

# Chapter 17

## The New Financial System: A Revolution Made by Fintechs

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### ABSTRACT

*This chapter shows the revolution that is happening in the financial system, having as main actor the technological companies—the fintechs—that don't have financial knowhow. The traditional banks didn't structure their business trying to attend the client's needs. The clients always suited themselves to banks' services. The fintechs are changing this reality by putting the client in another baseline, filling the gaps left by the banks, offering new services, and acting in places where banks have never gone before. The fintechs are offering these services with a lower price and more quality for the clients.*

### INTRODUCTION

This chapter aims to motivate the discussion about a huge revolution in financial system that is happening right now. Banks have always acted in society as the key agents in the intermediation of financial transactions. Since their inception, they have been important pieces for the economic development of the world, ensuring security and care of the money of people and nations.

After the crisis of 2008, generated by the neglect of the current financial system, the supremacy of the banks have become questioned. Moreover, the institutions did not evolve like other economic segments. Banks have continued to be bureaucratic, charging high rates for services and barely meeting customer needs. Most people consider going to the bank an unpleasant activity.

Fintechs are taking advantage of the abyss between the needs of customers and the services effectively provided by the banks to revolutionize the financial system as we know. The chapter will address the beginning of the global financial system, the economic crisis of 2008, followed by the challenges faced by the banks in the current scenario. Subsequently, it will be approached what are fintechs, their different segments, the unprecedented revolution that they are driving in the financial system and traditional banks reaction.

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## THE BEGINNING OF FINANCIAL SYSTEM

The banks are fundamental agents in the economic development of the nation. They are the financial intermediation between the population and the Central Bank.

The first banks were created in XVII century, in Europe. Due the expansion of the trade by the bourgeoisie, there was a need to keep the coins in somewhere safe. Since the bourgeoisie traveled for long distances, as they went about selling their wares, they accumulated more and more coins and it was dangerous to travel with large sums of money.

In this way, the bourgeois handed the coins to the bank, which gave them a paper as guarantee. After the presentation of this paper, the banks returned the coins. Over time, this paper began to be accepted as the bargaining chip in financial transactions.

The bourgeoisie restructured trade and integrated the regions which had so far lived only within their fiefs, propelling the end of the feudal period.

The activities of the banks provided security for the bourgeoisie and for people who had money beyond what was necessary for survival. This was paramount for the evolution of the trade and the development of the worldwide economy as we know it today.

Since then, the way that business were accomplished, has changed completely. Banks began to participate in most of the world's commercial and financial transactions, taking care of the money of individuals and nations. Always being considered as secure institutions, and often adding credibility to the transaction itself, just because they are involved in.

## BRAZILIAN BANK SYSTEM

In Brazil, the predominant financial institutions are the multiple banks that operate in several segments of the financial market, collecting deposits / savings, and intermediating credit and financial security transactions (Freaza, Guedes and Gomes, 2008).

The profitability of Brazilian banks has grown in recent years, according to Arienti (2007). The author says that the degree of profitability - the proportion of net income to shareholders' equity - that measures the capacity to generate income for shareholders on invested capital has increased in the country, as can be seen in the table 1 below.

Table 1 shows that, in 2002, the percentage of profitability reached the mark of 27%, the record of the period. Despite the fall in profitability in 2003 to 14.7%, this percentage is still higher than the profitability at the beginning of the analyzed period, 14.4% in 1994. In summary, Brazilian banks continue to

*Table 1. Percentage of profitability from Brazilian banks\**

| Year          | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 |
|---------------|------|------|------|------|------|------|------|------|------|------|
| Profitability | 14.4 | 11.9 | 12.3 | 8.5  | 16.3 | 23.0 | 19.2 | 19.2 | 27.0 | 14.7 |

\*Author's note: Banks selected until 1999 were América do Sul, Bandeirantes, BCN, Boavista, Bradesco, HSBC, Bamerindus, Itaú, Mercantil de São Paulo, Noroeste e Unibanco, after 2000 were Bradesco, Unibanco, Itaú, Safra, HSBC, Bank Boston, Citibank e ABN AMBRO.

Source: ARIENTI F. F. P. Reestruturação e consolidação do sistema bancário privado brasileiro, Ensaios FEE, Porto Alegre, v. 28, n. 2, p. 577-600, out. 2007.

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