

Funding the Future

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<https://www.taxresearch.org.uk/Blog/2025/09/02/stablecoin-meltdown/>

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This post was nearly complete yesterday when the MacBook on which I was writing it failed. I am told that when it is repaired, most of it will have been replaced. Apparently, it had tea or coffee in its workings, although I am very unsure as to how. Thankfully, it was insured for the risk of such eventualities arising.

The post remains relevant today, so here it is, a day late, and automatically saved during the crash that happened:

As the *FT* noted yesterday:

Jean Tirole, a Nobel Prize-winning economist, has warned about “insufficient supervision” of stablecoins and the possibility that governments will be forced into multibillion-dollar bailouts should the tokens unravel in a future financial crisis.

In an interview with the Financial Times, the winner of the 2014 Nobel Prize in economics said he was “very, very worried” about supervision of stablecoins and the possibility of a run by depositors if doubts materialised over the underlying reserve assets to which the digital tokens were pegged.

As he told the paper:

“If [stablecoins are] held by retail or institutional depositors who thought it was a perfectly safe deposit, then the government will be under a lot of pressure to rescue the depositors so they don’t lose their money.”

That single sentence goes to the heart of the problem. Stablecoins pretend to be money — and yet, unlike real money, they are neither guaranteed by governments nor properly supervised. It didn't take an economics prize winner to notice that, but he is right for a number of reasons.

The issues

First, what is being created here is a shadow banking system. The promise is that these so-called coins are “backed” by assets such as US Treasury bonds. However, those bonds often yield low returns in real terms. The temptation, as Tirole notes, is in that case to chase higher returns to increase profits, and that, inevitably, means riskier assets. Once that happens, the promise of stability disappears. A single shock could, in that case, unravel the whole edifice in Tirole's opinion, as I have been saying for some time. That risk is real.

Second, there is the politics of this matter. Tirole is explicit that when members of the US administration, including Donald Trump and his family, have personal and ideological stakes in this business, already weak regulation may be deliberately compromised. That, of course, is a recipe for cronyism and, ultimately, disaster. The likelihood of that happening is high.

Third, the systemic consequences cannot be overstated. So-called stablecoin savings now amount to nearly \$280 billion. That is not trivial. If even part of that unravels, retail and institutional holders will, as Tirole suggests, demand financial rescue from the state and politicians, fearing contagion and public anger, will almost certainly comply. What has begun as a “private innovation” might well end as a public bailout in that case.

Fourth, this is not just a financial stability issue. It is about sovereignty. A global system of dollar-linked private tokens undermines the ability of governments and central banks to conduct monetary policy. In effect, the private interests of supposed crypto entrepreneurs and the ideological obsessions of Trump could neuter the capacity of democratic states to manage their own economies.

The consequences are clear

First, we risk repeating the story of 2008: private actors chasing returns whilst regulators are asleep or looking the other way might create a crash, and the public will then be forced to pick up the bill when the inevitable collapse comes.

Second, the fiction that “innovation” in finance is always desirable is wrong: that is just a story told by those who make short-term gain. Stablecoins are nothing more than unregulated deposit-taking, dressed up in the language of technology.

Third, there is an issue for democracy here. If governments cede control of money creation and supervision to private actors with political patrons, then accountability in economic policy is lost. That makes the fight over the Fed look almost insignificant in comparison.

So what should be done?

First, regulators must end the pretence that stablecoins are harmless. They are not. They are systemic risks in the making.

Second, we should refuse the framing that this is “innovation”. It is not. It is the re-emergence of privately issued money, with all the instability that entails.

Third, governments must assert that money is, and must remain, a public good*. That means banning the effective private minting of supposed substitutes that pretend to be safe deposits but are nothing of the sort.

And finally, we must name the politics. This is not just a financial debate. It is about whether democracy retains control over money, or whether that control is handed to a network of oligarchs, speculators and opportunists, including politicians with the power to manipulate regulation.

Jean Tirole is right to be “very, very worried”. We should be, too.

*** A public good is usually something provided by a government without the aim of making a profit, which has two defining features. First, it is non-rivalrous, meaning one person’s use does not reduce what is available to others, and, second, it is non-excludable, meaning it is difficult or impossible to stop people from benefiting once it exists. Street lighting, clean air regulation, or national defence illustrate the point: everyone benefits, and no one can sensibly be excluded. Money also meets this criterion, as does an effective progressive taxation system. These qualities create the free rider problem, since private providers cannot charge effectively for use. As a result, markets underprovide public goods, making government intervention essential if society is to function well.**

Comments

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Taking further action

If you want to write a letter to your MP on the issues raised in this blog post, there is a ChatGPT prompt to assist you in doing so, with full instructions, [here](#).

***One word of warning, though: please ensure you have the correct MP.
ChatGPT can get it wrong.***