Chapter 5

The World’s Oldest Profession
– Now and Then:
Disruption of the Commercial Banking Model

Steven A. Cinelli
REMARQ, USA

ABSTRACT
Modern banking found its roots during the Renaissance period casted by the European merchant banks. Their success was due in large part to their aggregation, absorption and deployment of information about borrowers, structures and markets. In the 21st century, banking again is being advanced due to insights developed by vast amounts of information and data, this time gathered and managed through new technologies and models, in quest of efficiency, improved risk management and improved portfolio performance. New entrants into the business of banking operate outside of existing regulatory structures, and may enjoy a level of competitive flexibility compared to existing commercial banks. Might this portend the end of the so-called modern commercial banking model, or might it serve as a strategic imperative for the banks to adapt to innovation?

THE WORLD’S OLDEST PROFESSION: IN TIMES OF CHANGE

While the title of this chapter may have caused a heart to skip a beat, we are not referencing the happenings in a brothel where the practice of carnal frivolity may prevail. A quip by Rudyard Kipling in the 19th century laid claim to this descript, but in paging through history, we find that one industry may have even longer lineage, with such industry currently in the midst of one of its most significant transitions.

We are speaking of banking and the art of the money lending. Ascribed to Babylonia over four millennia ago, the practice of deposit taking and granting credit further evolved within ancient Greece and the Roman Empire. As some have placed the Code of Hammurabi (1800 BC) as the basis for use of women as chattel, commercializing the “other” old profession, the Code also laid out the basis for economic
transactions, seemingly a predicate for the practice of lending funds (Graeber, 2011). Even Asia developed a system of credit extension during select dynasties around 1000 AD. The modern age of banking is generally viewed as being borne from the European merchant banking families who saw opportunities to broaden their trading of goods and commodities to the extension of credit to other merchants desirous of trading themselves. Dating back to the 14th century and throughout the 19th century, families such as the Medicis, Fuggers, Warburgs, Barings, Hambros, Abs, and Rothschilds evolved from funding their own activities, to becoming financiers for others, including the largest of industrial companies and sovereigns. From the Renaissance period through the emergence of the modern commercial bank, such merchant banking activity drove economies. As Jared Diamond phrased it in his iconic tome, *Guns, Germs and Steel: The Fates of Human Societies*, “As society develops, so does the economic structure. Banking and finance are fundamental parts of the ‘societal genome’” (Diamond, 2007).

The success of the merchant banks during yesteryear is characterized by a prevailing attitude, one of which knowledge was everything, and those with it, carried the day and had their way. Whether that might encompass comprehending trade routes, financing structures, commodity prices, margins and risks, capital strength of a customer, even anticipating outcomes, the merchant bankers applied their skills as “merchants” first, and then how to profitability finance an independent project or party. Essentially, their knowledge of “conditions” proved to be both a value-add, but further a competitive edge over other potential financing parties, and sometimes even the businesses they financed. Walter Bagehot, a Victorian London banker, stated, “We must not let in daylight upon magic”, emphasizing the laconic nature of bankers to share information (Wechsberg, 1966). They used this to their advantage, underscoring that information was the elixir for optimal financial decision making.

In its essence, finance is truly an information business. Potential users of capital convey information to providers of capital and through an iterative process, an outcome of risk-adjusted finance emanates. Investing, trading, and lending results are determined by “good, better and best” information. Roll this observation forward to the 21st century, we witness the extensive power of information technology in banking and finance to generate, decipher, improve, expedite, analyze and regurgitate reams of data points to render broader yet tailored, robust yet quicker decisions, which are intended in the end to improve financing outcomes. Simply, it’s all about the information.

**A Challenge**

More so than other industries, banking and finance have historically sought applied technology to enable improvement in existing processes and reducing costs, including that of risk assessment. The challenge is that much of the earlier applied technology has been developed and adapted through many years, creating a spiders’ web of legacy systems, needing to be continually serviced.

Think about the analogy of telecommunications. Throughout much of the Americas, Europe, and Asia, there has been a constant evolution of telecommunications, but these developed countries, even with current wireless means, still have considerable investments in wiring, cabling, pipes, and poles, all supporting part of the telecom infrastructure, which remains costly and inefficient, and experiencing the law of diminishing returns. Consider now the developing regions, like Africa, parts of India and China, void of such legacy structures, which are launching immediately into a modern telecom infrastructure, and in the end, might enjoy considerable advantage.