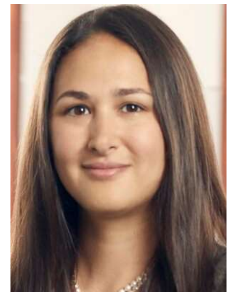
Understanding China's Crypto-Blockchain Dichotomy

By **Sasha Rosenthal-Larrea, Daniel Barabander and Leslie Liu** (September 6, 2023)



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Recent U.S. Securities and Exchange Commission enforcement actions have once again propelled blockchain and cryptocurrency to the forefront of public consciousness.[1]

While the two concepts are often conflated, they represent very distinct and different technologies. Although cryptocurrency is built on top of blockchain technology, blockchain fundamentally encompasses an innovative way to store data and has use cases far beyond cryptocurrency.

Even as China restricts cryptocurrency use, its actions frequently support blockchain as a complementary technology to real economy sectors. This article assesses China's relationship with blockchain technology and why the blockchain-cryptocurrency distinction is core to that relationship.

Diverging Attitudes Toward Technology

There is a popular narrative that China is hostile toward cryptocurrency.

There is some truth to this view. China has restricted cryptocurrency use since 2013 and, in 2021, China banned financial institutions from holding cryptocurrency or engaging in financial activities related to cryptocurrency, and foreign cryptocurrency exchanges from providing service to citizens living in China.[2]

This hostility makes sense because cryptocurrencies such as bitcoin inherently impede control by the government, and the Chinese government, known for its desire to be in control, therefore sees cryptocurrencies as a threat.

Yet, we frequently see the "crypto ban" narrative[3] conflated with China being antagonistic toward the full spectrum of technology undergirding cryptocurrency, including blockchain.

This is an oversimplification. The Chinese government has taken a series of initiatives that demonstrate an ambition to create a nationwide blockchain framework that focuses on the technology as an infrastructural tool to support the real economy.

For example, on May 10, Beijing established a National Blockchain Innovation Center. The center aims to increase interoperability across blockchain in the country to increase competitive and innovative capabilities.[4]

And on June 1, the Ministry of Industry and Information Technology published national guidelines for blockchain participants that will take effect in December, intending to standardize the industry.[5] Ensuring standardization and interoperability is a core feature of many of China's infrastructural projects.[6]

Infrastructure is meant to be built upon. And through public-private partnerships, China is investing in blockchains specifically designed to support the real economy.

Two nationwide, government-sponsored blockchain networks, Blockchain-based Service Network and ChainMaker, are laser-focused on real economy use cases, allowing small and medium businesses to build their own applications on top of these blockchain networks at low cost.[7]

Among Blockchain-based Service Network's business uses, Fujifilm has developed an application for on-chain business contracts and efficient payment transactions.[8]

And the State Grid Corp. of China is using ChainMaker to record carbon lifecycle data, while health care businesses are creating trusted data links through a blockchain built atop ChainMaker.[9] These blockchain environments explicitly do not permit or use cryptocurrencies or tokens to power the network.

China's embrace of blockchain in these fields makes sense and stands in direct contrast to its actions regarding cryptocurrency.

This is because, while cryptocurrency is sometimes associated with decentralization and evading government control, blockchain itself is neutral in this regard — that is, blockchain is simply a useful technology to store data that can be adapted to various scenarios, such as businesses in the real economy.

Hesitancy in National Guidance

On Feb. 27, in tandem with the 20th People's Congress, China's Central Committee and State Council — the country's highest lawmaking authority — published a summary of the plan for the Overall Layout of Building a Digital China[10].

Given the government's support for blockchain technology as an infrastructural tool, it would be natural to expect the plan to discuss blockchain technology as part of its vision for the future. Yet this did not occur. Although the plan details other specific areas of technological development — including 5G, IPv6 and the BeiDou Navigation Satellite System — it omits references to blockchain entirely. This was puzzling.

However, a close read of the plan shows how the national government continues to view technology through a real economy and infrastructural lens, which is consistent with China's stance toward blockchain technology as well.

Language linking digital technology and the real economy appears twice in the document, urging local governments to "promote a deep fusion between the digital economy and the real economy."

The plan highlights key traditional, real economy sectors that would benefit from digital transformation, such as agriculture, manufacturing, finance, education, health care, transportation and energy.

Not only does "digital infrastructure" appear four times in the document, but also the verb choice preceding the phrase — "hang shi" — is also telling. "Hang shi," which is construction industry jargon that translates roughly into "solidification," appears twice when describing "digital infrastructure."

In the Chinese language, this verb is generally used in connection with laying a physical foundation, such as when describing solidification of soil or compaction of concrete. The national government has historically made painstaking efforts to choose its words precisely in similar documents, suggesting that the tie between the two seemingly disparate concepts is no accident.

If the plan is consistent with China's focus on digital infrastructure, why didn't it mention blockchain? We believe this is a byproduct of China's uncomfortable relationship with cryptocurrency.

The fact is that blockchain technology and cryptocurrency continue to be widely conflated. While China clearly understands the benefits of blockchain technology as an infrastructural building block, it may still harbor some hesitancy in defining blockchain as part of its national strategy given its association with cryptocurrency.

While we expect China to continue its support for blockchain technology, until it is disaggregated in the public's conception from cryptocurrency, we may see the government engage in an ongoing balancing act in its public statements regarding the technology.

What is clear is that the narrative of "China hates crypto-related technology" is inaccurate — to the contrary, China's approach is quite nuanced and complicated.

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