The FTX crypto collapse and the underlying crisis of the capitalist financial system

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The UK bond market crisis last month, which led to the ousting of Liz Truss as prime minister, and the crash of the high-flying crypto company FTX over the past week have been driven by different immediate causes.

But these two events, which have sent out shock waves, have a common underlying cause—the vast shift in the conditions prevailing in the global financial system over the past eight months.

This is the turn by the Fed, followed by other central banks, to a higher interest rate regime after pumping trillions of dollars into the global financial system (quantitative easing) since the crisis of 2008 and the onset of COVID-19 at the beginning 2020 to prop up speculative finance capital and the stock markets.

Not only has the Fed lifted interest rates at a rapid pace since March, it has also initiated a program of quantitative tightening, reducing its asset holdings at the rate of $95 billion a month.

The significance of the shift was pointed to in a recent blog post by the economic historian Adam Tooze.

"The historical novelty of our situation should not be underestimated," he wrote. "The extent of global leverage [debt], the degree of interconnectedness, the rate at which interest rates are being hiked, the involvement of central banks around the entire world, the interlock with a new array of geopolitical tensions, all mark this as a significant moment of historical departure."

The speed with which these forces are being unleashed is reflected in both the UK and the crash of FTX.

In Britain, the adverse reaction of the financial markets to the Truss government's mini-budget of September 23, which cut taxes to the corporations and the super-rich without major cuts in public spending to pay for it and to further increase government debt, saw a plunge in bond prices and a historically unprecedented rise in their yields.

Almost overnight, pension funds, which had bought financial derivates to try to protect the value of their investments in long-term government bonds (gilts) in the expectation of falling yields, were faced with a major crisis. Their asset holdings, estimated to be as much as €1.5 trillion, were threatened because of the violent fall in bond prices (yields and prices move in opposite directions).

The form of the FTX collapse was very different but it unfolded at the same lightning speed, triggered by an article on the CoinDesk website less than two weeks ago. It pointed out that the FTX crypto exchange, established by Sam Bankman-Fried and Alameda, his trading company, purportedly separate entities, were in fact intimately connected.

It noted that Alameda was "largely made up of a coin that a sister company [FTX] invented, not an independent asset like another fiat currency or another crypto."

The article cited the comments by another crypto operator, who said that the "majority of the net equity in the Alameda business is actually FTX's own centrally controlled and printed-out-of-thin-air token."

These remarks have a broader significance because much of the rest of the financial system, and its various arcane mechanisms, is grounded on equally "thin air" foundations.

The revelations about FTX led Changpeng Zhao, head of rival crypto exchange Binance, to pull his money out of the exchange, prompting a rush for the exits by others.

Last Friday, FTX, supposedly worth $32 billion, filed for bankruptcy. The full extent of the financial fallout has yet to be gauged but the preliminary estimate is that there is a gap of at least $8 billion between the value of its assets and its liabilities.

Speed is not the only similarity to the UK crisis. The strategy of the British pension funds, so-called liability-driven investments, was not considered a risky venture. On the contrary, it was endorsed by Britain's pensions fund regulator.

FTX was financed by some major names in the financial world, including venture capital firm Sequoia. It received money from BlackRock, the Japanese financial firm Softbank and even a Canadian pension fund. This prompted a severe tut-tutting from a *Financial Times* editorial, recalling the scene in the wartime movie *Casablanca* in which the police chief Louis Renault is "shocked" to discover gambling is going on in Rick's Café.

But the FT did not seek to explain why such an event occurred, the second time this year a Canadian pension fund had been involved in a crypto collapse, the first being the demise of Celsius Network.

The LDI strategy pursued by UK pension funds, which almost led to their collapse, requiring the intervention of the Bank of England, resulted from their inability to obtain sufficient funds from their traditional source, gilts, because their yields had been driven so low. Likewise, the involvement of a Canadian pension fund in crypto had the same underlying cause.

They and other big name investors were drawn by the hype surrounding FTX, including naming rights for a major basketball stadium and endorsements by celebrities, such as the famous NFL (National Football League) quarterback Tom Brady.

Less than two months ago, Sequoia published a 13,800-word profile of Bankman-Fried, since removed after the company estimated the value of its FTX investment to be zero, saying he had reached the "status of legend" and had a "vision about the future of money itself."

In reporting on the FTX demise, the financial press has generally offered the reassurance that crypto is not a central component of the financial system, and there will be few direct flow-on effects.

That remains to be seen as the full story of the connections of FTX and its sister company Alameda has yet to emerge.

But in considering the possible fallout effects, it should be recalled that in early 2007, the then chair of the US Federal Reserve, Ben Bernanke, insisted the emerging crisis in the sub-prime mortgage market would not flow on because it was only a very small part of the overall market.

A year and a half later, in September 2008, a full-blown crisis erupted because the rot in the sub-prime market, resulting from speculation with cheap money, was rife throughout the financial system.

Any exclusive focus on the immediate connections of FTX ignores the fact that the ongoing financial storms have the same underlying cause—the shift in the operations of the global financial system.

The meaning and significance of this shift can only be grasped by probing deeper to the underlying social and class relations which assume such a mystified form in the world of finance.

The role of the Fed and other central banks is not, as they attempt to portray, to promote economic expansion or the well-being of the mass of the population. They are the guardians of the interests of finance capital above all else.

Ever more openly since the October 1987 stock market collapse, their number-one priority has been to promote the wealth of the corporations and the financial elites. Consequently, the financial system has become an institutionalised mechanism for siphoning up the wealth produced by the labour of the world's working people to the upper layers of society and their hangers-on—a fact attested to by data showing ever-widening social inequality.

For the past several decades, this objective has been achieved by pouring ever greater amounts of money into the financial markets, particularly in response to the crisis of 2008 and the onset of the COVID-19 pandemic in 2020.

The suppression of the working class by the trade unions and the continuous decline in real wages was a key factor in facilitating the financial orgy.

But now a vast change has taken place in class relations.

The refusal of capitalist governments to eliminate the virus through necessary public health measures, fearing their adverse impact on stock markets, the supply of still cheaper money and now the US-led war against Russia in Ukraine, have resulted in the highest inflation in four decades.

When inflationary pressures began to emerge in 2021, they were dismissed by the Fed and other central banks as "transitory" in the hope that the previous policies could continue.

But the persistence of inflation led to the development of the greatest of all the fears of finance capital and its guardian, the central banks—the emergence of the class struggle, as the working class moved to combat the continual cuts in its living standards.

Consequently, the Fed and its international counterparts insisted from March that monetary policy had to be geared to the "fight against inflation," above all, through interest rate hikes.

But no amount of interest rate increases is going to bring down prices in energy, food or other basic items. Rather, their aim is to slow the economy, if necessary, through a recession, to batter down the wage demands of workers all over the world. At the same time, the trade union apparatuses, tied by a thousand strings materially and politically to finance capital, are working to impose this agenda.

But this class war has major financial ramifications as interest rate hikes threaten to collapse the mountain of fictitious capital and debt based on cheap money.

The UK bond market storm, the demise of FTX and the deepening crisis of crypto it expresses, the sharp fall in interest rate-sensitive high-tech stocks on Wall Street are just some of the indications of this.

This last weekend the *New York Times* ran an article warning that with the rise in interest rates, "the corporate bond market, which lends money to many companies, has been hammered particularly hard."

The *Financial Times* has published a major article headlined "The global housing market is heading for a brutal downturn."

There are continuing reports in the financial press that liquidity in the $24 trillion US Treasury market, the basis of the global financial system, is the tightest it has been since it froze in March 2020 at the start of the pandemic.

The working class must grasp the implications of the deepening financial crisis, the consequences of which will go far beyond those of 2008, significant as they were.

The necessity for a socialist program is being established in the economic and financial facts of life. No amount of reformist tinkering can resolve what is an existential crisis.

The key task in the development of every immediate struggle is the fight for the advancement of the conquest of political power by the working class, to end forever the domination of finance capital over every aspect of daily life and to lay the foundations for an economy based on human need and not the dictates of the profit system.