Race for the Money: International Financial Centres in Asia

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Abstract

Asia's emergence as a key player in the global economy is witnessing intense competition within the region to become Asia's next great international financial centre. Hong Kong, Singapore and Shanghai, among others, are each vying for primacy, attempting to attract dense clusters of financial services firms and reap the lucrative rewards associated with this. This paper explores this emerging competition. It does so from the perspective of attempting to map the parameters necessary to become an international financial centre, particularly the institutional, political and spatial contexts that facilitate the concentration of international financial services. Why and how financial clustering occurs and the factors that determine the location of financial centres is an important public policy concern, both for established centres eager to maintain their competitive position as well as emerging economies keen to identify the policy levers necessary to support financial sector growth. To that end, the paper explores the experiences and strategies of three of Asia's current contenders; Hong Kong, Shanghai, and Singapore, analyzing the policy architecture, financial sector strategies, institutional mechanisms and spatial geographies undergirding financial sector growth, and the constraints, obstacles and challenges each face in developing and or consolidating their international financial centre.

Key Words: International financial centres; Asia, financial clustering, Shanghai, Singapore, Hong Kong, financial sector depth

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Introduction

'Money makes the world go around' according the popular cliché of the 1968 film classic, *Cabaret.* Perhaps more to the point, of course, is that money going around the world makes money, indeed great fortunes for those international financial centres (IFC) able to interdict the vast sums of fast moving money. For the winners, the pickings are lucrative and getting larger. By one estimate, for example, the value of the stock of wealth held offshore now stands at US$41trillion dollars, up from US$6 trillion a decade earlier and continuing to grow (Hampton & Christensen, 2002: 1657; Bailly, 2008). Similarly, the volume of cross border capital flows have expanded on average at 14.2 % annually since 1980, up from US$500 billion to US$8.231 trillion in 2006-7 ─ an eightfold increase since 1990 alone. And total cross border investments now stand at a massive US$74.5 trillion (Ferrell *et al*., 2008: 13-15). All this, however, is dwarfed by the daily turnover in traditional foreign exchange markets which currently stands at US$3.21 trillion or US$3,254 trillion annually (BIS, 2007:1). Indeed, if the daily turnover of non-traditional derivative products is added to the mix (US$2.1 trillion), then total daily turnover in foreign exchange markets now runs at a staggering US$5.31 trillion (BIS, 2007: 4).

Little wonder that there is a race on, a race for the money to become what Jessie Poon (2003) describes as one of the 'control centres of global financial flows;' an international financial centre. In Asia the race is wide open, with the region currently lacking 'a single dominant financial hub' (Farell *et al.*, 2008: 15). While Tokyo and Hong Kong have traditionally been the dominant players, the rise of China, flux in the institutional architecture of Tokyo's financial apparatus, consolidation in Singapore, and the addition of several other contenders from South Korea to Labuan, have added to the mix and made competition intense.

This paper explores the dynamics of this competition.. It does so from the perspective of attempting to map the parameters necessary to become an international financial centre, particularly the institutional, political and spatial contexts that facilitate the concentration of international financial services. Why and how financial clustering occurs and the factors that determine the location of financial centres is an important public policy concern, both for established centres eager to maintain their competitive position as well as emerging economies keen to identify the policy levers necessary to support financial sector growth. To that end, the paper explores the experiences and strategies of three of Asia's current contenders; Hong Kong, Shanghai, and Singapore, analyzing the policy architecture, financial sector strategies, institutional mechanisms and spatial geographies undergirding financial sector growth, and the constraints, obstacles and challenges each face in developing and or consolidating their international financial centre.

The paper is organized into three sections. The first surveys the theoretical literature examining the clustering, location and spatial distribution of international financial centres. The point here is not simply to describe the literature but set in place a series of discrete explanatory models which might then be 'tested' against empirical findings generated through the case studies. The second section then develops the three case studies, addressing financial sector composition and the policy and institutional mechanisms that provide the broader architecture for each of the international financial centres. Critical to the analysis in this section has been the perspectives gathered through fieldwork and interviews conducted with regulators and financial services firms. These reveal the various factors that weigh in the location and establishment decisions of financial services firms and how their prioritize attributes associated with specific financial centres. It also reveals the limitations and constraints that operate on public sector officials and affirms some of the theoretical explanations surveyed. Finally, the paper attempts to identify a nominal set of criteria for assessing the likely outcomes of the competition between Asia's financial centres, not by way of 'picking a winner' but

as a means of understanding the broader structural forces acting on the competitors and their likely implications.

I: Explaining IFCs: Location, Distribution and Size

Financial centres can be traced back as far as ancient times. One of the oldest cities in the world, Samerkand, for example, functioned as a major commercial centre servicing the Silk Road between China and Europe (Mainelli, 2006), providing brokerage, credit and allied services to the trade caravans that plied its route. Marrakech, Babylon, Timbuktu and Constantinople too have each functioned as major financial centres at various points in time. In the eighteenth and nineteenth centuries, larger financial centres emerged to service regional and international markets as the volume of economic exchanges and their complexity increased. Cities such as Berlin, Frankfurt, Amsterdam, Florence, Hamburg, London, Milan, Paris, New York, Rome, Philadelphia, Turin, Venice, Genoa, Shanghai and Zurich, all emerged as leading centres of finance and commerce (Kaufman, 2000; Fratianni, 2007).

The emergence of financial centres is commonly explained in relation to their role in financial intermediation. As Reed observes, financial centres emerge because of their ability to 'balance through time the savings and investments of individual entrepreneurs and to transfer financial capital from savers to investors' (Reed, 1980: 20). Financial centres thus 'perform a medium of exchange function and an interspatial store-of-value function' (Reed, 1980: 20). Some of these centres eventually evolve into international financial centres (IFCs) that possess 'highly specialized functions of lending abroad and serving as a clearinghouse for payments among countries' — in other words, they evolve an ability to 'effect payments and to transfer savings between places.'(Kindleberger, 1974; Reed, 1980: 20). At base, IFCs might thus be understood as central places for financial capital and currency to be 'collected, switched, disbursed and exchanged' (Tschoegl, 2000: 3). This latter point explains why financial centres have historically been major *cities* as opposed to nation-states, reflecting the role of

cities as mediums of habitation that concentrate population, commercial, industrial, legal, and administrative activity (Mainelli, 2006). Common definitions of financial centres thus normally highlight their role as places of *intense* exchange relations which exhibit a dense clustering of a wide variety of financial businesses in one centralized location (Mainelli, 2006).

Place Theory

While the role and functionality of IFCs is relatively uncontested in the literature, less so are the explanatory models explaining their location and the determining variables responsible for their size and spatial distribution. Here the literature is split between four separate but related schools of thought. The first reflects a long tradition of spatial analysis and explanatory variables such as hinterland proximity, geographic clustering and scale economies to explain the size, distribution and services composition of IFCs. Much of this literature has a distinctly geographic-theoretical lens, where the geography of space explains the bespoke configuration of financial centres, their size, distribution and their relationship to the economic hinterlands they service (Bertaud, 2004). Place theory famously developed by Walter Christaller (1966), for example, explains urban hierarchies as a function of their inequalities. These result as a consequence of the differing efficiencies to which goods can be supplied to markets relative to the distance that consumers need to travel to acquire them. In Christaller's thesis, goods have differing 'thresholds;' the higher the value of the good the higher is the 'range' or maximum distance consumers are prepared to travel to acquire the good. This inverse relationship between the 'threshold' of goods and the 'range' tolerance for purchasing them thus produces a spatial configuration of urban centres that disburses them hierarchically relative to the value order of the services and goods they produce. In Christaller's thesis, this produces distinctive spatial patterns with a relatively small number of large urban centres producing high order goods and services separated by wide distances while numerous smaller urban centres producing lower order goods and services are separated by smaller distances (Neal, 2008). Likewise, as the size of an

urban centre grows and the volume of high order goods and services it produces intensifies, the economic thresholds of the urban centre increases, in the process changing the absolute size of the economic hinterland it services and the spatial dynamics of adjacent urban centres.

World Cities

Strands of place theory can also be observed in more recent literatures that attempt to explain the formation, spatial and hierarchal distribution of financial centres. The 'world cities literature,' for example, as Jessie Poon (2003) notes, sees

> a global urban landscape . . . dominated by a small number of cities that are distinguished by their higher order functions of control and coordination of global economic flows. These cities are pivotally arranged in a hierarchical network of trade, investment, financial, and even government transactions, and are responsible for creating value up and down the global economic chain (Poon, 2003:136-137).

In the case of the world cities literature, the hierarchical distribution of IFCs is differentiated between 'world cities' and "global cities;' the latter creating a super-hierarchy (London, New York and Tokyo) who produce super-high order services that have a global financial hinterland. As Saskia Sassen notes (1999), the transformation of global capital markets is shrinking 'nationally based financial operations' and causing clustering up the value chain, which, in turn, is creating a series of dominant global players. The spate of deregulation of national financial markets since the 1970s coupled with the effects of deepening globalisation has, ironically, produced an asymmetrical process that sees the emergence of yet more international financial centres and 'world cities' but where the acute agglomeration of financial activities clusters around fewer mega-financial centres or "global cities". As Sassen observes, by the end of the last century, just

> . . . 23 cities controlled 83% of the world's equities under institutional management and accounted for roughly half of global market capitalization (around $20.9 trillion). Six or seven cities head the league; London, New York, and Tokyo combined hold a third of the world's institutionally managed equities and account for 58% of the global foreign exchange market (Sassen, 1999: 77)

Scale Economies

Allied approaches explain international financial centres and financial clustering as a function of scale economies. Clustering arises from the efficiency gains and reduction in costs associated with financial agglomeration, where the density of financial service firms not only reduces barriers to transaction facilitation but creates information symmetries and knowledge economies that reduce operating and transaction costs. Clustering, for example, produces allied markets and agglomerates skills capacity in financial management, engineering, legal and settlement systems which reduces collective industry costs and allows competition in the provision of services because of market size and specialization. It also provides employment pools of highly skilled labour that would otherwise require large upfront sunk costs for training and skills development. Further, scale economies and clustering allows for the emergence of trust relationships and of transactional norms that become institutionalized. Issuers of securities, project financiers, underwriters and insurers of structured financial products, for example, are able to orchestrate pools of capital, mediate transactions and secure outcomes with relatively low transaction costs in expedited timeframes. Similarly, scale economies allows for the commoditization of risk and for risk to be spread and on-sold between multiple agents who operate in specialized markets, further reducing transaction barriers.

The effects of scale economies combined with functional specialization is also used to explain the contrasting sizes, distribution and capacities of IFCs. London and New

York's scale advantages in foreign exchange, international bonds and the depth of their capital markets dwarf the capacities of other European (Paris, Frankfurt) or North American (Toronto, Chicago) financial centres producing self-reinforcing comparative advantages that deepen specialization and centralization and further enhance capacity and their spatial reach over a global financial hinterland. Size, in other words, rather than distance is what matters and orders the distribution and hierarchy of London and New York as dominant actors in global capital markets (Poon, Eldredge, Yeung, 2004: 414).

The pull of centralization through scale economies and specialization obviously has explanatory limitations, however. By this logic there should be fewer but larger global financial centres with the tendency for regional, smaller financial centres to be made redundant. As Sassen (1999), Tschoegl (2000) and Taylor *et al.* (2002) among others observe, however, two counterpoising trends are evident; centralization and the emergence of a small number of dominant 'global' financial centres (London, New York, Tokyo ─ the 'global three') but concomitantly the emergence of an increasing number of smaller regional financial centres. In the Asia-Pacific, Sydney, Singapore and Hong Kong have each prospered and grown despite the scale economies enjoyed by the global three ─ an apparent anomaly. What explains this?

Theorists like Parr (1978) emphasize the role of decentralization *and* fragmentation in financial globalisation that results in the emergence of bespoke relationships between similarly sized regional financial centres. Regional financial centres thus become important and prosper precisely because they deepen financial intermediation, connecting regional hinterlands into a global financial value chain. Others like Poon, Eldredge and Yeung (2004) highlight a combination of developments in communications technologies and outsourcing of lower value adding services that fosters decentralization and spurs the development of regional financial service centres. These centres enjoy their own knowledge economies, providing niche specializations that address the needs of localized markets and broker financial relationships between

regional hinterlands and the global three. Singapore and Hong Kong, for example, have specialized knowledge economies that serve Chinese business in both mainland China and the sizable Chinese diaspora throughout Southeast Asia. Sydney, by contrast, has specialized knowledge economies in local swap markets (Poon, Eldredge and Yeung, 2004: 414-415).

Finally, decentralization literatures point to the rapid modernization of developing economies over the last several decades and the emergence of localized demand for financial intermediation and specialist financial services. Dubai, Qutar, Beijing, Mumbai, Shanghai, Shenzhen and San Paulo, among others, display nascent economic developments in their immediate hinterlands and the deepening requirements for economic and financial complexity ─ not least the need to develop intermediating centres to tap into global financial networks and access and distribute capital (Farrell *et al.*, 2008: 63-68; Poon, Eldredge and Yeung, 2004: 414-415).

Beyond Space: Endowed Capacities

Spatially bounded theoretical literatures have held a dominant sway in explaining the location, size and distribution of financial centres. More recent literatures, however, question their validity. As the Financial Times noted, 'Banking is rapidly becoming indifferent to the constraints of time, place and currency' (as quoted in Harvey, 1990: 161), largely as a result of advances in communications technologies and the emergence of dependable instantaneous real-time telecommunications networks. For many theorists, such developments represent the 'obliteration of space' (Harvey, 1990; Lash & Urry, 1994) as a determining variable in the location, distribution and size of financial centres (Krstic, 2004:127). A nascent forth literature has thus emerged which addresses the endowed capacities necessary to support the emergence and development of a financial centre. This literature speaks to the physical, institutional, policy and knowledge environments that support the location decisions and thus clustering of financial services firms ─ and multinational corporations more generally (Zhao, Cai &

Zhang, 2005). Sagaram and Wickramanayake (2005), for example, identify 5 key factors that influence the location decisions of financial services firms, including (i) a favorable regulatory regime, (ii) competitive taxation structure, (iii) the presence of various socio-cultural factors like quality of the living environment for attracting and retaining talent pools, (iv) the presence of financial variables including critical market depth and sufficient turn-over volume, and (v) the existence of sufficient levels of economic activity as a means of undergirding a viable commercial banking sector. Tschoegl (2005) also includes variables like access to quality infrastructure such as telecommunications and aviation networks and the role of politics both in terms of political stability but also policy stability and domestic institutional adaptability (Tschoegl, 2005: 9-15). Other theorists like Wang and Zhao (2007) and Porteous (1995) extend the notion of knowledge economies and highlight the role of soft institutional structures and social networks that intermediate knowledge transfer and information flows and, in combination with the formal regulatory and institutional structures, create information economies that broker the orderly dissemination of information and create information transparencies necessary to the functioning and efficient operation of financial markets.

Competing Literatures

These four literatures represent related but competing explanations of the location, size and distribution of international financial centres. They also imply very different roles, capacities and strategies for governments eager to develop and or consolidate their financial centres. The endowed capacities literature, for example, implies the possibility of deliberative public policy creating the institutional and infrastructural environment able to evolve an international financial centre. The place theory, world cities and scales economies literatures, on the other hand, suggest a more marginal role for government, constrained by spatial processes associated with the presence of trade routes, various historical antecedents and the importance of first mover advantage. The following sections attempts to disentangle these issues by exploring the historical and institutional

contexts associated with the evolution and operation of three international financial centres: Hong Kong, Shanghai and Singapore.

II: Hong Kong, Shanghai and Singapore: Financial Sector Composition, Institutional and Policy Contexts

Hong Kong

Hong Kong has emerged as one of the world's leading financial centres. It is currently Asia's second largest stock market (after Japan), the world's sixth largest foreign exchange market, has one of the world's four largest gold markets, is the second largest funds management centre in Asia and ranks as the 12th largest international banking centre in external assets (HKMA, 2008; Dong *et al.*,2006:22). Beyond its formal banking sector, Hong Kong has also emerged as one of the region's foremost money and debt markets, derivitives (futures) markets, silver and gold markets, asset management centres and operates as one of the most open insurance centres in the world (HKMA, 2008).[2]

Established in the 19th century as a British colony and a trading entrepôt to service the lucrative market between the West and China, Hong Kong's fortunes have always been reliant on international trade and finance and on its relationship to China more generally (Schenk, 2002: 232).[3] While Shanghai dominated international finance in the Far East in the early 20th century, civil war and economic chaos in China throughout the 1930s and 1940s witnessed the emergence of Hong Kong as the region's foremost financial enclave. As Catherine Schenk observes, 'the local traditional banking sector in Hong

[2] As a general disclaimer, it is worth quoting a recent IMF working paper by Cynthia Leung and Olad Unteroberdoerster (2008) regarding the measures for ranking international financial centres. Leung and Unteroberdoerster observe 'There does not appear to be a universally accepted definition of the term 'international financial centre. Nor is there a unique framework of quantitative measures that would document their activities and relative performance' (Leung and Unteroberdoerster, 2008:3).

[3] Evidence of how lucrative East-West trade was for Hong Kong is revealed by the fact that in the 5 years from 1879 the number of large Chinese trading business grew from slightly less than 200 to a little over 400 while and the number of small trading firms grew from less than 300 to 2,400. See Hazel J. Johnson (2000), *Banking Alliances*. Singapore: World Scientific, pp.140-141.

Kong thrived on the chaos in China,' benefiting from an influx of Chinese political and economic émigrés, the relocation of Western business headquarters out of Shanghai, and massive capital in-flight as a result of Chinese hyper-inflation between 1947-1949. Shanghai's losses were Hong Kong's gains, with the colony enjoying the swelling talents of mainland émigrés who bought with them social and business networks that made the colony an intensely networked banking community — or what Meyer describes as the 'pivotal intermediary hub' of Asia's 'social networks of capital' (Schenk, 2002: 323-325; Schenk, 2000:746-751; Li, 2004:1; Meyer, 2000:242).

In the post war period, Hong Kong's rapid industrial development coupled with its entrepôt status witnessed huge increases in demand for banking services and expansion of the financial services sector (Jao, 1974:18; Schenk, 2002:340). By 1954, for example, Hong Kong had 94 licensed banks and hosted some 19 foreign banks, and between 1954 and 1972 witnessed massive expansion in the deposit base of its commercial banks, growing from HKD$1,068 to HKD$24,613 million (Jao, 1974: 23). Yet by far the single most important source of Hong Kong's advantage as a financial centre from the 1940s through to early 1970s was its free exchange market (Schenk, 2002:332; Liu, 1997:583-588). While the international system operated mostly under the Bretton Woods set of agreements with limited currency convertibility and a fixed peg exchange rate system, as a British colony Hong Kong enjoyed full access to the 'sterling area' comprised of commonwealth countries (except Canada) who pegged their currencies against sterling (Schenk, 2002: 332; Jao, 1974: 17). The arbitrage to be had from servicing this market coupled with the rapid increase in demand for foreign exchange to satisfy other trading requirements, created a parallel exchange market for Hong Kong Dollars (HKD) and, in turn, their exchange into Sterling and US dollars (Schenk, 2002:332; Ghose, 1987:22-29).[4] Hong Kong became a ' a lucuna in the otherwise

[4] As Catherine Schenk notes, the free exchange market offered by Hong Kong in an otherwise controlled international exchange rate regime allowed Hong Kong to generate tremendous wealth through foreign exchange arbitrage. 'Residents of Europe and North America used Hong Kong to buy Sterling cheaply at discounted rates to that of the officially pegged rates and thus settle their debts to UK residents.' Likewise, foreigners managed to 'convert their current into HK$' and then to convert 'HK$ to Sterling or US$ on the free market.' The people's Republic of China (PRC) too used the free exchange market in Hong Kong

closely controlled Bretton Woods system;' cementing its reputation as a 'money city' where deals, finance, exchange and trade made for the lifeblood of the colony (Schenk, 2002:333).

More recently, Hong Kong's fortunes have again rested largely on developments in China, particularly the mainland's opening to the West and the marketization of its economy. A combination of deepening demand for debt raising, equitization and IPOs, the privatization of state owned enterprise (SOEs), rapidly expanding China – West trade and accelerating demand for mainland banking services, has witnessed an allied expansion of Hong Kong's financial services sector. Hong Kong thus now boasts some 202 licensed banks, restricted licensed banks and deposited taking companies and a total of 145 fully licensed foreign banks. Of the top 100 banks in the world, 69 have an operational presence in Hong Kong and 82 foreign banks have representative offices. Hong Kong's banking sector thus now reveals a diverse and matured set of commercial activities ranging from traditional retail deposit taking, wholesale banking, securities brokering, trade finance, treasury activities and precious metal trading (HKMA, 2008). Indeed, the importance of financial services to Hong Kong has seen it designated a 'pillar' industry in recognition of its role as a key driver of employment and economic growth, with financial services contributing 23% of revenue from corporate income tax and fully 12% of Hong Kong's economic output (Dong *et al.*, 2006:22; Cheung & Yeung, 2007:5-7).

Institutional and Regulatory Contexts

While Hong Kong's fortunes clearly reflect its historically legacy as a entrepôt trade hub and its relationship to China, no less important to its success as a financial centre has been the institutional and regulatory architecture supporting business, transaction facilitation, clearing and settlement systems, and the system of regulatory oversight.

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as a means of satisfying its exchange needs for Sterling and its limited trading exchange relations (Schenk, 2002: 333; Ghose, 1978: 22-31).

Indeed, despite its reputation as a 'free city' and what Owen described as 'unique in its correspondence to the classical economists dream world which existed in the golden age before 1914' of laissez-faire, Hong Kong' s policy architecture more accurately reflects a position of 'positive non-interventionism . . . [as] a deliberate policy choice rather than merely an absence of policy' (as quoted in Schenk, 2002:322). The difference is a subtle one and underscores a policy culture that prides itself on a 'light touch' approach to regulatory oversight but set amid a firm belief in the value and necessity of strong institutions as the guardians of market functionality. Hong Kong's financial services sector has thus witnessed an evolution in its institutional forms and regulatory approaches with several significant reforms since the 1960s (Huat, Lim & Chen, 2004: 19). These culminated in the adoption of a prudential supervisory system based on risk management in support of bank safety and soundness with oversight authority vested in the Hong Kong Monetary Authority (HKMA) established in 1993.

As the peak institution responsible for financial sector oversight, the HKMA is charged with maintaining monetary and banking stability, continuity, bank safety, the stability of the Hong Kong dollar, and 'developing Hong Kong's financial infrastructure to enable money to flow smoothly, freely and without obstruction' (HKMA). Clearly, its role is more than that of a simple regulator as revealed in its charter objectives; 'to enhance the efficiency, integrity and development of the financial system, particularly payment and settlement arrangements' (HKMA). As one senior supervisor in the Banking Supervision division of the HKMA commented, "our role [the HKMA] is part supervision, part oversight, part audit, but essentially we are here to help grow the financial sector in Hong Kong and make it attractive as a centre to conduct business . . . What we do is make sure that things work and try and anticipate problems that might cause things to go wrong so that we protect our [Hong Kong's] reputation as a place of business" (Interview, October, 2007).[5]

[5] Interviews were conducted in-field in Hong Kong between June 18-26, 2008 and by phone with regulatory officials and private sector financial services firms in Shanghai at various times between June and August, 2007. Interviews with financial service firms in Singapore were conducted over the course of 2007 and between April 15 and July 25, 2008. A total of 14 interviews were conducted. Where the

Similar supervision come market promotion institutional arrangements are in place for Hong Kong's securities, futures and equities markets. The Securities and Futures Commission (SFC), for example, has oversight responsibilities for securities trading, leveraged foreign exchange trading, futures products and contracts, various investment products offered to the public, asset management, financial services licensing, as well as regulatory oversight of 'Hong Kong Exchanges and Clearing Limited (HKEx)' and the listing regulations for the HKEx (Securities and Futures Commission, 2007). At the same time, its lead mandate is 'to ensure Hong Kong's continued success and development as an international financial centre," in part through ensuring efficiency and innovation in the support infrastructure offered through clearing, settlement and payments systems and regulatory efficiency generally. Similar regulatory and institutional structures are in place for the insurance and precious metals markets (see Table 1 for an overview of financial services sector and regulatory architecture in Hong Kong).

Apart from the formal institutional regulatory bodies Hong Kong has also evolved what Cheung and Yeung (2007:26) describe as 'soft infrastructure:' a complex web of informal and semi-formal norms, procedures and practices (many of them ensconced in professional bodies / societies) that operate around corporate governance standards, insolvency procedures, securities regulation, accounting and audit bodies, disclosure and transparency practices — among others — and which broker the flow and orderly distribution of information necessary to the functioning of high capacity markets and the regulatory and institutional practices that support them. Arner and Norton (2000: 310) identify these as the tapestry of 'cultural traits' unique to Hong Kong and in large measure responsible for its innovative business environment and the competitive

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identities of interviewees are not revealed, this is at the request of the interviewees. Interviewees generally requested their identities to be concealed along with the identify of their organization. Most nominated concerns about 'offending' regulators, 'breaching confidences,' or upsetting 'trusted relationships' with regulators and or contacts in regulatory agencies as the reason for concealing their identity. Many were also concerned that should interviews not be 'off the record' they would be unable to talk without gaining permission from their legal affairs department. Their requests have been respected.

advantage it has enjoyed historically. Hong Kong's social and professional networks are what makes its financial markets work. Complex professional and social relationships disseminate, mediate and transact information and create information symmetries beyond formal organizational boundaries or institutionalized market rules (Dubini & Aldrich, 1991). In turn, such networks enhance regulatory efficiency, creating networked forms of governance that evolve implicit standards, norms and practices that serve to increase regulatory and market transparency, lower transactions costs and thus the intensity of financial transactions. As Karreman and van der Knaap (2007: 5-7) note, financial activity and financial service firms tend to concentrate around environments with high information symmetries; an attribute that has historically made Hong Kong a primary destination for financial services firms establishing in Asia. Indeed, Hong Kong's highly evolved networks are alluded to in various conversations with finance professionals. A senior executive responsible for identifying market opportunities and business development with a large British bank, for example, noted that 'in Hong Kong when you plug into the right people it's amazing . . . word gets out and whatever you need people suddenly get back to you to close it . . .It's the easiest place I have ever worked in terms of information and contacts' (Interview, June, 2008). Similar sentiments were expressed by a senior banker with an American financial institution who noted that 'in Hong Kong your networks are everything . . . because then it happens . . . you get to know what is going on and they know about you . . . Just a few phone calls and the word is out and what I need I can get quickly . . .' (Interview, June, 2008). The head of corporate strategy of a large West European Bank confirmed these observations, noting that Hong Kong is 'unique, it's networked to everywhere in China and back again!' (Interview, June, 2008).

Shanghai

Shanghai's institutional and regulatory contexts, by contrast, belie a very different history. In 1949 Shanghai was Asia's leading financial centre hosting 24 state banks, some 200 private lending, trust companies and financial institutions, and hosted the

world's third largest stock market behind New York and London (Laurenceson & Tang, 2005:147). For more than a century, Shanghai had been the 'modern crucible of China' and played a prestigious role as one of China's five 'open cities' stemming from the Treaty of Nanjing in 1842 (Lai, 2006:3). Its historical success and reputation, however, became its liability under communist rule, with Shanghai inextricably associated with capitalist excesses and a humiliating semi-colonial past.

When Shanghai re-emerged in the late 1970s it was a mere shadow of its former self; no longer a financial hub but transformed into what Wu describes as the 'locomotive of state-led industrialization' — the industrial cash cow of Beijing (Wu as quoted in Lai, 2006: 3). Apart from the obliteration of the formal regulatory apparatus and institutions responsible for oversight of free market transactions, Shanghai's general support infrastructure was abysmal. As Jao notes (2003), 'when foreign banks and business firms were again welcomed back in the early 1980s, they found that even basic facilities, such as office buildings and telephones, were lacking." In a word, conditions were 'harsh' with Shanghai lacking 'decent housing . . . supermarkets, international schools, social clubs, cultural centres, [and] concert halls;' all the soft goods necessary to attract and retain pools of high-skilled human capital (Jao, 2003:29, 32).[6]

Shanghai's changing fortunes began in the late 1980s, spurned by a combination of political calculation and economic ambition. An emerging consensus in Beijing recognized the changing nature of the global economy and of China's need to integrate itself into the international commercial system with Shanghai 'deemed strategically important for China to succeed on the international stage' (Lai, 2006:4). Shanghai would again be China's window to the world. Subsequently, the city was nominated as one of 14 open coastal cities in 1984, partly reflecting its strategic location on the Yangtze river delta and its role as a transportation gateway to central and northern China. Not until 1991, however, was Shanghai's status cemented. Deng Xiaoping

[6] By contrast as Karen Lai observes, 'In its pre-1949 glory days, Shanghai boasted the most sophisticated urban amenities and cosmopolitan reputation outside of Tokyo' (Lai, 2006:3).

observation that 'Shanghai was a financial centre in the past and was the place where currency was convertible' and that 'in the future Shanghai should still be the same" (as quoted in Xu, 2007: 1), henceforth ear marked the city for special treatment and semi-autonomous political and economic rule. Shanghai's fortunes were now inextricably linked to Beijing's vision for China's rapid transformation. At the 14th Congress the city's central role in this vision was announced: to open 'Shanghai Pudong, and to build Shanghai as the dragon head and one of international economic, finance, and trade centres, so as to drive the growth of the [Yangtze] River Delta and in turn the take-off of the whole economic region' (as quoted in Lai, 2006:4; Xu, 2007:1).

The 11th Five Year Plan laid down the blueprint for Shanghai's re-development; a three phase strategy designed to grow Shanghai as a hub of trade, finance, tertiary services and transportation. In the first phase, Shanghai would establish and consolidate its role as a national financial hub and transportation gateway to central and northern China, a hinterland of some 800 million people. To achieve this, Shanghai would be insulated from intra-national competition and provided with national resources for the development of its physical infrastructure, most of which would be concentrated on the development of the 'Pudong New Area.' Within Pudong, four new zones would be developed, the most important being the Lujiazui finance and trade zone immediately opposite the Bund — the old city centre and former financial sector (Meyer, 2000: 234-235; Lai, 2007:7).[7] Allied with this, national authorities would roll out regulatory, institutional and liberalization measures to undergird domestic financial intermediation and financial sector development (Meyer, 2000: 234). Second, authorities would consolidate Shanghai's position as a regional financial hub through attracting ever greater numbers of financial services firms and multinational enterprise. As Wu (1999:214) notes, Shanghai was designed to become China's Wall Street, an 'international landing strip to attract foreign finance capital' (Lai, 2006:7). And third,

[7] The three other zones of the Pudong New Area consist of the Jinqiao Export Processing zone; Waigaoqiao Free trade zone and the Zhangjiang high tech park.

authorities would champion Shanghai's emergence as an international financial centre through the progressive consolidation of the sector.

Institutional and Regulatory Contexts of Shanghai's Emergence as a Financial Centre

Unlike Hong Kong, Shanghai's financial sector development has been a process of institutional, regulatory and market design from the ground up. Strict comparisons between the two cities are thus made difficult because of the low base from which Shanghai is emerging and because of the rapid change and innovation evident at all levels of the institutional-regulatory spectrum. Indeed, attempting to map the regulatory environment or the strategy and drivers undergirding Shanghai's financial centre proves a challenging task. Much of this is explained by the fact that Shanghai's financial sector development is not its own but reflects a national development strategy substantially controlled by Beijing. As Lai notes, this makes for a 'complex relationship between state and market imperatives in the urban and economic transformation of the city' with the state playing a 'key role in determining the timing, pace and economic and spatial configuration of Shanghai's development' but where market requirements and the practicalities of financial sector governance create tensions between national objectives and local needs. Adding to this mix is the 'rescaling of governance as greater financial and political power is transferred from the central state to the local municipal government' but in a process that is not always contiguous, consistent or predictable (Lai, 2006:2).

Despite this, the broad construction of market institutions and on-going financial innovation have been an obvious feature of Shanghai's rapid financial sector development. This commenced in 1990 with the establishment of the Shanghai Securities Exchange (at that time one of only two in China —the other located in Shenzhen) but under tightly controlled listing, trading and access rules that favored state owned enterprises (SOEs). Market participation was restrictive and onerous trading rules made for thin volumes with little scope for significant capital raising. Beijing

responded by creating an 'A' and 'B' share registry in 1991, allowing SOEs and large Chinese enterprise to tap foreign investor capital by issuing 'B' shares (to a maximum of 49% of total issued capital) while preserving Chinese majority ownership and managerial control. These initial efforts, however, did not produce the kind of rapid financial sector development Shanghai municipal elites had hoped for. Beijing 's historical xenophobia, concerns about a domestic political backlash as well as vested interests in the Chinese banking system, made for an often cumbersome and incremental approach to marketization that left numerous obstacles in place to foreign participation in the sector (Meyer, 2000). By the end of the decade, Shanghai's appeal as a financial hub thus displayed only modest success, with the city managing to attract 41 major international banks and 119 financial service firms — a mere 30% of the foreign banks then operating in China (Lai, 2006:9; Meyer, 2000; Wei, 1999).

After 2001 the pace of reform accelerated. China's entry into the World Trade Organization and an agreed timetable for financial sector liberalization combined with rapid growth in demand for more financially complex instruments and trading platforms, witnessed accelerated liberalization and market innovation. In quick succession, Beijing rolled out a series of market institutions such as the establishment of a foreign exchange trading centre, RMB bonds trading centre, inter-bank loans centre, as well as gold and futures exchanges. As a result, the city's market density was rapidly transformed, with Shanghai enjoying one of the most concentrated periods of growth and new business arrivals in its history. By 2007, for example, the number of financial institutions in the city had swelled to 563, including 105 major foreign banks while the number of registered firms with foreign capital increased to over 25,000 — up from 3,635 in 1992 (see Table 2) (Shanghai Statistics, 2008). Shanghai's contribution to China's national economy also grew, with the city now generating 5% of China's GDP, 8% of the nation's industrial output, and handling 26% of the nation's exports through its ports, while attracting 10% of all FDI into the country (Laurenceson & Tang, 2005:153; Shanghai Statistical Yearbook, 2007).

While market density is an obvious feature of Shanghai's financial sector development, the regulatory and institutional environment supporting its maturation is more confused. Regulatory obfuscation and a lack of regulatory transparency and continuity are marked features of the financial sector environment. As Jonathan Anderson, UBS's Chief Asia economist notes, 'we can't think of a single topic that raises more questions, misconceptions and debate than the state of the Chinese banking System' (Anderson, 2007). Much of this arises from the rapid rate of development of regulatory systems, where emerging mandates or juridical responsibilities have created institutional stresses, regulatory confusion or, in some instances, regulatory competition. Since 1995, for example, the Central Bank Law has progressively transformed the People's Bank of China (PBOC) from one of three banks in the country's pre-1979 mono banking system into its central bank. As a result, PBOC has been forced to shed its lending functions other than to commercial banks, restrict its commercial practices to trade in government bonds, and is no longer permitted to issue guarantees other than through directives issued by the State Council. PBOC's new mandate involves oversight of bank capital adequacy ratios, audit and compliance functions, oversight of payment, settlement and clearing systems, as well as determining interest rate policy. At the same time, however, PBOC enjoys only limited autonomy in the discharge of its regulatory mandate compared to its international counterparts. Despite its central bank status, PBOC continues to be directly accountable to the State Council where regulatory decision making and monetary policy is ultimately determined (Wei, 1999:38). Such a radical re-designation of the bank's role, functions and responsibilities, as well its circumscribed independence, have placed serious stresses on the bank's internal culture and capacities, creating political anomalies in the discharge of its mandate and raised questions about its regulatory effectiveness.

Further regulatory confusion has also arisen with the creation of the China Banking Regulatory Commission (CBRC) established in 2003 (Barth, 2007). The CBRC is charged with approval authority over new banking institutions, audit of financial service firms, the formulation of prudential rules and regulations, development of early warning

systems and the detection of risk in the banking sector. The juridical edges where PBOC's mandate ends and CRBC's begins is clearly blurred, creating what one senior executive with an American bank described as 'regulatory black boxes' where 'no one knows what the heck is going on and no one wants to make a decision because they don't know if they have the jurisdiction' (Interview, June, 2007). Further, CBRC displays a 'command and control' approach in its regulatory style, where black letter laws are issued regularly, much to the confusion of market participants. In the first 3 years from its inception in 2003, for example, the CBRC issued no less than 150 rules, or about one per week, leading one senior executive of a British bank to note that 'it's orchestrated chaos' (Interview, June, 2007; Ping, 2006). Indeed, a recent survey by PriceWaterhouseCoopers (PWC, 2007:23) of foreign banks operating in China 'ranked regulatory risk as the greatest threat' they face. As the PWC's report noted, of all the risks ranked, regulatory risk 'almost received the maximum possible score' (PWC, 2007:20).

Much of this regulatory uncertainty reflects competing political interests. Shanghai's elites, for example, generally reflect a modernizing impulse and are keen to use liberalization and greater foreign bank participation as a tool to rapidly transform China's banking system. While similar political forces can be found in Beijing, protectionist sentiments and fears about a loss of control and influence has created a regulatory culture that at times appears antithetical to the sponsorship of Shanghai as a financial centre. In 2006, for example, in revising upwards its foreign equity ceiling on domestic bank ownership to 25% (a maximum of 20% for a single foreign institution), the CBRC simultaneously introduced restrictive foreign incorporation rules, prohibiting non-domestically incorporated banks from taking individual deposits of less than Renmnibi 1 million —effectively cutting them out of the domestic retail banking sector (Garcia-Herrero & Santabarbara, 2008:2, 23). Such developments have reinforced a 4 tier banking system that discriminates between domestic banking institutions, locally incorporated wholly owned foreign banks (WOFB), joint venture banks (JVB) and foreign bank branches (FBB). While WOFB's enjoy full domestic access and operate

on a similar footing to domestic banks, in practice their branch and ATM networks are restricted by CBRC approvals processes, limiting their commercial discretion (see Table 3). Consequently, as late as 2006 there were only 4 WOFBs (HSBC, Citibank, Standard Chartered, and Hong Kong Bank of East Asia), indicative of the still restrictive regulatory environment operating in China (Johnston & Parker, 2007:31-33; Barth, 2007:2).

Many of these same anomalies are also apparent in the development of the soft – institutional structures, professional and technical networks, clearing and settlement systems as well as the information symmetries emerging around Shanghai's financial sector. Central planning and the introduction of a uniform accounting system adopted from the Soviet model in the 1950s disestablished professional bodies such as accountants, lawyers and actuaries, among others. Consequently, only as recently as 1988 was the Chinese Institute of Certified Public Accounts (CICPA) established, not until 1991 were CPAs certified through a merit based examination process, and not until 1997 did the 'General Standard on Professional Ethics' for CPA's come into effect (Narayan and Reid, 2000:41-49, 51).[8] However, the degree to which these professional bodies are emerging independently or developing organic capacity is problematic. The CICPA, for example, while ostensibly an independent body falls under the direct supervision of the MOF and all its policies must be approved by the MOF. These same strictures are in place for professional bodies in the legal, para-legal and actuarial domains with certification, standards and accreditation systems still overseen by state agencies.

These 'centralising' tendencies cast a long shadow over the emergence and possible growth trajectories of the city's soft institutional capacities, creating information asymmetries at odds with Shanghai's ambitions to become a global financial centre. Even the flow of financial data and information – the life blood of a financial centre and

[8] Prior to 1991 accounts were certified via peer evaluation based upon work experience and other localized practices that varied greatly from region to region (Narayan and Reid, 2000:41-49).

critical to market functionality – has remained a closely protected commodity with authorities exerting monopoly control and vetting approval over content. The Xinhau News Agency, for example, the official news agency of the Community Party, has been the sanctioned agency carrying financial data and information into banks, brokerages and other financial intermediaries. External or competitor agencies like Dow Jones, Thompson Reuters and Bloomberg have been frozen out through anti-competitive practices that saw Xinhau act as both regulator over the sector and a commercial actor in the sector (see also Wang, Zhou & Wang, 2007:110-112).[9] With the backing of Beijing, Xinhau's has used onerous disclosure and compliance standards and various regulatory hurdles to effectively gate foreign operators out of the market, in the process advantaging Xinhau and allowing it to become a price setter of domestic financial data but, as a consequence, increasing transaction costs for financial sector participants. While such practices are being redressed, they betray a bifurcated rationality that, on the one hand, sees Beijing promote Shanghai as an emerging financial centre but, on the other, belies a continuing legacy to centralize control in ways that are at odds with the emergence of soft-institutional capacities and information symmetries that reduce transaction costs or provide the ability for an intensely networked financial community to emerge.

Singapore

Singapore and Hong Kong enjoy an historical rivalry that can be traced back to their days as entrepôt trade hubs and their British colonial status. In many senses, their experiences betray a common history but played out in different geographic and

[9] Until May, 2009, all foreign financial data firms were required to work through a Chinese agent and disclose commercial information to Chinese authorities, in practice the Xinhua News Agency who acted as the regulator of news and information services in China. Under pressure from the WTO and complaints lodged by the United States, the European Union and Canada, Beijing agreed in February, 2009, to establish an independent regulator (the State Council Information Office -- SCIO). Under the new guidelines, foreign commercial providers of financial information will be required to apply to the SCIO for permission to operate. The SCIO have discretionary authority in the issuance of licenses and their cancellation. No guidelines have been issued concerning the requirements for licensees, cancellation, or rights of appeal. See 'Controls Relaxed on Foreign Financial data Firms' *South China Morning Post*, Friday, May 1, 2009.

political contexts (Tan & Kim, 2004:1). While Hong Kong's future has reverted back to the PRC via an interim political agreement designed to ensure the former colony some level of autonomy from Beijing, Singapore's fortunes have been entirely its own since its independence in 1965.[10] As Bryant (1985) notes, the fact of Singapore's independence singularly explains its subsequent efforts to generate a financial services sector and propel its growth through financial activity. As a small city state of some 239 square miles, Singapore enjoys none of the natural resources, agricultural capacities, energy or food security of its immediate neighbors. Its economy was and remains entirely dependent on its capacity to generate services and attract capital and investment. Singapore's development has thus been defined by these vulnerabilities.

In the late 1960s the government responded to these vulnerabilities by initiating a series of aggressive development policies, one important component of which concerned the development of financial services as a growth driver in its own right (Bryant, 1985:8). The intent was not simply to grow the domestic banking capacity of the city-state but to 'orient financial institutions in an outward direction, encouraging them to see their role as servicing an international rather than solely a domestic clientele' (Bryant, 1985:8). In the late 1960s, Singapore was advantageously placed to do this. A widening war in Vietnam and increased US dollar expenditures, made for tight credit conditions and widening spreads between interest rates in the Euro-dollar market and the US dollar. It thus became lucrative for banks to tap existing dollar reserves in the Asia-Pacific region, creating a natural inducement for foreign (especially US banks) to establish in Asia. Under the advice of the then senior Dutch policy advisor to the Singaporean government, A Wiinsemius, plans were drawn up to tap this trend and host an Asian Dollar Market (ADM). While Hong Kong was viewed as an attractive destination for such a market, the imposition of a 15% withholding tax on interest income from foreign currency deposits and the unwillingness of Hong Kong authorities to remove this, created an opportunistic niche for Singapore. Subsequently, Singapore began a process

[10] Singapore achieved independence from Britain in 1963 and merged with Malaya, Sabah and Sarawak to form Malaysia. Within two years, however, Singapore seceded from the federation and became an independent republic on 9 August 1965.

of liberalization, opening up its financial sector to allow the entry and establishment of foreign banks, the progressive liberalization of the exchange rate control (fully liberalized in 1978), as well as the establishment of a series of favorable tax incentives designed to pull-in foreign banks and financial service firms (Ng, 1998:1).

Central to these initiatives was the roll out of Singapore's first financial legislation in 1967 and then a full-fledged Banking Act (1970) which set in place the primary architecture on which Singapore's banking system would evolve. This was followed soon afterwards with the enactment of further legislation establishing the Monetary Authority of Singapore (MAS), in essence Singapore's central bank. Most significant among the first initiatives taken by the Singaporean authorities, however, was the authorization of separate departments within banks to administer specified international transactions, assets and liabilities. These were denominated as an 'Asian Currency Unit' (ACU), with ACU's permitted to book certain transactions that enjoyed favorable tax and regulatory conditions. Under MAS guidelines, ACUs could deal in any currency denomination except Singapore dollars and could nominate ACU accounting on any transactions stipulated by the MAS, including: flotation, underwriting, buying / selling of shares, bond issues, securities, investment portfolio management, advisory services on M&A's, structured finance, lending, discounting of negotiable securities, and issue promissory notes—among other activities (MAS, 2009).[11]

The authorization of ACUs initiated Singapore's offshore banking facility, creating separate accounting entities that discriminated between ACUs and Domestic Banking Units (DBUs) within banks. For Singapore, this had unique advantages, preserving the regulatory and prudential apparatus over domestic banking activities and thus the efficacy of national fiscal and monetary policy while creating facilities that would promote and capture an Asian Dollar Market (Bryant, 1985:10-11; Khee-Giap, *et al.*,

[11] DBU's deal predominantly in loans and deposits denominated in Singapore dollars. They are subject to more stringent guidelines, including strict liquidity and reserve requirements and higher rates of tax compared to ACUs. While ACUs are regulated by the MAS and subject to MAS oversight, they are exempted from several provisions of the Banking Act (1970), including reserve and liquidity requirements. ACUs also enjoy a concessional tax rate on transactions (Hew, 2002:4) .

2001:2; Ng, 1998:4). More immediately, the adoption of a two-tier banking system allowed Singapore to protect its then nascent banking industry from larger and more sophisticated international competitors, all the time encouraging their location in the city state and the development of its financial centre (Hew, 2002:3).

The first ACU was setup by the Bank of America in 1968 and proved so lucrative that by 1971 half of the existing banks in Singapore had set up ACUs. Indeed, the attraction of the ACU facilities led to an influx of foreign banks in the early 1970s, generating fears that Singapore's domestic economy would soon be 'over banked.' In response, the government and MAS created a new 'restricted bank' license, with operators allowed to engage in the full gambit of banking activities but prohibited from accepting domestic deposits of less than S$250,000 and restricted to one location with no sub-branching rights (Bryant, 1985:14; Bryant, 1989:345). The first 6 restricted bank licenses were issued in 1971, with licensees opening ACU facilities that dominated their balance sheets. The popularity of restricted license banks saw their number double in the space of two years, prompting Singaporean authorities to introduce a third category banking license to cope with the influx of foreign banks. The 'offshore license' enabled licensees to participate in the full gamut of activities approved for ACU activities but with its DBU activities greatly constrained by MAS guidelines. By the mid 1980s Singapore had issued 72 offshore licenses.

As an offshore financial centre, Singapore quickly established an unsurpassed reputation in the region for its efficiency and business friendly environment, attracting European and North American banks in ever greater numbers. In line with foreign bank arrivals, ACUs expanded rapidly with a total of 160 licenses issued by 1984. More importantly, asset volumes under ACU's enjoyed rapid expansion, growing on average by 22% during the 1980s and accounting for 66.2% of all assets of Singapore's banks by the early 1990s (Hew, 2002:4). As an indicator of the success of Singapore's financial centre, the relative ratio of ACU to DBU assets also expanded, growing from 28% in 1970 to a peak of 596% in 1987, with ACU assets reaching 11 times

Singapore's GDP. By the mid 1990s, Singapore had established itself as one of the leading financial centres in Asia, attracting 185 foreign banks and operating the fourth largest foreign exchange market in the world behind London, New York and Tokyo, propelled largely off the back of a highly successful ADM. Policy initiatives in 1983 introducing tax incentives for the establishment of offshore funds management also witnessed Singapore emerge as one of the largest regional centres for wealth management, while allied initiatives to nurture increased financial depth witnessed Singapore emerge as the fifth largest derivatives market and the world's fourth largest currency derivatives financial centre. By the 1990s, rapid economic growth throughout Southeast Asia uniquely situated Singapore, making it a financial platform for European and North American investment into Southeast Asia and, in the process, attracting 5,000 multinational enterprises operating regional treasury and financing operations in the city state (Hew, 2002:5; Tan and Lim, 2007). By the turn of the century, the financial services sector was generating fully 13% of Singapore's nominal GDP (up from 6% in 1970), provided the largest value-add of any sector in the economy and was responsible for the largest source of tax revenue (Financial Services Working Group, 2002:ii).

Institutional and Regulatory Contexts of Singapore Development as a Financial Centre

Bryant (1985; 1989) long ago made the observation of Singapore that it was unlike other countries in terms of its approach to financial sector management and development. The MAS, for example, while the central bank of Singapore and responsible for the conduct of monetary policy, issuance of currency, oversight of payment systems and acting as banker and financial agent for the Government, functions more as an arm of government than a standalone statutory entity. As Bryant (1985:11) observes, 'monetary and financial policies in Singapore are jointly formulated and coordinated with government budgetary policies and overall strategy for the development of the Singapore economy.' As the peak regulator, MAS is 'effectively controlled by the key political figures in the Singapore government' (Bryant, 1985, 11). The MAS board, for example, is drawn heavily from the ranks of cabinet ministers and

currently chaired by Senior Minister Goh Chok Tong (former Prime Minister of Singapore), creating direct linkages between cabinet, government policy agendas and the management and operations of MAS.[12] This is in marked contrast to regulatory models developed in other financial centres and reflects Singapore's singular approach to policy development, implementation and coordination; a model that might more appropriately be characterized as 'Singapore Inc.' Mapping the regulatory and institutional apparatus responsible for financial sector oversight as distinctive organs independent of government is thus inappropriate in the Singapore context; regulatory politics is a whole of government concern and intimately associated with Singapore's image and attractiveness as an investment destination. More obviously, the central importance of Singapore's financial centre to the city state's economic future makes it of central concern to all stratums of government economic planning.

The result is a highly technocratic approach to financial sector management and oversight but one that is not always transparent. As one senior banker with a European bank observed, 'when I first came here I could not work it out . . . they seemed to make decisions behind closed doors and announce outcomes without consultation . . . now I understand that they do consult but through soundings . . . not directly. It's very indirect here unlike in Europe' (Interview, June, 2008). Another senior executive with a different European financial institution opined that in Singapore it's 'not about transparency it's about not speaking and making a statement that might not be government policy . . . so you tend to get a lot of deferment up the chain . . . they are really concerned not to send out conflicting signals . . .' (Interview May, 2008). This has created a singular unity between government policy and the objectives of the regulator, with one Swiss banking executive observing that its simple here 'because

[12] The current composition of MAS's management board, for example, is comprised of Mr. Goh Chok Tong (Chairman), Senior Minister; Mr. Lim Hng Kiang (Deputy Chairman), Minister for Trade & Industry; Mr. Heng Swee Keat, Managing Director, MAS; Professor Walter Woon Attorney-General, Attorney-General's Chambers; Mr. Koh Yong Guan, Chairman, Central Provident Fund Board; Mr. Tharman Shanmugaratnam, Minister for Finance; Mr. Teo Ming Kian, Permanent Secretary, Ministry of Finance; Mr. Lucien Wong Yuen Kuai, Managing Partner, Allen & Gledhill; Mr. Lim Chee Onn Executive Chairman, Keppel Corporation Limited (MAS, 2009).

there is no confusion between what the regulator wants and what politicians want . . . it's a very efficient system' (Interview, May, 2008).

This same 'singular unity' infuses into the institutional fabric that permeates the commercial practices and norms supporting Singapore's financial centre. While Singapore has emerged an extensive series of professional networks, the sense in which they work independently of government or at variance to government is a moot point. The boundaries that divide government from civil society are blurred given the historical importance of the state to Singapore's economic development. Professional bodies and networks in the financial services sector thus tend to look to government for indicative referents by which to inform their practices and commercial norms. This creates a kind of formalism or culture of legalism that frames commercial practices in the financial services sector. Interviews with foreign bank executives in Singapore, for example, commonly highlighted a propensity to administrative formalism compared to a more intensely networked atmosphere in Hong Kong that draws upon trust relationships among professional networks. As one executive with a European Bank observed, 'when I worked in Hong Kong the atmosphere was more intense . . . here (Singapore) it's more cliquish and not easy to connect with information . . . here (Singapore) the government drives things but . . . in Hong Kong the place is driven by the commercial guys . . . (interview, May, 2008).

III: Race for the Money: Contest and Competition Among Asia's Financial Centres

The changing nature of Asia's economic landscape is perhaps most dramatically felt in the flows of fast moving money sweeping between Asian capitals. From the mid 1960s through the early 1990s, Japan dominated Asia's financial landscape, controlling upwards of 23% of global financial assets – the second largest in the world behind the United States. In more recent years, however, Japan's importance has diminished. While remaining the third largest financial market in the world after the United States and the Eurozone economies, its relative importance in Asia is in virtual free fall. By 2007, for example, Japan's share of global financial assets had declined to just 12% while its financial market assets of US$19.5 trillion are now almost equaled in the rest of Asia at US$18.8 trillion dollars (Farrell, *et al*., 2008:13,21).[13] Similarly, between 1990 and 2006 the intensity and depth of Japan's financial connections to the region and the rest of the world stagnated while the rest of Asia enjoyed deepening financial linkages. Singapore, Hong Kong and Taiwan, for example, 'now have larger cross-border investments with China and other emerging economies than does Japan,' and where Tokyo managed to attract just 4 overseas listings on its stock exchange between 2004 and 2007, Singapore by contrast attracted 40 (Farrell, *et al*., 2008: 62; Tucker, 2007). As Farrell observes, while Asia has enjoyed increasing financial linkages, Japan has essentially been 'shut out of Asia's financial integration ─ in part reflecting the fact that Tokyo's financial might is almost entirely domestically focused; its debt markets driven by government securities and its equity markets semi-protected by onerous regulatory measures (Farrell, *et al*., 2008; see also Kawai, 2008).

[13] The most recent 'Global Financial Centres Index' (2009) had Tokyo's position as an international financial centre falling by eight positions to rank 15th in the world. The indices measures attributes such as the business environment, human resource availability and capacity, regulatory and compliance requirements, market access, infrastructure provision and competitiveness (Global Financial Centres Index, 2009).

The erosion of Japan's regional financial hegemony signals an intensifying race to become Asia's next great financial centre. More obviously, it also underscores a series of competitive parameters that both validate much of the existing theoretical literature while also highlighting its limitations. Place and space, for example, continue to cast a long shadow as mechanisms that engender financial clustering and determine its spatial distribution. Shanghai's reemergence as Northern China's preeminent trade hub, for instance, has been one of the primary catalysts driving growth in the city's financial services sector. Not only does Shanghai benefit from its strategic geography on the Yangtze River Delta, but since the early 1990s has been the chief beneficiary of State Council initiatives to integrate the region economically and promote the greater Yangtze Delta as the primary growth driver of the Chinese economy. The Yangtze regional economic integration plan commenced in 2004, for example, is designed to create a 16 city metropolis centreed on Shanghai, integrating the eight cities toward the south of Shanghai in Jiangsu Province (Nanjing, Suzhou, Wuxim Chanhzhou, Zhenjiang, Yangzhou, Taizhou, and Nantonmg) and the seven cities to the north in Zhejiang Province (Hangzhou, Ningbo, Jiaxing, Huzhou, Shaoxing, Taizhou and Zhoushan), through the eradication of trade barriers and the development of an integrated transportation network (Xinzhen, 2009:34). By 2012, a high-speed expressway, inter-city bus and train network will provide a 'three-hour metropolitan circle with Shanghai as the core city'; effectively turning Shanghai into the transportation epicentre of a region servicing over 80 million people, generating 19% of the country's GDP, 25% of the nation's fiscal revenue and 37% of the nation's total exports (Xinzhen, 2009:32).

Clearly, Shanghai's reemergence as a regional trade and transportation hub is a major impetus to financial clustering, with growth in the financial services sector strongly aligned with growth in trade volumes, manufacturing and related commercial activities in the Yangtze River Delta region. While other countries have tried to launch their own financial centres (Labuan in Malaysia, Bangkok International Finance Faculty, Thailand,) the evidence of success in the absence of being located on or at the

intersection of a major trade route, provides a telling lesson.[14] All three financial centres analyzed here, for example, occupy a geographically strategic niche at the cross-roads of major trade routes, each services a large economic hinterland and each acts as a be-spoke transportation hub to the region and beyond. The clustering of financial services around such hubs, from maritime and logistical services, insurance, brokerage firms, clearing and settlement houses, banks, foreign currency exchange, accounting and other merchant support services, is thus intimately related to growth in trade, exports, and manufacturing activity. It is thus no coincidence that as global trade has increased, and East-West and intra-Asian trade deepened over the last 30 years or so, the region's major trade ups, Hong Kong, Singapore and Shanghai, have likewise also emerged as leading financial centres.

Yet it would be inappropriate to dismiss the emergence of these centres as purely an accident of economic geography. Place and space might be necessary conditions but by themselves they are not sufficient for the emergence or retention of financial clustering. Despite the continuing legacy of Japan's trade hub status and its financial size, its declining status as an international financial centre relates as much to the nature of its policy environment and the institutional architecture facilitating external linkages and commercial practices as it does the rise of competitor centres and a transforming regional economic geography. It is interesting to observe, for example, the high correlation identified in the 'World City Relational Data' and the distribution of Asia's international financial centres (World City Relational Data, 1997-2001). In virtually

[14] Labuan (Labuan International Business and Financial Centre) was established in 1996 and originally championed by the Malaysian authorities as an international financial centre. In recent years, however, it has emerged as a 'booking centre'(see Tschoegl, 2000:5) for a wide range of financial products including investment banking services, funds management, investment holding, insurance, fund management, trustee holdings, Islamic finance and company management. Despite the intentions of the Malaysian authorities, Labuan has not been able to emerge beyond its 'booking centre' status and grow into a fully functional international financial centre (see Jarvis, 2004). Indeed, this may reflect Labuan's increasing reliance on booking business as the mainstay of its revenues ─ an outcome that has not escaped examination by international agencies because of the transparency and probity of the business booked through Labuan. Recent assessments by the IMF, for example, have highlighted needs for Labuan and the Labuan Offshore Financial Services Authority (LOSA) to increase transparency, corporate governance standards, as well as revise standards associated with its supervisory practices (IMF, Labuan, Malaysia, 2004:18-21).

each of the indices (Global Network Services Connectivity; The Relative Centrality of Cities Based upon Air Passenger Travel [1977-1997]; World Cities and Global Firms; International Tourism Arrivals, [2007]; among others), the distribution, size and changing relative hierarchies between Tokyo, Singapore, Hong Kong and Shanghai display a common unity ─ indicative of the changing depth of regional and global linkages of all types that these cities display. In other words, as the degree of external linkages has increased and various restrictive measures limiting engagement have been eased, the hierarchal distribution of Singapore, Hong Kong and Shanghai as international financial centres has been positively impacted. The lesson is obvious: financial sector, trade and commercial liberalization and deliberative policy that deepens regional – global economic linkages is highly positively correlated to financial sector development and financial clustering. Geography thus remains important, but absent a policy framework that encourages cross-border financial transactions the opportunities for intermediation of regional and global capital flows is ultimately diminished.

Blunter data suggesting a similar conclusion can also be inferred from global indices measuring, for example, globalisation. The 'A.T Kearney / Foreign Policy Globalisation Index' (2005) analyses 16 separate measures indicative of external linkages and the degree of openness to foreign direct investment (FDI), trade, technological engagement and economic integration. Again, perhaps not surprisingly, Singapore ranks first, Japan 28 and China 51. While Hong Kong SAR is not ranked independently, similar indices measuring openness such as the 'Index of Economic Freedom,' ranks Hong Kong first and Singapore second, while Japan is ranked 19 and China 132 (Index of Economic Freedom, 2009). Likewise, indices produced by the World Bank (World Bank, Doing Business, 2009) analyzing the ease of doing business such as startup business and compliance requirements, credit availability, trade barriers and employment restrictions,

similarly rank Hong Kong and Singapore in the top 10 best performing countries while Japan and China perform less well.[15]

The point, of course, is not to highlight the merits of such indices or the rankings produced, but to suggest that the metrics used focus on important enabling policies, capacities, institutional and regulatory arrangements that are central to financial clustering and increasing financial density. More generally, it speaks to a convergence in those attributes and characteristics identified in the world cities and endowed capacities literatures; specifically, the panoply of environmental factors from infrastructure (telecommunications, air links and transportation, etc.), the regulatory environment, availability and sophistication of human resources, depth of information symmetries, intensity of professional, social and financial networks, and the role of market and commercial norms in reducing transaction costs, as critical attributes for the success of financial centres. Further, it highlights an obvious correlation; that those places that display the greatest depth and sophistication of soft institutional attributes and capacities also tend to be the most open, interconnected and globally-regionally network cities.

In Asia, where greater flux, fast changing economic geographies and where financial and commercial linkages are not as historically ingrained, this probably suggests a greater sensitivity in the region's financial centres to competitive changes in these endowed capacities. Indeed, this conclusion seems to be born out in interviews with various executives in financial services firms in Hong Kong, Singapore and Shanghai. Interview questions that asked participants about what they perceived the advantages of

[15] Other indices of openness produced by the World Economic Forum also place Singapore and Hong Kong in the top performing ranks for competitiveness, with Japan and China placing lower. See the World Economic Forum, 'The Global Competitiveness Report 2008-2009' < http://www.weforum.org/documents/GCR0809/index.html>. Rankings produced specifically on the competitiveness, stability and openness of international financial centres, such as the Global Financial Centres Index (2009), rank Singapore third and Hong Kong fourth behind London (first) and New York (second) < www.cityoflondon.gov.uk/economicresearch>. See also the discussion in Richard Common (2001) "Globalisation and the Governance of Hong Kong," Globalisation and Urban Government: New Perspectives on the Local Politics of Global City Formulation , paper presented for the 51st *Political Studies Association Conference*, Manchester, United Kingdom, April 10-12.

locating financial services firms in their current domiciles were frequently answered by reference to endowed capacities, including air transport links (Hong Kong, Singapore), language and communication issues (Singapore and Hong Kong), quality of infrastructure (Singapore and Hong Kong), rule of law and political stability (Hong Kong and Singapore), as well as instrumental factors like financial capacity and depth of financial markets (Hong Kong and Singapore). As one UBS commodities trader noted on moving UBS regional headquarters to Singapore from Hong Kong, 'transparent laws, geographical location, efficiency in shipping and its global view give Singapore an edge over countries such as Japan, which can be rather introspective (as quoted in Huiwen, 2008). By contrast, interview respondents in Shanghai frequently made reference to the absence of many of these endowed capacities, noting, instead, the growth potential of Shanghai as a regional financial hub, emerging capacities, improving infrastructure and increasing financial depth. Such responses confirm previous studies (see Tschoegl, 2000:12-14) and the implicit role such factors play in the location decisions of financial services firms, finance professionals and thus the prospects for financial clustering (see also Beaverstock, 2002).

These are important observations since they suggest that the contours of the current competition to become Asia's next great financial centre will rest predominantly in changes to the endowed capacities each of these centres display — and the degree to which they are able to sustain dynamic and innovative renewal of these capacities. They also suggest the magnitude of the difficulties involved in fostering the development of such capacities and the dexterity required through policy coordination to sustain them. Despite its methodical state-based policy and planning apparatus, for example, Japan's policy elite have stumbled, seriously compromising the future of Tokyo financial status. In South Korea, where the role of the state in directing development has historically enjoyed high rates of success, attempts to nurture openness and develop Seoul into a regional financial hub have stalled. And in Thailand, the experiments of the Bangkok International Financial Facility (BIBF) in the 1990s demonstrate the dangers of poorly

sequenced and poorly managed policy in an impaired policy environment.[16] For Hong Kong, Singapore and Shanghai, this points to a first mover advantage and increasing barriers of entry for prospective new participants to the contest. Yet, it in no way guarantees the continuing success of these centres or marks an end to the contest. As Sagaram and Wickramanayake (2005) note:

> The importance of financial centres in the Asia-Pacific is likely to continue . . . However, it is not easy to predict which specific factors will emerge as crucial for each centre, nor indeed which specific centre will emerge in a leading position. This will depend not only of the static comparative advantage of the different cities but also the dynamic competitive advantages created by their policies and strategies. Incumbents (such as Australia, Hong Kong, Japan and Singapore) will always have their own comparative advantage, but no lead is totally unassailable, as London found to its dismay in 1998 when ─ in the space of just a few months ─ Frankfurt snatched away the trade of German Bund futures (Sagaram & Wickramanayake, 2005: 21).

Likely Trajectories: Shanghai, Hong Kong and Singapore

These observations provide a means of assessing the likely outcomes of the competition between Shanghai, Hong Kong and Singapore to become Asia's next great financial centre. If policy dexterity, innovativeness, adeptness and the ability to respond quickly and with whole of government approaches are leading measures for financial centre growth, then Shanghai will likely prove the laggard. Ironically, this will be through no fault of Shanghai or the municipal leadership but through the inability of Shanghai to control its own destiny. Beijing remains a major obstacle to Shanghai's desire to

[16] States as diverse as Thailand, Malaysia, Korea (ROK), Australia, Taiwan and Indonesia, for example, have all set their sights on becoming a leading financial centre in the Asia Pacific. See, for example, "Taiwan Sets Sights to Become Financial Centre," The China Post, May 20, 2008 < http://www.chinapost.com.tw/business/asia/%20taiwan/2008/05/20/157258/Taiwan-sets.htm>; "Indonesia to Become Major Shariah Financial Centre: President" Europe News, March 2, 2009 < http://europenews.dk/en/node/20497>.

liberalize its financial services sector and implement policies aimed at speeding up the process of financial clustering and increasing financial density. Much of this derives from a cumbersome, opaque and inherently slow policy making process in Beijing, where a historically cautious and conservative culture among the senior party leadership and State Council make it difficult to get clear policy signals and directives on which to base policy development or set policy agendas. In the absence of definitive policy directives, Shanghai's municipal government can only wait, watch and anticipate when next Beijing will announce new initiatives, all the time scrambling to measure the consequences of these for its financial services sector.

Perhaps of more concern for Shanghai, however, is the fact that Beijing may not have made up its mind about what to do with Shanghai. To be sure, many of the signals that emanate from Beijing send assurances that Shanghai is the chosen city to become China's window to the world. As Liu Tienan, Vice Minister of the powerful National Development and Reform Commission (NDRC — China's preeminent policy planning apparatus with direct input into State Council) noted recently, 'Shanghai is the most qualified metropolitan city on the Chinese mainland to pursue the ambition of building international shipping and financial centres' (as quoted in Xinzhen, 2009: 32). But the debate is not settled. Beijing itself has ambitions to develop its already extensive financial sector, leveraging off the presence of leading national and international banks as well as a sizeable number of multinational enterprises. Guo Jinlong, Beijing's all powerful mayor, for example, has at various times promoted Beijing as China's natural financial capital, going so far in November, 2008, to participate and host a general assembly on energy and finance convened in Beijing, that spoke of developing Beijing into an international financial centre.[17] Importantly, as Mayor of Beijing, Guo Jinlong occupies a strategic position which, along with Beijing's Municipal Committee Secretary, exerts considerable influence in China's all powerful elite ruling body, the Politburo. It might thus be premature to assume that support for Shanghai to develop its

[17] See <http://tipcare.cn/_d269216179.htm>

financial centre will always be contiguous and forthcoming, or that Beijing will adjure to a 'single city' national plan centred on Shanghai as China's primary financial capital ─ Beijing could change its mind or simply vacillate, leaving Shanghai in the unenviable position of being a financial vicariate of Beijing.

Indeed, there are reasons to suppose this conclusion might gain poignancy. Immediately to the North of Beijing, for example, Tianjin has also been promoted by Beijing as a future financial centre. Like Shanghai, Tianjin is the only other municipality to have been afforded preferential treatment and favorable funding policies, indicative of Beijing's support to see the municipality develop its financial services sector. The Binhai District of Tianjin, for example, was the first to be granted dispensation by the State Administration of Foreign Exchange to engage in direct investment in overseas securities. Similarly, the China Insurance Regulatory Commission has allowed the district to engage in self-directed insurance reform and liberalization while State Council approved Tianjin's Port as China's largest free port (China Stakes, 2008).

All this points to a vexed and contradictory series of policy signals that could seriously hinder Shanghai's latitude to develop those capacities necessary for its financial sector. While Hong Kong and Singapore enjoy autonomous governance and can engineer whole of government responses to position their financial centres competitively, Shanghai struggles for autonomy and remains far from the seat of government and decision making. Where Hong Kong and Singapore can rely on the HKMA and the MAS who act as both regulatory and protector of their respective financial centres, Shanghai is forced to rely on the planning, oversight and regulatory capacity of the PBOC and the CBRC, who operate outside of Shanghai's political orbit and maintain only regional offices in the city and who are charged with national regulatory and financial sector oversight, compliance and enforcement and not, as such, the promotion of Shanghai's financial services sector. As Wang *et al.* (2005:116) notes, while observers bemoan the problems that Beijing creates through intervention in China's financial system, 'ironically, it is exactly the intervention itself that solidifies Beijing's

financial competence' and provides the city with a highly competitive edge over Shanghai. Beijing's agential power over all facets of China's financial system thus makes the city structurally important, pulling in national and international financial services firms whose location in Beijing reflects their attempts to manage and reduce asymmetrical information barriers by locating at the epicentre of decision making ─ with Beijing hosting the largest share of representative offices of foreign financial institutions in China (44%) while Shanghai accounts for only 25% (Wang *et al.,* 2005:114). Ironically, then, it is foreigners who probably have greater confidence in the assumption that Shanghai will be China's next international financial centre than do the Chinese or residents of Shanghai themselves.

As always, however, the signals out of Beijing continue to make for a complex environment. The announcement by Beijing on May 12, 2009, for example, that it would allow foreign companies to list on the Shanghai stock exchange reaffirms Beijing's support for Shanghai and raises the specter of Shanghai commencing international listings and IPOs (initial public offerings) in direct competition with Hong Kong.[18] For Hong Kong, this points to a longer term danger that threatens its viability as one of Asia's premier international financial centres. Hong Kong currently acts as the Mainland's preferred bourse for listing large numbers of Mainland enterprises (H shares). Indeed, Hong Kong has become increasingly reliant on its H share listings, in part reflecting its declining role in cross-border banking intermediation between Asia and the rest of the world and its increasingly role as an intermediator of FDI and portfolio investment into Mainland China. The HKEx, for example, now hosts some 141 H listings compared to only 8 international (non-Mainland) listings (Cheung and Yeung, 2007: 28; Leung and Unteroberdoerster, 2008:9).

Hong Kong's current competitive advantage, however, is inversely related to the immaturity, lack of depth of debt markets, perceived political instability and the

[18] BBC World News, May 12, 2009. The timing and precise details about the instigation of overseas listings on the Shanghai Stock Exchange have not been clarified at the time of writing.

political risk associated with Beijing's interventionism into the financial markets in the Mainland. If, as has been announced, Beijing moves to aggressively promote international listings on the Mainland in the Shanghai Stock Exchange, the arbitrage Hong Kong has traditionally enjoyed will begin to erode. The longer term fear for Hong Kong thus resides in it losing its current status as China's financial window to the World, as investors engage directly with Mainland financial centres. Indeed, it is these fears that likely prompted Hong Kong's recently announced transparency initiatives that aim to increase the frequency of reporting and disclosure practices of listed companies on the HKSx. These aim to more closely align the regulatory practices of Hong Kong with major bourses in the United States and Europe, creating regulatory synergies designed to facilitate increased overseas listings on the HKSE and, at the same time, lessen its reliance on H share listings (Global Financial Centres Index:5, 2009:17).

The extent to which Hong Kong's fears will be realized in the short term, however, are problematic. Hong Kong's financial depth, intensive social and professional networks and the sheer depth of its soft-institutional structures, creates comparative advantages that will likely linger for another generation. Despite rapidly developing institutions and regulatory systems and vast improvements in the capacity of agencies like the PBOC and CRBC in recent years, Shanghai lags well behind its southern counterpart. This may have been one of the reasons behind Beijing indicating its preference for Hong Kong to develop its offshore Yuan business ─ the only place outside of the Mainland permitted to do so (Huang, 2009). Whatever its intentions toward Shanghai, Beijing is equally aware of its limited albeit growing capacities. Hong Kong's will thus continue to benefit from this for the foreseeable future; indeed will likely prosper because of its financial capacity to aid China's immersion into global financial networks. As in the past, Hong Kong's continued fortunes will thus lie inextricably with the Mainland's, but only insofar as Hong Kong manages to steer a fine line between servicing Mainland financial needs while preserving its ability to define its own policy environment and pursue discretionary policies that competitively advantage its financial services sector.

Singapore, by contrast, faces a series of more diffuse issues. Historically, its role as a 'safety box' centre for capital in Southeast Asia has provided the city state with its comparative advantage and its engine of growth. For Singapore the trick lies in maintaining this but in an environment where 'safe box' banking will come under increasing scrutiny. At the G20 Summit in London in 2009, for example, the OECD placed Singapore on its 'grey list' of states that 'are committed to the international OECD standard on sharing information on taxes but not yet substantially implementing it" (OECD, 2009). The move prompted Singapore (May, 2009) to announce its intention to amend laws relating to its financial centre in order to meet OECD transparency and disclosure standards. Yet, in doing so, the regulatory arbitrage Singapore has enjoyed in its push to become the 'little Switzerland of Asia' and a centre of wealth management, will likely erode. Singapore will thus have to look elsewhere to sustain growth drivers in its financial services sector and in a sub-region where growth is robust but otherwise dwarfed by the intensity of financial activity occurring in Northeast Asia. All this points to a series of larger systemic problems facing Singapore and how to intermediate capital that increasingly will be drawn not to Southeast Asia but China.

While the 'safety box' appeal of Singapore will of course remain in a region that still faces political uncertainties (especially for its Chinese Diaspora in Indonesia, Malaysia and Thailand), sustained growth in its financial services sector will need to come from alternative specializations. Rather, the city state's role in debt raising, insurance, attracting overseas listings to its stock exchange, and banking intermediation between Asia and the rest of the world, will need to be deepened but in ways that go beyond relaying on organic growth in the global economy. The problem for Singapore lies in how to do this, especially in an environment which, as Maurice Tse notes, lacks a 'traditional free market culture' unlike Hong Kong that reduces 'the scope for financial and economic innovation in Singapore' (Tse, 2006:1). While Singapore's debt markets have grown impressively, for example, less impressive has been its ability to develop and innovate financial products and to originate financial instruments (Ferrell *et al*.,

2008:66). Yet, it is precisely in this domain where growth in Singapore's financial centre will need to come if its longer term viability and relevance to a fast changing region is to remain. For Singapore, as for Hong Kong, adroit policy that nurtures such an environment will prove all critical in the race to dominate Asia's financial landscape.

Table 1: Hong Kong Financial Centre: Banking Sector and Financial Sector Composition				
Sector	**Composition**	**Structure**	**Description**	**Regulator**
Banking	- 142 Licensed Banks - 29 Restricted License Banks - 30 Deposit taking companies - 82 representatives offices of foreign banks	Three-Tier system of deposit taking institutions: i). Licensed Banks ii). Restricted License Banks iii). Deposit taking Companies Designated as Authorized Institutions (AIs) and subject to the 'Banking Ordinance' AIs may operate as either locally incorporated companies or branches of foreign banks	Only licensed banks able to operate current accounts and accept deposits of any size / maturity Restricted license banks principally engaged in merchant banking & capital market activities; may accept deposits of any maturity above HK$500,000 Deposit taking companies predominantly owned by licensed banks; restricted to taking deposits above HK$100,000 with minimum maturity of 3 months	Hong Kong Monetary Authority (HKMA) AI's subject to the provisions of the 'Banking Ordinance' requiring them to i). maintain adequate liquidity and capital adequacy ration's; ii). Submit periodic statistical returns to HKMA; iii). Adhere to limitations on loans determined by the 'Banking Ordinance'; iv).seek HKMA approval for appointment of directors, chief executives, changes in governance Overseas which operate as 'branches' are not required to hold capital in Hong Kong and are not subject to capital adequacy rations or capital based limits in large exposures Depositors protected via 'Deposit Protection Scheme'
Foreign Exchange Market	Open (various participants and mediators: wholesale and retail)	Absence of exchange controls (free market) Linked to leading international foreign exchange markets around the world	Hong Kong operates an open foreign exchange market marked by the absence of exchange controls	Hong Kong Monetary Authority (HKMA) Settlement systems stipulated via the 'Clearing and Settlement Systems Ordinance" with specified settlement systems for

		Linked Exchange rate system of Hong Kong Dollar to US Dollar		specific instruments under the 'Central Moneymarkets Unit' of the HKMA. These include: : i). Hong Kong Dollar Clearing House Automated Transfer System ii). Continuous Linked Settlement (CLS) System iii).Euro Clearing House Automated Transfer System iv).US Dollar Clearing House Automated Transfer System v). Renminbi Clearing House Automated Transfer System
Debt Market	Open pool market	Daily turnover averages HK$48.4 billion	One of the largest and most liquid debt markets in the region.	Central Money Market Unit Service (CMU) established in 1990 under the auspices of the HKMA provides clearing and custodian system for the exchange of bills and notes
Money Market	Inter-bank Market Utilized by institutions at the wholesale level	Hong Kong Interbank Offer rate determined by supply / demand for funds between market players. Lead indicator of the price of short term funds		Hong Kong Monetary Authority (HKMA)
Equities Market	Hong Kong Exchanges and Clearing Limited (HKEx) (private listed company but empowered with listing approvals and registration, audit and compliance of register companies) Non restricted and open trading	- Securities Market - Derivative and futures Market	Comprised of a securities and futures / derivative market Provides full Clearing and Settlement Services, Depository & Common Nominee Services Trading Mechanism	Securities and Futures Commission (SFC): Facilitates and encourages participation in the Hong Kong Markets; formulates regulatory policy and compliance requirements; regulates approved share registrars; oversees investor

	platform subject to compliance with the rules and requirements of the HKEx Interlinked with various global bources to enable trades on multiple exchanges			compensation funds; responsible for transparency and rectitude of markets and information symmetries; works with the HKEx and clearing houses to ensure transactional efficiency, systems innovation and product development
Precious Metals Market	The Chinese Gold and Silver Market (founded in 1918).	Open platform subject to participant registration for clearing and settlement purposes	Enjoys key position in the international gold market	The Chinese Gold and Silver Exchange provides a trading place, facilities and related services to its members for gold, silver and precious metals transactions; establishes and implements rules and regulations, and normalizes precious metal transactions; oversees the transaction process, settlements and delivery arrangement; designs trading contracts and regulations, and to monitor the fulfillment and completion of the contract.
Asset management	Assorted wealth and asset management companies	Institutional fund management Portfolio management Personal wealth management Unit trusts and mutual funds	One of the largest asset management centres in Asia ; regional centre for portfolio management activity	Subject to oversight by the HKMA and normal listing / registration requirements.
Derivatives Market (Futures)	Hong Kong Futures Exchange (HKFE)and Stock Exchange of Hong Kong (SEHK) Derivatives market composed of four types of futures: i). Index futures; ii). Stick futures; iii). Interest rate futures; iv).	Transactions on the two exchanges cleared / settled via the Hong Kong Securities Clearing Company (HKSCC) and the Stock Exchange of Hong Kong Options Clearing House Company (SEOCH) and the Hong Kong Futures		

		Exchange Clearing Corporation (HKCC)		
Insurance	Open non restricted participation subject to approval of the Insurance Authority.	181 authorized insurers (90 incorporated in Hong Kong). Sector mainly composed of large, international insurance companies (retail and re-insurance).	Marine, aviation, insurance on structured financial products, retail, life, health; reinsurance	Office of the Commissioner of Insurance (OCI) heads Insurance Authority (IA). Mandated by the Insurance Companies Ordinance which allows for the prudential supervision of all insurance business operating in Hong Kong regardless of the place of inc OCI responsible for development of policy and prudential regulatory measures

Source: Hong Kong Monetary Authority; Leung, Cynthia and Olad Unteroberdoerster (2008), Hong Kong SAR as a Financial Centre for Asia: Trends and Implications. *IMF Working Paper* (WO/08/57), International Monetary Fund, March, Washington, DC.

Table 2: Evolution of Financial Services Sector in Shanghai: 1990 to 2007			
Financial Institution / Market Innovation	**Established**	**Content**	**National Market Share and or Status**
Shanghai Securities exchange	1990	Main capital market (equity, bonds) ; Shanghai Stock Exchange (SSE)	80% of total trading turnover of China
Shanghai Securities Exchange allowed to list 'B' shares	1991	Issued by large SOEs targeted at foreign investors, denominated in local currency but trades in US Dollars	B Shares limited to 49% of total issued capital of SOEs and other enterprises. Designed to tap the foreign investor market while maintaining Chinese control over SOEs and related enterprises
Foreign Exchange Trading centre	1994	Foreign exchange	Main vehicle for FX markets in China & Head office for national trading
Inter- bank loan centre	1996	Money market	National centre for interbank trading
RMB bonds trading centre	1997	Money market	National centre for bond trading
Citicorp enters retail banking sector in China	1997	Single branch in Bund, retail banking	Number of branches restricted by Chinese authorities and financial activities require approval
Foreign financial institutions allowed to conduct local currency business in renminbi	1999	Wholesale banking, structured products, limited retail banking	Only foreign financial institutions with branch assets above US$150 million allowed to operate
Shanghai Futures Exchange	1999	Rubber, copper / aluminum / fuel oil	60% of all futures trading volume in China
China joints World Trade Organization	2001		China agrees to timeframe for the liberalization of financial sector and greater foreign participation
Shanghai Gold Exchange	2002	Gold market	Only gold market in China

Note market service centre	2003	note transaction information and service	Principal note pricing system in China
Shanghai Municipal government announces Action Plan to develop Shanghai as an International Financial Centre (IFC)	2004		Plan consists of a strategy target of Five years for foundation building; Ten years for regulatory framework construction; Twenty years to realize status of Shanghai as an international financial centre.
People's Bank of China (PBOC) establishes a second headquarters in Shanghai	2005		PBOC recognizes emergence of Shanghai as the country's eminent financial centre.
Shanghai petroleum market	2006	Futures transaction	Only petroleum futures market in China
China financial futures Exchange	2006	Financial derivatives transaction	Only derivative market in China

Source: Adapted from Xu, Mingqi (2007), 'Building Shanghai International Financial Centre: Strategic Target, Challenges and Opportunities,' Paper presented at the PECC International Conference "Competition among Financial Centres in the Asia-Pacific: Prospects, Benefits, and Costs — Stumbling Blocks or Building Blocks towards a Regional Financial Community,' Westin Chosun Hotel, Seoul, Korea, October 16-16.

Table 3: PRC Banking System		
Bank Type	*Licensing Requirements*	*Restrictions*
Domestic Bank	Minimum paid in capital of RMB 1 Billion; minimum operating capital per branch of RMB 100 million	None. Subject to PBOC and CBRC prudential oversight
Wholly Owned Foreign Bank	Paid in and operating capital requirements same as domestic banks	Branch and ATM network subject to approval; licensing subject to previous FBB operation of 2 years; has to demonstrate profitability for license issue
Joint Venture Bank	Paid in and operating capital requirements same as domestic banks	As of end of 2006, restrictions of RMB business lifted as per the WTO time-line for liberalization
Foreign Bank Branch	Minimum capital requirement of RMB 300 million	Can only accept depositions of RMB 1 million and above

Source: Xiuying, Jan & Richard Lung (2007) "China's New Bank Regulations," *Asia Focus Newsletter*, May, Federal Reserve Bank of San Francisco

Table 4: Singapore Financial Centre: Banking Sector and Financial Sector Composition				
Sector	**Composition**	**Structure**	**Description**	**Regulator**
Banking	- 114 Commercial Banks - 33 Full Banks - 41 Wholesale Banks - 40 Offshore Banks - 50 Merchant Banks - 36 Representative Offices of Banks	Three-tier system of commercial banks: full banks, wholesale banks, and offshore banks.	Full banks provide the whole range of banking business approved under the Banking Act. Wholesale banks do not carry out Singapore Dollar (SGD) retail banking activities. They operate within the Guidelines for Operations of Wholesale Banks issued by MAS. Offshore banks can engage in the same activities as full and wholesale banks for businesses transacted through their Asian Currency Units (ACUs).	Monetary Authority of Singapore (MAS) The MAS is responsible for the regulation/ supervision of the banking sector: i). implementing monetary policy; ii). supervisor of the banking systems; iii). banker to the government; iv). banker to the banks; v).controller of international reserves; vi).issuer of currency; vii).issuer of banking licenses; viii).lender of last resort Merchant banks are approved under the MAS Act and their operations are governed by the Merchant Bank Directives.
Foreign Exchange Market	Open (after SGD was floated in 1973, banks were free to quote exchange rates)	Absence of exchange controls (free market) It follows a floating foreign exchange system and links Exchange rate system of SGD to US Dollar.	SGD is one of the 11 currencies in the Continuous Linked Settlement (CLS). This eliminates foreign exchange (Fx) settlement risk. The average Fx daily trading volumes reached to US$229 billion in October 2007 average daily Fx turnover reached US$231 billion .	Singapore Foreign Exchange Market Committee (SFEMC), sponsored by MAS. By 1 June 1978, Singapore has completely removed its exchange control regulations. SFEMC published *Singapore Guide to Conduct and Market Practices for Treasury Activities* as the standard and code of Fx market activities.
Debt Market	Debt securities include bonds, debenture, loan stock,	It is comprised of corporate debt market and	770 companies with a combined market capitalization of	Incentives have been given to financial institutions with

	NCDs and others.	Singapore Government Securities (SGS, inc. treasury bills, SGS bonds).	S$671 billion. SGS market counties to grow.	approved Bond Intermediary (ABI) status. The *Qualifying Debt Securities* (QDS) scheme was granted to investors.
Money Market	- Inter-bank Market - Discount Market The major participants in the market are commercial banks, merchant banks, money brokers and MAS.	All four discount houses are joint ventures by major local banks and foreign finance groups.	The interbank market refers to transactions among the banks. The basic function of Discount Houses is to accept short-term funds from commercial banks, and to a lesser extent from other financial institutions.	Monetary Authority of Singapore (MAS) Under the Banking Act, commercial banks are required to maintain accounts with MAS. The major instruments are: i). Treasury bills; ii).government stocks and bonds; iii). bills of exchange; vi). negotiable certificates of deposit.
Equities Market	- Primary market - Secondary market	Several methods to raise capital in the equity market: public issue, offer for sale, private placement, bonus issue and rights issue.	A primary market for issuing new equities, including shares. The secondary market, the stock exchange, is where these equities traded after flotation.	Companies that have raised equity capital through public subscription have to seek a listing on the Singapore Exchange (SGX).
Gold and Commodities Markets	Gold market is comprised of 2 major segments: - Spot market (including Loco London market and Singapore kilobar market) - Futures market Singapore Commodity Exchange (SICOM): trading of commodity futures (e.g. Rubber)	Companies, individuals, residents as well as non-residents are allowed to participate freely in. Gold bars of the light-weight class are also traded in the physical gold market.	SICOM maintains a computerized network that links the market makers and the brokers. All contracts are cleared through the Clearing House.	Committee on Rubber Trading (CRT) oversee the privatization of Rubber Association Singapore.(RAS)
Asset Management	The collective investment schemes (CIS) include the unit trust, money market fund, property fund.	Other financial institutions, such as banks and insurance companies, are	Recognized as one of the premier asset management centres in the Asia Pacific	MAS support for the asset mgt industry by introducing incentives:

	Alternative investment: Real Estate Investment Trusts (REITs), private equity, venture capital and hedge funds.	involved in the asset management.		i).enhancement to the tax exemption scheme for foreign investors; ii). Enhancement to the tax exemption of income of foreign trusts scheme; iii). Enhancement to the Designated Unit Trust (DUT) scheme. The listing of investment funds on the SGX-ST are required to follow the listing criteria.
Asian Dollar Market	Sources from central banks, government agencies, commercial banks and other financial institutions. Non-bank sources include MNCs, affluent individuals, and business firms involved in international trade.	In relation to the wider concept of international capital market. It is comprised of financial institutions borrowing and lending dollars and other currencies outside the countries of origin.	The market is an international financial market where institutions accept the deposit of hard currencies outside their countries of issues.	Financial Sector Incentive (FSI). ACUs are automatically granted the Standard Tier award for five years.
Derivatives Market (Futures)	Derivatives products composed of five types of futures: i). Equity index futures; ii). Interest rate futures; iii). Middle East Crude Oil (MECO) futures; iv). DRAM futures; v). Single stock futures	The SGX Derivatives Trading Division (SGX-DT) operates 2 trading systems: the open outcry and the Electronic Trading System.	SGX-DT has become a leading derivatives exchange in Asia.	Singapore Exchange Derivatives Clearing Pte Ltd (SGX-DC) performs daily clearing and settlement, and supervises delivery of contracts. It administers the Mutual Offset System (MOS). SGX securities trading rules ensure to reflect current market practices.
Insurance	- 151 Registered Insurers - 61 Direct Insurers - 28 Reinsurers - 62 Captive Insurers - 6 Authorized Reinsurers	Insurers may conduct insurance activities in Singapore as registered insurers, authorized reinsurers or foreign insurers.	Registered insurers are approved under Section 8 of the Insurance Act (Cap 142) to conduct life and/or general insurance business. Reinsurers without	The Committee on Efficient Distribution of Life Insurance (CEDLI) is appointed by MAS to improve the life insurance products. The direct general

		S$152.8 billion overall issuance volume	an operating presence in Singapore can conduct reinsurance business in Singapore as authorized reinsurers under Section 8A of the Act.	insurance brokers adopt the *General Insurance Code of Practice and the Guidelines*, jointly developed by the General Insurance Association of Singapore (GIA) and the Singapore Insurance Brokers Association. (SIBA)

Source: Monetary Authority of Singapore (MAS).

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