Major crypto lender files for bankruptcy

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The filing for bankruptcy by the major crypto currency lender Celsius Network in New York on Wednesday has been characterised as crypto's "Lehman Brothers moment."

The demise of the US investment bank in September 2008 was the trigger for the global financial crisis which required massive intervention by the US government and the Federal Reserve, as well as international action, to prevent a complete meltdown.

The company had liabilities of $5.5 billion, most of them to Celsius users, and assets of $4.3 billion.

While the crisis in the crypto market is not on the scale of the 2008 breakdown, neither is it an isolated event without broader financial significance.

This is because, while the crypto market has been rightly regarded as a kind of Ponzi scheme, the collapse of Celsius and other crypto firms is the result of the tightening monetary policies of the Fed affecting all areas of the financial system.

In order to lure depositors, Celsius offered large rates of return on their money which it then lent to other crypto firms, using the rhetoric of the entire crypto world to present itself as a kind of rebellion against the banking system.

Back in 2020, as the crypto boom was taking off, Celsius CEO Alex Mashinsky issued video addresses in which he railed against the rigged financial system and greedy bankers, claiming to offer an alternative.

In a major article this week, the *Financial Times* (FT) recalled remarks he made during an interview last year. "There is a continuing squeeze of the 99 percent by the 1 percent to extract more profit," he said. In a 2020 interview he claimed that Celsius was "actually safer than most banks."

The bankruptcy filing told a very different story.

A press release by the Celsius board of directors said the bankruptcy followed the difficult but necessary decision last month to halt withdrawals, swaps and transfers to stabilise its business and to protect its customers.

Had it not done so then there would have been a run on deposits and customers who got in first would have been paid in full leaving others with illiquid and uncertain claims. In other words, Celsius would have been subject to what amounted to a bank run.

The advocates of crypto have claimed it is a new system not dependent on central banks. But the history of this market shows that it has been highly dependent on the outflow of trillions of dollars into the financial system by the Fed and other central banks. The provision of ultra-cheap money was the fuel which drove the crypto boom in 2020 and 2021, such that the market value of crypto assets reached $3 trillion in November last year.

Since then, monetary policy tightening by the Fed in response to rising inflation has seen the market value of crypto fall by around two thirds, with the value of bitcoin down by 70 percent.

The signs of an emerging crisis appeared earlier this year when a so-called stable coin TerraUSD that was supposed to be pegged one-to-one to the US dollar fell below parity, accompanied by the collapse of sister token Luna.

Then came the collapse of the Singapore-based crypto hedge fund Three Arrows Capital which suffered major losses because of its exposure to Terra and Luna. Another crypto firm Voyager Capital has also filed for bankruptcy.

Since the Terra implosion in May, according to the FT, "at least a dozen hedge funds, exchanges and lenders such as Celsius have crumbled, blocking customer withdrawals, raising money at fire-sale prices, or collapsing into bankruptcy."

In its analysis of the Celsius demise, the FT noted that it relied on "a stream of deposits from retail investors that it lent to large crypto companies and used for risky bets on untested ventures.” But last year, as the demand for loans from institutional investors declined, it began to take greater risks.

Small investors were drawn in by the promise of rates of return as much as 18 percent. But the top return was only provided to those who agreed to receive their payments in the form of the company’s CEL token.

According to the FT report, even as the value of the CEL token was falling from the 2021 high of $8 to the level of $1 today, the company was urging investors to hold on to their investments and not sell.

But while these statements were being issued, internal company documents reveal that Daniel Leon, one of the Celsius co-founders, as well as others “had already sold millions of dollars’ worth of their own CEL holdings back to the company.”

Last December, as the crypto slide was beginning, Mashinsky tweeted that all Celsius Network founders had made purchases of CEL and were not sellers of the token.

But the crypto analysis firm Arkham Intelligence has estimated he had sold $44 million worth of CEL tokens through exchanges. So much for the claims by the company in its bankruptcy filing statement that its actions were aimed at protecting customers.

The FT report cited an internal document of the company produced in February last year warning that employees were able to move assets from one fund to another in order to disguise losses and obscure the true value of assets under management (AUM).

“The company may be inflating its representations of AUM and driving up stock price/token price using false financial information,” it said.

The amounts involved have not been small. According to one former trader: “We were clicking in with billions of dollars like any small trader would with $10.”

Back in 2011 in its report on the 2008 crash a US Senate sub-committee found, in the words of its chairman Carl Levin, basing himself on work carried out by investigators, a “financial snake pit rife with greed, conflicts of interest and wrongdoing.”

The significance of the ongoing revelations of the operations of the crypto market is not only that nothing has changed but that it is certain to have worsened in the decade since, given the further massive amounts of money pumped into financial markets by the Fed used to finance speculation.

Much as attempts may be made to characterise the crypto market as some kind of outlier, its rise and rise has been made possible by the same conditions—the provision of ultra-cheap money—that produced a boom in the stock market and all other financial assets.

While the crypto crisis may not be a “Lehman moment” for the broader financial market—at least not yet—it can certainly be characterised as a “canary in the coal mine.”