocking policy in terms of the economy, security, and cryptocurrency ecosystem that has been formed in China since its inception. However, this is part of the cost and benefit that China has calculated before taking the policy to block cryptocurrency activities.

### C. CONCLUSION

The policy taken by China is a form of rational calculation of the costs and benefits to be received. The policy of blocking all domestic cryptocurrency market activities that has been built against the background of the interests of maintaining economic stability, securing the value of the Yuan, stemming the possibility of receiving high losses due to cybercrime, image and prestige as a country capable of having its own cryptocurrency, to preparing itself in entering the cryptocurrency industry against other major countries such as the US and Japan which currently have created a cryptocurrency platform. The positive and negative impacts that China receives from adopting these policies are more beneficial, compared to if China chooses to regulate

such as the US and Japan. Readiness that is not yet fully owned by China makes it play in a safe zone by blocking foreign cryptocurrency activities in the domestic market, and preparing to bring up domestic products to counter existing global cryptocurrency markets.

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