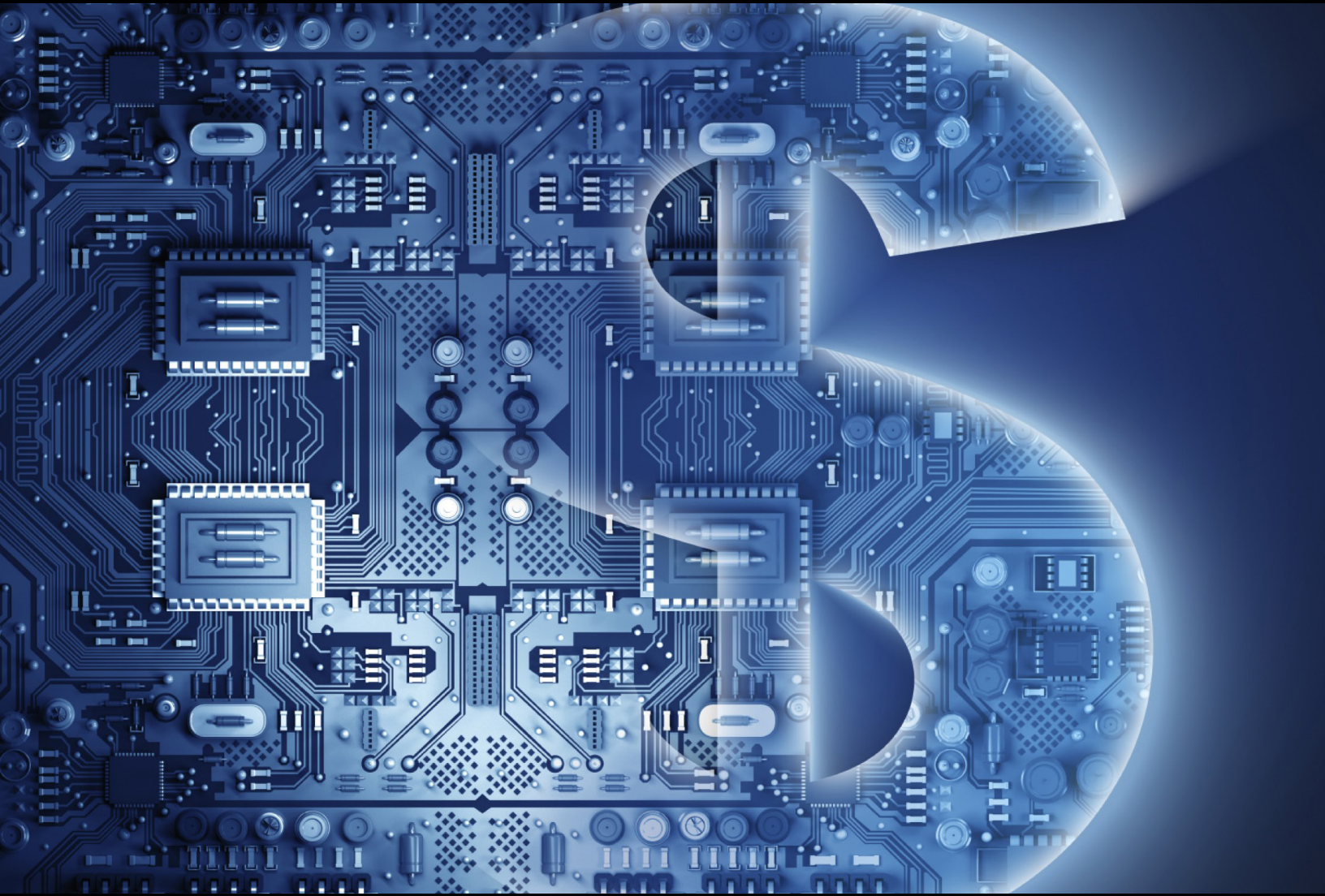


A REPORT FROM SOVEREIGNMAN.COM



THE FUTURE OF FINANCE

FINANCIAL TECHNOLOGY IS REVOLUTIONIZING
HOW THE WORLD DOES MONEY

**A
BLACK
PAPER**



It's the 9th century C.E.

A monk sits in a scriptorium, in silence, painstakingly pricking the margins of parchment leaf with a compass. Using his goose quill, he will soon slowly connect the points to draw a margin.

The monk is one of the few people in the Western world allowed to do something rare and amazing — make a book. For days and weeks and months, he copies text from an older Bible. In Latin. Withallofthewordsrunningtogether, as is the custom of the time.

Then he — or another scribe — illuminates it in gold.

The painstaking, manual process takes months... all for one book.



In the end, a priest or other powerful figure will bestow the book upon a chosen, wealthy, powerful recipient. For centuries, circulation has been — and will remain — tightly controlled.

That is, until Johannes Gutenberg, a skilled metalworker and engraver, enters the scene. He sees a business opportunity and perfects techniques long in use in the East. By 1456, he is creating hundreds of Bibles with his moveable type printing press.

Gutenberg changed history. I don't say that lightly.

Although he died poor, without realizing the immensity of his contribution to humanity, his was one of the truly revolutionary technologies that come along once every few centuries... fundamentally changing the course of human civilization.

The invention of the wheel, the Agricultural Revolution, the Industrial Revolution... all were game changers.

But it's Gutenberg's printing press that offer parallels to what we will discuss today.



*3D Model of Gutenberg's
Printing Press*

For centuries, **a select few in a highly centralized system were able to exercise tremendous power over the rest of the population.**

The elite decided what was produced and distributed. The elite influenced how books were read and interpreted. The elite chose who received what information.

Gutenberg changed all of that... forever.

In Europe, the number of books produced went from a few thousand handwritten copies per year to millions of printed books over only a few decades.

All across Europe, every big university got its own printing press. The stranglehold on the dissemination of information — a key component of power — was forever broken.

In 1517, when Martin Luther first nailed his *95 Theses* to the castle door at Wittenberg, he was able to have copies made for others wanting a Protestant Reformation.

The ideas of Rousseau, Locke, and the American Founding Fathers all were widely distributed. Because of access to the written word, people became more free.

Now fast forward to the present day.

The digital age has further disseminated information — at the lowest cost in history.

But there is another centralized, power-based industry— invented even earlier than the printing press—that is stubbornly trying to remain immune to major change.

More than 500 years after Gutenberg unleashed his printing press on the world, a new revolution — one that, again, will empower the masses against the elite —is occurring. This time in the world of finance.

And it is new technology, again, that is fueling the change.

Status Quo: Institutional Levels of Centralization

The concepts of lending and credit have been known to man since ancient times. Some 4,000 years ago in ancient Babylonia and Assyria, lenders made their first loans to farmers to buy grain, and to traders to buy goods.

Much later in ancient Greece, lenders also started accepting deposits... and even converted money to facilitate trade between different currencies.

Back then, such actions were revolutionary.

An individual no longer had to keep all his gold at home. The merchant in Athens knew he could exchange his silver drachmas to the currencies of his trading partners.

Imagine the possibilities that this exchange system alone opened up...

The system kept evolving.

Banking as we know it today emerged more than 600 years ago when prominent families such as the Bardi, Peruzzis, and later the Medicis, opened “bancos” in prosperous Italian nation-states such as Florence, Genoa, and Venice.

(Fun fact for your next cocktail party: the word “banco” — or “bank” — translates as “bench” in Italian, as financial transactions typically were conducted on benches in marketplaces. The name stuck.)

These early banks took gold and silver for secure storage, then charged a small fee for doing so. Just like any other secure storage today.

The banks then typically issued something called a “bank note,” and the person holding the note could claim the gold back.

Eventually, these bank notes started changing hands in lieu of physical gold and silver... becoming the currency in circulation.



Bankers in Medieval Italy

Banks also were involved in lending, which fueled commerce. They loaned money to merchants who traded all over the world, and they charged a percentage as a reward for the risk taken. If banks made too many bad lending decisions, they went under.

Back then, good lending decisions were an imperative. Reputation was everything.

And reputation wasn't the only thing on the line: the punishment for not being able to repay depositors' gold even included, in some cases, beheading.

THE BANKING SYSTEM TODAY IS COMPLETELY OUTDATED

Today, as we witnessed in the aftermath of the 2008 debacle, banks make arrogant, risky decisions with our money... and then, when they lose big, they receive little more than a slap on the wrist... followed by a taxpayer-funded rescue.

Other than that, the banking system today generally is not that different from what the Italians invented more than six centuries ago.

The major difference is that instead of using gold and silver, banks use fiat money — currency that a government has declared to be legal tender, but that is not backed by a physical commodity. Not only is this fiat money not tied to gold or silver or anything real... but it's mostly digital.

Still, the systems, processes, and intermediaries are largely as they were before—and heavily centralized.

Big international banks have become giant agglomerates, **so vast and complicated that no one can ever tell anymore what they actually have on their balance sheets.**

Most banks today hold hardly any of their customers' deposits in reserves.

Almost all of it is being loaned out or invested in toxic derivative instruments.

If a bank's activity proves to be too risky and they go under, again, not only is no one beheaded or even shamed... but governments — read “*taxpayers*” — bail them out.

In exchange, the politicians who help them eventually retire to cushy bank “consulting” positions.

As a taxpayer, not only are you on the hook for their arrogant stupidity... but with negative interest rates now spilling over to retail customers, keeping money in a bank means that **you're actually paying the bank for the privilege of them making those ridiculous loans with YOUR money.**

The situation is perverse.

Banking is also archaic and largely redundant.

Hundreds of years ago it might have made perfect sense for a bank to be involved in every possible financial transaction occurring between two individuals.

But in the age of the Internet and advanced technology, a third-party nanny isn't necessary.

Think about it—when you send a wire transfer of \$5,000 from one bank to another, that's simply a ledger modification on both banks' balance sheets.

And it should be instantaneous. Just like sending an email.

No one is physically hauling a bag of money from one bank to another across the country or continent.

Still, this simple process takes up to 24 hours for domestic wire transfers... and costs a minimum of \$25.

Not only that, but as my sister discovered the other day, you'll likely get a call *demanding an explanation of the transaction*.

As if it is the bank's business that you're helping an elderly, computer-illiterate relative unload an heirloom through an online sale.

Then there are international wire transfers, which take 3-5 business days to clear and are much more expensive. Some banks in Europe even have the audacity to charge a percentage of the amount transferred.

(In all fairness, in some countries, such as Chile, domestic wire transfers are instant and absolutely free.)

There is no need for a bank to be in the middle of every possible financial transaction.

But banks do their best to resist any change.

PLUS, THE BANKS ARE IN BED WITH GOVERNMENTS AND SERVE THEM MORE THAN THEY SERVE YOU

Moreover, all banks today are unpaid spies of their governments.

Note, again, the phone calls — not one, but *two* - that my sister received from her longtime bank last week. **They told her they would not complete her wire transaction without a detailed explanation of why the rather paltry amount was being transferred.** We're talking about a couple thousand dollars. Within the United States.

US banks and other financial institutions submit more than 50,000 Suspicious Activity Reports (SARs) EVERY SINGLE DAY. The financial system has become completely Orwellian.

Just like law enforcement agencies — who by and large have sadly deviated from their original purpose of serving and protecting— banks simply no longer exist to be responsible custodians of their customers' money.

They make horrible bets with your hard-earned savings and maintain precariously illiquid balance sheets. Then they use clever accounting tricks to mask their true financial condition, destabilizing the world's financial system along the way.

They're supported by undercapitalized deposit insurance funds and by insolvent governments.



Obama shaking hands with Jamie Dimon

They're constantly being fined for exchange rate fixing and other market manipulation.

They treat you like a criminal if you try to withdraw too much of your own money.

They'll freeze you out of your own funds in a heartbeat if they wish to, or if the government tells them to do so.

They routinely report you to government agencies.

And your reward for all this trouble?

In the Land of the Free, it's a whopping 0.1% interest rate.

In Japan and Denmark, it's actually a *negative* rate.

Taken together, does it make sense to keep 100% of your life savings tied up in such an outdated and rigged system?

I think not.

Fortunately for all of us, technology is creating better, cheaper, faster, and safer alternatives.

How technology has changed industries – next up: Finance

Just as the printing press broke open the world of knowledge, today's technology is decentralizing the world of finance... whether the powers that be like it or not.

I've repeatedly said that banking as we know it will not exist in 10 years.



In fact, most of the banks who will fail to adapt will have to close their doors, going the way of Blockbuster video rentals (remember those?).

And the main drivers behind the change are two recent and equally important developments—the **blockchain technology** and **Peer-to-Peer (P2P) platforms**, both of which we'll detail in a bit.

First, let's go over some readily-available alternatives you can use to increase your financial freedom and control today.

Traditional alternatives for storing wealth

There are several ways to move your savings out of the banking system altogether.

But before I get into that, let me repeat the three-part strategy we recommend for protecting yourself from financial shocks, discussed previously in the pages of *Sovereign Man*:

Confidential:

1. Hold physical cash in lower denominations.
2. Own physical gold and silver.
3. Have at least a portion of your savings in a safe bank in a stable jurisdiction overseas.

The first two solutions in this strategy are also alternatives for storing your wealth outside of the banking system.

The most straightforward move is to withdraw and keep physical cash in your possession (perhaps in a home safe). We recommend storing enough cash to cover a few months' worth of expenses.

In case of a financial shock and some form of capital controls, \$10,000 in your home safe may prove much more valuable than \$500,000 in your frozen bank account.

The people of Cyprus learned this the hard way in 2013.

For your physical cash holdings, we recommend using lower denomination banknotes. Avoid 100s for dollars, or 200 notes for euros. In an ongoing and escalating war on cash, higher denomination banknotes will attract unneeded attention.

Then, of course, there is the most traditional way to avoid the banking system and fiat currency at the same time: storing gold and silver.

We recommend that you keep a portion of it where you can easily access it. But the majority of your precious metals should be stored overseas, in a safe, in a stable jurisdiction, where your government or overly zealous creditors won't be able to expropriate it easily.

We previously recommended secure storage facilities overseas such as [Das Safe](#), located in Vienna, Austria; [New Zealand Vault](#), located in both Auckland and Wellington, New Zealand; and [The Safe House](#) in Singapore.

Alternatives for payment processing

If you ever tried opening a merchant account with a bank to process credit card payments, you know how tedious this process can be... and usually is.

Until recently, your only choice was to follow that path and lose days and weeks of your life that you'll never get back.

But now you can completely circumvent traditional banks for payment processing.

For several years, PayPal has been the go-to platform in this area. It processed around \$300 billion in transactions for its clients in 2015.

Unfortunately, however, PayPal has become to the payment processing industry what banks have become to the financial industry as a whole.

PayPal is now too big... and its customers' needs have become secondary priority.

The market was in need of a better and more convenient solution, and that is when [Stripe](#) stepped in.

Stripe doesn't require setting up a merchant account. Your online store can start processing credit card sales right away. To set it up, you can choose a simple checkout system: just copy and paste into your online store.

And... it even supports Bitcoin transactions. (More on Bitcoin in a bit.)

Alternatives for money transfer and currency exchange

Although **PayPal** is imperfect, it was still one of the first companies to tackle the banks' monopoly over money and financial services.

It was one of the pioneers of e-commerce, especially popularized through its link to eBay.

And although PayPal is probably too big for large volumes of payment processing, it's great for transferring money within one country. The service is free and fast.

It gets much more expensive, though, with cross border/cross currency transactions.

For the latter, consider using [Transferwise](#), which has transferred more than a billion dollars in its short history.

The business model is ingeniously simple – they match up transfers going in one direction with those going in the opposite.

Therefore, the money you send overseas never actually leaves the country—it's rerouted to someone who is being sent a similar amount by someone from overseas. And your foreign recipient, meanwhile, receives his funds from someone sending money out of his own country.

XE, World Remit, Zoom, CurrencyFair, Azimo, Dwolla, and Revolut are just some of the many other examples of transfer services that can send funds cheaper and faster than banks.

The list keeps growing, which is why [Moneytis](#) was created: it helps you navigate the international transfer waters. Moneytis is the Expedia of international transfer services and will give you the comparison of all choices that currently exist, all over the world. Just choose the amount of money you wish to send and where you want your money to go FROM and TO.

We strongly recommend checking them out before you transfer one more dollar across the globe.

Say you want to send 1,000 USD from United States to China. Moneytis might give you the following options:

		You receive*	Receiver gets % more than traditional wire transfer	Transfer type	Transfer time
1	Transferwise	6,458 CNY	+4.8%	Bank transfer	4 Days
2	World Remit	6,418 CNY	+4.1%	Bank transfer	1 Day
3	MoneyGram	6,412 CNY	+4.1%	Bank transfer	Instant
4	Western Union	6,243 CNY	+1.3%	Cash pick-up	2 days
5	Traditional banks**	6,161 CNY	-	Bank transfer	6 days

(1 USD = 6.55 CNY as of this writing)

* Transfer fees are included in the final amount.

** Moneytis is using World Bank's database to estimate traditional banks' fees. Real result will differ from one bank to another.

You can save up to 5% in this example.

That's the good news. Transfers, however, can still take several days to complete.

This is because total transfer time depends on two things:

- 1) the time it takes to move money from your bank to a transfer company, and,
- 2) the time it takes the transfer company itself to perform a transaction. (That speed depends on the red tape of the two countries in question.)

Note that for some destinations, Moneytis also shows a transfer option using **blockchain technology** (crypto-currencies such as Bitcoin).

Because of China's rather strict currency control rules, Bitcoin has become one of the go-to options for wealthy Chinese wanting to get their money OUT of the country.

Truly, such option does not have any boundaries since Bitcoin exists only electronically and is accessible from anywhere with Internet connection. No government is controlling it (although they all dream about it).

More on the blockchain and Bitcoin below.

Modern alternatives for storing wealth – crypto-currencies

I've already mentioned several examples of services and businesses that are dealing in Bitcoins. Crypto-currencies, as you can see, are making their mark across the entire financial world.

If gold and silver are on one end of the spectrum of assets that are outside of the banking system, crypto-currencies are on the opposite end.



Bitcoin

The former is the oldest form of money there is. The latter is the newest.

The most famous example of crypto-currency, is, of course Bitcoin. (The complete list of existing crypto-currencies is rather long.)

At Sovereign Man, we don't like using the term "digital currency" when describing Bitcoin, because in essence, all major "paper" currencies are much more digital than physical these days.

For example, fewer than 10% of all dollars in circulation today exist in physical cash. More than 90% of them are created — and used — only digitally.

Euros, dollars, yen... all are little more than just digital records on cloud ledgers of central banks around the world. That makes most currencies nearly as digital as Bitcoin.

However, that's where the similarities end.

Fiat currencies are highly centralized and heavily controlled by central banks and governments.

Crypto-currencies are decentralized, and aren't controlled by any one entity.

Before we dive into the topic, let's talk more about the technology on which Bitcoin is based – the Blockchain.

THE BLOCKCHAIN

The blockchain is essentially a giant ledger keeping track of who owns how much Bitcoin... and tallying who has owned every single Bitcoin... since the dawn of bit.

As Bitcoins go from from one owner to another, the transfers are noted in new “blocks,” authenticated and published about every ten minutes.

This is the part that confuses people, because the coins are not digital files, but rather entries on that ledger. Which means that if you own a Bitcoin, what you really have is an entry in the blockchain.

Let's think about it in dollar terms.

Suppose every dollar created has a unique ID number. And every individual has a unique ID number (like a Social Security number).

You could think of the Blockchain as a giant accounting system that matches every unique dollar ID number with the Social Security number of its owner.

The system would show you the entire history of every unique dollar and how it has changed hands since being created, as well as the account of any single person.



That's more or less what the Blockchain is, but with some MAJOR caveats.

- 1) The Blockchain is *pseudonymous* (more on this later). So there's no Social Security numbers, or even names involved. All the entries are just strings of alphanumeric codes.
- 2) No one controls the Blockchain. Unlike your bank which can fiddle with its own internal database whenever it wants, it's not possible to adjust anyone's entry within the Blockchain without a legitimate transaction.
- 3) The Blockchain is public. So, again, unlike you bank which keeps everything private, Blockchain technology is fully transparent; even the software is open-source, which means that anyone can view the source code.

To get an idea of what it looks like, check out <http://www.blockchain.info>.

HOW THE BLOCKCHAIN CREATES CRYPTO-CURRENCIES

Imagine there's a room that anyone can access.

Inside the room are piggy banks made of indestructible clear plastic, so everyone can see what is inside every piggy bank at all times.

The piggy banks can't be removed from the room, and everyone has a key to their own piggy bank.

The room is equipped with security cameras that anyone in the world can view at any time, and every second of footage is also viewable at any time by anyone, forever.

When I want to pay someone, I go into the room wearing a mask – everyone can see I'm doing it, but they don't know who I am.

I unlock my piggy bank, and take out some money, then put it in the other person's piggy bank.

Again, everyone can see me do it because it's caught on video.

BLOCKCHAIN'S OTHER USES

The Blockchain can be used in a number of areas where it is crucial to correctly record a public transaction. Land and property title histories are a great example.

In most countries, the process of registering the sale of a real estate transaction in the official public registry (likely at the local courthouse) takes days and costs a minimum of 50 USD. In many parts of the world, proper title registries do not exist at all.

But with title registry based on Blockchain technology, the title transfer can be done within seconds, and would be virtually free.

Recently the government of the Republic of Georgia announced that they would be implementing such a registry. A similar project is currently underway in Honduras as well. Consistent success could potentially cause a domino effect around the world.

As you can imagine, further application of this technology is nearly limitless. Any asset or security, ranging from shares of Apple to songwriter royalties, can be entitled in the Blockchain.

That history of footage represents all the Bitcoin transactions of every market participant starting from the creation of the first Bitcoin data block. (That first block included 50 Bitcoins).

In traditional finance systems that room is locked away deep in the belly of a big bank and the only people who can access it (and the security footage) are the people running the bank.

Those “chosen ones” have total control over the room and can use that power to promote their agendas... such as printing trillions of new currency units... or freezing you out of your account.

In the case of Bitcoin, the room can be seen by millions of different market participants. Every participant has the same status about the room, so no one has a monopoly over the information, and therefore cannot control or manipulate the footage.

Such a decentralized system means that no one can tamper with the footage in order to gain any advantage or influence over any other market participant.

And even if they try, there are other copies of the footage in circulation. Even if you modify your own copy, it's impossible to modify anyone else's.

Additionally, the number of Bitcoin units in existence is finite and predetermined by a computer algorithm. It is set to a maximum of 21 million units, which will be reached by the year 2110.

Today there are a little over 15.5 million Bitcoins in existence, with a total market value of roughly 10 billion dollars (which is rather tiny if you think about it – the US racks up \$10 billion in debt in a couple of days).

Euros and dollars – the representatives of traditional monetary system – on the other hand, can be created in the trillions on a whim, thereby debasing the value to current holders.

Gutenberg's printing press directly led to the liberation and democratization of knowledge and information... as well as huge innovations in how society organizes itself.

We foresee the same thing happening with crypto-currency, a digital rather than mechanical invention.

Once government-controlled-and-issued money becomes obsolete, the implications for our society will be enormous.

Here's what an IMF report had to say about it:

“[Virtual Currencies], in principle, **question the paradigm of state-supported fiat currencies and the dominant role that central banks** and conventional financial institutions have played in the operation of the financial system.”

And that report is from one of their own. Imagine the quaking in those boots.

Don't get me wrong, crypto-currencies definitely have their flaws and problems as well. After all, they are still in the experimental stage.



It's not unusual for Bitcoin, for example, to have wild price swings (when priced in fiat currencies). That discourages most people from using it as an everyday medium of exchange. However, this volatility should decline as the Bitcoin market matures.

Various technological flaws surface periodically and need to be addressed as well.

Hackers pose a threat to Bitcoin users, especially to web-based Bitcoin wallets. Luckily, you can secure your Bitcoins by taking them completely offline (more on that in a bit).

The biggest issue crypto-currencies face, however, is increasing resistance from governments.

Governments consider Bitcoin a major threat to the status quo, so they are trying to associate it with nefarious activities such as money laundering, drug dealing, black markets, and terrorist activities.

Russia, for example, has explicitly outlawed the use of Bitcoin. Many other countries are considering the idea as well.

However, these bans are very difficult to enforce. And there are many central banks now toying with the idea of setting up their own Blockchain technology.

The technology on which crypto-currencies are based is getting better and better. Wild swings should become a thing of the past once their adoption becomes more widespread and the correct price is "discovered" by the market.

It's clear that widespread adoption is the direction things are going.

In 2013, there were some famous experiments where people had to get by for a couple of weeks using only Bitcoins. It wasn't easy, but they did it. Bitcoin has already come a long way since then.

The number of daily transactions in Bitcoins has been growing exponentially over the last few years, so it is a matter of time before Bitcoin (or perhaps some more advanced crypto-currency) becomes a truly widespread medium of exchange.

To find local brick-and-mortar businesses that accept Bitcoins, click on this [interactive map](#).

And if you are interested in learning how to own and trade Bitcoin, the [Coindesk](#) website is a great starting point.¹



1. For more information on purchasing or storing your Bitcoins, please read through the 'Guides' section on Coindesk's [homepage](#).

IS BITCOIN REALLY ANONYMOUS AND SECURE?

The short answer is: Yes, Bitcoin CAN be as anonymous and as secure as you want it to be. Gaining substantial anonymity and security will require some effort, though.

Let me start with security first.

Be wary of any online service provider (web wallets). Security breaches are not rare... and they can take customers' Bitcoins with them.

If you choose to use a desktop wallet (by storing your wallet locally on your PC), make sure you back up your data from the start. A simple hard drive crash might make you significantly poorer.

Encrypting your wallets is always a good idea as well.

The best method from a security standpoint is to use so-called cold storage – a hardware or paper wallet that is not constantly connected to the Internet. **Treat your hardware or paper wallets like gold — literally — and store them in your home safe.**

Then there's anonymity. On the one hand, the media loves to say that drug dealers and criminals use Bitcoin to exchange funds. But surprisingly, Bitcoin's anonymity level is far from perfect (in most cases).

As you already know, the Blockchain is completely transparent – everyone can see the entire history of transactions of any particular Bitcoin address.

On the other hand, the original system was designed to have no identifying connection between any particular Bitcoin address and the person owning it, therefore resulting in pseudo-anonymity (or pseudonymity).

Hence, **technically, Bitcoin is pseudonymous, rather than completely anonymous**, and this is an important point to understand.



Sample Bitcoin cold storage



Sample Bitcoin digital wallet



But there is a caveat – since a big part of the modern Bitcoin trading and storing happens through convenient and modern exchanges, plus online stores and wallet providers... the **anonymity is compromised since all of these sites typically require a comprehensive identity verification process, in accordance with KYC rules.**

There are a number of ways to fight back and gain the level of pseudonymity that you desire, such as using different addresses for each transaction, or hiding your IP address using various technologies like Virtual Private Networks or the Tor network.

While the use of Bitcoin may not be widely accepted yet, there is another alternative to gaining financial freedom and control that has been quickly adopted by the masses – Peer-to-Peer networks.

Peer-to Peer Alternatives for term deposits and credit access

Aside from the Blockchain and crypto-currencies, the other major tech development affecting how we use money is Peer-to-Peer, or P2P.

P2P is quickly eliminating the costly and redundant link of bank-as-intermediary.

It's inevitable, this elimination of the middle man.

It's already happening on a larger scale in other industries: Airbnb disrupted the hospitality industry. Uber and other similar taxi-hailing apps did that for those who need a ride. Amazon and eBay revolutionized the shopping experience, removing the need for expensive physical retail stores.

Music is another great example.

In 1982 Michael Jackson released the best-selling album of all time. *Thriller* sold more than 60 million copies worldwide. Back then, if you wanted to listen to "Billie Jean," you had to go to the store and buy a physical record. Today, you can download it from iTunes within seconds.

No intermediary.

P2P is leading the way for the same to happen in investment and loan space.

Since the 2008-09 crisis, interest rates in most of the developed world have largely gone to zero, and even into negative territory.

Earning 0.25% or less on your US savings account? You're not alone.

Luckily, alternatives exist.

P2P lending platforms and their offshoot, crowdfunding, are probably the most popular ones, and are living proof that alternative solutions work. And work well.

In 2015 the overall crowdfunding + P2P lending volume reached \$35 billion; it's been growing at a rate of more than 100% per year.

In just 10 years, the world has gone from almost zero dollars raised outside of the

banking system to \$35 billion a year raised from the “crowd.”

Asia, Africa, and Latin America are just getting their first taste of P2P lending and crowdfunding, so there’s still a huge potential for growth. And these are the regions where traditional credit is typically hard to come by, especially for small- to medium-scale entrepreneurs.

Imagine a farmer in Paraguay who wants to buy a milk cow so that he can sell the milk and feed the family. Applying for a loan for his little project with a local bank would likely be onerous and ineffective.

With P2P lending platforms and crowdfunding, though, he has a substantially higher chance of getting the money. Now he can get \$10,000 or \$5,000 — or even just a \$100 if that’s what he’s looking for.

All he needs is Internet access and a compelling story to convince investors to lend to him.

P2P LENDING PLATFORMS

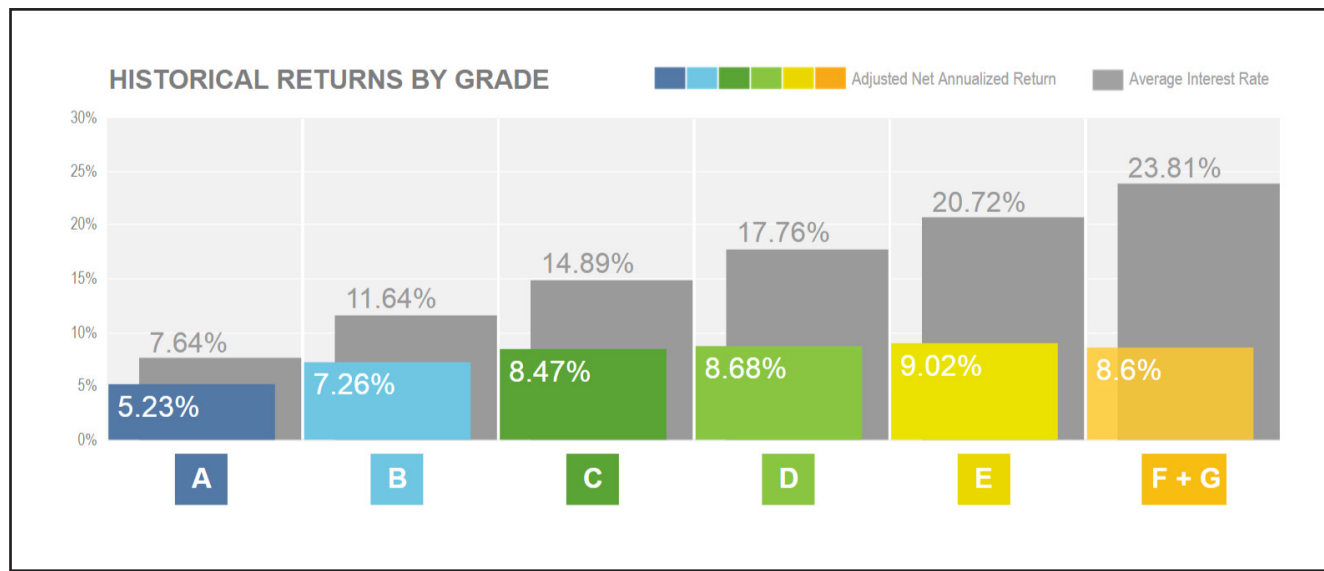
Kiva.org is a non-profit organization that specializes in helping people in underdeveloped countries. Please note that investors in this platform do not earn interest on their money, but rather just receive their principle back.

Investors therefore can deploy their money again and again to fund the next project in the next underdeveloped country and therefore help fuel commerce in parts of the world that need it the most.

As for investors looking for real returns, other P2P lending platforms offer potentially superior ROI, plus the ability to easily diversify a lending portfolio to minimize risk.

The most established commercial P2P lending platforms are [Lending Club](#) and [Prosper](#) in the US, and [Zopa](#) and [Funding Circle](#) in the UK.

To give you an idea of how much you can actually make with these platforms, let’s look at what Lending Club has to offer its investors.



Lending Club assigns a grade (from A to G) to each loan based on the borrower’s credit quality and underlying risk. The lowest interest rates are assigned to the least risky grade A, which reflect the potentially lower default rates and lower volatility in returns for investors.

As you can see from the graph above, grade A borrowers are being charged a 7.64% interest on average by the Lending Club. Investors, on the other hand, on average receive 5.25% as a reward for lending their money.

Why the difference?

The difference of 2.39% (7.64% - 5.25%) comes from Lending Club’s service and collection fees, recovery costs on delinquent loans, loan defaults, and estimated future losses.

The further you go towards the end of the loan grade alphabet, the higher the interest rate borrowers are paying – grade F and G borrowers are paying around 25% interest.

But what’s interesting is that while interest rate on loans grow substantially, rates of return for investors grow much more slowly... and even start to decrease when you get to F and G grade loans.

That happens because there are many more loans in the categories that are being defaulted on. Recovery efforts and eventual loan defaults are eating into the investors’ profits.

Some other facts about Lending Club:

- Starting from 2007 and up to the 1st quarter of 2016, Lending Club has issued more than \$15 billion worth of loans

- Of these 15 billion, 22.6% are already fully paid, 54.11% are current, 1.13% are late, 3.86% are charged off (defaulted)
- The majority of the loans are graded B and C (about 27% of total dollar amount loaned) followed by grades A and D (about 16% each of total dollar amount). Grades E, F and G combined constitute the remaining 14%
- Average loan size: \$14,853
- Loan terms are fixed at 36 and 60 months
- Investors typically do not invest in the entire loan amount, but rather own a portion of each loan. As little as \$25 can be invested into any single loan.
- The majority of borrowers use the loans to pay off high interest rate loans they already have (mostly credit card balances). The average interest rate on credit cards in the US is around 18%.

Important to mention – diversification is crucial here. You definitely do not want to invest all of your designated investment capital into just one loan (even if it is grade A), as it may suffer a possible future default. Lending Club recommends investing in 200 different loans rather than 20.

It's also safe to assume that in the case of a major financial crisis, the number of loan defaults will increase significantly. That would negatively affect investors' rates of return... and possibly cause them to lose part or all of their initial investments. *Caveat creditor.*

Speaking of other potential risks, some analysts are already talking about a bubble in P2P lending. Indeed, the meteoric rise of P2P lending does not represent a sustainable rate of growth over the long term.

Additionally, Wall Street has already started packaging and redistributing securities based on P2P loans, bringing fresh memories of the devastating subprime mortgage crisis...

On a positive note, Zopa, which has a decade of experience in the space, reportedly approves only 20 percent of all loan applications, and an average Lending Club's borrower has a FICO score of 699 (not excellent, but definitely not subprime).

Borrowers are still mostly in a "prime" category. For now.

In addition, the total lending volume of \$35 billion (or even the ~\$70 billion expected by the end of the year) is still nothing more but a rounding error when compared to traditional debt (household and business)...estimated at upwards of \$96 trillion in the world today.

There is still a lot of potential for P2P lending to reach.

LIMITATIONS AND TAX IMPLICATIONS OF P2P LENDING

If you decide to invest with P2P platforms, I encourage you to first learn about the limitations and potential tax implications:

- There may be limitations on who exactly can lend the money with P2P platforms. For instance, Lending Club [explains on their website](#) that (for most states) an annual gross income of at least \$70,000 AND a net worth (exclusive of home, home furnishings, and automobile) of at least \$70,000, OR a net worth of at least \$250,000 (same exclusions apply) is necessary.

The good news is that once you comply with these requirements, there are typically no limitations on how much (or how little) you can invest.

In UK-based platforms, there are currently no financial requirements for potential lenders.

- To be able to invest with US-based P2P platforms, you or your entity must also be based in the US.

UK-based platforms, similarly, will require you to have at least a UK residency and a UK bank account.

- For your tax reporting, UK-based platforms generate an annual income statement, and US-based platforms generate 1099 forms to use for tax reporting.

Lending Club also releases a tax guide every year. [You can find the most recent one here.](#)

Please note that *Sovereign Man* is not in a position to give you personalized tax advice. Before jumping into the waters of P2P lending please make sure you understand all tax implications by consulting with your tax advisor.

CROWDFUNDING PLATFORMS

Crowdfunding platforms, unlike P2P platforms, are mostly for entrepreneurs with a solid idea who are looking for startup funding... and for investors who wish to support an idea and/or business (rather than an individual with credit card or medical debt).

Crowdfunding is a great step towards eliminating over-lording banks. Instead of raising money from big investors, entrepreneurs can raise it from the “crowd” and essentially pre-sell their products, which gives them the capital needed to actually start production.

[Kickstarter](#) and [Indiegogo](#) are the two most well-known crowdfunding platforms. Money can be raised for anything from smartwatches to software to new crypto-currencies.

And when I say anything, I mean *anything*. Some crowdfunding platforms, like GoFundMe.com, often raise money for personal things like a 20-year-old’s trip to Europe.

You may recall that I provided financial assistance to a wounded US Army veteran who lost his leg in Afghanistan. I first came across him from the site GoFundMe—he was trying to raise \$70,000 for prosthetic treatment after being abandoned by the US government.

In 2014, Sylvester Stallone even used two crowdfunding sites to raise \$250,000 for an independent film project *Reach Me*. The movie was as total flop, but Sly’s crowdfunding campaign was very successful.

Here are some other P2P and crowdfunding platforms that bring creative ways of connecting borrowers with lenders:

- If you already have a traditional business, such as a restaurant or vet clinic, and need money to buy out a partner or expand, you can use [Fundera](#) and choose from dozens of different lenders competing for your business.
- [CircleUp](#) takes it to the next level and connects accredited investors (those with big money) with high-growth consumer companies seeking funding. Unlike Kickstarter, investors in CircleUp receive equity in the company they are investing in (becoming co-owners). The average amount raised is more than a million dollars.
- [Fundrise](#) is a real estate crowdfunding site in which the founders personally screen, vet and buy every real estate deal they present on their website. After that, they “resell” it to their investor pool.

- [Vouch](#) offers an intriguing concept – if you have many friends who have faith in your creditworthiness and would officially vouch for you, why not put it to good use?

It takes only one sponsor to get started with Vouch, but the more people who sponsor you, the higher the amount you can borrow, and the lower the interest rate.

Beware when vouching – the friends have to pay if the borrower doesn't. So don't vouch for someone you don't truly believe in.

Conclusion

We are living in incredibly exciting times.

Many traditional industries that have been around for centuries are undergoing a complete, positive transformation powered by modern technology and private enterprise.

Airbnb changed the hospitality industry. Uber and Amazon have forever changed the way people move around and how they shop.

Netflix and Hulu revolutionized the ways how people watch TV.

iTunes and Spotify have done the same with the music industry.

3D printing is gaining momentum, becoming faster, cheaper, and more convenient by the day, and quickly becoming the better alternative to traditional manufacturing. In a few years, most goods will be made on demand, close to their end destination, and will not have to be transported thousands of miles overseas.

Technology has changed our lives and disrupted entire industries... making products and services more competitive, more convenient and cheaper.

The same will happen to the financial industry. It has barely changed for centuries... and is due for a major overhaul.

It's very likely that in just a few short years we'll be keeping our savings in a gold-denominated digital currency (in Bitcoins or an improved and more advanced crypto-currency).

We'll be wiring money instantly, using services like Transferwise to avoid outrageous currency exchange fees.

We'll be taking out business loans and even home mortgages via peer-to-peer lending platforms.

It's not a fantasy. The majority of these services already exist today. It's just a matter of time before their use spreads as wide as that of Airbnb or Netflix.

The likely major turning point will be the next financial crisis... one that potentially will be much bigger than the one we experienced in 2008.

People will be frozen out of their accounts. They will not be able to get their money out of the country due to capital controls. The value of their fiat money will deteriorate because governments will have created too much of it.

That is exactly when the vast majority of people will realize that alternative solutions have become the much better, safer, and cheaper options.

And when traditional banks realize that they are losing the game, and are going the way of dinosaurs, they will have to start innovating again in order to stay in business.

Many banks are already seeing the writing on the wall... and are getting on board with the Fintech revolution themselves.

Citigroup seems to understand better than any other financial agglomerate that the Fintech revolution is imminent. It has invested in, or bought out, more than a dozen different Fintech startups since 2010.

Citigroup itself estimates that in ten years, by 2026, about 30% of its workforce will be replaced by automated online services. (How many times did you actually have to visit the physical offices of Airbnb or Uber to use them?)

Eventually, inevitable increases in competition will cause banks to stop being corrupt giants, trying to control and manipulate every aspect of the economy... all while bribing the politicians to push their agendas.

As Thomas Jefferson once famously said: "...power should be taken from the banks and restored to the people, to whom it properly belongs."

That process has already begun.