



ANALYSIS OF BITCOIN LEGALIZATION AS AN OFFICIAL TRANSACTION TOOL IN EL SALVADOR

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ABSTRACT

This research begins with the phenomenon of the emergence of Cryptocurrency, one of which is Bitcoin, which is used as currency in El Salvador. In this regard, the research aims to question El Salvador's reasons for legalizing Bitcoin as an official means of transaction. This paper answers questions through qualitative methods using secondary data. The data were then analyzed using a qualitative descriptive analysis. The results of this study indicate that El Salvador's reason for legalizing Bitcoin is to reduce dependence on the United States dollar, attract investors from abroad, and improve the El Salvador economy.

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INTRODUCTION

In the era of globalization, technological advances continue to experience developments in all fields, including the economy. In the economic sphere, innovations have also appeared in decentralized digital transaction facilities, namely *cryptocurrency*, one type of which is Bitcoin. Bitcoin was first created by Satoshi Nakamoto in 2009 (Daufina, N., 2014). The principle of Bitcoin is that it is digital, *peer-to-peer*, third is global, fourth is anonymity but all transactions can be seen on the Blockchain, and decentralized.

Bitcoin also has advantages and disadvantages. The advantages of Bitcoin are like using Bitcoin so that all users can make transactions anywhere and anytime, operational time is 1x24 hours, has no country boundaries. Then Bitcoin is able to be more resistant to monetary inflation and more transparent, and so on. Bitcoin also has a weakness, namely that behind its anonymity it also carries the risk of money laundering. Then Bitcoin is also prone to high volatility or can experience fluctuations in a very short time. Then Bitcoin is also difficult to predict and not all countries want to accept the existence of Bitcoin.

Along with the development of globalization, one of which gave rise to Bitcoin so that in September 2021 El Salvador became the first country to legalize Bitcoin as an official means of transaction in its country besides the United States dollar. In this case the institution that did the conversion was *the Development Bank of El Salvador* (BANDESAL). Therefore with the official Bitcoin being everything that was previously implemented in USD can now also be using Bitcoin.



From an economic point of view, El Salvador according to data from *the International Monetary Fund* in 2020 has a GDP of \$24.56 *billions of US dollars* (*International Monetary Fund*, 2020). Then in the following year, namely 2021, El Salvador recorded an increase in GDP, so that GDP in 2021 was recorded at \$ 28.74 *billions of US dollars* (*International Monetary Fund*, 2021). In addition, according to World Bank data, El Salvador's GDP in 2020 ranks 105th out of 206 countries recorded. From this data it can be concluded that El Salvador is in a position as a middle and developing country. From the *Personal Remittances Received (% of GDP)* indicator, according to *the World Bank*, in 2020 it will reach 24.1% of El Salvador's economy (*The World Bank*, 2020). El Salvador has a dependence on receiving money from people who are abroad.

In the realm of international trade transaction activities in general it involves actors and depends extensively on transactions that tend to use physical media and some of the long processes that go through. Therefore, the length of the procedure is often associated with high costs and the number of parties involved. Then, from this gap, many industries, especially in the field of information technology, are starting to explore the potential of *Blockchain technology* for these trade transactions. El Salvador is also a member of *Latin America and the Caribbean* or LAC which also uses Blockchain's potential for trading in the region so that it can restore the economy.

In El Salvador's level of use of information technology and the internet based on data from *Internet World Stats* in 2019 El Salvador recorded an internet penetration population in the country of 57.4% or around 3,700,000 (*Internet World Stats*, 2019). Then based on *the Speedtest Global Index* for 2022 El Salvador's internet speed with the *mobile speed indicator* is in 88th place out of 140 countries and the *fixed broadband speed indicator* is in 112th place out of 182 (*Speedtest Global Index*, 2022). Compared to the global average *performance*, El Salvador is still far below it. If implementing a transaction system with Bitcoin, it is also balanced with the capacity of technology and internet that supports it, but what happened in El Salvador was recorded as still being in a position below the *global performance average*.

Under the leadership of President Nayib Bukele, El Salvador in 2021 legalizes Bitcoin as an official means of transaction side by side with the United States dollar. According to the data previously described, it is common for developing countries to have a conservative tendency, especially towards existing changes. However, the phenomenon that occurred was that El Salvador, one of the developing countries, became the first country to legalize Bitcoin as an official means of transaction. Therefore, the authors are interested in conducting this research entitled: *Analysis of Bitcoin Legalization as an Official Transaction Tool in El Salvador*. The purpose of this study is to find out why El Salvador made a policy of legalizing Bitcoin as an official means of transaction.

RESEARCH METHODS

The research method is a method or process that is implemented in scientific work that aims to describe and analyze a phenomenon or problem that has been determined. In this study using qualitative methods. The author's research approach also describes related phenomena and issues that take place in the international economy, one of which is Bitcoin and El Salvador as a domestic sphere.

In conducting this research the authors used data collection methods sourced from literature study. This method includes secondary data types obtained through the media of books, newspapers, online reading sources, the internet, *e-books* and other reading data sources related to international economic issues including Bitcoin in El Salvador.



RESULTS AND DISCUSSION

Theoretical framework

Intermestic Approach Theory

The existence of globalization has created changes globally caused by developments in technology, industry, scientific developments, and so on. This also brings the study of the study of International Relations is also increasingly widespread. Studies that were previously not the realm of IR studies, are now even becoming studies within the study of IR studies. Then this came the intermestic theory which was first used by Henry Kissinger in the 1970s which is nothing but an abbreviation of international and domestic. Intermestic can be said as a new approach in the study of International Relations. Intermestic theory has links between issues and international and domestic policies, the link between the two can be in the form of influence, impact, or response (Kusumaningrum, 2015). This theory also describes policies, issues, to ideas/norms that take place at the domestic level but in its development can also be at the global level.

Intermestik examines how the response to the influence of an international system on the domestic sphere. This is classified into three domains in the main analysis, namely *issues*, *policies*, and *values*. As previously explained, the intermestic approach to interrelationships, especially in the discussion of interactions and activities, can be explained by the first influence, *namely* changing conditions or behavior. The second impact (*effect*) is how this brings benefits or vice versa. The third is the response, *namely* how the actors respond to policy adoption, the pros and cons of issues, to create social movements (Kusumaningrum, 2015).

In the topic of research conducted by the author, the author examines the reasons for the legalization of Bitcoin that occurred in El Salvador. El Salvador under the leadership of president Nayib Bukele adopted Bitcoin and legalized it as an official transaction tool in El Salvador. In the study of intermestic theory, here the author takes the realm *of policy* or policies from the three domains of intermestic theory that have been previously described. Furthermore, this has links between international and domestic issues, where Bitcoin is currently an international issue and El Salvador as a domestic domain legalizes Bitcoin as an official means of transaction. This brought influence, impact, and a response from the domestic sphere itself, which was none other than El Salvador.

International Political Economy Concept

The second concept used by the author is the concept of international political economy. Political economy is an applicable-empirical study that discusses the relationships and interactions that are taking place or influencing each other between market mechanisms and government policy factors to social change (Salim, A, 2023).

The concept of international political economy has several issues discussed starting from the international trading system, the international monetary system, multinational companies, to studying state development (Apridar, 2009 as quoted in Suharto, AT, 2018). In its development, the international political economy is also supported by globalization. In addition, the latest technological developments also have an impact on the development of the international economy. In this case, the author uses the concept of international political economy to understand the Bitcoin phenomenon in implementing policies in a country.

Results and Discussion

1. Reducing Dependence on the United States Dollar

One of the reasons behind El Salvador's reason to legalize Bitcoin is to reduce dependence on the United States dollar. The influence of intervention by the United States has indeed been going on for a long time in El Salvador, as there was an attempt by the United States to fortify El Salvador from the influx of communism by



providing military and economic assistance, especially to anti-socialist groups in El Salvador. Until El Salvador dollarized when it had strong fundamentals economically (Swiston, A. 2021, p.177). Then this argument is also based on the entry of trade, foreign investment, to economic growth (Swiston, 2012 as cited in Hinds 1992, 2002).

President Nayib Bukele made a statement in the general assembly forum of the *House of Representatives* in May 2022 that it is time for the international world to jointly stop dependence on one currency in various ways (CNBC, 2022). Furthermore, when President Nayib Bukele first announced the Bitcoin policy in June 2021, he stated that by legalizing Bitcoin, this would be able to digitize the El Salvador economy, reduce dependence on the use of the United States dollar, thereby reducing the cost of remittances and encouraging investment (Brigida, A & Schwartz, L., 2022).

In general, a country maximizes state revenues and minimizes expenses, which later will also affect policy makers based on existing considerations. El Salvador legalized Bitcoin as the existence of the cryptocurrency system phenomenon which later became a motivation for El Salvador not to depend too much on the existence of the United States dollar and to maximize state revenues by one of them maximizing the application of Bitcoin. According to Otto Mora (2021) this is a dual strategy for El Salvador to solve the problem of dependence on the United States and minimize shipping costs or remittance costs.

The Bitcoin legalization policy carried out under the administration of President Nayib Bukele hopes that this will be able to solve the economic problem where more than 20% of El Salvador's GDP is dominated by *personal remittances*, but they also have to pay high remittance fees and it is recorded that 70% of Salvadorans do not have accounts at bank. By implementing Bitcoin, it will make it easier for El Salvador to carry out cross-border transactions with efficient time, low fees, and don't even require the role of a third party.

After El Salvador legalized Bitcoin in 2021, remittance fees decreased. The cost of remittances issued by El Salvador in 2019 to 2020 reached 6 billion United States dollars. Then in 2021 and 2022 where in 2021 El Salvador legalized Bitcoin, remittance fees were recorded to decrease by 2 to 3 billion United States dollars in 2022 (Brunazzi, E., 2022 as quoted in Nurfakriyah, NH, 2022). By reducing the cost of remittances, El Salvador can reduce the level of dependence on remittances using US dollars.

2. Attracting Foreign Investors

Before El Salvador officially legalized Bitcoin, President Nayib Bukele had announced plans to build *Bitcoin City*. The government of El Salvador under President Nayib Bukele has budgeted up to \$375 million for the launch of Bitcoin, this includes \$150 million in conversions, then about \$120 million for a \$30 Bitcoin bonus program for El Salvadorans who download Chivo Wallet. Then about \$104 million that has been publicly announced by the government for Bitcoin spending (CNBC, 2022). In addition, other efforts were also made by the government of El Salvador in order to attract investors from abroad, one of which was to provide incentives for investors to invest early. The Bitcoin City program is partly funded from Bitcoin volcano bonds of up to \$1 billion (Jha, P., 2022).

Furthermore, President Nayib Bukele also invited Samson Mow, who at that time served as *chief strategy officer of a cryptocurrency company* called Blockstream. Mow said that while Bitcoin City is being funded by Bitcoin volcano bonds, half of the funds raised will be used to set up energy and mining infrastructure, and the other half to buy Bitcoin. According to Mow, if Bitcoin continues to increase then El Salvador will also benefit and repay bondholders with interest (Brigida, A & Schwartz, L., 2022).

Regarding one of the reasons behind El Salvador to legalize Bitcoin is attracting foreign investment which in the end is one of the *national interests* for El Salvador. The existence of Blockchain technology contained in Bitcoin is utilized by El Salvador to increase the number of investors because using this technology brings more practical financial services. President Nayib Bukele stated that legalizing Bitcoin is a promising prospect with the



calculations and capabilities of investors (Kshetri, N, 2022). Using blockchain technology makes it possible for El Salvador to be able to increase the number of investors because payments via Bitcoin have easier financial services (Kshetri, N, 2022). President Nayib Bukele also said that investors in El Salvador would not be subject to *income tax, capital gains tax, property tax, payroll tax and municipal tax* (Brigida, A & Schwartz, L., 2022).

3. Improve El Salvador's Economy

El Salvador is one of the countries that is dependent on remittances made by its citizens who are abroad, in fact this contributes to El Salvador's GDP by more than 20% according to World Bank data *in* 2019. When sending money conventionally, such as via *Western Union* intermediaries or other intermediaries in money transfers have several regulations and also transaction fees that are not low. This certainly complicates El Salvador when compared to the crypto system where the crypto system can be used by anyone to anywhere. David Coker, a financial and *fintech academic* from *the University of Westminster*, considers that El Salvador has followed the progress of economic innovation to the acceptance of Bitcoin as an official means of transaction (Coker, D., 2021).

The legalization of Bitcoin in El Salvador has to do with sending funds, namely the reduction in the cost of remittances issued. Remittance fees are charged by the sender and local currency conversion fees to recipients in other countries. Remittance agents, especially banks, obtain an indirect fee in the form of interest or *float* before the funds are sent to the recipient. This is what then makes interest rates high. By using Bitcoin, users can directly send funds to recipients. With the enactment of Bitcoin, one of El Salvador's interests in an effort to maximize its economy, one of which is by minimizing expenses. By adopting Bitcoin, it is hoped that this can reduce the cost of remittances issued by up to US\$ 400 million (Baskoro, FM, 2021)

CONCLUSION

Technological advances and innovations as a result of globalization. The innovations that are present are also included in the economic field, one of which is the emergence of *Cryptocurrency* which is decentralized, volatile, and *peer-to-peer*. El Salvador under the leadership of President Nayib Bukele became the first country to issue a policy of legalizing Bitcoin as a means of official transaction alongside the United States dollar which had been in force previously. This is of course motivated by several reasons that made El Salvador legalize Bitcoin. The first is to reduce El Salvador's dependence on the United States dollar, which has been in effect since 2001. With dollarization, El Salvador is ultimately unable to carry out its own monetary policy. The second is in order to attract foreign investment. El Salvador, which has a more objective goal of attracting more investors to its *Bitcoin City*, one of which is by providing special incentives for investors. Later this program has been partially funded by Bitcoin *volcano bonds* up to \$1 billion. It can be concluded that El Salvador has an interest in raising more funds from investors to support El Salvador's economy. The third is improving El Salvador's economy, where it is known that more than 20% of the country's GDP comes from *personal remittances*. By legalizing Bitcoin, this is able to reduce expenses caused by remittance fees so that it can optimize the inflow of funds to El Salvador.

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