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CONTACTS

Tedrick A. Housh III,
CIPP/US
Kansas City
T: 816.460.5642
[Email](#)

Dale A. Werts
Kansas City
T: 816.460.5828
[Email](#)

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Bitcoin Lessons from Venezuela, Where Hyperinflation Reigns

Most U.S. businesses have been introduced to the concept of blockchain and Bitcoin by now. Even with scalability and other concerns, investment grows in these technologies. In Venezuela, we have a real-world business laboratory for Bitcoin in the face of a hostile government.

Why is Bitcoin Use Surging in Venezuela?

Not long ago, Venezuela was the richest country in Latin America, supported by the world's largest supply of crude oil. Its economy is now in freefall and its money is broken. For at least some Venezuelans, Bitcoin represents a potential financial lifeline, not merely a speculative investment.

Venezuela's currency, ironically called the "bolivar fuerte" ("strong bolivar"), has lost 99.99 percent of its value since 2011.¹ At black market rates, one dollar bought 3,164 bolivars in January 2017.² Just a year later, in January, 2018, a dollar bought about 191,000 bolivars.³ On June 8, 2018, one dollar bought 2.1 million bolivars.⁴ Some economists predict the exchange rate to rise to 58 million bolivars per dollar by year end.⁵

Not surprisingly, prices are skyrocketing. In 2011, Venezuela's annual inflation rate of 27 percent was one of the worst in the world. As of a couple of weeks ago, according to Professor Steve Hanke of Johns Hopkins University, Venezuela's annual inflation rate was an astonishing 36,569 percent.⁶ In contrast to the prior 57 instances of hyperinflation since the French Revolution,⁷ there is now an alternative digital currency available: Bitcoin (BTC).

How Do Venezuelans Purchase Bitcoin?

Bitcoin itself is volatile; it is now valued at about \$6,000 per BTC, down from near \$20,000 in 2017.⁸ Still, it holds its value better than the bolivar, which has been battered by Venezuela's economic policies of the last decade or so.⁹ Dollars are scarce and can attract the attention of both the government and criminals. The Venezuelan government shut down two cryptocurrency exchanges in April, freezing over a thousand bank accounts in the process.¹⁰ One Reddit contributor

explained:

[B]itcoin allows us to have complete control over our funds, to hide them so bad people don't know they even exist in our possessions, plus we can really easily purchase them or sell them at a 3 percent exchange fee at localBitcoins, and doing so safely by choosing a seller/buyer who has 100 percent positive feedback, 1000+ transactions and at least 250BTC volume history on his account.¹¹

"LocalBitcoins," referenced above, is the world's most popular blockchain platform for peer-to-peer Bitcoin exchanges. Since May, Venezuelans have doubled their LocalBitcoins trading volume, setting a new platform record nearly every week.¹² LocalBitcoins recently began requiring Know Your Customer (KYC) details from frequent customers, which may slow its momentum.

Another cryptocurrency exchange founded by Venezuelans, Cryptobuyer, set up cryptocurrency ATMs at banks in Panama, so Venezuelan ex-pats could, among other things, transfer cryptocurrencies to their relatives. The brokerage claims over 10,000 registered users, a black-market exchange rate and lower commission fees than banks. Citing scalability issues, however, Cryptobuyer claimed to drop Bitcoin for a time in favor of Dash and Litecoin. It now appears to offer all three. Its demonstration of an ATM crypto-transaction is currently available on YouTube.¹³

Uses for Bitcoin in Venezuela

As Currency. On rare occasions, a Venezuelan merchant might accept direct payments of Bitcoin for its goods or services. In the entire country, however, only about 180 businesses currently do so.¹⁴

As Bank Account. A Venezuelan will typically hold his or her Bitcoins in an account, find a low-volume trader who will exchange bolivars for Bitcoin, then try to spend those bolivars quickly before they lose too much value.¹⁵ Transactions are difficult. Point-of-sale terminals often do not work, bolivars are physically scarce, and prices can change by the hour or day.

To expedite payment, merchants sometimes give customers their banking account information, but a regular bank transfer of bolivars can take four days or more.¹⁶ If the customer uses the same bank, however, he or she can instantly e-transfer bolivars to the merchant's account by mobile phone. If the customer uses a different bank, the customer can seek out a low-volume trader with the same bank as the merchant, and the trader can serve as middleman.¹⁷

For Mining Income. Mining involves the use of computers to solve complex algorithms and create blocks for the blockchain, for which the miner receives a cryptocurrency reward. Mining takes large amounts of energy, but electricity is cheap in Venezuela. A successful miner can earn up to \$500 in crypto per machine per month, a princely sum.¹⁸ Payment is in cryptocurrency, not bolivars. The downside is that the government watches for unusually high electric usage, then takes the computers and/or arrests or extorts the miners.

Other Alternatives to Bolivars

The Petro. The Venezuelan government recently created its own cryptocurrency, the “Petro,” purportedly backed by the country’s oil reserves. Numerous cryptocurrency observers have labeled the Petro a sham for lack of transparency and in part because of blockchain and Bitcoin’s anti-government, libertarian origins.¹⁹

Gift Cards. Venezuelan residents can use their Bitcoins, for example, to acquire gift cards they can use in online marketplaces such as Amazon, although there have apparently been issues with credit limits and exchange rates.

Internet Goods. If a Venezuelan wanted to purchase gold jewelry or other goods online to avoid devaluation of the bolivar, PayPal typically would charge a 30 percent fee to exchange currencies, which most view as an unacceptable double tax.²⁰ Goods have less liquidity than currency in any form, and remain subject to depreciation or theft.

Virtual Dollars. AirTM currently provides virtual dollar accounts (cryptocurrency tied to the value of the dollar – like Ripple) to around 200,000 Venezuelans.²¹ Likewise, Abra uses smart contracts on a blockchain platform so that an individual keeps Bitcoin in hand at all times, but can “virtually” trade for fiat currencies and other cryptocurrencies, always getting paid in Bitcoin (or Litecoin) on any positive spread.²²

In summary, necessity is the mother of invention, or in this case, adaptation. One hopes that the suffering of the Venezuelan people eases soon. In struggling for their future, they are showing the rest of the world how Bitcoin and blockchain platforms may perform under pressure in daily life.

Let the members of the Blockchain and Disruptive Technologies practice group at Lathrop Gage, led by Tedrick Housh and Dale Werts, answer your questions regarding the legal aspects of new technologies, like Blockchain and Bitcoin.

Endnotes:

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