Warnings of new financial bubble as bitcoin price hits $10,000

By Andre Damon
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The price of the digital currency bitcoin reached $10,000 late Tuesday, an eleven-fold increase since the start of the year, when it was valued at $900.

The explosive surge of bitcoin, the first so-called "cryptocurrency," or digital money, has eclipsed the run-up of any comparable asset in modern history. As the *New York Times* noted Tuesday, "The Dow Jones industrial average, in its biggest year, 1915, went up 82 percent, or one-tenth as much as Bitcoin has gone up this year. Amazon's red-hot stock is up only one-fifteenth as much as Bitcoin this year."

To find financial bubbles comparable in scale, commentators have reached back hundreds of years to compare the bitcoin mania with the Dutch Tulip bubble of the 17th century and the South Sea bubble of 1721.

But with the rally in bitcoin and other cryptocurrencies showing no signs of stopping, Wall Street and major financial institutions around the world are pouring billions of dollars into a financial asset that is totally unregulated, has no clear rules for lending and exchange, and no consumer safeguards.

With major investors flush with cash from open central bank spigots and soaring stock prices, there is every indication that this dangerous asset class is assuming an ever-larger presence on the balance sheets of banks, hedge funds and other outposts of the financial system.

The odds are increasing of another global financial meltdown on the scale of 2008, this time centered on cryptocurrencies instead of subprime mortgages.

The origins of bitcoin are shrouded in mystery. First introduced in January of 2009 by an unknown individual or group claiming to be a Japanese man named Satoshi Nakamoto, its nameless creator is now sitting on a nominal fortune of some $7 billion.

The currency was initially proposed as an anonymous and secure method of payment that bypassed central banks and government regulations, leading to its early adoption by anarchist and libertarian-minded individuals. In the ensuing years, however, it became clear that, due to its wild price fluctuations and institutional restrictions, bitcoin was inconvenient as a method of payment.

While an array of other cryptocurrencies have been created in an attempt to fill bitcoin's purported role as a cash substitute, bitcoin's proponents now advocate it as a long-term store of value, similar to gold, and supposedly immune to geopolitical instability. They promote it as a safe haven for investors living in countries with unstable currencies.

While the role of cryptocurrencies as either cash substitutes or as long-term stores of value remains unclear, bitcoin has proven its worth in one respect: as a vessel for rampant financial speculation.

This was made clear by hedge fund billionaire Mike Novogratz, who declared earlier this week that he expects the price of bitcoin to hit $40,000 by the end of next year. "There's a big wave of money coming, not just here but all around the world," the billionaire told the business cable channel CNBC.

"What's different about these coins than other commodities," he said, is that "there is no supply response here. So it's a speculator's dream in that as buying happens, there's no new supply response that comes up. So every price move gets exaggerated. It's going to get exaggerated on the way up. There will be 50 percent corrections. It will get exaggerated on the way down."

To bolster his bullish claims about bitcoin, Novogratz billed it as a direct competitor to gold. "Bitcoin really has taken the use-case of digital gold," he said.

In a telling example of the type of speculative mania that has taken hold among the financial elites, he candidly admitted to holding 30 percent of his net worth in cryptocurrencies, despite having advised even very rich investors to hold no more than five percent of their net worth in such assets just seconds earlier.

Whatever the merits of cryptocurrency as a store of value—and these have been widely questioned by financial, technology and security experts—the idea that Wall Street is going to create a substitute for gold out of thin air, then keep trillions of dollars of this magical substance on its balance sheets and watch what happens, is a recipe for a financial disaster.

On Wall Street, such an outcome is not totally unwelcome, given that the financial elite made out like bandits from the last crash.

Bitcoin is the latest in a series of financial bubbles that have been inflated since the stock market crash of October 1987, from the low interest rate, deregulated regime introduced by then-Fed Chairman Alan Greenspan, which fueled the 1997-1998 Asian, Russian and Long-Term Capital Management crises, to the dot-com bubble collapse of 2000-2002, to the 2007-2008 subprime mortgage implosion. Increasingly, US and world capitalism have relied, addict-like, on the most parasitic and socially destructive forms of financial speculation.

The 2008 financial crisis was triggered by the collapse of the subprime mortgage bubble, which was driven by lending to consumers who were sold houses they could not afford and told their mortgages were investments that were sure to make money. As it turned out, the major Wall Street banks and hedge funds had massively speculated in subprime mortgages, which were repackaged as "collateralized debt obligations" and held on the balance sheets of financial firms.

An accelerating rise in default rates caused a massive sell-off in mortgage-backed securities, blowing multibillion-dollar holes in the balance sheets of leading banks and financial companies. The US government responded by using taxpayer dollars to finance multitrillion-dollar bailouts to the biggest Wall Street banks.

In the aftermath of the bailout, central banks around the world kept interest rates at historically low rates and introduced further measures to expand the money supply, such as the US Federal Reserve's quantitative easing program. This led the US stock market to increase in value by more than 3.5 times over the ensuing seven years, a rally that has continued, with all three major US stock indexes hitting new records Tuesday.

Now, with financial markets flush with cash, billionaire investors are eyeing cryptocurrencies as a means of securing even more massive returns on their investments. When and how this bubble pops is difficult to predict, but one thing is clear: When it does, it will take a substantial chunk of the real economy with it, with disastrous consequences for working people all over the world.