

## A Brief History of the Brazilian Financial System: From the 19th Century to the Current Dynamics of Financialization and Concentration

*Uma breve história do sistema financeiro brasileiro: do século XIX até as atuais dinâmicas de concentração e financeirização\**

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**Resumo:** Com a intensificação da financeirização da economia brasileira nas últimas décadas, torna-se cada vez mais importante a compreensão das dinâmicas em torno do Sistema Financeiro Brasileiro (SFB). Com o intuito de contribuir com essa empreitada, o presente artigo reconstitui um breve histórico do SFB, partindo do século XIX até as primeiras décadas do século XXI. Além disso, os dados examinados no processo de reconstituição da história do SFB corroboram a visão do SFB atualmente caracterizado pela financeirização e concentração de ativos em poucas instituições.

**Palavras-chave:** Sistema Financeiro Brasileiro. História do Sistema Financeiro Brasileiro. Financeirização.

**Abstract:** With the intensification of the financialization of the Brazilian economy in recent decades it has become increasingly important to understand the dynamics surrounding the Brazilian Financial System (BFS). To contribute to this endeavor, this article reconstitutes a brief history of the BFS, starting from the 19th century to the first decades of the 21st century. Furthermore, the data examined in the process of reconstituting the history of the BFS corroborate the view of the BFS currently characterized by financialization and concentration of assets in a few institutions.

**Keywords:** Brazilian Financial System. History of the Brazilian Financial System. Financialization.

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## 1. Introduction

Since the neoliberal turn and the end of the Bretton Woods conventions (Gowan, 1999; Harvey, 2008; Chesnais, 1996; 2016) the process of financialization has intensified worldwide, and Brazil is no exception. Financialization is understood as a process through which financial capital has become predominant to the detriment of productive capital, in synthesis, "[...] a regime of accumulation with the dominance of financial valorization." (Paulani, 2009, p. 26). That is, "[...] a rentier phase in which the imperatives of capital as property override the imperatives of capital as a functioning element in the production of goods and services." (Paulani, 2017, p, 30).

Specifically with respect to Brazil, some arguments point in this direction. First, gross investment in fixed capital (machinery and equipment, structures and buildings, livestock, and permanent crops) has declined since the 1980s, from 18.5% of GDP in the 1980s, to something around 14% in the first decade of the 21st century. (Paulani; Pato, 2005; Paulani, 2012). Second, Brazil has been transforming itself into an international platform for financial valorization. (Paulani, 2017). If in the 1980s and 1990s Brazilian remittances abroad were tied to the foreign debt crisis and the economic opening, respectively, in the 21st century most of these remittances have come to be composed of income from investments in Brazilian public debt securities quoted on the international market. (Paulani; Pato, 2005). Third, there is a scenario of exorbitant interest rates and yields above the world average. For example, credit card interest rates at major banks were around 257.4% in May 2020 (Anefac, 2020a). This scenario shows household consumption, and business investment, and provides little incentive for financial institutions to act as dynamizers of the economy (Dowbor, 2015; 2018). And fourth, both the profits and assets of the major financial institutions have increased substantially in recent decades. In 2019, for example, Itaú's profits broke a record, with a 20.6% increase over the previous year.

Even in the face of such a political-economic phenomenon there are few works that seek to synthesize the historical dynamics and current characteristics of the Brazilian Financial System (BFS), a key actor in the face of financialization. Considering this gap, in this paper we propose to provide a brief history of the BFS, covering from the nineteenth century to recent developments. To this end, we have compiled a series of papers on the BFS and financialization in the country

and combined them with some secondary data provided by the Central Bank (BACEN). In this way, the paper provides a brief history of the Brazilian Financial System up until the 21st century and summarizes some positions on the advance of financialization in Brazil. Furthermore, the data examined in the reconstruction of the history of the BFS corroborate the view of the BFS currently characterized by the advance of financialization and a significant increase in the concentration of assets in a few institutions.

Without further delay, the paper is structured as follows. First, we will give a brief historical overview of the BFS will be constructed, starting from the 19th century – marked by the search for a stable system through the institutional figure of the Banco do Brasil – to the 1970s and 1980s, which were characterized by financial crises and increasing public debt. We will then look at the liberalization of the 1990s, a paradigmatic moment for the BFS and its integration into global financial circuits. In a third part we will deal with the main elements that characterize the Brazilian Financial System – and, more generally, the Brazilian economy itself – in the 21st century. Finally, we will present the concluding considerations.

## **2. History until the 1980s**

In 1808, the first Banco do Brasil was established to deal with the growing commercial demands generated by the opening of Brazilian ports. This first – of three versions – of the Banco do Brasil marked the beginning of a financial system that would be marked by crises and reforms throughout the 19<sup>th</sup> century, but also by the need to expand for the banking sector in light of the growth of the Brazilian economy due to the expansion of the coffee sector. In 1829, the bank was dissolved. Thus, until the re-establishment of the Banco do Brasil in 1853, the country did not have a banking institution officially linked to the State, help it provide credit and currency. With the creation of the new Banco do Brasil through the liquidation of the Banco Comercial do Rio de Janeiro and Banco do Brasil de Mauá, a process began in which several regional institutions were incorporated into the Banco do Brasil or became its branches. This involved Banco Comercial da Bahia (founded in 1845 and incorporated in 1856), the Banco Comercial do Maranhão (founded in 1846 and converted into a branch in 1858), the Banco Comercial do Pará (founded in 1847 and incorporated in 1856), and the Banco de

Pernambuco (founded in 1851 and incorporated in 1855) (Calogeras, 1960; Pessoa, 2016).

Thus, the second Banco do Brasil obtained the monopoly of emissions in Brazil in 1853. In addition, as Pessoa (2016) points out, the institution was instrumental in maintaining the balance of the system, albeit temporarily, rescuing institutions that suffered from the crisis of the early 1860s. However, its monopoly on the currency issue lasted only until 1857, when it lost its ability to issue currency and bonds to institutions in other provinces, especially Rio de Janeiro. In 1890, the merger of the Banco dos Estados Unidos do Brasil and the Banco Nacional created the Banco da República dos Estados Unidos do Brasil. The following year, Banco do Brasil is forced to transfer to Banco da República its currency issuance privilege, becoming a bank for deposits and discounts only. Shortly thereafter, Banco do Brasil merged with the new Banco da República to create Banco da República do Brasil, with the objective of providing for the national industrial needs. Finally, amid an acute banking crisis in the early 20th century, it is proposed that Banco da República do Brasil be reformulated to deal with the growing monetary and exchange problems. The derivative institution takes back the old name Banco do Brasil – for the third time – and returns to have the monopoly of issuing currency in the country, a status that lasted until 1986 (Calogeras, 1960; Pessoa, 2016).

In general, Banco do Brasil in the 19th century was part of a difficult economic context, marked by colonial liabilities, the decline of the sugar economy, the rise of coffee economy and attempts to submit to the monetary rules prevailing in Europe – the gold standard. (Furtado, 2007). As Furtado (2007) states, “[the] installation of a rudimentary administrative system, the creation of a national bank and a few governmental initiatives constituted – while preserving national unity – the net result of this long period of difficulties”. (Furtado, 2007, p. 164).

The Brazilian financial system in the 19th and early 20th centuries was not only characterized by the back-and-forth over the Banco do Brasil. Foreign institutions were also present in the country. In 1863, the London and Brazil Bank was established in the country, followed by other British and German institutions. Lured by the coffee boom triggered by high commodity prices on international markets, these institutions focused on financing the international coffee trade. Thus began a period that lasted until the 1920s characterized by the strong presence of

foreign institutions in the BFS. In 1912, 56% of bank loans came from foreign owned institutions. In 1926, for example, there were 13 foreign banks and only 9 domestic banks in the state of São Paulo. Foreign capital was even directly related to the creation of new financial institutions in different states of the federation. French capital enabled the creation of Banco de Crédito Hipotecário e Agrícola do Estado de São Paulo (later transformed into Banespa) in 1909 and Banco do Estado do Espírito Santo in 1919. In a similar process, Crédito Real de Minas Gerais - founded in 1889, - and Crédito Hipotecário e Agrícola de Minas Gerais, founded in 1911, were created in Minas Gerais. However, the presence of foreign capital in the BFS in the period was fundamentally directed at operations with low risk and higher rates of return, basically commercial loans and foreign exchange operations. Thus, foreign financial institutions practically did not allocate capital to domestic trade and agriculture, leaving domestic banking transactions to public and private domestic institutions (Rocha, 2002).

From the 1930s until 1946, due to the 1934 and 1937 Constitutions and the World War II, the presence of foreign financial institutions in BFS was drastically reduced. (Rocha, 2002). However, the scenario changed in 1946, when the new Constitution ended the distinction between domestic and foreign banks regarding bank control. Thus, foreign banks began to enjoy free access to the Brazilian Financial System, to the extent that the capital of financial institutions headquartered in Brazil could be exclusively foreign. Until 1964, then, foreign institutions had complete freedom of access to the Brazilian Financial System (Penido; Prates, 1998; Corazza; Oliveira, 2007).

In 1964-65, after the Military Coup, a major banking reform took place in the country through Laws no. 4595 of 12/31/1964 (Banking Reform Law) and 4728 of 07/14/1965 (Capital Markets Law), inspired by the US model and its Glass Steagal Act. One of the main objectives of the reform was to create the necessary conditions for the constitution of a long-term private segment in Brazil, as well as to create financing mechanisms capable of sustaining the industrialization process underway. Two results derived from the reform. The main one was the creation of the Central Bank of Brazil (BACEN). Until that moment Brazil did not have a central bank. Until 1945 the Banco do Brasil performed this function, which passed into the hands of the Superintendency of Money and Credit (SUMOC) in the same year. The 1964-65 reform also gave the BACEN the authority to allow financial

institutions to operate in the country, as well as to supervise and impose penalties on these institutions. The second result was capital market legislation. This initiated a period of great activity in the stock markets of Rio de Janeiro and São Paulo between 1967 and 1971, a bonanza that ended with the international crisis of the early 1970s (Gambiagi *et al.*, 2011; Leite, 2011; Barbosa, 2020; Assaf Neto, 2008; Yoshino, 1998).

The banking reform of 1964-65 also introduced the application of the reciprocity principle to govern the activities of foreign financial institutions in the Brazilian Financial System. This principle, in general, established "[...] that the access and activities of foreign financial institutions are subject to the same restrictions or prohibitions that apply to national banks, present or interested in establishing themselves, in the financial markets of their countries of origin." (Penido; Prates, 1998, p. 188). In this way, the control of Brazilian financial institutions by foreign institutions was limited to 30%. The principle of reciprocity lasted until 1995, and during this period the creation of representative offices of foreign financial institutions was freely permitted. In this way, the reform also promoted financial openness, which was understood as an instrument that could contribute to both the efficiency and effectiveness of the SFB, beliefs that were also present in the opening of the 1990s, as we shall see in the following pages. (Penido; Prates, 1998, 2001; Corazza; Oliveira, 2007; Gambiagi *et al.*, 2011).

In the late 1960s, Brazil experienced an unprecedented financial opening. This opening, however, was not marked by the entry of foreign financial institutions into the country, but by a huge absorption of foreign loans. The country's foreign debt, which in 1966 was more than 4 billion dollars, reached 50 billion dollars in 1979. Part of this increase can be credited to the effects of the oil crisis and changes in US economic policy (Moura, 1981).

In the early 1970s, with the introduction of the National Treasury Bills (LTN), a short-term National Treasury security that was sold at a discount from its face value, the Brazilian open market for securities began. All the operations involving these securities were carried out by the BACEN. However, at that time, the LTN was created much more with the purpose of serving as a monetary policy instrument, than as a financial "product" per se. It was also in the 1970s, specifically in 1976, that the joint-stock companies and securities markets Act was enacted. The law also established the Comissão de Valores Mobiliários (CVM),

with the objective of ensuring the operation and efficiency of the securities and stock markets (Leite, 2011; Barbosa, 2020).

In the 1970s and 1980s, the first financial conglomerates began to emerge in the country. Initially, these conglomerates consisted of several companies with their own legal personality and specialization in distinct segments of the financial market. Skirting the legal restrictions in place at the time, these groups ended up developing administrative mechanisms that in practice turned the different companies into one. It was to some extent to deal with this situation that in 1988, through Resolution 1524, *bancos múltiplos* (financial conglomerates) were created. Thus, commercial, investment or development banks, credit, financing and investment companies, and real estate credit companies were allowed to be reorganized as a single institution. Thus, it was established that these institutions should have at least two credit portfolios, one of which must be commercial or investment (Barbosa, 2020).

### **3. The Liberalization of the 1990s**

The 1988 Federal Constitution (CF) established that the guiding axis of the national financial system should be its economic and social utility, that is its function should be to promote a balanced development of the country that serves the interests of the community. Thus, it was established that the maximum annual interest rate should be 12% above inflation. However, in 1999, with the Proposed Constitutional Amendment (PEC) 53/1999, later transformed into Constitutional Amendment 40/2003, the set of paragraphs of article 192 of CF 1988 dedicated to the regulation of the national financial system was repealed. (Ianoni, 2010; Dowbor, 2018). The CF 1988 also prohibited the entrance of foreign capital into the BFS. This occurred due to the need for the elaboration of a legal framework by Congress, which has not yet been established. In any case, article 52 of the Transitional Constitutional Provisions Act (ADCT) left open the possibility that the presence of foreign capital could increase in the following specific cases: authorizations resulting from international agreements, application of the principle of reciprocity, as a counterpart for the establishment of branches of Brazilian banks abroad, and finally, if considered to be of national interest by the government. It was precisely by taking advantage of the latter case that, in August 1995, the entrance and expansion of foreign participation in the BFS was allowed (Penido;

Prates, 1998; Corazza; Oliveira, 2007; Penido, 2011).

This does not mean, however, that from the enactment of CF88 until 1995 the BFS was completely closed or that no moves were taken toward financial openness. At the beginning of the 1990s, 32 foreign banks were operating in the country in the form of subsidiaries and branches. Several of these banks had already been present in Brazil for several decades, such as Citibank, Chase Manhattan, Bank of Boston, ABN, Loyds and Deutsche Bank. Another 32 national banks had minority foreign ownership. (Penido, 2011). In the same period, the Collor Plan waved to the financial sector through the reformulation of foreign exchange markets and the creation of the “dólar livre”, including for financial transactions, which led to a growing internationalization already in the year 1990 (Burle, 1995; Gennari, 2001).

In turn, Paulani and Pato (2005) show that in 1992, with Itamar Franco, there were changes of great magnitude that prepared the country for its insertion in the international circuit of financial appreciation. During the negotiations that were supposed to guarantee the internationalization of the Brazilian securities market and the securitization of the external debt, BACEN's foreign affairs department advanced in promoting the deregulation of the Brazilian financial market and the opening of the international flow of capital through two measures. First, it broadens the concept of "non-resident". With this measure, the "non-resident" category included - in addition to the legal entities and individuals who were in transit through the country - the accounts of financial institutions that were not authorized to operate in Brazil. Second, the remittance of funds abroad is made more flexible. Thus, the authors clarify, it was created "[...] the possibility for any agent, regardless of being a resident or non-resident, to freely send resources abroad, simply by depositing domestic currency in the account of a non-resident financial institution." (Paulani; Pato, 2005, p. 20). In summary, the listed changes "[...] produced, together, the form and substance of Brazil's insertion in internationalized market finance." (Paulani; Pato, 2005 p. 21). This occurs because, with the Brazilian debt securities launched abroad, the country places itself as an issuer of fictitious capital, while the financial liberalization and the guarantee of free transit of financial capital allowed operators to maximize the use of restrictive monetary policies and the high interest rates of the Brazilian economy (Paulani; Pato, 2005). These measures were later complemented with Law No.



9249 of December 26, 1995, in which profits, dividends, and the financial investments of individuals were tax exempt; with the legal entity being taxed at 15% (Dowbor, 2018).

Another decisive step came with the Real Plan. In addition to its stabilizing function by combating high inflation, the plan led by Fernando Henrique Cardoso (FHC) – then Minister of Finance – contributed in two decisive ways to the opening of the BFS. First, it guaranteed the functioning of Brazil as a platform for financial valorization, at a time when high inflation made it impossible to attract short-term foreign capital. Second, it created the basis for several measures that would be adopted by the FHC government, such as the economic opening, privatizations, maintenance of the overvaluation of the Real, and the increase in the real interest rate – all justified by the need to preserve the stability achieved by the Real Plan (Paulani; Pato, 2005).

However, the "official" opening of the BFS came in 1995. Through the Explanatory Memorandum nº 311, the government declared that it was in the national interest to expand the foreign participation in the BFS. Still aiming to increase direct investment, the National Monetary Council (CMN) ended the requirement that the minimum capital of a foreign bank should be double that required of a national bank; thus, equating the rules for national and foreign banks. (Penido, 2011). In the same year the participation of foreign investors in BOVESPA reached 29.4% of the 233.3 million dollars traded – a considerable increase compared with 6% of the 28.4 million dollars traded in 1991 – maintaining the virtuous growth of previous years. Foreign participation in the Brazilian banking system also intensified. In 1994 11% of the banking system's assets belonged to foreign institutions, rising to 24.8% in June 1998 (Penido; Prates, 1998).

This increase in foreign participation in the Brazilian banking system is largely due to the PROER and PROES programs. These programs occurred in a context of severe banking crisis, in a sector that had to readjust with the end of hyperinflation provided by the Real Plan. Between June 1994 and August 1996 alone, 11 banks, 100 credit cooperatives, 21 brokerage houses, 74 distributors and 213 bank branches were closed. Interventions at Banespa and Banerj, in December 1994, were emblematic. In this context of crisis, 40 financial institutions were liquidated or intervened in. The National Treasury was responsible for financing

most of the troubled public and private banks, among them the Banco do Brasil itself, the Central Bank, and the Caixa Econômica Federal, showing a national financial system where troubled institutions represented almost 2/3 of total assets (Yoshino, 1998).

The Provisional Measure (MP) 1179 of November 3, 1995, established the Program of Stimulus to the Restructuring and Strengthening of the National Financial System (PROER) was launched to facilitate the acquisition of insolvent banks. This was intended to preserve the normality of the financial system and avoid a systemic crisis, the fear of which had grown after the interventions at Banco Econômico and the Banco Nacional. Through the creation of credit lines, fiscal incentives, tax benefits and temporary exemption from compliance with certain banking rules, PROER promoted a restructuring of the BFS. Under the aegis of the program there were 62 changes in shareholder control, 33 mergers and 44 bank liquidations. Notable among these was the sale of Bamerindus to HSBC (Corazza, Oliveira, 2007).

In turn, MP no. 1514 of 08/16/1996 established the Program of Incentives to the Reduction of the State Public Sector (PROES), aimed at privatizing the state banks. The justification for this program was, besides reducing the presence of these banks, to eliminate the financing of state government budget deficits and to contain monetary emissions that could fuel inflation. Between 1997 and 2005, 12 state banks were privatized, 9 of which were acquired by private banks with national capital. Bradesco was the main beneficiary, acquiring 5 state banks, while Itaú acquired 4 – including Banerj and Bemge. The remaining banks were acquired by foreign capital institutions. Santander acquired Banespa – the largest among the state banks - and ABN Amro bought the banks of Pernambuco and Paraíba to consolidate its presence in the Northeast (Corazza, Oliveira, 2007; Penido, 2011).

With the movements of the BACEN, the Real Plan, the PROES and PROER, are characterized what Penido and Prates (2001) defined as the two central axes of the Brazilian financial opening in the 1990s: the "[...] flexibilization of the entry of foreign investors in the Brazilian financial market and the adequacy of the domestic regulatory framework to the contemporary model of international financing, anchored in the issuance of securities (fixed income securities and shares)." (Penido; Prates, 2001, p. 85).

By the end of the 1990s, there were already some diagnoses of the effects

of the opening of the BFS. The first one refers specifically to the banking system. Corazza and Oliveira (2007) state that the privatization wave led to a process of banking concentration accompanied by greater capitalization arising from the new rules in the sector, "[...] which implied, among other things, new forms of financing, which resulted in increased profits for banks." (Corazza; Oliveira, 2007, p. 156). With this concentration, Bradesco, Itaú and Unibanco were consolidated by the year 2000 as the main national private banks. (Penido; Prates, 2001). It is worth noting that this process was also accompanied by a significant increase in the assets of these institutions, to the extent that in 1997, six Brazilian banks were already among the largest in Latin America. (Penido; Prates, 1998). It is also necessary to realize that it is at this moment of opening and reconfiguration of the BFS that the Brazilian financial elite consolidates itself as a major social and political actor, and figures such as Armínio Fraga gain prominence in the media and popular imagination – perceived by the large number of articles about Fraga in vehicles such as *Veja*, *Exame* and *Istoé*, that a simple Google search reveals.

The presence of foreign institutions in BFS was also consolidated with the opening of the 1990s. In 1994 there was only one foreign bank among the 10 largest operating in the country – Lloyds. By the end of 2000, six foreign banks were already among the 10 largest institutions: ABN Amro, Santander, HSBC, Bank of Boston, Citibank and Sudameris. However, the increase in the presence of foreign banks in the Brazilian Financial System did not have the expected effect. The expectations of reduced costs of credit and banking services, and a greater supply of long-term credit – which were supposed to occur as a result of greater expertise – did not occur. The new banks ended up adopting practices like those of national private banks and foreign banks already present in the BFS prior to liberalization. In practice, throughout the 1990s the BNDES continued to be the provider of long-term resources for the financing of productive investments (Penido; Prates, 2001; Penido, 2011).

In general, the opening of the Brazilian financial system in the 1990s did not bring the hoped-for dynamism. The liberalization of the economy and the financial market, as pillars of the neoliberal agenda, should have a positive impact on the growth of developing economies, in the sense that it would allow the absorption of external resources, as well as increase efficiency through new competition with foreign agents. However, argue Feijó, Lamônica and Lima

(2019), the general effect observed was a reduction in the political possibilities of the Brazilian State and an increase in financial fragility to external shocks, in addition to a worrying early deindustrialization (Feijo; Lamônica; Lima, 2019).

Saad-Filho and Morais (2002) point out that the main change in the Brazilian economy throughout the 1990s was the abandonment of industrialization by substituting imports in favor of an accumulation model based on the integration of the productive base and financial capital with the transnational circuits. This change was brought about largely by the Real Plan, which ended up functioning as a broad neo monetarist or neoliberal economic program aimed at repressing distributive conflicts in the country and reducing the State's capacities to deal with the social costs of its economic policies (Saad-Filho; Morais, 2002; Saad-Filho; Mollo, 2002).

Thus, the changes that occurred throughout the 1990s represented a change in the form of insertion of Brazil in the global financial market, in which inflationary gains – characteristic of the period of the 1980s – are replaced by high income from interest (Lavina; Araújo; Bruno, 2017). In the following two decades, this process intensifies to the point where Brazil can be characterized as a financialized economy.

#### **4. The BFS in the 21st century: financialization and concentration**

##### **4.1 Intensified financialization**

In the last two decades the Brazilian banking sector has consolidated through the increase in its concentration, expanding the presence of large retail banks, and increasing the participation of federal public banks. (Pinheiro; Savóia; Securato, 2015). From 2000 onwards, Brazil not only deepened its financial openness, but also consolidated itself as an emerging financialized economy (Penido; Prates, 2001). At the beginning of the 21st century, the BFS was also already integrated into the global financial system, through an extensive transnational banking network in which São Paulo had strong ties with New York and Tokyo, but which also included several other Brazilian cities. (Rossi; Taylor, 2005).

Although the process of financialization acquired its sharper contours in the 1990s and intensified in the first decades of the 21st century, it was during the

military regime that the foundations for the process were laid. Already in 1967, under the government of General Costa e Silva, whose finance minister was economist Delfim Netto, the Central Bank issued Resolution 63. In this resolution, Brazilian banks were authorized to raise funds in the international financial market in order to pass on such resources to domestic companies. Guerra *et al.* (2019), show us that this resolution originated two processes that unfolded in the following decades. First, the resolution served as the trigger for Brazil's exorbitant foreign debt. Second, it caused the interests of Brazilian financial groups to move closer to the interests of financial agents in the international market (Guerra *et al.*, 2019).

Lavina, Araújo, and Bruno (2017) see the 1970s and 1980s as the gestation period of the current Brazilian financialization. Inertial inflation arising from the fiscal and foreign debt crises of the 1980s enabled an unprecedented financial expansion and banking concentration until then. With a highly indebted state in foreign currency and unable to fight the devaluation of its currency, "[...] the banking-financial development in this period had as its main axis the rentier accumulation based on inflationary gains derived from the rolling over of public debt in the process that would become known as 'ciranda financeira' (overnight)." (Lavina; Araújo; Bruno, 2017, p. 10). In view of this, for the authors, the banking-financial sector begins precisely in this period to consolidate itself as hegemonic before the other national productive sectors, being able to guide the institutional transformations that characterized the economic liberalization of the 1990s (Lavina; Araújo; Bruno, 2017).

With the foundations laid and liberalization in the 1990s, finance in Brazil found fertile ground for a significant expansion at the beginning of the 21st century. In the first years of the new century, still under the FHC administration, the opening process initiated in the 1990s was consolidated by Armínio Fraga's presidency of the Central Bank, making the banking sector fully open to foreign investors. In summary, with the changes promoted, the "[...] investments made through the commercial exchange market are no longer subject to restrictions regarding the type of instrument used, the portfolio composition and the nature of the investor (individuals or legal entities)". (Penido; Prates, 2001, p. 85). Two resolutions are fundamental to the process. The first, Resolution nº 2689 of 26/01/2000 directly affected Foreign Portfolio Investment (FDI), allowing non-resident investors to have access to the same investments available to residents. In

addition, fixed income investments became subject to the same taxation applied to resident investors. The second, Resolution no. 2770 of 08/30/2000, eliminated a series of regulations - 237 in total - that limited the issue of fixed-income securities abroad, including BACEN's permission for any type of fund raising (Penido; Prates, 2001).

In the Lula government, against the market's initial scaremongering, the process of financialization in Brazil continues. As Paulani (2012) points out, additional measures have been taken to consolidate Brazil's insertion in financial accumulation circuits. These included the extension of the social security reform – initiated by FHC – to the civil service, reform of the bankruptcy law to prioritize financial creditors, and the adoption of more measures to increase the degree of financial openness. These measures were accompanied by macroeconomic policies - liquidity control, maintenance of high interest rates, and increase in the primary surplus – that guaranteed significant returns to financial market agents over the last two decades (Giambiagi *et al.*, 2011; Paulani, 2012; Teixeira; Pinto, 2012).

All these macroeconomic and regulatory measures, in general, contributed to the insertion of the Brazilian economy in a financial dynamic – which is not unique to Brazil – in which the financial system began to drain the productive system, instead of boosting it. In a scenario in which financial investments yield over 5%, while the world GDP grows at a rate of 1% to 2.5%, we face a global financial culture where investments are much more profitable than productive investment. This illuminates, at least in parts, the question of why, for example, Brazil's major financial institutions have broken profit records in recent years while the economy was sluggish (Dowbor, 2015; 2018).

This limiting financial dynamic, according to Dowbor (2015; 2018), can currently be perceived in five dimensions of the Brazilian economy. The first is foreign trade, about which Brazil would have little control over its current constraints. Just as the country "surfed" the commodities boom at the beginning of the 21st century, it was also a victim of the significant drop in their price; for example, a 21.14% reduction between April 2015 and April 2016. The fall in the price of primary products, such as soy and iron ore, negatively affects the country's trade balance, largely dependent on the export of these products. At this point the country finds itself adrift in the world market. However, the limiting character of

the current financial dynamics is revealed in the advance of financialization in the commodities market. Currently, at the international level, the prices of commodities are largely affected by financial activities. Large groups of commodity traders, more interested in the intermediation of products and in the consequent speculation around price oscillation, end up having a decisive impact on commodity prices. However, this dimension of the external market would not be the main axis in which financial dynamics would generate greater impact on the Brazilian economy. As Dowbor (2018) highlights, Brazilian exports represent, on average, 10% of GDP. Thus, the central axis of the economy is in the domestic market, where the impacts of financialization are more damaging, as can be seen in the following points (Dowbor, 2018).

The second dimension affected by financialization is internal demand, or the demand of Brazilian families. The general lines of argument here are that abusive interest rates end up amputating a large part of the Brazilian population's consumption capacity, while financial institutions feed a financial circle where credit, not consumption, is encouraged. According to Dowbor (2015, 2018), the problem already begins in the way interest rates are commonly presented in the country. Unlike most countries in the world, in Brazil interest rates are presented in their monthly form instead of annually. Thus, a monthly interest of 6.87% per month, for example, hides a rate of 122% per year. This form, which is very common in the credit plans of the financial arms of the country's major retail chains, reveals that, by practicing an exorbitant average annual rate - 88.83% in February 2018 and 73.92% in May 2020 - "[...] simply means that this type of commerce, instead of providing decent commercial services, has essentially become a bank, and profits by practicing loan sharking." (Dowbor, 2018, p. 192). In comparative terms, the European retail chain Midia@market charged an interest rate of 13.3 percent per year on its payday loans in 2018 (Dowbor, 2015, 2018; Anefac, 2020a).

A similar scenario is found in the interest rates charged by the major banks on their "financial products" for individuals – credit cards, overdrafts, loans, etc. In February 2018, the average annual interest rate was 318.5% for credit cards, 297.18% for overdrafts, 138.18% for personal loans taken out with financial institutions, and 64.22% for those made at banks. In May 2020, these average interest rates were 257.48% for credit cards, 131.1% for overdrafts, 108.87% for

loans made at financial institutions, and 47.13% for loans at banks. While in Europe in 2018, interest rates for similar products were between 1.5% and 3.5% per year, with overdrafts reaching around 6.5% per year (Dowbor, 2018; Anefac, 2020a).

These abusive interest rates end up locking in demand, as Dowbor (2018) shows: "We have in this case much of the purchasing capacity of new consumers drained away to financial intermediaries, sterilizing the dynamization of the economy on the demand side." (Dowbor, 2018, p. 198). In this way, consumers end up consuming half of what they theoretically could, putting the brakes on an important engine of the economy, household demand. The author also adds: "Families are spending much more, a result of the high level of employment and the increased purchasing power of the base of society, but interest rates sterilize the ability to boost the economy by the demand that these expenditures could represent." (Dowbor, 2015, p. 266). Taxes, often placed as the main villain of the economy, here lose their position to the detour of purchasing capacity to interest payments (Dowbor, 2015, 2018).

The third dimension, in which the financialization of the Brazilian economy can be perceived, is in business activity, or rather, in the blocking of it. This blockage occurs in three ways. The first is the result of the very locking of household demand caused by high interest rates on consumption. The reasoning is simple. With lower consumption, companies have less demand for their products, thus reducing the pace of production and consequently their investments. In this process employment is also affected. The second is the interest rates for companies that are practiced in the country. Just as for individuals, companies find absurd rates when looking for credit. In February 2018, the average annual interest rate for companies was 63.08%. In May 2020, this average rate was 43.58% per year. For working capital, the interest rates were 28.93% per year, 34.96% per year for trade bill discounting, and 146.83% per year for secured accounts, all rates for February 2018. In May 2020, the annual interest rates for working capital were 14.98%, 17.88% for trade bill discounting, and 116.05% for the secured account. A considerable reduction between 2018 and 2020, but still exorbitant if we consider that the average cost of credit for companies in the euro zone was around 2% to 3% per year in 2018. A third factor related to financialization still contributes to the blockage of production: the exuberant profitability offered by investments



in Treasury bonds, an alternative for entrepreneurs to make their capital yield without the need to face the efforts and risk inherent to investments in productive activities. (Dowbor, 2015, 2018; Anefac, 2020b).

The fourth dimension in which we can perceive the impacts of financialization is precisely the financing of the Brazilian public debt. While in most countries of the world the public debt bonds pay around 0.5% to 1% per year, in Brazil in 2016 the bonds yielded 13% per year (measured through the Selic interest rate). Since then, the yield on the bonds has fallen sharply, reaching a Selic interest rate of 3% in 2020. However, largely due to the economic crisis of the last few years, inflation has also been reducing, which still maintains considerable gains for those with enough capital to invest in government bonds. In any case, the rule is that Brazil in the last three decades has rewarded with exceptional yields - as high as 46% during the FHC government - the "investors", generating a proliferation of rent-seekers in the country with the opening of investments in Treasury bonds to any saver. Whether the vertiginous reduction in the Selic rate is a structural change or just a conjunctural one, it is still not possible to say, but the fact that Constitutional Amendment 95, which limited public spending for the next 20 years, has not limited spending on public debt, gives us some indication. What is certain is that until today astronomical sums of national wealth have been drained from productive activities. In 2015, for example, spending on public debt - the famous primary surplus - reached 8.5% of GDP, an amount around 500 billion reais. This debt service ends up having a harmful effect, to the extent that these considerable volumes of national wealth are transferred to financial institutions and a small group of financial agents, thus halting public investment in a country with clear bottlenecks in its infrastructure and with one of the most unequal societies on the planet (Dowbor, 2015; 2018).

Faced with a scenario of exorbitant interest rates and yields above the world average, we are inserted in a process in which the Brazilian financial system ends up, according to Dowbor (2015; 2018) and Paulani (2017), hindering - or even halting - the country's own development. Dowbor (2018) estimates that about 15% of the national GDP is annually displaced for the remuneration of financial intermediaries - for the payment of the debt of individuals and corporations - that is, to "honor" the public debt. In this scenario, in 2019 - a year in which Brazilian GDP grew 1.1% - Itaú had the highest profit in the history of Brazilian banks, a

high of 20.6% in 2019 with respect to 2018. Bradesco, meanwhile, profited 18.32% more than in 2018; Santander 16.6% and Banco do Brasil 43%. The net profit of these four institutions combined was more than 81 billion reais in 2019. It is interesting to note, that in the same news where the earnings of these banks are demonstrated, it is also revealed, for example, that Banco do Brasil's credit portfolio retreated 2.6% compared to 2018 (G1, 2020a; 2020b).

To complete this distressing scenario, the financialization of the global economy still directly affects the Brazilian fiscal dimension. Not being isolated from the international financial system, many companies and individuals in Brazil use the structure of tax havens, often used for tax evasion and money laundering of illicit origin. (Fossen, 2012). According to Dowbor (2018), in 2016 tax evasion in Brazil was estimated at 9.1% of GDP, about 570 billion reais. We have arrived at a scenario in which, in addition to the fact that a large part of the profits from the financial sector are not invested in the country's economy, part of these profits does not even pay taxes. With tax evasion, coupled with "[...] the low-income tax rate, the exemption of tax on profits and dividends, the non-existence of a wealth tax, and the fact that indirect taxes account for 56% of tax collection [...]" (Dowbor, 2018, p. 218), we are facing a seriously distorted economic scenario.

In summary, according to Dowbor (2015), we can consider Brazil as part of an international financial system deformed by the growing accumulation of economic and political power of financial intermediaries. Consequently, the Brazilian financial system also presents a structural deformation, that is, "[...] global financialization, with its various forms of organization according to countries and legislations, has acquired here different ways of locking the economy, national dimension of a deformation today planetary (Dowbor, 2015: 270).

Given such a scenario of financialization, some authors (Paulani: Pato, 2005; Paulani, 2009; 2012; Bruno *et al.*, 2011) mobilize additional arguments to conclude that, currently, Brazil can be understood as an emerging financial power. The first is the significant drop in Gross Fixed Capital Formation as a proportion of GDP (GFCF/GDP) starting in the 1980s. The GFCF is an indicator of the country's productive capacity, computing the total value of gross investments in fixed capital – machinery and equipment, structures and buildings, livestock and permanent crops – made by public and private companies over the course of a year.

This indicator, which in the average of the 1980s was around 18.55%, fell to 15.05% in the average of the 1990s and reached 14.07% in the period 2000-2004 (Paulani; Pato, 2005) – remaining at a similar level until the end of the first decade of the 21st century (Paulani, 2012). In other words, Brazil's productive capacity retreated, which in the diagnosis of Paulani and Pato (2005) compromised the country's ability to grow, reducing its per capita GDP.

This productive decline of the Brazilian economy was accompanied by another factor: the increase in the remittance of income abroad compared to the increase in GDP and GDP per capita itself. In the period from 1975 to 2004, Paulani and Pato clarify that,

the country's annual expenditure on factor services (profits and dividends from direct investments and interest on intercompany loans; profits, dividends and interest on portfolio investments; and interest on conventional loans) grew by 1,085% (from \$2 billion to \$23.7 billion), while over the same period the GDP grew by 129% and per capita GDP by 42%. Thus, while the remittance of income abroad grew in this period 10.9 times, the GDP grew 1.3 times and the per capita GDP only 0.4 times (Paulani; Pato, 2005, p. 4).

It is worth noting that in the 1980s a significant portion of these remittances abroad were directly related to the debt crisis. In the 1990s, it is the assets derived from privatizations that come to the fore. However, already in the beginning of the 21st century, most of the remittances are composed of income from portfolio investments – Brazilian public debt securities quoted on the international market. In this way, Brazil ended up transforming itself from an importer of liquid capital to an exporter (Paulani; Pato, 2005).

Further data are presented by Bruno *et al.* (2011) that corroborate Brazilian financialization. According to the authors, the process has developed in such a way that public finances have become hostage to rentier accumulation. This entrapment occurs, the authors point out, by the importance that public debt acquires for the maintenance of gains, largely perceptible by the positive correlation between public debt and the real Selic interest rate – demonstrated through the elaboration of econometric models that reveals "[...] that investment decisions are 'commanded', primarily, by the norm of real profitability offered by financial markets." (Bruno *et al.*, 2011, p. 736). The consequences of such a process are

cruel, to the extent that, "[...] the autonomy of economic policy is significantly reduced, and its format and management are permanently monitored by the expectations and rationality inherent to the financial revaluation of capital." (Bruno *et al.*, 2011, p. 746). In summary, for the authors, the financial macro-structure ended up imprisoning Brazilian public finances. In this scenario, any economic development strategy faces structural limits imposed by the dynamics of financialization, which has required a considerable increase in the tax burden to pay the public debt, resources that, as already mentioned, could be applied in other areas (Bruno *et al.*, 2011; Dowbor, 2018).

It is interesting to note that in the last three decades, while the country's productive capacity declined and the public debt was advancing, bank profits reached unprecedented levels, as seen earlier. The increase in profits of financial institutions – profits derived basically from income from public debt securities (Teixeira; Pinto, 2012) – was accompanied by a rapid growth in the patrimony of business groups operating in the country's financial sector. While the Brazilian GDP increased by 28% between 2003 and 2008, the patrimony of financial groups increased by 71.7% (Paulani, 2012). As we will see below, the assets of these institutions also increased at a much higher rate than the increase in the national GDP.

In this context, Paulani (2012) is categorical: "[...] the Brazilian economy is now a financialized economy, with an accelerated process of capital centralization and completely integrated into the dominant rentier capitalism." (Paulani, 2012, p. 97). The author continues: whether for the benefit of rentiers residing in Brazil or abroad, "[...] the Brazilian economy today stands on the world stage as an emerging platform for financial valorization, ensuring unparalleled gains in a world where real interest rates are zero or negative." (Paulani, 2012, p. 98).

#### **4.2 A highly concentrated financial system**

In the last two decades it is possible to see an increasing concentration in the BFS's assets. Corazza and Oliveira already observed this process in 2004, when 60% of total assets were controlled by the 5 largest institutions: Banco do Brasil, Bradesco, Caixa, Itaú and Unibanco. When considering the 10 largest institutions active in the BFS that year, the concentration reached 79.3% of total assets in the

hands of these few institutions (Corazza; Oliveira, 2007). With the merger of Itaú and Unibanco in 2008, the position of largest Brazilian private bank is taken from Bradesco, which further accentuates the concentration of SFB in the first decade of the 21st century.

The data provided by BACEN (Table 1); it is possible to have a broader perspective on this concentration that marks the BFS (Graph 1). Taking as a source the institutions listed by BACEN which are active in the BFS and their respective assets in millions of reais, one can see that in 2001 the 10 largest institutions in the SFB concentrated 69.2% of the 1.08 billion in total assets of the system. The five largest institutions in terms of assets concentrated 51%. In 2010 the 10 largest institutions concentrated 84.7% of the 4.3 billion in total assets. If we consider only the 5 largest, this degree of concentration reaches 67.6% of assets. In 2019, the 10 largest concentrated 80.5% of 9.4 billion in total assets, while the 5 largest concentrated 66.9%. Thus, it is possible to observe a process of intensification of concentration of the BFS in the last two decades, higher even than that noted by Corazza and Oliveira (2007) in 2004. From 2001 to 2019, as can be seen in Graph 1, the concentration of assets in the control of the 10 largest BFS institutions increased from 69.2% to 80.5%. The control of the 5 largest institutions went from 51% to 66.9%.

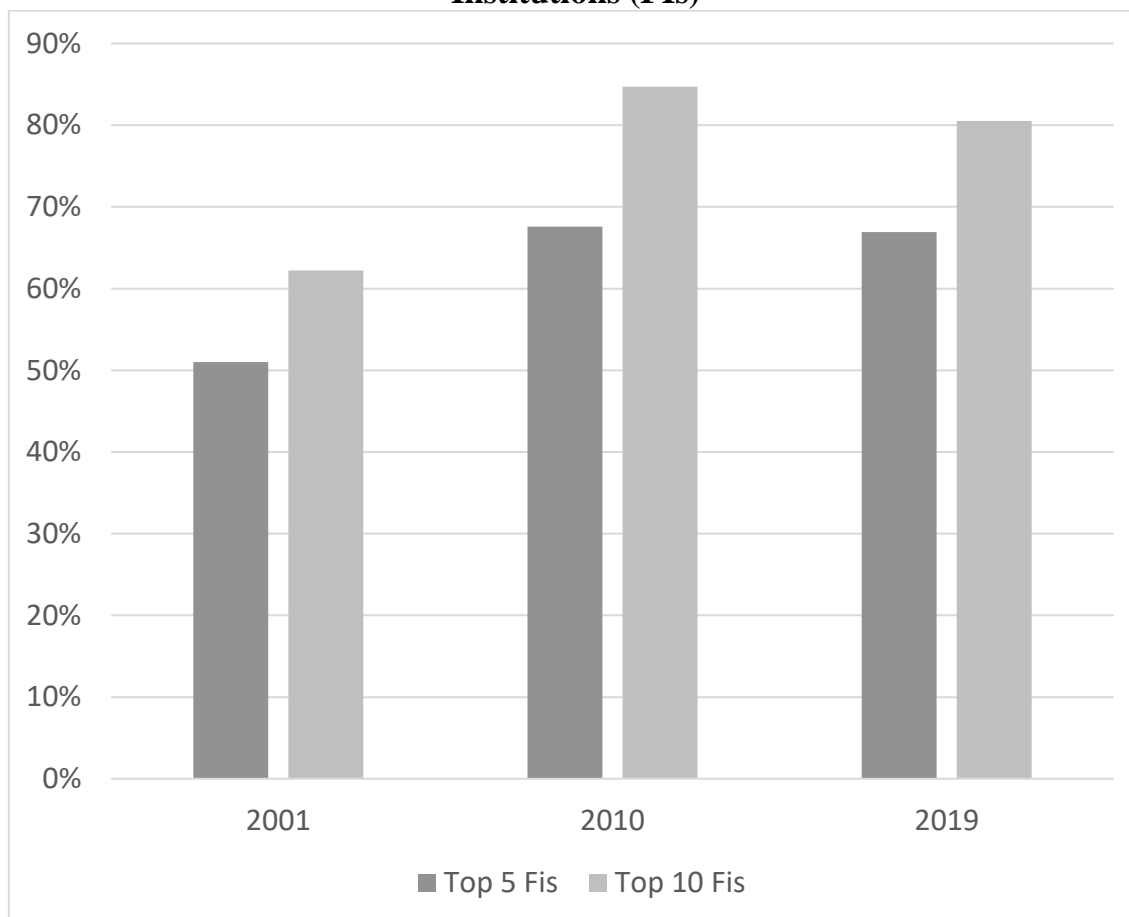
**Table 1 - Top 10 BFS institutions by assets in millions of reais.**

2001		2010		2019	
INSTITUTION	ASSET S	INSTITUTIO N	ASSET S	INSTITUTIO N	ASSET S
Banco do Brasil	165,1	Banco do Brasil	728,6	Itaú	1.566,9
BNDES	114,6	Itaú	720,3	Banco do Brasil	1.473,2
Caixa Econômica Federal	101,3	Bradesco	562,6	Caixa Econômica Federal	1.293,4
Bradesco	95,0	BNDES	520,8	Bradesco	1.145,3
Itaú	78,6	Caixa Econômica Federal	401,4	Santander	850,3
Santander Banespa	57,4	Santander	376,0	BNDES	739,7
Unibanco	51,7	HSBC	124,6	BTG pactual	184,9
ABN Amro	32,1	Votorantim	110,7	Safra	172,8

Safra	30,3	Safra	76,2	Votorantim	96,8
BankBoston	25,7	Citibank	54,4	Cielo S.A.	93,5

Source: created by the author with data provided by BACEN.

**Graph 1 – Concentration, in percentage, of assets by the main Financial Institutions (FIs)**

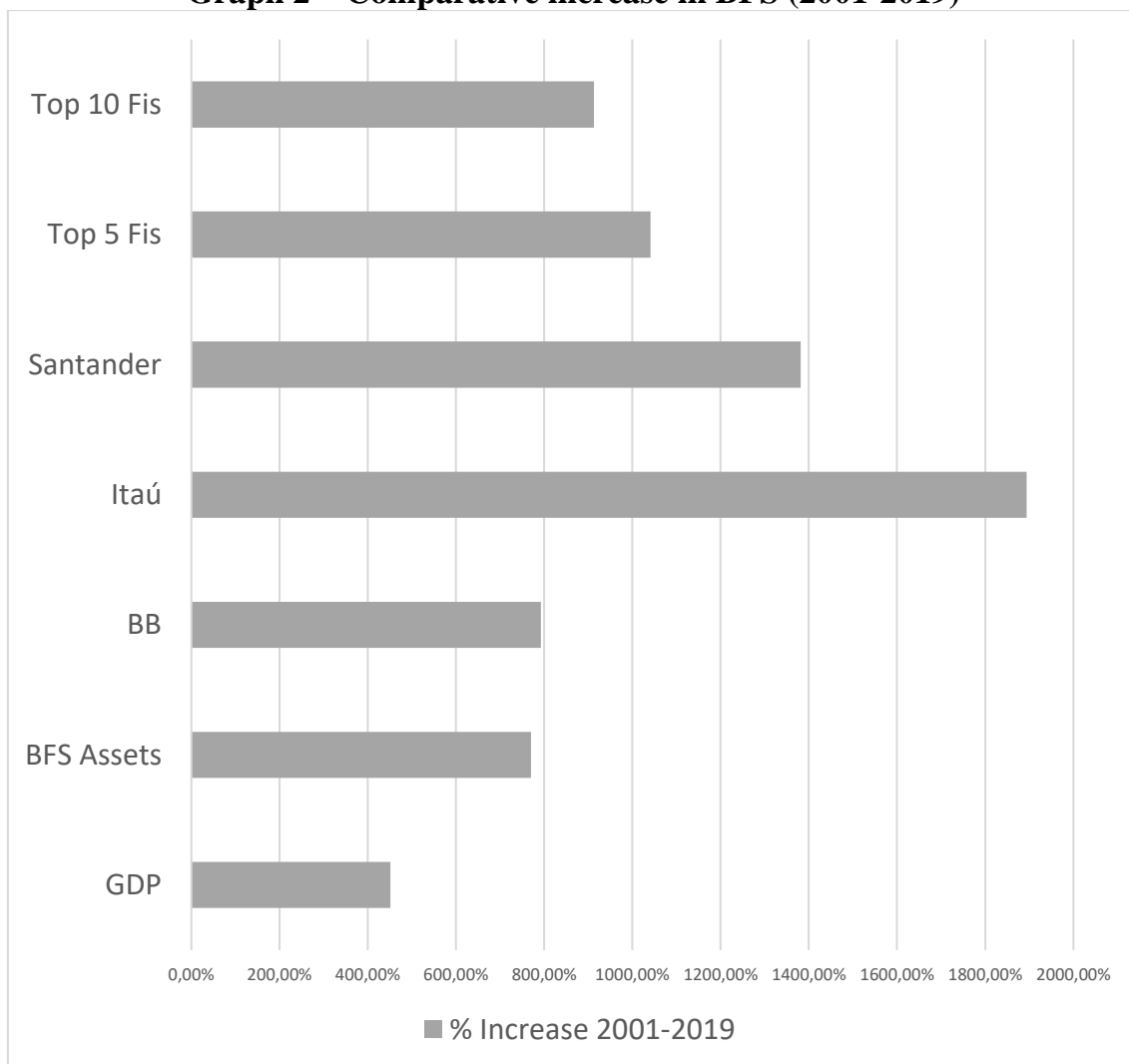


Source: created by the author with data provided by BACEN.

Even the total volume of assets in these few institutions has increased sharply over the last two decades, as can be seen in Graph 2. Between 2001 and 2019, the total volume of assets under the control of the 10 largest BFS institutions increased by 912.6%. The volume among the 5 largest, on the other hand, increased by 1040.8%. If we look at SFB institutions in isolation, we also see an impressive growth in the assets of these institutions over the 21st century. Banco do Brasil, for example, the largest public financial institution in Brazil, increased its assets by 792.3% between 2001 and 2019. In turn, Itaú, the largest national private bank, increased its assets by 1893.5% over the same period. Santander, meanwhile, the largest foreign private equity bank in BFS, increased its assets by 1381.3%. In

terms of comparison, Brazil's nominal GDP between 2001 and 2019 grew by 451.1%. BFS's total assets, meanwhile, increased by 770.2% between 2001 and 2019.

**Graph 2 – Comparative increase in BFS (2001-2019)**



Source: created by the author with data provided by BACEN.

Despite the high number of institutions listed by BACEN - 1861 in 2001, 1786 in 2010 and 1309 in 2019 – the assets are concentrated in just a few institutions. The concentration of assets in a few institutions is a global trend (Minella, 2003), however, this does not detract from the fact that great economic power is concentrated in a few financial institutions operating in the country. It happens that, many times, this economic power ends up manifesting itself in political power through voluminous donations to electoral campaigns. In the 1994

and 1998 elections for Congress and Presidency, for example, there was a large volume of donations from private financial institutions. In FHC's 1994 and 1998 campaigns, financial institutions were his main donors. In 1998, the largest and third largest donors were, respectively, Itaú and ABN Amro. Of the total declared in the 1994 elections, 23% came from the financial sector. In 1998 this participation reached 26.73%. In general, among the largest private banks active in Brazil, at least 5 participated actively in campaign financing in 1994, 1998 and 2002: Bradesco, Itaú, Unibanco, Santander, Votorantim and ABN Amro (Minella, 1996; 2003; 2007; Miranda, 2003). More recently, among the 10 companies that donated the most to the 2014 election campaigns are the two largest private financial institutions in the country: Bradesco and Itaú. The former donated more than R\$ 20 million, helping to elect 113 deputies from 16 different parties. Itaú donated "only" R\$ 6.5 million, helping to elect 84 deputies from 16 different parties. There were also 42 deputies funded by the two institutions (Maia, Bulgarelli e Toledo, 2014).

In addition to this significant concentration, the BFS is also characterized by a predominance of public and private institutions with majority national capital. In 2019, among the top 10 institutions in the BFS, 3 were public institutions, 6 private institutions with majority national capital, and only 1 – Santander – was a foreign private institution. This profile and the institutions that make it up have varied little over the past two decades. The three public giants - Banco do Brasil, Caixa and BNDES - have always been among the main institutions in the system. Banco do Brasil was even the leading institution in assets until 2018, when it was taken over by Itaú. This institution, which was already one of the largest in the BFS, became a true financial giant after its merger with Unibanco in 2008, reaching the level of national private institution with the largest volume of assets already in 2009. In addition to Itaú, Bradesco and Votorantim are two other private institutions with majority national capital that have always been among the main ones in the BFS. Bradesco is one of the four institutions that have currently broken the 1 billion reais mark in assets. Among the foreign institutions, the highlight is Banco Santander, which after the purchase of Banespa in 2000, consolidated itself as one of the main institutions in the BFS. If we consider the top 100 financial institutions by assets listed by BACEN in 2019, this profile does not change significantly. Of these, 12% are public institutions, 52% are private institutions



with mostly domestic capital, and 36% are foreign institutions.

Considering these discussions and information, we have the following panorama: a Brazilian economy inserted in a context of financialization, which is perceived through the impacts on domestic demand, business activity, public debt, and the Brazilian fiscal dimension. In this context, Brazil is already moving towards being an emerging financial power, in which its productive capacity is shrinking while its public debt and remittances of income abroad are increasing. In this scenario a small number of financial institutions have consolidated themselves as the main players in an increasingly concentrated national financial system, where the main institutions break profit records, substantially increase their patrimony, and accumulate ever larger sums of assets. This could be taken as a summary of the current general structure of the BFS.

## 5. Final Considerations

In this paper we have aimed to build a brief history of the Brazilian Financial System. Starting in the 19th century and the attempts to stabilize the system around the Banco do Brasil, passing through the first liberalizing measures under the military regime and the explosive growth of the foreign debt, and then giving a more detailed attention to the 1990s, a paradigmatic moment of the liberalization of the BFS. This history revealed two points: first, the economic opening ended up generating a highly concentrated financial system, with a large part of its assets in the hands of a few, mostly national, institutions. Second, especially since the 2000s, there is an intensification of the financialization process of the Brazilian economy, which ended up, in the view of authors such as Dowbor (2018), draining the Brazilian productive system instead of boosting it.

This dynamic, evident in the BFS's history, have not receded during the Covid-19 pandemic. Despite an initial reduction in the Selic rate in 2020, by 2022 it had already been revised many times, returning to the level of 12.75% per year. The interest rates charged by financial institutions continue at frightening levels; on average 115,81% per year for individuals and 55,37% per year for companies in April 2022 (Anefac, 2022a; 2022b). In addition, the project of independence for the Central Bank came out of the drawer after three decades and was approved, guaranteeing for the institution, at least on paper, independence to establish certain monetary policies – independence validated by the Brazilian Supreme Court.

Everything indicates that the dynamics of financialization and concentration of the BFS will continue to advance in the country, at least in the short and medium term.

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