Approaches to 'Markets':
The Development of Shanghai as an International Financial Centre

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Abstract

This thesis opens up the black box of ‘markets’ by scrutinising the process of market formation and examining its complexities in the context of Shanghai’s development as an international financial centre. The financial markets in Shanghai are framed, understood and acted upon differently by the Chinese local and central governments, regulatory institutions, local and foreign financial institutions and transnational interests. The construction of a financial centre in Shanghai is thus not only an outcome of its own historical context and development trajectory but also intrinsically bound up with the interests and decisions of other agencies acting across spatial scales and negotiated amidst conflicts of interests and power struggles. Based on empirical research that includes field observations of financial markets development in Shanghai, archival research and personal interviews conducted with local and foreign financial institutions, and Chinese government and regulatory officials in Shanghai (with some conducted in London), this study focuses on the banking sector, the securities market and strategies of foreign banks as they negotiate between the local regulatory environment and market conditions and the wider context of their global operations and strategies. I examine the relationship between state institutions and global finance capital in Shanghai and tease out how these different ‘framings’ of markets are played out in Shanghai. In doing so, I critically engage with the concept of ‘markets’ and ‘from-plan-to-market’ economy to expose its multiple identities and conceptualisations and the contested nature of the ‘marketisation’ process. I also analyse the factors contributing to Shanghai’s success, identify future challenges and highlight the complementary roles played by Shanghai as a ‘business and commercial centre’, Beijing as a ‘political centre’ and Hong Kong as an ‘offshore financial centre’.

Keywords: Markets, finance, economic geography, state, regulation, power, Shanghai

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Contents

List of Figures

List of Tables

List of Common Abbreviations

BOC	Bank of China
BOCOM	Bank of Communications
CAS	Chinese Accounting Standards
CBD	Central business district
CBOE	Chicago Board Option Exchange
CBRC	China Banking Regulatory Commission
CIRC	China Insurance Regulatory Commission
CPC	Communist Party of China
CSRC	China Securities Regulatory Commission
EU	European Union
FDI	Foreign direct investment
FSA	Financial Services Authority
GDP	Gross National Product
GNP	Gross National Product
HKSE	Hong Kong Stock Exchange
IAS	International Accounting Standards
ICBC	Industrial and Commercial Bank of China
ICT	Information and communication technology
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IPE	International political economy
IPO	Initial public offering
LFTZ	Lujiazui Finance and Trade Zone
MOF	Ministry of Finance
MOU	Memorandum of Understanding
OCC	Open Coastal City
OFC	Offshore financial centre
PBOC	People's Bank of China
PRC	People's Republic of China
QDII	Qualified Domestic Institutional Investor
QFII	Qualified Foreign Institutional Investor
RMB	Renminbi
SAFE	State Administration of Foreign Exchange
SEZ	Special Economic Zone
SME	Small- and medium-sized enterprises
SMG	Shanghai Municipal Government
SOEs	State-owned enterprises
SSE	Shanghai Stock Exchange
TNC	Transnational corporation
SSF	Social studies of finance

Chapter 1

Introduction

> *Roller-coaster rides are not unusual for China's stock markets, which sometimes resemble a casino in Macau. What happened next, however, was decidedly unusual: investors in New York's equity markets woke up, saw that Shanghai had tanked, and had a collective heart attack: they sent the Dow Jones industrial average down more than 400 points [...] The drop in New York, in turn, fuelled fear in markets across Asia the following day, and suddenly investors were seized by visions of a rerun of 1997's "Asian contagion" [...] On Feb. 28, as this new outbreak of investor gloom spread, India's main stock index tumbled 4%, Singapore's dropped 3.7%, Japan's fell 2.9%, South Korea's lost 2.6%, and Hong Kong's slipped 2.5%. (TIME magazine, 28 February 2007)*

On 27 February 2007, Shanghai's stock index dropped 8.8 per cent and resulted in knock-on effects in stock markets around the world. This chain reaction demonstrated the increasingly influential place China now occupies in the minds of global investors. But while investors are aware of China's economic importance to the world, they are still confused about how to interpret a decline in Chinese stocks. The reaction to China's market swoon was clearly overwrought as all major stock markets bounced back within a week (including Shanghai's), but the event raised some intriguing questions about the role of the stock market in China's economy. Its limited participation by local and foreign investors, small market size vis-à-vis its huge economy and its minor role in company financing and assessment points to the effect of expectations and hyperbole more than the impact of actual market transactions on the stock exchange.

For the past 10 years, Shanghai has recorded double-digit overall annual economic growth and is at present seen as the most attractive place for setting up local control offices and production facilities by many transnational corporations (TNCs). Finance and foreign trade have been heavily promoted and it possesses

China's premier stock market and only foreign exchange centre. Since the early 1990s, Shanghai has been actively promoting investment in the tertiary sector with the backing of the central government. Foreign insurers were initially allowed to operate only in Shanghai, and all foreign banks currently licensed are located in Shanghai's Pudong New Area (the largest Special Economic Zone (SEZ) in China). The latter is a key initiative in developing Shanghai's international financial and business capacities. Within Pudong, the Lujiazui Finance and Trade Zone (LFTZ) forms the focal point of development. It is envisaged to be a revitalised central business district (CBD) for Shanghai, with particular emphasis on financial services, retail, real estate, business consulting and government services. In promotional materials, Lujiazui is envisaged to be the "Manhattan of 21st century Shanghai" (Yeh, 1996; Olds, 1997) and China's "Wall Street" (W. Wu, 1999: 214). The current frenzy of international interest surrounding Shanghai's urban and economic development and its international aspirations is not without basis. Expectations for Shanghai's future run high because of its illustrious history as a centre of trade and industry of national importance. It was one of the most cosmopolitan cities in the world in the early-20th century and the most advanced and important financial centre in Asia before 1949, particularly notable for its receptiveness to international capital and influence. Under the new orientation, Shanghai is targeted to be the new flagship city, connecting China into an increasingly integrated world economy.

A financial centre is an agglomeration of financial and service enterprises and corporate headquarters, particularly foreign ones. Other than providing retail services such as branch banking, a financial centre also provides expertise in high level financial and professional services that serve a much larger area on national, regional and even global scales, as evident in the presence of head offices of multinational financial and non-financial institutions. International financial centres typically develop as national centres that subsequently assume wider regional and global status from a rise in demand to service international capital transactions with increased international trade. Such growth requires that national centres expand their financial markets to include regional neighbours. Many international financial centres, therefore, gain their international status by operating at two levels of regionalism – subnational and supranational. In recent years, Shanghai is emerging as an important centre for financial activities within the Chinese economy. Can that influence extend to the supranational scale? How is this process of market formation implemented and interpreted by official and business communities in Shanghai? The translation and adoption of capitalist ideas and principles in developing financial markets in Shanghai is a highly complex and contested process. How is this process envisioned and implemented at the governmental level and how are the changes interpreted and acted upon by the business community?

Whether as an idea(l), a system or as economic practice, markets lie at the heart of capitalist societies but they remain one of the most elusive concepts within social sciences. In this thesis, I open up the black box of 'markets' by scrutinising the process of market formation and examining its complexities through the experience and context of Shanghai. The development of Shanghai as an international financial centre can be seen as part of a global process servicing finance capital but this conceals the complex reasons behind why such processes are taking *place* in Shanghai and at a particular point in time and space. The process of market-making in Shanghai and the actors involved are also spread across scales and much of what is happening within the city is determined by economic, social and political considerations elsewhere on the national, regional and global levels. The financial markets in Shanghai are framed, understood and acted upon differently by the Shanghai municipal government, the central government in Beijing, local financial institutions, and foreign financial institutions in Shanghai within the wider context of their global operations and strategies. Transnational interests and roles of organisations such as the World Trade Organisation (WTO) and agencies in other financial centres such as the City of London are also important actors in this process.

The actors listed above are many and varied in terms of their institutional capacities, financial clout, regulatory power and geographical location. This recognition of the variety of actors and interests within a market setting and an emphasis on power, conflict and negotiation is central to my analysis. The form, structure and pace of market formation taking place in Shanghai is a contested process that has to be negotiated amongst the different interests of ‘incumbents’ and ‘challengers’ (Fligstein, 2001), involving a variety of actors including local and foreign firms, national and local state bodies, foreign state institutions and transnational practices. The dominant ‘mode of exchange’ (Lie, 1992, 1993) that emerges in Shanghai is the outcome of a conflictual process between multiple parties but is also itself constantly ‘under threat’ due to shifting agendas and contexts. Markets are understood and experienced by actors in a variety of ways, invested with different meanings and acted upon according to different interests and contingent social relations (see, for example, Zelizer, 1988, 1993, 1994). This discursive construction of markets has material consequences in affecting policies and practices. The central Chinese state and Shanghai government have particular understandings and visions of financial markets in Shanghai; the local and foreign financial institutions in Shanghai are also ‘framing markets’ according to their own interests, agendas, experience and interpretations of what a market *should* be. How are these different 'framings' of market played out in Shanghai?

In this thesis, I use the term 'marketisation' to refer to the on-going process of instituting market-led practices into the Chinese economy. I do not take 'marketisation' to refer to an unproblematic and progressive journey from centrally-planned to market economy. Rather than the wholesale adoption of neoliberal market practices and principles, the Chinese state continues to exercise considerable control over the pace and structure of reforms with clear political and social objectives in mind. My placing of the word in inverted commas is intended to highlight its unique conceptualisation and utilisation by the Chinese state and institutions and to distance myself from the conceptual baggage of 'West is best' often implicated in popular discourse about market-based economies and practices. This process of 'marketisation' is complex and highly contested at various levels. Regulatory changes, technological innovations and the globalisation of markets and monetary flows are remapping the financial landscape towards deterritorialisation, but states remain important arbiters in determining the shape and speed of such processes. The state and its institutions continue to exert significant influence within their national space economy as well as on the international arena through channels of supranational organisations (such as the International Monetary Fund (IMF), the European Union (EU) and WTO). The case of China's journey towards 'marketisation' in its financial sector reforms demonstrates this complex and fluid relationship between states and finance capital.

In acknowledging that markets are the products of social relations that vary across time and space, empirical research needs to examine how financial markets are being constructed, regulated and reproduced. Who are the actors involved in the making and maintenance of a market? What are the historical, social and cultural factors affecting these processes and in what ways? Whose vision of 'market' is more persuasive and what happens when different visions collide? In this dissertation, my objectives are as follows:

1) To critically engage with the concept of 'markets' and 'from-plan-to-market' economy, exposing its multiple identities and conceptualisations and the contested nature of the 'marketisation' process;
2) To analyse the development of regulatory frameworks and 'market' practices in China, focusing on the actors involved, their interpretations and agendas, how power is exercised, and the process of contestation and negotiation.
3) To analyse the different perspectives of foreign and Chinese actors in the banking market, examine how and why they might hold different views on the pace, structure and direction of financial sector reforms and their business strategies in response to such changes.
4) To evaluate the development of financial centre capacities in Shanghai and implications at different geographical scales (e.g. for Shanghai, the Chinese economy as a whole, the wider East Asia region and the global financial space-economy)

These processes will be examined through the lens of Shanghai's experience and aspiration to become an international financial centre. In particular, I focus on the development of the Shanghai stock market and the strategies and experience of local and foreign financial institutions (mainly commercial banks) located in Shanghai to examine how contested visions of markets are negotiated in the process of instituting market reforms in the capital markets and banking market.

The next chapter (Chapter 2) provides the background to current developments in Shanghai. The changing roles of Shanghai within the national economy and its history in the early-20th century in particular, are vital to understanding Shanghai's current aspirations and in contextualising the perspectives and strategies of officials, regulators and the business community located in the city and elsewhere. The development of the Lujiazui Trade & Finance Zone in Pudong is also significant in signalling the central government's commitment to developing the financial sector in Shanghai and confirms Shanghai's status as a 'dragonhead' to link China to the global economy and serves as a gateway through which foreign investors are permitted to enter the Chinese market.

The experience of Shanghai as it develops its financial markets and pursues the coveted status of international financial centre offers exciting opportunities to (re)examine various theoretical issues within geographies of money and finance, the global cities literature, and, in particular, the concept of 'markets'. Chapters 3 and 4 consist of literature reviews of different approaches to conceptualising global financial flows and framing markets, and through which I develop the theoretical basis of this thesis. In Chapter 3, I highlight the contribution of the *political economy* approach in emphasising the interconnectedness of economics and politics across international as well as national scales, and argue for an analytical approach that embeds local phenomenon within an international context, emphasising flows, interconnectivity and power. At the same time, I am also keen to emphasise the *social and cultural embeddedness* of finance capital and financial markets as the world of money is discursively constructed through particular social-cultural practices. To do so, I focus on four main areas of existing research on money and the international financial system, the state and finance capital, the making of international financial centres, and framing markets. The latter is taken up more fully in Chapter 4 where I further develop my theoretical framework by focusing on the meanings and treatments of ‘markets’ and how that might affect the lenses through which we analyse economic processes and phenomena. To do this, I consider the lineage and contributions of identifying and theorising markets in fields such as orthodox economics, economic sociology, political economy, economic anthropology, social studies of finance and economic geography, and I argue for an actor-focused, contextual, socialised and political approach to framing markets. I then combine some of the key insights from these approaches to inform my empirical research into Shanghai’s financial markets and, in turn, to reflect on the implications for issues of power, states and market formation.

In Chapter 5, I present the choice of research instruments used in this empirical study as well as elaborate on the process of research practice, such as how the topic evolved, its ongoing and dialogic character, and the way the project changed in the process. The research themes and empirical work of this thesis were derived and conducted in a circular rather than linear fashion, as is often assumed to be the case, and my reflections on the research process highlights this. The research methods employed are predominantly qualitative in nature, comprising archival/library research, analysis of secondary data (e.g. press releases, news articles, government/official reports, and industrial publications), in-depth semi-structured interviews and the maintenance of a field journal. At the end of the chapter, I also comment on issues of research practice and positionality, paying particular attention to how my complex ethnic identities have influenced the fieldwork process and possible implications for the resultant analysis and claims of this study.

In Chapter 6, the first of three analytical chapters, I examine how the state, through government institutions and regulatory bodies, manages tensions between the desire to maintain regulatory control and the various imperatives of global finance capital. China's approach to the 'marketisation' of its finance sector has been fairly conservative and remains tightly controlled by the state. However, there are also clear indications of international influence and cooperation with regulatory counterparts in the City of London, New York, Hong Kong and Singapore, the influence of global institutions such as the WTO and the involvement of foreign financial institutions in Shanghai in pushing for reforms. I examine how particular knowledge networks are constructed to build up the expertise and skills required for the legal and regulatory frameworks needed by Shanghai in building its financial markets. The case of China's WTO accession illustrates the tension between the imperatives of the state and international pressures. Specific regulations and 'sociological power' are also used to control the activities of foreign banks in Shanghai and thereby the pace of 'marketisation'.

In Chapter 7, I focus on the development of the Shanghai stock market and the strategies and experience of foreign banks in Shanghai to examine how contesting visions of markets are negotiated in the process of instituting market reforms. My objective is not to point out its 'peculiarities' or simply present a 'stock-market-with-Chinese-characteristics' but to highlight the process of market reforms in which the structure and meaning of 'market' in the context of the Shanghai stock market evolves through contingent social relations amongst market participants. I also highlight the implications of scalar politics as much of what is happening in Shanghai is arguably the outcome of political and economic processes elsewhere, with institutional forces in Beijing still determining the pace and process of ‘marketisation’ in Shanghai, and the influence of the international business community on developments in Shanghai depending on how Shanghai (or China as a whole) fits into their globalisation strategies. The experience of foreign banks in Shanghai, the history and strategies of their involvement, relationships with their global headquarters and other (local and foreign) banks in Shanghai is used as a window through which to gain insights into the process of instituting market reforms in China’s banking sector.

In Chapter 8, I focus on why this particular process of market formation and reforms are taking *place* in Shanghai. Based on the insights and experience of regulatory authorities, local government and foreign and local financial institutions, I examine the key factors influencing the development of Shanghai in its financial centre aspiration to date and future challenges. Beijing and Hong Kong are commonly seen as other competing regional centres for the title of international financial centre for China. I assess their comparative advantages and place-based characteristics and their influence on Shanghai’s role in national and global financial services and flows. I then identify the most pressing issues faced by Shanghai that need to be addressed in order for Shanghai to capitalise on its advantages and achieve its aspiration, which will be of particular interest to policy makers and planners.

The final chapter (Chapter 9) summarises the theoretical and empirical strands of the thesis, situating this research within broader debates in geographies of money and finance and the literature on ‘markets’ in the social sciences more widely. I also reflect on the major strengths and weaknesses of the research as a whole and suggests ways in which it might be extended empirically, to include comparisons and co-analysis with other Chinese cities and international financial centres, and theoretically, through developing a research agenda centring on the complex and contested nature of market formation and issues of global standards and governance. By engaging with existing literature on ‘markets’ and empirical research in Shanghai, I aim to draw economic geography into the debate and explore the contribution of a spatial perspective on the market in understanding financial centres and global capital flows.

Chapter 2

The Transformation of Shanghai:

From 'Paris of the Orient' to 'New York of Asia'?

2.1 INTRODUCTION

The current frenzy of international interest surrounding Shanghai's urban and economic development and its international aspirations is not without basis. Expectations for Shanghai's future run high because of its illustrious history as a centre of trade and industry of national importance. It was Asia's most significant financial centre prior to 1949 and was notable for its receptiveness to international capital. Following the implementation of the Open Door policy by Deng Xiaoping in December 1978, China's economic development has captured intense international interest. In the economic reforms that followed to develop China's internationalisation strategy, Shanghai emerged as one of the key cities of national strategic importance for China to achieve its development objective. Apart from rapid urban and infrastructural changes, the industrial and financial structure of the city has been dramatically transformed over the past two decades. There has been much discussion around the (re)emergence of Shanghai as a world city (Leman, 1994: 86-87; Thant et al., 1998; Yusuf and Wu, 2002; Zaloom, 2003; Ng and Hills, 2003) and in a recent comparative study of prominent Asian Pacific cities such as Tokyo, Hong Kong, Singapore and Taipei (Ng and Hills, 2003), Shanghai was specifically included as "a rising star in the reforming socialist market economy of China" (p. 155). This chapter explores Shanghai's history as the 'Paris of the Orient' at the beginning of the 20th century, its subsequent development during the post-1949 reforms and the remaking of the city into an international economic, financial and trade centre since the early-1990s. Knowledge of Shanghai's historical roles and development trajectories enables better understanding of its current position in the context of national economic development and its global aspirations, and this provides a sound basis from which to analyse the actions and perspectives of the different actors and interest groups both within and outside of Shanghai.

As with other cities in China, the development of Shanghai is closely tied to the country's national development strategy. A large proportion of the recent literature explores the complex relationship between state and market imperatives in the urban and economic transformation of the city (see, for example, Ho and Tsui, 1996; Yusuf and Wu, 2002; Zhang, 2003). While the state plays a key role in determining the timing, pace and economic and spatial configuration of Shanghai's development, market considerations feature prominently in the decision-making process. Moreover, the role of the state in the recent development of Shanghai is rendered more complex by the rescaling of governance as greater financial and political/institutional power is transferred from central state to local municipal government in the process (Thant et al., 1998).

In the next section, I outline the changing roles of Shanghai as it moves form being a 'bridgehead' to a 'locomotive' and then 'dragonhead' of China's economy. The development of Pudong New Area and especially LFTZ were pivotal in the transformation of Shanghai into an economic and financial force. Section 2.3 focuses on Pudong's conception, development and international reception. In section 2.4, I outline some of the key financial reforms in recent decades and Shanghai's ambition to be an international financial centre for China and the wider region.

2.2 THE RISE AND FALL OF SHANGHAI: FROM 'BRIDGEHEAD' TO LOCOMOTIVE' TO 'DRAGONHEAD'[1]

> *Shanghai used to be a financial centre where people exchanged currency freely, and it should continue to serve as the centre. To attain an international seat in banking, China has to rely on Shanghai first. (Deng Xiaoping in 1992; quoted in Olds, 1997)*

> *Between 2000 and 2010 we want to turn Shanghai into a financial and trading centre of the Asian and Pacific region. Our objective is to achieve complementarity with other regional financial centres. (Shanghai Mayor Huang Ju in 1993, quoted in Olds, 1995: 111)*

2.2.1 Shanghai as 'Bridgehead'

Shanghai is located at the estuary of the Yangtze River, one of the richest agricultural areas in China (the Yangtze River Delta accounts for about one-third of China's population and 40 percent of its GDP), and its development has been linked to its history as China's largest seaport (Figure 2.1). Shanghai had always been prominent amongst other Chinese cities due to its size (with a land area of 6,340 square kilometres), population density (more than 22,700 persons per square kilometre in the central city) and its importance to the national economy (accounting for more than 5 percent of national industrial output) (Yusuf and Wu, 2002: 207).

[1] These three metaphorical periods of Shanghai's development are identified in F. Wu (2003).

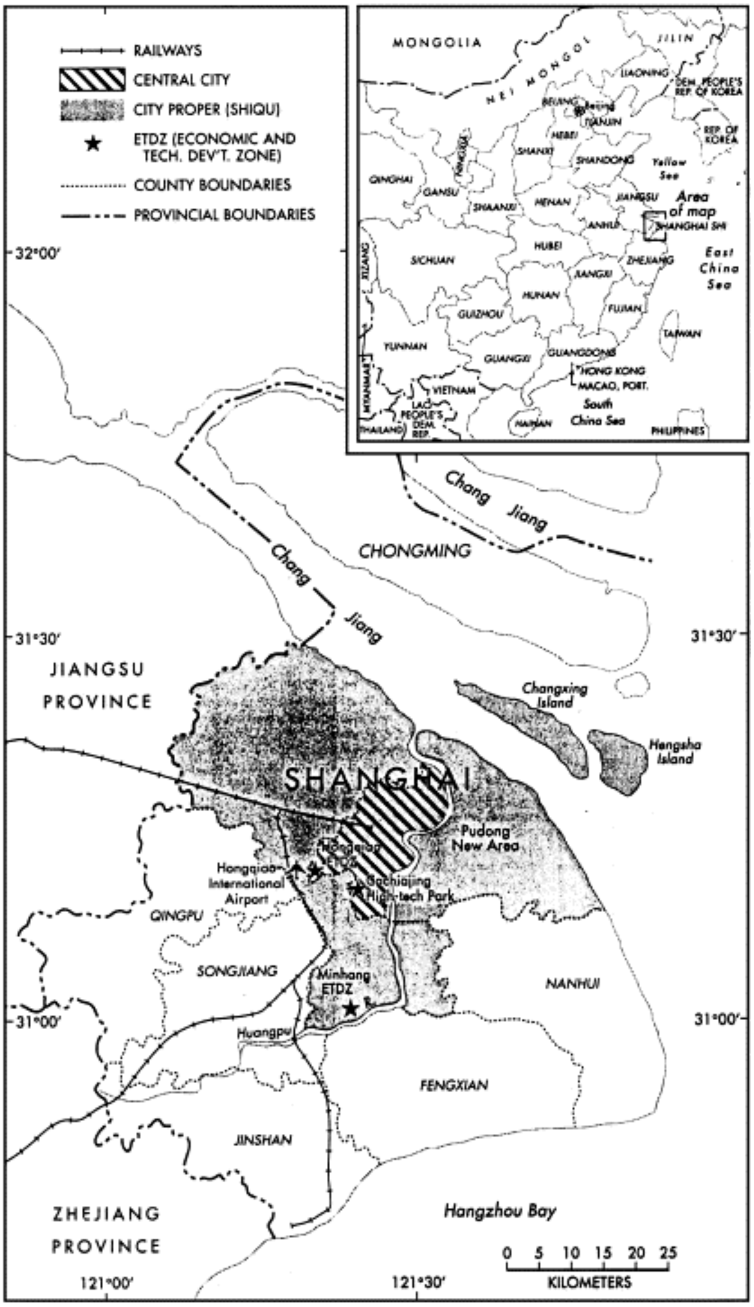


Figure 2.1 The Shanghai metropolitan area. *(Source: Yusuf and Wu, 2002: 208)*

First established as a fishing village in the tenth century, Shanghai became a county in 1271. Merchant families from nearby Ningbo (in Zhejiang province) were instrumental in transforming the city into an integral part of the coastal trading system and Shanghai developed steadily into an important regional commercial centre, such that it surpassed Guangzhou (Canton) as China's premier trading city by

1853 (Yusuf and Wu, 2002). Often called the "crucible of modern China" (Yusuf and Wu, 2002), Shanghai entered the stage of modern commercial and industrial development in the second half of the 19th century. After it was named one of five open cities, provided by the Treaty of Nanking in 1842 following the Opium War, Shanghai was opened to Western trade and residence.[2] The British, which subsequently governed a large part of Shanghai, ran the city according to mercantile principles and Shanghai's location at the mouth of the Yangtze River made it the chief conduit for trade to and from China's interior. The combination of Western capitalism, Chinese entrepreneurialism and strategic geographical location produced more than a century of unprecedented and dramatic growth for the city. The result was startling as Shanghai rapidly transformed itself from a small town into a thriving and leading international metropolis. It developed vibrant commodity, stock and foreign exchange markets, with nearly 30 percent of the world's most important foreign banks setting up branches there by 1935 (Yatsko, 2001: 56). It became the largest international financial centre in the Far East with 28 foreign bank offices, 58 headquarters of domestic banks and 182 branches. About 90 percent of the nation's financial assets and over half its foreign trade were concentrated there (F. Wu, 2000b). By 1936, Shanghai was the seventh largest city in the world with a population of 3.81 million (Y. Yeung, 1996: 2). In its pre-1949 glory days, Shanghai boasted the most sophisticated urban amenities and cosmopolitan reputation in Asia outside of Tokyo (Figures 2.2 and 2.3). It functioned as a 'bridgehead' during this

[2] During the late-18th and early-19th centuries, the British and other European traders were importing expensive tea and silk from China but the Chinese had little interest in Western products. Faced with a significant and growing trade deficit, the British discovered opium and started to export to the Chinese market in 1820. By the 1830s, opium had become a vice in China. Stocks of British opium were seized and publicly destroyed by the Chinese government in 1839, which sparked off British hostilities. The Opium War lasted from 1840 to 1842 with the Chinese army defeated and the signing of the Treaty of Nanjing. Under the treaty, the Qing government was forced to pay reparations for the destroyed British opium and war costs, Hong Kong Island was ceded to the UK, and the Treaty Ports of Guangzhou, Xiamen (Amoy), Fuzhou (Foochow), Shanghai, and Ningbo were established.

were imported and agricultural

2002: 1681-1682).

Figure 2.2 Prosperous Nanjing Road in the 1930s *(Source: Author's own photograph of display at Shanghai Development Museum)*

Figure 2.3 The first Western system for goods exchange was the Shanghai Stocks and Goods Exchange founded in 1920. This is a recreation of the Shanghai Wheat Exchange in 1921 *(Source: Author's own photograph of display at Shanghai Development Museum)*

2.2.2 Shanghai as 'Locomotive'

Development in Shanghai after the establishment of the People's Republic of China (PRC) in 1949 was radically different. Shanghai's new role in state socialism has been described as that of a 'locomotive' of state-led industrialisation (Yusuf and Wu, 2002: 1682-1683). The development of Shanghai was associated with the state's new priority of developing national defence capacity via industrialisation. Its role therefore changed from that of a trade, finance and distribution core to that of an industrial city. During the first three decades of Communist rule, Shanghai was officially viewed as problematic due to its former capitalist success; it was viewed as an unwelcome legacy of a humiliating and resented semi-colonial past. Skilled labour, goods, tools and even whole factories were relocated from the city to assist the development of new inland industrial centres and Shanghai subsequently grew more slowly than in the past (Murphy, 1988: 158). Nevertheless, Shanghai became one of the largest industrial bases in China during the post-revolutionary period. In the 1970s, Shanghai's industrial output accounted for more than 10 percent of the national total and contributed more than 15 percent to national fiscal revenue (F. Wu, 2000a: 350).

Despite its significance to the national economy, Shanghai did not particularly benefit from early economic reforms which sought to address regional imbalances between urban and rural regions. In 1979, when the post-Maoist reform programme first started, and with the designation of four SEZs (Shenzhen, Zhuhai, Shantou and Xiamen), central government policy emphasised the development of Guangdong and Fujian in the south. Although Shanghai was one of the 14 Open Coastal Cities (OCCs) designated in 1984, which were granted some of the special policies available to SEZs, its financial power in generating revenue for local development was still very limited. Thus, while cities such as Guangdong and Fujian enjoyed the benefits of the open-door policy with preferential fiscal contracts with the central government and experienced rapid economic and urban growth, Shanghai, on the other hand, experienced only modest growth during this period. Its ranking and share in the national economy fell rapidly during the reform period as its economic dominance was increasingly challenged by other thriving coastal provinces. On the list of China's top contributors to national income, Shanghai fell from first place in 1978 to sixth in 1985 and to 10^{th} by 1990. Compared to other fast-growing provinces in the 1979-1989 period, Shanghai's growth rates in national income was considerably lower and below the national average (Table 2.1). In summary, despite the reform programmes, the city remained a major manufacturer of industrial products, ranging from steel to chemicals to domestic electrical appliances, although it was being overshadowed by the emergence of new industrial bases.

Table 2.1 Percentage growth of national income in selected provinces, 1953-1989

	Shanghai	**Shandong**	**Jiangsu**	**Zhejiang**	**Guangdong**	**National average**
1953-1978	8.7	5.7	5.6	5.6	5.3	6.0
1979-1989	7.6	10.4	11.0	12.8	11.6	8.1
(Source: Cheung, 1996: 53)						

Various studies also alleged strained relations between Shanghai and the central government due to the unfair distribution of revenues (Cheung, 1996; Ho and Tsui, 1996; Lam, 1996). Between 1949 and 1983, as much as 87 percent of Shanghai's revenue of RMB 350 billion was remitted to Beijing, leaving only 13 percent for its own use (Cheung, 1996: 55). This contrasts with the average of 30 percent available for local spending in cities like Beijing and Tianjin (Lam, 1996). Consequently, Shanghai was often described as the 'cash cow' of the planned economy during this period (Ho and Tsui, 1996; Thant et al., 1998; Zhang, 2003).

Some scholars believe that had Shanghai kept the revenue for its own development, it would have been on par with Hong Kong or Singapore in terms of economic strength and standards of living (Thant et al., 1998).

2.2.3 Shanghai as 'Dragonhead'

The reversal of Shanghai's fortunes did not come about till the late 1980s, when the need to expedite the opening and development of Shanghai's economy was declared by Deng Xiaoping, the architect of China's economic reforms. In particular, a consensus emerged in Beijing that China must prepare itself for a globalising world economy and Shanghai was deemed strategically important for success on the international stage. The re-globalisation of Shanghai was of national significance from the onset, and the role of the central government was instrumental in the level of economic freedom and preferential policies granted to the city in the 1990s (Cheung, 1996; Thant et al., 1998; Yusuf and Wu, 2002; Zhao, 2003). Shanghai has, since 1949, always enjoyed strong political representation in the Communist Party of China (CPC) and state hierarchy and the politics of the city has been closely associated with the new generation of China's leadership. For example, former presidents Jiang Zemin and Zhu Rongji, and former Vice Premiere Wu Bangguo were all leaders of Shanghai before moving to Beijing to further their political careers, a connection that could only be useful to Shanghai's aspirations (Thant et al., 1998; Yatsko, 2001: 56) (Table 2. 2).

With the adoption of an export-oriented development strategy in the coastal region, China needed a global city to strengthen its link to the world economy with increased international trade and creating competitive city-regions became a top priority. Due to its strategic location in the Yangtze River Delta (YRD) and its unique history as the largest financial centre in East Asia, Shanghai was chosen to fulfil this ambitious role. In 1992, the 14th Congress of the China Communist Party announced that the primary role of Shanghai was to:

> seize the opportunity of development and [the] opening of Shanghai Pudong, and to build Shanghai as the dragon head and one of international economic, finance, and trade centre, so as to drive the growth of the [Yangtze] River Delta and in turn the take-off of the whole economic region. (Gu and Chen, 1999 quoted in Yusuf and Wu, 2002: 1684)

Table 2.2 Shanghai's Communist Party of China and state leadership

CPC Shanghai Committee secretary	**Mayor of Shanghai**
Rao Shushi (1949-1950)	Chen Yi (1949-1958)
Chen Yi (1950-1954)	Ke Qingshi (1958-1965)
Ke Qingshi (1954-1965)	Cao Diqiu (1965-1967)
Chen Pixian (1965-1967)	Zhang Chunqiao (1967-1976)
Zhang Chunqiao (1967-1976)	Su Zhenhua (1976-1979)
Su Zhenhua (1976-1979)	Peng Chong (1979-1980)
Peng Chong (1979-1980)	Wang Daohan (1980-1985)
Chen Guodong (1980-1985)	Jiang Zemin (1985-1988)
Rui Xingwen (1985-1987)	Zhu Rongji (1988-1991)
Jiang Zemin (1987-1989)	Huang Ju (1991-1995)
Zhu Rongji (1989-1991)	Xu Kuangdi (1995-2001)
Wu Bangguo (1991-1994)	Chen Liangyu (2001-2003)
Huang Ju (1995-2002)	Han Zheng (2003-present)
Chen Liangyu (2003-2006)	
Xi Jinping (2007-present)	
(Sources: Cheung, 1996: 61; various news articles)	

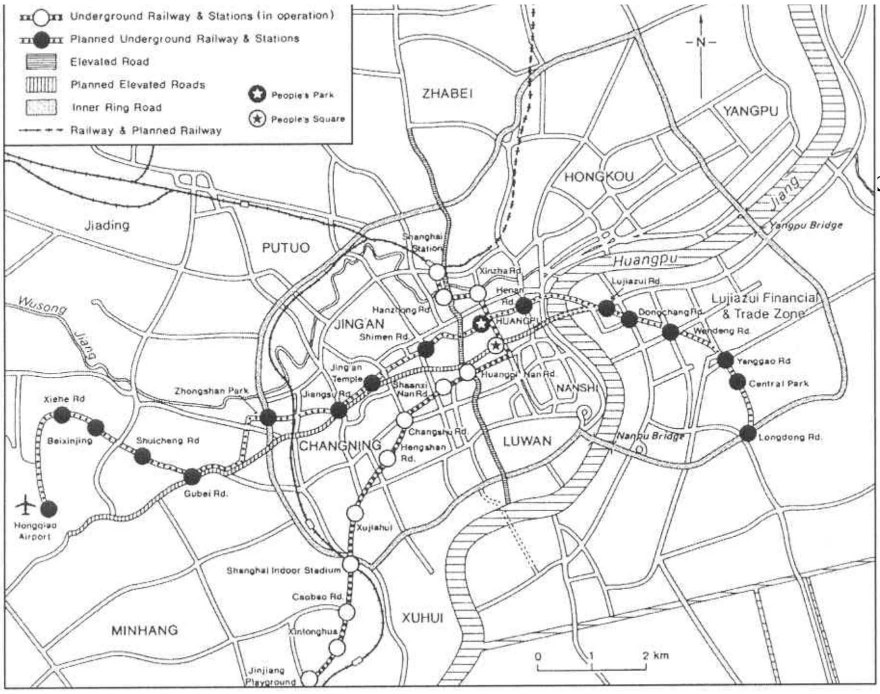
Greater emphasis was placed on the goals of enhanced economic efficiency, rapid economic growth and an increasing role for markets in the circulation and distribution of goods, services, capital and waged labour; Shanghai was to connect China to the global system in this process. In 1988, Shanghai was granted a fiscal contracting system that was previously exclusively enjoyed by Guangdong and Fujian (Yeung and Sung, 1996). In this context, Shanghai was empowered to have more control over its financial resources, using the principle of *zong er fen cheng, yi nian yi ding* (总而分成，一年一定; share of the total revenue between the local and central states according to proportions fixed annually) to redefine its fiscal relationship to the central state and allow the city to keep a larger share of its revenue (Thant et al., 1998: 2094).

National reforms and increasing levels of political support for Shanghai from Beijing also led to a process of urban development that is arguably unmatched in scale and speed in recent urban history. According to state officials, Shanghai was to take on three principle economic roles (Olds, 1995: 111, emphasis added):

- As China's major *transactional city* providing access to what was expected to become the 10th largest trading nation by 2000[3];
- As the principal *economic powerhouse*, or 'dragon head' of the country's largest integrated economic basin in the Yangtze River Basin (in which one-third of the national population produces more than 50 percent of the country's industrial and agricultural outputs);
- As the major *economic anchor* in the Yangtze Delta Region in which 160 million people (13 percent of the national population) account for more than 27 percent of China's industrial output.

A wide variety of initiatives were launched to accomplish these goals, developed by various arms of the Shanghai Municipal Government (SMG) and state-supported institutions (some based at universities) which assisted the relevant bureaus and commissions of the SMG. The role of foreign firms and institutions was also important from the onset in the SMG's efforts to strategically plan Shanghai's restructuring. The World Bank and the Asian Development Bank funded transportation projects such as bridges and road systems and strategic planning initiatives to guide the city's territorial and sectoral restructuring. The SMG also hired consultants such as the Paris-based Institut d'Aménagement et d'Urbanisme de

[3] In 2003, China ranked fifth in terms of volume of trade, after the US, Germany, Japan and France (People's Daily Online, 24 April 2003). In 2004, it replaced Japan as the world's third largest trader following the US and Germany with its trade volume hitting US$1.15 trillion (Zhou, 2005).



development of metropolitan

Figure 2.4 Map of the central city of Shanghai *(Source: Yusuf and Wu, 2002: 210)*

In contrast to the industrial development of past decades, Shanghai was to develop its tertiary sector as part of its transformation into an international economic, financial and trade centre. In 1978, the proportion of Shanghai's GDP derived from tertiary trade was only 18 percent. By the end of 1990, this increased to 30.8 percent and grew steadily to 39.6 percent in 1994. A mix of policies was implemented to relocate industries out of the central city, reduce population density there, and to attract overseas capital, foreign technology, management skills and knowledge about development strategy. These policies, together with central government reform initiatives were designed to facilitate the restructuring of Shanghai's economy in a similar fashion to that experienced in other world cities such as Hong Kong, Singapore, Tokyo and New York (Olds, 1995). An ambitious infrastructural scheme, largely funded by foreign capital flows, was also conceived which included the construction of bridges, inner and outer ring roads, subway lines, port upgrading, a new international airport in Pudong, a new national fibre-optic cable network and massive construction of new housing and office spaces. Specific development zones were also identified, in the older parts of the city as well as Pudong, for high-tech parks, financial and trade services (Figure 2.5). The objective was to reorientate and reintegrate Shanghai (and the wider region) into the global economy.

With the above policies and investments, Shanghai has recorded double-digit overall annual economic growth for the past 10 years. Table 2.3 shows that Shanghai's economic power has become far greater than any other city in China. Its GDP was larger than that of Beijing, Tianjin and Chongqing combined, and also more than the combined values of Guangzhou and Shenzhen, the most important cities in the Pearl River Delta. With the largest total volume of wholesale and retail sales and high residents' savings and total premium income, it is the biggest trading centre and market in China, only moderately challenged by Beijing and Guangzhou. The latter were however left far behind in terms of FDI of which Shanghai accounted for up to 15 percent of the country's total since 1990 (see Table 2.4).

The development of the Pudong New Area is clearly instrumental in the economic transformation and growth of Shanghai; it was specifically designed for the city to resume its former role as China's leading international financial, trade and economic centre. The next section focuses on the development of this remarkable urban project.

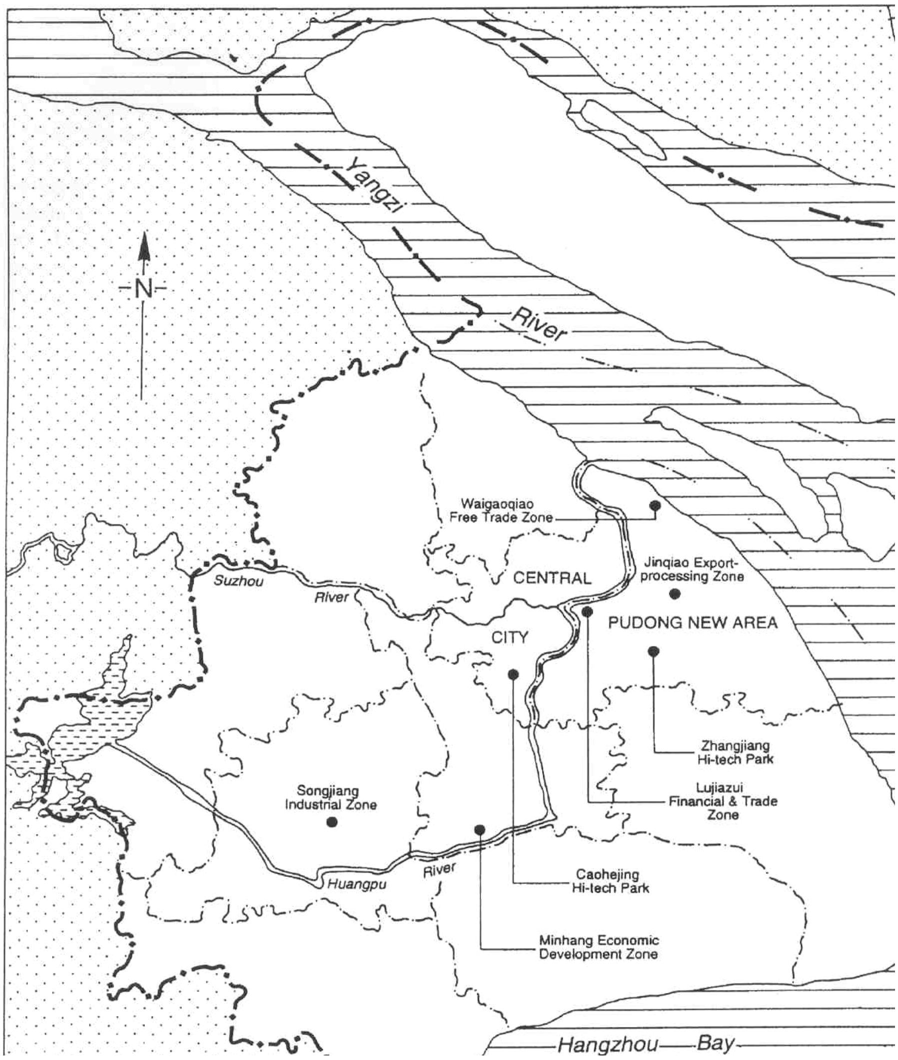


Figure 2.5 Development zones in Shanghai *(Source: Olds and Yeung, 1999: 520)*

Table 2.3 Comparison of overall economic strength among key Chinese cities, 1999

Cities	Population (million)	Area of city (km^2)	Built-up area (km^2)	GDP (billion RMB)	GDP per capita (RMB)
Shanghai	11.1	3924	550	361.6	32577
Beijing	10.5	6496	488	182.5	17381
Tianjin	6.0	4335	378	114.5	19083
Chongqing	8.4	12449	243	57.2	6810
Guangzhou	4.1	1444	284	145.2	35390
Shenzhen	1.2	1949	132	143.7	119750
Nanjing	2.8	1026	194	67.5	24107
Hangzhou	1.8	683	171	60.5	33611
Shenyang	4.8	3495	202	84.3	17563
Dalian	2.6	2415	234	58.6	22538
Wuhan	7.4	8467	208	108.6	14676
(Source: Zaloom, 2003: 437)					

Table 2.4 Comparison of utilised FDI in 1999 (billion US$)

City	Utilised FDI
Shanghai	3.05
Beijing	1.15
Chongqing	0.29
Guangzhou	2.26
Shenzhen	1.78
Nanjing	0.56
Hangzhou	0.30
Shenyang	1.02
Dalian	1.09
Wuhan	0.48
(Source: Zaloom, 2003: 438)	

2.3 THE REMAKING OF SHANGHAI: PUDONG NEW AREA

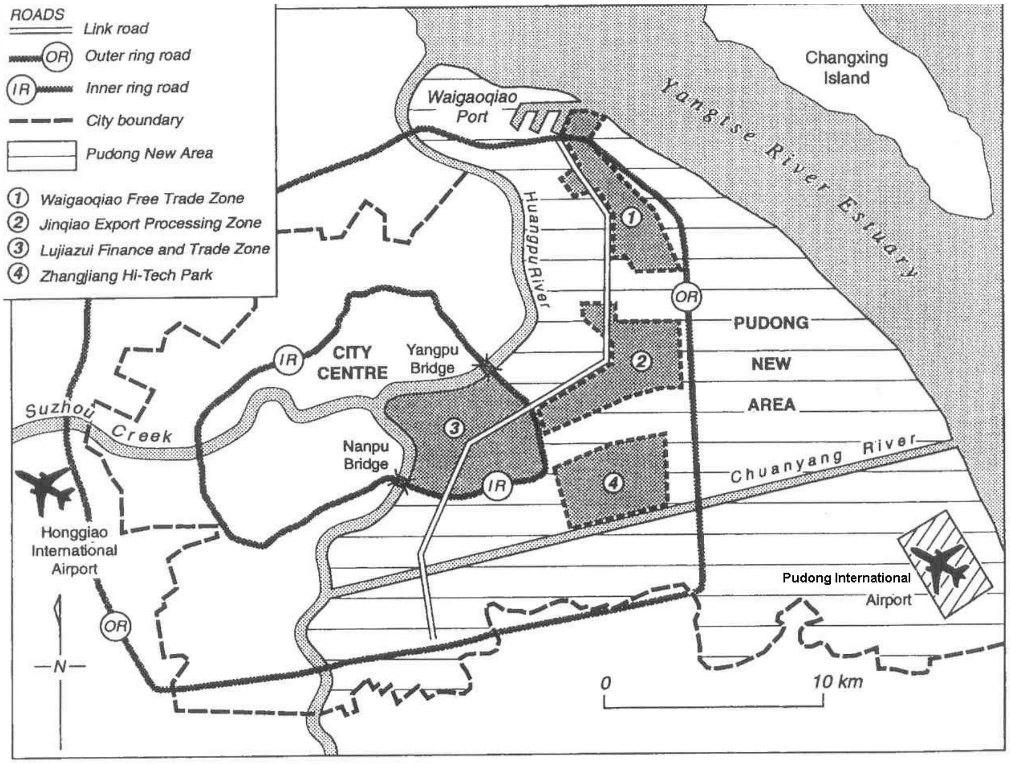
In April 1990, former Premier Li Peng announced the central government decision to develop Pudong into the largest SEZ in China. Pudong's strategic importance in China's modernization trajectory was further consolidated two years later. According to the 1992 *Report of the 14th Chinese Communist Party Congress*, Pudong was to act as a 'dragon head' for the cities along Yangtze River and that it was urgent to build Shanghai into an international economic, financial and trade centre in order to stimulate a new economic leap forward in the Yangtze River Delta and valley (Thant et al., 1998: 2096).

For the central government, the development of Pudong contributed to more than just Shanghai's revitalisation. Firstly, the Pudong New Area project signified the commitment of the central government to continue its reform and open-door policy (MacPherson, 1994; Thant et al., 1998; Yusuf and Wu, 2002).[4] Secondly, the Pudong project was to facilitate the spread of investment and stimulate economic development along the Yangtze River. Thirdly, Pudong could also be seen as an economic experiment in higher levels of foreign investment and economic restructuring (Thant et al., 1998). Preferential treatment was allowed under specific policies approved by the central government, including tax breaks, greater foreign investment permitted than elsewhere in China and the retention of financial income for further development (Table 2.5). Financial support was also provided for the development of Pudong under the Eighth and Ninth Five-Year Plan period (1991-1995; 1996-2000) (Table 2.6) and it was guaranteed US$0.1 billion in foreign loans and US$0.2 billion from the Bank of China every year (Yusuf and Wu, 2002: 213).

Table 2.5 Preferential policies implemented by the central government for the Pudong New Area project

• Tax deductions and breaks for enterprises operating in the new area. • Enterprises were to be assessed for income tax using a special low rate. • Tax-free import of materials and equipment and export of products. • Foreign investment allowed in projects such as airports, seaport, railways, highways and power plants, as well as in financial and retailing establishments (These areas were not open to foreign investors in other areas of China). • Preferential tax treatment given to domestic investors similar to that given to foreign investors. • Land-use rights could be transacted in the market. • Foreign investors could be directly involved in the development of large parcels of land. • Financial income from Pudong was allowed to be retained for further development and improvement of Pudong, instead of being submitted to the central government.
(Adapted from Thant et al., 1998: 2097)

[4] It was hardly a coincidence that the announcement to develop the Pudong area was made following the 1989 Tiananmen Square student demonstration, as the incident led to criticisms from the international community and cast doubts amongst investors on China's reforms.



ıe central government for the

ion in five years)
(RMB1 billion in 5 years)
r (RMB1.5 billion in 5 years)
ople's bank per year (RMB2

ıs a total area of 522 square ıi). Designed to relieve the a new centre of industrial, velopment zones: Lujiazui Finance and Trade Zone (Shanghai's new CBD), Jinqiao Export Processing Zone, Weigaoqiao Free Trade Zone and Zhangjiang High-Tech Park (Figure 2.6). The new Pudong International Airport and Weigaoqiao port are especially crucial to the development of Shanghai as an international commercial and trading centre.

Figure 2.6 The Pudong New Area project *(Source: Olds, 1995: 113)*

Major industrial and property developments have been established in Pudong over the past decade. Baoshan Steel Corporation, China's biggest steel conglomerate, has leased over 80 acres of land for a giant steel plant. Japan's retail giant Yaohan group has built the largest shopping centre in Asia in Lujiazui, at a cost of US$100 million. The Shanghai Security Exchange and other major financial institutions have also moved to new facilities in Pudong. Large TNC operations have also located production capacities in Pudong, including Shanghai-Bell, Eriksson, Phillips, Xerox, General Motors, Mitsubishi and Hitachi. During 1990-2000, a total of US$50.8 billion of inward foreign investment was utilised by Shanghai, of which US$31.2 billion (61 per cent) was in FDI (Zhang, 2003: 1557). Figure 2.7 shows the marked increase in FDI following the opening of Pudong in 1990. This success in attracting FDI was attributed to Shanghai's strategic location (midway along the east coast – China's paramount economic belt), its impressive industrialisation and urbanisation tradition as well as opportunities available in Pudong with its array of preferential policies (Olds and Yeung, 1999; Zhang, 2003).

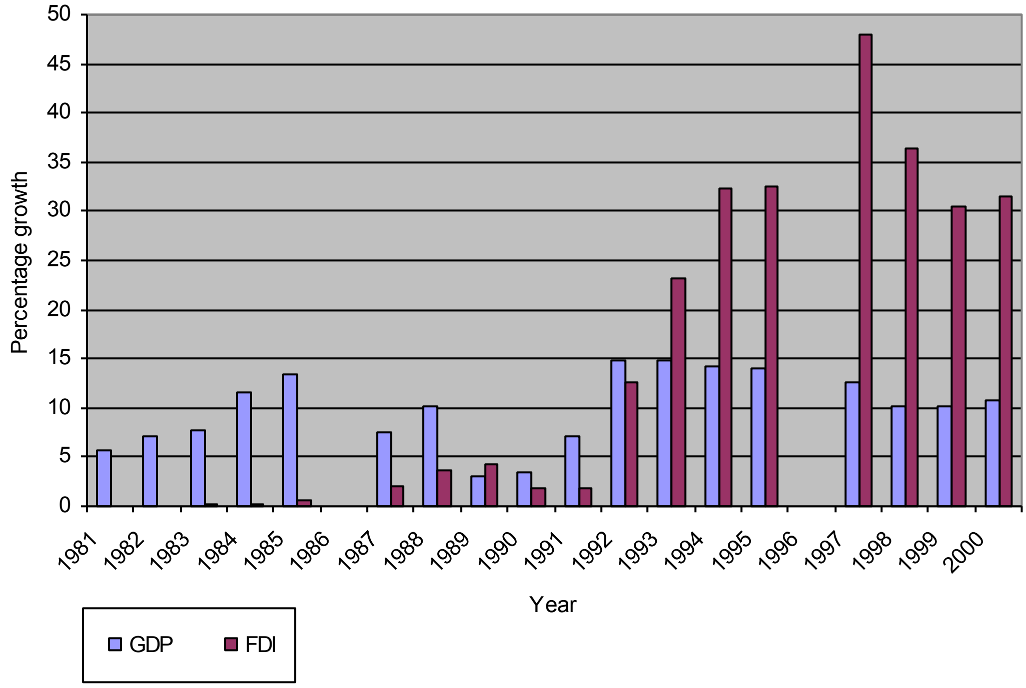


Figure 2.7 Annual growth of GDP and utilised FDI in Shanghai, 1981-2000. Note: No data available for 1986 and 1996. *(Based on Zhang, 2003: 1558)*

The LFTZ, situated immediately opposite the Bund in the old city centre, across the Huangpu River, formed the focal point of development. The traditional centre of the city surrounded by two commercial avenues, Nanjing Road and Huaihai Road, was approaching saturation; a revitalised CBD for Shanghai was to house a variety of business activities, especially financial and tertiary services that are the backbone of major world cities. This was taken up by Liujiazui, which was envisaged to be the Manhattan of 21st century Shanghai (Yeh, 1996; Olds, 1995). The new CBD in Lujiazui was to help revitalise the Bund, which housed over a hundred financial buildings before 1949, and transform it into China's "Wall Street" (Yusuf and Wu, 2002: 214); it would thus become a modern extension of the colonial-era Bund, or a '21st century Bund' (Olds, 1995) (Figures 2.8 and 2.9). Historic layers of built form and social formation had been replaced by what Olds

(1995: 114) conceptualised as an "international standard 'landing strip' to 'lure in' deregulated foreign finance capital".[5] The Lujiazui Finance and Trade Zone was thus planned as Shanghai's new tertiary sector centre with particular emphasis on financial services, as well as retail, real estate, business consulting and government services.

Figure 2.8 The revitalised Bund along Huangpu River *(Source: Author's own photograph)*

[5] Although my research indicates that the process is more complex due to how different actors interpret and respond to the nature of regulation in Shanghai.

Figure 2.9 The Pudong skyline across from the Bund *(Source: Author's own photograph)*

Shanghai needed the long-term support of both Beijing and international investors in order to achieve its aspiration. The Chinese gatekeepers of global flows were certainly operating within the context of the global economy in the planning and transformation of Shanghai and Pudong. However, these flows were invited and guided into specific territorial 'windows', shaped into specific forms with regulatory restrictions and preferential policies, and subsequently exploited for various political and economic purposes. While Pudong was built with the aim of attracting international capital, its conception and development was intrinsically tied to national development strategies.

2.4 FINANCIAL REFORMS AND SHANGHAI AS FINANCIAL CENTRE

> *Watching Shanghai's capital markets in the 1990s was like riding a rollercoaster whose brakes had failed because the ride operator had neglected to install and service them properly (Yatsko, 2001: 51).*

More than just a symbolic model of China’s global aspirations and urban transformation, Shanghai is also the site where much of China’s financial reforms are implemented as the city aims to reclaim its role as an international financial centre. Before 1979, the Chinese financial system was characterised by mono-banking practices as there were only three state banks – the People’s Bank of China (PBOC), the Bank of China (BOC), and the People’s Construction Bank of China. A sphere of responsibility and a clientele of enterprises were specified for each bank such that the influence of these banks in resource allocation was minimal and their role in promoting economic development was very limited and passive. Subsequent reforms promoted more efficient resource allocation and raised economic performance through the mobilisation of savings, better credit allocation and macroeconomic stability (Xu, 1998: 2). In the mid-1980s, one of the major developments in the financial sector was the introduction of financial markets in bonds and securities. Although such markets were very small, they represented the outcome of new thinking about building up a more diversified financial system.

Xu (1998: 94-98) identifies four periods of financial development from 1979 to the early 1990s. The first was the *emerging period* from 1979 to 1984. Various forms of ‘raising funds from society’ (社会集资; *shehui jizi*) were used to finance the operations of township and village enterprises, raising funds directly from surplus units instead of through the intermediation of the formal banking system. The State Council also started issuing state treasury bonds in 1981 to cover fiscal deficits. The emergence of new financial instruments and markets during this period was not the outcome of explicit government policies; rather, it was wider economic reforms that created opportunities and new demands. The spontaneous and rudimentary nature of financial market development was typified by the absence of professional financial bodies to direct the issue of various kinds of securities. As such, there were no standards for issuers to follow in setting terms and conditions and there was also a general lack of knowledge regarding liquidity, risk, rate of return and other key aspects.

The *developing period* (1985-1988) saw the emergence of a money market for interbank transactions and a secondary market for trading securities. In 1986 Shanghai was permitted to issue bonds in the international capital market, guaranteed by the central government. This raised US$3.2 billion, which was used to improve urban infrastructure and upgrade industrial facilities. A new fund management system was also introduced (Xu, 1998: 95-96). In 1985, financial institutions were allowed for the first time to issue financial bonds and the first such issue was made by the Industrial and Commerical Bank of China (ICBC) Shanghai branch to a value of RMB 500 million. Following the establishment of the Shanghai Short-term Fund Market in 1986, more than 300 fund markets appeared at provincial, regional and county levels. During this period, various kinds of bonds and securities were introduced and the term ‘financial markets’ began appearing frequently in the press and the concept of raising funds directly through issuing securities become more widely accepted.

Shanghai’s financial system then entered a *semi-stagnant period* in 1989 and 1990 as China’s economy started to overheat in the second half of 1988. The central government then adopted an austerity programme under which financial activities were restricted. Money markets in particular suffered from the credit squeeze pushed through by the PBOC. Trading in financial markets was largely suspended while the bond markets continued to develop albeit at a much slower pace.

Financial markets activities rebounded after 1990, during the *recovery and expansion period*, with the establishment of the first securities exchange in Shanghai in November 1990. After Pudong was designated a SEZ in 1990, Shanghai attracted four foreign bank branches later that year. The Chinese stock market was formally initiated in 1990 although access to the stock market was tightly controlled by the state through a quota system, which strongly favoured the larger state-owned enterprises (SOEs) (Zhang, 2003). The establishment of the Shanghai Stock Exchange (SSE), one of only two in China (the smaller being in Shenzhen), was a milestone. Its total market capitalisation at the start of 1999 reached RMB 1.06 billion (US$128 billion), compared with RMB 888 million (US$107 billion) at the country's second exchange in Shenzhen, with some 480 companies listing shares (53 more than Shenzhen). Shanghai also handles most of the country's treasury bond trading in primary and secondary markets. In terms of companies listed and volume of turnover, it seemed destined to eventually surpass Hong Kong; indeed, during the bull markets of 1996 and 1997 the exchange's daily turnover exceeded Hong Kong's on some days (Yatsko, 2001: 61).

By 1998, 41 major foreign banks had branches in Shanghai, including the Bank of America, Hong Kong and Shanghai Banking Corporation, Credit Lyonnais and Standard Chartered Bank, representing about 30 percent of the country's total. Another 119 foreign financial service firms had set up representative offices in the city (Yatsko, 2001: 59). By early 1999, the number of foreign bank branches in Shanghai had climbed to 64. Major commercial banks such as Citibank and Standard Chartered declared Shanghai their China headquarters and moved senior executives in charge of China business to the city. By the end of 1998, a total of 18,984 foreign invested enterprises had been approved and 1,490 foreign firms had invested a total of US$5.8 billion, despite the Asian financial crisis. According to the China Banking Regulatory Commission (CBRC), there are now 72 foreign banks in Shanghai.

Shanghai had a pioneering role in the market development process in the country as whole, with most of the initial experiments in financial markets formation originating from the city. Perhaps the most important development of the Shanghai stock market was the issue of so-called 'B' shares in late-1991. B-shares were normally issued by large SOEs and targeted at foreign investors (while A-shares are restricted to local investors).[6] They were denominated in local currency but traded in US dollars (in Shanghai) or HK dollars (in Shenzhen).[7] The number of B-shares was not to exceed 49 percent of the total issued capital of the enterprises. The issue of B-shares was intended to tap foreign funds for the country's economic development. Tables 2.7 and 2.8 indicate the dramatic growth of the securities market in Shanghai.

Table 2.7 Value of securities traded in the Shanghai market, 1986-1991 (RMB million)

	1986	1987	1988	1989	1990	1991
State Bonds	-	-	236.01	764.63	2,361.19	9,810.00
T-bond	-	-	263.01	760.60	2,359.30	9,154.99
(Fiscal bond)	-	-	-	-	-	-
State construction bond	-	-	-	-	0.47	-
Key construction bond	-	-	-	4.03	1.42	655.01
(Special T-bond)	-	-	-	-	-	-
(Indexed bond)	-	-	-	-	-	-
(State Invest. Co. Bond)	-	-	-	-	-	-
(Key enterprise bond)	-	-	-	-	-	-
(Capital construction bond)	-	-	-	-	-	-
Financial Bond	-	-	-	11.84	1.14	671.00
(Local) Enterprise Bond	0.11	27.58	37.32	18.64	17.52	594.00
Enterprise share	.0575	2.62	4.45	7.77	49.63	1,620.00
Total	0.685	30.2	304.78	802.88	2,429.48	12,695.00
Note: Bonds in brackets were allowed to be traded but the value of trading was negligible. *(Source: Xu, 1998: 115)*						

[6] This division in types of shares was meant to restrict foreign participation in the Chinese stock markets so that the Chinese state could maintain control over flows of foreign exchange into and out of the country. More details in Chapter 7.

[7] Similar products called H-shares are also traded in Hong Kong. See Chapter 7 for details on the different types of shares.

Table 2.8 New issues and volume of stock trading in Shanghai, 1986-1991 (RMB million)

	1986	1987	1988	1989	1990	1991
New issues	5.80	785.60	44.90	23.30	9.00	130.60
Trading	0.58	2.62	4.45	7.77	46.60	1620.00
(Source: Xu, 1998: 115)						

2.5 CONCLUSION

Over the last two decades of rapid economic development, a number of cities in Asia have devoted themselves to attaining global city status and climbing the urban hierarchy as a key development goal. Competition is intense between traditional rivals such as Singapore and Hong Kong, as well as other emerging nodes like Kuala Lumpur, Bangkok and Taipei. As China's relationship to the global economy changes, cities such as Shanghai are increasingly participant in the global city network and active players in the emerging world economic system. In examining inter-city relations, Taylor (2006) noted the increasingly global orientation of Shanghai and its integration into the world city network. In *The Global Financial Centres Index* commissioned by the City of London (Mainelli and Yeandle, 2007) Shanghai was ranked 24th, ahead of Dubai, Brussels and Milan and just behind Amsterdam and the Channel Islands.[8]

Shi and Hamnett (1998) argue that only Hong Kong, Shanghai and Beijing have the potential to attain leading positions in the global urban system in the future. Hong Kong already occupied an established spot in the global cities network, especially in terms of financial services and connections. Shanghai had long been a commercial and financial centre in the Far East before 1949 and its recent economic and urban transformation and international interest lend further credence to its aspiration of achieving its former glory. However, Shanghai's development trajectory towards a national financial centre status had been questioned by some

[8] Beijing was ranked 36th.

commentators, especially with regards to its relationship with Beijing (Zhao, 2003, Zhao et al., 2004). Beijing's most significant competitive advantage lies in its role as the capital of centralist, socialist China for almost half a century, being the primary location for institutions and organisations responsible for managing and determining the economic and political life of the country. It is the location of the country's central bank, along with the head offices of the many of the largest state-owned banks and major national companies. However, considering that it possesses the largest stock market, the only foreign exchange centre in the country and other important financial markets such as commodities exchange and futures exchange, Shanghai has an undisputedly important role as an economic and financial hub.

The remarkable success of Shanghai in attracting investment in the 1990s needs to be understood in the context of its historical success, the rise of the Chinese economy and China's historical transition towards a market economy towards the end of that century. In this process, the central state's ambition to develop China into an industrialised and globalised economy and the local government's desire to join the ranks of global cities produced one of the most dramatic instances of urban and economic transformation in the 20th century. Official rhetoric about the development and progress of Shanghai often harks back to its glorious past. This is still physically evident in the Shanghai Pudong Development Bank's headquarters on the Bund, which was formerly occupied by the Hong Kong & Shanghai Bank prior to 1949 (Figure 2.13) (Yatsko, 2001: 56-57). On the ceiling of the neoclassical building's enormous lobby is a colourful mosaic depicting Shanghai, New York, London, Calcutta and Tokyo – the world's most important financial and trading hubs in those days. The fact that Shanghai once climbed to such heights makes its current aspirations all the more plausible to many in the international financial services industry. China's recent entry into the WTO has been hailed as a milestone for its development trajectory. Amongst other promises, it grants foreign commercial banks the right to conduct local-currency transactions with domestic companies within two years of China's accession and with individual retail customers after five years. Overall, China's WTO entry is expected to accelerate the reform of China's state enterprises, banking system and financial services industry, which will almost certainly benefit Shanghai.

Figure 2.10 The former Hong Kong & Shanghai Bank building on the Bund *(Source: Author's own photograph)*

However, Shanghai's success in its aspiration to be the 'New York of the East' remains to be seen. Compared to developed market economies, its financial markets are still in their infancy and remain problematic due to the following issues.

First, there is a lack of self-regulating mechanisms to oversee the operations in the market. The role of the government in the market generally remains one of market creation rather then market supervision. Second, the functions of the securities market in promoting optimal capital flows between different industries and sectors remain weak as the main attraction of the stock market to both securities issuers and investors is its almost guaranteed short term profit. Finally, this speculation remains widespread, due to the lack of sound regulatory infrastructure and the general public's ignorance about securities investment.

In this chapter, I have examined Shanghai's current development and aspiration in the context of its historical roles within the broader Chinese economy and its particular advantages in terms of its geographical location, Pudong's SEZ status and special policies sanctioned by the central government to aid its development. In the following two chapters, I explore how we could conceptualise Shanghai's aspiration to be a financial centre and the development of its financial markets within extant literature on the spaces of global financial flows, and how an examination of Shanghai's experience could extend the theoretical boundaries of the geographies of money and finance and conceptualisations of 'markets'.

Chapter 3

Conceptualising Global Financial Flows

3.1 INTRODUCTION

> *"Consider [...] how fantastical are futures contracts and Eurobond markets, and how we, as supposedly sophisticated individuals, have placed our faith first in gold and silver, then in paper monies, and now in electronic representations of these paper tokens of 'real' value. Yet we have no choice but to take (construct) money for granted in this way [...] Fantastic as our faith might be, it is a necessary faith. We must believe in the modern money form because money greases the wheels of industry; money makes the world go around. Money makes possible the complexity of modern life and the extended divisions of labour that are at its core. Without global money, there can be no global trade and industry; no modern forms of globalisation. While money is undoubtedly an abstraction, it is also concrete. Money shapes the lives of men and women almost everywhere." – Stuart Corbridge and Nigel Thrift (1994: 21)*

Even as money has become an increasingly intangible commodity, freely exchanged within national boundaries and in internationally competitive markets, particular localities remain critical to the production and reproduction of global finance and the uneven geographies of finance have specific impacts on localities. More than an impersonal force, money is a social, cultural and political process that has inherently spatial qualities. Even as particular configurations of space and place enable its historical and contemporary workings, these financial flows, networks and nodes have spatial consequences. In conceptualising money and global financial flows in this chapter, I want to emphasise three points. Firstly, I want to highlight the contribution of the *political economy* approach in emphasising the interconnectedness of economics and politics across international as well as national scales. This approach seems to have fallen out of favour (or fashion) since its heyday in the 1980s and early 1990s, but I would argue that it is particularly useful for understanding specific local or national scale phenomena by embedding them within an international context that emphasise flows, interconnectivity and power. The second point to bear in mind is the *social and cultural embeddedness* of finance capital and financial markets. Much of this draws inspiration from the works of economic sociologists and anthropologists, although geographers have increasingly made links between the economy of international money and the distribution and formation of social power (Thrift, 1994; Pryke and Lee, 1995; Leyshon, 1996; Reszat, 2002). The world of money is discursively constructed through particular social-cultural practices. Finally, the world of money and global finance has a *distinctive geography*, which operates at a number of different spatial frames or scales. Leyshon (1996) puts it most succinctly in arguing that "money does not just have a geography; *money is itself a geography*" (p. 3; original emphasis).

A number of geographers have noted the neglect of money and finance within economic geography research (see Leyshon, 1995; Martin, 1999c; Leyshon, 2000). Economic geography has been preoccupied with industrial landscapes since its inception and throughout the 1950s and 1960s the passions of economic geographers and regional economists remained focused on industrial development and agglomeration; there were little, if any, consideration of monetary issues. Since the late 1980s, however, there has been a growing wave of work on the spatial dimensions of money and increasing recognition and appreciation of the theoretical and empirical importance of finance and money for understanding the forces shaping economic landscapes. David Harvey (1982, 1985a, 1989), for instance, started to elaborate on the key role of finance in his evolving Marxist theorisation of the uneven development and crisis-prone tendencies of the capitalist economy. There was also a growing number of more specific studies that dealt with the spatial organisation and operation of financial institutions, services and markets (Leyshon and Thrift, 1992; Cerny, 1993a, 1993b; Corbridge et al., 1994; Roberts, 1994; Thrift and Leyshon, 1994; Leyshon, 1996; Hudson, 1999), as well as the economic, political and social dynamics of international financial centres (Pryke, 1991; Zukin, 1992; Thrift, 1994; Pryke and Lee, 1995; McDowell, 1997; Porteous, 1999). This period was also marked by the publication of influential texts on financial geography by Corbridge et al. (1994), Leyshon and Thrift (1997a) and Martin (1999a).

This chapter does not seek to provide a comprehensive overview of all the work undertaken in geographical accounts of money and finance (see Leyshon, 1995, 1997, 1998; Martin, 1999c). Rather, my objective is to focus upon four main areas of research which falls into two broad themes: (i) the regulation of the international financial system and (ii) the making of financial (market)places. The former follows a broadly *political economy* perspective and latter a *social constructivist* perspective (Table 3.1). The regulation of the international financial system takes place on a variety of scales. In examining research on geographies of money and finance under the broad umbrella of political economy (section 3.2), I proceed in two stages. First, I deal with research focusing on the role of money and finance within broader historical context of capitalist accumulation and transformation. Much of this work was conducted in the international political economy (IPE) tradition relying on concepts of regulation, hegemony and post-hegemony. Second, I focus on the complex and dynamic relationship between finance capital and nation-states. How do states regulate their own national economic spaces and financial flows? How do they frame finance capital and what are the implications for the rise of the competitive state? The second perspective has become more popular as geographers become dissatisfied with the limitations of a political economy interpretation. Under the umbrella of social constructivism, in section 3.3, I examine a more social and cultural interpretation of international financial centres and the centrality of knowledge (its formation, interpretation and circulation). The conceptual treatment and framing of 'markets' will be covered in the next chapter (Chapter 4).

Table 3.1 Conceptualising global financial flows

Political economy perspective	Social constructivist perspective
Money and the international financial system	The making of international financial centres
States and finance capital	Framing markets

In what follows I examine research in the above areas by outlining their position within the broad theoretical perspective and their contribution to the literature. After outlining each area of research, I discuss how these ideas and concepts informed my research on 'markets' and Shanghai's development, how they influenced the framing of my research questions and the theoretical contribution of my empirical research.

3.2 THE POLITICAL ECONOMY PERSPECTIVE

The political economy approach featured prominently in earlier studies on geographies of money and finance. The term 'geopolitical economy' can be traced to the works of David Harvey (1985b), John Agnew and Stuart Corbridge (Agnew and Corbridge, 1989; Corbridge and Agnew, 1991) and refers to geographical and structural shifts in power between states, between states and markets, and between groups of social and economic actors involved in the regulation and operation of markets (Leyshon, 1995) as the globalisation of capital and ideas disrupted traditional forms of sovereignty and international regulation. Many of these studies focused on understanding the dynamics of financial capital in terms of international relations and global political economy. Regulatory changes, technological innovations and the globalisation of markets and monetary flows are remapping the financial landscape towards increasing deterritorialisation but states remain important arbiters in determining the shape and speed of such processes. They continue to exert significant influence within their national space economies as well as on the international arena. Research within the political economy perspective thus covers various spatial scales from global systemic analysis to national strategies to financial centres at the city-level.

3.2.1 Money and the International Financial System

This area of research is concerned with the broader transformation of space, of which the work of David Harvey is particularly important. In *The Limits to Capital* (1982), Harvey provides an incisive analysis of the dynamics of the financial system under capitalism. The role of money and finance, in particular, is given centre stage in examining the circulation and accumulation of capital and their spatial implications. He argues that the imperatives of the financial system have brought about a world characterised by time-space compression. This shrinking of the world occurs as capitalist producers are locked into a perpetual race to exploit new markets and to reduce the turnover time of capital, which brought about a major transformation in the nature of capitalism as a whole. Harvey thus connects with regulation theory in explaining why capitalism appears to be increasingly beset by crisis and volatility, such as how and why the relative stability of the “Fordist-Keynesian” era had been dislocated by the rise of “flexible accumulation”, brought about by an acceleration of time-space compression (Harvey, 1989). Harvey then goes on to connect with a broader IPE literature that examines the ways in which the international monetary and financial system constitute a kind of regulatory space, holding together broader processes of accumulation. This research draws attention to the changing scale of financial activity that had become increasingly globalised, and its implications for state actors and the international financial system.

There is no all-encompassing definition of the term ‘regulation’ but Leyshon and Thrift (1997a: 60) offer two uses of the term that are prevalent in the literature. Firstly, regulation refers to the maintenance of a systemic equilibrium, in which an economic or social system is controlled by a ‘governing mechanism’. Second, it refers to a framework of legal and administrative rules. Both interpretations are often mutually constitutive. The form of systemic equilibrium in operation will influence the drafting of rules and guidelines, which are used to ensure that the system reproduces itself. Despite the restraining imposition of regulatory measures, crises remain a persistent feature within capitalist economies because all systems of regulation are fragile and temporal within a highly dynamic and spatially variegated capitalist system. As economic agents continually seek to surmount barriers to the generation of profits and value, the nature of activities being regulated often change in ways that render existing governing mechanisms redundant. Moreover, the spatially bounded nature of regulation (often organised according to political-territorial boundaries) makes it possible for economic agents to move between different ‘regulatory spaces’ in order to circumvent constraints associated with particular regulatory regime. This form of ‘regulatory arbitrage’ (Leyshon and Thrift, 1997a; Cerny, 1993a) has increased dramatically with improvements in information and communication technologies (ICT) (see Leyshon, 1996).

An important influence in this area of research is the notion of hegemonic stability – the idea that one powerful state will impose order on the international financial system such that it provides a platform on which more general processes of capital accumulation follows. Studies on the making and breaking of earlier systems of international regulation in the 19th and 20th centuries largely focus on British financial capitalism and the pivotal role of the City of London (Chapman, 1992; Michie, 1992; Rubinstein, 1993; Kynaston, 1994), and the rise and fall of U.S. financial hegemony during the post-war period (Corbridge and Agnew, 1991; Leyshon, 1992; Cerny, 1993b). In the late-19th century, an international gold standard was constructed as an attempt at economic regulation at the international level. This rule of money consolidated the power of the City of London as adherence to principles of free trade was in line with the financial rationality and economic liberalism that governed development within Britain. This form of regulatory order was soon undermined by rising industrial powers such as the USA, Germany and Japan as their developmentalist orientation involved some degree of closure from the international economy, usually through protectionist barrier to trade and capital. The rise of nationally regulated capitalism eventually overrode the prevailing regulatory mechanisms of international order and facilitated the breaking away from the gold standard (Eichengreen, 1996; Rothbard, 1998; Yeager, 1998). In the immediate post-war era, the Bretton Woods system was constructed as an attempt to build an international order that allows separate accumulation strategies to be pursued but prevent states from retreating into defensive blocs (Corbridge, 1994b). During the period of 1945 to 1971, the US dollar was linked directly to gold while all other currencies were linked indirectly through fixed exchange rates against the dollar. This system of fixed exchange rates was to bring stability to the currency markets and facilitate international trade. With post-war economic recovery in the core capitalist states, however, accumulation soon came up against the limits of the national market. As economic activity became increasingly internationalised, the geographical integrity of national economies was eroded and regulatory dislocation began to unfold. The development of Euromarkets, for example, threatened the control that national governments exercised over national space-economies and symbolised the emerging power and mobility of private capital (see Corbridge, 1994a). Eventually, various regulatory contradictions and pressures forced the system to collapse in 1973, which brought about a more volatile and spatially extensive global financial system that is less conducive to the regulatory strictures of national governments (Underhill, 1991; Gill, 1992; Gill, 1993; Cerny, 1993b; Helleiner, 1993b, 1994; Corbridge, 1994a; Leyshon and Tickell, 1994).

Even though it seems to offer a progressive and contextualised interpretation of the international political economy, the concept of hegemonic stability has been criticised by a number of researchers (Cerny, 1993b; Corbridge, 1994a; Leyshon and Tickell, 1994). Cerny (1993b), for example, points out that 'British hegemony' in the 19th century was actually controlled not by the British state per se but by a structure of powerful financial market actors that might have been centred in London but which stretched around the financial world. This wider network was essentially a transnational one cutting across British, French and other financial systems and tying them into a set of international norms and practices, underpinned by the gold standard. Be that as it may, a more volatile financial system has significant implications for corporate behaviour and national and regional development. An important sub-theme within this area of research has been to consider regulatory changes and experiments in Europe that were introduced to inject some measure of monetary stability in response to the collapse of Bretton Woods and in pursuit of the European integration project (Swyngedouw, 1992; Leyshon and Thrift, 1992; Leyshon and Thrift, 1995). Furthermore, there is an increasing shift in power towards the transnational interests of social elites, particularly those associated with global financial capital as documented in the works of Gill (1990, 1992), Leyshon and Tickell (1994) and Underhill (1994).

These developments led researchers to consider the concept of post-hegemony as the internationalisation of economic activity beyond and across the space-economies of individual states undermine the coherence of the old hegemonic order. Cerny (1993b), for example, argues that future national control would be limited, indirect and constrained to conform to the imperatives of the transnational financial markets. Governments, international regimes and regulatory authorities within governments will become increasingly squeezed between different sectors and forms in the financial services industry seeking the most ‘amenable’ regulators and permissive rules. Different ‘state actors’ linked into different policy communities will increasingly operate within transnational networks, with securities regulators establishing networks with counterparts abroad as well as with multinational securities firms, as they compete with similar networks among banking or insurance regulators and so on. In this sense:

> Hegemonic power no longer resides in one territorial state (if it ever did); it resides in a number of nodal points (and vectors or flows) that describe a decentred hegemonic core. (Corbridge, 1994a: 1849)

This decentred hegemonic core is anchored by a variety of actors, including supranational organisations such as the World Bank and International Monetary Fund (IMF), large private capital and particular actors or communities (be they policy, finance or other interest groups) in the USA, European Union and Japan. Figure 3.1 shows how these major core-regions or institutions of capitalism and other ‘lesser’ city-regions are held together by circuits of capital, pulling them ever inwards through changing configurations to prevent the international system from unravelling.

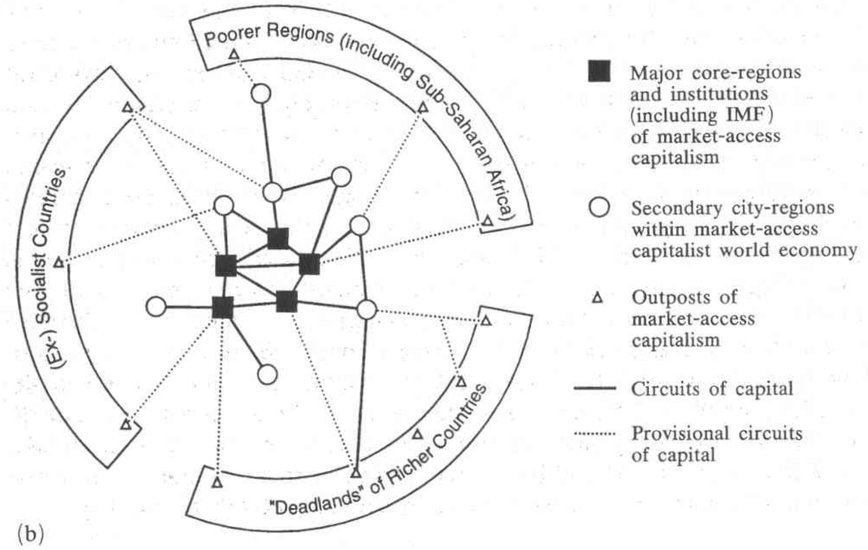


Figure 3.1 State of post-hegemony after Bretton Woods *(Source: Corbridge, 1994a: 1850)*

Implications for Research

How is the changing governance of Shanghai's financial system typical (or not) of changes in the international financial system? London was the undisputed leader in international finance in the 19th century as the City benefited from the imperial activities of Great Britain. The USA, however, took over this position in the mid-20th century as New York started to finance much of Europe's debt following the Second World War (Budd, 1999; Hudson, 1999). Japan was predicted to take over as the leading international financial centre in the 1980s, as its banks became the largest and most powerful in the world and Tokyo controlled large flows of international finance capital. This vision, however, was never realised due to various geopolitical and economic factors (Helleiner, 1993a; Leyshon, 1994). In the 21st century, there is increasing interest and concern regarding the rise of China (in the economic as well as geopolitical realm) and the possible dominance of Shanghai as an international financial centre (Ratliff and Gu, 2006; Kynge, 2007; D. Smith, 2007).

Following the concept of post-hegemony, we should discard any false expectation of hegemonic stability in the form of having one powerful state impose global regulatory order, but it is worth considering what impact a more powerful China might have on the global flows and configurations of capital. On 21 July 2005, China departed from a regime of fixed exchange rate by having the renminbi (RMB) weighted against a basket of currencies instead of pegged to the US dollar. This measure is still tightly controlled by the state, allowing only minimal currency fluctuation. However, there are also clear indications of international influence and cooperation as different Chinese state actors, such as regulators of banking and securities sectors, connect with their counterparts in the City of London, New York, Hong Kong and Singapore for expertise and knowledge transfer. The influence of global institutions such as the WTO is also clearly implicated in the deregulation of China's financial services and economic strategies. The issue of power is foremost in this consideration and my empirical research highlights the complex nature of these processes and how they might be contested by a variety of actors and institutions within China and in the international community.

3.2.2 The Relationship between States and Finance Capital

Owners of finance capital, especially international financial institutions but also increasingly states themselves, began to switch money rapidly between national economies as they seek to avoid devaluation of money capital. With this practice of spatial-regulatory arbitrage, national economic policies became increasingly sensitive to the power of international money and orientated to the pursuit of low inflation and relative price stability in the constant bid to retain such 'hot money'. This growing power of financial capital vis-à-vis the state at an international level was paralleled by an inability of nation-states to control the creation and circulation of money within the national economy (Jessop et al., 1990). Advances in ICT accelerated the rate of product and process innovation within the financial sector that continually undermines the regulatory power of the state. The state attempts to enforce financial prudence and responsibility by constraining the behaviour of financial institutions, often through structural regulation; that is, a form of regulation that demarcates the financial system, and is designed to restrict financial institutions to prescribed areas of financial activity. But while the partitioning of the financial system is designed to constrain activities of financial institutions and offset the development of a systemic crisis, this mode of regulation tends to be undermined by the inherent tendency for these institutions to engage in financial innovation. This is a process by which financial institutions develop new financial instruments that enable them to move outside of existing regulatory frameworks and into new areas of financial activity as yet unconstrained by regulatory control (see Table 3.2). This tendency towards financial innovation ensures that the regulatory and supervisory authorities of the state are faced with the constant task of reappraising and restructuring the regulatory framework. Therefore, “by nature [regulation] is reactive rather than proactive” (Laulajainen, 2000: 228). As money capital became increasingly internationalised, it brought about a tendency for the power of international finance capital to wax and for the economic power of individual nation-states to wane (Leyshon and Thrift, 1992).

Table 3.2 Financial innovations in the United States, 1970-1982

Types	Level of interest rates	General price level	Tax effects	Volatility of interest rates	Technology	Legislative initiative	Internatio-nalisation	Other
A. Cash Management	*							
Money market mutual funds	*							
Cash management/sweep accounts	*							
Money market certificates	*				*			
Debit card	*					*		
NOW accounts	*				*			
ATS accounts	*				*			
Point of sale terminals					*			
Automated clearing houses					*			
CHIPS (same-day settlement)					*			
Automated teller machines					*			
B. Investment contracts								
Primary market								
Floating rate notes				*				
Deep discount (zero coupon) bonds	*	*		*				
Stripped bonds	*	*		*				
Bonds with put options or warrants	*			*				
Floating prime rate loans				*				
Variable rate mortgages				*				
Commodity linked (silver) bonds				*				
Eurocurrency bonds	*						*	
Interest rate futures				*				
Foreign currency futures						*		
Cash settlement (stock index) futures				*				
Options on futures			*	*				
Pass-through securities				*				
Consumer type								
Universal life insurance				*				
Variable life policies		*						
IRA/Keogh accounts			*	*				
Municipal bonds funds			*	*				
All-saver certificates	*			*				
Equity access account	*			*				
C. Market structures								
Exchange-traded options								*
Direct public sale of securities								
Green Mountain Power Co.				*				
Shelf registration				*		*		
Electronic trading								
NASDAQ					*			
GARBAN					*			
Discount brokerage						*		
Interstate depository institutions					*	*		
D. Institutional organisation								
Investment bankers/Commodity dealers	*				*			
Salomon/Phibro, Goldman Sachs/J. Aron,								*
DLJ/ACLI								
Brokers/general finance Shearson/Amex,								
Bache/Prudential Schwab/Bank of	*				*		*	
America								*
Thrifts with commercial banks								
Financial centres (Sears Roebuck)								
(Source: Leyshon and Thrift, 1997a: 131-132)								

Cerny (1993a) identifies a 'first financial revolution' in the late-18th and early-19th centuries and a 'second financial revolution' in the 1980s and 1990s. The first phase was driven by the imperatives of the nation-state and the state-based international system. This involved the consolidation and expansion of the state apparatus itself, which required secure sources of capital, and the rise of economic competition between nation-states, which required the expansion of national wealth and development of new production and consumption processes. Finance was widely seen as a vital strategic industry, too important to be left to the market alone, which resulted in the incremental development of financial regulation. The main principle of regulation was compartmentalisation, which involved the separation of different financial 'markets' to prevent failure in one from creating a chain reaction through the others (as had happened in 1929). This nationally based system became increasingly difficult to sustain with the rapidly expanding world of international integration of production and trade. The second financial revolution was a consequence of this structural contradiction and financial market deregulation was a response to the inadequacy of such nationally based regulatory systems to deal with the new internationalisation of finance.

The term 'deregulation', however, masks a complex process of regulatory change. Regulations cannot merely be lifted as the very operation of market economies is dependent on the existence of *a priori* rules and mechanisms to deal with market failures. This so-called 'deregulation' has not resulted in a reduction of regulation or overall state intervention but has generally led to a complex process of drafting new regulation – a process more usefully conceptualised as 're-regulation' (Cerny, 1993a). The major changes in financial market structures driving this process of re-regulation are a) decompartmentalisation, b) disintermediation and securitisation, c) financial innovation, d) marketisation of the state, and e) globalisation. These processes are briefly described in Table 3.3.

Table 3.3 Re-regulation and changes in financial market structures

a) Decompartmentalisation	▪ Removing geographical or hierarchical limitations within particular financial sectors or between different functions. ▪ E.g. the lifting of exchange controls and credit controls following the 'Big Bang' in the City of London
b) Disintermediation and securitisation	▪ Twin processes ▪ Disintermediation concerns the slower growth or decline in supply of intermediated bank credit (i.e. loans) ▪ Securitisation involves the growth of negotiable securities issues and trading
c) Financial innovation	▪ The development of new financial (mostly securities and 'off-balance-sheet') instruments ▪ Take advantage of regulatory loopholes or the lack of regulatory structures, in the continuous search for higher returns on capital
d) Marketisation of the state	▪ Changing role of governments not merely as regulators but as participants in the markets themselves ▪ Goals: ensuring their own solvency; manipulating monetary and fiscal levers; and promoting international competitiveness of home-based firms
e) Globalisation	▪ The crystallisation of transnational linkages ▪ Enabled and accelerated by ICT ▪ Intertwined with all of the changes above
(Based on: Cerny, 1993a: 56-69)	

These developments have changed relationships between states and finance capital especially with respect to the rise of the 'competitive state'. A fundamental reworking of the relations between capital and space underpins and reinforces the contraction of the Keynesian welfare state. According to Castells (2000), the 'network society' of contemporary capitalism has become dominated by a 'space of flows' rather than a 'space of places' as advances in ICT enabled capital to become not only mobile but hypermobile (Warf, 1999). This hypermobility of capital led to the emergence of a globalised, post-Fordist production regime that rode on a global wave of deregulation and privatisation, new trade regimes, and the integration of world financial markets. The emergence of the post-Keynesian state reflected the inability of the welfare state to adjust to the realities of late-20th century capitalism. As the difficulty of 'trapping' capital led to heightened competition between localities, planning became more concerned with market rationality and local competitiveness rather than comprehensiveness and equity. Hypermobility thus pressured national and local governments to accommodate global capital in ever more earnest ways, but other factors like pools of expertise, specialised information and institutional thickness concurrently increased in significance. The winners of this process have been particular global cities that have become attuned to the rhythms of the global economy and adept at pinning down hypermobile capital and offshore financial centres (OFCs). The wave of deregulation and liberalisation policies introduced in the leading industrial nations from the mid-1970s onwards was an on-going attempt to embed their markets into specific territorial and regulatory spaces. Table 3.4 summarises the changing regimes of financial regulation during the post-war period.

Table 3.4 The changing regimes of financial regulation

Period	Regime of regulation	Characteristics
Mid-1940s to early-1970s	Embedded liberalism	▪ National regulatory system bound by fixed exchange and capital controls, underpinned by the international convertibility of the dollar
Late-1950s to early-1960s	Regulatory challenge of Euromarkets	▪ Differences in national regulatory systems established concept of 'regulatory asymmetry' between financial centres ▪ International demand for dollar deposits outside the control of Federal Reserve led to Euro dollar market being established in London, which had the most liberal regulatory regime
Mid-1970s to mid-1980s	Successive international deregulation	▪ Aftermath of the Bretton Woods system created the need for some international 'thermostatic device' to recycle excess, in particular dollar liquidity ▪ New technologies, financial innovation and the need for risk-managing financial instruments created the environment in which New York stock exchange was deregulated in 1975 ▪ The potential loss of London's international position led successive British governments to consider deregulation from 1978 onwards, culminating in 'Big Bang' in 1986 which increased London's international exposure ▪ The other major centres in the European time zone quickly followed suit, albeit on a smaller scale ▪ The locus of a few large financial centres embeds international flows in these few places
Late-1980s onwards	New re-regulation	▪ Increased systemic risk from increased exposure to derivatives and fall-out from associated scandals, as well as the East Asian crisis, leading to demands for global re-regulation ▪ In the European Union, the single European Market Programme of 1992 extends Europe-wide

		regulation to financial markets ▪ Combination of electronic trading and moves toward regulatory 'level playing field' threatens locational embeddedness of large centres though increase in placeless financial flows ▪ Negotiation of real estate markets as strategy of re-regulating and re-embedding financial flows into specific financial locales
(Source: Budd, 1999: 119)		

The privatisation of national economies was another trend that became ubiquitous alongside processes of deregulation and re-regulation. From a regulationist point of view, the large scale state-ownership of services and industries in the 20th century formed a logical component of the Fordist regime of economic production and accumulation. But since the 1980s, this model has been unravelling under the pressures of transnational flows of trade and finance. The privatisation of public-sector activities was partly due to the collapse of the Keynesian welfare state model, but also partly a product of political-ideological motives to create a 'popular capitalism' by spreading individual share-ownership across society. 'Selling off the state' became a global phenomenon and accepted state economic policy, especially in the former socialist bloc (Martin, 1999b). In the case of Britain, for example, the privatisation of British Telecom and the flotation of other state assets were amongst the core policies of Thatcherism. Martin's (*ibid.*) study shows that the ambition to make Britain a nation of shareholders was, however, largely unfulfilled as there was a larger increase in institutional investors than individual investors. The size of large institutional shareholders was such that they could have considerable influence over equity markets and company stock valuations. The rise of this 'money manager capitalism', in which large international financial institutions came to own significant portions of economic assets (through their control of finance capital) in various national economies around the world became a considerable economic force that state actors had to reckon with.

More recent work within this tradition has explored the transformation of financial space in more detail, such as the growth of 'offshore' financial spaces, where more permissive regulatory environments served as havens from the restrictions that national governments placed on financial activities (Roberts, 1994, 1995; Hudson, 1998, 1999; Cobb, 1998). Hudson (1999), for example, examines the links between onshore and offshore regulatory spaces in the development of international banking facilities in US and its relationship to offshore financial activities in the Bahamas and Cayman Islands. The development of OFCs was in part a response to increasing onshore restrictions. International banking facilities were then established in the US to attract monies back onshore although they failed to do so due to a variety of social and historical reasons.

Leyshon and Thrift (1997a) speculated on the rise of a 'phantom state' in which governance is no longer based on individual nation-states but rather transnational linkages of overlapping actor-networks: the nation-state, the media, money capitalists and machine intelligence. During the Bretton Woods period, money capitalists were held in check by state regulation. Post-Bretton Woods, power shifted back to money capitalists who have gone global with advances in ICT. But even as power shifted from state-based institutions to transnational actors and increasingly disembedded flows, the pressures of multiple networks lead to the need for embodied, interpersonal and face to face interaction. Therefore there is both an invisible and visible hand – disembedded electronic spaces as well as re-embedded set of meeting *places*. Places such as the City of London, for example, became a centre for face to face communication, electronic information gathering and transmission, textual interpretation, cultural authority (*ibid.*: 318-319). The rise of a 'phantom state' is thus based on ICT and a few (g)localities, consisting of actor-networks that rely on money-power and communicative power rather than bureaucratic administrative power of the state form.

Even as some scholars point to the shift in power from states to markets (Strange, 1994; Clark, 1999; Martin, 1999b; Warf, 1999), others have pointed to the continued relevance of the state in the international financial system through its regulatory role (Budd, 1999; Helleiner, 1995; Laulajainen, 2000). States remain important arbiters in determining the shape of finance and governments have continued to put considerable efforts at writing international rules in favour of either firms from their territories, such as the U.S. lobbying of the Bank for International Settlements and the WTO, or their territorial interests, evident in how the Bank of England promotes the interests of the City of London (Cohen, 1998). The role of the state is clearly vital in creating and maintaining the *physical* infrastructure that is necessary for a city's high standing within the network of global cities, but national and local state agents are also highly implicated through their contributions to the *institutional* infrastructure of these cities. State regulation, in particular, is an important part of 'institutional thickness' (Amin and Thrift, 2000) – a product of the interaction and collective strategies of institutions of all kinds, including firms, financial institutions, trade associations, non- or inter-governmental organisations, economic development agencies as well as state and local governments – that seems to set successful places and regions apart from others in the global economy. The growing importance of supranational organisations and international forums of monetary and economic coordination, such as the Group of Seven (Gill, 1993) and Bank for International Settlements (Simmons, 1993) are also noted. All these development has a tendency towards 'deterritorialisation' such that conventional understandings of state power and economic boundaries are blurred and works on geographies of money and finance become more concerned with flux, fluidity and the geography of flows (Thrift and Johnston, 1993).

At this point, it is important to note that the end result of the above processes is not an evenly integrated, global 24-hour financial market-place or that the international financial system has brought about the ‘end of geography’ (O'Brien, 1992). The development of transnational market structures has been very uneven and although the major trends are toward global integration, most markets can be found along a continuum from being highly globalised to being essentially national with some transnational linkages. The world, therefore, remains a patchwork of different financial spaces or systems; the patchwork that is the nation-state, to a certain extent, represents a geography of capitalisms (Agnew, 1994; Lash and Urry, 1994). What is clear is that such developments point to tensions emerging in the geography of money and finance, between processes of disembedding and homogenisation on the one hand and re-embedding and difference on the other (Leyshon, 1996).

Implications for Research

Within the long-term context of regulatory changes, different models of financial systems have fallen in and out of favour throughout history (Leyshon and Thrift, 1997; Warf, 1999; Martin, 1999). A mode of structural regulation is prominent within the Marxist perspective that views the finance sector as being parasitic, as well as with the Keynesian model that emphasises control due to the fear of contagion. This was seen in the compartmentalisation of financial activities prevalent in the 19th and 20th centuries. With the crisis of the Keynesian state and Fordist regime of accumulation, this gave way to a different mode of regulation that tends to set broad guidelines and emphasise notions of accountability and transparency instead of centralised control. The first model views the role of finance as being solely to lubricate the wheels of the economy, and the objective is therefore to be conservative so as to limit the risk of crisis and contagion. This is in contrast with the second model that has a very different self-image in which finance has a purpose in and of itself, with its own autonomy, authority and logic that operate in a brave new world of brash financiers and fluid rules (Budd, 1999). As such, it should not be constricted but allowed to flourish and innovate, albeit within certain guidelines and a fair regulatory environment.

How is China's financial system reforms and process of market formation reflective of the above trends? The first view seems to match China's current experience as its regulators seek to enforce and maintain control over every aspect of the financial system as far as possible. Unlike commercial banks in the UK, US or Singapore, banks in China are much more limited in the types of financial activities they are allowed to conduct. For example, while a single bank in New York might offer bank deposits, asset management, financial leasing and consultancy, these activities are divided up among separate and specialised financial institutions. The rationale is that if one part of the financial market should fail, the crisis would be confined to one sector and not spread across the system as a whole, thereby limiting the economic and social impact (and political consequences, by implication). The priority of limiting risk and contagion is clear.

The stock market listing process is another example. Every initial public offering (IPO) application has to be individually approved by the China Securities Regulatory Commission (CSRC) according to a rather opaque list of criteria that includes a quota for each province. If the quota for a particular province has been exceeded for that year, a company would not be able to list during that round. On the other hand, a less competent and valuable company from another province that has not filled its quota would be able to list that year. In recent years, new IPOs have also been suspended due to fears that the market is not able to absorb new IPOs. Such decisions are thus taken out of the 'invisible hands' of the market and market participants and firmly held within the visible hands of the regulators. The fear of losing control (and the possibility of dire consequences) is clearly holding back the pace of financial reforms.

Even as states remain important arbiters in determining the shape of finance within their national economies, they have to negotiate with a range of actors and institutions that operate on and across spatial scales: from international financial institutions and individual money capitalists to other state actors and interest groups. By engaging in a detailed enquiry into the process of market formation in Shanghai, my research findings could offer valuable insights into how state actors manage tensions between the desire to maintain regulatory control and the imperative of global financial capital.

3.3 THE SOCIAL CONSTRUCTIVIST APPROACH: THE MAKING OF INTERNATIONAL FINANCIAL CENTRES

Within the literature on geographies of money and finance, an alternative approach to the relationship between money, space and place can be labelled broadly as social constructivist. This approach, which has proved particularly popular over the last decade, rejects smooth linear accounts of social change and favours instead disjunctive, interrupted and non-linear accounts. In contrast to the notion of progress and the value of rationality encapsulated by the political economy approach, social constructivism sees 'truth' and our understanding of the world as contingent and contextual, varying across time and place. This breaks from the tradition of treating and defining money as purely economic as geographers seek inspiration from the work of sociologists who see money as a partial and anthropological phenomenon. This belies the idea of a single, centred model of money in favour of viewing money as being constituted in different networks of human practices and used and thought of in different ways. Monetary networks can thus be conceptualised according to different properties and practices, such as calculative practices, regulative practices, spatial practices, reflexive practices, and practices of sociability (Leyshon and Thrift, 1997a: 189-190).

How does a more social and cultural construction of money and finance improve our understanding of global financial space and places? The persistence, and indeed, increasing importance of international financial centres as strategic basing points for global capital in a world of fast-flowing and switching monies is a paradox that has particularly benefited from a social constructivist perspective. Its critical stance on the construction of 'knowledge' and 'reality' highlights the importance of problematising taken-for-granted categories such as money (Leyshon and Thrift, 1997a; Leyshon, 1997), gender (Rose, 1993) and the economy (O'Neill and Gibson-Graham, 1999).

As opportunities arise due to regulatory gaps in different national systems (e.g. between New York and London, which led to the development of the Eurodollar market), international financial markets grew out of a combination of official policy and market responses. The increased globalisation of finance is due to the constant search for above average returns through financial innovation and risk management. This led to the rise of a 'global neoclassicism' whereby financial globalisation is the agency through which national economies become subservient to international markets (Budd, 1999). Although the internationalisation of financial markets may have promoted the conditions for global neoclassicism, the change in the nature of the relationship between money and space is complex and specific localities remain critical in the production and reproduction of global finance, as evident in studies done on the development and territorial embeddedness of financial centres (Roberts, 1994; Leyshon and Thrift, 1997b; Thrift, 1998; Budd, 1999; Hudson, 1999; Porteous, 1999) as well as their social and cultural constructions (Thrift, 1994, 1996, Clark and O'Conner, 1997; Leyshon, 1997; Reszat, 2002). The concept of monetary networks, for example, was particularly instructive in theoretical analyses that explored the mutual constitution of the global and the local (see Martin, 1994; Clark and O'Conner, 1997; Beaverstock, 2002), in which "there is not a global financial structure 'out there', as a *deus ex machina*, but rather a spatially distributed network of money/social power which encompasses the globe… [The] local and the global intermesh, running into one another in all manner of ways" (Thrift, 1990: 81; quoted in Tickell, 2000: 235).

Although the international importance of the City of London, for example, in the international financial system was vigorously promoted by a series of regulatory decisions made by the British authorities (such as those relating to the 'Big Bang' in the 1980s) (Pryke, 1991; Strange, 1994), financial centres also develop and are sustained by information, expertise and contacts (Porteous, 1999). Economic geographers have sought to unravel the apparent paradox of the durability and persistence of international financial centres in an age where ICT would appear to be shrinking the world in dimensions of both time and space (Marshall, 1988; Daniels, 1987, 1993). Although not strictly in the social constructivist vein, the works of Saskia Sassen (1991, 1999, 2000, 2002a) have been instrumental in theorising the role of centrality and concentration in the development of international financial centres. She argues that the transformation of the world economy over the last two decades has been accompanied by a shift towards services and finance, which have renewed the importance of major cities as sites for certain types of activities and functions. These global cities are centres of command in the organisation of the world economy, as key locations, marketplaces and major sites of production and innovation for finance and specialised services. But even as particular cities (such as London and New York) become dominant, global cities must inevitably engage one another in fulfilling their functions as this new form of growth seen in these cities are the results of these *networks* of cities – "There is no such entity as a single global city" (Sassen, 2000: 4, see also Knox and Taylor, 1995; Sassen, 2002b).

The notion of centrality is extended by Nigel Thrift (1994, 1996) who focuses on the importance of culture and embodiment within the monetary networks that make up the modern financial centre. He explains why international financial centres have not simply melted into a generalised and electronic 'space of flows' (Castells, 2000) by considering the influence of a wide range of social and cultural factors contributing to their success and survival. This departs from a more abstract political economy approach by conceptualising financial centres as active and dynamic ensembles of networks – of bodies, machines, concepts, interpretations and information. Information is particularly important as the role of a financial centre is to generate, capture and interpret the vast amounts of monetary information that flows through every day. Rather than merely physical locations of financial markets and institutions, international financial centres are centres of representation and chief points of surveillance for the global finance industry, centres of expertise where product innovation and marketing are conducted, and centres of social interaction amongst finance workers (Thrift, 1994: 335-336). Successful monetary networks within the financial system are bound to particular places; to go beyond the network and localities means stepping outside the loop of information, knowledge and interpretation. Such a step could be extremely costly in a financial world that has become increasingly complex and speeded up. Focusing on the City of London, Thrift shows how the City's role as a centre of knowledge, expertise and contacts, of narrativity, has persisted and even increased in importance with the increase in speed and volume of capital flows and human mobility.

The issue of trust is another important feature of the literature, which explores how the business of finance still thrives on close inter-firm and inter-personal relationships, such that physical proximity as being in an international financial centre is integral to the operation and reproduction of the financial system itself. Although formal institutions and mechanisms exist that underwrite trust in finance, such as credit rating agencies Standard & Poor and Moody's (Sinclair, 1994, 2000, 2001), informal and personal relationships continue to be vital lubricants in the wheels of international finance. As the financial system becomes increasingly complex, such trust relationships have also become central strategies to reduce risk through the development and maintenance of interpersonal relationships, often achieved through regular face-to-face contact (Zuker, 1986; Boden, 1994). This "active construction of trust" (Thrift, 1994: 335) is more easily performed in relatively spatially circumscribed spaces such as financial centres, although trust relationships are also vulnerable to abuse, as in the case of fraudulent activities that led to the fall of Barings Bank (Tickell, 1996; Clark, 1997).

As geographers begin to pay greater attention to the significance of discourses and metaphors in shaping spatial formations (Barnes, 1992; Neil and

Katz, 1993; Schoenberger, 1998; O'Neill and Gibson-Graham, 1999; O'Neill, 2001; Bunnell, 2002), the importance of discursive representations, practices and narrativity is increasingly explored in research on financial centres. The term 'discourses' can be used to broadly describe various ways through which meanings are constructed and conveyed (un)intentionally to their recipients. These meanings are often embodied in representational devices such as metaphors and analogies and are transmitted through communicative materials such as texts, speeches, films, images and so on. As such, the acceptance and deployment of discourses are highly politicised acts because the process reflects the ideological stances of the actors and agencies involved and influences their responses and actions. The active branding exercise conducted by state actors and institutions has become critical to the imaging of particular global cities as having the right credentials and expertise to claim the status of 'international financial centre' in a world of flux. The City of London, for example, increasingly markets itself as a centre of cultural authority for global financial services and as a place where people meet from around the world due to the knowledge, expertise and contacts concentrated there. To this end, there is a 'rediscovery of tradition' as the City consciously plays to this role:

> The old gentlemanly discourse may have dissolved but the 'trappings of trust' still remains: quiet, wood-panelled dining rooms, crested china, discount round top hats, City police uniforms and so on are all used to 'brand' the City, to boost its image of solidarity and trustworthiness. (Thrift, 1994: 350)

Such branding exercises are more than symbolic reconstruction; they have material consequences with the reconfiguration of city centres to meet the demands of capital. The development of the London Docklands and Battery Park City in New York are the material expressions of a shift from organising the city as an assortment of concrete production spaces towards visualising it as a coherent space of abstract financial processes and consumption (Zukin, 1992). The building of Shanghai as an international financial centre draws from various discourses out of ideology at the national level, political aspirations at the municipal level, from narratives of historical success and eminence, and particular visions of 'global city' status and what that might entail (Olds, 1997). Yet, in developing capitalist spaces of finance, the landscape of power reflects the institutional interventions of the national and local states as well as the social and cultural reorganisation of business, political and artistic elites who wield varying levers of social power. The representations of specific visions or versions of reality embody particular agendas but the power to represent is also limited and countered by the power to resist those representations as other economic actors and institutions draw upon differing and distinctive experiences and counter-discourses (Kelly, 2001; Lai and Yeung, 2003).

All these literature relate to a broader trend of problematising the 'economic' in economic geography, reinforced by an increasing number of articles by geographers informed as much by cultural studies and feminism as by traditional economic theory or political economy (Barnes, 1996; Thrift, 1996; Rothbard, 1998). Studies in this vein range from the iconography of the City's built environment (Jacobs, 1994), to analyses of media representations of financial crises (Tickell, 1996; Kelly, 2001), to issues of gender relations and representations of the body and embodiment in understanding the spatialities of financial services and practices (McDowell, 1997; McDowell and Court, 1994a, 1994b; Leidner, 1991, 1993). Economic activities are social and cultural processes that are not merely shaped and directed by distinctive sets of social relations but actively constituted through social and cultural practices that cannot be reduced to stimulus-response models of rational economic actors or the socially-sterile operation of economic forces.

Implications for Research

An approach that emphasises the social and cultural construction of financial centres is useful in examining Shanghai's financial centre development with the recognition that it is driven by a range of actors who cannot be reduced to rational, economic entities. Economic actors are inherently social, cultural and political; they have different politics, agendas, interpretations and practices that operate at and across various spatial scales in monetary networks. Viewing money as being constituted in different networks of human practices brings to the fore the necessity of critically examining these contestations of meanings and the process of negotiation between owners of finance capital, state actors and other agents of power.

In the case of Shanghai, its financial centre development in banking and securities is very much influenced by forces and actors operates from and across different spatial scales. The SMG and the Lujiazui Finance Commission pursue specific urbanisation projects and implement policies such as tax incentives geared towards the capture of international capital flows by attracting international financial institutions. However, this process is also strongly influenced and driven by actors elsewhere: on the one hand, the interest and politics of officials in Beijing who are attuned to national development strategies as a whole as well as Beijing's own financial centre aspirations; on the other hand, the international banks and financial institutions that have become crucial to the functioning and image of an international financial centre and how business activities in Shanghai might fit into the global investment strategies of their own corporations. A deep analysis of how development in Shanghai is driven and influenced by processes elsewhere and how this process is negotiated will improve our understanding of the international financial system, relationship between state actors and global capital and how financial centres operate within international monetary networks. Sensitivity to the importance of scalar politics in such processes will also be a useful geographical contribution to the money and finance literature (see Swyngedouw, 1992; H. Yeung, 2000).

The historical image and contemporary branding of Shanghai as a cosmopolitan world city and international financial centre play a significant role in its development strategies. This is prominent in official discourses and (state-controlled) media representations as well as the expectations of foreign investors. How do these discursive representations and interpretations influence (and are constituted by) policy actions and investment strategies? A more socially inflected approach is necessary in teasing out such motivations and their rationale and practices, which are crucial to the development of Shanghai as a financial centre.

3.4 CONCLUSION

In the first part of this chapter I highlighted the political economy approach in emphasising the interconnectedness of economics and politics across international as well as national scales. I examined how various scholars have treated the concepts of hegemony and post-hegemony in the regulation of the international financial system and explored their relevance for China's changing economic structure and the development of financial markets in Shanghai. The changing roles and relationships between states and finance capital in the on-going process of spatial-regulatory arbitrage is another important feature of the literature. Even as power appears to shift from states to markets, the state maintains a crucial role in the international financial system through its participation within supranational organisations such as the WTO and IMF, and maintaining the physical and institutional infrastructure of global cities. While states remain important arbiters in determining the shape of finance within their national economies, they also actively negotiate with a range of actors and institutions across spatial scales. This tension between the desire to maintain regulatory control and to meet the imperatives of global financial capital has to be constantly balanced and renegotiated.

The second part of the chapter focused on the social and cultural embeddedness of money and finance and the social constructivist approach which belies the idea of a single, centred model of money in favour of viewing money as being constituted in different networks of human practices and used and thought of in different ways. This highlights the significance of place in the formation of international financial centres as specific localities remain critical in the (re)production of global finance. The centrality of knowledge, the importance of socio-cultural elements such as trust in economic transactions, and discursive constructions of space and place all have important bearings on the flows and structure of global finance. Viewing money as being constituted in different networks of human practices highlights the significance of contested meanings and processes of negotiation between owners of finance capital, state actors and other agents of power.

One of the key objectives of this thesis is to critically engage with the concept of 'markets', to expose its multiple identities and conceptualisations and examine the contested nature of the 'marketisation' process. In the next chapter, I turn to research on the framing of financial markets and its role in the formation of a financial centre. Although this falls under the social constructive perspective in Table 3.1, I have devoted Chapter 4 to examining and problematising its conceptualisation in various fields due to its significance to my arguments. The literature in economic geography has been largely silent on the role of markets and the actual process and politics of market formation that is crucial to a modern financial centre. A theoretical engagement with markets and its conceptualisation in various fields could thus provide additional insights to studies of geographies of finance and processes that drive the international financial system.

Chapter 4

Framing Markets

4.1 INTRODUCTION

> *"The market, it turns out, is the hollow core at the heart of economics" – John Lie (1997: 342)*

> *"The market is no longer a safe place to theorise. Its longstanding neutrality is being increasingly violated by scholars from various disciplines who refuse to treat the market as a purely economic institution." – Viviana Zelizer (1988: 614)*

Contemporary social sciences, including economic geography, have largely overlooked the conceptual and political status of markets and market formation. Whether as an idea(l), a system or as economic practice, markets lie at the heart of capitalist societies but they remain one of the most elusive concepts within social sciences and the challenge of engaging with contemporary capitalism though the theoretical lens of the market has gone largely unmet (Sayer, 2001). In line with the social constructivist perspective, I wish to highlight two points in the treatment of markets. First, markets, like other institutions involved in economic practices, are not ontologically stable, unified, straightforward or entirely predictable (see Gibson-Graham, 1996; O'Neill and Gibson-Graham, 1999; O'Neill, 2001; Slater, 2002). They are riddled with contradictions, full of complexities and operate in changing contexts as various actors (be they states, firms, institutions or individuals) interact in the active production of markets (ideas, practices, regulations etc.). Second, in acknowledging that markets are the products of social relations that vary across time and space, empirical research needs to examine how financial markets are being constructed, regulated and reproduced. Who are the actors involved in the making and maintenance of a market? What are the historical, social and cultural factors affecting these processes and in what ways?

Although some geographers have examined the construction of various financial markets (see, for example, French, 2000, 2002; Hall, 2007), the literature on geographies of money and finance has been largely silent on the role of markets and the actual process and politics of market formation that is so crucial to a modern international financial centre. A theoretical engagement with markets can provide additional insights to studies of geographies of finance and processes that drive global cities. Even though much of contemporary social sciences have largely written over markets as social practices, disciplines such as heterodox economics, economic sociology and economic anthropology are well ahead of the game compared to economic geography in exploring the conceptual and political significance of the market. In this chapter, I examine the different ways of theorising the market in orthodox and heterodox economics (e.g. new institutional economics), economic sociology, anthropology and cultural studies and assess their contributions and implications for my conceptual understanding and empirical study of Shanghai.

4.2 ORTHODOX ECONOMICS

The classical period of economics is usually defined by the publication of Adam Smith's *Wealth of Nations* in 1776 and John Stuart Mill's *Principle of Political Economy* in 1848. Classical economists place great emphasis on the concept of *laissez faire* to resolve conflicting self-interest in a manner that would benefit the community as a whole, via the 'invisible hand' of market competition as depicted by Adam Smith. Orthodox economics, in both the classical and neoclassical traditions, has the tendency to treat market exchange as the base for all economics activities, portraying other organising principles as second-rate or sub-optimal alternatives. This exchange system consists of individual actors, each acting rationally to maximise their individual utility. As such, it is in the individual's best interest to produce what they are most economically efficient at and exchange the surplus produced with other actors who have also produced what they are most economically efficient at producing. This "market optic" (Sayer, 2003) not only privileges the market over other modes of economic and social organisation but also abstracts economic action from wider political, social and spatial contexts. Neoclassical economists abstract the market from concrete places and social relations to an isotropic space where all producers have equal access to transport, labour and raw materials (i.e. the *ceteris paribus* principle). The concern is thus with the *abstract* interplay of forces of demand and supply, concentrating on the circumstances in which these will tend towards *equilibrium*.

> A market exists when buyers wishing to exchange money for a good or service are in contact with sellers wishing to exchange goods or services for money. Thus a market is defined in terms of fundamental forces of demand and supply and is not… confined to any particular geographical location (Bannock, Bexter and Rees 1978: 297, quoted in Lie, 1992: 509)

As such, the neoclassical market is devoid of social relations, institutions, geography and sociological concerns such as power, norms and networks. There is a belief in the natural, evolutionary progress of the market as a succession of solutions – with perfect competition, information, mobility and the *laissez faire* government protecting property rights – that is continuous and consensual rather than discontinuous and conflictual.

Sustained discussions of the market occur primarily among critics of the orthodoxy. Five common theoretical and epistemological stances can be identified in heterodox economics such as institutional economics, economic sociology, and economic geography that are in many ways responses to the perceived limitations of orthodox economics. First, they tend to share broader socialised and plural conceptions of the economic, with particular interest in understanding the interdependencies between places and individuals, between economic, political, social and cultural processes (Sheppard, 2000). Second, space is conceptualised as heterogeneous instead of isotropic, places are different in site and situation which create different possibilities for economic action. This is evident from discussions in Chapter 3 on international financial centres and offshore centres that have played crucial roles in driving global financial services in particular ways (Thrift, 1994; Cobb, 1998; Hudson, 1999). The historical and institutional contexts of difference places are also emphasised instead of written off in the neoclassical tradition (North, 1990; Hodgson, 2000). Third, they share a commitment to primary data collection and ‘dirty hands’ in the pursuit of grounded theorising (Hirsch et al., 1987; Peck, 2005). Apart from in-depth, semi-structured interviews, a wide range of qualitative methods is used such as participant observation and ethnographic studies (Abolafia, 1998; Hertz, 1998) and corporate autobiographies (Schoenberger, 2001). Fourth, they do not believe that an ‘equilibrium’ can exist as the economy is constantly being (re)constructed through everyday production, distribution and consumption that are steeped in processes of power and negotiation. More attention is thus paid to disequilibria and the dynamic unpredictability of much of economic life (Sheppard, 2000). Fifth, there is a shared scepticism about the logical and normative superiority of markets, and a healthy disregard for disciplinary boundaries.

Beyond these broad inter-disciplinary similarities, a significant difference can be identified in terms of the empirical object of study between economic geography and other heterodox economics: the former has not taken the market seriously as an object of study in its own right to same extent. Research on geographies of finance has typically concentrated on money but has not seriously engaged in research on the market.[1] This is potentially problematic since to be taken seriously in academic and policy circles outside of economic geography, it is erroneous not to make a theoretical and empirical claim on the market seeing as it lies at the heart of our *market* capitalist societies.

4.3 ALTERNATIVES IN ECONOMICS

4.3.1 Institutional and Evolutionary Economics

While economic geography has been slow in engaging directly with debates about markets,[2] other fields have developed different ways of conceptualising and engaging with market theories and practices. New institutional economics and evolutionary economics have sought to overcome the limitations of orthodox economics by attempting to infuse institutional and historical factors into their analysis. Hodgson (1999: 3) argues that "formalism [as practiced in neoclassical economics] became a way to escape from reality rather than a tool to help it". The abstraction of economic action from the wider social sphere and its analysis in isolation made the resultant explanations unrealistic. These critics argue for the need to study real economic processes, systems and institutions, instead of creating simplified models that do not apply to the real world.

[1] Although this has started to change in recent years as more geographers are engaged in the new inter-disciplinary grouping called the Social Studies of Finance (see section 4.4).
[2] It is worth noting, however, that much of recent economic geography research has drawn from heterodox approaches to markets, such as institutional approaches and conceptions of embeddedness in studying industrial districts, creative clusters and regional development (see, for example, Grabher, 1993; Amin and Thrift, 1995; Amin, 1999; Asheim, 2000; Feldmand, 2000; Scott, 2000b)

Institutions are taken as the unit of analysis, defined as generally accepted and recognised systems or routines that organise human actions and activities (Mäki and Gustafsson, 1993: 13). Institutions also define and limit the set of choices available to individuals through formal and informal rules that guide actions and behaviours (North, 1990). As conditions such as perfect information and mobility do not exist in the empirical world, transaction costs in the form of collecting information and enforcing rights are likely to be high. In this aspect, institutions help to provide regulatory frameworks and stability through the implementation and enforcement of acceptable forms of behaviour and procedures. Rather than being treated as isotropic, the environment of the decision-maker is accorded special significance in institutional analysis where there is significant distinction between the real world and the actor's perception of it, which is in turn affected by institutional contexts. This concept of *bounded* rationality is introduced in contrast to the neo-classical concept of *perfect* rationality. The creation of knowledge is a socially-embedded phenomenon and process. More than just the input of facts, learning also involves interpretation, development, reconstitution, creation and destruction, all of which are contingent upon institutional contexts, social norms and values (Hodgson, 1999). Such institutional constraints in knowledge construction and adoption may lead to a situation of path dependency. Because of such path dependencies, history matters; there is a need to understand the past in order to explain present phenomena and processes. In terms of policy-making and recommendations, this also has implications for the transferability of solutions; the same rule or solution may not create the same type or magnitude of development in different places due to their specific historical experiences and institutional configurations. Therefore, institutional analysis highlights the awareness of such constraints in economic and political models and their relevance in cross-applications. In contrast to models of stage-by-stage linear economic development with the input of the requisite economic factors, institutional economists caution that what may be the most effective and efficient policies in one instance are unlikely to be so in all environments.

In their effort to bring knowledge, uncertainty, history and other institutional considerations (i.e. transaction costs) into the discourse of economics, institutional and evolutionary economists overcome some of the limitations of the neoclassical approach. However, their analysis remains politically thin. To the extent that they discuss power and institutions, the focus remains on the state and property rights and they share the neoclassical problem of neglecting power struggles among social groups. Although state actions are alluded to in the form of legislation and law enforcement, they fail to include the interventionist role of the state, as policy-maker and entrepreneur, who may be very active in the creation and adaptation of social and economic institutions. Governments thus assume a neo-liberal and non-interventionist approach in their analyses, which exclude how developmental states, for example, may contribute very significantly to the institutional development, and economic performance and trajectories of their national economies. This lack of consideration given to the political economy, and the interventionist and entrepreneurial role played by state agencies present a conspicuous weakness in institutional analysis.

4.3.2 Economic Sociology and Embeddedness

> *"If economic action is embedded in networks of relations, it is logical to begin our investigation by discussing the nature of those relations." – Granovetter (1993: 3)*

In economic sociology, the rational, individualistic and utility-maximising *homo economicus* is rejected in favour of a wider and richer conception of the socially constructed actor whose actions are constrained and influenced by cultural norms group relations and other social and meaning structures. Instead of 'freezing' social relations while focusing on economic exchange, the market and the economy in the manner of neoclassical economic practices, the sociological conception of economy views market relations as being socially structured and constituted, and argues that the 'economy' cannot be fully understood without examining the institutional and cultural parameters that constitutes its societal context.

Most contemporary American economic sociologists work under the banner of the embeddedness approach in which network analysis is particularly important. In 'The Great Transformation', Karl Polanyi argues that the increasingly market-based nature of 19th-century Western society meant that "instead of the economy being embedded in social relations, social relations are embedded in the economic system" (Polanyi, [1944] 2001: 60).[3] As economic life is embedded in broader social, political and cultural settings, social and structural factors are crucial in examining economic relations and phenomena:

> The human society, then, is embedded and enmeshed in institutions, economic and noneconomic. The inclusion of the noneconomic is vital. For religion or government may be as important for the structure and functioning of the economy as monetary institutions or the availability of tolls and machines themselves that lighten the toil of labour" (Polanyi, [1957] 2001: 36).

Therefore, there is nothing automatic or *laissez faire* about the growth of market society as it "is never traceable to the mere desire of individuals to truck, barter and

[3] Polanyi used the term 'embeddedness' to refer to a particular moment in capitalism's historical development at a macroeconomic and social scale, but its usage has since been expanded by sociologists and geographers.

exchange" (quoted in Lie, 1993: 277). It was new economic sociology, and the work of Mark Granovetter in particular, that moved the embeddedness concept from its initial societal scale analysis to a more institutional and actor-based account of economic life. His influential paper, 'Economic Action and Social Structures: the Problem of Embeddedness' (1985), grew out of a conviction that in order to address the inadequate treatment of economic phenomena by economists, such as the neglect of social structures and reduction of individuals to isolated actors, sociologists should attempt to 'embed' economic actions and activities in social structures conceived as interpersonal networks. More specifically, he was critical of what he called "oversocialised" and "undersocialised" conceptions of economic actions and actors in both economics and sociology as both views suffer from isolating actors from their immediate social contexts:

> Actors do not behave or decide as atoms outside a social context, nor do they adhere slavishly to a script written for them by the particular intersection of social categories that they happen to occupy. Their attempts at purposive action are instead embedded in concrete, ongoing systems of social relations (*Ibid.*, p. 487).

The embeddedness approach is thus proposed as a "middle ground" or "third way" (Powell and Smith-Doerr, 1994: 368) between oversocialised and undersocialised views. Economic action takes place within the networks of social relations that make up the social structure, and the "problem [is thus about]… to what extent economic activity is mediated by – or shall I say, 'embedded in' – networks of personal relations" (Granovetter, 1990: 96). Others such as Zukin and DiMaggio (1990) have attempted to distinguish between different types of embeddedness, such as cognitive, cultural, structural and political. The fallacious separation of the economic from the social, typical of conventional economic analysis, is also rejected, with the view that market actions are constituted and shaped by the social relations, institutional norms, and interpersonal networks in which they are embedded.

The disciplinary objective of new economic sociology is to reclaim 'core' economic issues (such as the market) rather than focusing on the economic 'leftovers' such as analysing 'irrational' behaviour and 'suboptimal' institutions because "social relations are *fundamental* to 'market processes'" (Granovetter, 1985: 500; added emphasis). Take the concept of the market, for example. The neoclassical market is highly abstracted, stripped of social relations or institutions and devoid of sociological concerns like power, norms and networks. The embeddedness approach on the other hand argues that social networks "built on kinship or friendship, trust or goodwill" (Lie, 1997: 349) are necessary to build and sustain economic relations and institutions such as markets. Instead of simply examining markets in terms of price mechanisms, economic sociologists treat markets as social structures and in terms of exchange (i.e. networks) (Swedberg, 1994). In avoiding both the oversocialised and undersocialised approaches, the embeddedness approach seeks to strike a balance in analysing markets and other economic phenomena and institutions, while emphasising power and control struggles as constituent elements of markets by examining the state and legal systems, social relations of market actors and different types of markets, such as 'flea markets', peasant economies and bazaars (White, 1981; Granovetter, 1993; Lie, 1997). White's (1993) analysis of production markets emphasises struggles for control and autonomy that generate the market as a social category. Mizruchi and Stearns (1994) highlight the contribution of a sociological approach to money, banking and financial markets in making explicit the cultural embeddedness of money and monetary institutions, examining the effects of social networks on economic decision-making and the ways in which social and political power influence both economic action and the character of economic institutions. Lie (1991: 230) argues that:

> By taking the embeddedness thesis seriously, we can penetrate the ideological veil of the market to reveal the distinct social organisations of commodity exchange. … Rather than assuming the invisible hand, we should investigate the concrete social relations of those who buy and sell: the *visible* hand of the market. (Emphasis added)

Despite its widespread currency in economic sociology and other social sciences, the concept of embeddedness and networks remain theoretically underspecified in many ways. Rather ironically, some works by economic sociologists suffer from the very abstraction and reification of categories which were found wanting in mainstream economics. For example, in defining the sociological approach to the economy, Granovetter asserts economic sociological research should be guided not by conventional disciplinary boundaries but the analytical aspect of networks of ongoing social relations. According to this conceptualisation, new economic sociology becomes an exercise in abstraction in which concrete objects are examined in a single aspect (i.e. networks) rather than in their complex multi-dimensionality (Krippner, 2001).[4] In taking up the challenge to treat market activity as a social phenomenon, a common approach has been the 'add-social-context-and-stir' method, which involves correcting the economic model of a 'free' market by uncovering non-economic constraints of economic. There is also a tendency to defer to an idealised market by placing the market at one end of a spectrum with more socialised versions of the economy along the opposite end, or to rely on the abstract market as an analytical foil. Paradoxically, this could contribute to the very

[4] As such, Granovetter's concept of embeddedness departs from Polanyi's usage which calls for the analysis of concrete institutions in terms of multiple intersecting dimensions, and in their complex political, cultural and ideological contexts.

naturalisation of markets that it sets out to transcend by theorising context and embeddedness in such a way that it seems easy to siphon them off from a 'pre-social' market. This kind of conceptual slippage leads Peck (2005: 145) to question: "are *all* economic phenomena socially constructed and embedded, or are some markets more embedded than others?" (Original emphasis) Krippner also criticised the 'adding' social consideration to market analysis and the concept of a continuum:

> [E]very transaction, no matter how instantaneous, is *social* in the broader sense of the term: congealed into every market exchange is a history of struggle and contestation that has produced actors with certain understandings of themselves and the world that predispose them to exchange under certain set of social rules and not another. In that sense, the state, culture, and politics are *contained* in every market act […] (Krippner, 2001: 785; original emphasis)

Sayer (2003) also criticises the tendency in theorising about embeddedness, networks and trust within economic sociology to idealise them, such that it inadvertently produces an overly *benign* view of economic relations and processes. Economic relations that were previously seen as governed by narrow self interest are embedded in relations of trust, in which there are shared norms and forms of reciprocity. But the social embedding of economy activity also often involves relations of *domination*, some of them based on gender, class or race. Relations within and across networks are seen to be more reciprocal and more egalitarian because of the emphasis on interaction, but not all networks are non-hierarchical or mutually beneficial. This idealistic and 'soft' conceptualisation of networks downplays issues of power and inequality. Stable forms of embedding such as networks or regulation are also not necessarily the product of free consensus, they may represent an uneasy compromise between interests that would realign themselves given the opportunity (such as in a crisis). Thus, networks do not necessarily fuse the self-interest of different actors into a harmonious and egalitarian whole but may be characterised by inequalities of power, strategic coalitions, dissembling and opportunistic collaboration. However good the networking, or however strong the reliance on information and trust, economic survival for capitalist firms depends on costs and cash; although extraordinarily this literature says remarkably little about these factors, the bottom line remains the bottom line (*Ibid.*, p. 50).

The challenge of incorporating macroeconomic structures and issues of power and conflict has not gone unheeded. John Lie (1992, 1993), for example, has proposed the concept of 'mode of exchange' as an alternative to the disembedded concept of the market offered by neoclassical economics. This mode of exchange refers to "an ensemble of traders engaged in commodity exchange under historically specific technological and socioinstitutional constraints" (Lie, 1992: 510). Rather than portraying the rise of market society as an evolutionary progress toward a homogenous market, Lie emphasises the *variety* of forms assumed by the 'mode of exchange' and analyses commercial history as a product of power struggles among social groups attempting to shape exchange relations in their interest. The case of England is used to show how different modes of exchange waxed and waned from 1550 to 1750 (Lie, 1993). In late medieval England, marketplaces proliferated under a market mode where simple commodity production was geared toward local consumption and recurrent face-to-face interaction among producers and consumers. These marketplaces were held together by sociological basis of trust in a region where traders knew each other and through formal regulations such as a local market court. In the 17^{th} century, an entrepreneurial mode emerged, constituted by a nexus of travelling merchants in tandem with provincial shopkeepers, which was largely complementary to the continuing operation of the market mode. In the late-17th century, however, a mercantile mode was constructed by London-based middlemen merchants in which they sought direct deals with rural elites, bypassing the onerous regulations of the open market. This also led to a shift from intraregional to interregional trade and transformed the social relations of exchange. The struggle between the entrepreneurial and mercantile modes is highlighted by the royal grant of patents that gave London merchants the right to hire 'agents' to harass local manufacturers and peddlers who threatened their monopoly. Lie's (1992) market revisionist account also reveals distinct social organisations involved in commodity exchange and points to discontinuities in the economic history of Japan from the Tokugawa to the Meiji period (1600 to 1900). Power struggles among different groups, advocating different social organisations of commodity exchange, thus determines which mode of exchange will predominate in a particular time and place. Rather than harmonious cooperation ensured by the invisible hand or the coercive power of the state, concrete social groups construct 'markets' through power struggles against other groups and other possible forms of markets.

A further example is the work of Neil Fligstein (2001) on the evolution of large industrial firms in the US. He conceives of markets at various stages of development as containing the firm and the state as actors rather than simply opposing an ill defined market concept to alternative institutional logics. Market institutions are emergent, forged through political contestation over shifting social and cultural beliefs. There is thus a recognition of the variety of actors and interests within a market setting and an emphasis on power and conflict and processes of negotiation and resolution. Fligstein conceives of markets as social arenas that exist for the production and sale of goods or services and are characterised by structured exchange. This implies that actors expect repeated exchanges for such goods or services and therefore require rules and social structures to guide and organise exchange. These requisites are often facilitated by government structures and the state plays an important role in his conceptualisation of market.

Theoretically, the market is examined in terms of fields, actors and rules. Using a political-cultural approach, Fligstein (2001) argues that social action takes place in arenas that might be termed fields (Bourdieu, 1977), which contain collective actors who try to produce a system of domination in that space. This requires the production of a local culture that defines local social relations between actors. Once in place, the social interaction in fields can be seen as 'games' whereby groups in the field who have more power use the acceptable cultural rules to reproduce their power. As such, action in fields is continuously *conflictual* and inherently *political*. The theory of fields thus focuses on the opening of new social space, how it becomes and remains stable (i.e. becomes a field) and the forces that may transform them. Market orders are governed by a general set of rules, which consists of common understandings and laws that allow capitalist firms to exist. The dominance of different groups in society means that those rules tend to reflect one set of interests over others.[5] Structured exchange within markets can thus be understood as a 'field' because any social structure (including markets) are cultural constructions where actors are locked into a 'game' in which the dominant players try to reproduce their advantageous position while the dominated try to challenge the power of the former. The social order of the state is also seen as a set of fields of policy domains where actors claim the power to make and enforce rules for other actors in society.

[5] Increasingly, these rules are also being established on a transnational level such as in the EU and WTO.

These orders are governed by formal and informal rules that create and limit social and political interaction within particular domains.

Fligstein divides the actors within a market into incumbent and challenger firms. Incumbent firms dominate a particular market by creating stable relations with other producers, customers and the government and tend to set the agenda within a market. Challenger firms fit into the dominant logic of a stable market either by finding a niche or framing their action with reference to the dominant firms. The goal of action within markets is to create and maintain a stable balance of power and (re)produce social relationships across firms that enable them to survive. This production of social structures in markets is guided by four types of rules as shown in Table 4.1.

Table 4.1 Four types of rules governing the production of social structures in markets.

Property rights are rules that define who has claims on the profits of firms and includes issues of different legal forms, the relationship between shareholders, employees, communities, customers etc. and the role of the state in providing and maintaining a governance structure to ensure these rights. They define the social relationships between owners and everyone else, which stabilises the market by making clear who is risking what and who stands to reap the rewards. Stability is produced by defining the power relations between different actors and signalling to other firms who the dominant actors are.
Governance structures are general rules within a society that define relations of competition and cooperation and the organisation of firms. They can take the form of formal laws or informal institutional practices embedded in existing organisations as routines and accepted practices.
Rules of exchange define who can transact with whom and conditions under which transactions are carried out. They help reproduce conditions of stability by ensuring that exchanges occur under conditions that are applicable to all.
Conceptions of control are forms of local knowledge that reflects market specific agreements between actors regarding internal organisation, tactics for competition and cooperation and the hierarchy of firms within a market. It is a worldview that enables actors to interpret the actions of others and a reflection of how the market is structured. They are historically specific and are cultural in that they form a set of understandings and practices about how things work in a particular market. In a stable market as a social field, a conception of control defines the social relations between incumbent and challenger firms such that those relations are reproduced over time.
(Source: Fligstein, 2001: 32-35)

The theory of fields also suggests how states as a set of fields interact with markets as a set of fields. Creating a general set of rules where stable markets can be reproduced helps to structure exchange in particular fields. Fligstein argues that for countries in the process of establishing modern capitalist markets, creating stable conceptions of control is more difficult precisely because the other rules, i.e. property rights, governance structures and rules of exchange, which are necessary pre-conditions, are not well specified. Creating these new institutions requires the interaction of firms, political parties, states and new, revised or borrowed conceptions of regulation. The policy domains of the state can be organised according to interventionist or regulatory principles. In an interventionist regime, governments can make substantive decisions for the markets directly by owning firms, controlling the financial sector, direct investment and exercise strong control over firms' activities. In contrast, regulatory states put organisations in place that theoretically do not reflect the interest of any one group but use rules impartially to police the interaction of actors. However, it is possible for a particular group to capture the regulatory agency and get officials to accept their view of the industry and influence the rules of governance.

This political-cultural approach implies that the historical problems of instability for market participants, the formation of institutions in response to these problems and the configuration of economic and political elites are crucial to the formation of stable markets. Once established, they tend to reproduce entrenched interests and structure the operation of markets in that society. Fligstein's approach also allocates a key role to states in market-building and explains the existence (and persistence) of many national capitalisms. If firms survive by stabilising their relationships with their competitors, then the social relations that are the outcome of this process are not necessarily maximising the efficient allocation of resources for society, contrary to the normative claims of neoclassical economics. "If firms are effective and not efficient [by operating within a very wide set of social relations] then the claim that one form of market organisation is always superior to other forms is probably false" (Fligstein, 2001: 22).[6]

4.4 ANTHROPOLOGICAL AND CULTURAL ALTERNATIVES

In questioning the normative claims of neoclassical economics, other scholars have pointed to the discursive power of economics as a discipline and the need to distinguish between economics as theory and economics as practice. More importantly, research has shown how theories *about* markets have had an impact *on* those very markets. Callon (1998) and Miller (2002a) suggest that theories, especially from economics, have a tendency to create the world which they purport to describe, such that reality comes to mirror theory through the policies and practices of the powerful. Metcalfe and Warde (2003) remark at the unparalleled, if not entirely unprecedented, confidence expressed about markets at the end of the 20th century and how the spread of the market can be seen in ever more areas of society. This overt promotion of the market requires strong legitimisation from a discourse of 'market virtues' (Table 4.2). The power of this discourse operates through political rhetoric, in business practice and through the ghostly role of markets in economic analysis. According to Sayer (2003), this tendency to treat market exchange as the atomic structure of all economic processes and as the *default* form of economic coordination is problematic as other forms of organisation thus become marginalised or treated as problematic exceptions. The market optic and its normative presumption in favour of markets both mystifies and promotes unfettered capitalist dynamics and social relations. He argues that these issues are especially significant given the

[6] This claim also places his argument and contribution within the 'varieties of capitalism' school (Hall and Soskice, 2001).

prevalence of neoliberal dogmatism and fatalism that are driving a particular model of economic development, which is being hailed as the only workable model (see also Peck and Tickell, 2002). Lie (1997) also observes that this approach has resulted in an assumed progression of market practices in socialist economies. The post-Cold War period saw an avalanche of proposals to privatise formerly communist economics and to effect a transition from planned economy to market. Empirical investigations, however, reveal the complexity of institutional legacies that differ across Eastern Europe and China. The assumption of market essentialism forecloses considerations of alternative forms of exchange relations and structures. “If the only alternatives were plan and market, then market socialism, for example, would be an oxymoron (*ibid.*, p. 353).

Table 4.2 Propositions of the ‘virtuous market’

• The market enshrines the principle of consumer sovereignty. • The market permits, sustains and delivers individual freedom of choice and action across the economic and social spheres. • The market is an ideal mechanism for exchange because its incentive structures are consistent with basic features of human nature • The market is applicable to many, if not all, forms of human activity, its principal mode of rational calculation being suitable to all spheres of life. • The market is the epitome of efficiency in the allocation of resources and is unfailingly superior to any other system of economic governance. • The market is the best guarantor of reliable quality in products and services. • The market guarantees sustained growth in standards of living in all countries, whatever their level of development.
(Source: Metcalfe and Warde, 2003: 4)

There is thus a need to unpack the ‘essentialist’ and ‘virtuous’ market and to scrutinise its inner workings through its microstructures, institutions and constituent actors. Studies that employ an anthropological and cultural perspective have made use of ethnographic and intensive qualitative research methods to uncover the richness of market meanings and practices. Viviana Zelizer (1988), for example, presents a ‘multiple markets’ model as an alternative to the neoclassical paradigm of *the* market, in which the market is analysed as one category of social relations involving consumption, production and exchange under a variety of cultural and structural settings. The theoretical and empirical task is thus to investigate the social and cultural variation of these 'multiple markets'. The objective, she argues, is to capture the complex interplay between economic, cultural and social structural factors in the production of multiple markets. She applies this multiple markets model in empirical research on life insurance, which stresses the cultural response to life insurance by examining changing attitudes to the monetary evaluation of human life and changing cultural definitions of risk (Zelizer, 1983). Another study examines the interaction between market or price (i.e. economic worth) and personal and moral values in tracing the social construction of the economically 'useless' but emotionally 'priceless' child in the US between 1870 and 1930 (Zelizer, 1987). It reveals how children's insurance policies, compensation awards and the market for the adoption and sale of children contribute to rethinking about markets as being regulated in part by non-economic criteria. In more recent studies, she adopts a historical-cultural approach in examining the institutional circuits through which the most reified product of the market – money – travels, and how it acquires distinct social meanings (Zelizer, 1989, 1993, 1994). Her bold thesis is that rather than money depersonalising social relations, social relations personalise money, which accounts for its multiple meanings and usage. Money is neither culturally neutral nor socially anonymous. There is no single, uniform, generalised money but multiple monies as people embed money in particular times, places and social relations by earmarking different currencies for various social interactions. Different currencies are created through social and cultural processes in the forms of domestic money, gifts of money, institutional money and moral money. Through these studies, Zelizer demonstrates how a sociological and culturally inflected model of money offers an alternative approach to aspects of economic life, including the market. Economic processes of exchange and consumption are defined as a particular category of social relations, much like friendship, kinship or patron-client ties, and that economic phenomena are interdependent with historically variable systems of meanings and structures of social relations.

One of the provocative claims made by Michel Callon (1998) in 'The Laws of the Markets' is that sociologists should rethink their relation to economics. Rather than denounce orthodox economics for its impoverished account of society and culture, sociologists should examine the role of economics in the constitution of markets. Callon is less interested in the question of whether economics gives a good or bad representation of markets than in the part played by economics (in a broad sense) in *performing* markets. In this sense, economics has to be understood broadly to include not only academic economic theory but all related institutions, techniques and professional practices (e.g. accountancy and audit). Daniel Miller (2002b) also argues that we should stop thinking of economics as the study of economies but focus on the degree to which economics and other abstract models manage to accrue such power that they are able to transform actual economic practices to accord more with those same models. He introduces the concept of 'virtualism' as a way to understand the growth and power of abstraction in the contemporary economy, to examine the ability of economists and other agents such as audit and consultancy to transform the world into closer approximations of their theories and models (Carrier and Miller, 1998; Miller, 1998; Leyshon et al., 2005). Economics is not a set of falsifiable claims about the economy, or an ideological construction of the economy, but rather a *participant* in its construction (see Mackenzie et al., 2007). This makes enormous sense when one considers, as noted earlier, the diffusion of neoliberalism through virtually every social institution over the last 20 years, with very real effects on marketisation and consequent abstraction of social relationships.

The performativity of economics is explored by Donald MacKenzie in his research on arbitrage and option pricing theory (MacKenzie and Millo, 2003; MacKenzie, 2005a, 2006). Through the use of oral-history interviewing, archival research and non-participant observation, MacKenzie and Millo (2003) examine how the Nobel Prize winning theory of option pricing developed by Black, Scholes and Merton became integral to the success of the Chicago Board Option Exchange (CBOE). In the first instance, the option pricing theory conferred legitimacy to the CBOE. What used to be regarded with suspicion as gambling or speculation came to be understood as efficient pricing when framed within the option pricing theory, which later led to the subsequent legitimisation and acceptance of the derivatives market. When Black and Scholes tested their formula against prices in the pre-CBOE ad hoc options market in 1972, they found only approximate agreement; the basis of their work was theoretical rather than empirical. However, the fit began to improve over the course of the CBOE's history. Mackenzie and Millo argue that this empirical success was not due to the model describing a pre-existing reality but was the result of two interrelated processes. First, there were changes in market conditions over time that came closer to what were unrealistic assumptions made by Black, Scholes and Merton – various forms of regulation were later waived for bona fide hedging by options market makers, stock borrowing became easier, and with technological advances price dissemination and transaction processing was improved. The second process was the model's growing use as a guide to trading itself; theoretical prices were printed on sheets of paper and carried on the floor. As the options markets grew, options were traded on more stocks, including high volatility newcomers as well as ‘blue chip’ companies. More expensive errors made pricing models seem indispensable:

> Seat-of-the-pants trading or simple heuristics could not suffice when implementing a position across several markets and carrying dozens or hundreds of such positions. Pricing models were necessary for risk management and, crucially, offered a way of communicating and coordinating activities, of *talking* about options. (*Ibid.*, p. 125; original emphasis).

Pricing models thus came to shape the very way participants thought and talked about options. The use of the Black-Scholes-Merton model in arbitrage had the effect of reducing discrepancies between empirical prices and the model. Gradually, the CBOE participants began to price options as economists suggest *homo economicus* should. The process thus concurs with Callon’s formulation that: “Yes, *homo economicus* does exist, but is not an a-historical reality; he does not describe the hidden nature of the human being. He is the result of a process of configuration. [… W]e should not forget the essential contribution of economics in the performing of the economy” (Callon, 1998: 22-23).

Knorr Cetina and Bruegger (2002a, 2002b) employ an innovative combination of participant and non-participant observation on trading floors, interviews and trading transcripts drawn from inter-bank currency trading in global investment banks to explore the global microstructures of the foreign exchange market and theorise about a postsocial relationship between traders and financial markets. For traders, the most fascinating part of their environment is the market with which they appear to be obsessively engaged during their working and waking hours. The process and content of this intense engagement is the focus of their study (2002a). In the past, the foreign exchange market was nested in territorial space, hidden in transnational banking networks of institutions that did not share the same information. The advent of the computer screen, however, brought a geographically dispersed and invisible market close to participants, rendering it interactionally present. After the introduction of the screens, they argue, the market became fully available and identified as a separate entity in its own right with prices, interests and actions of other participants all visually indicated on screen. Traders were then able to simultaneously position themselves inside the market in the sense of becoming players, and to relate to the market on screen as an exteriorised other, a 'master-being' that observes all transactions and includes their contextual conditions and motivations. "In a sense, *the screen is a building site on which a whole economic and epistemological world is erected*. It is not simply a 'medium' for the transmission of other interactions" (*ibid.*, p. 167; original emphasis). They examine how traders consider the market as 'everything' that cannot be reduced to just prices, news or known groups of players:

> [The market is] Everything. Everything. How loudly he's screaming, how excited he gets, who's selling, who's buying, where, which centre, what central banks are doing, what the large hedge funds are doing, what the press is saying, what's happening to the CDU, what the Malaysian prime minister is saying, it's everything – everything all the time. (Quoted in Knorr Cetina and Bruegger, 2002b: 168)

The market is also considered a 'greater being', an empirical object of on-going activities and effects that changes all the time such that traders have to continually redefine their relationship to the market. As the traders take a position (open their accounts and start buying and selling currencies), they are also able to 'enter' this life form cognitively and emotionally and become part of it. The inability to control the market is turned into a sophisticated game as Knorr Cetina and Bruegger reveal a trading room culture of star systems and how the market not only provide the obvious goal of making money but also a secondary goal of excitement and mastery in the sheer joy of 'winning'. As markets are always in the process of being materially defined, they provide an unending series of new challenges. The term 'postsocial' thus refers to new kinds of bonds such as those constructed between humans and objects and calls for a rethinking of sociality along lines that include objects in the concept of social relations. They also suggest that fields in which geographically distant participants are oriented towards one another can be bound together by global microstructures – i.e. patterns of relatedness and coordination that are global in scope but microsocial in character and that assemble and link global domains, such as the global foreign exchange market. Their study (2002b) explores how the foreign exchange market as seen through the practices of traders is governed by institutional rules, informal codes of honours and structural use of interaction to manage and sustain social order, even as they are scattered among the financial hubs of major time zones such as in New York, London, Zurich, Singapore and Tokyo.

Abolafia (1998) argues that when people are engaged in market exchange, they are socially embedded in a network of social relations and culturally embedded in a meaning system of norms, rules and cognitive scripts. In focusing on markets as cultures, he examines them as fields of repeated interaction and transaction in which they exhibit distinct sets of mutual understandings. These understandings, in turn, are both enabling and restraining in that market participants are able to use them both to pursue their interests as well as to limit the range of alternatives available to each other. But market culture is also not fixed or given and must be continually reproduced through exchange relations that is vulnerable to change through social or institutional power. Through the use of interview data and extended periods of observation on the floor, Abolafia's ethnographic research on the stock, bond and futures markets in New York focuses on the subjective experience of market makers as they enact their rules and roles, drawing attention to the fact that they are actively constructed and fluid. Market participants construct rich social identities that come to define behaviour and interaction as they employ a toolkit of strategies to reduce uncertainty and risk in their environment and to maximise survival. Constitutive rules and roles such as an 'entrepreneurial' identity, emotional control, risk-taking and the strategic use of guile are actively employed by market participants to construct and interact with the market (Abolafia, 1996). By treating markets as cultures, rationality is treated as a community-based, context-dependent cultural form. He thus explores the market participants' construction and understandings of the decision making process and the individual as well as social means of establishing value in the marketplace.

The above studies fall under a new inter-disciplinary grouping called social studies of finance (SSF)[7] which focuses on the creation, development and effects of financial markets. This approach combines perspectives from disciplines such as anthropology, geography, history, politics, sociology, social studies of science and legal studies. Rather than focusing on the theoretical category of the market per se, social studies of finance focus on empirical research on financial markets (Knorr Cetina and Preda, 2005). The literature can be summarised as a commitment to post-disciplinary social science, including cultural and social anthropological accounts of trading floors (Abolafia, 1996; Zaloom, 2003; Hassoun, 2005), electronic capital markets (Sassen, 2005), the deployment of mathematical economics model in the making of an options market (MacKenzie and Millo, 2003), the sociology of interactions between humans and objects in markets (Knorr Cetina and Bruegger,

[7] See http://www.sociology.ed.ac.uk/finance/

2002b), the importance of mundane management processes within multinational financial service firms in structuring dispersed knowledge and risk in global financial markets (Clark and Thrift, 2003), and how finance is 'performed' through the media and the regulatory implications of 'finance entertainment' (Clark et al., 2004). These in-depth studies yield rich accounts of market practices, constructions, agencies and governance that are often overlooked and beyond the epistemological scope of orthodox economics and its myopic framing of markets.

Implications for Research

> *By precluding attention to non-rational elements of human behaviour, economists leave themselves no mechanism for learning about the crude and messy empirical world that so defies their models. Economists pay a heavy price for the very simplicity and elegance of their models: empirical ignorance, misunderstanding, and relatedly, unrealistic and bizarre policy recommendations. – Hirsch et al. (1987: 320; original emphasis)*

The challenge of learning about the "crude and messy empirical world" in its complexity has been taken up by a variety of heterodox economics, anthropological and cultural approaches that have significantly enriched our understanding and appreciation of economic processes and the important concept of markets. Martin and Sunley (2001), however, observes that many 'new' (cultural) economic geographers have limited understanding of institutional and evolutionary economics, economic sociology and other heterodox fields of economics and suffer from a 'cherry picking' syndrome of jumping onto the latest theoretical bandwagon that is en vogue. In the preceding sections, I reviewed the theoretical approaches and empirical studies conducted in various fields to assess their strengths and contribution to understandings of the market. These provide a conceptual toolkit in framing markets, each with their strengths and limitations. There is no single tool suitable for all tasks and a project will often require a selection of tools appropriate to the task at hand. My intention is to combine some of the key insights from these approaches to inform my empirical research into Shanghai's financial markets and, in turn, to reflect on the implications for issues of power, states and market building.

First, I want to highlight the importance of power and inequality in examining market structures and processes. Soft conceptualisation of networks, trust and embeddedness has to be reformulated if we are to avoid an overly benign view of how social relations operate in making markets (Sayer, 2003). Much of the network literature has tended to neutralise or obfuscate relations of power, domination, exploitation and inequality while demoting structural forces and contexts to the sidelines. Lie's (1993) and Fligstein's (2001) studies demonstrate the importance of embedding concepts of power and governance into the theorisation of markets and how they not only enrich accounts of market formation and processes but are crucial to their explanations. Rather than harmonious cooperation ensured by the invisible hand or the coercive power of the state, concrete social groups construct 'markets' through power struggles against other groups and other possible forms of markets. The recognition of the variety of actors and interests within a market setting and an emphasis on power and conflict and processes of negotiation and resolution is central to my research. The form, structure and pace of market formation taking place in Shanghai is a contested process that has to be negotiated amongst the different interests of incumbents and challengers, involving a variety of actors including local firms, foreign firms, national and local state bodies, foreign state institutions and transnational organisations. The dominant 'mode of exchange' that emerges is the outcome of a conflictual process between multiple parties but is itself also constantly 'under threat' due to shifting agendas and contexts. This process of power, negotiation and conflict resolution amongst actors in the field forms the main focus of my empirical enquiry in Shanghai.

Second, I want to highlight the key role of states and state institutions in the process of market building. The distinction between states and market has proved unhelpful and unrealistic by considering the state and the market to be two analytically separate realities, placed at two ends of a continuum, while a particular form of economy can be defined as mixed, a combination of two types. This paradigm has proved to lack realism both historically and theoretically. The state does not intervene in the market, it participates in the constitution of the economy and its role is always essential. I concur with Callon (1998: 41) in questioning: "Could we say that the waffle exists independently of the waffle-iron? Of course not. Similarly, we cannot say of an organised market activity that exists without the state." In theorising about conceptions of control, governance structures and rules of exchange, Fligstein (2001) demonstrates how issues of governance and regulation are central to market enquiries. The question should thus be: how and with what methods does the state contribute to the performance of calculative agencies and the organisation of their relations? This implies the existence of a wide range of possible configurations. The case of China (and other post-socialist economies) is valuable in demonstrating this. The term 'transitional economy' reflects the old paradigm; there is nothing of a transition in the developments observed or in the diversity between countries such as Poland, Ukraine or China. It is more useful to conceptualise them as reconfigurations, combinations and re-arrangements peculiar to their historical contexts. In these rearrangements, the state often plays a crucial role and the dynamics in place, in turn, impact on its own position and contribution to the economy. The case of Shanghai should therefore not be seen simply as a transition ‘from plan to market’ but a process of reconfiguration specific to its historical and geographical context, of which the constitutive role of the state is crucial. The experience of market building in Shanghai can thus illuminate how different constructions of capitalism evolve, how they intersect, and how a geographic sensibility makes a difference to the form and function of variegated capitalist economies. In the face of neoliberal fatalism, the active construction of neoliberal (market) ideology needs to be exposed through theoretically informed empirical research (Gibson-Graham, 1996; Peck and Tickell, 2002; Peck, 2005).

Third, I concur with Zelizer (1988) and Krippner (2001) that the ‘add-social-context-and-stir’ approach common in earlier economic sociology tradition is an erroneous conceptualisation of economy and society relations which impoverish both arenas. We need to move beyond the notion that economic phenomena are abstract and disembodied and need culture to be added to them. By seeing economic goods as the outcome of what Callon (1998; see also Barry and Slater, 2002) calls a “double process of dis-entanglement and entanglement”, they become richer and more meaningful. Zelizer’s (1988, 1993) multiple markets approach is particularly instructive in this sense by capturing the complex interplay between economic, cultural and social structural factors in the production of multiple markets, without privileging any one aspect but demonstrating how they are mutually constitutive. The anthropological and cultural approaches to ‘markets’ have shown how markets are understood and experienced by actors in a variety of ways, invested with different meanings and acted upon according to different interests and through contingent social relations. The discursive construction of markets has material consequences in affecting policies and practices and is implicated through the exercise of power structures in the interest of particular groups. The central Chinese government and

SMG have particular understandings and visions of the financial markets in Shanghai; the local and foreign financial institutions in Shanghai are also ‘framing markets’ according to their own interests, agendas, experience and interpretations of what a market *should* be. How are these different ‘framings’ of market played out in Shanghai?

With in-depth empirical studies and rich accounts of market practices, agencies and governance, the SSF has become increasingly prominent in studies on financial markets. In this thesis, however, I focus on the *political economy* of ‘markets’, rather than adopt a SSF approach, in emphasising broader structural issues and the nature of regulation in Shanghai (and at wider national and transnational scales). There is no royal road to markets. Although SSF research has opened up the field by challenging myopic framings of ‘markets’ with rich empirical data and innovative studies, it tends to focus on market practices and processes at the micro- or meso-level that neglects certain aspects of power (such as between state institutions and finance capital). In this thesis, I reiterate the contribution of a political economy approach (as highlighted at the beginning of Chapter 3) in understanding specific local or national scale phenomena, by embedding them within an international context that emphasise flows, interconnectivity and power in the case of Shanghai’s financial markets.

4.5 CONCLUSION: OPENING THE BLACK BOX OF MARKETS

In eschewing a Marxist political economy approach in favour of more discursive accounts, recent research has contributed to more nuanced understanding and richer accounts of the geographies of money and finance. By problematising the ‘economic’ and rejecting the artificial distinction between the economic sphere and ‘other spheres’ (be they cultural, social or political), such arguments allow for a greater appreciation of their mutually constitutive relationships. However, I would concur with Tickell (2000: 242-243) that:

> analyses should remain sensitive to the fact that however much financial flows and geographies are socially embedded, culturally inflected, discursively mediated, and symbolically inscribed, financial geographies are also geographies of power.

The social constructivist approaches have traditionally been criticised for being politically thin and having a soft conceptualisation of power and inequality. Recently, an increasing number of scholars have sought to transcend the divide between a macrostructural view and socially and culturally inflected approach. This is evident in Fligstein’s (2001) political-cultural approach, more holistic conceptualisations of state and economies (Mizruchi and Stearns, 1994; Callon, 1998; MacKenzie, 2005b) and assigning greater explanatory weight to the role of power and conflict in socially and culturally inflected accounts of the market (Lie, 1992, 1993; Abolafia, 1996).

Issues of power are addressed in both structural (political economy) approaches as well as social constructivist approaches, albeit in slightly different ways. I argue that combining insights from various conceptualisations and understandings of power structures and processes contribute to a more holistic picture of its workings and impacts. In this study, I investigate the production and maintenance of financial markets in Shanghai through the frames of the regulation of the international financial system and the making of financial (market)places. To this end, I employ a socially and culturally inflected approach in understanding the rich accounts and multiple conceptualisations of the markets through the experience of variegated actors in Shanghai (and elsewhere) while placing them within broader structural contexts of the international financial system (traditionally associated with the political economy approach).

Within economic geography, much of the recent theoretical discussion of networks has been pushing in a similar critical direction by making a case for more political-economic content within network analyses, taking asymmetrical power more seriously and locating networks within their macroeconomic and institutional contexts (Olds and Yeung, 1999; Dicken et al., 2001; Henderson et al., 2001; Gertler, 2002; Yeung, 2003). I would argue that much of the above engagement with markets and economies that I have reviewed in this chapter lack an appreciation of the significance of geographic context and spatial embeddedness, with little attention to issues of uneven development, place making or scalar constitution. Much more can be done to explore the historical geographies of market making and state building, at a variety of scales and in a variety of spatial contexts and to examine the social (re)construction of economic institutions more generally (Peck, 2005). The development of Shanghai as an international financial centre can be seen as part of a global process servicing finance capital but this conceals the complex reasons behind why such processes are taking *place* in Shanghai and at a particular point in time and space. The process of market making in Shanghai and the actors involved are also spread across scales and much of what is happening within the city is determined by economic, social and political considerations elsewhere on the national, regional and global level.

Through my empirical research, I demonstrate how ‘markets’ in Shanghai are framed, understood and acted upon different by the SMG, the central government in Beijing, regulatory bodies, domestic financial institutions and foreign financial institutions in Shanghai within the wider context of their global operations and strategies. Transnational interests and roles of organisations such as the WTO and other state agencies from the financial centres of London, New York, Singapore and Hong Kong are also considered. The construction of a financial centre in Shanghai is thus the outcome of not only its own historical context, economic advantages and development trajectory (important as they are) but is also intrinsically bound up with the interests and decision of other agencies acting across spatial scales and negotiated amidst conflicts of interests and power struggles.

Deconstructing markets, market relations and market ideologies means confronting the messy reality of economic behaviour and economic structures instead of assuming them away in the tradition of orthodox economics or impoverished accounts of the economy. According to MacKenzie (2005b), the concept of 'black box' is originally an engineer's phrase, describing a device whose internal structure can be disregarded; as long as the device transforms given inputs into predictable outputs, how it does this can be ignored. It can thus be treated as opaque as if its content cannot be seen. Treating artefacts (computers, watches, car engines), organisations (banks, retailers) and expertise (surgeons, pilots) as black boxes may be an inescapable part of societies in high modernity but what may be unavoidable as a practical matter should not be satisfactory on an intellectual level: "Not to examine the contents of black boxes is to miss a critical part of how societies are constructed" (*ibid.*, p. 557). Power is exercised through the ability to sit on top of black boxes. According to Callon and Latour (1981), macro actors of social life (i.e. those who wield power) are micro actors grown large through their capacities to mobilise and command black boxes. The contents of black boxes are therefore not mere details; if a black box ceases to function as such, then the power of a macro actor can be disturbed and undermined. By opening the black box of 'markets' in the context of

Shanghai's experience, and examining the underlying processes taking place in the city as well as across spatial scales, we can better understand the complex processes of market making and undermine the power of a seemingly unified (neoliberal) market discourse.

Chapter 5

Doing 'Market' Research

Methods and Practice

5.1 INTRODUCTION

Economic geography has grappled with a range of epistemological and methodological approaches over time. These range from quantitative economic geography, to Marxian political-economy, to the more recent culturally inflected economic geographies (Scott, 2000a; Barnes, 2001). The resulting methodological pluralism that has come to characterise the sub-discipline in recent years has been a response to, as well as a driver of, debates about where economic geography situates itself within the discipline and wider social sciences (Thrift, 2003; Amin and Thrift, 2000; Peck, 2003)[1]. Over the past decade, in particular, the concept of the 'economic' has been refigured as scholars have rejected conventional dualisms between 'the economic' and 'the cultural' in favour of a range of more fluid and hybrid conceptions that emphasises the mutual constitution and fundamental inseparability of these two spheres. Several progress reports and review articles have documented these exciting developments, known collectively as 'new economic geographies' (Barnes, 1996; Thrift, 2003; Lee and Wills, 1997; Lee, 2000; Sheppard and Barnes, 2000), which have influenced empirical research in geographies of firms (H. Yeung, 1994; McDowell, 1998; Schoenberger, 1997; Lai and Yeung, 2003), political economy (Barnes, 1995, 1998; Scott, 2000b), geographies of money and finance (Hudson, 1998; Jacobs, 1994; Leyshon, 1998; Leyshon and Thrift, 1997) and geographies of consumption (Crewe, 2000; Jackson, 2002). This 'cultural turn' is a

[1] See also the responses to Amin and Thrift's (2000) article in a 2001 special issue of 'Antipode' 33 (2).

direct response to the new economic realities that have accompanied the shift to a post-industrial, knowledge-based, global capitalist economy as well as wider epistemological developments within human geography. New economic geographers have advanced the frontiers of geographical research to incorporate substantive issues traditionally considered to be outside mainstream economic geography. The discipline has benefited considerably as scholars drew attention to new subject matters and scales of analysis, accorded roles to previously ignored and subordinated players, and encouraged a diversity of analytical frameworks. At the same time, new economic geographers have also invoked new metaphors, strategies of writing and authorship, and research methods.

Despite these advances, however, many commentators have questioned the rigour and relevance of much of these ‘cultural economic geographies’ (James, 2006). Martin and Sunley (2001) criticise “the new (cultural) economic geography” for its “vague theory and thin empirics” (p. 153), which privilege an oversocialised epistemology and a less-than-rigorous methodological framework. Markusen (1999) similarly highlights what she considers to be the waning quality of in-depth empirical work that results in “fuzzy concepts, scanty evidence [and] policy distance” (p. 869). There is now increasing recognition that the methodological component of new economic geographies continues to lag behind their ontological and epistemological counterparts (see Jackson, 2002; H. Yeung, 2003; James, 2006). James (2006), for example, calls for greater reflections on effective methodologies in terms of the broader sets of standards and guidelines (rather than rigid mandatory rules that are at odds with the epistemology of new economic geographies research) used in formulating whole research strategies, “from the derivation of research questions, to data collection, empirical analysis, theory-building and write-up” (p. 291). As such, our research methodologies should go beyond simply the *choice* of research instruments *per se* to include the entire *process* of practicing research itself (H. Yeung, 2003). Research practice includes aspects of research activity that are often left out of conventional accounts of method and methodology, such as how the topic evolves, its ongoing and dialogic character, and the way the project changes in the process (Raghuram and Strange, 2001).

In this chapter, I document and reflect on how the research themes and empirical work of this thesis were derived and conducted in a circular rather than linear fashion (moving straightforwardly from theory through to epistemology to methods), as is often assumed to be the case. This study did not start with preconceived notions such as the success of market-building in Shanghai, systems of governance and regulatory goals of the Chinese state bodies, and strategies of foreign and domestic financial institutions, at the stage of literature review or the stage of data collection. While iterative abstractions were constantly underway from an immanent critique to data analysis, the notion and significance of 'markets' did not fully emerge until empirical data were triangulated and theories on 'markets' were grounded in these data. Following H. Yeung (2003), I employ a process-based methodological framework, whereby the configuration of different methodological practices is driven by the research process itself rather than some preordained philosophical positions. This inductive approach is particularly relevant since my objective is to expose and critically engage with the multiple identities, conceptualisations and contested nature of 'markets' and the 'marketisation' process,. In doing so, I allow field observations and the experience and perspectives of market participants to 'speak out' as I analyse the empirical data to discern patterns and regularities (as well as irregularities). Some tentative hypotheses are formed which are then progressively modified, refined and reaffirmed through the course of further empirical research.

The research methods employed in this study took a multi-pronged and complementary approach, comprising archival/library research, analysis of secondary data (e.g. press releases, news articles, government/official reports, bank reports and other industrial publications) and in-depth semi-structured interviews. In the next section, I elaborate on the specific research methods employed with regards to my research themes and the types of data collected. As personal interviews form a prominent component of my empirical research, a separate section (5.2.2) documents its use in this study and highlights issues that emerged in the course of fieldwork. In section 5.3, I take a reflexive approach in examining issues of research practice (Raghuram and Strange, 2001) and positionality (Rose, 1997; Cormode and Hughes, 1999; Ward and Jones, 1999) that emerged in the course of my field research, paying particular attention to how my complex ethnic identities have influenced the fieldwork process. Rather than self-indulgent navel-gazing, I argue that this reflexivity is important as our fluid positionalities and hybrid identities invariably influence which doors are opened or closed to us as researchers and the content and dynamics of the interview process and, as such, have important implications for the resultant analysis and claims of our research.

5.2 RESEARCH METHODS

5.2.1 Research Agenda

The objective of my thesis is to open up the ‘black box’ of markets and critically examine the process of market formation by studying Shanghai’s experience. Statistics on public listings on the SSE and the types of policies and regulations at different points are useful in providing a timeline and broad picture of events but are not particularly informative in revealing the motivations and rationale underlying specific decisions and actions, which I argue is vital to a deeper understanding of the market-formation process. The initial plan was to conduct an intensive and in-depth study of a particular financial market in Shanghai, i.e. the Shanghai stock market. However, problems of access became a serious obstacle as it became clear that I was unable to obtain any interviews with employees of the stock exchange. The China Securities Regulatory Commission (CSRC) was in the process of implementing reforms to the stock markets and share structures in 2006, during which the bulk of my fieldwork was conducted. Officials and workers were particularly sensitive about questions relating to the history, performance and structure of the stock market and were not keen to entertain interview requests from a foreigner.[2]

In the course of fieldwork in Shanghai and through conversation with people in the industry, it emerged that in spite of the hyperbole and international media attention surrounding the SSE, the securities market is only a very small part of the story in developing 'markets' in Shanghai and its aspiration towards being an international financial centre. I had almost fallen into the trap of pigeon-holing 'market formation' as pertaining to only capital markets (e.g. stock market, futures market, commodities market). This reflects with Carrier and Miller's (1998) argument regarding the growth and power of abstraction in the contemporary economy such that our lives are made to conform to the virtual reality of economic thought – the trap of 'virtualism'. Much of the financial sector reforms underway in China are in the banking sector; this is unsurprising given its traditionally prominent role in China's finance sector. However, the development of capital markets is also

[2] The intersection of politics and time has a significant impact on research access and the interview process as a game of positionalities. Ward and Jones (1999) highlight this political-temporal contingency in research access during their studies of UK local government bodies.

integral to the success (or lack thereof) of these banking reforms along with the relaxation of rules regarding the roles and activities of foreign banks in Shanghai. The development of financial markets from a banking perspective is more important than I initially expected and I became interested in how different actors in this sector (foreign banks, local Chinese banks, Chinese regulatory authorities) position themselves in Shanghai and how different visions of 'markets' might be framed, understood and acted upon differently. There is also an element of serendipity in this as the interviews I had the most success obtaining were with senior managers and country representatives in the banking sector (a point to which I will return to later). Financial markets in Shanghai are being developed through conflicts and negotiations between competing agendas and visions and power play as foreign banks, local Chinese banks and local government and regulatory authorities are actively involved in the process (Figure 5.1). These processes are also spread across scales as much of what is happening within the city is determined by economic, social and political considerations elsewhere on the national, regional and global level. These include directives from head offices of foreign banks, influence of the national government, transnational interests and roles of organisations such as the WTO and other financial centres such as London and Hong Kong.

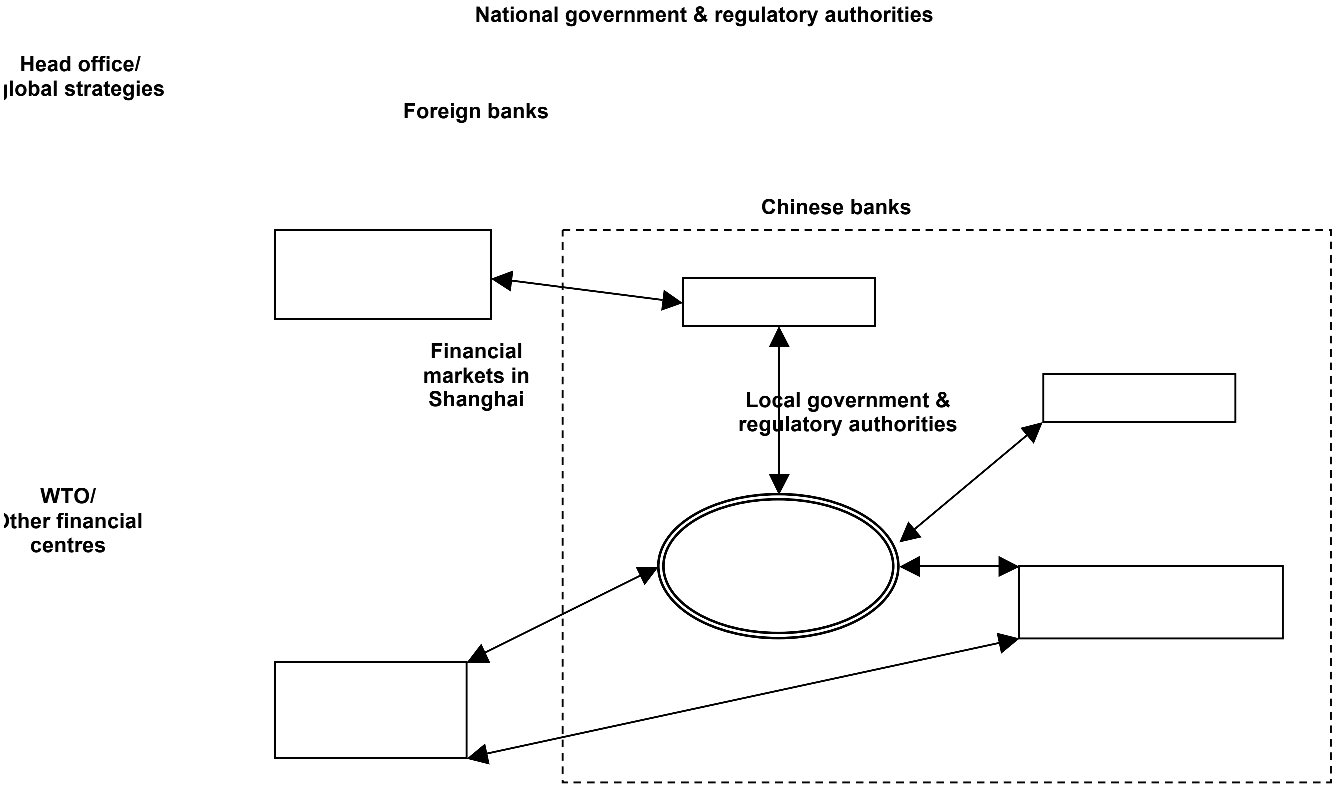


Figure 5.1 Negotiating different visions of 'markets': the main players

To begin with, I collected background information on the historical context of Shanghai's economic development, focusing on the finance sector, and the structure of the banking sector and stock market, in order to understand the empirical context of my study. Background information on the political economy and financial centre of Shanghai was mainly obtained through archival research (library and internet searches) of books, journal articles and newspaper reports and websites. These include research conducted by Chinese scholars on China's financial system, financial markets and regulatory changes, as well as secondary data and statistics from yearbooks and government reports, in a mix of Chinese and English language material. Whilst in the field, I collected news articles from local newspapers (such as the *China Daily* and *Shanghai Daily*) and business magazines (e.g. *BizShanghai*), tracked relevant announcements from banks and regulators, and collected reports produced by local analysts in financial institutions and regulatory bodies.

Approximately half of these materials were in Chinese. I also kept a field journal to record experiences as well as events as they were occurring in local and national politics and reported in the media, particularly those relating to changes in the finance industry or being circulated in the industry grapevine. More detailed accounts were obtained through interviews with official sources and independent bodies such as the SMG, the Shanghai Lujiazui Development (Group) Co. Ltd, the China-Britain Business Council, British Chamber of Commerce and EU Chamber of Commerce.

I also needed to access in-depth and interpretative views and experience of individuals and institutions involved in the development of financial centre capacities, specifically the changing structure and activities of the banking sector and capitalisation of the stock market, both of which are part of the 'marketisation' strategy implemented by the Chinese regulatory authorities. What were their expectations of financial reforms in Shanghai (or China more broadly)? What particular challenges or difficulties did they experience? What were their plans (corporate strategies or institutional policies) for these markets? How were they being implemented? What skills or knowledges were needed to 'create' or 'reform' a financial market (especially with regards to developing regulatory frameworks and the legal environment) and how were they obtained or transferred? What opportunities and prospects did they perceive in the future for the banking sector, the capital markets, the region and for Shanghai as a financial centre? What were the most vital issues to be resolved?

Reading literature on capital markets and finance provided a general background on the structures and functions of the stock market and the banking sector, but sterile data on the number of IPOs and other market trends are not particularly helpful in examining the landscapes of power and actors involved in the complexities of market formation. Quantitative techniques such as questionnaire surveys to securities firms and banks are also inadequate means of understanding people's views and experience; they may capture the material effects but not the underlying rationale of actors engaged in complex and on-going processes (Schoenberger, 1991). Qualitative and interpretative techniques are more appropriate in this respect as their flexibility allow for a greater variety and richness of data to be captured. To access the views and experience of those involved in the process of market formation, personal interviews were conducted with senior managers, directors or country representatives of foreign and Chinese financial institutions (banks and securities firms), and government and regulatory authorities in Shanghai with some interviews in the UK. Semi-structured interviewing was employed so that not only specific research questions could be answered, but new and interesting points could also be raised during the course of a more fluid interaction (Hughes, 1999). This allows existing theories of the economy and its geographies to be continually reworked in the light of conversations with people who actively engaged with and in the 'market'. As this thesis draws largely from interview data, I will elaborate on this aspect in the next section.

5.2.2 Corporate Interviews

As one of the main objectives of this thesis is to understand the perspectives, meanings and relationships in the process of market-making, as well as individual interpretations of changing events, the research methodology invariably lends itself to an interpretative approach. The economic phenomena of capital flows, information exchange and development of financial centres are not defined or examined in purely ‘objective’ or economistic terms as the world is organised in a subjective manner that is open to a multiplicity of different interpretations or ‘readings’. If “the world can only be known indirectly through ideas” (Johnston, 1997: 187), the process and politics of economic phenomena have to be understood by taking into account individual motivations, ideologies, personal experiences, unique resources and (sometimes conflicting) objectives. I adopted a method of semi-structured interviews consisting of a checklist of topics to be covered while allowing the direction and content of interviews to also be guided by the specific knowledge of the interviewees and the dynamics of our conversations. In exploring the views and experiences of institutional and individual actors, I argue that each interpretation is equally valid and accurate insofar as they reflect the worldviews of the actors concerned. In other words, what matters most is not what *is* but what people *believe* is, as these beliefs have their consequences (Jackson, 1988). In this vein, this research is anchored in the subjective understanding of the meanings, motivations and relationships amongst government bodies, institutions, firms and individuals and the ways in which financial knowledge, government policies and specific events are experienced, understood and acted upon. Rather than focusing on quantitative, large-scale samples, the field research concentrated on smaller numbers but more intensive and in-depth analyses of particular institutions. The idea is not to extrapolate representations to a larger population, but to use these cases to demonstrate the conceptual underpinnings of this study. Such an approach emphasises “information rich cases” rather than statistical representativeness (Baxter and Eyles, 1997: 513).

The task of studying and interviewing business elites, high-level corporate executives and other professionals can often be a frustrating experience. It has been variously argued that ‘elite’ groups (those who are socially, economically or politically powerful, for example, celebrities, the aristocracy, high-ranking lawyers and investment bankers, and senior politicians and diplomats) are more difficult to penetrate than other groups as they are better equipped to protect themselves and better positioned to manipulate research results and even dissemination (Hertz and Imber, 1995; Cochrane, 1998; Hughes and Cormodes, 1998; McDowell, 1998; Parry, 1998; Sabot, 1999). Obtaining an interview can be extremely difficult when access to powerful business people is constrained not only by their elite status but also by their demanding schedules. However, other scholars have also cautioned against a distinction between 'elite' interviewees and other types of interviewees that is based on inadequate conceptions of power and dualistic identities. Alternative suggestions include employing a poststructural understanding of power (K. Smith, 2006) in order to transcend the dualistic categories of 'elite' and 'non-elite' (or 'powerful' and 'vulnerable') or using the concept of the 'hybrid elite' (Parry, 1998) to better reflect the fluid and complex relationships between the researcher and the researched.

In the context of my research, gaining access to the initial few respondents had been crucial. Other researchers have pointed out that the use of social connections and institutional affiliations are often valuable starting points in establishing rapport with elite interviewees. McDowell (1998), for example, described how she used her college connections in Cambridge University to contact members on the boards of banks in setting up interviews with high-status merchant bank workers in the City. Through personal and university contacts, I conducted four pilot interviews in 2005 (one in Nottingham, two in the City of London and one in Shanghai). These interviews helped to verify the relevance and industry interest of the research themes in this thesis and establish rapport and contacts for later fieldwork in Shanghai. Conducting the initial interviews in London also had the advantage of providing a view from the ‘outside’ in the triangulation of field data. Given the historical connection and contemporary business interests between the UK and Shanghai, the views and experience of counterparts in the City provided additional insights into trends and prospects of developments in Shanghai. These respondents also helped to connect me with their overseas operations in Shanghai for further interviews. In Shanghai, the British Chamber of Commerce and UK Trade & Investment department of the British Consulate-General also recommended some potential interviewees in their network or database. Subsequent interviews were then largely based on a snowballing or “reputational method” (Fainstein, 1994: 17) in which researchers rely on informants to supply names of people who are prominent actors or other well-informed/connected people in their respective professional networks. Previous research experience has shown this method to work better than a purposeful selection of samples from a list given the difficulty of obtaining up-to-date and comprehensive listings in most industry sectors in China. More importantly, experience has also shown it is extremely difficult to solicit favourable response from ‘cold-calling/emailing’ potential respondents; the personal nature of a face-to-face interview, the elite status of professionals in the finance industry and their busy schedules made it difficult to obtain interviews without a recommendation or introduction from another contact.

A total of 51 interviews were conducted, the majority of which were carried out in Shanghai between February to November 2006. Respondents were mainly from foreign and local Chinese financial institutions (mostly banks and a few securities companies), and Chinese regulators and officials (e.g. CBRC, Shanghai Office for Finance, Lujiazui Financial Zone). I also interviewed two foreign companies in China with manufacturing or service operations in Shanghai to document their experience and perspectives as service clients and spoke to representatives from the British Chamber of Commerce and EU Chamber of Commerce Banking Group. Interviews with foreign entities were conducted in English (except for one) and those with Chinese organisations were conducted in Mandarin or a mixture of English and Mandarin. All the interviews were taped with permission (with the exception of one interview in the UK, two interviews in Shanghai and one email interview from Hong Kong). They lasted between 45 to 90 minutes and were all transcribed and translated by myself. Details of the respondents are listed in Appendix A.

Apart from problems of access, other issues had to be considered in the interpretation and analysis of interview data. Lim (1998) warns that elite interviewees may exaggerate or distort their roles and experience in past events, intentionally or otherwise. Some of my interviewees have relatively high public profiles in the local and international media. Given their experience in presenting their views to the public, to what extent were their comments during interviews be 'rehearsed'? This can be a rather slippery problem to negotiate and highlights the importance of data triangulation by corroborating interviewees' comments against other interviews and field data. I collected information from a wide range of sources, including field observations, interview data, the media, published reports from different agencies and so on. In this way, triangulation helps to reduce methodological problems associated with eclecticism as different practices are brought together with a common purpose of cross-checking research results and interpretations, thus improving the validity and reliability of findings (H. Yeung, 2003). Some critics have urged a move away from what they see as "unwarranted selectivity in the choice of respondents" (Markusen, 1999: 872, see also Martin and

Sunley, 2001) when utilising the 'snowballing' or case-study method. Most researchers probably start with an 'ideal' sample of research participants but as James (2006) points out, the selectivity of the respondent sample that we achieve in *practice* ultimately rests on our ability to gain access, something that can be particularly problematic as junior researchers with limited resources.[3] Rather than simply disclaiming responsibility, triangulation can help to improve the integrity of empirical findings and subsequent interpretations.

Analysing data from these interviews was a critical step in the development of theoretically valid claims about the nature, politics and process of 'markets' formation (as presented in Chapters 6, 7 and 8). My strategy for analysing the interview transcripts was to employ a systematic set of coding and recoding processes, informed by some of the techniques of grounded theory (Strauss and Corbin, 1990), which guide the researcher through the building rather than 'testing' of theories through iterative abstraction (Crang, 1997). I first sifted through the data through a process of open coding, annotating and making notes. This involved analysing transcripts, noting particular observations, sentences and paragraphs and giving each discrete incident, idea or event particular themes or codes. At the same time, I also examined the data in terms of the actors involved, their motives and positionalities and events that were happening at the time of interviews (e.g. in policy, politics and industry) that could have bearing on the issues that were discussed. As ideas emerged they were jotted down as theoretical memos. Similar phenomena identified by open coding were then brought together into common

[3] My own sampling strategy, for example, started with an 'ideal' set of interviews with foreign financial institutions, local financial institutions and regulatory and government officials in Shanghai, with an equal number of interviews conducted with each group. In the end, foreign financial institutions came to occupy a much more significant portion of my final sample and I had much fewer interviews with Chinese regulatory and government officials. Various factors that contributed to this final distribution are discussed in section 5.3.

categories and given conceptual labels, sometimes borrowing words and phrases used by the participants themselves. The themes were then re-analysed and refined in relation to my theoretical analysis of extant literature and as new empirical material was collected. Contradictions in interview responses were not conceptualised as problems but as the source of potentially fruitful new lines of enquiry in subsequent interviews. Moreover, they highlight the complexities and contradictions of 'marketisation' in Shanghai.

Finally, all interviewees were offered anonymity, which can be important given the nature of possibly sensitive information and 'stories' that are shared and the highly regulated context of China. Brief profiles of respondents are listed in Appendix A, which provides important information in interpreting the interview data but identifying traits such as individual and names of institutions have been excluded. Having said that, I am aware that for small organisations such as certain business or governmental institutions, true anonymity may not be possible since it will not difficult to deduce whom I had spoken to if one is familiar with the financial sector and events in China and do a search on the internet. In any case, I have endeavoured to provide as much contextual information as possible to be useful for interpretation and analysis without revealing too much specificities that could identify individuals.

5.3 RESEARCH PRACTICE: REFLECTIONS ON THE FIELDWORK PROCESS

5.3.1 The Contingencies of 'Snowballing'

All too often, only 'success stories' (of say X number of interviews conducted) are presented in research findings without revealing the process of actually obtaining interview data or whether other interview requests were rejected, as if discussion of the latter would somehow undermine the integrity of methods and findings. The written presentation of research findings is clearly important but what does *not* appear (and why) can also be useful and revealing of the empirical context. Crang (2005) points out that silences can point to significant moments of resistance, both in society and the process of research. Hostility to interviews or refusals due to fear, mistrust or other reasons are not just barriers to overcome but also an instructive part of the research process. In my field research, the snowballing technique for obtaining interviews proved largely successful with foreign respondents but was surprisingly limited with the Chinese. While the foreign respondents were often happy to literally dig through their business cards collection and offer contact details of friends or professional contacts, the Chinese respondents were mostly reticent. This might be explained by the different ways in which interpersonal networks seem to operate within these two communities (if one could label them as separate and cohesive groups, at least in juxtaposition to each other).

My experience with foreign interviewees in Shanghai seems to concur with work conducted on the expatriate community elsewhere (e.g. Beaverstock, 2002, 2004, 2005), in which the international experience and personal circumstances of expatriates produce a certain openness to engagement with new ideas and people, and thereby a willingness to recommend 'strangers' to friends in professional circles and to talk to said 'strangers' as well. All this is done in the spirit of helping out a 'newcomer' to the city, just as they would have benefited from similar practices when they first arrived. The snowballing technique thus works well when there are already complementary social practices and networks present within the group of target respondents. My experience was quite different with the Chinese respondents.

Relational networks appear to operate on a more trust-based and personal basis amongst the Chinese, such that while the initial respondent might suggest one or two further contacts, the 'obligation' of the latter (who were otherwise generally helpful and generous with their time and knowledge) would seldom extend to suggesting further contacts as I would then be at least twice removed down a hierarchy of relationship.

Therefore, while snowballing operates in the form of A1 recommends A2 recommends A3 recommends A4 and so on for foreign interviewees, the situation with Chinese respondents tend to be B1 recommends B2 (and possibly B3), and stop at that point as I do not have sufficient social capital with B2 and B3 (they do not know me well enough) for them to grant further contacts (Figures 5.2 and 5.3). This suggests that interpersonal networks seem to operate more like a chain for the expatriate community while they tend to form a hierarchy based on closeness of association for the Chinese community. Interviewees in the B1 category were mostly family relations or university contacts and their friends or colleagues. They were very willing to put me in touch with their contacts, often in a very personal manner such as driving me to the interview venue or calling me after the interview to inquire about how it went. B2 interviewees, on the other hand, were further removed in the relational hierarchy and were hesitant to 'recommend' me to someone else as they could not personally vouch for my credentials or status or whatever criteria was deemed important. Another point worth noting is how the contact lists of local Chinese and foreign respondents appeared to be distinct and separate, i.e. local respondents would recommend another local contact and foreign interviewees would suggest foreign ones. This alludes to the rather rigid separation between local

B1 B2 B3

A1 A2 A3 A4

Chinese and foreign participants in the Shanghai financial sector and is very much a product of the regulatory environment, a point that I will pick up in later chapters.

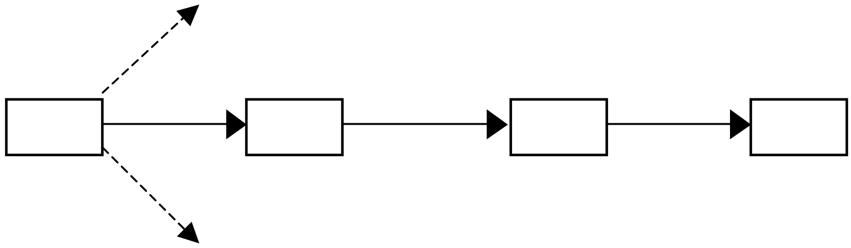


Figure 5.2 Snowballing 'foreign' style

Figure 5.3 Snowballing 'Chinese' style

The socio-cultural dimension in Shanghai's finance community has thus proved more complicated than expected in utilising the snowballing method. While the foreign banks and contacts were relatively easy to get hold of, it took a lot more time than I anticipated to obtain information and contact local Chinese respondents. While the former were happy to arrange meetings on emails, which was very efficient and helpful for advanced planning, the latter were often only contactable through telephone calls as I often received no response through emails. This could partly be due to technical difficulties in rendering Chinese characters on email programmes and internet browsers on different computer systems (one often gets nonsensical squares or symbols in place of characters within an email). The University of Nottingham's web-based email system could not handle Chinese characters which meant I could only exchange very brief emails with Chinese respondents who could write in English or had to write Chinese emails in a separate word document and email that as an attachment. Apart from the tedium of the above procedure, the relative success of telephone requests could also be due to its more personal nature and is preferable given the more trust-based nature of relational networks amongst the Chinese respondents. The process of obtaining interviews thus took longer and proved more complicated than expected. The situation improved during subsequent trips when I was able to gather more local contacts but the difference in styles of communication between the two groups did affect my final sample.

5.3.2 Not Chinese Enough? Positionalities and Hybrid Identities

Some scholars have suggested that 'insiders' – researchers who study a group to whom they belong – have an advantage because they are able to obtain greater insights through intrinsic knowledge or traits (Hill-Collins, 1991; Lughod, 1988). By contrast, 'outsiders' argue that by not 'belonging' they are more likely to be perceived as neutral and provided with information that might not be accessible to an insider (Fonow and Cook, 1991). They also claim to have greater degree of objectivity and ability to observe behaviour and phenomena without distorting their meanings. In examining the issue of positionality in the field, some geographers have problematised this insider/outsider binary which assumes that being an 'insider' or 'outsider' is a fixed attribute. This binary is in reality a boundary that is highly unstable and ignores the dynamism of positionalities in time and through space (Herod, 1999; Mullings, 1999; Sabot, 1999; K. Smith, 2006). The research process is a social one in which both interviewer and interviewee are active participants in knowledge creation and therefore although the 'insider' and 'outsider' may shape this process in different ways, it is erroneous to assume that one version is necessarily more 'true' in some absolute and 'objective' sense (Herod, 1999). Mullings (1999), for example, speak of 'positional spaces' as areas where the situated knowledges of both parties in the interview encounter engender a level of trust and cooperation. When academics have attempted to problematise the research process, positionality is often taken to refer to the physical or socio-cultural characteristics of the interviewer (race, gender, class, age, nationality etc.) but such categories are themselves problematic and not necessarily obvious to the interviewer or interviewee. One could consciously manipulate ones positionality; how others view one's positionality could be different from one's own perspective; and a researcher's positionality could also change over time (Herod, 1999).

At the beginning of the research project, I thought that my identity as an ethnic Chinese who can speak, read and write English and Mandarin would help me build trust and rapport with the local Chinese and ease communication. On the one hand, these were probably naïve assumptions on my part, but, on the other hand, it points to complex issues about positionality that I have highlighted above. Contrary to initial expectations, I had far greater interview success with the foreign respondents compared to the Chinese. To the foreign interviewees, I am an ethnic-Chinese scholar from Singapore, based in the UK, who speaks fluent English and have (presumably) 'westernised' perspectives and experience.[4] I thus stand out from most other Chinese people that they come into contact with and am, to them, rather interesting as a person. Hertz (1995) and Green (2004) also spoke of similar experiences as 'Westerners' whom their Chinese respondents found rather

[4] Almost every foreign interviewee commented on my English and asked why I speak the language so well. Few people are aware that English is taught as the first language and language of instruction in Singapore schools.

fascinating as they spoke Mandarin and even some Shanghainese (in the case of Hertz). This went a long way toward facilitating access and the process of field interaction. To the local Chinese, on the other hand, it would seem that I appeared to be a bit of a conundrum. I am a competent Mandarin speaker but not as fluent compared to a native speaker. This was especially apparent when I had to deal with technical and business terminology. I prepared (and was constantly adding to) a list of corresponding Mandarin and English phrases, terminology and names of institutions to help me in Mandarin interviews (see Appendix B) but it was still difficult at times because I just did not have the same finesse with Mandarin as I do with English when, for example, trying to ask a question in different ways to tease out particular details and corroborate the validity of claims. I also do not speak Shanghainese, which, although not problematic in communication, might have given me additional cultural capital. Although I am, technically speaking, a 'foreigner' who speaks Mandarin as a second language, I had a rather different experience compared to Hertz and Green because I am ethnically Chinese. Thus, I seem to occupy a liminal space in the field of not being foreign enough to make me 'interesting' to the Chinese respondents and yet not being local enough to ease access and communication with the locals.

Out of the 51 interviews, I only managed to obtain three with local regulatory and government officials (with another four Chinese interviewees having previously worked for regulatory bodies and were asked to reflect on their experience and official stances there). Apart from the problem associated with accessing local respondents in general (as explained earlier), I was also told by a number of local respondents and one of the three officials that the official policy was not to give interviews to scholars or journalists without prior approval (which is very difficult to obtain). Even when I was successful in getting a meeting through specific recommendations, the interview process often proved to be more difficult than prior experience. I found myself having to press and prod more than I ever had to (while worrying about whether I was being rude!) for further elaboration and examples to be given. This made it very difficult to obtain their views and experience of the regulatory environment in Shanghai and China, changes in the system and potential problems and progress. I also came to question the usefulness of such interviews. Advice from local contacts (personal contacts as well as local Chinese postgraduate and faculty researchers) revealed that my experience is common and that Chinese government officials and regulators tend to be very taciturn in interviews. They pointed out that there might be little value-added information in what I obtain from such interviews compared to information publicly available from official websites, official reports and press release due to the closely-regulated nature of information management in China. My experience thus echoes that of Sabot's (1999) in her interviews with local French officials where the institutional context is such that mistrust and minimal disclosure of information are the rule:

> The right behaviour to adopt is: first, if possible, try to postpone the appointment, hoping that (s)he will lose patience. Secondly, if the stubborn researcher insists on having an interview, receive him/her very politely, with all regard due to his/her position, but avoid giving any written documents […] which could be used in a distorted way […]. Thirdly, be careful about what one says by adopting a stereotypical formal language; avoiding all the sensitive current events; cultivating ambiguity in order to confuse […] and never complaining about anything or anyone, because every word spoken can boomerang back and cause serious damage (p. 332).

And indeed, I was never given any documentation at those meetings and vague language permeated the course of our conversations.[5] As a result, the main sources that I used for local government and regulatory authorities' vision of market formation were from official websites, official reports, press release and news articles, which can still be very informative if one knows how to read between the lines. When speaking to interviewees from local and foreign financial institutions, I also actively sought their views on local regulatory processes and frameworks and their encounters and interaction with local officials and regulators to get a sense of the (changing) regulatory environment. This helped me to corroborate what I read from official or publicly available reports with a spoken discourse, which I could triangulate with the interview data from those three 'official' respondents and other Chinese interviewees with regulatory experience.

Herod (1999) and Sabot (1999) note that in their experience being foreign Western academic researchers afforded a warmer reception than being local researchers, i.e. being an 'outsider' was important in conducting the research. My field experience seems to mirror those observations particularly in my interaction with the Chinese interviewees. A number of them were quite careful in enquiring about my affiliation and nationality at the beginning of the interview, as if assessing how much of a 'threat' I might be and how much information would be safe to reveal. Although it would be hard to prove conclusively, 'playing up' my identity as a Singaporean – i.e. emphasising my status as a foreigner and 'outsider' with little understanding of the Shanghai context – allowed me to ask questions without being perceived as too inquisitive or intrusive and might have given me some advantage in

[5] Conversations with local academic researchers in Shanghai reveal that the majority of research projects in universities are funded or commissioned by government or other official bodies and the conspicuous use of letters from those authorities are vital to the research process in obtaining interviews and documents.

that interviewees perhaps perceive me as a harmless ‘foreign’ academic rather than, say, a threatening ‘local’ investigator. By lowering the (perceived) risk of reprisals, they might have been more open and candid in sharing their views and experience. Certainly there were various points during which I felt very strongly that I would have been told even less if I had been a local researcher, such as when I was specifically asked about my affiliation and nationality to establish my ‘foreign’ status before the interview progressed.

5.4 CONCLUSION

> *Somehow you have to get in there, and although we often, in writing up our results, talk blandly of our samples or our case studies, letting the reader assume that the particular industry, location, site, and respondents were the optimal or ideal for investigating the particular issue in which we were interested, we all know that the ‘reality’ – if I can use that old modernist term – is a lot messier. A great deal depends on luck and chance, connections and networks, and the particular circumstances at the time (McDowell, 1998: 2135)*

McDowell (1998), Parry (1998) and Hughes (1999) firmly acknowledge the role of chance in accessing corporate elites and eliciting information from them. My research journey was also guided, at least in part, by an element of luck and circumstances which I could not have anticipated. Such is the rich yet ambiguous and messy world of doing qualitative research. Thrift (2003: 106) notes that “more often it is a curious mix of humiliations and intimidations mixed with moments of insight and even enjoyment.” Some of the taken-for-grantedness about fieldwork has indeed been replaced, as evident from the critical and reflexive engagements from the geographers mentioned in this chapter. But others scholars have continued to push the boundaries of qualitative research (see, for example, Schoenberger, 2001; Latham, 2003; Crang, 2005; Wiles et al., 2005; James, 2006). Interviews have tended to form the ‘bedrock’ of qualitative research methods with some attempts made to reach beyond the limitations of this through focus groups and, to some extent, ethnographic research (usually in the form of participant-observation). Valentine (1999), for example, incorporates methods such as food and photographic and video diaries in addition to in-depth interviews and focus groups and Latham (2003) uses photographs, text and time diaries produced by respondents to convey a sense of practising places.

For this research, I have found it very useful to keep a research diary (or field journal) to record field experience as well as events that were happening in the media and local and national politics, especially those relating to changes in the finance industry, and news or rumours circulating in the industry grapevine that emerge in the course of conversations (Table 5.1). Such records helped me to put interview data in context of events that were happening during that time as well as to capture fresh thoughts, ideas and observations that emerge not only in the course of conducting the interviews themselves but also when obtaining contacts, requesting for meetings, walking around the LFTZ, going in and out of office buildings, having lunches with interviewees and local academics, and so on. Field data should not be seen as only consisting of interview transcripts but needs to include the more holistic experience of being 'out there' in the field and the observations, interaction and insights obtained in that process. I certainly would not have been able to write much of this chapter without having kept a research diary to record my thoughts and experience as they happened and I would argue that this has added richness and additional insights into my analysis. As researchers of 'elite' geographies, it is perhaps more difficult for us to employ methods such as participant-diaries or ethnography but we do need to think of creative ways of collecting and incorporating empirical material that begins to unpeg the corporate interview from its currently privileged position in the economic geographer's research toolkit.

Table 5.1 Excerpts from research diary

"Over the past 10 days, the local news was filled with reports on the NPC (National People's Congress) & CPPCC (Chinese People's Political Consultative Conference). Focus was on building a 'Socialist countryside' and a 'harmonious society', Also on technology and innovation in science and technology sectors. Not much on finance itself. That seems to have taken a back seat after being in the limelight for the past decade. Income and regional inequalities are high on the agenda with development targets for the western inner regions of China." (14 March 2006)
"I was rather hopeful about this one because it was important. The Shanghai Municipal Council Office of Financial Services. I hoped to get some good stuff. But it was rather disappointing. That guy was very taciturn and just didn't seem very interested in general. Of all the interviews that I've done, I have never had to push as hard as for this one. I kept pushing for more details, asking for elaboration, specific examples and so on but he just wasn't keen on giving too much detail. I was feeling rather discouraged and embarrassed actually. I knew on a professional level this was my job and I was supposed to just keep pushing and seeking, to be bold and thick-skinned. But on a personal level I felt really awkward and impertinent. I felt really bad about it. It felt like he just wanted to get me out of his office as quickly as possible. A day later, when I was having dinner with QY (a PhD student from East China Normal University), she related similar experiences when she interviewed officials. I was quite relieved that it wasn't just me. She also confirmed other people's opinions that I might not find it all that useful to interview officials because they are not always very cooperative in interviews and are unlikely to offer any extra info that one could not obtain from published sources. Definitely something to keep in mind…" (22 April 2006)
"The interview was difficult in that he was unwilling to talk about operations of [the securities company] itself. He was quite firm in only wanting to talk about very general or macro issues and refused to go into specifics. I found it interesting how he asked whether I was local or Singaporean or from the UK. It was as if he would have told me even less if I was Chinese! When I asked for his views, he kept saying how we should leave the government to do the right thing and not criticise what they are doing. We can put forward suggestions or recommendations but not say what they are doing is right or wrong. Basically refused to comment from personal experience or perspective unless he has actually done a report or project on that specific topic. It's incredulous. I found it incredible, the very tangible fear of saying something 'wrong' and of getting into trouble for that. Absolutely incredible." (17 October 2006)

In this chapter, I have considered the multiple identities and roles that I took on in the field (positioning myself as sometimes foreign, sometimes Chinese, sometimes knowledgeable and sometimes an enquiring student), as well as roles accorded to me that I did not anticipate or had little control over. A researcher's (fluid and shifting) positionalities influence the kinds of 'data' collected and thus the information that becomes coded as 'knowledge'. 'Position' indicates the kind of power that enabled a certain kind of knowledge and knowledge thus positioned, or situated, can no longer claim universality:

> In contrast to the god-trick of claiming to see the whole world while remaining distanced from it, subjugated and critical knowledges work from their situatedness

> to produce partial perspectives on the world. They see the world from specific locations, embodied and particular, and never innocent; siting is intimately involved in sighting. (Rose, 1997: 308)

This reflexivity and transparency in presenting the methods and results of empirical research is particularly important in establishing 'rigour' in qualitative research. The quality of intensive and case-study methods should be judged on the veracity of the claims made rather than on the grounds of representativeness, replicability, and generalisability. In his response to Markusen (1999), Peck (2003) disputes the claim that the shift towards qualitative methods in regional studies and economic geography has led to declining standards of evidence, 'fuzzy' theorising and policy irrelevance. He argues that qualitative and case-study methodologies need not be any less rigorous (than, say, quantitative methods) if appropriate steps are taken towards setting high standards of research design, better corroboration and triangulation of data to improve their validity of claims; nor should they be less relevant as intensive methods have an important role to play in the spirit of methodological pluralism. "There is no royal road here, only different methodological paths" (Peck, 2003: 732) and the shift towards qualitative methods "does not [necessarily] imply lower 'standards of evidence'; it entails *different* standards of evidence" (p. 738).

The situatedness of my knowledge and the knowledge that I derive from an extensive reading of the work of others shape my own interpretations and presentation of the research. Establishing certainty in the claims that I make required the use of a number of techniques ranging from the triangulation of information from multiple sources, methods and theories to the unveiling of the constructs that guided the research and the limits posed by the sample used. Reflexivity is an important process for making clear the landscapes of power within which our research practices are invariably bound up with. In this chapter, I have sought to make visible my position within the written research by revealing the circumstances that surrounded my field research and how that process has shaped the data collected and subsequent analysis. Gaining access to a range of respondents and being able to corroborate their views and identify inconsistencies can go some way towards validating findings based on corporate interviews, but recognising that the information we as researchers receive will always be partial makes our claims more circumspect and our stance more reflexive. This is a consideration that is particularly important for producing valid accounts of economic landscapes and processes based on qualitative methodologies.

Chapter 6

Walking the Chinese Road to 'Marketisation'

State Institutions and Re-regulation

6.1 INTRODUCTION

> *"Shanghai's goal is to develop an international finance and trade centre. […] If China doesn't have a financial centre, it will not have much standing in this world. A financial centre, there are only a few financial centres in the world. There is New York, London, we can feel that they are truly global financial centres. […] No matter where it is [sic], if there are some changes to the financial markets in these places, there will be changes globally as well. Global markets will be affected, so they have global impacts." (Planning official for LFTZ: #19, 10 April 2006)*

The desire for China to have a role on the world stage through developing a financial centre in Shanghai is expressed above by a government official from the Administration of Pudong New Area in Shanghai. The Shanghai stock market might have achieved some global influence, as seen in the knock-on effects it had on the US and world stock markets when the Shanghai stock index dropped 8.8 per cent on 27 February 2007 (*Time Magazine*, 18 February 2007), but this on-going process of instituting market-led practices into the Chinese economy is complex and contested. Regulatory changes, technological innovations and the globalisation of markets and monetary flows are remapping the financial landscape towards deterritorialisation but states remain important arbiters in determining the shape and speed of such processes. The state and state institutions continue to exert significant influence within their national space economy as well as on the international arena through the channels of supranational organisations (such as the IMF, the EU and WTO). The case of China's journey towards 'marketisation' in its financial sector reform demonstrates this complex and fluid relationship between state and finance capital.

In this chapter, I examine how the state, through government institutions and regulatory bodies, manage tensions between the desire to maintain regulatory control and the imperative of global finance capital. To do this, I examine the process of 're-regulation' through the experience of government and regulatory authorities, and foreign financial institutions in Shanghai. In the next section (6.2), I examine how knowledge networks are constructed to build up the necessary expertise and skills in developing the legal and regulatory frameworks needed by Shanghai in building its financial markets. Who are the actors involved in such flows and how and why are different concepts and principles adopted or rejected by the Chinese officials and regulators? The pace and style of reforms have been tightly controlled by the state. In section 6.3, I analyse the reactions and views of foreign and Chinese interviewees from financial institutions in Shanghai and their assessment of how much control the government exerts over the 'marketisation' process. Is this pace deemed too quick, too slow or appropriate by financial institutions and participants in Shanghai? In section 6.4, I discuss some of the problems associated with current regulatory structures and procedures, which have been pointed out as problematic by interview respondents. In section 6.5, I use the case of China's WTO commitments to illustrate the tension between the imperatives of the state and international pressures. Finally, in section 6.6, I examine how specific regulations and 'soft power' are used to control the activities of foreign banks in Shanghai, to solicit 'appropriate' behaviour and cooperation, and thereby control the pace of 'marketisation'.

6.2 ADOPTING BEST PRACTICE? KNOWLEDGE TRANSFER AND ACQUISITION

As China's central bank, the PBOC is in charge of more than the country's monetary policies; for most of its existence it has served as the cashier for the Ministry of Finance (MOF) under Soviet-style planning. In addition to handing out working capital loans to SOEs, its attractiveness to all levels of the state was enhanced by its control of China's mints. Until the passing of the Central Bank Law in 1994, the PBOC was the banker of last resort for the national, as well as many local, budgets. Although it was called the 'central bank', the PBOC was in fact a very decentralised entity with principal staffing and functions at the provincial level and a small staff of only a few hundred in Beijing. Local branches, although reporting on a direct line to Beijing, had strong links to local governments such that the local party had the right to nominate senior branch staff. With this background, there were doubts as to whether the PBOC would be an appropriate candidate to act as the national regulator of a rapidly evolving market-based experiment (Walter and Howie, 2003).

Creating effective institutions, the rules that govern economic transactions that are monitored and enforced by regulatory agencies (as well as other institutions like the courts, accountants, media and industry participants) lies at the heart of a successful market-based economy. To ensure that the use and trading of property rights is fair and transparent, and that abuses are punished appropriately, a complex set of regulatory institutions must be created, including an architecture of rules and organisations to monitor and enforce compliance with those rules (Hutton, 2007). To achieve these objectives, three regulatory bodies were created as spin-offs from the PBOC. The China Securities Regulatory Commission (CSRC) was established in 1992 as China experimented with stock markets in Shanghai and Shenzhen; the

China Insurance Regulatory Commission (CIRC) was established in 1998 to regulate the insurance industry; and the China Banking Regulatory Commission (CBRC) was the latest to be set up in 2003 to implement banking reforms and open up the banking sector to foreign competition under WTO commitments. This allowed the central bank to focus on monetary policy and financial system stability while the three regulatory bodies focus on securities, insurance and banking regulation and restructuring (see Figure 6.1). The establishment of these regulatory bodies, with their specific areas of responsibility and mandates, were widely seen as indicative of China's commitment to reforming its financial sector along market principles and opening up to foreign investors and competition (*People's Daily Online*, 24 April 2003).

At the launch of the CBRC, its Chairman, Liu Mingkang, pledged the regulator's commitment to "further deepening financial reform, improving financial supervision and mitigating financial risks, so as to maintain a safe, sound and efficient financial system in China". He also declared that the establishment of the CBRC "demonstrates that China's financial sector has been opened up further to the outside world, while the financial supervisory regime has been brought closer to the international best practices" (quoted in *EuroBiz Magazine*, July 2003). How are clearly capitalist market principles being implemented in an economy where such structures do not exist (or are in their infancy) and in a society that is still broadly 'socialist' in official rhetoric? How are "international best practices" being accessed and adopted by regulatory bodies such as the CBRC? These are done through networks of knowledge transfer and skills acquisition (i) at the regulatory level with counterparts in other financial centres, (ii) at the industrial level through consultation and lobbying and (iii) at the individual level through recruitment strategies.

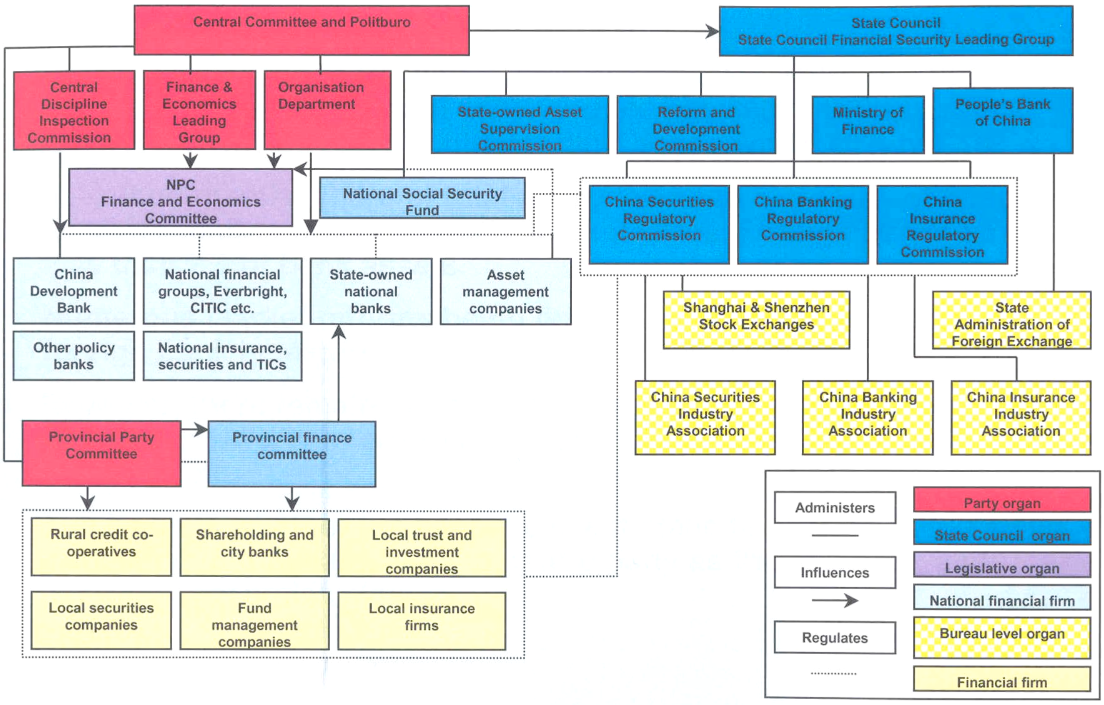


Figure 6.1 China's financial eco-system *(Source: Chatham House material from interview #4)*

Specific channels of knowledge and skills transfer were set up by the regulators to connect with sources of expertise both within and outside of China. On the regulatory level, the CBRC has a Regulatory Cooperation Memorandum (监管合作备忘录; *jianguan hezuo beiwanglu*) with counterparts from about 20 other countries and financial centres, ranging from London, New York and Russia to New Zealand, Hong Kong and Singapore. The idea was to "stand on the shoulders of giants" (planning official for LFTZ: #19, 10 April 2006), to learn from their regulatory models and methods and then assess how best to implement particular aspects of those in China or specific areas like Shanghai:

> I think you have to learn from real world cases and experience. But you must have contextual knowledge. Like you know how the Americans do it, how it is done in Singapore, how it is done in Hong Kong, then you think about how you should do

> this here. That is the best method. And that is how we are doing it. […] We use a global view to examine our own problem, to see how we should develop. (*Ibid.*)

Memorandums of understanding (MOUs) (for example, between the CBRC and the Hong Kong Monetary Authority,[1] and between the CSRC and the HM Treasury of the UK[2]) provided frameworks for cooperation, including channels for communication, increased mutual understanding and the exchange of regulatory and technical information. Through these international channels, the Chinese regulators were able to acquire technical support and access different conceptual understandings of banking and finance restructuring and management, learning from different regulatory methods and experience. These were done through specially organised conferences and workshops held in China or other countries, fact-finding trips to different financial centres, and training and internship programmes. The Monetary Authority of Singapore, the Federal Reserve of the USA, the IMF, World Bank and Asian Development Bank, for example, regularly hosted officials from the CBRC, CSRC, and PBOC on training workshops or attachment programmes in their respective country offices and also sent their representatives over to China every year on training visits and exchange programmes (economist for foreign bank: #7, 22 February 2006; CBRC official: #25, 16 April 2006).

Within these networks of knowledge transfer, some regulatory models or practices were deemed more attractive or suitable than others with respect to China's political and economic context. While Hong Kong's proximity and success as an international financial centre and close economic ties with China might render it a natural role model for mainland China's financial sector reforms (according to some interviewees), its specific economic history and governance system made it

[1] http://www.info.gov.hk/hkma/eng/press/2003/ 20030825e3.htm
[2]http://www.hm-treasury.gov.uk/documents/financial_services/securities_and_investments/fin_sec_china.cfm

problematic to transfer regulatory principles and frameworks. In examining the experience of other developing economies, Singapore's more conservative regulatory style (vis-à-vis Hong Kong) and success based on a managed market-economy was deemed closer to China's experience and had been highlighted as a valuable learning partner (government official from Office of Financial Services: #28, 20 April 2006). Amongst developed economies, the UK appeared to be a preferred learning partner. Special committees consisting of industry experts, economists and regulators from the UK (particularly the City of London) have advised the Chinese on aspects such as interest rates deregulation and bankruptcy laws. Rather than being one amongst many countries, the UK was often consulted in isolation and asked to advise on specific issues on financial sector reforms. This could partly be due to the UK being seen as having a more prudent approach to financial services regulation compared to, for example, the US (economist from an international bank in London: #4, 11 January 2006), but such consideration could also be down to personal ties. Liu Mingkang, the chairman of the CBRC obtained his postgraduate degree in the UK. He was reputedly very good friends with Howard Davies, former chairman of the Financial Services Authority (FSA) and had mentioned the possibility of modelling the Chinese financial regulatory system on the FSA. There were working groups from the CBRC that visited the FSA on a regular basis, as well as interns who worked within the FSA not only to absorb ideas and techniques but also to establish contacts that are maintained when they return to China (country representative of foreign bank: #16, 9 March 2006; chief representative of foreign bank, #29, 12 October 2006). The development of regulatory expertise and structures in China were clearly influenced by models, experience and actors elsewhere in the global financial space.

Apart from regulatory counterparts overseas, industry participants within China were also tapped upon for specific skills and knowledge of the banking and finance industry. The CBRC in Shanghai and Office for Financial Services of the SMG would consult the financial institutions in Shanghai to understand their perspectives on particular issues, problems that they were facing and suggestions for improvement. Rather than on a regular basis, industry participants tend to be consulted on a particular topic or just before the drafting of new policies or reforms and both foreign and local banks in Shanghai would be consulted depending on the issues at hand. The CBRC in Shanghai also had an international banking committee which held regular meetings to keep in touch with the concerns of the international banking community in Shanghai (head of department of foreign bank: #49, 3 November 2006). One such example was how the CBRC worked on encouraging more business lending to small- and medium-sized enterprises (SMEs), a business sector that had been largely neglected by the Chinese state-owned banks. The CBRC went directly to specific foreign banks that had been successful in this loan sector to learn from their experience and seek advice:

> They [the CBRC] definitely consulted Standard Chartered Bank because [they] were so successful in SME banking. At that time the government was really wanting to do something for the SMEs […] State owned banks are very reluctant to extend loans because there is no credit, credibility, you know, no financial report that sort of thing. […] They asked [for] a report saying 'how are you doing, what is your business with SMEs like, what are your views on SME banking and what are your success stories'. All sorts of things. 'What are your concerns?' So they are very willing to learn. And I believe that they consult other foreign banks as well. HSBC definitely. And… within a month after that, produce a regulation just to… guiding the state owned banks to be more willing to extend loans to SME sector. (Deputy representative of foreign bank: #30, 12 October 2006)

Through these consultative channels, industry participants were able to influence aspects of banking reforms, albeit only by invitation from the regulators. Professional bodies within the industry such as the Securities Association of China[3] and Shanghai Banking Association[4] were also involved in the building of expertise and raising professional standards of its members by inviting overseas experts into China for training seminars and collaborating with other professional bodies in places like Hong Kong for joint programmes and training. The International Advisory Services department of Lloyds TSB[5] in London, for example, conducted training programmes on corporate credit assessment, international trade finance and bank analysis that had been attended by representatives from regulatory bodies as well as state-owned banks from China (international bank in London: #49, 12 March 2007).

Apart from being partners in consultative meetings and offering training programmes, foreign financial institutions in China were also key actors in the 'marketisation' process through institutional affiliations with foreign chambers of commerce. The EU Chamber of Commerce (EUCC) in China, for example, published an annual Position Paper representing an overall view of European companies doing business in China.[6] It detailed the key concerns and recommendations from each of its 30 Working Groups regarding issues such as WTO implementation, trade, regulatory issues and broader policy-related issues. Each Working Group highlighted the five most important issues relevant to its sector or industry, explained the problems, and offered advice and solutions. The Position Papers were presented to the Chinese government each year with the aim of

[3] http://www.sac.net.cn/en/homepage/index_en.jsp
[4] http://www.sbacn.org/introduction/default.asp?LanguageID=2
[5] http://www3.lloydstsbcorporatemarkets.com/internationalservices/ias.asp
[6] http://www.europeanchamber.com.cn/show/details.php?type=3

improving the investment climate in China and were often used as a basis for negotiations between the EU and China. They were also given to EU authorities and visiting delegates as a basis for lobbying on specific areas of trade and foreign investment concern. The American Chamber of Commerce[7] also have similar groups and publications as basis for negotiations with the Chinese regulators and other state institutions.

The EUCC Banking Working Group in Shanghai met once a month to share problems that individual members/banks were facing and discuss issues of concern, which were then forwarded to the CBRC and PBOC for their consideration. Before the launch or approval of each financial products the PBOC, CBRC or CSRC would hold rounds of consultation with banks and individual specialists within financial institutions to troubleshoot and identify potential problems. Before the announcement of new regulations, draft copies would be sent out to individual banks to assess market reaction and garner responses. Very often, those banks would bring the draft regulations to their respective banking groups or associations and the groups would send in an official response if necessary. An interviewee related this process of how:

> [b]efore [the] launch of each products, normally like PBOC or CBRC or other regulators they will consult rounds of times with banks, specialists, saying what is the impact of this new product launch, what is the technical issue, what is the other issue that needs to be considered before we launch it. So after rounds of discussions, they will have introduction of this product in the end and then we will have several rounds of education to pass information to banks. […] Also before the launch of each product, we as well as other foreign banks and local banks have been invited to Beijing to Shanghai or other places to discuss about these markets, to give your

[7] http://www.amcham-shanghai.org/AmChamPortal/MCMS/Presentation/Publication/WhitePaper/Default.aspx?HLLink= Sl_Pub_2&tb_Name=Publications

> views, concerns, difficulties, benefits, everything, to share… for them to make the last decision. (Deputy head of department of foreign bank: #15, 7 March 2006)

There was thus a clear channel of dialogue between these market participants and regulators. However, some interviewees expressed their reservations regarding the influence of these Position Papers and consultation on real market and regulatory environments:

> The problem is of course with these [draft] regulations they have a lot of funny things in there. You can tell them this is all rubbish, what you wrote there, but… they will never totally change this. They won't take it back and write something totally different. What you can do is you can try to fix certain issues in the draft, but the general thing usually stays the same. And then you just have to live with it. (Chief representative of foreign bank: #45, 1 November 2006).

In terms of the EUCC Banking Working Group Position Paper, for example, the top five issues highlighted in the report had remained the same in the past five years with only very minor improvements (*ibid.*). The regulators often knew very well the concerns of the foreign banks and the desired regulatory changes but reforms were not always carried through due to other political and economic considerations. The regulators had to be careful about giving the impression that they might be giving away too many incentives to foreign financial institutions instead of helping the local Chinese banks. The pace and structure of reforms seen as appropriate and desirable by the foreign banks were also not always deemed appropriate for the current Chinese context (more on this in section 5.3). Even though the power of foreign financial institutions was limited in these channels, such networks of influence was still valued by both the industry actors and regulators as a basis for knowledge transfer and negotiation and did have significant bearing on the content and structure of reforms and longer term trend of 'marketisation'.

At the individual level, another strategy had been to attract overseas Chinese to return to China where they could contribute their knowledge and experience in regulatory bodies. Many of them were educated in the US, Europe and Australia and most had experience working on Wall Street, the City of London or Hong Kong. Amongst the most prominent of the '*hai gui pai*',[8] or faction of returnees, at the CSRC were Gao Xiqing and Laura Cha (more generally known as Shi Meilun on the mainland), both of whom were vice-chairman of the CSRC. Laura Cha held a US law degree and was formerly vice-chairman of the Hong Kong Securities and Futures Commission. Her CSRC appointment in 2003 was part of an initiative by Zhu Rongji to hire world class talent into China. Although these returnees wielded considerable influence, they were sometimes criticised for promoting policies that are perceived to be ill-suited to China, such as the pace and style of reform being too quick or inappropriate for the local financial and regulatory system. Gao, for example, had been a consistent advocate of a mandatory disclosure system similar to that of the US. He had been critical of the Chinese government's insistence on approving all listed stocks as it gave an apparent signal to investors that the investment was a good one. The number of listed companies had grown dramatically as a result but in his opinion only less than 10 percent of those companies were really worth investing in. The Chinese government, on the other hand, was more concerned about bolstering investor confidence when they embarked on the stock market experiment and was more comfortable with the familiar government's-stamp-of-approval method, regardless of the market signals that it conveyed. It was not difficult to see why many of these returnees did not stay for long[9] (analysts for local securities firms: #22, 12

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[8] Returnees are often referred to as 'sea turtles' (海龟) in a joking or in a slightly derogatory manner. It is a pun (homonym) on the word 'hai gui' which sounds the same as 'returnees' or 'sea turtles'.

[9] Laura Cha was at the CSRC from 2001 to 2004. She is now is a member of the executive council of the Hong Kong Special Administrative Region (SAR) and non-executive chairman of HSBC

April 2006; #34, 17 October 2006; general manager of foreign bank: #41, 27 October 2006).

6.3 '*DI FANG HUA*' AND THE PACE OF REFORMS

All (current and former) Chinese regulators and officials whom I interviewed were keen to emphasise a contextualised approach in learning from the regulatory models and experience of other countries, to adapt such knowledge and expertise to the historical context and economic needs of China. While "the original idea is from abroad, learning from those overseas […] as it comes into China, it has to change its flavour, to '*di fang hua*' (地方化; localise)" (Planning official for Lujiazui Finance Zone: #19, 10 April 2006) to suit economic and political conditions in China. Gao Xiqing, the former Vice-Chairman of the CBRC noted that:

> While we tried to copy [the American securities system] in many ways, we also borrowed rules from the British, Taiwanese, Japanese, and German systems, because the American rules of laissez faire sometimes just wouldn't work in China. [The Chinese] people wouldn't agree to it. Even after all these years, we have a system that looks on the surface like others, but when you talk about the enforcement level, and the actual details of the laws, it's very different.[10]

This emphasis that 'foreign concepts' would not work in China were also particularly prominent amongst most of the ethnic-Chinese respondents from financial institutions (both foreign and local) that I interviewed. Their argument was that due to different political and economic histories, different philosophies of market development and approaches, level of maturity and economic structures, the

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Investment Asia Holdings Limited. Gao Xiqing served from 1999 to 2003 before moving on the position of vice chairman of the National Council for Social Security Fund in China.

[10] http://www.law.duke.edu/magazine/2005fall/profiles/prcgaoxiqing.html

‘markets’ being developed in China must necessarily be different from that of other countries. A local respondent, for example, pointed out that:

> Of course we would like the market to grow as quickly as possible, as a business. We can only work for a few decades and I hope that things can develop quickly during my working life, that we can attain the same standards as Wall Street. But I think that is not practical. I think it will be up to the next generation and I am willing to push things up to the right level for them to take over. [… T]hese things are determined by background. We cannot go according to a western, mature market, do you understand my meaning? Our backgrounds are also different; we have a more planned economy approach. We don’t have the same experience of market development as in other countries. (Local manager of Chinese securities firm: #35, 18 October 2006; translated from Mandarin)

Another Chinese interviewee emphasised China’s “unique characteristics” that must be taken into account in its ‘marketisation’ strategy:

> China does have its own unique characteristics. So if you rely completely on foreign concepts and methods, maybe it seems very advanced and attractive theoretically, but in practice it may not be possible in China. Cannot be done. (Local analyst of Chinese securities firm: #22, 12 April 2006; translated from Mandarin)

This ‘*di fang hua*’ or localised approach to ‘marketisation’ relates to the actual content or structure of regulatory frameworks as they are developed as well as the pace of reforms. Instead of making sweeping changes to existing regulatory frameworks or opening up the financial service sectors to foreign competition with bold liberalisation policies, the approach taken by the Chinese authorities had been a very measured and cautious one, to take things step by step, examine the implications and results, make further adjustments and then take another small step. Once again, this was related to a ‘Chinese style’ of implementing reforms, which had to be taken in a slow and cautious manner to avoid political and social unrest. The word, '*jinshen*' (谨慎), meaning prudent or cautious, was often used by interviewees to describe the Chinese style of reform. Looking at the experience of Soviet Russia and Eastern Europe, the Chinese state had drawn the conclusion that the so-called 'big bang' liberalisation of sudden and comprehensive price reforms combined with wholesale privatisation had led to the sale of national assets to foreign powers and economic, political and social instability (Green, 2004; Nolan, 2004). This experience was contrasted with China where an incremental reform process had been preferred and relatively successful (if problematic in other ways):

> Firstly, you have to identify the problems, what are the main problems and what do you need to do? In this aspect they know what is needed but to implement sweeping reforms, that is impossible. And it is not in line with the Chinese style of reforms. The Chinese style of reforms has always been very cautious (谨慎; *jinshen*) and gradual. Not like in Russia or like *perestroika*, basically it is not possible to happen here. (Local analyst of Chinese securities firm: interview: #22, 12 April 2006; translated from Mandarin)

In terms of launching new financial products and approval new business areas for banks and financial institutions, the regulators had been very conservative and moving very slowly due to the fear of instability in the financial markets, the economy and thereby political and social instability. The ability to *control* the pace and structure of re-regulation and 'marketisation' was a top priority in order to avoid market chaos and social unrest.

In terms of reaction from the industry, opinions differ somewhat between the Chinese and foreign respondents. Many of the Chinese interviewees viewed the current pace of 'marketisation' as being either appropriate for China or a little too quick, and expressed concerns about the abilities of Chinese banks, finance workers and the common people (small investors) to 'catch up' with the new concepts and practices as well as broader issues of economic and social inequality in China:

> The thing is that the market is too big and difficult to manage. […] It was a centrally planned economy […] and now to deal with more market economy… So there are many contradictions. I just feel that Chinese people like to '*juan xiao kong zi*' (砖小空子; poke small holes). Meaning… looking for loopholes in the laws or regulations… the Chinese love doing that. If the regulators are not strict, I think there will be problems too. The RMB exchange rate, for example, I think it is a good thing that they don't let go all of a sudden. Too quick. The big problem in China is that there are too many peasants, if they cannot adapt they may revolt! (Local manager of foreign bank: #44, 27 October 2006; translated from Mandarin)

The foreign interviewees, on the other hand, tended to view the speed of development as being too slow for their liking, particularly from their business perspective, but almost all of them conceded that the pace of change is appropriate in the China context:

> For China, [the pace is] appropriate. Again, it's like a decision making process. There are so many single-interest, pressure groups, involved that they have to find a way through this to balance things. And again when you consider where China is standing from and where it is standing today, you could run this country into chaos. Yeah, so it's amazing to see what they do. And again, for foreigners, it's always easy to say that, 'Hey you've got to do this', the US says 'you have to appreciate [the RMB] right away'… but hey, it's not their country, and these people who run it are very clever, very smart, they know what they're doing. So, step by step, take it easy, they have 5000 years of history; doesn't matter if it takes another 5000. I think for China it's just right. (Foreign manager of foreign bank: #41, 27 October 2006)

A Chinese respondent who worked for a foreign bank expressed the exact dilemma faced by the regulators in instituting reforms and opening up the finance sector to foreign competition:

> Of course you want Shanghai to be, to establish our financial centre, to be able to compete especially for the banks, to be able to compete with the foreign banks worldwide. On the other hand, you fully realise the problems with the state-owned banks, so you have mixed feelings because the time is not enough for them… So being a Chinese, [I] always have very mixed feelings. First of all, working in an international bank, I can see the potential of this competition, all these sort of things going on. But on the other hand, I think about the mass population and… the state-owned banks who employ so many people. So if the country do [*sic*] fully open up, what about the problems that will be caused? I am fully in support of the open up policy, that sort of thing, in support of what the regulators are doing, but in some ways, I think maybe we need a little bit more time for the state-owned banks. They are doing pretty well. Three of the four state-owned banks are going public. Especially like ICBC, going public in November. But probably I think they need a little bit more time. (Local deputy representative of foreign bank: #30, 12 October 2006)

The process of change, therefore, had more to do with the ability of the Chinese industry and society to adapt rather than the capabilities and knowledge of the regulators themselves. Almost all Chinese and foreign respondents that I met with expressed their high opinion and confidence in the knowledge and skills of the Chinese regulators and officials that they have met, and approved of their avoidance of 'shock therapy' in reforms. The regulators had to balance the demands of the finance industry, of foreign financial institutions, state-owned banks and private Chinese institutions, with pressure from institutional and small investors, lobbying by other governments and supranational organisations, and political considerations of central administrators in Beijing. They might know the problems that needed to be tackled but were not always free to act on them due to other constraints. A foreign interviewee from a foreign bank (#40, 25 October 2006) revealed her assessment through dealings with the Chinese regulators:

> [I] went to Beijing to try to meet some CSRC people, really quite impressed because these guys they know the reality and when you are talking to them they are very direct. 'Ok, you are right, we need to improve the regulation like that. But wait a little bit…' But they know, they know perfectly. They know perfectly well what's the problem.

The philosophy behind the 'marketisation' process, of the banking industry, securities market and other areas of the finance sector, had always been that of experimentation, with an eye on an 'exit route' such that if things should go wrong they could be shut down and restarted again when underlying conditions and problems were corrected. This concept was spearheaded by Deng Xiaoping back in 1992 when he pushed for the development of stock markets in Shanghai and Shenzhen:

> As for securities and the stock market, are they finally good or bad? Are they dangerous? Are they things that only capitalism has or can socialism also make use of them? To decide whether they can be used, we must experiment first. If we think they work, if after a year or two we think they are good, then we can expand them. If problems arise, we can close them down, immediately and completely. And even if we close them down, we can do so quickly or slowly, or we could even leave a little tail. (Quoted in: Green, 2004: 138-139)

However, many of my respondents expressed their reservations and doubts as to whether 'shutting down' was still an option now when the process of re-regulation and 'marketisation' had gone so far. With the involvement of foreign participants such as foreign financial institutions and global capital, relationships established with foreign governments and regulatory bodies, and commitments made to organisations such as the WTO, China might no longer be able to pull the plug as easily as it might wish to. As one respondent put it "the genie is out of the bottle, it's so far out you cannot push it back anymore […] you're so far [along that] the only way is to continue" (Foreign manager of foreign bank: #46, 2 November 2006). The 'marketisation' of the finance sector was seen as part of an irreversible trend towards the loosening of the government's grip on economy and society. This view was also echoed by a CBRC official who agreed that "After taking the first step, you cannot go back, right? […] That's the way it is, you cannot turn back. You cannot go back" (#25, 16 April 2006; translated from Mandarin). Such sentiments could explain why foreign financial institutions in Shanghai were willing to put up with the slow pace of change and limited business opportunities thus far because they had confidence in the long term liberalisation of financial services and were also keenly aware of the importance of stability in a large emerging economy like China.

6.4 REGULATORY CONFUSION? SOME ISSUES AND PROBLEMS WITH REGULATORY STRUCTURES AND PROCECURES

The Chinese style of 'marketisation' and regulatory reforms had drawn criticism from international commentators as well as industry participants. Although they acknowledged the appropriateness of the pace and structure of reforms with regards to the China context, and expressed confidence in the knowledge and abilities of the regulators to varying extents, both local and foreign financial institutions in Shanghai had their complaints about the 'style' of such re-regulation on their business activities and environment. As discussed in the above section, the Chinese regulators did not implement bold reforms but would test the market in small ways before issuing new regulations. The new regulation would generally be very vague to allow for further adjustments and refinement after gathering information and advice from financial institutions, professional bodies and other organisation (such as the foreign chambers of commerce and banking groups). These steps were described by a foreign manager of a foreign bank in Shanghai:

> When they issue a new law, in all processes concerning banking, they will let a rumour go in the market. They will let a rumour go and they will see how the market reacts, see whether it will be a complete catastrophe or will they revolt or whatever. And if they don't hear that much they will issue a law and the law will be *very* vague. It will be general blah-blah-blah, and then all these questions will come up and then they will issue an implementation after that to explain what they meant. (#36, 18 October 2006; original emphasis)

By developing and implementing new regulations in the above manner, rumours, vague rules, amendments and clarifications were constantly circulating in the market, and changes were always being implemented in small but frequent steps. With new policies being announced almost every month, the business and regulatory environments were constantly shifting and market participants often found it difficult to keep on top of these changes. This problem was compounded by the lack of transparency in regulatory procedures and stilted information dissemination. Even as regulatory frameworks, such as those governing the public listing process on the SSE and the launch of new derivatives products, were being implemented, the precise criteria to be met and application process to obtain regulatory approval were not always made explicit and public. This led to one of the most frequently cited criticisms amongst respondents, that of disorientation and confusion due to the lack of transparency and clear structures. A Chinese interviewee likened the regulatory environment to a pot of soup in which different ingredients were just thrown into a pot and mixed together in an ad hoc manner:

> For the market to work, regulation is very important, the structure is very important. Everyone must follow the same rule to work, that will make things much better. Otherwise it all gets very messy and this market just cannot get off the ground. Even

> if you have good companies, they can't do anything. In the end you just get the feeling of everything being *yi guo tang* (一锅汤; one pot of soup, meaning all mixed together) and you can't differentiate, can't make head or tail of things. (Local consultant for Chinese financial institution: #24, 15 April 2006; translated from Mandarin).

The application process for a public listing on the SSE was highlighted by a number of interviewees as a prime example of the rules being fuzzy and the lack of transparency in dealings with regulators. The procedure of listing, documents required and other related information were publicly available on the SSE website[11] (see Table 6.1) but even if one had ticked all the boxes and fulfilled the requirements following the checklist, there was still no guarantee of success due to other undisclosed criteria. For example, the first step in the listing procedure was to obtain CSRC approval, after which the company could then submit the various required documents. But how one would go about obtaining CSRC approval was not specified[12] and that was clearly a hurdle that could stop potential IPOs in their tracks from the onset. A Chinese investment analyst (#48, 3 November 2006) spoke of the use of personal leverage and 'guanxi' to push through such applications and that the undisclosed criteria were usually understood by potential companies (through rumours, informal chats with others in the industry) such that they would know whether they would be successful even before they submitted an application:

> Analyst: It's about 70-80 percent [of the requirements that are disclosed]. Under the circumstances, you cannot say for sure [whether your application will be successful]. For large state-owned enterprises or private companies, it is largely done through *guanxi* or maybe the brokers have some special access and they can

[11] http://www.sse.com.cn/sseportal/en_us/ps/lc/lst_req.shtml

[12] One could contact the Shanghai CSRC office for formal enquiries but there is no indication of what exactly it takes to obtain the go-ahead to proceed with documents submission and the rest of the listing procedure.

help you do things. But purely market-style operation is not possible, it doesn't happen. […] There are two systems: one says that you just have to fulfil certain requirements, like Hong Kong and USA, [if you fulfil the criteria] they have no reason to disallow your IPO; the other system is whereby you have to fulfil certain criteria as well as be approved.

KL: So this process of approval is rather fuzzy…? You cannot be 100 percent certain what it is they are looking for?

Analyst: That's right. Although you also know in your heart what they look for! Like what I've said… they will not write it down but you also know yourself and you don't even have to try, there is no need to even try [*laughs*]. (Translated from Mandarin)

Table 6.1 Listing procedure for the Shanghai Stock Exchange and documents required

Listing Procedure

1. CSRC approval. The applications of companies for the listing of their shares are subject to the approval of the China Securities Regulatory Commission approval;
2. Submission of listing application documents. Only after gaining the approval of the CSRC, can the company make an application for listing to the SSE and submit the listing application documents required by the SSE.
3. Share custody. Before a company's shares can be listed and trading commenced, it must entrust its full register of shareholders to the Shanghai Branch of the China Securities Registration and Clearing Co., Ltd.
4. Determination of the date of listing;
5. Publish a listing notice. Following examination and verification of the SSE, the company must publish a listing notice 5 days prior to the listing and trading of its shares.
6. Listing and trading.

List of Documents

According to the provisions of the "Securities Law of the People's Republic of China", limited liability companies must submit the following documents when making an application for the listing of their shares to the Securities Supervisory Institutions of the State Council:

1. Listing Announcement;
2. General meeting of shareholders resolution to apply for listing;
3. Company Ordinance;
4. Company business license;
5. Financial accounting materials for the last three years or since the founding of the company following verification by legal verification organization;
6. Legal opinions in writing and a letter of recommendation from a securities company;
7. The most recent share prospectus.

In addition, companies must submit the following related documents according to the provisions of the Exchange's rules for the listing of shares:

1. Listing Application;
2. Documents from the CSRC approving its share issue and issue and listing declarations approved by the CSRC;
3. Newly added financial materials as required following issue of the share;
4. Photocopy of its business license;
5. Personal particulars of the secretary of the board of directors and contact details of the secretary of the board of directors, securities representative and legal representative;

6.	Report regarding the shareholdings of the company directors, supervisors and senior management of the company;
7.	Circular determining the listing abbreviation of the company's stock;
8.	Documentation showing the full custody of the company's stock;
9.	A written pledge of the company's largest shareholder pledging not to sell or repurchase its shareholding for a period of twelve months.
10.	Other documents required by the Exchange.

(Source: Shanghai Stock Exchange Website, http://www.sse.com.cn/sseportal/en_us/ps/lc/lst_req.shtml)

This lack of transparency in regulatory procedures also extended to application for various branch and business licenses which was applicable to all foreign financial institutions when they set up or expanded their operation in Shanghai and other parts of China. A foreign manager of a foreign bank contrasted her experience with the regulatory environment in developed economies in Europe where

> "you just go to the internet and dadada… you know in UK or France, you know whatever, how to get your information and then, ok, maybe you go to a law firm. But here things are just not that clear. They are spread out, you need your advisors, a lot of things are based on trust, on connections, on… things are not always clearly spelled out. Not like one, two, three, four, five… and then you get the license. Nuh-uh. That's not how it works and that makes it fuzzy for many people" (foreign manager of foreign bank: #46, 2 November 2006).

This 'fuzziness' was particularly problematic for foreign banks as they try to negotiate the local regulatory environment in developing their financial operations in China. The types of activities permitted for a representative office was one such example. In legal terms, a representative office may only engage in non-profit making activities, such as conducting research; providing data and promotional materials to potential clients and partners; conducting research and surveying for its parent company in the local market; liaising with local and foreign contacts in China on behalf of its parent company; acting as a coordinator for the parent company's activities in China; making travel arrangements for parent company representatives and potential Chinese clients; and other non-profit making business activities.[13] The line that must not be crossed was that of *business-taking and profit making* activities, but certain activities, such as operating as a post-box for local customers, forwarding documents and letters of applications to the bank's head offices and branches in Hong Kong, *could* be interpreted as profit-making activities or being outside of its research and consultancy mandate depending on which legal counsel and regulators one consulted. Therefore even approved licenses came with significant grey areas that could be frustrating for foreign financial institutions used to having clear rules of operation. Knowledge about the scope of activities for a representative office was therefore acquired slowly through more experiential and sociological means of personal interaction and information exchange with other banks in Shanghai, meetings with CBRC officials and becoming increasingly in touch with the 'spirit' of the rules over time. This notion of understanding a loosely-defined and illusive 'spirit' of the legal meanings was highlighted by a foreign representative of a foreign bank office in Shanghai and whom I interviewed from the beginning of its operations and then again 10 months later. He described the process through which he learned about the activities a representative office should and should not engage in:

> Foreign banks represent less than two percent […] of the total banking community in China. To have a banking presence here is a long term strategic view for any foreign bank and the regulator, the CBRC would say, you've got to do your time, you've got to sit there and you've got to… see what you want to do. Don't jump in and have the activities and I think that's the *spirit* of it. So, therefore, they would say you can consider that, you can do that, you can *research* the marketplace, *build good relationships* with regulators and government for your future. It's very much a long term view, and I think that's probably the spirit of it. […] A lot of it is understanding what people can do in the other banks, CBRC, talking to people, understanding what

[13] www.export.gov/china/exporting_to_china/RepOffice.pdf

> sort of activities are permissible and what would be frowned upon. […] You mustn't do any transactions. You mustn't be seen to be actually transacting and certainly the CBRC came to do our field audit and they inspected our computer system. They opened them up to see whether we have any programmes or any ability to do transactions, which we don't do. We simply facilitate. We market the name and we help, creating business activities for our overseas branches, which is *our interpretation* of what we can do, and I think that's acceptable. And I think that sits within the grey area but it's on the right side of grey. (Foreign chief representative of foreign bank: #29, 12 October 2006; emphasis added)

Apart from the problem of administration transparency, Chinese rules were normally expressed in generalities and did not usually provide sufficient details for practical resolution. Implementation and enforcement were often subject to the interpretation and articulation of local administrative authorities and could vary from case to case. If formally published policy information could not be interpreted 'correctly' by information users, tacit information became more important for conducting business in China in order to stay on "the right side of grey". The regulators used this 'fuzziness' and grey areas as extra room for policy manoeuvre, to refine aspects of the framework after monitoring market reaction and the behaviour and actions of participants. Some of my Chinese respondents explained that Chinese laws were deliberately vague because of the ways in which Chinese regulatory bodies were structured across spatial scales. Regulators at the national, provincial and local levels were faced with different problems and demands and the very vagueness of the laws allowed them to be adapted according to local contexts and requirements. As a local analyst for a joint-venture fund management company explained:

> If you issue a regulation or a new law, maybe this new law is suitable for places like Shanghai, Guangzhou and Beijing but the problem is when this law reaches Wuhan,

> Sichuan, you may find that this regulation does not quite work because the method of governance is looser and there are more loopholes. If you issue a regulation that is very tight, you may find that it controls risk in those places very well but inhibits business in other places. (#48, 3 November 2006).

Banking regulations in China can be divided into 'published laws' and 'regulations'; Beijing publishes the law, but the regulations are interpreted and implemented by local entities. "Chinese laws are [thus] inspirational statements" (Foreign Chamber of Commerce in Shanghai: #2, 17 August 2005) that are open to interpretation by local bureaucrats. Although this was a particular strategy used by the Chinese state and regulators to manage the political economy that had developed out of specific contexts, it created uncertainty, inhibited business decisions and raised transaction costs particularly for foreign investors who arguably had greater difficulty accessing such non-policy information compared to their local counterparts (Yusuf and Wu, 2002: 1222). Another example was the legally binding nature of contracts. What was deemed a basic part of the legal framework was not always understood in the same way by foreign and Chinese partners, as a legacy of allowing for multiple interpretations of one law. A foreign interviewee had come to see the Chinese laws as more like guidelines. Using the spatial metaphor of a journey, he explained that:

> The contract is more a… description… of the path you want to walk together. […] The problem with the path is it goes up and down the hill, and then after the hill you don't see if there is a fork in the road. For the Chinese person, if there is a fork in the road, the contract is no longer valid. We have this style of, 'Hey, here is the contract, this is the deal!' 'Yes, so… that was the deal, that moment in time when we walked the path. And we walked for two years very happily together, and now we fork. Now we negotiate how to part.' The one thing that the lawyer keeps on saying is contracts are a different concept. It's… it's just a start of a journey. If the journey goes

> different ways, then you part. It's not like in Europe. (Foreign director of foreign company: #6, 21 February 2006)

Therefore, many respondents pointed out it is a misconception that there are insufficient laws in China to govern property rights and rules of exchange; the real problem lies with their *execution and enforcement*. Their characteristic vagueness allows for more specific treatment and interpretations by local authorities according to local contexts, but the lack of clarity proved highly confusing and frustrating for foreign investors who might not understand their rationale and mode of operation. Through consultations, working groups, position papers and training programmes, foreign financial institutions and regulatory bodies had contributed to greater clarity of new and existing regulations with some success as seen from the on-going drafting and re-drafting of laws and policies to govern new and existing products and markets. However, the Chinese regulators clearly value the ability to control market activities through an opaque system that allowed them the power and flexibility to quicken, interrupt or slow the process of 'marketisation'. It also allows for adaptation to local needs by local branches in the context of a huge country with widely varied regional and local political economies. As such, the 'fuzzy' characteristic of Chinese laws and regulations is likely to continue while particular areas within are refined in response to changing local, national and international considerations.

Apart from the lack of administrative transparency and the 'fuzziness' of the laws and regulations, regulatory confusion also extended to having what was seen as too many regulatory bodies. When the CBRC, CSRC and CIRC were set up as separate institutions from the PBOC, the move was seen as a sign of China's commitment to strengthening regulatory frameworks, introducing international standards and improving supervision of the respective financial sectors (Lyons, 2005). However, having three individual regulatory bodies instead of one (like the FSA, for example) created confusion for financial institutions whose products and services sometimes span across banking, securities and insurance. The QFII and QDII schemes, for example, were banking as well as securities products. Financial futures are regulated by the CSRC but they are mostly done through banks. These overlapping jurisdiction means industry participants could get caught between two regulators and figuring out which set of rules and procedures to follow takes time and raises transaction costs. Many banks have to deal with up to six regulatory bodies (CBRC, CSRC, CIRC, PBOC, SAFE and the local tax office) on a regular basis and significant amounts of time and effort has to be invested into maintaining the good relationships essential to business in China. A Chinese respondent from a local credit rating agency described the regulatory confusion that they faced when they had to figure out which regulator to liaise with depending on the specific project:

> They always talk about the regulatory body – [but] who is actually the regulator? Let's say we want to do some corporate rating exercise in Shanghai; the PBOC in Shanghai will regulate us. If we want to do another kind of rating, maybe it could be CSRC. If we want to do some rating for credit guarantee organisations or insurance companies, then we get regulated by the CIRC. Then… so it's very messy and we can't even make sense of it ourselves! Now we are all asking, so who is regulating us? If you are talking about this area, maybe they are the regulators; if you are talking about another area, maybe someone else is the regulator (#24, 15 April 2006).

Shuttling between regulators might be inconvenient, but being given contradictory instructions and interpretations of rules was even more problematic. As mentioned earlier, new laws and regulations are announced in Beijing with the implementation carried out by local regulatory offices. This allows for a wide interpretation and implementation of rules which could result in the regulators contradicting one another depending on where they are and who they talk to:

> All of them, they have made regulations that affect our business and many times [they] contradict. […] We call SAFE in Shanghai; we call SAFE in Beijing. You can get different answers on the same policy. So even clarification doesn't help, this cannot exist. The only reason it is the way it is right now is because regulations change so quickly that even the regulators cannot keep up with itself [*sic*]. […] it needs to be the point where if you call the regulators they can explain their own regulation! [chuckles] And if you call two regulators in different cities you [need to be able to] get the same answer. That's the minimum requirement that is not fulfilled at the moment. (Foreign manager of foreign bank: #43, 27 October 2006)

Because of the constant amendments and re-drafting of existing regulations, and the announcement of new ones, some interviewees even expressed doubts that the regulation were even read by the local offices. This tended to be less of a problem in larger and more 'international' and business-oriented cities like Shanghai, Tianjin or Shenzhen, but in smaller centres some interviewees said they had to convince the local regulators that particular regulations even existed or they had to negotiate past the 'strange interpretations' of local officials:

> Shanghai SAFE, totally fine, but the further you go inland or away from the main centres, the more strict they interpret, or the [more strangely] they interpret the rules. So you have answers like, 'Oh, the contract should have been written within 10 days after it's signed, we can't accept it', or… all kinds of weird things, 'Oh, it should be written in Chinese and… it should be under laws of China', and we say, 'You can actually use the law under Hong Kong'. And they [would] say, 'We obviously don't understand the law there so we want you to write in Chinese law'. And all these 'fun' requests. So what I do not like is the fact that you are left to all these various interpretations. (Foreign manager of foreign bank: #36, 18 October 2006)

These problems had been highlighted to the regulators and they had demonstrated some efforts at better communication across the regulatory bodies. A MOU was signed between the CBRC, CSRC and CIRC "aimed at clarifying respective responsibilities in financial supervision and regulation, coordinating the actions of three commissions to avoid absence and overlaps of supervision and regulation, enhancing efficiency and encouraging financial innovation so as to ensure that all financial institutions and their financial businesses are under continuous and effective supervision" (CBRC website)[14]. Ensuring better communication and cooperation across regulatory bodies would clearly be an on-going process and was an encouraging sign. However, the existence of separate regulators for banking, securities and insurance is likely to continue as long as the overall governance structure of China's finance sector remains divided according to industry.

Financial institutions in China are governed based on the principles of separate business sectors (分业; *fenye*), i.e. they cannot engaged in mixed-business (混业; *hunye*). Unlike financial institutions in the UK, USA or Singapore, those in China are much more limited in the types of financial activities they are permitted to conduct. For example, while a bank in New York might offer bank deposits, asset management, financial leasing, consultancy and derivative products – likened to "financial [products] supermarkets" (local analyst from Chinese securities company: #22, 12 April 2006; translated from Mandarin) – these would not allowed to be offered by a singular bank or financial institution in China and have to be conducted by separate financial institutions. The rationale for this is so that if one aspect of the business should fail, there would be limited economic and social impact (and

[14] http://www.cbrc.gov.cn/english/home/jsp/docView.jsp?docID=718

political consequences) compared to the collapse of a large financial conglomerate. The importance of limiting risk and contagion is clearly paramount:

> Currently, the Chinese government feels that separate-sectors is… regulatory standards cannot catch up. A mixed-sectors approach brings too much risk. Too much risk, without the means to control them. This is why it is still separate-sectors. In terms of securities, there is the CSRC to regulate them. Insurance has the CIRC, banking has CBRC, so it's all separate. They feel that it is easier to control risk by regulating them separately. […] But from separate to mixed sectors approach, how do we make this change? The regulators are also thinking about this now. This is the trend. (Local analyst from Chinese securities company: #22, 12 April 2006; translated from Mandarin)

The absence of big financial conglomerates that are able to offer a range of products and services across business sectors is seen as holding back the development of an international financial centre in Shanghai. The separate-sectors structure places a limit to growth and innovation on financial institutions in Shanghai, which would be detrimental to its future growth and development as financial institutions if financial institutions such as banks and securities companies could only conduct designated businesses. Securities companies in China, for example, are still primarily dependent on commission from trading business on the secondary markets. This is in contrast to other countries where the income of similar financial institutions also comes from financing, consultancy, intermediary business and other information sourcing business. This makes them less reliant on the securities markets and trading volumes compared to the Chinese counterparts and they are better able to spread their business risks.

Respondents who had been in Shanghai over the past decade indicated that they had seen a clear improvement in regulatory expertise over time and the on-going reforms and negotiations were testament to their efforts. However, the regulators still tended to err on the side of caution as a guiding principle which tended to stifle business activities and financial innovation.

> [B]anks have the possibility of applying for a derivatives license but still there is still a very small range of products allowed to do. Usually I always felt that the regulators, if there is a product they don't understand, they won't allow it. They understand more and more so they allow more and more. But still there is a lot to do. […]of course you have to be careful, but you can also be too careful sometimes. (Foreign representative of foreign bank: #45, 1 November 2006)

This (some would say overly) cautious attitude could result in very long approval process while the regulators deliberated over the appropriateness of new products for the Chinese market. Depending on the type of products, it could take up to three months to obtain approval. For a fast-moving business in commercial banking, this limits quick market turnaround and when "you have to wait three months, and then you do the sales for two weeks and then you have to start doing a new product, […] this is very *ma fan* (麻烦; troublesome), very difficult … very restrictive" (*ibid.*) This conservative attitude of regulators can be described as a 'No U-Turn Syndrome'[15], whereby drivers in one country are not allowed to make a U-turn *unless* a sign specifically allows them to do so. This is in contrast to other countries where drivers may make U-turns freely *so long as* the 'No U-turn' sign is not present. This mirrors the experience that foreign banks have with the Chinese regulators. For example, from the perspective of the local regulators, industry actors

[15] 'No U-Turn Syndrome' is a term coined by a Singapore entrepreneur, Wong Hoo Sim, to describe the social behaviour of Singaporeans as having a mindset of compliance to higher authorities before proceeding with any action. In his book *Chaotic Thoughts from the Old Millennium* (1999), he uses a comparison of traffic rules in Singapore to those found overseas, to describe the phenomenon: In Singapore, drivers are not allowed to make a U-turn unless a sign specifically allows them to do so, while in some other countries drivers may make U-turns freely so long as the 'No U-turn' sign is not present. This analogy is used to explain the red tape he has encountered with hard-nosed bureaucrats, which in turn stifles the very creativity that the Singaporean government has been trying to promote in the recent years.

could only conduct particular transactions or venture into another business area if permission has been granted; if permission is not granted they cannot do so. For foreign banks, their experience overseas has been the case of if the regulators did not specify that they cannot do a particular business, it means they can. This problem was highlighted by a number of local and foreign interviewees as another instance of regulatory confusion (due to different expectations and regulatory experience) as well as a limit to financial innovation and business activities:

> In foreign countries, if it is not mentioned, you can do it. If the law did not specify [that it is not allowed], you can do it. But here in China, if we say that you can do it, then you can do it. If it is not specified, you cannot do it. Isn't that confusing? Ok, in other countries, […] if you did not say that this is not allowed, I can do it and the courts will not say that I am guilty, that I have broken the law. But here in China this is not the case. What you are doing, the law did not say that you can do this. If you do it, there will be problems. (Local manager of Chinese financial institution: interview no. 9, 27 February 2006; translated from Mandarin)

This is a legacy of ex-ante planning (see Sayer, 1995) that runs through the CCP planning system and the above experience marks a clear continuity with that system in spite of stated commitments to 'market-style' reforms.

6.5 CHINA'S WTO COMMITMENTS: OPENING ONE DOOR AND CLOSING OTHERS?

In December 2001, China joined the WTO as its 143rd member. In exchange for WTO membership, China made a series of concessions and commitments to further open up its domestic industries to foreign imports and investment. The WTO agreement was expected to fundamentally transform the existing socialist market system in China into a 'real' market system, and to establish Chinese global trade and production systems that comply with the global ‘rules of the game’ (Zhao et al., 2002). Accession to the WTO is seen as China’s public recognition of marketisation and internationalisation as the primary sources of its rapid growth since the 1980s (Lughod, 1988).

As part of China’s WTO commitments, it had to open up its banking sector to foreign banks with regards to 1) the types of business they can engage with (foreign or local currency business), 2) the types of customers (corporate or retail) and 3) by geography (cities and regions where such business is permitted). For foreign currency business, foreign financial institutions should be permitted to provide services in China without restriction as to clients or geographical areas upon accession. Geographical restrictions on foreign banks on Chinese currency businesses were to be phased out by opening up four cities (Shanghai, Shenzhen, Tianjin, and Dalian) upon accession and a few more cities every subsequent year. All geographical restrictions were to be removed within the fifth year after accession. For local currency business, foreign financial institutions should be permitted to provide services to Chinese enterprises within two years after accession (before the end of 2003). Within five years after accession (before the end of 2006), foreign financial institutions should be permitted to provide services to all Chinese clients. Within five years after accession (before end of 2006), any existing non-prudential measures restricting ownership, operation, and juridical form of foreign financial institutions, including on internal branching and licenses, should be eliminated. In other words, by the end of 2006, foreign banks in China were to receive ‘national treatment’, i.e. be treated the same as domestic Chinese banks, in banking regulation (*People’s Daily*, 12 June 2001; World Trade Organisation, 2001). The timetable for lifting these restrictions is shown in Tables 6.2 and 6.3.

Table 6.2 WTO phases by business and customer groups

Business	**Customer**	
Corporate Banking	***Foreign corporations***	***Chinese Corporations***
Deposits and lending RMB	Immediate	WTO + 2 years
Deposits and lending FOREX	Immediate	Immediate
Settlements and remittances	Immediate	WTO + 2 years
Foreign exchange transactions	Immediate	Immediate
Foreign currency guarantees	Immediate	WTO + 2 years
Interbank – deposits and lending	Immediate	
Interbank – discounting	Immediate	
Retail Banking	***Foreign citizens***	***Chinese citizens***
Deposits and lending RMB	Immediate	WTO + 5 years
Deposits and lending foreign currency	Immediate	Immediate
(Sources: People Daily, 12 June 2001; Low, 2003: 1-2)		

Table6.3 WTO phases by geography

Foreign Currency	
Time	***Region***
Immediate	No geographic restrictions
RMB	
Time	***Region***
Immediate	Shanghai, Shenzhen, Tianjin, Dalian
WTO + 1	Guangzhou, Qingdao, Nanjing, Wuhan
WTO + 2	Jinan, Fuzhou, Chengdu, Chongqing
WTO + 3	Kunming, Beijing, Xiamen, Zhuhai
WTO + 4	Shantou, Ningbo, Shenyang, Xian
WTO + 5	No geographic restrictions
(Sources: People Daily, 12 June 2001; Low, 2003: 3)	

The opening up process proceeded according to schedule. By the end of October 2005, there were 138 foreign banks approved for conducting yuan-related businesses in China. Their assets amounted to US$84.5 billion, equivalent to two percent of total assets in China's domestic banking sector. Their share of China's foreign exchange loan market rose to more than 20 percent. In Shanghai, foreign banks achieved a share of total banking assets as high as 12.4 percent and a share of the foreign exchange loan market of 54.5 percent (CBRC, 2005). Almost all interviewees agreed that China's WTO commitments have helped quicken the pace and strengthened the direction of reforms. External pressures and international expectations for China to meet the deadlines and fulfil its commitments had played a significant role in regulatory reforms and the 'marketisation' process. However, this should not be seen simply as a decline of state power vis-à-vis the demands of global capital, supranational organisations and pressure from foreign states. Even within the terms of WTO ascensions, there was plenty of scope for the Chinese state and regulatory bodies to act according to their interests and agendas, even as they had to negotiate with the agendas and considerations of other interest groups. An official from the CBRC admitted that it was a delicate task having to juggle WTO commitments with local consideration and national politics and agendas:

> Regulations have to keep up with that, develop in tandem. If we go deeper into this… With so many foreigners coming in here, what do the local enterprises do? What if they… get eaten up? They [foreign firms] can, through M&A [merger and acquisition], swallow up all the local enterprises, right? So for China's economy… it definitely has to consider the locals. But you still have to fulfil your WTO commitment, your promise, so this will require a lot of skill… it's a rather… complex relationship. (#25, 16 April 2006; translated from Mandarin)

Another official from the SMG pointed out rather candidly that the WTO commitments did not come with very specific stipulations so there was room to manoeuvre within those areas, so long as the broad principles were adhered to. "Yes, there is that commitment, but it could work out differently *on the ground*. The WTO regulations are not very specific. So they [the regulators] can work through other ways and means to impose some restrictions" (#28, 20 April 2006; translated from Mandarin and emphasis added). A few other interviewees whom I spoke to in early- to mid-2006 also expressed their scepticism and the expectation that non-tariff barriers would be imposed to allow the Chinese regulators to maintain control over the pace of reforms and extent of foreign competition while still honouring their WTO commitments. When I raised the question of WTO during interviews, a number of respondents would interrupt saying "in theory… in theory", stressing the difference between theory and practice with regards to WTO compliance and expressing their doubts that a truly level-playing field would be instituted.

When I returned to Shanghai again in late-2006, close to the final WTO deadline of fully opening up its banking sector to foreign banks regardless of business activities, customers and geographical regions, those doubts were revealed to be justified with the announcement of a new law that effectively restricted the expansion and activities of foreign banks in China. The lifting of restrictions had been largely in keeping with WTO commitments but the reality was that high capitalisation requirements and other conditions such as onerous reporting requirements (see Chapter 7) often made it commercially unviable or difficult for foreign banks to expand their range of businesses and customers. These conditions operated on a tier basis: each tier had a minimum capitalisation requirement – the higher the tier, the broader the permitted scope of business and access to customers but also the higher the capitalisation requirement. An example of this was the new rules regarding foreign banks wanting to engage in RMB retail banking. Since 2001, foreign banks had been able to conduct foreign currency business with both corporate and retail customers and they had been able to conduct RMB business with corporate clients since 2003. But the 'big fish' that foreign banks had been angling for was RMB retail business with what was expected to be a large and growing Chinese middle-class population. A draft amendment on *Regulations on Administration of Foreign Banks* was circulated by the CBRC amongst the foreign banks in September 2006 for comments, as per usual practice, relating to the opening up of RMB retail banking to foreign banks. Despite the "moans and disagreements" (foreign representative of foreign bank: #29, 12 October 2006) from the international banking community, the amendment was subsequently passed with little changes to the draft just before the WTO deadline of December 2006.

The amended regulation stated that foreign banks that had prior approval to conduct RMB corporate business with Chinese enterprises would not be automatically permitted to conduct RMB retail business; instead, they would have to reapply and fulfil specific conditions. Apart from having to meet existing condition of "profit-making for two consecutive years during the first three years since its opening" (while having its business activities restricted) (State Council, 2006), the banks would also be required to commit unprecedented amounts of money as registered capital. The operating capital for foreign bank branches to conduct foreign currency business (with both corporate and retail clients) would stay the same at RMB 200 million. The requirement for foreign currency and RMB business with corporate customers would also remain at RMB 300 million. However, banks that wanted to engage in RMB retail banking would have to acquire 'legal person' status, which involved being locally incorporated (in China) and a registered capital of RMB 1 billion yuan. If the foreign banks were not locally incorporated, they would only be allowed to accept deposits of over RMB 1 million yuan from Chinese individual residents and would not be able to issue bank cards. This move had been criticised as China giving with one hand and taking with the other (Areddy, 2006; Shao and Lou, 2006). Some described the capitalisation requirements as an example of China perverting its WTO commitments as the bar for foreign banks had been set much higher than many have anticipated (Low, 2003).

Many interviewees viewed the new amendment as a means of controlling the activities of foreign banks in China and maintaining a grip on the pace and nature of 'competition' in the banking sector. There was a sense that the Chinese government might have 'given away' too much in opening up the banking markets to foreign competition over the past five years under WTO agreements and that the local banks were in danger of being left behind. Although there was never much doubt that the Chinese government would adhere to their WTO commitments, my interviewees were also not entirely surprised that "they [the government] will find all kinds of ways to make life very difficult for foreign banks because they feel that right now foreign banks are getting too aggressive and too effective in competing with local banks. That's why you have new regulation on incorporation, foreign banks can only effectively compete with local banks if you incorporate locally. That is a very painful, expensive process. It has a lot of disadvantages for foreign banks. So… it is not easy, not many banks will go that route" (foreign head of department of foreign bank: #42, 27 October 2006). By imposing more stringent rules and raising the barrier to entry on foreign banks, a 'level' playing field was offered to foreign participants (as stipulated under its 'national treatment' WTO agreement) but the conditions attached to that imposed financial costs which not every bank that entered China with the goal of RMB retail banking could afford to meet:

> You might say, well, fair enough, to be on a level playing field with the Chinese banks, they incorporated here in China then you should incorporate here in China, that's fair enough. But then of course it implies a massive financial commitment because in order to incorporate a bank, […] So it's… It's a way of… not penalising but it's a *cost* involved […] It's just a control mechanism. So what I'm saying is that whatever you do and however they do it, it's a *sort of* level playing field but it's a conditional one. (Foreign manager of foreign bank: #37, 19 October 2006; original emphasis)

This suspicion expressed by the foreign finance community, that the Chinese government was seen as having conceded too much to foreign investors, was confirmed by other Chinese respondents. Some local interviewees expressed their concerns about the abilities of the local Chinese banks to raise themselves to international standards of management, risk control, compliance, reporting and many other areas that required a period of time for new concepts and methods to be learned and instituted, and that the five-year deadline under WTO was too short. Other interviewees were more candid and blunt in their assessment and viewed foreign players as treating the Chinese market like a mine, digging up what was valuable and depriving the locals of opportunities and wealth:

> Take for example, the securities sector, [which] is currently closed to foreign investors. I am in complete agreement with that, personally, that is. From the company's point of view, of course opening up is good for business but I have found that when they cooperate with us, at this stage, it is mostly a case of taking away, it is like mining, I can tell you! […] They have brought some things, such as management, personnel, but their ultimate goal is to buy up companies. They want to take hold of a certain company, to enter the market. They don't really have much contribution, not much. This is like mining, do you understand my meaning? Like a

> coal mine, if you dig down, you get coal. They have come here to dig into the mainland mine. (Local analyst of Chinese securities company: #34, 18 October 2006; translated from Mandarin)

The concept of 'competition' was thus viewed differently amongst local and foreign respondents. The foreigners saw such non-tariff barriers as giving unfair advantages to the local financial institutions while the Chinese saw it as unfair if foreign investors were given free rein in business activities and to enter all segments of the financial industry before local financial institutions were fully prepared and mature:

> Why don't we build up our own strengths and our own people? […] Our securities companies have not adapted to the international market, they have not done any international business or transactions. […] When they have not been properly trained […i]f you let the foreign institutions in now, isn't that courting your own death? It will be very easy for them to pull your good employees over, and it will be even easier for them to pull your clients over. […] *Under these conditions, how can you compete?* So I think it is right that the doors are closed to foreign investors at this point. […] there needs to be a process for *healing and recovery* before allowing the foreign investors in. It is just a matter of time. (*ibid.*; emphasis added)

Therefore, although China's WTO accession was taken as a indication of its commitment to further liberalisation and reforms and adherence to international standards and agreements, the actual implementation on the ground revealed the complex balance of interests between the Chinese government, regulatory bodies, foreign and local financial institutions and negotiating their different concepts of what constitutes 'fair competition'.

6.6 GOVERNANCE AND CONTROL: THE USE OF WRITTEN RULES AND SOCIOLOGICAL POWER

As discussed above, specific regulatory measures were used to control the business activities of foreign banks in China so as to control the pace of 'marketisation' and soften the impact of foreign 'competition' on local financial institutions. In this section, I present accounts of how such control is exercised through published rules as well as through the use of 'sociological power' to influence the behaviour and 'cooperation' of foreign financial institutions. While the Chinese government might have been accused of subverting the terms of its WTO commitment to fully open up the banking sector by the end of 2006 through new conditions, foreign banks in Shanghai were also actively seeking loopholes to get around the various regulatory restrictions placed on their business activities. It was a constant game of 'catch me if you can' as foreign banks employed creative means of routing money from abroad and obtaining the necessary documents from alternative sources to get around existing rules even as the Chinese regulators were catching on to the trends and issuing amendments to plug loopholes and foreign banks seeking other avenues again. The following examples illustrate how specific rules and regulatory requirements were used to restrict the business activities of foreign banks. However, the relationship was always contested and unstable as the latter sought to circumvent foreign and local currency restrictions in order to expand their business scope which necessitates further regulatory response.

Foreign and domestic banks were on an uneven playing field especially with regards to building an RMB deposit base. Factors that handicap foreign banks include the high level of capitalisation (mentioned in section 6.5) which locked up significant sums of money as registered capital; a one branch per year rule which inhibited their ability to expand customer bases; and customer types being restricted depending on the WTO timetable and licensing. In terms of RMB business, most foreign banks were limited to corporate customers and foreign retail clients who had limited RMB deposits. This is in contrast to the local Chinese banks that held huge amounts of RMB deposits from their large client base. The significance of being handicapped in building an RMB deposit base was that foreign banks were effectively forced to rely on interbank borrowing to fund their own RMB business. The margins were thus lowered by the narrow difference between interbank borrowing and the regulated interest earnings on customer loans.[16] Foreign banks were thus at a serious commercial disadvantage compared to their domestic counterparts. Due to their reliance on interbank loans, any restriction on accessing this source of funding would strain their capacity to do RMB business. Such a restriction was passed in 2006, which applied to both foreign and local banks, stating that a bank's total RMB interbank borrowings could not exceed 40 percent of its total RMB liabilities. Theoretically, the purpose of the regulation was to put overseas banks in line with domestic banks that were already subject to the 40 percent rule. However, the practical effect of the regulation had a disproportionately negative impact on foreign banks because they were restricted in expanding their RMB deposit base:

> That's the 'level playing field', because that's how the Chinese banks fund themselves, through deposits. But when you extend that 'level playing field' to the foreign banks, without deposits, things get screwed entirely! Because they don't have deposits, it's like a reversal playing field. It's a wonderful way of controlling the foreign banks. (Foreign president of foreign bank: #32, 13 October 2006)

[16] Interest rates in China are fixed and regulated. Banks therefore have very limited scope for offering more 'competitive' rates to attract new customers.

Foreign banks in China were limited in terms of the types and amount of business they could do due to licensing restrictions (having to apply for separate license for foreign currency or RMB business). They also had to contend with specific quotas on the amount of lending business they can conduct. All foreign banks in China were subject to a foreign currency lending quota which they could not exceed for that year. Although the foreign banks only had a small presence in China and restricted scope for RMB business, they could theoretically mobilise a significant amount of funds from their head offices or bank branches elsewhere in the region (such as Hong Kong or Singapore). However, regulations controlling how much banks could borrow from abroad (which includes interbank loans from abroad) effectively restricted their lending business and was a way of slowing down the foreign banks in terms of their business expansion in China. The Beijing regulators gave the local regulators (to the local SAFE office for short-term lending and the local CBRC for medium-term loans) a quota every year to be allocated amongst the banks in Shanghai. The local regulators would examine the balance sheets of the banks, inspect the banks' applications based on their expected level of business, assess their needs and grant them a figure for the amount of foreign currency lending they were allowed to conduct for that year. The banks could apply for an increase to that limit but only on a case-by-case basis. Having the government specify the amount of business that could be done was certainly a strange concept for most foreign banks and did not make commercial sense. From the Chinese government and regulators' point of view, however, it was an effective tool to control the pace of foreign competition. A foreign manager of a foreign bank expressed the frustration of having to turn down business opportunities due to quota restrictions:

> So if we get a short terms deal, [person X] comes to me and say 'oh we've got a brilliant deal, we'll like you to fund us for $10 million for 3 months', and he did it

> today, I can't do it because I've got about \$25 million of space left. \$20 million already spoken for, and the other bits and pieces. So you're limited in terms of the amount of business you can do. […] And that's it, that's the limit. A fantastic, huge deal comes along and you can't do it. (#33, 13 October 2006)

Not only did this penalise foreign banks vis-à-vis their local counterparts, the quota system practically dictated the nature of competition amongst the foreign banks since the regulators determined the amount of lending business each bank could do. A more established foreign bank with a larger loan portfolio was more likely to be given a higher quota for foreign currency lending compared to a smaller and newer entrant into the Chinese banking market:

> [T]he general way to calculate your quota is your business portfolio. How much loan you have is how much quota you will get. Then of course if you [are] a new bank here, it's very difficult to borrow. If you've set up for a long time and you have a large loan portfolio then your quota will also be much bigger so your position is much better. This is not them [just] treating the foreign banks compared to local banks unfair[ly] but also treating the foreign banks among each other unfair[ly]. (Foreign representative of foreign bank: interview no. 45, 1 November 2006)

A foreign manager of a foreign bank in Shanghai gave me an extended account of how foreign banks and regulators were constantly trying to keep a step ahead of one another to further their commercial or regulatory agendas. For banks that did not have the appropriate license for RMB business, they could lend a corporate customer US dollars which they could then convert to local currency at a local bank to pay their bills, overheads and so on. However, this was halted in June 2004 when the government passed a law whereby a foreign currency loan made to a customer had to be utilised in that currency and could not be converted to RMB.[17] In order for the corporate customer to convert the loan into local currency,

[17] Theoretically, this is to prevent speculation on the appreciation of the RMB.

documentation was required to demonstrate the reasons for the conversion (such as import or export documents). In response, some foreign banks employed creative means of regulatory arbitrage:

> The banks might stretch the rules a little bit by saying that this company wants RMB financing; we can't do the financing because we haven't got a RMB license and if we lend you dollars you can't convert it. And he might say that a year ago I bought some machinery from so-and-so company and provided he can produce the right documentation, we're allowed to make loans on that basis and he can repay… he can demonstrate that he has imported… (Foreign manager of foreign bank, #37, 19 October 2006)

Another tactic used by foreign banks that did not have a RMB license was to sign a corporation agreement with a Chinese bank which stated that they would offer a guarantee if the local bank lent local currency to their clients. This allowed the foreign banks to still participate in RMB lending in some form even if they could not provide the loans directly. However, the regulators soon caught up with this and issued a new law stating that foreign banks in China were not allowed to issue guarantees or standby letters of credit (LC) to support local companies wanting to borrow RMB. "But what they forgot is that we can issue a standby LC from abroad. So what we do now is issue a standby LC from Italy directly to the Chinese bank. We just rang the customer with their requirement, send into ICBC, issue a standby letter of credit from Italy to ICBC and they lend them the money, which is fine" (*ibid.*). But even this loophole was closed later by another regulation concerning the borrowing gap, even though it governed corporations instead of banks. The borrowing gap was defined as the financial gap between the registered capital and the total investment. If a company had a registered capital of US$3 million and total investment of US$9 million, its maximum borrowing (the borrowing gap) would be

US$6 million. When the regulators tightened up the rules on domestic standby LC and the foreign banks issued them from abroad instead, they tightened the rules on the borrowing gap such that if a company had local currency borrowing supported by a foreign currency guarantee of any type, that would count as debt. So if the company that had US$6 million of borrowing would still like to borrow another 20 million RMB supported by a US$2 million foreign currency guarantee, it would find that it has reached its permitted amount of borrowing because the US$2 million was outside the borrowing gap. The company was responsible for managing the borrowing gap, but when a bank granted the loan it had to demonstrate that it made the appropriate enquiries and that the company was operating within the limits. In this instance, the tightened regulatory measures not only restricted the business scope of the foreign banks but also their corporate clients, who would either have to limit their business activities or expansion in China or turn to the Chinese banks for their borrowing needs even if the rates or level of service were less favourable.

It was not only published rules that are used by the Chinese regulators to control the pace of 'marketisation' and govern the behaviour of foreign financial institutions; other less tangible and more sociological means of influence are also at work. In international relations, the term 'soft power' was coined by Nye (1990) to describe the growing importance of non-traditional ways, such as culture and values, a country could wield to influence others. According to Nye, soft power lies in the ability to co-opt, rather than coerce, other countries, so that a country "may obtain the outcomes it wants in world politics because other countries – admiring its values, emulating its example, aspiring to its level of prosperity and openness – want to follow it' (Nye, 2004: 15). In contemporary international politics the term 'soft power' is used to supplement or conceal the exercise of military and economic power. The goal underlying the use of this concept is for a country, particularly one with global influence, to convince the world or particular groups of the correctness of its principles and ideas. Culture is thus seen as a means of public relations and a method of strengthening a country's influence. Although operating on different scales and originating from different political contexts, this concept echoes Gramsci's (1971) notion of hegemony, which refers to a process of moral and intellectual leadership through which the subordinate classes of post-1870 industrial Western European nations 'consent' to their own domination by the ruling classes, as opposed to being simply forced or coerced into accepting inferior positions. This is accomplished by states through the use of the popular culture, mass media, education, and religion to reinforce an ideology which supports the position of dominant classes. Buried in everyday life, hegemonic processes thus become taken-for-granted and 'natural'. In the case of my empirical study, power was used not necessarily to convince financial actors about the 'rightness' of regulatory actions or principles but more in the form of indirect coercion and influence through cultural and sociological means (rather than specific regulatory rules) in order to solicit the desired response or actions. As such, the use of specific rules and regulations to limit the behaviour and activities of foreign banks could be conceptualised as 'hard power' while indirect methods of governance and control could be conceptualised as 'sociological power'[18], although one could argue that the latter is more effective when it is backed up by the implicit threat of 'hard power'. The examples below illustrate the workings of sociological power in the finance community in China.

A number of interviewees emphasised the importance of establishing good working relationships with the regulators so that they were more likely to be 'on your

[18] I use the term 'sociological power' in order to differentiate my usage and conceptualisation of the term from Nye's (1990) notion of 'soft power'.

side' when certain decisions had to be made that might be favourable to you or another party. In their experience, regulatory and commercial decisions especially in smaller centres outside of Shanghai tended to be structured by '*guanxi*' (关系; directly translated as 'connections' and 'relationships'),[19] which meant establishing and cultivating relationships with the local regulatory bodies (who interpreted the laws passed from Beijing and oversaw the local implementation) who could have significant impact on business activities. Part of this was due to the tiered structure of government in China where local government officials and regulatory bodies had considerable autonomy to make decision based on the broad guidelines issued by the central government. Local officials were usually keen to protect the interests of local institutions whom they had regular contact and good *guanxi* with. Most foreign bank branches were located in Shanghai as it was the first city to be opened up. However, the rising cost of labour, land and other resources within Shanghai meant that most industrial activities took place in the surrounding provinces of Zhejiang and Jiangsu, which had also become the preferred location of many foreign manufacturing companies. If a foreign company in China wanted to open a bank account outside of the province it was located in, it required permission from the local SAFE or PBOC office (depending on the type of account and transactions). The foreign company might wish to open a bank account with a foreign bank located in Shanghai due to existing client relationships in other parts of the world, reputation or particular banking services, but permission could be denied by the local SAFE or PBOC office who would rather the bank account be opened with a domestic Chinese bank within that province. The decisions made by the local regulators were thus not only based

[19] 'Guanxi' refers to a basic dynamic in personalised networks of influence associated with Chinese societies (even outside of China) and is treated as a form of social capital.

on interpretation of published rules but also heavily influenced by a strong localised social network between government, banks and enterprises:

> So a new Italian company says 'I'm setting up a new company in Suzhou industrial park. My initial capital is going to be a million dollars. I would like to open a capital account with [your bank because] you're our bank [back in the home country]. And we say, 'Great!' He needs to get the permission of his local SAFE in Suzhou and also SAFE Shanghai. SAFE Shanghai is no problem because they're here, we know them and that's fine. But the local SAFE in Suzhou, the guy who runs it there, you know, goes out every week with the guys from the Bank of China and ABC [Agricultural Bank of China]; he will not give permission to the Italian company to open a capital account with us. He would say, 'No, no, open it locally'. They just have a way of doing things… because you *need* to have these people on board and you *need* to have a good relationship as a company with your local SAFE office, and your local this office and that office. (Foreign manager of foreign bank: #37, 19 October 2006; original emphasis)

It was difficult to overcome local *guanxi* networks especially when the local regulators were already predisposed to protecting their local institutions. Foreign banks could thus find themselves facing additional barriers in attracting new clients or even retaining existing international corporate customers.

Foreign banks could also find themselves under pressure from the regulators to 'toe the line' and display the 'appropriate' behaviour even outside of the application process for licenses. There was a fear that if one should annoy the regulators, through misfiling of forms, not turning up at certain official functions or stepping on their toes in one way or another, the regulators could withhold permission for certain requests or delay the application process of various licenses. The foreign banks thus felt additional pressure to be especially diplomatic in their dealings with the regulators; "You've got to play nice-nice and be nice-nice… and make sure you get it right. And almost, it's kind of pathetic to see all these *lao wai*[20] paying court and homage to the CRBC" (president of foreign bank: #20, 11 April 2006). The above respondent related an event that occurred the day before our interview where there was a presentation by the Spanish central bank at the Shangri-La hotel, under the auspices of the CBRC. There was a large guest list which includes Liu Mingkang, the chairman of the CBRC from Beijing. For official events like these, some of the banking figures invited would either miss the event due to other demands on their schedule or they would turn up to sign in, collect printed material and then leave after a short period. For that particular event, however, due to its high profile nature and attendance by the CBRC head from Beijing, all the invited guests were called up individually and their attendance were firmly requested, with the unspoken but understood pressure of knowing that the regulators have the power to quicken or slow down (or even halt) their business progress in Shanghai:

> At this one, I was called, *everybody* was called, and if you didn't go and your name was on the list they called you. And they called, the compliance office, and said, '*Get there. Get there, be there*'. And so there was an instant fear that if you didn't turn up, you're in the black book. I trotted down there for lunch, and the […] little ladies behind the desk, sort of, 'Where have you been? Why weren't you here?' 'Can I have a badge?' 'No, you can't have a badge.' They weren't going to register me as being there unless I've stayed all afternoon. Fortunately, my friend at the central bank came in with a little bag of goodies with my badge, so I shot off for the afternoon. But I know the Japanese were all in, and lots of people were called, you know, 'You come. You've been invited, you *be* here.' And every time, everyone is at a different stage of development, every bank. With licenses, with the renminbi licenses or with branch licenses, so everybody has this to fear. And there *is* a fear here; if I piss off the central bank, you know, what will they do? Will they hold me up? And then of course if it's a multinational bank, there is a fear that if you screw

[20] 老外, a Mandarin slang for 'foreigners', more specifically referring to 'Westerners' or 'Caucasians'.

> up, then head office gets to hear about it, then you're double-damned! […] It's a very powerful beast in terms of keeping control, you know… it's the general run-of-the-mill bureaucracy and then there's the sort of blackmail of be-good-or-else! (*Ibid.*; original emphasis)

This use of 'sociological power' by the regulators to control the behaviour of foreign banks was mentioned by a few other interviewees but the above account is the clearest example of how the regulators use official powers to solicit the desired forms of behaviour from foreign banks. Therefore, while soft power or Gramscian notions of hegemony operate by having actors confirm willingly, the foreign finance community in Shanghai found themselves complying grudgingly rather than willingly due to the fear of undesirable consequences, even if such threats were never made explicit. Due to the degree of control that the regulatory bodies had over the business activities of foreign banks in China, the latter had to constantly work at staying in their good graces and cultivate good relationships outside of the formal application procedures.

6.7 CONCLUSION

The regulation of a financial market requires the maintenance of some form of systemic equilibrium and a framework of legal and administrative rules (Leyshon and Thrift, 1997: 60). All systems of regulation, however, are fragile and temporal within a highly dynamic and spatially variegated capitalist system especially in an age of post-hegemony where governments, international regimes and regulatory authorities are increasingly squeezed between various sectors and firms in the finance industry pushing for more permissive rules. The concept of post-hegemony, highlighted in Chapter 3, captures how the internationalisation of economic activity beyond and across the space-economies of individual states is undermining the coherence of the old hegemonic order such that “hegemonic power no longer resides in one territorial state (if it ever did) [but] resides in a number of nodal points (and vectors and flows) that describe a decentred hegemonic core” (Corbridge, 1994: 1849). This idea of a decentred core of actors is useful in conceptualising how power in influencing regulatory regimes and capital flows is distributed amongst a variety of actors, including state institutions, supranational organisations, large private capital and particular actors or communities (e.g. policy, finance or other interest groups) across the global space economy. China’s approach to the ‘marketisation’ of its finance sector had been fairly conservative and remained tightly controlled by the state with regards to the specific nature of foreign competition, information disclosure and levels of transparency and pace of reforms. However, there were also clear indications of international influence and cooperation as regulatory counterparts in the places such as the City of London, New York, Hong Kong and Singapore were actively involved in the development of regulatory capacities in the financial sector in China. The influence of global institutions such as the WTO was also clearly implicated in the deregulation of China’s financial services and economic strategies. In addition, foreign financial institutions in Shanghai were actively engaged in pushing for reforms in specific areas important to their business operations in Shanghai, in their search for ever higher returns on capital investment. As discussed above, they also sought to exploit loopholes and employ creative means of routing money from abroad and obtaining the necessary documents from alternative sources to get around existing rules that restricted their business activities. The process of ‘marketisation’ was thus highly contested and influenced by a variety of actors and institutions both within Shanghai, the larger context of China and the international community.

As the finance sector in Shanghai (and elsewhere in China at different stages and pace) is opened up to foreign participants and regulatory and legal frameworks are being developed, the concept of 're-regulation' is useful in capturing the complex process of regulatory change (Cerny, 1993). Regulations are not simply lifted as the very operation of market economies is dependent on the existence of *a priori* rules and mechanisms, many of which were actually lacking in China. This process of 're-regulation', in the drafting of new regulations, the adaptation of existing rules and better policing of how these rules are implemented, is not purely for the purpose of attracting foreign capital. In the case of Shanghai, the pace and nature of re-regulation is also used as a means of controlling the speed of financial reforms and to achieve particular objectives set by the Chinese government. The Chinese state clearly maintains a key role in determining the shape of finance within the national space-economy but they do still have to negotiate with a range of other actors and institutions that operate on and across spatial scales.

In this chapter, I began by examining the ways in which knowledge and expertise regarding the implementation of 'market' practices and structures were acquired, interpreted and adapted by the Chinese regulatory institutions through MOUs with counterparts in other countries, channels of consultation and dialogue with industry participants and attracting overseas 'returnees' with the relevant skills and experience to change and implement economic practices from within the organisations. The importance of a '*difang hua*' approach, highlighting the specificities of the Chinese historical, economic and political context, was shown to be the guiding principle in determining the structure and pace of reforms. There were different views regarding whether the pace of financial reforms and liberalisation had been too quick, too slow or appropriate, as well as different conceptualisation of ‘competition’ between foreign and local market participants. By combining different concepts, philosophies and methods, financial reforms in China were borne out of a complex balance of interests amongst market participants in Shanghai, regulatory bodies and state institutions in different parts of China (who had different interpretations, views and agendas), and other financial, regulatory and institutional actors in the global space economy. The case of China’s WTO accession demonstrated the role of supranational organisations in establishing market order and governing terms of exchange and competition through specific sets of rules. It had arguably quickened the pace of reforms and boosted international confidence in China’s commitment to fairer terms of competition and opening up its markets to foreign players. However, non-tariff barriers that had a disproportionately negative impact on foreign banks vis-à-vis domestic banks were seen as a means of ‘subverting’ their commitments. In addition to specific regulations that were used to control the activities of foreign banks and pace of ‘marketisation’, the use of ‘sociological power’ was also important in disciplining foreign financial institutions.

In the next chapter, I focus on the building of specific capital markets development in Shanghai and how contesting visions of markets were negotiated in the process of instituting market reforms. The reasons why such processes were taking *place* in Shanghai at a specific moment will also be explored with regards to its historical context and forces and actors operating across global, national and local scales.

Chapter 7

Contesting Visions of Financial Markets in Shanghai

7.1 INTRODUCTION

Of the numerous financial reforms that took centre-stage in the national development agenda since the early 1990s, the most conspicuous was the establishment of capital markets in Shanghai where none existed before or were closed for many decades. The financial markets in Shanghai include securities, inter-bank offerings, bonds, futures, foreign currency and gold amongst other. In terms of recent changes in financial markets, the public listing of the big Chinese banks, especially the state-owned banks, is an important trend and one that is likely to continue. Table 7.1 lists some of the publicly listed Chinese banks over the past five years. Although there has been some criticism levelled at the process and objectives of such listings, it has at least opened up the banks to some public scrutiny and improved systems of corporate governance to some extent (Lyons, 2005). The push towards international public listings is also important in aligning Chinese firms, financial institutions and individuals with international practices and conventions of corporate governance, regulatory process and accounting and legal standards. In late-July 2006, China ended its decade-old peg of the RMB to the US dollar and introduced a managed float, weighted against a basket of four major currencies. The US dollar, the Euro, the Japanese yen and the Korean won were chosen as they represent the economies of China's four largest trading partners. This was seen as a small but important step towards the internationalisation of the RMB in the longer term. Stock market reforms had been especially prominent in the past five years as the CSRC work at dissolving the artificial divisions within the segmented Chinese stock market, allowing greater foreign participation in the domestic market as well as allowing domestic investors to invest in overseas markets.

Table 7.1 Recent public listings of Chinese banks

Bank	**Date of IPO**	**Listed in**	**Capital raised (US$ billion)**
Shanghai Pudong Development Bank[1]	November 1999	Shanghai	0.48
China Construction Bank[2]	21 October 2005	Hong Kong	8.0
Bank of China[3]	24 May 2006	Hong Kong	9.7
China Merchants Bank[4]	22 September 2006 (Hong Kong)	Shanghai & Hong Kong	2.4 (Hong Kong)
Industrial and Commercial Bank of China[5]	27 October 2006	Shanghai & Hong Kong	19.1
China CITIC Bank[6]	16 April 2007	Shanghai & Hong Kong	5.4
(Sources: 1. http://www.gbcc.org.uk/iss18_1.htm 2. http://www.chinadaily.com.cn/english/doc/2005-10/21/content_486689.htm 3. http://www.iht.com/articles/2006/05/24/business/boc.php 4. http://www.boston.com/business/articles/2006/09/22/china_merchants_bank_ipo_makes_debut/ 5. http://www.iht.com/articles/ap/2006/10/28/business/AS_FIN_China_ICBC_IPO.php 6. http://www.iht.com/articles/2007/04/29/news/bxcitic.php)			

The actors involved in the recent trends described above are many and varied in terms of their institutional capacities, financial clout, regulatory power and geographical location. The recognition of the variety of actors and interests within a market setting and an emphasis on power, conflict and negotiation is central to my analysis. The form, structure and pace of market formation taking place in Shanghai is a contested process that has to be negotiated amongst the different interests of ‘incumbents’ and ‘challengers’ (Fligstein, 2001), involving a variety of actors such as local firms, foreign firms, national and local state bodies, foreign state institutions and transnational practices. The dominant ‘mode of exchange’ (Lie, 1992, 1993) that emerges in Shanghai is the outcome of a conflictual process between multiple parties but is also itself constantly ‘under threat’ due to shifting agendas and contexts. In this vein, anthropological and cultural approaches to an understanding of markets (see, for example, Zelizer, 1988, 1993, 1994) are particularly instructive in demonstrating how markets are understood and experienced by actors in a variety of ways, invested with different meanings and acted upon according to different interests and contingent social relations. This discursive construction of markets has material consequences in affecting policies and practices. The central Chinese state and Shanghai government have particular understandings and visions of financial markets in Shanghai; the local and foreign financial institutions in Shanghai are also framing markets according to their own interests, agendas, experience and interpretations of what a market *should* be. How are these different 'framings' of market played out in Shanghai?

In this chapter, I focus on the development of the Shanghai stock market and the strategies and experience of foreign banks in Shanghai to examine how contesting visions of markets are negotiated in the process of instituting market reforms. Section 7.2 presents a close examination of the structure and characteristics of the Shanghai stock market as I tease out some of the contradictions and complexities in the process of China's 'marketisation' in its capital markets formation. The particular structure of the Shanghai stock market is a product of historical and economic contexts that it is embedded in as well as specific objectives set by the Chinese state, but it has also constantly evolved in response to broader national economic development, international pressure from foreign investors, financial institutions and supranational organisations and increasing maturity of local financial institutions and investors. My objective is therefore not to point out its 'peculiarities' or simply to present a 'stock-market-with-Chinese-characteristics' but to highlight the process of market reforms in which the structure and meaning of 'market' in the context of the Shanghai stock market evolves through contingent social relations amongst market participants.

The SMG is keen to promote the city as an international financial centre to attract foreign capital and has been largely successful as evident from the large foreign bank presence in Shanghai. However, much of what is happening in Shanghai is arguably the outcome of political and economic processes elsewhere. On the one hand, institutional forces in Beijing still determine the pace and process of 'marketisation' in Shanghai; on the other hand, developments in Shanghai are also determined by the business needs of the international community and how Shanghai (or China as a whole) fits into their globalisation strategies. In section 7.3, I examine how scalar politics is implicated in the development of Shanghai's financial markets by examining the extent to which central government policies, regulatory forces and economic development at the national and regional levels influence the development of financial markets in Shanghai. In section 7.4, I use the experience of foreign banks in Shanghai, the history and strategies of their involvement, relationships with their global headquarters and other (local and foreign) banks in Shanghai as a lens through which to gain insights into the process of instituting market reforms in China's banking sector. Through this, I reveal the often conflicting, sometimes cooperative and always fluid relationships amongst the domestic and foreign banks and regulatory authorities as they pursue their contesting visions of 'markets'.

7.2 THE SHANGHAI STOCK MARKET: ONE MARKET, TWO SYSTEMS?

> *"Why do you want to visit the trading floor?" smiles Fang Xinghai, deputy chief executive of the Shanghai Stock Exchange. "There is nothing to see." He is right. But this has little to do with the switch from open-outcry to electronic share-trading to which he refers, because the exchange simply replaced traders' paper slips with computers and kept everyone on the floor. The desks are mostly unmanned, however, or given over to card games. An elegant gong greet new listings, the equivalent of New York's famous bell, gathered dust for months until a ban on IPOs was lifted in January. The only movement is on electronic wall charts tracking*

prices and volumes – and that is resolutely downwards. (The Economist, 24 February 2005)

In 1990, China became the first communist country in the world to have stock exchanges and the only socialist country to initiate building a 'market style' enterprise system through a corporatisation and shareholding framework without privatising its SOEs. The Chinese political-economic concepts of 'socialism with Chinese characteristics' and 'socialist market economy'[1] were reflected in its practices of a quota system for the primary equity market, segmented share structure and restrictions on the trading of shares held by the state (and its affiliates) in the secondary market. The conversion of state enterprises into stock corporations, flotation and listing of shares, and the pricing of firms in the primary and secondary markets did not operate according to common understandings of 'capitalist' principles and 'market'-determined criteria (such as price-to-earning (P/E) ratio, book value, cash flow forecasts, historical performance, quality management and product niches), but were subject to central control and national planning.

Implementation of the shareholding system was set out in the 1992 Trial Measures on Shareholding System, which stated that it was to observe the principle of preserving 'public ownership' (by the state) and 'cooperative ownership' (based on contractual arrangement among the employees, enterprise, and the state) as the mainstay of China's economic system. The framework for this shareholding system is set out in Table 7.2. In capitalist economies, a shareholding system is used to maintain the fundamental structure of private ownership of the means of production. In a socialist economy like China, the shareholding system was utilised to preserve public ownership of the means of production as the mainstay of the national

[1] As stated in the 1992 Fourteenth Party Congress report (Yao, 1998)

economy, through distribution of shares such that it resulted in the dominance of state ownership amidst private ownership. In other words, the system dilutes, but did not completely undermine, state ownership. Shares issued by stock corporations were thus classified and segregated into different types of shares to fit an investor-specific share structure (e.g. state shares, state-owned legal person shares, Chinese individual shares, and foreign person shares), each type being subject to unique sets of laws which aimed to preserve the dominance of the socialist public ownership in the overall share structure.

Table 7.2 Guidelines for implementing the shareholding system in China

▪ It shall be *prohibited* to those lines of business related to national security, national defence technology, rare metals mining, or any lines of business that call for state monopoly. ▪ It may be *adopted*, subject to the state holding controlling interests, for those lines of business that are among the key development industries listed in national industrial policies, such as energy, transportation, and communication industries. ▪ It shall be *encouraged* for those lines of business that are developed in accordance with the national industrial policies and where competition is intense, particularly for those industries that are capital intensive or technology intensive, or that are large scale in terms of economic size.
(Source: Yao, 1998: 5)

7.2.1 The Alphabet-soup of Share Structure

Some of the contradictions and complexities in the process of China's financial 'marketisation' are most clearly revealed in its stock markets and share structures. Ideally, regulators and exchanges should create conditions in which information affecting the price of a company is equitably available to all buyers and sellers on the stock markets. With a sufficient degree of transparency, investors have a (more or less) level playing field on which to base their investment decisions, whether for the purchase of a just a handful of shares or millions to secure the control of an entire company. These decisions, in aggregate, determine the market value, or market capitalisation, of listed companies. For Chinese companies, stock markets do not particularly fulfil this function for the simple reason that the different categories of stock trade in different and functionally independent markets.

The stock shares in the PRC are classified into Chinese public shares (also known as A shares), domestically listed foreign person shares (B shares), state shares, state-owned legal person shares (C shares), and overseas floated and listed foreign person shares (e.g. H and N shares). Table 7.3 lists the legal definitions of these categories. Under the popular classification in use on the stock markets, shares are divided into A, B, C, H and N shares. *A shares* are shares denominated and payable in RMB and held by individual Chinese citizens; *B shares* are denominated in RMB and payable in a foreign currency, listed within China, and held by foreign individual or institutional investors; *C shares* are denominated and payable in RMB and held by state-owned legal persons; *H shares* are shares floated and listed on the Hong Kong Stock Exchange; and *N shares* are shares floated and listed in New York (on the New York Stock Exchange or NASDAQ). This classification of stocks into different types of shares based on the identities of investors, and which attach different sets of rights, interests and obligations to each, is problematic for many reasons. Creating a hierarchy of investors goes against the principle of share equality – a share is a share. This practice of attaching different sets of legal rights and market characteristics to each type of share based solely on investor's identity, and not on any economic differentials in terms of capital contribution or investment risk, produces different market prices for the same stock, increased levels of uncertainty and hence greater investment risk (which I will elaborate upon later).

Table 7.3 Types of shares in the PRC stock market and their legal definitions and characteristics

Individual A shares	▪ Domestically listed shares denominated in local currency ▪ Owned by individuals and legal persons. ▪ Make up about one-third of a typical company's equity. ▪ Foreign investors were not allowed to own these shares prior to the QFII scheme.
Individual B shares	▪ Domestically listed shares of China-incorporated companies, denominated in US$ in Shanghai and HK$ in Shenzhen. ▪ Owned by individuals and legal persons. ▪ Initially reserved for foreign investors, domestic institutions and individuals now account for most trading
Legal person C shares	▪ About one-third of every listed firm's equity is transferred to domestic institutions (stock companies, non-bank financial institutions and SOEs with at least one non-state owner) at the time of restructuring and cannot be traded on the stock market. ▪ Since 1997 an active market in one-to-one deals in legal person shares have evolved, usually involving state legal person shareholders selling out to private companies but only in state approved deals.
State shares	▪ About one-third of equity is transferred to the state (central and local government bureaux and SOEs wholly owned by the state). ▪ The ultimate owner of these state shares is the State Council but the shares are managed by the Ministry of Finance or state asset management bureaux. ▪ State shares are not tradable.
H shares	▪ Individual shares of PRC registered companies listed in Hong Kong.
Red Chips	▪ Shares of companies registered overseas and listed abroad (principally in Hong Kong), having substantial Mainland interests and controlled by affiliates or agencies of the PRC government.
(Source: Yao, 1998: 8-19, Green, 2004: 29)	

The conversion of SOEs into stock corporations was to comply with the policies outlined above to ensure the necessary dominant position for state shares and the secondary position for state-owned legal person shares, with Chinese public shares occupying the third, non-controlling and minority position. As a result, the trading of state shares was banned, the trading of state-owned legal person shares was confined within the scope of state-owned legal persons (i.e. they could only trade with one another), and likewise the Chinese public could only trade Chinese public shares among themselves. Fixing this hierarchy in the primary market and the insulation and fragmentation in the secondary market was intended to achieve the Constitutional mandate of preserving the predominance of the state's share interests (Yao, 1998). However, this resulted in poor liquidity and produced differentiated prices for various types of shares of the same stock in the fragmented markets.

Within the Shanghai stock market, for example, traded A shares and B shares, for the same company's stock, had different prices, while H shares (in Hong

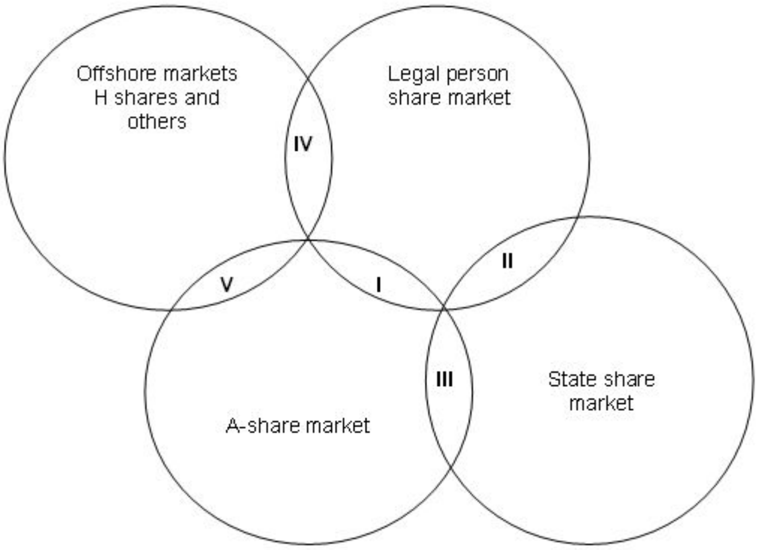
Kong) of the same company's stock were also traded at another price. This begged the question of which price was an accurate reflection of issuer value and created confusion for investors as well as corporate financing as the firm would need to consider the pricing of each share compartment to make project investment decisions. Due to tight currency controls, the A share investors (i.e. the Chinese public) had few investment alternatives. They could invest in A shares, B shares (if they had foreign currency) or put their money in the bank. Even if they had foreign currencies and overseas bank or securities accounts, they were restricted as to how much they could send abroad. China's investors were thus faced with very limited investment options and this created a situation of too much money chasing too limited a supply of (A) shares. This was in contrast with overseas investors who could freely convert their currencies and have much greater choice in markets and types of securities. Table 7.4 shows that A shares were generally traded at a P/E ratio much higher than B shares or H shares, compared to the average P/E ratios in the United States in the range of 15 to 22 and to any given issuer having only one P/E (Yao, 1998: 22). Such wide differences in P/Es for the same issuer in different markets could not be accounted for by exchange rate differentials alone. So if A shares, B shares and H shares for the same company had different prices and different trade volumes, which was more indicative of the company's actual performance and value? The concept of using the trading price of a company's shares on the secondary market to value its performance is still relatively new in China where valuation is still largely based on financial reports. Risk is indicated only if a company's financial reports show a loss over a period of three consecutive years. The biggest problem with this method is that it provides incentive for company owners to ‘cook the books’, as pointed out by a local analyst for a Chinese securities company (#22, 12 April 2006; translated from Mandarin):

> The first problem is that the company could move its finances around, create false accounts to avoid this. Another thing is it is over 3 years. So if it was making a loss in the first 2 years but make a profit in the third year, then it’s ok! So as long as it does well for that one year, it has bought itself another 3-years time! There are many problems in this. This is very different from overseas… But this is already changing now, but it still does not really follow stock price from the secondary markets.

Table 7.4 The P/E ratios of Chinese stock markets

Year	Shanghai A-shares	Shanghai B-shares	Shenzhen A-shares	Shenzhen B-shares	H shares	Red Chips
1990	28.05	-	-	-	-	-
1991	81.83	-	26.71	-	-	-
1992	72.65	17.40	57.52	35.56	-	-
1993	42.48	-	44.21	20.11	-	-
1994	29.67	9.94	10.67	7.02	11.61	-
1995	16.32	8.00	9.80	6.01	10.05	-
1996	32.65	14.04	38.88	14.07	10.85	-
1997	43.43	11.99	42.66	10.67	14.84	-
1998	34.38	6.04	32.31	5.71	7.11	10.44
1999	38.14	10.05	37.56	10.38	-	-
2000	59.14	25.23	58.75	13.06	-	-
2001	37.59	43.39	40.76	25.30	6.41	18.72
2002	34.50	30.61	38.22	17.51	9.52	13.17
(Source: Walter and Howie, 2003: 181)						

Normally, only one liquid market should exist, the A share market. Legal person shares and state shares are not tradable on the open market but could be transferred within each class. However, this is only done with specific transaction approval by the state. Then there are the B shares market and overseas listings. Over time, at least four parallel markets have developed, with each market being restricted in terms of types of investors and trading (Figure 7.1). The intersection of the A-share and legal person share market in Area I and with the state share market in Area II are open only to legal person entities on a negotiated basis; the typical A-share investor is excluded. Areas III, IV and V are growing in significance with stock



v greater foreign investor
ıt are released and sold in
indicate participation by
ıborate upon later. Such a
ıpital market has been
t a capital market that is
ıe same rights, the same
interests and the same obligations as every other share of the stock, the Chinese stock markets continue to confuse and frustrate both local and foreign investors and suffer from poor liquidity.

Figure 7.1 Parallel markets (Source: Walter and Howie, 2003: 177)

[2] Named after the PRC's policy of 'one country, two systems' of socialism for mainland China and of capitalism for Hong Kong, under the aegis of one China.

Moreover, the amount of tradable stocks is only a very small portion of the actual issued stocks of the company. The markets, or a single company's capital structure, can be seen as a series of concentric rings or wheels (Figure 7.2). At its heart lies the state with absolute control via state shares; next come the state-affiliated institutions holding legal person shares; then come the 'alphabet' share holders. Over time, the wheels themselves have grown in size due to new listings and other financing. In general, however, the non-tradable share of this system has remained at around 70 percent (see Appendix C for the equity structure of Chinese listed companies on the SSE and Shenzhen Stock Exchange). The majority of shares are held by the state, state entities or company employees and are non-tradable on the open market for three to five years, after which they are often bought back by the company and then re-issued to employees again. However, there is plenty of activity at the boundaries of each wheel as they grind against each other. The further out from the centre, the greater the number and diversity of the investors, and further one is away from the state itself. There is a big difference between holders of state-owned legal person shares and foreign investors at the outer reaches of the circles. As this system spins, friction and centrifugal force gradually push the shares located in the centre (the state shares) into the next layer (legal person shares), into the next (A shares) and so on. This process, driven by the unending quest for capital by the state, companies and investors, is happening now with reforms underway in China's stock markets.

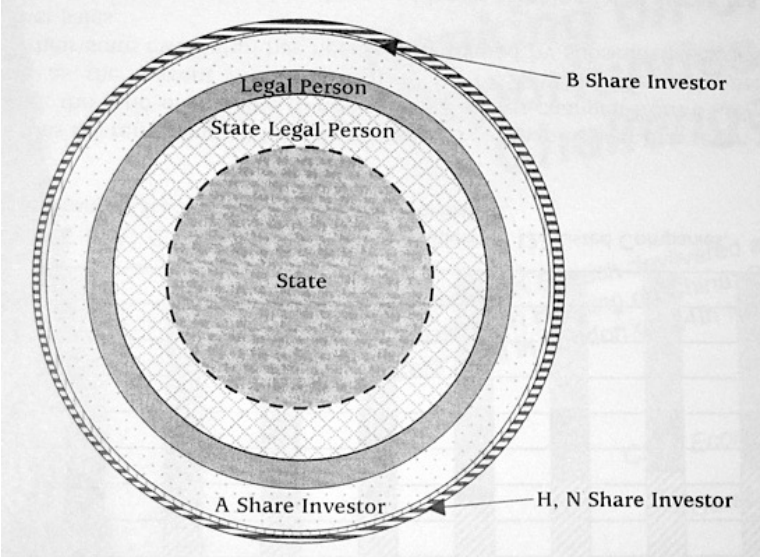


Figure 7.2 Circles of ownership (Source: Walter and Howie, 2003: 201)

Over the past few years, the Chinese government had begun to try to unify China's stock markets. This was largely due to the practical need for more capital and involved selling at least part of the state's holdings into the A-share market. Other factors driving the effort included a political willingness on the part of the state to divest itself from non-essential industries (抓大放小; *zhuada fangxiao* – keep hold of the big and let go of the small) (Green, 2004). Finally, a number of my respondents also pointed out that there had been growing realisation among policy makers that the current share system would have an increasingly negative impact on the future growth of the market and economy at large if the inconsistencies and contradictions persisted (Chinese regulatory official: #24, 16 April 2006; local official from Office for Financial Services: #28, 20 April 2006; local analyst from joint-venture company: #48, 3 November 2006).

One of the key reforms was in the B share market, which had been problematic for the past decade. The market bloomed during its inception in the early

1990s but then quickly stagnated with the beginning of overseas listings in 1992. In general, lack of interest, a dearth of quality companies and shallow trading volumes had plagued the market. There were other better Chinese investment opportunities such as H shares, Red Chips and other listings, which had all trumped the role that the B share market was supposed to play. The exclusion of domestic investors, coupled with the lack of foreign interest, meant that B shares had historically traded at an 80 to 90 percent discount to their A share counterparts (Walter and Howie, 2003). To address the B share market problem, the CSRC announced the opening of the market to domestic investors with foreign currency accounts in March 2001. This had some limited success as the B share price discount fell rapidly within a few months from around 75 percent to 30 percent and then levelled out at around 45 to 50 percent after 18 months of trading (Walter and Howie, 2003: 180).

Since late-1999, the CSRC and State Council had initiated a number of regulations, with limited success, to reduce the state's holdings. On 29 November 1999, the CSRC announced the selection of 10 listed companies chosen to auction off a portion of their state shares to the A share market. Pricing was set at around 20 percent that of tradable shares. The response, however, was surprisingly cool and many of the newly released shares were undersubscribed (Walter and Howie, 2003: 196-199). The failure of the experiment reflected people's expectations of much lower pricing with the knowledge that there were more state shares to come. A second effort was launched in June 2001, which was arguably instrumental in bringing to an end the two-year-old bull run in the Chinese stock markets as the prospects of that many low-priced shares 'flooding' the market had an adverse effect on stock prices. The conclusion was that the domestic equity market was still not broad enough or deep enough to absorb even a part of the huge state sector, which explains the continued reliance on overseas offerings for major listings. The way out required time and the development of an investor base beyond the retail sector and market punters.

There was a constant call in the state share sale debate that the value of existing A share holdings must not be diminished but this was impossible as no market could maintain its current prices against a big influx of new supply unless there was fresh capital entering and in this case, the fresh capital had to come from foreign sources. The introduction of a Qualified Foreign Institutional Investor (QFII) scheme was particularly welcomed in this regard, the objective of which was to attract long term investment into the domestic market. On 5 November 2002, the CSRC and PBOC introduced the QFII programme as a provision for foreign capital to access China's RMB-denominated equity and bond markets. Foreign entities with QFII status were thus allowed to participate in the previously locals-only A share market, although some restrictions still apply. Investors, such as overseas invested China funds, were required to keep their money in China for a minimum period of three years. Shares could be bought and sold freely within that period but funds could not be repatriated during that time. Since then, revisions to the rule have lowered the threshold of capital lock-up first to one year and then down to as little as three months (People's Daily Online, 2006). As of 14 October 2004, a total of 25 foreign institutions have received QFII licenses with quotas ranging from US$50 million to US$800 million, amounting to more than US$2.8 billion authorised for investment in the Chinese markets (China Daily, 2005). Table 7.5 shows the latest list of QFIIs in China.

Table 7.5 List of QFIIs (as of December 2006)

No.	Names of QFII	Date authorised
1	UBS AG	23/05/2003
2	Nomura Securities co, Ltd.	23/05/2003
3	Morgan Stanley & Co. International Limited	05/06/2003
4	Citigroup Global Markets Limited	05/06/2003
5	Goldman, Sachs &Co	04/07/2003
6	Deutsche Bank Aktiengesellschaft	30/07/2003
7	The Hong Kong and Shanghai Banking Corporation Limited	04/08/2003
8	ING Bank N. V.	10/09/2003
9	JPMORGAN CHASE BANK	30/09/2003
10	Credit Suisse (Hong Kong) Limited	24/10/2003
11	Standard Chartered Bank(Hong Kong) limited	11/12/2003
12	Nikko Asset Management Co. Ltd.	11/12/2003
13	Merrill Lynch International	30/04/2004
14	Hang Seng Bank	10/05/2004
15	Daiwa Securities SMBC CO.Ltd.	10/05/2004
16	Lehman Brothers International(Europe)	06/07/2004
17	Bill & Melinda Gates Foundation	19/07/2004
18	INVESCO Asset Management Limited	04/08/2004
19	ABN AMRO Bank N.V.	02/09/2004
20	Société Générale	02/09/2004
21	Templeton Asset Management Ltd	14/09/2004
22	Barclays bank PLC	15/09/2004
23	Dresdner Bank Aktiengesellschaft	27/09/2004
24	Fortis Bank SA/NV	29/09/2004
25	BNP Paribas	29/09/2004
26	Power Corporation of Canada	15/10/2004
27	CALYONS.A.	15/10/2004
28	Goldman Sachs Asset Management International.	09/05/2005
29	Martin Currie Investment Management Ltd	25/10/2005
30	Government of Singapore Investment Corporation Pte Ltd	25/10/2005
31	AIG Global Investment Corp	14/11/2005
32	Temasek Fullerton Alpha Investments Pte Ltd	15/11/2005
33	JF Asset Management Limited	28/12/2005
34	The Dai-ichi Mutual Life Insurance Company	28/12/2005
35	DBS Bank Ltd.	13/02/2006
36	AMP Capital Investors Limited	10/04/2006
37	The Bank of Nova Scotia	10/04/2006
38	KBC Financial Products UK Limited	10/04/2006
39	La Compagnie Financierr Edmond de Rothschild Banque	10/04/2006
40	Yale University	14/04/2006
41	Morgan Stanley Investment Management Inc.	07/07/2006
42	Prudential Asset Management(Hong Kong)Limited	07/07/2006
43	Stanford University	05/08/2006
44	GE Asset Management Incorporated	05/08/2006
45	United Overseas Bank Limited	05/08/2006
46	Schroder investment Management Limited	29/08/2006
47	HSBC Investments (Hong Kong) Limited	05/09/2006
48	Shinko Securities Co .Ltd	05/09/2006
49	UBS Global Asset Management(Singapore) Ltd	25/09/2006
50	Sumitomo Mitsui Asset Management Company, Limited	25/09/2006
51	Norges Bank	24/10/2006
52	Pictet Asset Management Limited	25/10/2006
(Source: CSRC website)		

Faced with the increasing demands of domestic individuals and institutions for asset management in the context of limited opportunities within the mainland capital markets, the Qualified Domestic Institutional Investor (QDII) scheme was announced by the PBOC on 13 April 2006. This provided a much needed investment option for individuals and institutions, through entities with QDII status, to invest in overseas markets. When combined with the QFII scheme, which allowed foreign capital to invest in the mainland's A shares and bonds, the scheme established a two-way channel for capital to flow in and out of China via institutional investors. By reducing net capital-inflow, the QDII scheme was also expected to ease appreciation pressure on the RMB. So far, investments had been mainly in the market for US$ bonds, the global bond market, the stock market in Hong Kong and the stock market in the USA (Liang, 2007). Table 7.6 shows the list of approved QDII and their foreign exchange limits.

Table 7.6 List of QDIIs

Qualified institutions	**Foreign exchange conversion limits (US£ million)**
Bank of China	2500
Industrial and Commercial Bank of China	2000
China Construction Bank	2000
Bank of Communications	1500
China Merchants Bank	1000
HSBC	500
Hua An Asset Management	500
China CITIC Bank	500
Bank of East Asia	300
Industrial Bank*	-
China Everbright Bank*	-
China Minsheng Bank*	-
Hang Seng Bank*	-
Citibank*	-
Standard Chartered Bank*	-
(Source: Hang Seng Bank, 2006)	

The 'split share reform' was a more recent effort to reform China's stock market. The split share structure refers to the existence of both tradable shares and non-tradable shares owned by the state and legal persons. Non-tradable shares account for about two-thirds of the shares of the firms listed on the two markets in Shanghai and Shenzhen (see Appendix C). The system, with major shareholders indifferent to price fluctuations, greatly hindered stock transactions and capital allocation and was seen as the key culprit for China's stagnant stock market. On 2 February 2004, the Nine Provisions of the State Council declared that "the issue of split-share structure must be settled in a positive and reliable manner. In solving the problem, we should respect the rule of the market and exercise diligence in protecting the lawful rights and interests of investors, especially public investors" (quoted in *China Daily*, 10 August 2005). According to the guidelines, more than 1,400 listed companies could "gradually" convert their non-tradable shares. From May 2006, a total of 46 listed companies in two groups took part in the trial reform.[3] According to the reform proposal, the companies or major shareholders should compensate about three shares per 10 shares tradable to shareholders. However, investors in China's B-share and H-share markets would not take part in the A-share market reform and therefore would not get compensation. This 'gradualist' approach to the split share reform mirrored wider trends in the re-regulation of the financial sector in China. Although it is too early to tell, optimistic responses from my interviewees indicated that they saw this as a very positive trend and expected these reforms to be very helpful in creating a better market environment with more transparent pricing that would reflect value and risk more accurately.

It is not only the share structure of the stock markets but also the listing process that is problematic. Every IPO has to be individually approved by the CSRC. Table 6.1 in the previous chapter shows the listing procedure for the SSE as published on its website. The first step in the listing procedure is to obtain CSRC approval, after which the company then submit the various required documents; but how one goes about obtaining CSRC approval is not specified. Part of this

[3] Of which only one of the firms was vetoed by public stock holders at a plenary session of the shareholders of the company as they were not satisfied with the compensation offer.

undisclosed criterion is a quota set for every province; only a certain number of companies from each province are allowed to issue IPOs each year. If the quota for a particular province has been reached for that year, a company would not be able to list during that round and have to wait in a queue. On the other hand, a weaker company (in terms of performance and valuation) from another province that has not fulfilled its quota would be able to list that year, ahead of better-performing companies (local analyst from Chinese financial institution: #24, 15 April 2006). In recent years, new IPOs had been suspended due to fears that the market was not able to absorb new IPOs. Such decisions were taken out of the 'invisible hands' of the market and market participants and firmly held within the visible hands of the regulators. A former employee of the SSE, now an official at a SMG bureau, recounted how companies were frustrated in their attempts to discern the undisclosed criteria for public listing:

> There would be other criteria or requirements that are not publicly stated. It is like a case by case consideration, so the process was not transparent. This is very frustrating for the corporation. It may want to issue an IPO but the regulator may say, 'No, you cannot do so due to this and that reason' – reasons that were never stated initially. The corporation may not be able to bear the transaction cost of that going through the application and then have it rejected. For example, if the stock market is not performing very well at the moment, there might be considerations about the effect of a new listing on the market, whether the market can accept that. But these things should not be the concern of the regulatory bodies; the market should decide whether or not it can accept a new listing. (#28, 20 April 2006; translated from Mandarin)

What was also left out of the published listing procedure and requirement was the discriminatory practice by the CSRC and other state institutions in their treatment of SOEs and private companies. This resulted in unequal treatment and

SOEs were given more favourable treatment and special consideration, be it in terms of obtaining bank financing or CSRC approval for public listing:

> On the one hand you have economic intervention, and sometimes that does not happen according to market principles, it's according to government principles. The other thing is that the government is often more mindful of state owned enterprises. So […] when there is a problem they always support the SOEs first. That means SOEs, compared to other companies, they are not treated in an equal manner in the marketplace. In terms of banking finance, in terms of entering new markets, in terms of obtaining approval and so on, they are treated differently. (Local manager of Chinese financial institution: #9, 27 February 2006; translated from Mandarin)

Due to large numbers of companies that were seeking public listing on the Mainland, and the quotas imposed on the number of listings each year (amongst other criteria), there was always a long queue of companies waiting to be approved by the CSRC for IPOs. Some local respondents remarked that it was common for SOEs to 'jump the queue' and had their applications fast-tracked and be publicly listed ahead of smaller, private companies:

> The CSRC put them in a queue and there may be about 200 of them. In reality you can only wait for the market conditions to change, or some of them can jump the queue [laughs], like some SOEs. So if you are a small company you are stuck waiting. […] This is not just a matter of companies wanting to get listed; there are too many other issues to consider. The state has done so much to get rid of the bad loans in the company so if you don't let it be publicly listed now and wait for another six months, maybe by then it will have another lot of bad loans. So you can only let it jump the queue and get listed. This is an IPO problem that must be resolved. (Chinese analyst for joint-venture company: #47, 3 November 2006; translated from Mandarin)

Therefore, it is not only the share structure of the stock market that needs to be reformed, but also the application procedure and regulatory system for approving public listings as this affects the very role and function of the stock market.

7.2.2 'This Little Pig Goes to Market'… But Which Market?

Issuers competing in the stock market for capital and investment decisions rely on the information available in a fair and efficient capital market. In order for issuers to compete on the basis of their fundamentals, investors must be able to determine the investment value of a project, the firm's cost of capital, its risk and value – all of which should ideally be reflected in the market price of the company stock. The practice of government determined listings in the primary market and government controlled liquidity in the secondary market disables accurate determination of the investment value of projects and distorts fair pricing of firms[4], both of which are two crucial functions of an efficient capital market. This view, however, misses the point in that the very functions of a capital market are viewed differently depending on the desired outcomes from the point of view of different actors. If 'a rose is a rose is a rose', a financial market should be unproblematic in its role and function in the circulation of capital (i.e. there is only a particular model to follow). But in reality, financial markets present different possibilities and serve different purposes for different groups. The central Chinese state and Shanghai government had particular understandings and visions of the financial markets in Shanghai; the local and foreign financial institutions in Shanghai were also 'framing markets' according to their own interests, agendas, experience and interpretations of what a market should be.

[4] At least according to neoliberal concepts of markets.

Table 7.7 presents a summary of the contesting visions held by the Chinese state and regulators on the one hand and foreign investors and international business on the other. In the case of Shanghai, finance capitalists and international business want financial markets that would allow them to raise capital quickly and efficiently, the ability to participate in markets that they deemed profitable or strategic, the ability to move capital in and out of the country easily, listing procedures that would improve the efficiency and corporate governance of listed companies, and clear and transparent laws and regulations that were compatible with international standards and systems. The Chinese regulators want financial markets that would finance cash-strapped SOEs, reduce long-standing reliance on domestic banks for financing, the prestige that an international financial centre with vibrant financial markets would bring, and also to control the pace and degree of change so as to manage systemic risk in the economic as well as social dimensions. Not all of these are necessarily conflicting aims, but the different visions of what the Shanghai financial markets should look like, what roles and functions they should perform, and more importantly, *how* it should go about developing the necessary capacities and infrastructures and *how quickly* it should do so, are sources of contestations.

Table 7.7 Different views on the functions of the Chinese stock markets

Chinese state & regulators	Investors
▪ Raise capital for SOEs ▪ Reduce reliance on bank loans for corporate financing ▪ Prestige ▪ Manage pace and degree of 'marketisation' reforms	▪ Improve returns on capital quickly and efficiently ▪ Freedom in market participation ▪ Choice of investment options ▪ Movement of capital in and out ▪ Improved corporate governance ▪ Clear and transparent laws and regulatory frameworks ▪ Ability to assess companies and investment

At the moment, although foreign investors are able to participate in the B share market and increasingly in the A share market through the QFII scheme, opportunities are still limited due to the lack of quality listings on the mainland (with many of China's top companies listing H shares and Red Chips in Hong Kong and N shares in New York) and restrictions on foreign exchange and capital repatriation. Chinese listed companies have been sliced and diced in the process of changing ownership of its constituent parts and to raise capital, but separate share markets for different share classes fail to promote fundamental changes in performance. This can only come about if the stock markets, through valuing all the company's shares, directly influence management decision-making, and this will only happen with greater shareholder interest in the company rather than in its short-term stock price performance. However, shareholder interest and power is constrained by the limited amount of tradable shares and, thereby, limited influence on the listed companies. The importance of accurately valuing companies should be, but has only superficially been, a crucial part of China's SOE reform programme. The stock market's current inability to clearly value listed companies is a consequence of the state's perpetuation of illiquid markets. The Chinese company, viewed through the prism of the various stock markets, is a fragmented entity that is hard to discern, difficult to value and unattractive to invest in.

A Chinese respondent who formerly worked at the SSE candidly admitted that financing SOEs and changing their ownership structures were the primary objectives in setting up the stock market. The result was that it emphasised financing but neglected other aspects of corporate and financial reforms that could have been pushed forward with the formation of capital markets:

> Of course that was the case when the SSE started. There was a problem… When we want to actually develop the stock market, we need to look into the objectives of

> development. Why do we want a stock market? One of [the reasons] is to serve the purpose of SOE reforms, provide finance capital for SOEs, so that they don't have to depend on bank loans but can also go to the capital markets. Another aspect is to change some operation and structure of SOEs. This is a good thing but the result was that it emphasised financing but neglected other aspects of reform. (Local SMG official: #27, 20 April 2006; translated from Mandarin)

Because raising capital for cash-strapped SOEs was the main objective, the approval process did not focus on a company's fundamentals but rather whether it needed capital. This resulted in a severe neglect of investors' interest and created lingering problems within the stock market that resulted in its lacklustre performance due to the perception of lack of quality companies, illiquid markets and problems of transparency:

> [The state] wanted to raise capital for companies; that was the objective. They were doing it for the companies, not for the investors. That kind of concept can create a lot of problems. In planning for a company listing, they were not looking at whether the company was doing well, but they were looking at whether the company needed money. If there were two companies, one company was doing very well with good plans for future development and required more capital for international expansion, and another company was not doing very well but it had many workers and if there was no cash injection it might go bankrupt, the preference would actually lean towards the one that is less efficient. Of course, that goes against economic sense. […] The regulators are aware of this problem and are beginning to cater more to investors. There are plans to revise the system, to change non-tradable shares into tradable share. We can see a clear general direction towards an international standard of stock market development. (Local manager for foreign bank: #11, 6 March 2006; translated from Mandarin)

From the Chinese central government's perspective, however, the stock market did fulfil its function (albeit with associated problems) of raising cash for

SOEs, diversifying the financial markets away from bank loans, and measures controlling the participation of foreign capital in the domestic capital market, and the release of non-tradable state shares and legal person shares onto the open market allowed regulators to control the pace of reforms, thereby controlling the fear of widespread social and economic (and thereby political) instability. A number of my Chinese respondents were careful to point out that social stability in China was of paramount importance and that financial stability was very much part of that process:

> The regulators are part of the government, and the government needs to ensure social stability, financial stability. Financial stability is part of social stability; if there is no financial stability, there is no social stability. If people lose money on some corporate bonds that are not capital-guaranteed, they will create trouble. They will bring it up with the government, because they have been approved by the government. […] So the people can complain that, 'You have approved this. We don't understand this but since you have approved it you must have the responsibility to protect our investment. If we can't get our money back…' then they will create trouble. So it is a matter of social stability. (Local vice-director of Chinese asset management company: #26, 18 April 2006; translated from Mandarin)

Corporate ownership reforms and capital market reforms thus had to be done at a particular pace and through specific structures that would minimise the risk of market instability, especially when this was an area that was still largely experimental. The goal of prestige, as identified in the opening quote of Chapter 6, might have been achieved to some small extent (as seen by the surge of interest and capital inflow into the A and B share markets in the early 1990s) but that had arguably been overshadowed by persistent problems with the Shanghai's segmented stock market and poor performance. By maintaining the divisions between state shares, domestic and foreign share structures, China was able to continue with its 'marketisation' reforms without eroding its constitutional command of the basic structure socialism with public ownership as the mainstay of the national economy. Moreover, a blending of domestic and foreign shares would increase demand on the full convertibility of the RMB on the capital account, which China was not ready to proceed with.[5] The concept of 'public ownership' remains the *raison d'etre* for the Chinese economic and political system and must be maintained, at least in some form. Capital market reforms thus have to address political concerns about 'selling off' Chinese 'public' companies (i.e. SOEs) to foreigners through public listings if shares are to be fully tradable. This argument was commonly used by my Chinese respondents (both in regulatory and financial business capacities) to defend the apparent shortcomings and failures of the Chinese stock markets and to emphasis the need for more time to put in place the appropriate measures and reforms:

> When the stock markets were first set up we were not in the WTO. You cannot say that [it] was wrong because perhaps the market did not allow for that. The market did not allow for a fully tradable structure, because that would mean selling everything! All the companies would get sold off! So you can buy and sell your shares, not the state owned shares, that's ok, that is not wrong. So it's political issues again. Now, if you talk about a stock market in North Korea, you don't have a stock market. Vietnam didn't have a stock market either and now they do. So this is a *process*, and you should not be too hasty. (Local manager of Chinese securities company: #35, 18 October 2006; original emphasis and translated from Mandarin)

So far, the Chinese regulators seemed to be 'winning' as they continued to hold the reins of financial reforms firmly in hand and even international business and finance capitalists had been remarkably patient. Much of that patience (or some might say tolerance) had to do with China's enormous market potential that nobody wanted to miss out on, such that China could afford to remain largely unmoved in the

[5] Other than with the 'gradualist' approach that it has taken as with reforms in all other sectors. The unpegging of the RMB from the US dollar to being weighted against a basket of four currencies on 21 July 2005 was seen as a small step towards RMB convertibility.

face of international pressure because it possessed a very good hand of cards. A foreign interviewee summed this up perfectly when he made the point that for all the problems and slow pace of reform, the Chinese market was so big and the opportunities were potentially so huge that firms and financial institutions could not afford to miss out on the action, even if there were better investment opportunities elsewhere. For all the restrictions, prohibitive capital requirements, onerous reporting requirements, confusing application process and opaque regulatory systems, China is China:

> I think Shanghai will be important in global terms but it's going to be a long time before it could really compete. Because markets like London or Singapore, which are regulated, but in a sort of free market way, are able to offer products, you know, sophisticated products and financial services without all the control, and I think it's just difficult. But having said that, you know, *China is China*. (Foreign manager of foreign bank: #37, 19 October 2006; emphasis added)

To sum up, the aim of raising capital from stock issues was clear, but other functions of a classic stock market – to improve transparency and corporate governance through the IPO process, to provide additional avenues of investment for the public, to diversify the financial system and spread risk – had been less evident.

7.3 WHOSE VISION: BEIJING'S OR SHANGHAI'S?

> *I mean, for a financial centre to form you need decision makers. And there are no… Look at all these buildings (gesturing out the window at the skyscrapers in Pudong) and there won't be a single – with the exception of a few foreign banks – there won't be a single CEO in any of them. I mean, with the regulator, exactly the same thing – there won't be a single decision maker here, they are all in Beijing. […] Of course the stock market, the stock exchange is here but it might as well be in Chongqing because so much of what's happening in Shanghai is controlled from Beijing, in terms of regulation. (Foreign analyst from foreign bank: #7, 22 February 2006)*

The above quote captured a general concern expressed by a number of (particularly foreign) respondents that I spoke to in Shanghai. We were sitting in the middle of the

impressive view of an array of

us (Figure 7.3). His observation,

d see in Shanghai was the product

of the SMG or were the reins of

government in Beijing, and what

***Figure** 7.3* Bank logos at Lujiazui *(Source: Author's own photograph)*

Politics and policies at the national level clearly played a vital role in affecting Shanghai's growth, development and policies pursued. A number of local respondents pointed out how the philosophy of regional development for the country as a whole had changed from Deng Xiaoping to Jiang Zemin to Hu Jintao, and how that in turn had influenced the rise of different regional economies in China. When Deng Xiaoping announced the Open Door Policy of China in December 1978, Shenzhen, Zhuhai, Shantou and Xiamen were earmarked as SEZs to take advantage of their geographic proximity to the overseas Chinese communities in Hong Kong, Taiwan and Macau and connections to other overseas Chinese (Cai and Sit, 2003, Yao, 1998, Crawford, 2000). Foreign investment was encouraged and new factories were established in these SEZs by offering tax privileges such as reduced import tariffs on raw materials and tax exemption for importation of certain capital goods. Shenzhen was the first SEZ in 1980 and it became the focus of Beijing's efforts to demonstrate the efficacy of its new international economic policies. It was partly because of its proximity to Hong Kong and partly because of special assistance from the central government that it grew from a small rural town of 20,000 inhabitants to an industrial city with a population of 10 million in 2005. Its economy was anchored by light industry, especially the production of arts and crafts, textiles, footwear, clothing, medicines and building material. The focus shifted to Shanghai and the Yangtze River Delta in the early 1990s when it was designated as the 'dragonhead' of the Chinese economy to connect a modern, industrial China to the global economy (F. Wu, 2000a, 2003). Unlike the earlier phase of development which focused on industrial production, Shanghai was to specifically develop its tertiary sector and its financial services industry in particular.

Regional development policies are not uncommon as economic development strategies but what is particularly interesting in the case of China is how much those regional policies are associated with particular leaders of the central government. The personality cult has significant influence on politics and policies in China which has to be considered when examining economic development strategies and outcomes. Echoing the sentiments of a number of local respondents that I spoke to, a Chinese manager of a foreign bank associated the development of each region with the visions of individual leaders during particular periods:

> Back then, Deng Xiaoping drew a circle on [the Pearl River Delta], and then Jiang Zemin drew a circle on Shanghai here. So now it seems that Hu Jintao has drawn a circle there [in Bohai]. Of course… it is difficult to say but, not that Shanghai will stop growing but I think it is possible that it will not be double-digit growth like in the past. Maybe things will slow down a bit. (#44, 27 October 2006; translated from Mandarin)

The Bohai Bay area in northeast China was earmarked in the early-2000s as the latest development zone, centered on the cities of Beijing and Tianjin. Its focus would be on developing trade and manufacturing capacities in areas such as pharmaceuticals, communications, iron and steel, machinery and agribusiness, and capitalising on its proximity to trading partners such as Korea and Japan.[6] Some interviewees saw this as a shift in attention (and resources) away from the south and Shanghai and towards the north. The northwestern parts of China, which had been relatively neglected in earlier economic policies (that focused on the coastal regions), had become increasingly important in national economic agendas since Hu Jintao assumed leadership. Such shifts had not gone unnoticed by business leaders and observers:

> During the 13 years of Jiang Zemin's leadership, that was when Shanghai grew most rapidly. Now, under the era of Hu [Jintao], Shanghai cannot be said to be growing slowly, but compared to previous years, it has slowed down. […] But this has to do with the philosophy of development for the country as a whole. Under Hu Jintao, the problem that he is most concerned about is rural development, development of western parts of China, sustaining China's economic development. He needs to consider all these things. So for coastal areas, you just have to maintain growth, no need to be as spectacular as before. So there is a big change in policy. (Local manager of Chinese financial institution: #9, 27 February 2006; translated from Mandarin)

[6] http://www2.tjftz.gov.cn/system/2006/10/05/010001281.shtml

The fact that Shanghai had always enjoyed strong political representation in the CPC and state hierarchy since 1949 had always been seen as a significant factor in Shanghai's economic success. Former president Jiang Zemin, President Zhu Rongji, former Vice Premier Wu Bangguo and current Vice Premier Huang Ju were all leaders of Shanghai (see Table 2.2). The connection was widely seen as useful, if not instrumental, to Shanghai's aspirations and development as a financial hub (Han, 2000, Yatsko, 2001). The situation, however, is uncertain now that the 'Shanghai gang' is no longer in power and Hu Jintao appears to have a different priority in focusing development in the northeast and northwestern parts of the country:

> Jiang Zemin was Shanghainese, so if you wanted to do something it was easier; now it's not that certain. So now if Shanghai is to go to the National State Council, the premier is Wen Jiabao, it is not certain whether Huang Ju can always do what he wants. And now the general secretary is Hu Jintao. So for many things, my feeling is that… it's not as smooth as before. In the past even if things have to go through PBOC, there is Jiang Zemin so when Shanghai wanted to get things done it was pretty quick. (Local manager of Chinese financial institution: #9, 27 February 2006; translated from Mandarin)

As mentioned in Chapter 6, the laws are passed from the central authorities in Beijing, be it the PBOC, SAFE, CBRC or CSRC. However, the regulations are implemented and interpreted by the local branch offices. This regulatory autonomy is an important consideration in understanding Chinese administration and policies. While the very generalised statements of the law from Beijing might be accused of being too vague and 'fuzzy', its lack of specificities allows for adaptation to local needs by local branches in the context of a huge country with widely varied regional and local political economies. As such, the local regulatory bodies have considerable power to interpret and implement policies to control the structure and pace of economic growth and development and this applies to the case of Shanghai. Therefore, while it is true that the ultimate decision-making as to what laws are passed are restricted to policy-making circles in Beijing, the authorities in Shanghai are given a lot of leeway in which to implement them and the fact that the headquarters of the regulatory bodies are housed in Beijing need not be seen as an impediment to Shanghai's aspirations. The branch offices in CSRC and CBRC offices in Shanghai have been given increasing levels of authority in their operations. New applications for products and branch licenses are also submitted to the local offices which are then forwarded to the Beijing regulators where the final decision is made. However, most of the communication process and liaising will be with officials in Shanghai rather than Beijing. According to a regulatory official who recently moved from Shanghai to Beijing, this is a trend that is set to continue as the regulatory bodies seek to improve their efficiency and service quality:

> [To] increase regulatory efficiency, and to be close to the market, the regulatory bodies have also delegated more authority to these [CSRC and CBRC] branch offices. Some former headquarter functions have moved here so the branches can just make their own decisions here. This is to increase the efficiency of supervision and approval process, and decrease the transaction costs of banks. For some things that have been delegated to the branch offices, regarding products… and reports, they just have to submit to the local branch office and that's fine. For other things like application for new business areas, status of the bank director and so on, that still has to be done in Beijing. (#25, 16 April 2006; translated from Mandarin)

On 10 August 2005, the second headquarters of the PBOC was inaugurated in Shanghai. Zhou Xiaochuan, a governor of the PBOC said that due to Shanghai's importance as a financial hub, the existing Shanghai Branch of PBOC often assumed a role of greater importance than a mere regional branch and this was a key consideration in establishing a headquarter in the city (Shandong Business Net, 2005). The Beijing headquarters will continue to run policy-oriented operations related to monetary policy, financial research, note issuance, statistical data and anti-money laundering while the Shanghai headquarters will focus on market-oriented and international activities such as regulating the financial market, conducting financial supervision, making financial and trust analysis, and coordinating regional financial cooperation. To further improve the central bank's management, it will also transfer some of its bureaus for payment and liquidation and national credit profiling to Shanghai headquarters over the next three years (*China Daily*, 10 August 2005). While the policies are still made in Beijing, the Shanghai headquarters will not only operationalise them but also play an important role in consolidating feedback from market participants in Shanghai and affecting subsequent policy changes. A local SMG official pointed out that the two headquarters will thus play complementary roles (#19, 10 April 2006). The establishment of the second headquarters is thus a highly symbolic act but also one with operational impact in highlighting Shanghai's mandate from Beijing:

> The central bank is still there [in Beijing], the main decision making unit has to stay in Beijing because it is the capital. That is normal. Moving a second headquarter here is indicative of Shanghai's development. A whole range of departments and services have been moved here. […] When you are operating in an environment where your business activities are restricted, you will have a poor impression… Because he thinks that what he can do depends on the policies from Beijing, and there is a problem with that simplistic understanding. Beijing has its policies which then allow Shanghai to pursue its own local policies. That is very normal. You have to understand it that way. It is not that Shanghai is not doing anything or it is powerless. The central government's objective for Shanghai to be a financial centre is confirmed, it cannot be changed, that's why [the second headquarter of PBOC] is

> placed here. (Local manager of Chinese securities company: #35, 18 October 2006; translated from Mandarin)

During my time in the field, there were also rumours circulating in the grapevine that the foreign reserves of the central bank might be moved to Shanghai; as the central bank had become the largest in the world its reserves required more effective management and investment, which was best done in Shanghai. This would further consolidate Shanghai's position as the national financial hub and boost the development of its financial markets and services.

As part of a tertiary industry that relies on the growth of and demand for financial and advanced producer services, the development of a financial centre in Shanghai is very much dependent on the economic growth of its hinterland. The Yangtze River Delta has been the fastest growing economic region in China for the last decade and this increase in production and trade activities has played a significant role in developing a market for financial services in Shanghai. Therefore, other than considering politics and economic development strategies at the national level, Shanghai needs to harness the growth potential of the regional economy in the neighbouring provinces of Jiangsu and Zhejiang, in order to build on and sustain its own growth and further develop the financial services sector and capital markets. A Chinese respondent spoke of the concept of Greater Shanghai:

> That means linking up Jiangsu and Zhejiang with Shanghai, to develop a regional economy. Finance has to be backed up by production. Without the support of production, finance is empty. So in order to develop Shanghai, you have to consider the development of Jiangsu and Zhejiang together as well. In the past, Shanghai tended to consider only its own economy but now you should think about how to harness the development of Jiangsu and Zhejiang, how to attract investment to this region. Financial services and flows may be in Shanghai but the production facilities

> are over there. (Local analyst of joint-venture financial institution: #48, 3 November 2006; translated from Mandarin)

On 10 December 2005, the Yangshan Deepwater Port in Hangzhou Bay, south of Shanghai, was officially opened. Expected to be fully completed in 2012, the new port will eventually have a container handling capacity of 15 million TEUs (20-foot equivalent units) with more than 30 berths. The Shanghai port had been fast approaching maximum capacity and its shallow waters prevented the docking of third and fourth generation containers. Since the 1980s, the SMG had been concerned about managing the ever rising trading volumes at the Shanghai port and Yangshan was conceived as part of Shanghai's ambition of becoming a shipping hub in Northeast Asia and to enable it to compete against other ports in the region such as Kao-hsiung in Taiwan, Busan in South Korea and Yokohama in Japan (*People's Daily Online*, 12 December 2005). The Yangshan Deepwater Port was expected to open up new opportunities for the logistics business in Shanghai and the Yangtze River Delta and was accorded a key role in promoting regional economic development of the Yangtze River into a so-called "Golden Waterway" (*People's Daily Online*, 15 June 2006). This growth in trading activities could only be beneficial to Shanghai's aspirations in developing its financial markets and services.

At the local level, the SMG was instrumental in developing the infrastructural capacities of Shanghai and Lujiazui (as detailed in Chapter 2) and in offering tax and other incentives to attract foreign financial institutions into the city. The SMG Office for Financial Services was tasked with specifically promoting Shanghai's financial centre to foreign investors and was also in charge of managing financial institutions owned by the SMG (such as the Shanghai Pudong Development Bank and Pacific Insurance Company). Officials from the bureau played an active role in attracting foreign financial institutions and would target specific companies to convince them to locate in Shanghai (rather than elsewhere in China). When Lloyd's of London was considering setting up an office in China, the bureau sent a team to London to offer advice and services, convincing them to locate in Shanghai (rather than Beijing) (local SMG official: #28, 20 April 2006). Lloyd's of London subsequently set up an office in Lujiazui, which was officially opened on 16 April 2007, specialising in reinsurance (*International Herald Tribune*, 2 March 2007, *The Independent*, 15 April 2007).

7.4 'MARKETISATION' THROUGH THE EXPERIENCE OF FOREIGN BANKS IN SHANGHAI

As prominent participants in the making of financial markets of Shanghai, the experience of foreign financial institutions as they set up and develop their business activities in Shanghai reveal the complexities of processes and relationships involved in instituting market practices, infrastructure and frameworks. In the rest of this chapter, I focus on the experience and perspective of foreign banks in Shanghai and how they make sense of and capitalise on the 'marketisation' process in China while being sandwiched between the demands of their head offices and the challenging regulatory and business environment in Shanghai. In section 7.4.1, I examine how foreign banks in Shanghai negotiate different visions of the Chinese market environment with their head offices before, during, and after their Shanghai operations were established. Section 7.4.2 deals with the roles and functions of foreign banks in Shanghai, as seen from the perspectives and agendas of foreign and domestic banks and the Chinese regulatory authorities. In section 7.4.3, I examine the business strategies of foreign banks in Shanghai, focusing on how they target different market niches and different clients depending on their firm-specific characteristics as well as how different expectations of foreign and local clients affect their business strategies and operation in Shanghai.

7.4.1 Between a Rock and a Hard Place? Contesting Visions of 'Market' Within the Organisation

Different visions of 'markets' are not only negotiated between different groups of market participants (such as between the Chinese state institutions and foreign investors) but also within an organisation spread across global economic space (see, for example, Schoenberger, 1997). The demands and visions of the head office, for example, can differ significantly from those held by representatives in Shanghai, who are often 'stuck' between the regulatory demands in Shanghai and having to convince their head offices back in Europe or elsewhere of the realities of the business environment in China. According to a foreign respondent from the London head office of a bank, one of the biggest issues faced by many foreign banks in setting up in Shanghai was convincing their head offices in the first instance, having to put together strategy papers and convincing the board of directors to approve a China branch or representative office. In spite of the market potential of the Chinese banking sector, in terms of the corporate banking market as well as the growing retail banking sector, there were substantial costs involved in terms of large capital commitment, fuzzy legal and regulatory environment and restricted business activities due to licensing rules:

> I guess if you've got a CEO who is very much Asia-focused and sees the potential in China, then it's an easy sell. We always say that sometimes selling internally is more difficult than selling externally, and sometimes that can be the case. So once the CEO has decided that he wants to move into Asia, he wants to move into China,

> then it becomes a lot easier. […] Building the business case can be… convincing people there is a justification for having a branch, because there are fairly substantial costs involved, that can be a difficult thing, having to convince the board. For a bank our size there are quite a number of levels to go through as well. (Head of department of a bank in London: #3, 12 December 2005)

Even before the banks encountered the minefield of Chinese regulatory requirements and the restricted business environment in Shanghai, those who were keen on pushing for a vision of the banks' presence in Shanghai had to get through the 'internal sell', after which they then face the difficult process of obtaining all the necessary regulatory approval with the Chinese authorities. A foreign interviewee in Shanghai, who set up a representative office there less than a year ago, spoke of the "hideous process" of getting into China due to the long list of requirements and the specific nature of those documents (#16, 9 March 2006) (see Table 7.8). A representative office had to be established for two years before a foreign bank could convert that to a branch office that could actually conduct business transactions. This required committing large amounts of capital into the country with a different amount for foreign currency or RMB lending, and for retail or corporate banking. Moreover, fresh sums of capital had to be committed for every single branch and new business licenses which increased the costs of building up a branch network in China to often prohibitive levels (foreign manager of foreign bank: #36, 19 October 2006). When talking about this process of setting up their overseas branches and representative offices in Shanghai and elsewhere in China, my respondents highlighted the significance of internal organisational politics within their corporations. They described the long, complex and sometimes frustrating process that they had to go through to make the business case for Shanghai to their head offices. In spite of its almost unquestioned potential, the China market still occupied a relatively small percentage of global business to these TNCs. As such, their requests to the lawyers, accountants, board of directors and chief executive officers in their global headquarters were not always met with the most prompt or favourable responses and they had to be very persistent:

> To try to collect a board resolution from a FTSE100 company, where the CBRC actually want to see these documents, they actually want to get a letter from the group of chief executives, to get notarised copies of the documents that you would require to submit… it's *incredibly* difficult to actually bring that together. Because also, whilst it is important because we've never had a presence in China, in terms of economic reasons, for a company that makes just under £4 billion in profit, this is a drop in the ocean. So getting the attention of our group legal people, to say, 'Ok, I need this and that' is very difficult. So it was quite a challenge actually. That was probably one of the biggest challenges, actually submitting the application. […] There isn't much room for manoeuvre. […] It's interesting when you're negotiating with your group legal people and you say that the CBRC require a letter from our regulators, a reference letter essentially from the FSA. And then they would come back and say, 'Oh they don't want all that. They want this, this and this, that will do the job'. And I would go… '*No*. The *CBRC* has asked for this letter and that is what they want'. […] Yeah, don't try to be clever, don't try to deviate from that. Just give them exactly what you've got. (Foreign representative of foreign bank: #16, 9 March 2006; original emphasis).

Table 7.8 List of documents required to apply for a bank representative office in China

1. Application form for Establishment of Representative Offices of Foreign-Funded Financial Institutions in the People's Republic of China
2. Notarised business license
3. Articles of association
4. Name list of Board members
5. Shareholder list of the Bank
6. Annual reports for the last three years
7. Opinion issued by Financial Services Authority in connection with establishment of Representative Office in Shanghai, China by the Bank
8. The identification, academic certificates and resume of proposed chief representative
9. A statement of a clear record signed by proposed chief representative
10. Notarised Power of Attorney for the appointment of the chief representative
11. Anti-money laundering policy of the Bank
(Source: From interview respondent #16, 9 March 2006)

Even after the foreign bank had set up in Shanghai, the representatives had to constantly explain the peculiarities of the Chinese system to those back in the head offices when it came to dealing with cross-border payment and other business activities when they ran up against Chinese regulatory restrictions that were unfamiliar to those in other regulatory environment. The non-convertibility of the RMB was one of the most common issues that had to be explained as what would have been a very simple transaction could become problematic due to currency controls:

> [C]oming from Europe and especially from the Netherlands, seeing all these regulations really feels like, 'Huh? Is it possible that the government interferes in these kind of things?' It's so unnatural… It doesn't make sense, it completely does not make sense for Europeans that RMB is not freely convertible. I have to explain that every time because people say, 'Well, you [can] just send some money…'. 'No… It's not possible!' […] For me, it's very important in my normal working life, I explain it at least once a day. Because people just don't understand. (Foreign manager of foreign bank: #46, 2 November 2006)

Other respondents also talked about the onerous compliance – reporting and documentation – process that was endemic to the Chinese administration. A significant cost of business for foreign banks in Shanghai was reporting, having to comply with both Chinese as well as home country reporting obligations. This required two or more languages and applying two countries' accounting rules and was very time-consuming and costly. In comparison, domestic Chinese banks only had to comply with one language and one set of accounting rules. They also had to comply with the multiple steps of documentation that would not exist elsewhere due to the preference for paper-copies in China and the importance of maintaining control through administrative procedures. A foreign respondent elaborated on how simple transactions that are conducted electronically or 'invisibly' in Europe would be split up into multiple steps and complicated with multiple signatories and copies:

> The payment form that's signed by the customer is quadruplicate, because one copy has to be for the bank, one goes to the customer, one probably goes to SAFE and the other probably goes to someone else. You can't do electronic banking here the same way as you do in Europe in terms of payment and things like that because you can't get the documents signed if you're using [an] electronic payment system. […] First the request is signed off by the company, then the signature is verified, then it's signed by the assistant who checks the balance of available funds and so on, then it's signed by the compliance officer who makes sure that they've got the appropriate documentation, and then it's signed by the manager who authorises the payment on basis that all the checks have been done. Whereas abroad, the payment would just go in and out without even being seen by anyone because, you know, the computer will tell you if there's a balance on the account or whatever. So in that sense it's a lot more onerous and paper-based. (Foreign manager of foreign bank: #37, 19 October 2006)

A number of my respondents revealed how they were often at pains to explain the business situation on the ground to “headquarter tourists” who often flew in for a few days and judge the business opportunities from the impressive exterior of Shanghai’s urban development and went away with erroneous assumptions of the business environment in China. Judging by the numerous skyscrapers plastered with logos of TNCs and financial institutions, the developed transportation network and array of upmarket restaurants and hotels, these “headquarter tourists” would conceive of very different visions of ‘market’ in Shanghai (and projecting that to the rest of China) compared to their counterparts based in Shanghai who had to wrestle through regulatory ‘grey areas’ and various restrictions placed onto their business operations:

> They came here to Shanghai to a conference by business class, was shuttled from the airport directly to five-star hotel, have a wonderful conference with decent food… […] Have a wonderful party at night at one of these really posh places, and then they go back by the shuttle to airport and then they think, ‘Ok, I know China, must be quite easy doing business there’. And that’s not what is happening. (Head of department in foreign bank: #42, 27 October 2006)

> People come here, they come to Jin Mao [Tower], they fly to Pudong, they take a car to Jin Mao, they go to the Hyatt, leave their suitcases and come down to the office and say, ‘Oh, I see a sea of opportunities! It’s got to be great! Why don’t you sell more?’ It’s like, ‘Erm, this is *not* China *at all*!’ (Foreign manager of foreign bank: #46, 2 November 2006; original emphasis)

One respondent was careful to point out, however, that it was important to have these visitors from the head office because he was keen to make them understand the kind of environment he is working in. But such visits took up a lot of time and did not particularly add to his day to day operation in Shanghai (foreign chief executive of foreign TNC: #31, 13 October 2006). Another interviewee gave an account of how she was anxious to prepare a presentation to the CEO of her bank, "I was really thinking how I could use that time to get [across] the message 'This. Is. Not. China.' This is basically my message, give us time, things are slower here, things are different, but this is not China" (foreign manager of foreign bank: #46, 2 November 2006). Circumstances were such that the CEO was stranded at an airport in Guangzhou due to a storm and his Blackberry device had stopped working. He tried to get himself booked onto a different flight but nobody could understand him due to the language barrier. In the end, he resorted to drawing two airplanes on a piece of paper and drawing arrows to get his point across. He eventually arrived in Shanghai too late for a presentation but his personal experience was enough to impress upon him the difficulties of day to day operation in China, not to mention specificities of the business and regulatory environment:

> So he came here very late so we couldn't do the presentation anymore. But in the end he was here and we had dinner and he said, 'I'm only here for a few hours now but I think I saw a good piece of China. I do understand that it's not that easy for you.' So I thought, [that] saved me, well, [a] one-hour explanation on the differences and things like that. It's really good. (*Ibid.*)

7.4.2 'Kicking' Local Banks into Shape: The Roles of Foreign Banks in the Shanghai Banking Market

> *There are 60 foreign banks, I think, in Shanghai, branches and rep offices and stuff like that. Sixty branches, I think, yeah. And why are they all here? I mean, they are not all here because they can do business, they are not all here because they can make profits; they are here because it's China. Because someone somewhere says they have to be here. I think, the China Dream as such, everybody is chasing the end of the China rainbow and the pot of gold is not there for a lot of these guys. (Foreign president of foreign bank: #20, 11 April 2006)*

With the numerous business restrictions and difficulties of setting up in Shanghai, foreign banks were clearly there for strategic reasons and with a long-term view.

Many of them were not making profits and the representative offices (that had not fulfilled their 2-year term before being allowed to apply for a branch license or those who preferred to maintain that representative status) were definitely not making business transactions. The ‘China Dream’, however, was compelling and foreign banks were keen to get a slice of the growing financial markets, whether that was in corporate banking, retail banking or structured financial products.

A number of foreign respondents pointed out that it was still an elementary market in Shanghai in terms of banking and especially in terms of capital markets. The range of products on offer was limited due to foreign exchange and other restrictions and, as mentioned in Chapter 6, banks were limited as to the types and amount of business that they could do due to licensing restrictions and quotas set by regulatory bodies like SAFE. With such limited business opportunities (at least thus far), a number of foreign banks had entered into strategic partnerships with local Chinese banks by buying minority stakes. Table 7.9 shows a list of foreign banks and their percentage shares in Chinese banks.

Table 7.9 Foreign banks buying into Chinese banks

Chinese Bank	**Foreign banks/institutional investors (headquarters) and their equity stake**
Bank of Beijing	ING Group (Netherlands) 19.9%
Bank of China	RBS (UK) 5.16%; Merrill Lynch (US) & Li Ka-shing (Hong Kong) 5%
Bank of Communications	HSBC 19.9%
Bank of Shanghai	HSBC (UK) 8%
Bohai Bank	Standard Chartered (UK) 19.99%
China Construction Bank	Temasek Holdings (Singapore) 5.1%; Bank of America (US) 9.1%
China Industrial Bank	Hang Seng Bank (Hong Kong) 15.98%
Hangzhou City Commercial Bank	Commonwealth Bank of Australia 19.9%
Industrial and Commercial Bank of China	Goldman Sachs 10%
Jinan City Commercial Bank	Commonwealth Bank of Australia 11%
Minsheng Bank	Temasek Holdings 4.55%
Shanghai Pudong Development Bank	Citigroup (US) 19.9%
Shenzhen Development Bank	Newbridge Capital (US) 17.89%
Tianjin City Commercial Bank	ANZ (New Zealand) 19.9%
Xi’an City Commercial Bank	Bank of Nova Scotia (Canada) 2.5%
Sources: (Time, 2005, Times Online, 2005)	

The bad publicity that had dogged Chinese banks for decades regarding bad loans, and senior managers imprisoned for embezzlement and fraud was indicative of management and financial problems in Chinese banks and having the input of foreign partners was hoped to help turn things around (International Herald Tribune, 2007). Foreign investors brought capital, management skills, modern lending practices, new products and internationally accepted standards of corporate governance. For foreign banks, having an established local partner could cut down on the time, effort and money needed to build a network of branches and attract customers. Their interest was in using the partner bank in China to distribute financial products and services that would be very difficult for them to do on their own; they could make use of the enormous local branch networks of the Chinese banks and client base to break into the (previously closed) consumer markets such as in insurance, credit cards and mutual funds (Figure 7.4). These investments also allowed foreign banks to learn about the market and gain experience that could be applied to building their own brand in China.

Figure 7.4 An advertisement in Shanghai featuring credit cards issued by HSBC and Bank of Communications (Source: Author's own photograph)

For the Chinese banks, they benefited primarily from the large capital injection brought in by foreign banks through the purchase of equity stakes of up to 19.99 percent (the current legal limit in domestic banks). This much-needed capital helped to settle outstanding non-performing loans and get the Chinese banks up to a better footing for public listings and developing other financial products and services. Apart from capital injection, the transfer of skills and management styles, exposure to different corporate cultures, philosophies, and international standards were also highlighted by my respondents as valuable benefits. A number of my Chinese respondents also pointed out that having a well-established international bank as a partner or stakeholder helped to boost the reputation and brand recognition of the local bank, which was particularly useful for its public listing and internationalization strategies. Two interviewees used the example of how Bank of Shanghai, a relatively small Chinese bank compared to the Big Four state-owned banks, benefited from its partnership with HSBC, and this was true even for a large bank like Bank of Communications (BOCOM):

> The main customers of Bank of Shanghai used to be small savings account holders and small businesses in the city. And then it entered into talks with HSBC a few years ago. […] So after selling 20 percent to HSBC, they can say to customers that, 'We are together with HSBC'. It is the same with BOCOM. That will increase the value of its brand name as a bank. […] So if a foreign bank invests in you, what it says is that, they [the foreign bank] decided that my company is valuable and attractive and worth investing in, based on fair and advanced valuation techniques. So, HSBC decides to invest in me because my company is worth investing in, it has good value and is a brand that can be trusted. (Local manager of foreign TNC: #12, 6 March 2006; translated from Mandarin)

> You see, for BOCOM, only people in China know about BOCOM. But HSBC is known internationally. […] So when they (BOCOM) go to the US, they can say that our shareholder is HSBC. (Local manager of foreign bank: #11, 6 March 2006; translated from Mandarin)

Foreign banks therefore played an important in the 'marketisation' process by accelerating the pace of change, and bringing in skills, knowledge and best practice, for example, in compliance, pricing systems and risk management (as detailed in Chapter 6). Their very presence in the market changed the terms of competition and also increased the pressure on local Chinese banks to speed up their financial and management reforms in order to not lose their customers to foreign competitors. The fact that foreign banks were still very much restricted in terms of the products and services they could offer gave local banks some breathing space to bring themselves up to par without the dangers of having domestic banks collapse in the face of foreign competition (an outcome that was politically and socially unacceptable in a Socialist-market Chinese economy). A local interviewee also concurred with the value of foreign competition in terms of skills and knowledge transfer as well as in fostering creativity and product innovation:

> When the foreign banks come here, they bring with them their concepts, capital, management, and that will be a good thing for the development of the capital markets here in the long term. Otherwise [the service of domestic banks] is too sub-standard! There are many things they cannot do. There was no pressure from competition. Now with foreigners in here, there is the element of competition and they have to survive, that will naturally create the desire for creativity and innovation and so on. […] that should be the way to go. If you don't know what the international trends are, how can you interact with other people and how can you innovate? (Local analyst from Chinese securities company: #34, 17 October 2006; translated from Mandarin)

A couple of my foreign respondents were, however, more blunt in their assessment that foreign banks were being used by the Chinese regulators to 'kick the local banks' into shape and to force reforms. One of them put it as such:

> The bottom line is actually very simple: China wants to open up the banking industry, at the same time they have to protect the local banks. The only reason they want to open up the banking industry is not because they like foreign banks – it is to use the foreign banks to kick the local banks to reform. Because the regulators' only interest, the key objective they have, is to have a strong banking system in China that is controlled by local banks. That's the objective. The way to make it happen is,

> unfortunately, to allow foreign banks to come in to kick the local banks, because they will not reform by themselves. That's what they tried to do last 30 years, doesn't happen. Reform only happens when there's pressure from outside. (Foreign country head of foreign bank: #43, 27 October 2006)

There continued to be some simmering resentment or grumbles amongst foreign banks about the numerous restrictions placed on them while recognising that the Chinese state and regulatory bodies were clearly operating in the interest of domestic banks. By allowing foreign banks to purchase small stakes in domestic banks, foreign investors were offered a small channel through which to enter the Chinese market (since their organic expansion was severely constrained by capital requirements and licensing restrictions) and many Chinese banks had been snapped up. The foreign banks might have been able to gain a foothold on the Chinese market through this route but a number of respondents questioned the wisdom of buying into local banks, whether having a minority stake with little power on the board of directors and management was worth the risk of taking on bad debts and a corporate culture that they knew little about. The benefits to such partnerships were clearly geared towards long-term interests of developing further banking relationships and brand recognition in China. For the Chinese banks, on the other hand, the benefits were more immediately evident in the form of capital injection and transfer of skills and expertise in management styles, systems improvement and product design. The plan was to bring the Chinese banks up to par as quickly as possible so that by the WTO deadline at the end of 2006, when the banking industry was to be fully opened to foreign banks, local banks would be able to at least survive even if they could not compete effectively as yet.[7] Therefore, while the foreign banks were welcomed to

[7] Although as noted in Chapter 6, non-tariff barriers had been put in place to so the 'theoretical' level playing field had not worked out as such in practical terms for foreign banks even after the WTO

improve standards and practices and allowed to place competitive pressure on the local banks, they could not be given too much freedom to compete in the market in case local banks collapse under the pressure:

> We are allowed to kick [the local banks] but we cannot kick them too hard because they will fall over! So that is the balance, you have to allow foreign banks to kick the local banks by giving them products and making them competitive and allowing them to enter into the market but not too competitive because the [local] banks will fall over. (*Ibid.*)

The Chinese regulators could not force the local banks to undergo reforms on their own and needed the help of foreign banks to kick the local banks into shape through competition. This should also mean that they would be careful not to drive the foreign banks away through too much regulatory bias. Therefore, while the regulators needed to maintain a balance of allowing foreign banks to pressure local banks without the latter being crushed, they also had to maintain a balance of restricting the activities and limiting the success of foreign banks in the Chinese market without driving them away through the lack of business prospect. Therefore, with reference to position papers written by a banking group to press the CBRC and PBOC for further liberalisation of the banking sector to foreign financial institutions, a foreign representative of a foreign bank commented that there would be greater political will to grant concessions to foreign pressure if foreign banks were on the verge of abandoning the Chinese market:

> The overriding principle is to what extent are foreign banks allowed to compete with local banks. Basically we are too effective so everything that we say will not be honoured. If foreign banks are *dying*… at the moment of leaving China […], which was the case maybe 5 years ago because we didn't see any hope, at that moment…

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deadline. Such barriers in varying forms are expected to persist for the next few years, or as long as it takes for the domestic Chinese banks to complete their reforms.

> [… If the] foreign banks will leave the country then they'll think, well, there's no one to reform the local banks. *Then* they will look at the position paper and make some changes. But at the moment there is no political will to help us because they have helped us too much already, it's the politics. (#45, 1 November 2006; original emphasis)

On the other hand, the regulators could not be seen to be giving too many incentives to foreign financial institutions as that would rouse the ire of locals who felt that Chinese interests should be prioritised. This sentiment was echoed by one of my Chinese interviewees who felt that perhaps too much concession had been given to foreign investors that local institutions should be more entitled to:

> You have to give many incentives to attract foreign investors in here, give them many things. Actually, looking at our development to date, there is no reason why we should give so many things to other people. We have so many people who need… we should be giving to our own citizens. If anything, we should favour our own citizens instead of foreigners. So even if we do give [special treatment], it should be given slowly, slowly. That's how I feel. (Local analyst from Chinese securities company: #34, 17 October 2006; translated from Mandarin)

Therefore, the roles accorded to foreign banks in Shanghai, as permitted by regulatory and licensing rules, had to be carefully balanced to address the desire of the foreign banks to exploit the business opportunities in China, the need of the domestic banks to implement practices and obtain the necessary skills and knowledge to compete effectively in the Chinese and international financial markets, and the interests of the regulators to use the foreign banks to force local banks to reform without seeming to favour or neglect either sets of market players. This balance was constantly shifting in response to the pace of change within the organisations themselves as well as to external events such as the WTO commitments, regulatory changes and general economic and capital market environments which affected the performance, strategies and outlook of local and foreign financial institutions. If greater access was given to foreign banks to enter previously closed markets (such as being allowed to offer financial services in RMB and to retail customers instead of being restricted to foreign currency business and corporate customers), another restriction might be imposed (such as SAFE restrictions on borrowing money from abroad) to slow down the business expansion of foreign banks, in order to protect the local banks. If the pace of reforms and 'marketisation' was too slow and regulators were getting feedback from foreign financial institutions that they were no longer optimistic about their future development in the Chinese market, some concessions might be made to allow more products or services to be offered, or reduce some other regulatory requirement to placate foreign investors and convince them that it was worth their while to stay on in China in spite of currently unfavourable circumstances. This balance thus had to be constantly (re)negotiated with changing circumstances and with an eye on the long term goal of developing Shanghai as a financial centre with developed banking and capital markets supported by a strong base of domestic financial institutions as well as a wide range of foreign financial institutions.

7.4.3 Making the Most of Market Niches: The Strategies of Foreign Banks in Shanghai

There are currently around 65 to 70 foreign banks in Shanghai (figures vary according to the banks' status of application and registration) and Table 7.10 shows a list of those registered with the CBRC in 2005. While this does not seem like many compared to Tokyo, London or Hong Kong, it borders on overcrowding when one considers that business operations of foreign banks are still very much limited even in Shanghai (still the most open city in China). Many large foreign banks had been given RMB licenses that would allow them to conduct RMB business with local corporate clients, but they still could not issue credit cards, invest directly in capital markets or offer risk management products without going through a local bank or financial institution (through joint-ventures or using the latter as agent banks). Local and foreign financial institutions were still subject to regulatory bias in spite of the WTO-level-playing-field rhetoric, so much so that some market participants had described the system as ‘one country, two banking systems’. An interviewee from a UK bank confided that:

> [Foreign banks in Shanghai] say that most of the branches aren’t making any money. I guess they probably just break even or something like that […] So when WTO kicks in […] there should be some relaxation, which would then allow foreign banks to do RMB lending. Which at the moment is quite restricted. And *that's* the market that everybody is eyeing. Everybody s going in the market now thinking, ‘Well, OK, I’ve got potentially a short-term loss here, I have to run some operational losses with a long-term future.’ So everybody is looking at it, ‘Right, 2006, WTO...’ In practice whether that actually happens or not remains to be seen. (Head of research at a London bank: #3, 12 December 2005; original emphasis).

Table 7.10 List of foreign banks in Shanghai and their country of origin (as of 2005)

ABN Amro (Netherlands)	Intesa Bci (Italy)
Australia and New Zealand Banking Group (Australia)	JP Morgan Chase (USA)
Banca Di Roma (Italy)	KBC Bank (Belgium)
Banca Intesa (Italy)	Korea Development Bank (Korea)
Bangkok Bank (Thailand)	Korea Exchange (Korea)
Bank of America (USA)	Maybank (Malaysia)
Bank of East Asia (Hong Kong)	Metropolitan Bank (USA)
Bank of Montreal (Canada)	Mizuho Corporate Bank (Japan)
Bank of New York (USA)	Natexis Banques (France)
Bank of Nova Scotia (Canada)	Ningbo International**
Barclays Bank PLC (UK)	Nord/LB (Germany)
Bayerische Landesbank (Germany)	United Overseas Bank (Singapore)
BNP Paribas S.A. (France)	Norddeutsche Landesbank (Germany)
Business Development Bank (Germany/Thailand)**	Overseas Chinese Banking Corporation (Singapore)
Calyon (France)	Pinan SH*
Chai Tai Finance*	RaboBank (Netherlands)
Citibank (USA)	Raiffeisen Zentralbank Osterreich AG (Austria)
CITIC Ka Wah Bank (Hong Kong)	Royal Bank of Scotland (UK)
Credit Suisse First Boston (UK)	Sanpaolo IMI S.p.A. (Italy)
Dah Sing Bank (Hong Kong)	SEB (Sweden)

Development Bank of Singapore (Singapore) Commerzbank (Germany) Deutsche Bank (Germany) Dresdner Bank (Germany) First Sino Bank (Taiwan/Hong Kong/China) Fortis Bank (Netherlands) GE Finance (UK) Hana Bank (Korea) Hang Seng Bank (Hong Kong) HSBC (UK) IBPS Alliance Bank (UK) Industrial Bank of Korea (Korea) ING Bank (Belgium)	Shinhan Bank (Korea) Société Générale (France) Standard Chartered (UK) Sumitomo Mitsui (Japan) Sumitomo Trust (Japan) Svenska Handlsbanken Tokyo-Mitsubishi (Japan) Bank of Tokyo-Mitsubishi UFJ (Japan) Wachovia Bank (USA) Westdeutsche Landesbank (Germany) Woori Bank (Korea) Wing Heng Bank (Hong Kong) Wing Lung Bank (Hong Kong) Xiaman International (Hong Kong/China/Japan/USA)**
** Information not available ** China-incorporated foreign bank Note: This list does not include representative offices Based on: (Metcalfe, 2005), CBRC data from interview respondent*	

However the attractiveness of the Chinese market was such that foreign banks had not simply packed up and left; in fact, more were entering every year. In the current regulatory environment, possible strategies include: i) to sit and wait (either maintaining a representative office or keeping to current levels of business activities permitted) until China further opens up its financial markets, ii) move into niche markets and iii) expand by way of merger or co-operation with a domestic bank. Most banks employed a combination of the above strategies, such as concentrating on specific market or product niches or enter into joint agreements with domestic banks, while waiting for regulatory and market changes.

A number of foreign banks had opted to expand their business opportunities through cooperative agreements and joint-ventures with domestic banks, often by taking minority stakes (see Table 7.9). This trend had been particularly prominent over the last 3 years. For most foreign banks, however, their key strategy was to focus their limited capital and human resources on specific market niches based on their country of origin, product expertise and/or existing client base. This specialisation in market niches could be seen in terms of a) products, b) sectors, and c) client base. Only a few very large foreign banks (such as HSBC, Standard Chartered and Citibank) were keen on being active in all sectors of the banking market to offer a comprehensive range of banking services; most other foreign banks that I spoke to preferred to focus on specific product areas such as corporate or wholesale banking, trade financing or SME financing as their specialty. Many foreign banks went into China as a result of following up on client relationships elsewhere. In the 1980s and 1990s, many companies from the developed economies were moving production facilities and opening new branches in China due to new market opportunities and their banks followed in order to maintain those client relationships and as business opportunities began to develop for them as well within China. An interviewee based in London pointed out the simple fact that, "We've got a global customer base; the customers are going to China. […] If [the companies] are there in China and we are not there as well to support them, opportunities are going to go elsewhere" (Head of department in London bank: #3, 12 December 2005). In following these corporate customers, the foreign banks therefore tended to focus on banking products that they were most familiar with in wholesale/correspondent banking such as trade finance, loans syndication, structured lending, and mergers & acquisitions. Other than specialising in particular financial products and services, many foreign banks also capitalised on sector-specialisation due to their expertise and experience on finance and market research in particular sectors elsewhere in the global economy. This sector approach enabled banks to provide clients with in-house sector expertise and to combine that with extensive product knowledge available across their organization network worldwide. Some of the foreign banks that I spoke to specialised in areas such as the aerospace industry, agriculture and agribusiness, food and beverage industry, construction and building materials, transport and logistics and SME financing.

The third area of specialisation was in terms of client base. Many of these foreign banks (particularly the smaller ones) moved into the Chinese market with the expressed mandate of servicing their existing clients from their home countries. An Italian bank that I interviewed, for example, focused on servicing its Italian clients in Shanghai and the surrounding provinces of Suzhou and Zhejiang. Some smaller German banks that I spoke to also focused on their clients from Germany who had already entered or were considering entry into the Chinese market. One of the German banks, for example, had a specific German desk to concentrate on attracting and retaining German clients. This country-specific focus tended to be particularly prominent for the non-English-speaking client base. For corporate customers who were not fluent in English (or Mandarin), they faced additional difficulties apart from the normal hurdles already faced by counterparts from the US, UK and other English-speaking countries. These banks therefore sought to provide a value-added service in consultancy and business services by capitalising on their country and linguistic advantage:

> That's the reason why [the new head of German desk] is on board. In all countries of this world, despite the globalised world, people, customers who are not as fluent in a foreign language just tend to like to speak in their mother tongue. (Foreign manager of foreign bank: #41; 27 October 2006)

Even with the above strategies of market specialisation in terms of products, sectors and client base, some foreign banks still found it difficult to sustain their business operations in China. Due to currency and licensing restrictions, there was a mismatch in terms of the types of financial services that corporate customers required and what the foreign banks could provide. An Italian bank, for example, could not offer RMB lending services to its potential clients as it was still in the three-year waiting period of applying for the requisite license. This reduced its business opportunities while at the same time increased the pressure of having to be profit-making for two out of those three years in order to meet the criteria for a RMB license:

> Since I came here I've visited maybe 30 or 40 large foreign corporate that have business in China. We've done very, very little in terms of business with them because essentially what they do in China is they need local currency […] because they need to pay their local suppliers, pay their salaries and pay their rent and things. [F]or a lot of the foreign corporates who are our target, whether it be Carrefour or Decathon or Michelin… They only want local currency. (Foreign manager of foreign bank: #37; 19 October 2006).

Due to the various business restrictions, high capital requirements for banking licenses, and onerous application process, some foreign banks opted to maintain a purely research and consultative role (for existing home customers), or to service Chinese banks and enterprises going abroad (capitalising on their global network) without actually conducting business in the monetary sense. This enabled them to adopt a wait-and-see attitude, monitor market and regulatory changes as they planned their next move, while maintaining linkages with existing clients moving into China.

For foreign banks that had started breaking into the local market, they also had particular strategies for targeting certain types of Chinese corporate clients. Traditionally, most Chinese banks would only extend loans to large SOEs and SMEs in China would find it very difficult to secure business loans as domestic banks were unwilling to take the risk without government backing. One of the foreign banks that I interviewed spotted this neglected sector and established itself in Shanghai to provide corporate banking services to this niche market. This was, however, a rather unique case and most foreign banks that just started to move into the Chinese corporate banking market still prefer large SOE clients due to perceptions of risk and the difficulties of assessing Chinese companies. Most interviewees claimed that the foreign clients that they worked with tend to have more transparent accounting practices and records and since they often already had existing client relationships elsewhere in their global network, the banks would already have some knowledge of their group financial data and status. These established relationships and history of engagement enabled the banks to have greater confidence in their foreign corporate clients while they often felt a great deal more uncertain about local companies. A respondent from a foreign bank that had established itself in Shanghai a few years ago explained that:

> Initially when you go into a market, you probably look at foreign companies as a base. Either joint-ventures or multinational corporates would be where foreign banks would go to. Mainly because in China we probably can't get comfortable with the credit, because the annual report and accounts, we don't know how accurate they are. So until we get to a stage where the country produce internationally… you know, accounts to an internationally accepted standard, [unless] something like PWC [PricewaterhouseCoopers] or whoever is auditing the accounts [otherwise] it's probably difficult for a bank like ours to get comfortable with that. You might find that some of the Hong Kong banks that are based in China or HSBC who has been there a long time, or Standard Chartered, will have a slightly more relaxed view than ourselves. But I know that even they are quite cautious in terms of the sort of local corporate exposure that they will take on their books. (Director from a bank in London: #3, 12 December 2005)

The lack of standardised accounting practices within China was another issue of concern for foreign banks in dealing with Chinese corporate clients. Compared to foreign corporates who applied international accounting standards (IAS) and were often audited by international accounting firms (which was seen to increase confidence and reliability of the numbers reported), Chinese companies often had rather ad hoc approaches to accounting practices that were not easily comparable and rendered the process of assessing risk and rather opaque, at least from the perspective of foreign banks. A respondent who worked in corporate relations explains that for foreign companies:

> [a]ll their financials are very… transparent, and audited by international audit firms. For local firms the situation varies. Some of them apply international accounting standards or this kind of standard, but for many others they do not have a very long financial history for you to track, their credit risks, their performances… […] And if they are not listed companies, their accounting, their accounts may not be audited by a national audit firm, so… we can say that the reliability and the transparency is lower. (Local vice-president of foreign bank: #14; 7 March 2006).

Another respondent compared the accounting standards between established foreign client and potential Chinese clients:

> For the German companies you have your long lasting established relationship, you have the respective laws in place where you can rely on guarantees, collaterals etc. If you have a new Chinese client, you cannot rely on the financial, you know, there two or three statements they produce, one for the tax, one for the auditors, one for the company itself, for the investors, and maybe one for the shareholders… it's very, very tough. It's Chinese accounting standards, they have Chinese characteristics. (Foreign manager of foreign bank: #41, 27 October 2006)

Due to what is deemed their incompatibility (or incomparability) with accepted 'international' standards, these unique "Chinese characteristics" were seen as problematic in hindering accurate assessment of accounts and valuation of companies on the part of foreign banks who were unfamiliar with the local environment and frameworks.

Other than the questionable reliability of accounts and statements, the documentary process with Chinese corporates was another issue. A Chinese respondent who had corporate dealings with both foreign and local banks in Shanghai pointed out that many Chinese clients were not used to what they saw as overly strict interpretation of laws. This was perhaps related to the regulatory style in China whereby broad laws and guidelines were established by central authorities which were then interpreted and enforced by local authorities with a great degree of flexibility to local contexts as well as on a case-by-case basis. Chinese clients of foreign banks often had the impression that foreign banks were too strict in enforcing all the rules with little 'flexibility' and interpreted that as poor customer service or bureaucracy:

> There is also a difference in culture between local and foreign banks, different concepts of service and operation. For foreign banks, their valuation of corporates and requirements… internal management methods, they are more strict. Some [local] customers may not be able to accept this, thinking that they are too strict and should be more relaxed or flexible. […] For foreign banks, they operate and adhere very strictly to the rule of law as laid down by the regulators. But for local banks… Foreign banks are very, very careful, but the local banks are different. […] For foreign banks, white is white and black is black. But for local banks there are more grey areas. (Local manager for foreign TNC: #12; 6 March 2007; translated from Mandarin)

He went on to give an example of how a local bank might bend the rules for a Chinese client in requiring only three documents instead of five, while the foreign banks, who were anxious to keep on the good side of the Chinese regulators, would stick by the rules and insist on five documents, or even request for additional documents as a safeguard in an unfamiliar business environment. This would frustrate potential Chinese clients whose expectations of superior customer service with a foreign bank were then dashed by what they see as unnecessary and complicated requirements:

> [For certain transactions, banks] have to fulfil some legal requirements, have to submit various forms and accounts. But for local banks, they may only require you to submit three documents, even though the legal requirement is to submit five. But for HSBC or Citibank or Standard Chartered, they will stick with the five documents requirement, or they may even ask for five, including a letter of guarantee or something. [The customer may then complain] 'Hey, why is it that when I was dealing with ICBC in the past I only needed to give 3 documents? Why is it so much more troublesome with you?' Trust is another issue. If you borrow money from HSBC as a client […] they may ask your company for more documents and letters of guarantee. They need to understand your business well and build up knowledge and trust that way. But if I am at ICBC, I may say, 'Hey, Karen, we have a good relationship and I know you very well,' so when I require documents from you, it makes things a lot simpler. (*Ibid.*)

Due to complications like these in dealing with Chinese corporates, foreign banks that were just slowly moving into the Chinese corporate sector tended to target only SOEs due to the perception that they were too big and too strategically important to the Chinese economy and state to be allowed to fail. Government backing of these SOEs thus acted as a form of guarantee even if the financial status of these firms were poor:

> For Chinese clients, we look at the credit base, which is big operation in China so there's actually something to bank on, you have actual cash flows, right? And we look at the fact that *they are state owned and too big to fail*. That applies to all companies, [like] Sinopec, Sinochem, COSCO [China Ocean Shipping Company] […] these big names, there's a list of 200 state owned enterprises, all these enterprises are targeted to be in the Global Fortune 500 one day, they are considered too big to fail. So even if the cash flows doesn't [*sic*] actually add up it's still bankable. (Foreign country head of foreign bank: #43, 27 October 2006; emphasis added)

Another foreign interviewee elaborated on the policy of his bank in dealing with Chinese corporate clients. Apart from examining individual cases to obtain an internal rating and pricing guide, an important criteria was that they were SOEs as they found the small Chinese companies difficult to understand and too risky without the assurance of government backing:

> If we do Chinese large corporate… because our bank is very conservative and very cautious, we aim to deal with investment grade companies. Also the high end of investment grade, really triple-B and above. Our policy is that if a company has a public rating or it doesn't, we still go through an analysis for assessment and give an internal rating by looking for numbers, macroeconomic, bits and pieces, all that stuff, [and] give an internal rating which allows us to price it to make sure we get our required return on capital. The Chinese companies would tend to be state owned companies, you know, like Sinopec, the big players. We don't do the little ones because we don't trust them. (Foreign manager of foreign bank: #37, 19 October 2006)

Therefore, with the exception of only one foreign bank that focused particularly on the Chinese SMEs niche market as a specialist, all the foreign banks that I spoke to limit their exposure to Chinese corporations by targeting SOEs. The approach was a very cautious and prudent one in which the banks stuck with the market sectors that they were most familiar with (international clients from their home country or existing global network) and moved slowly into the local Chinese corporate market by only engaging with the SOEs deemed too large and politically significant to fail or publicly listed companies (also mainly SOEs) who had at least gone through the listing procedure and had their accounts and documents scrutinised by reputable auditing firms. The business strategy of the following foreign bank summed up the view of most foreign banks in Shanghai:

> [For] our bank we stay very, very close to our core strategy. We don't try and do all things for all people. The Italian business, we know and understand and that's fine. Trade finance, we know and understand and that's fine. And the corporate business it's just the SOEs, whom we feel wouldn't fail because of the state involvement. (*Ibid.*)

However, given that almost all the foreign banks in Shanghai were chasing crumbs from that same SOE-pie, competition was stiff and margins were very slim as banks tried to undercut each other. Foreign banks would thus have to seek new markets in terms of sectors and products in order to maintain and expand their operations in China. While some banks were eyeing the RMB retail sector, others were focusing on securities and derivative products as the capital markets continue to mature and open up to foreign players.

7.5 CONCLUSION

In this chapter, I examined the characteristics and objectives of the SSE and the contesting visions of this market according to the Chinese state and state institutions and to foreign financial institutions and investors. The particular structure of the Shanghai stock market was a product of historical and economic contexts that it was embedded in as well as specific objectives set by the Chinese state, but it has also constantly evolved in response to broader national economic development, international pressure from foreign investors, financial institutions and supranational organisations and increasing maturity of local financial institutions and investors. My objective was not only to point out its 'peculiarities' or simply to present a 'stock-market-with-Chinese-characteristics' but to highlight the process of market reforms in which the structure and meaning of 'market' in the context of the Shanghai stock market evolved through contingent social relations amongst market participants.

The SMG was keen to promote the city as an international financial centre to attract foreign capital and had been largely successful as evident from the large foreign bank presence in Shanghai. However, much of what was happening in Shanghai was arguably the outcome of political and economic processes elsewhere. On the one hand, institutional forces in Beijing still determined the pace and process of 'marketisation' in Shanghai; on the other hand, developments in Shanghai were also determined by the business needs of the international community and how Shanghai (or China as a whole) fitted into their globalisation strategies. Foreign financial institutions were eager to tap into the huge market potential of the Chinese banking sector. However, perspectives and expectations of their roles and strategies in China varied amongst actors in the financial markets. Foreign banks, local banks and regulatory institutions had their own interpretations of 'competition' and agendas for cooperation. The terms of these relationships had to be constantly renegotiated according to changing circumstances in order to maintain a balance of interest amongst the different stake holders, for example, whether to support local banks in the face of foreign competition or to relax restrictions on foreign financial institutions so as not to 'chase them away'.

In the face of regulatory bias, foreign banks had persisted in pursuing their 'China Dreams' through various business strategies, focusing on particular market niches according to products, sectors and client base. Given the difficulties of negotiating the regulatory environment in China as well as the accounting systems with 'Chinese characteristics' which most foreign banks found difficult to negotiate, many banks chose to focus only on SOEs. One option was to finance these SOEs in RMB from within China but an emerging trend had been to capitalise on the global networks and expertise of foreign banks in international banking to assist Chinese financial institutions and companies as they invest overseas (*Financial Times*, 26 July 2007). China National Offshore Oil Corporation's (CNOOC) bid to buy Unocal, the ninth largest oil company in the world (*Time Magazine*, 23 May 2005), and the investment of the China Development Bank into Barclays Bank in partnership with the latter's bid for the Dutch bank ABN Amro (BBC News, 23 July 2007, *The Guardian*, 24 July 2007) were some prominent examples of such overseas forays by Chinese banks and companies in recent years. As Chinese banks and companies continue to expand their operations globally, there will be more opportunities for foreign banks in China to offer their financial services as part of their global networks.

In the next chapter, I turn my analysis towards locational and policy considerations in assessing the place-based nature of market processes, examine factors influencing the development of Shanghai into a financial centre, its relationship with other competing centres such as Beijing and Hong Kong, and highlight some future challenges for the city.

Chapter 8

The Making of (Market)places in Shanghai and Its Future as an International Financial Centre

8.1 INTRODUCTION

The financial landscape in China has changed dramatically over the past 10-15 years and the impact has been most clearly felt in Shanghai where reforms and regulatory changes were the first to be implemented. The first key step was the liberalisation and opening up of Shanghai's financial sector to foreign financial institutions. Most of the impact has been in the banking market[1] as foreign banks were allowed to offer more products and services and compete with domestic banks in sectors that were previously closed to them (even though the terms of competition have not been entirely favourable, as discussed in Chapters 6 and 7). Within the process of liberalisation, the opening up of the RMB corporate business sector to foreign banks was particularly significant as it allows the latter to tap into the Chinese corporate market. China's accession to the WTO was also important as it verified its commitments to financial reforms and liberalisation in an international setting. One of the biggest changes was the foreign exchange reforms which started from 21 July 2005 when China abandoned its decades old RMB peg to the US dollar and allowed it to 'float' against a basket of currencies. This introduction of some (albeit very small) flexibility to the RMB enabled the launch of derivative products such as RMB forward, RMB spot and RMB FX swap, which were not possible before. In turn, this

[1] The impact of foreign financial institutions is also increasingly felt in insurance and capital markets as those sectors are slowly opening up for foreign investment and participation.

boosted the development of the derivatives market and helped to broaden Shanghai's capital markets.

Shanghai was selected by the central government as the 'dragon head' to drive the growth of the Yangtze River Delta region and to connect China to the global economy through its financial services sector. However, the success of Shanghai was also dependent on other key actors such as the foreign and local financial institutions located in Shanghai as well as international players outside of China. The internationalisation of financial markets has not brought about the simple end of geography; financial centres remain crucial to global financial architecture and flows. Various studies done on the development and territorial embeddedness of financial centres have demonstrated this enduring trend (see, for example, Roberts, 1994; Leyshon and Thrift, 1997; Thrift, 1998; Budd, 1999; Hudson, 1999; Porteous, 1999). The social and cultural constructions of financial centres are particularly important in this process (Thrift, 1994, 1996; Clark and O'Conner, 1997; Leyshon, 1997; Reszat, 2002). Although the importance of financial centres are often vigorously promoted by regulatory decisions made by state institutions (such as those relating to the City of London's 'Big Bang' in the 1980s) (Pryke, 1991; Strange, 1994), financial centres also develop through, and are sustained, by socio-cultural factors such as information, expertise, contacts and even historical legacy (Porteous, 1999).

Why did local and foreign financial institutions choose to locate in Shanghai (rather than, for example, Beijing, Shenzhen or Hong Kong)? Why were particular markets being experimented with and taking *place* in Shanghai? What particular advantages did Shanghai enjoy such that processes of regulatory changes, financial liberalisation and innovation and various actors associated with them were ‘grounded’ in this city? These are some of the issues I will address in this chapter, focusing on factors influencing the development of Shanghai in its financial centre aspiration to date and future challenges. The insights and experience of key actors involved in this process, namely regulatory authorities, local government and foreign and local financial institutions, provide the basis for analysis. In the next section, I examine the factors that have contributed to Shanghai’s relative success over the past two decades. In section 8.3, I assess Shanghai’s aspiration and achievement vis-à-vis other regional centres that might be seen as competing for the title of international financial centre for China, namely Beijing and Hong Kong. What are their comparative advantages and place-based characteristics and how might they affect Shanghai’s role in national and global financial services and flows? Finally, in section 8.4, I present the most pressing issues faced by Shanghai that, from the perspective of interview respondents, should be addressed in the next five to 10 years in order for Shanghai to capitalise on its advantages and develop its capacities as an international financial centre.

8.2 THE SHANGHAI ADVANTAGE

> *We have to consider whether a place has the right conditions, culture, standards; if you don’t have the right factors, you won’t succeed. Shanghai has the right background, the people skills, the requirements. (Local manager for Chinese securities firm: #35, 18 October 2006; translated from Mandarin)*

While there were debates as to exactly when it might be achieved, there was almost unanimous agreement amongst my interviewees on the eventual success of Shanghai as an international financial centre. The initial euphoria and gushing enthusiasm that permeated local and foreign media and investor sentiments in the early-1990s might have dissipated; however, there was still firm belief in Shanghai’s long-term success amongst both the local and foreign respondents that I spoke to.

Factors ranging from the historical, political, economic, and cultural, contributed to Shanghai's current success as well as continued optimism for its future in spite of setbacks and difficulties encountered. Firstly, the historical image and contemporary branding of Shanghai as a cosmopolitan world city and international financial centre played an important role in its development strategies. The significance of discourses and metaphors in shaping spatial formations have been studied by various scholars (Barnes, 1992; Neil and Katz, 1993; O'Neill, 2001, Bunnell, 2002); the use of discursive representations, practices and narratives are just as important in the development of financial centres such as Shanghai. Many of my interviewees drew upon Shanghai's historical success in the early-20th century as a financial centre (see chapter 2) to account for its contemporary cosmopolitanism and receptiveness to foreign investment, ideas and practices. Most local Shanghainese saw it as perfectly 'natural' that Shanghai should become the most cosmopolitan and commercially successful city in China (and becoming a financial centre was the epitome of that achievement) due to its cultural propensity to be open to outside influence and investors and an ethic for commerce, built up over generations:

> There is a history here, it did not happened only now, [it has developed] over generations. For example, my father, mother, grandfather, they might be doing this back then: working in trade, working in Western companies, there were many of them. So from this angle, Shanghai has a natural… background as an international, cosmopolitan city. So it was easy for it to become a big city. This is from the historical angle. Also from the cultural perspective… have you been to the Bund? The Bund, the different foreign settlements, the French Settlement, the English settlements, Japanese and so on. All these cultures were there. So the impression at that time was that there were many foreigners. This has been passed down and is something natural to Shanghai, cultural. (Local manager of private Chinese financial institution: #9, 27 February 2006; translated from Mandarin)

With its colonial-style trading houses, old bank buildings and opulent hotels, Shanghai's Bund was once the wealthiest, most decadent district in China and the entire Far East when it was one of the major financial centres of the world in the 1930s and 1930s, with lively music filling the night clubs, jazz clubs and hotels at night (Figure 8.1). In the 1990s, Shanghai's renaissance left the Bund behind as urban development swept across Shanghai. Shopping malls sprouted up on Nanjing Road and Huaihai Road west of the Bund and international banks returned to Shanghai but headed east of the river for Pudong. This could be due to the Bund's symbolism as it represented a district built by foreigners who profited from concessions forced upon a weaker China. Following a renewed mandate by the central government for Shanghai to reclaim its commercial status, the Bund was rebranded and celebrated as a site of international commerce and cosmopolitan exchange rather than colonial humiliation (Olds, 1997; F. Wu, 2000a, 2003) (Figure 8.2). Although the stately buildings along the historic promenade are now occupied less by banks than by Michelin-star restaurants, luxury hotels, glitzy bars and art galleries, its symbolism of historical success and reputation is no less potent. The past has become a source of confidence for the future, as well as the basis for a set of discourses about Shanghai that is frequently drawn upon in official promotions and to justify business presence on the part of foreign financial institutions. The 'buzz' that Shanghai had continues to reverberate particularly with the expatriate community and that energy translates into a vibrant commercial environment where reforms, experiments with new markets and new products are possible in a city that is 'daring':

> Shanghai is a sexy place, because it has the history and at one time it was naughty. There was the French Concession and there is a sort of romanticism about what it was. (Foreign president of a foreign bank: #20, 11 April 2006)

Figure 8.1 The Bund in the early-20th century *(Source: http://www.earnshaw.com/shanghai-ed-india/tales/t-buil01.htm)*

Figure 8.2 The contemporary Bund. Many of the old bank buildings (such as the former HSBC building with the dome) are now occupied by Chinese financial institutions. *(Source: Author's own photograph)*

Secondly, the preferential policies implemented in the early-1990s helped to boost Shanghai's status especially amongst foreign investors, although one could say that the latter had little choice as Shanghai was the only Chinese city opened to them in those early years. As detailed in Chapter 2, the Pudong New Area (and the LFTZ in particular) was specifically designed for the city to resume its former role as China's leading international financial, trade and economic centre. It also signified the commitment of the central government to continue its reform and open door policy, and this government backing was widely taken to be a strong indicator for success by both local and foreign investors:

> Because the government has decided to put the financial centre here, the leadership has set out their ideas very clearly, that is why things have grown so quickly. This gave foreign investors very strong confidence. The trend is very clear now but it remains to be seen what is to be done in the future. (Local manager of Chinese securities firm: #35, 18 October 2006; translated from Mandarin)

Certain preferential treatment was approved by the central government including tax breaks to both foreign and local investors located in Pudong, greater foreign participation permitted in sectors that were closed to foreign investors elsewhere in China and the retention of financial income by Pudong for further development. More than just a symbolic model of China's global aspirations and urban transformation, Shanghai was also the site where much of China's financial reforms were tested. As China continues to experiment with and developed capital markets, the largest stock exchange in the country and the only futures and derivatives exchange in China are all established in Shanghai, which further boosts the latter's status as the pre-eminent financial centre in China.

Thirdly, Shanghai benefits from access to China's huge domestic market (the affluent eastern seaboard in particular) as an economic hinterland. Whether the domestic market will be realised can be problematic but the allure of this potential is undeniably prominent in the minds of local and foreign investors alike. The Yangtze River Delta is currently the most vibrant economic region in China with a booming manufacturing sector and the recent opening of the Yangshan deepwater port in 2006 is also expected to increase trade volumes and the demand for related financial and other producer services (see section 7.3). The growth potential of neighbouring provinces of Jiangsu and Zhejiang has a spillover effect on Shanghai as financial institutions located in Shanghai seek to harness growth in the region to further develop financial products and services and capital markets.

Fourthly, the dramatic changes that have already taken place in the finance sector in Shanghai constitute a trend towards marketisation that is expected to continue as respondents pointed out that it would be unthinkable to turn back. Although there is still strong government influence in the decision-making processes, regulatory procedures, and business decisions, there is general consensus amongst my respondents that market consideration is definitely on the rise with a clear trend towards marketisation (市场化; *shichang hua*). A local interviewee from a Chinese state-owned bank explained that:

> In the past in China, we rely on the regulators and administrators saying we have to do this in this way, so there wasn't much consideration about market response. Now there is more incorporation of market factors, in terms of price fixing, transaction volume, financing and so on. (#26, 19 April 2006; translated from Mandarin)

A number of respondents were convinced that developments in the financial markets of Shanghai are so far along that there is now no turning back, in spite of the rhetoric of experimentation with the option of shutting down markets and businesses if they should threaten the stability of the economy and capacity of regulatory infrastructures. China wanted to gain international recognition and influence through

Shanghai's financial centre development and the price of that accomplishment (to whatever extent) was that it now has to honour international commitments and adhere to international standards and protocols of behaviour, instead of having the freedom to shut down particular markets, interrupt capital flows and shut out foreign investors as and when they were deemed undesirable. This point was emphasised by a CBRC official (#25, 16 April 2006) who clearly believed that the current reforms towards marketisation and scaling back of government influence in the financial sector will continue. Another interviewee likened it to having released a genie whereby when "the ghost is out of the bottle, by then it's so far out you cannot push it back anymore [… such that] you're so far the only way is to continue" (foreign manager of foreign bank: #46, 2 November 2006). As the first locality in China where such reforms were carried out and new financial products and markets tested, these trends were much more prominent and established in Shanghai compared to other more recently 'opened' cities.

Fifthly, the living environment is also an important factor in attracting foreigners to move to Shanghai compared to other cities in China. The high standards of living with good international schools, quality housing, growing arts and cultural scene, developed retail sector and the urbanised and cosmopolitan environment set Shanghai apart from almost all other cities in China, even compared to other big cities the likes of Beijing, Shenzhen, Guangzhou, Tianjin and Dalian. Many foreign respondents indicated that it would be easier to entice an expatriate staff to move to Shanghai compared to Beijing, for example, due to the more 'westernised' and cosmopolitan urban environment and relatively lower levels of pollution.

Finally, the geographical location of Shanghai is a key asset. Related to the latter point on living environment, Shanghai benefits from relatively mild weather (other than the hot and humid summer months) compared to, for example, the very harsh winters and very hot and dry summers of Beijing. Its location in the middle of the eastern seaboard makes it an ideal base for travelling to other parts of the country, only two hours flight time to either Beijing in the north or Guangzhou or Hong Kong in the south. It is also a major transportation hub for rail, air and sea travel and transport and benefits from the huge flows of people and goods.

Although there was general optimism and belief in the eventual success of Shanghai as an international financial centre, most interviewees agreed that it would be a long-term process and unlikely to happen before the next 20 to 30 years due to numerous issues still outstanding and regulatory frameworks, skilled labour and market infrastructures to be developed over time (see section 8.4). The building of Shanghai as an international financial centre drew upon ideology at the national level, from political aspirations at the municipal level, from narratives of historical success and eminence, and particular visions of 'global city' status and what that might entail. The cultural capital that Shanghai possesses due to its historical success clearly influences the perception and practices of both locals and foreigners in their evaluation of Shanghai's potential. According to Thrift (Amin and Thrift, 1992; Thrift, 1994, 1996) the importance of financial centres lies not only in their role as centres of financial products and business services but as places where information about the global economy, companies and financial flows is exchanged and interpreted. Their success is thus sustained by acting as centres of representation and interpretation; as centres of expertise and innovation due to the concentration of expertise, contacts and liquidity; and as centres of contacts and social interaction. In the case of Shanghai, its success thus far can be attributed to its 'cultural capital' of having been the 'Paris of the East', its cosmopolitan environment and openness to ideas and influence outside of China, as a centre of experimentation for new financial products and the location of choice for the China headquarters of foreign banks and, increasingly, domestic banks. Yet, in developing capitalist spaces of finance in Shanghai, the landscapes of power not only reflect the institutional interventions of the national and local states but also the social and cultural reorganisation of business and political and artistic elites[2] who wield varying levers of social power. The representations of particular visions or versions of reality embody particular agendas but the power to represent is also limited and countered by the power to resist those representations as other economic actors and institutions draw upon differing and distinctive experiences and counter-discourses.

8.3 COMPETITION OR COMPLEMENTARITIES? SHANGHAI VERSUS BEIJING AND HONG KONG

8.3.1 Shanghai and Beijing: Dual Headquarter Strategy?

Shanghai's development trajectory towards national financial centre status has been questioned by some, primarily due to its relationship with Beijing (Zhao, 2003; Zhao et al., 2004). As seen in Table 8.1, Shanghai and Beijing are the largest and most developed cities in mainland China. Although Shanghai is at the top of the Chinese urban hierarchy, with the largest population and GDP contribution, Beijing handles more foreign trade and has a more developed tertiary sector. Beijing's most significant competitive advantage lies in its role as the capital of socialist China for almost half a century, being the primary location for institutions and organisations responsible for managing and determining the economic and political life of the

[2] The opening of establishments such as *M on the Bund* and *Three on the Bund* by celebrity chefs and restaurateurs like Michelle Garnaut and Jean-Georges Vongeritchten, famed architects like Michael Graves and hotel chain Mandarin Oriental over the five years have been key to a cultural renaissance of the iconic Bund (Gluckman, 2001, 2004)

country. It is the location of the country's central bank, headquarters of the main financial regulatory institutions such as the CBRC, CSRC, CIRC, and SAFE, along with the head offices of the many of the largest domestic banks and SOEs. When a political decision was made to develop Shanghai as a financial centre, with the development of Pudong and Lujiazui in the 1990s and the location of the country's main stock exchange in Shanghai towards the end of 2000, the city's future as the national financial centre for China seemed assured. However, some recent studies (Yatsko, 2001; Shi and Hamnett, 2002; Cai and Sit, 2003; Zhao, 2003; Zhao et al., 2004) have cast doubts on Shanghai's position and influence.

Table 8.1 Economic indicators for China's largest cities (population > 2.5 million), 1997

City	Population (million)	GDP (RMB million)	Primary industry (% of GDP)	Secondary industry (% of GDP)	Tertiary industry (% of GDP)	Total value of foreign trade (US$ billion)
Shanghai	9.61	290.2	2.5	54.5	43.0	52.9
Beijing	8.27	136.3	5.2	42.3	52.5	53.9
Tianjing	5.93	85.8	6.4	53.0	40.6	21.7
Chongqing	5.46	41.9	10.0	56.6	33.4	1.0*
Wuhan	5.12	78.2	9.2	46.8	44.0	2.0*
Shengyan	4.76	77.2	8.0	42.7	49.3	1.5*
Guangzhou	3.90	95.0	5.6	46.7	47.7	43.3
Chengdu	3.08	35.4	6.9	37.8	55.3	1.4*
Xi'an	3.03	32.3	3.3	40.9	55.8	1.3*
Harbin	2.95	33.9	4.9	36.5	58.6	1.8*
Changchu	2.70	31.3	5.5	52.2	42.3	0.8*
Nanjing	2.69	51.1	1.3	51.0	47.7	2.5*
Dalian	2.54	51.4	5.9	43.3	50.8	12.2*

* 1994 data
(Source: Shi and Hamnett, 2002: 129)

In their empirical studies on the agglomeration tendencies and locational preferences of global TNC head offices, Zhao (2003) and Zhao et al. (2004) found that although Shanghai has been heavily publicised and promoted as China's number one financial centre, more foreign companies choose to locate their head offices in Beijing. If the presence of head offices of TNCs and financial institutions provide a good indicator for overall assessment and ranking of international financial centres and, by association, global city status (see Porteous, 1995; Dickens, 1998), the premiere position of Shanghai appears to be threatened by Beijing. Hong Kong has the largest cluster of local/regional offices of *Fortune 500* companies; it is also the preferred location for Asia-Pacific headquarters, with 94 per cent of them setting up in Hong Kong (Table 8.2). But in terms of the Chinese market, more *Fortune 500* companies choose Beijing as a base over Hong Kong, with Shanghai ranking third, followed by Guangzhou and Shenzhen. Zhao (2003) and Zhao et al. (2004) attribute the preference for Beijing over Shanghai to the problem of information asymmetry. In financial markets, there is an asymmetry of regulatory information when administrative agents know more than participating agents in the market. Firms and their agents, particularly foreign ones, do not know local market regulations as well as the government or appointed agents. This is particularly so in the Chinese case as the government relies heavily on 'rules' – laws, orders, regulations, directives – to manage the economy. Apart from the problem of administration transparency, Chinese rules are normally expressed in generalities and do not usually provide sufficient details for practical resolution. As such, implementation and enforcement are often subject to the interpretation and articulation of administrative authorities and can vary from case to case. If formally published policy information cannot be interpreted 'correctly' by information users, non-standardised policy information becomes crucial for conducting business in China. However, such information is difficult to gather or access without intensive policy contact with specific information providers, which is often facilitated by geographical proximity. In a questionnaire survey, 'proximity to central government departments' was cited by respondents across several industries as the most important factor in influencing location choice of TNC regional headquarters in China (Zhao, 2003: 556; Zhao et al., 2004: 585). According to Zhao, major financial firms and global TNCs prefer to locate their head offices as close as possible to the functional departments of the central government in Beijing in order to access as efficiently as possible non-standardised policy information. Therefore, although Shanghai may have a prominent (and officially sanctioned) role in developing various kinds of financial markets and services, he concludes that its claim to being the national financial centre may not be as strong as Beijing due to the effect of information asymmetry.

Table 8.2 Headquarters or first-level subsidiaries of *Fortune 500* companies in China (2000)

City	Regional/local office		China regional headquarters		Asia-Pacific headquarters		Total
	No.	%	No.	%	No.	%	
Hong Kong	57	40	28	30	17	94	102
Beijing	25	17	34	37	0	0	59
Shanghai	25	17	19	21	1	6	45
Guangzhou	11	8	5	5	0	0	16
Shenzhen	8	6	0	0	0	0	8
Others	17	12	6	7	0	0	23
Total	143	100	92	100	18	100	253
(Source: Zhao, 2003: 554)							

Beijing's advantage is also seen in other areas. Its position as the seat of the central government makes it the source of political and economic information. It is host to many domestic and joint-ventured financial institutions on its *Jinrong Jie* (Financial Street), such as SAFE, CSRC, CIRC, all China's major banks, China International Capital Corporation (China's first and largest investment bank joint-ventured by China's Construction Bank and Morgan Stanley Dean Witter), Everbright Securities (one of the largest stock brokerage firms in China), and headquarters of the PBOC (Zhao, 2003: 564-565; Yatsko, 2001: 86-87). Shanghai is most important in terms of retail finance in China as suggested in Table 8.3, but in terms of representative offices of foreign institutions, Beijing has the largest share (44 percent) while Shanghai accounts for only 25 percent. Although Shanghai is the site of China's major financial markets, real power arguably rests with the Beijing-based institutions that make key decisions:

> If Shanghai wants to issue a Yankee bond, it needs Beijing's permission. If Shanghai Industrial, the Shanghai government's flagship firm, wants to do a backdoor listing, it needs Beijing's permission. If a foreign securities firm based in Shanghai wants to change the English name of its company, it again needs Beijing's permission. The Shanghai branch of the People's Bank of China does not have approval authority over even that small a matter… As Richard Graham, the former Shanghai-based chief representative for ING Barings, cleverly put it: "Shanghai proposes, Beijing disposes" (Yatsko, 2001: 88).

The above concern was echoed by a few of my respondents who questioned whether the fact that decision-making abilities were held in Beijing and not in Shanghai would be an obstacle to Shanghai's aspirations (see section 7.3). One of them was of the opinion that, "Of course the stock market, the stock exchange is here but it might as well be in Chongqing because so much of what's happening in Shanghai is controlled from Beijing, in terms of regulation" (Foreign economist of foreign bank: #7, 22 February 2006).

Table 8.3 Distribution of bank branches[a] and representative[b] offices of foreign institutions in China (1998)

	Foreign-owned bank branch (%)	Representative offices (%)
Beijing	16 (11)	122 (44)
Shanghai	45 (30)	68 (25)
Guangzhou	15 (10)	23 (8)
Shenzhen	23 (15)	10 (4)
Other Chinese regions	53 (35)	54 (19)
Total	152 (100)	277 (100)

[a] Solely foreign-owned
[b] Foreign-owned or foreign-China joint venture
(Source: Zhao et al., 2004: 588)

Although Zhao's argument and data are persuasive, I would disagree with his assessment that Beijing is necessarily outmanoeuvring Shanghai in developing financial centre capacities. Based on my field research (particularly from interview data, research diary records of casual conversations and tracking the local media), the situation is more complex than revealed from the *quantitative* data of which city has more financial services offices or corporate headquarters. The *qualitative* functions of these two cities are clearly different from the perspectives of most of my interviewees and their operational structures and business strategies reflect that division of labour. Most of my respondents (both local and foreign) saw a clear division between the roles of Beijing and Shanghai with the former being predominantly a *political* centre and the latter a predominantly *business* and *commercial* hub. A Chinese interviewee, for example, was insistent that:

> In building a financial centre, financial services, knowledge and skills in this aspect, Beijing cannot catch up with Shanghai because Beijing is better at other aspects. It is better in terms of relationships, *guanxi*, policies; Shanghai is more business. That is a very clear division of labour. (Local manager of Chinese securities firm: #35, 18 October 2006; translated from Mandarin)

Another local respondent described how the general political atmosphere is reflected in the everyday topics of conversation on the street in what he calls '*guan hua*' (官话; literally, official speak/talk/conversation). He contrasted this with Shanghai where people's focus tended to be on business opportunities rather than on the fortunes of specific political figures or events:

> I think Shanghai has more of a commercial and economic atmosphere. It has more of a commercial feel. Beijing has more of a political atmosphere […] Many in Beijing speak '*guan hua*' (official talk). Official talk is like… 'Ah, we are holding this meeting now… What is this leader saying… Oh, this leader is going up, that leader is coming down'. Many people are concerned about things like that, that includes taxi drivers! They have a lot to say! 'Oh, this leader is not good; this leader is great; this person is on the way up' […] So there is a lot more talk about political stuff. This is much less so in Shanghai. (Local manager of private Chinese financial institution: #9, 27 February 2006; translated from Mandarin).

One could critique these stereotypes but they clearly influenced the perceptions and business decisions of financial actors who believed that the jawing culture in Beijing was in contrast to people in Shanghai whom they viewed as more practical and focused on producing results. Another local respondent from a Chinese state-owned bank compared this practical culture in Shanghai to the tendency to rely on 'empty talk' in Beijing where there was plenty of discussion but little concrete accomplishment:

> [I]f I take you to Beijing… the people in Beijing are very good at talking… They will talk and are very good at saying this and that, very convincing, very skilled! They can talk to you as a stranger and go on and on about everything. I think in Shanghai we are more practical, we will work on producing results. Maybe we are not as good in talking but our execution is stronger, that's what I think. So I think we should produce some results and then use that to support our case, and that is better than '*kong tan*' (空谈; empty-talk) [laughs]. (#27, 19 April, 2006; translated from Mandarin)

The history of Shanghai as a commercial and financial hub in the early-20th century was often brought up when comparing Beijing and Shanghai and how that might account for the more open-minded approach and efficiency of the latter compared to the more relationship-driven approach of the former in which who you knew was much more important. According to my respondents, this could account for why foreigners might feel more welcomed and comfortable living and working in Shanghai compared to Beijing, which as mentioned above was a significant factor for its success:

> And the thing is of course Shanghai has the history, so… […] I think it's the fact that, it's not so much to do with us but it has to do with the Shanghainese. They are much more comfortable dealing with foreigners. So for us, you feel much more… at ease here than in Beijing. In Beijing there's much more of an inner crowd, where

> you have no idea… Much more patriotic, much more political, much more slow. Shanghai has a much higher productivity per employee than other places in China. But it seems to be much more accepting of foreigners. English is much better. I think quality of living, that's it. (Foreign manager of foreign bank: #36, 18 October 2006)

He went on to describe how who-you-know and personal connections were much more important in Beijing due to the relationship-driven nature of interaction there:

> In Beijing it's very important which family you're from, how old is your family, how many generations have you been in Beijing and all that stuff. And so the lady that runs our Beijing rep office, her family have been in Beijing for five generations, something which is supposedly… like, she knows a lot of people or something. (*Ibid.*)

Therefore, Beijing and Shanghai were clearly not seen to be competing as financial centres due to the very different political and corporate cultures in those localities. A Chinese respondent stressed that, even within financial services, both cities had different emphasis in terms of sectors and areas of expertise, with Beijing being tasked with policy-making and macro-planning while Shanghai was dedicated to testing new products and markets and financial innovation. As such, there is no contradiction or zero-sum-game competition:

> China has already set Shanghai's role in developing its financial centre; that will not change. Beijing is also developing its financial markets, Shanghai is also developing its financial markets. They may emphasise different things. Shanghai may focus on financial innovation, new system and so on. Beijing may focus on regulation, macro adjustments and these aspects. The PBOC has just placed its second headquarters in Shanghai. The operational aspects are in Shanghai, the macro aspects, elements of control are in Beijing. Making policies, macro planning, these are in Beijing. After planning, the details are then carried out in Shanghai, that's basically how it is. When foreign exchange has been relaxed, it is done in Shanghai. New financial

> products are first tested out in Shanghai. So its main functions as a financial centre are different from Beijing. (Local vice-director of Chinese fund management company: #26, 18 April 2006; translated from Mandarin)

This distinction in the political and corporate cultures as well as financial specialisation between Shanghai and Beijing was reflected particularly in the business strategies and organisation structures of the foreign financial institutions whom I interviewed. One spoke of Beijing as an "administrative capital" while Shanghai is a "business capital" (foreign manager of foreign bank: #13, 7 March 2006). Therefore, most foreign banks in China had a dual-strategy to reflect that specialisation by having offices in both Shanghai and Beijing. While almost all Chinese banks have their headquarters in Beijing (with the exception of BOCOM and China Merchants Bank) due to historical and political reasons, and the headquarters of regulatory bodies such as SAFE, PBOC and CBRC remain in Beijing, the head offices of foreign banks tend to be in Shanghai, and even the Chinese banks have moved their credit facilities, accounting departments, reporting branch and other functions to Shanghai, which reflect the volume and significance of business being conducted out of the city. Offices in Beijing remained very much as "diplomatic posts" (foreign president of foreign bank: interview no. 20, 11 April 2006) with specific tasks allocated to them such as maintaining relationships with Chinese corporate clients, government and regulatory officials and lobbying on particular issues. It is not simply a matter of one city being seen as more important than the other but that they each have their own advantages and significance in the scheme of the banks' operations and they have to structure their network accordingly:

> Shanghai has its advantages and Beijing has its advantages. Shanghai's advantage is that you are closer to the market, closer to your customers. […] Our head office is

> set in Shanghai so our branch manager at the Beijing branch has a special mission. His role is to maintain communication with the regulators in Beijing […] the main role of the branch manager is to look after official relations and not bank operations. On the other hand, for banks that have head offices in Beijing, they would not neglect the Shanghai market either. They will have representative offices and branch offices in Shanghai as well. So it's not just a matter of where the head office is; there is a dual strategy. (Local manager of foreign bank: #11, 6 March 2006; translated from Mandarin)

One of my foreign respondents said that their head office (and branch office) was in Shanghai for the simple reason that their customers were in Shanghai and not in Beijing. However, they still saw the value of maintaining a representative office in Beijing because of the opportunities to be had in keeping an ear close to the political centre:

> [We have the Beijing office b]ecause of the head offices of the Chinese companies, the Chinese conglomerates, that's the reason. We're close to the politics, to the policy makers, but also in this country it's like a big market place, of opportunity, ideas… So it's worthwhile, it's worthwhile. I wouldn't scrap that one [office]. (Foreign manager of foreign bank: #41, 27 October 2006)

Another foreign respondent was equally direct in his view that: "For [foreign] banks it's clear. You need a rep office. The minimum set up you need in China as a foreign bank is a branch in Shanghai and a rep office in Beijing" (foreign branch manager of foreign bank: #43, 27 October 2006). As mentioned earlier, the head offices of regulatory bodies and state-owned financial institutions and companies were located in Beijing, and this affected the locational strategies of foreign banks. For those whose target clients were the Chinese SOEs, it was more important to have a presence in Beijing; for those who were interested in business with other foreign TNCs, who tended to be concentrated in and around Shanghai and the Yangtze River

Delta, that would be the focus of the banks' business activities. Since most foreign banks in China had foreign companies as their primary client base, it was not surprising that they preferred to locate their head offices in Shanghai rather than in Beijing. The typical set up of a foreign bank was to have a branch office of between 10 to 50 people in Shanghai that conduct business transactions and offer financial products and services, and between three to eight people in a representative office in Beijing who would maintain linkages with Chinese companies headquartered there, the relevant regulatory and government institutions and perhaps a research desk as well. When asked if they could only have one office in either Shanghai or Beijing, most of my respondents opted for Shanghai due to its geographical location in the middle of the eastern seaboard and the presence of a large international financial services community. The lack of proximity to political and regulatory decision-makers did not appear to dampen Shanghai's attraction. Unless a financial institution was targeting specific sectors such as energy, telecommunications and utilities, which were tightly controlled by the central government, they saw little need to have a large operation in Beijing:

> If you mainly target big Chinese companies, if you target the big Chinese banks, if you want to do [some] kind of political lobbying or whatever, then you better be in Beijing. If you more looking [*sic*] for your corporate clients then you better be in Shanghai. If you don't know, then you better be in Shanghai, because then you're just more in the centre. Because from… this is just a logistical question, because from Shanghai to south China is faster than from Beijing. And of course you have a much bigger banking community here. (Foreign chief representative of foreign bank: #45, 1 November 2006)

> The team that's got energy and utility clients, for example, they are in Beijing because they need to be close to the clients and the clients are close to the

> government. From the bank business, Shanghai is in the centre of the financial markets and I think the foreign banks… I think they have all put their offices here in Shanghai. (Foreign manager of foreign bank: #13, 7 March 2006).

For these banks, their Beijing offices had a clear mandate to build relationships with key contacts, maintain such linkages, be keyed in on major announcements and developments that might affect their targeted clients' business sector and to conduct research sometimes on behalf of the branch offices or clients based elsewhere in China. This fits in with other descriptions of Beijing offices being 'diplomatic posts' where the routine of power lunches, cocktail parties and charity dinners assume more importance than actual business transactions or discussion. This foreign respondent, for example, described how their Beijing representatives work hard at establishing and maintaining good *guanxi*:

> Our rep is usually doing a lot of research, do a lot of lunching and cocktail parties, and they maintain contacts, build good relationships… And in China that's very important, you know, the whole concept of *guanxi* is very important. (Foreign manager of foreign bank: #37, 19 October 2006)

Another foreign respondent highlights the differences in the kind of information gathering that occurs in the two cities:

> The situation in Beijing is more political so she [the Beijing representative] talks more to institutions. Not really only the regulators but also the… kind of foreign institutions, like the European Union have a delegation there, of course you have the embassy, you have… certain German institutions have their rep office in Beijing and there it is much more political contact. Also gathering information. Here [in Shanghai], the information we collect, this is more on the business side. There [in Beijing], it is on the political or macroeconomic side. (Foreign representative of foreign bank: #45, 1 November 2006)

According to a government official (SMG Office for Financial Services: #28, 20 April 2006), the above characteristics had led to a division or specialisation in the types of foreign financial institutions and functions found in Shanghai and Beijing. Most investment banks such as Goldman Sachs, BNP Paribus, Morgan Stanley and Credit Suisse located themselves in Beijing as they needed to be close to their target client group of Chinese SOEs in the energy, telecommunications and utilities industry and state-owned banks (which are still under tightly controlled by the central government). The latter had their headquarters in Beijing due to historical reasons, as they used to be part of different government ministries that were subsequently farmed out and corporatised. Commercial banks, on the other hand, such as HSBC, Standard Chartered, Citibank, Bank of East Asia, Deutsche Bank and ABN Amro, preferred to locate in Shanghai to serve their clients (foreign TNCs and local private enterprises) located in the Yangtze River Delta. For banks with both investment banking and commercial banking divisions, their investment banking function would be in Beijing but their equity research, trading, asset management functions would be placed in Shanghai. He called this emerging trend a "dual-headquarter structure". This reflected the qualitatively different advantages that each locality enjoyed with their distinctive political, economic and social environments, with no one particular city being a clear 'winner' in all aspects.

8.3.2 Shanghai and Hong Kong: A Long Way Off

During the 1980s and 1990s, Hong Kong's strategic advantage as a link between global capital and China led to the rapid development of its financial industries and economy. But as China opens up its economy and establishes *direct* linkages with the world, the future of Hong Kong as a financial centre is increasingly tied to its special relationship to China. As China develops better economic infrastructure and encourages more business investments, there is increasing concern that Shanghai may usurp Hong Kong as the pre-eminent financial centre within China, if not the wider Asian region. With the rapid development of financial services in Shanghai, will Hong Kong be bypassed as its traditional role if it is rendered obsolete? The general consensus that I gathered from my field research revealed that such fears were often exaggerated and did not take into account the regulatory complexities and shortcomings that still plagued the immature financial markets in Shanghai (for all its hype and rapid development) and the comparative advantages that Hong Kong continued to enjoy.

The growing stock market in Shanghai was one such area of possible competition since a Chinese mainland company could, theoretically, list on either the SSE or HKSE. When asked whether a Chinese company considering an IPO would prefer to list in Shanghai or Hong Kong, most of my respondents thought that, given the opportunity, most companies would prefer a public listing in Hong Kong although some might prefer a Shanghai listing for specific reasons. Table 8.4 lists some of the reasons for listing in Shanghai or Hong Kong. The biggest advantage that the Hong Stock Exchange (HKSE) enjoys is that it is much bigger and more liquid compared to the SSE. A-shares and B-shares listed in Shanghai are subject to different rules (see chapter 7) with the locals-only A-share market seen as particularly restrictive. The HKSE is not hindered by such regulatory restrictions regarding the listing of shares on the primary market and buying and selling of shares on the secondary market. Since international investors are allowed to trade freely on the stock exchange, listed companies are able to raise more capital from their IPOs. Due to the international reputation of the HKSE and Hong Kong as a financial centre, a public listing there is seen to boost the international brand recognition of the company. The choice is also related to the company's business expansion plans and internationalisation strategy; if it intends to expand overseas into, for example, Hong Kong, New York or other parts of Asia, a listing in the relevant markets would raise its regional and international profile ahead of actual expansion:

> It has to do with the company's business strategy. The location of a company's IPO will definitely increase the brand recognition and reputation of the company in that country. If Hong Kong is my target market or if New York is my target market, I will try to get myself listed there because then locals will be more aware and familiar with my company's name and products. That is publicity, save on advertising! It also has to do with the differences between the stock markets themselves. (Local manager of foreign bank: #11, 6 March 2006; translated from Mandarin)

Table 8.4 Some reasons for a mainland Chinese company to list in Shanghai or Hong Kong

Reasons for listing on SSE	**Reasons for on HKSE**
▪ Lower fees ▪ Shorter listing process ▪ Large RMB capital market, possibility of obtaining better price per share ▪ Politically motivated choice for listing on a mainland stock market	▪ Bigger and more liquid market, able to raise more capital ▪ Improves international reputation and increases brand recognition ▪ More stringent listing process seen as a boost to corporate governance ▪ For private companies, a better option compared to queuing with SOEs on the mainland

Many respondents pointed to Hong Kong's prudent regulatory system as a key advantage and reasoned that being listed successfully on the HKSE would therefore reflect positively on the company's accounting standards, corporate governance and business management:

> To list in Hong Kong, the company will have to fulfil the requirements of the Hong Kong securities regulators. This has a positive impact on the brand recognition and status of the company. It is different if I say that my company is listed in the US, in

> Hong Kong, or on NASDAQ. That is because everybody knows that to get listed there you have to fulfil certain requirements set by the local regulators. So there will be the impression that your company has very good corporate governance and is very well-managed and that could affect the valuation of your company. (Local manager of foreign TNC: #12, 6 March 2006; translated from Mandarin)

A foreign interviewee, for example, said that when assessing a local company as a potential client, he would look at not only whether they are publicly listed but also *where* they are listed for some form of assurance regarding their financial status and stability:

> Sinopec, 85… nearly 90 percent of their balance sheet is actually… listed company in Hong Kong and that gives us confidence because once you've got a listing in Hong Kong or whatever, we know that your accounting is going to be of a better standard than your regular Chinese company. Even if it's listed in Shanghai, I don't know [how robust that company is] (Foreign manager of foreign bank: #37, 19 October 2006)

The opaque listing criteria and procedure for the SSE has been under increasing scrutiny and criticism (see Chapter 6.4). The discriminatory practice by the CSRC and other state institutions in their treatment of SOEs and private companies has resulted in unequal treatment with SOEs given special consideration (see section 7.2.1). This regulatory bias is especially apparent in the IPO process on the mainland. With a long queue of companies waiting to be approved by the CSRC for IPOs, SOEs often get to 'jump the queue' and have their applications fast-tracked and be publicly listed ahead of smaller, private companies. In this case, the latter often find Hong Kong a much more attractive option for a public listing. On the other hand, a company might prefer to list publicly in Shanghai due to the lower fees (accounting, brokerage etc.) and relatively less stringent listing requirements. For a cash-strapped SOE who might be 'fast-tracked', the SSE could be a better option for raising capital quickly. For a company that is looking to expand its operations overseas, it might be more advantageous to get the exposure of listing in Hong Kong and to obtain foreign currency in capital, but for a company that wants to focus on the large Chinese domestic market, it might get a better price per share with an IPO in Shanghai (where it is already well-known on the mainland) compared to an IPO in Hong Kong (where it might have to spend more money on advertising and publicity ahead of the IPO to raise investor awareness and interest).

The decision to list publicly on the SSE or HKSE could also be politically motivated. Special permission has to be given by the state for a mainland company to be publicly listed in Hong Kong. There had been some local concerns about the number of mainland companies who are listing in Hong Kong, particularly in the past three years when the Shanghai stock market was performing badly and new listings were halted in the midst of share reforms. The general impression was that the best Chinese companies were going abroad for public listings while the mediocre companies were the ones who stay and list in Shanghai (or Shenzhen). This generated some concerns about having the country's wealth and opportunities 'leaking' out of the mainland to Hong Kong and foreign investors rather than benefiting the Chinese citizenry:

> If the good companies choose to go to Hong Kong, the opportunities of China from its reforms and growth will end up being distributed to Hong Kongers or other foreigners, and the Chinese people don't get to benefit from these good companies, the benefits of reforms. If only mediocre companies stay in China and the good companies go to Hong Kong, that is an unequal situation. I think this situation will change, China is now also aware of this problem. Good enterprises should come back and issue shares here. (Local vice-director of Chinese securities/fund management company: #26, 18 April 2006; translated from Mandarin)

While this was arguably a myopic view, it reflected rather accurately the sentiments of some locals that I spoke to, both in formal interviews and casual conversation.

When asked about whether Shanghai could take over Hong Kong's position as the financial centre for China and the East Asia region, there seemed to be a divide in opinions between my local and foreign respondents. Most of my Chinese respondents were fairly confident about Shanghai's future and thought it had particular advantages over Hong Kong due to state support and its achievements thus far. In their view, the past and present success of Hong Kong was too reliant on China as its hinterland and its success in attracting high-profile IPOs of mainland companies was dependent on the Chinese state giving special permission for them to do so. Therefore, they saw the continued success of Hong Kong's financial markets as being dependent on China's economic and political development and since the central government was keen to promote and develop Shanghai's financial sectors, Hong Kong would likely become less important in the future. There was also a tangible sense of patriotism in the way the local interviewees responded to the issue of competition between Shanghai and Hong Kong. Although they acknowledged that there was still a considerable gap between the two in terms of regulatory frameworks, legal structures and skills and expertise in financial market and products, they tended to be almost dismissive about such concerns, being very confident that Shanghai would catch up and bridge that gap very quickly in a few years (five to 10 years were the most common estimates).

This was in sharp contrast to the sentiments of foreign interviewees who are more cautious in their assessment. In their opinion, Shanghai was in no way comparable to Hong Kong at the moment. One foreign respondent saw this comparison as almost meaningless, like comparing apples and pears, two entirely different entities, and that "it's only when you have two apples that you can make a financial centre out of one of them" (Foreign manager of foreign bank: #39, 24 October 2006). For many others, the scenario of Shanghai being on the same footing as Hong Kong in order to compete was as far away as 20 to 30 years in the future. For another foreign interviewee (foreign branch manager of foreign bank: #43, 27 October 2006), the non-convertibility of the RMB and the free port status of Hong Kong (within the setting of Greater China) were key factors holding back Shanghai's progress. Even though the headquarters of many companies were moving to Beijing and Shanghai, which had pulled some sales and services functions of banks onto the mainland as they followed their clients, the production functions such as dealing and treasury business were still conducted out of Hong Kong or Singapore as the non-convertibility of the RMB and foreign exchange restrictions were such that those activities were simply not possible in Shanghai at the moment:

> On the banking industry, it's definitely not comparable because Hong Kong is one of the freest economy [*sic*] in the world, it's a financial centre with convertible currency, so therefore it is completely not comparable. On the business side, it is different. Already the headquarters of many of the companies have moved away from Singapore and Hong Kong into Shanghai. So if you look at the client base, Hong Kong is losing out big time. But on the banking side, not yet, because the RMB is not convertible. (Foreign branch manager of foreign bank: #43, 27 October 2006)

Due to the very different regulatory and business environments, Hong Kong and Shanghai were developing as parallel markets rather than competing directly:

> As long as that kind of differentiation is still tolerated, for the financial market, that means there are two standards. And for the time being the Hong Kong is better and more appreciated than the Shanghai standard. And as long as Beijing is not willing to give Shanghai that kind of same treatment as Hong Kong, then I think that

> [Shanghai taking over Hong Kong] is not going to happen. (Foreign manager of foreign: #39, 24 October 2006).

Since the mid-1990s, Hong Kong has effectively taken on the role of international capital intermediation centre for China. In conjunction with the PRC authorities, it has helped develop a number of financial products and services, including the listing of PRC equities on the Hong Kong stock exchange, the listing of red chip companies[3] and the development of China-related venture-capital, private-loan syndications and planned renminbi (RMB) options. In addition to Hong Kong's link with China, regional consolidation of business in Hong Kong is another important focus for the business community. Both the organisation and distribution of regional financial services are managed out of Hong Kong and financial institutions have been focusing on attaining critical mass, enhancing productivity and differentiating their client relationship capabilities as the industry matures. There are minimal barriers to entrepreneurship and business entry, no discrimination against foreign investors, no special conditions attached to foreign investment, no exchange controls and no restriction on overseas remittance of capital or profits. Taxation is straightforward and rates are low by international standards. Hong Kong also benefits from a legal system that is based on the rule of law and the independence of the judiciary.

My foreign interviewees were careful not to dismiss the growing importance of Shanghai, especially in the light of the rapid changes over the past decade, but while Shanghai would continue to play an important role in the region and even exert some influence on the global market, they agreed that it would take a long time for its regulatory capacities to catch up to the level that it could really compete with

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[3] Hong Kong incorporated companies whose assets and business interests are predominantly in the PRC.

Hong Kong. As one of them put it rather bluntly, “there is no competition” (foreign manager of foreign bank: #41, 27 October 2006). Compared to other international financial centres in the region such as Hong Kong and Singapore, Shanghai was still very much in its infancy, as pointed out by the following two foreign interviewees:

> I think Shanghai will be *important* in global terms but it’s going to be a long time before it could *really* compete. Because markets like London or Singapore, which are regulated, but in a sort of free market way, are able to offer products, you know, sophisticated products and financial services without all the control, and I think it’s just difficult. (Foreign manager of foreign bank: #37, 19 October 2006)

> I mean, take a look at Singapore, take a look at Hong Kong, on taxation issues. From… what other issues are there to run a bank, how much quota do you have, fees… many issues. Regulatory issues, that’s mainly the point. That’s going to take a long, long time. Those are specific areas [that needs to be addressed before] Shanghai will become a financial centre but overall financial centre, I would say Hong Kong or Singapore. (Foreign manager of foreign bank: #41, 27 October 2006)

Although there seemed to be a general divide between the local and foreign respondents to regarding competition and comparative advantages between Hong Kong and Shanghai, there were a few (mainly Chinese officials and foreign interviewees) who did not see it as a purely competitive relationship between the two. The dual listing of companies on the Shanghai and Hong Kong stock exchanges was brought up as an example of the mutual dependence of Hong Kong and Shanghai. China Life, Sinopec, China Merchants Bank and ICBC were the biggest companies trading in both Hong Kong and Shanghai. While some companies such as ICBC opted to launch its IPO simultaneously in both centres, others had an initial listing in Shanghai and then sought a secondary listing in Hong Kong (or in London or New York). This strategy enabled the company to gain some experience in public listings and capital injection from the large Chinese domestic market before venturing overseas to woo foreign investors. This enabled them to benefit from the different advantages of listing in Shanghai and Hong Kong. For a number of foreign respondents, Hong Kong would also continue to have a niche market in offshore products, especially for foreign banks with limited business licenses on the mainland. Business operations on the mainland in cities such as Shanghai would thus complement operations in Hong Kong to serve their customers in the China and East Asia region with a holistic range of products and services.

Hong Kong's future role will depend on the development of its stock market, the maintenance of stable exchange rates, the development of its capital and debt markets and basic financial laws that guarantees that the financial sector remains intact after 1997 and the smooth financial cooperation between Hong Kong and China in the years to come. Much of those anxieties have been addressed by the Basic Law[4], which embodies the concept of 'one country, two systems', a term that has been most often used in a political sense. However, 'one country, two systems' also describes the financial systems, monetary authorities and currencies of China and Hong Kong, and describes not only the relationship that exists between these polities but also the stages of development of the two financial systems (Li, 1995: 40). Over the past decade, there have been concerted efforts at enhancing the market orientation of the finance industry in mainland China and to develop Shanghai as a financial centre. While Shanghai may grow to become an important domestic financial centre, China is still working to put in place several of the key elements that Hong Kong already possesses and its financial services market is still comparatively

[4] The principles of free enterprise and supporting legal framework were enshrined in the Basic Law of 1995, which became Hong Kong's constitution in July 1997. The Basic Law states that the government of Hong Kong SAR shall provide an economic environment that maintains Hong Kong's status as an international financial centre and promotes investment and trade.

restricted. China, as an evolving market economy, is only beginning to develop a suitable legal system while Shanghai also lacks an efficient banking sector, which is vital for a financial centre. Moreover, financial centres consist of more than banking systems; they are a network of financial markets and those in Shanghai are still in their infancy, in spite of rapid growth since the late-1990s. Even as Shanghai continues to upgrade its regulatory environment, Hong Kong already offers an internationally accepted regulatory environment and legal system with minimal government intervention. Finally, the development of an international financial centre in Shanghai is hampered by the lack of an internationally tradable currency. To believe that Shanghai and Hong Kong are destined for competition rather than complementarity neglects the differences, comparative advantages and challenges that each faces. Gaeta (1995), for example, argues that over time Shanghai is likely to evolve as the leading domestic financial centre and international gateway to North and Central China, while Hong Kong will emerge as the leading international financial centre and gateway to South China. This regional specialisation would be akin to the current specialisation of Singapore as financial hub for Southeast Asia and Hong Kong for East Asia (H. Yeung, 1998; Ho, 2000).

8.3.3 Functional Coordination

From the above, it is clear that Beijing, Shanghai and Hong Kong, in spite of common perceptions of rivalry and competition, each have their own distinctive characteristics and comparative advantages. Both my local and foreign respondents clearly saw distinctive roles for each city with Beijing being a ‘political centre’, Shanghai as a ‘business centre’ and Hong Kong performing the role of an ‘offshore financial centre’. This regional division of labour was reflected in the operations of the financial institutions located there, such as representative offices and investment banks in Beijing, commercial banks in Shanghai and treasury business in Hong Kong.

This concurs with Shi and Hamnett's (2002) study which compares the roles and development of Hong Kong, Shanghai and Beijing and suggests some form of functional coordination among the three centres to make up for each other's limitations. They suggest that Hong Kong would be kept as an international financial centre as it possesses distinct advantages in administrative capability, stability, knowledge and international reputation. The continued prosperity of Hong Kong is also important as the lack of confidence in the latter could have serious knock-on impacts on other Chinese cities, as well as affect the relationship between Taiwan and mainland China.[5] Beijing, on the other hand, could relinquish some economic functions and focus on its role as a cultural and political centre, giving Shanghai more room to develop its national economic and financial role. This is already evident in the moving of more market-based functions of the PBOC to its second headquarter in Shanghai, for example, while maintaining its policy-based and macroeconomic functions in Beijing. Hong Kong's role could parallel that of New York in the US economy as it continues to serve as the largest international financial centre linked to China and as the frontier on China's path towards globalising its economy, at least for the next few decades. Its superior administrative and regulatory expertise, free port status and international reputation are too far ahead of Shanghai's at the moment for them to be comparable. As Shanghai develops and acquires the necessary institutions, systems and skilled labour over time, it could then play a key

[5] Hong Kong is Beijing's bridge to Taiwan; the concept of 'one country, two systems' was devised with Taiwan in mind and is the basis for the policy of peaceful unification. Apart from political considerations, Hong Kong has also been instrumental in facilitating capital flows between Taiwan and the mainland, acting as a conduit for economic relations for those in South China and Taiwan to circumvent their respective governments' sanctions and controls (see Knox and Taylor, 1995).

role as the premier national financial centre with economic influence in the Asia region, similar to the role of Chicago in the USA, while Beijing would hold the position of national political and cultural centre with relatively weaker economic functions (Shi and Hamnett, 2002: 133). This view of complementary roles and functions was echoed by some of my respondents who view the relationship between Shanghai and Hong Kong as "*huxiang fubu*" (互相负补) (Chinese chairperson of private Chinese company: #1, 10 December 2004; translated from Mandarin) – mutually compensating and complementing, in their roles as financial centres. When one considers that China is the geographical size of Europe, notes the number of financial centres within Europe, and then also considers the size and potential of China's growing economy, it would be fallacious to expect China to have only one large international financial centre. London, Frankfurt, Paris, Amsterdam and Madrid are of varying sizes and importance in the regional and international economy, specialising in particular financial markets, products and services. New York, Chicago and San Francisco in the USA are further examples. Therefore, it would be reasonable to expect similar developments in China as its economy and institutional capacities develop with the need for more sophisticated and specialised financial products and services in different parts of a large country.

8.4 CURRENT ISSUES AND FUTURE CHALLENGES

Shanghai has made remarkable progress in the past 15 years in opening up its economy to foreign investors, implementing policies conducive for capitalist market development, developing the financial capacities of its firms and institutions, and raising its international profile as a prime location for business activities. In spite of these achievements, however, it still faces particular challenges in its aspiration to become an international financial centre, some of which have been alluded to in the preceding section as well as in Chapters 6 and 7. Most of my respondents from foreign financial institutions do not think Shanghai will become a financial centre on a similar calibre to Hong Kong for at least another 20 to 30 years. This finding concurs with other studies which conclude that while there has been astonishing progress, Shanghai's aspiration to be the financial centre of Asia will not be fulfilled for many years (Y. Yeung, 1996; Xu, 1998; Yatsko, 2001; Yusuf and Wu, 2002; Zhang, 2003).

In terms of building up the 'hardware' of a financial centre, such as setting up stock markets, establishing brokerages, and listing companies, it is catching up rapidly with other financial centres but the slow introduction of a financial centre's 'software' is holding the city back (Yatsko, 2001: 62-63). The 'software' capacities of information standards and regulatory structures need to be developed to match 'hardware' provisions in order for Shanghai to achieve its financial centre aspiration. This is an issue that the local government and regulatory authorities are aware of and often refer to as a discrepancy between the 'form' or 'structure' (形式*; xingshi*) and 'content' (内容; *neirong*) of development. A local interviewee who used to work on research projects for the SMG examining the development of Shanghai as an international financial centre agrees that there is a gap in achievement which the local municipal government acknowledges but finds it difficult to redress:

> When I was in the municipal government, we talked about 'form' and 'content'. The 'form' was very well done, look at all the things that have been built up, but the 'content', many measures and such were not done properly. Service levels not raised and so on. […] Now, these things [hardware aspects] are already put in place but I feel that it is [still] very difficult. Although you have set up the framework, the structure, it doesn't really feel like an international financial centre. But I can't say why. I can't really put my finger to it. (Local analyst for Chinese securities company: #34, 17 October 2006; translated from Mandarin)

This interviewee was unwilling to go into detail what precisely is lacking in 'content' but other respondents were more forthcoming with their views based on their experience of setting up and seeking business opportunities in Shanghai.[6] I asked my respondents what they thought were the most pressing issues and challenges currently facing Shanghai that must be addressed or resolved in the next five years in order for its financial sector and markets to move forward. The most frequently occurring topics included the regulatory environment, shortage of skilled labour, RMB convertibility, restrictions on foreign financial institutions, financial education and literacy, and corruption. Almost all of these fall under the 'software' or 'content' aspects and concurs with views reflected in other studies. According to Morgan Stanley's Jack Wadsworth (quoted in Yatsko, 2001: 62), Shanghai needs "a yuan convertible on the capital account; high-quality listed companies; a series of reliable intermediaries (i.e. securities companies); and finally the development of derivatives instruments and options [before it can be] an international financial centre of extraordinary proportions". Xu (1998) cites similar concerns in listing the criteria for a developed securities market that Shanghai has to meet: high standards of information reporting and disclosure; a substantial supply of stocks, well-developed information and communications systems and high standards of trading floor regulations (p. 119).

8.4.1 Improving Regulatory Frameworks & Environment

> *I don't think Shanghai can really compete with the other Asian financial centres until you've got a market that allows people to do what they want to do. And I think for the Chinese, with all the best will in the world, I think they know where they want to be but they just can't let go yet and they don't let go yet. (Foreign manager of foreign bank: #36, 19 October 2006)*

[6] This reluctance to commit themselves to particular opinions or details about specific projects is remarkably consistent with other interviews I conducted with other local regulatory and government officials. For more details, see Chapter 4.

Improvement to the regulatory frameworks and environment was the top cited issue that needed to be addressed. This was unsurprising given the regulatory problems discussed in chapters 6 and 7, be it due to over-regulation with too many rules and bureaucratic procedures, too many grey areas and unclear guidelines, opaque system of applications and approvals, or the lack of information and regulatory confusion between different regulatory bodies and branch offices. Although both local and foreign respondents agreed on the need to improve in the above areas, foreign financial institutions often bore the brunt of frustrations with the lack of regulatory clarity and lack of information particularly when they are new to the environment. A foreign respondent who opened a representative office recently in Shanghai was particularly confused about the types of activities permitted as they were not clearly specified. As argued in chapter 6, this allowed the regulatory bodies to fine tune its rules and regulations over time but created uncertainty for foreign banks who did not how far they should push the boundaries, particularly when they had to explain their actions and situation to the head office which might not appreciate the type of regulatory environment that they were operating in:

> I suppose from my perspective, we could do with some clearer regulatory rules and understanding of what can and can't be done, and what the limits are. I think there's a lot of grey areas which any society or regulatory legal framework has when it's developing. It simply doesn't know quite where the boundaries are. […] I still think there are lots of grey areas that is not crystal clear on what we [as a representative office] can and can't do. […] So, interpretation… And sometimes that works in your favour, that's in your advantage. But in other ways, you simply… particularly when you've got an audit team based in London who have a very clear black and white and then you've got this grey area here. (Foreign representative of foreign bank: #16, 9 March 2006)

Other respondents pointed out that reporting criteria and procedures, which were currently onerous and tedious, needed to be whittled down. Complaints about how "every time you do any transaction, if you do a loan, there are probably six work processes here that don't exist abroad" (foreign manager of foreign bank: #37, 19 October 2006) were common. The latter compared the situation between loan repayment in London and in Shanghai:

> In London, when a loan's repaid, the company pays in dollars, he'll pay our account at the bank, we'll see it on our account, when the loan matures, and that goes up against that and it's done. Here, when the loan is repaid, the money comes into our account, then we have to put the money off there onto a specific repayment account, which then goes against the loan account, which then goes into a SAFE declaration system to declare that we've got a million dollars that's coming in from this company, we have to input who it's come from, we have to get a tax code or a code number from the company, we have to match it up with the invoice we originally financed, which is in another system over there… We've got about four or five different computers which have… one is a PBOC, one is a SAFE one, and you have to input in all these data and it's just a *real headache*! (*Ibid.*; original emphasis)

Therefore, even as regulatory standards and expertise are being raised through learning from counterparts in other financial centres and recruiting overseas Chinese with relevant market experience into the fold, there needs to be greater clarity in existing rules and agreement between different offices about their interpretation. Unlike the FSA in London, China has different regulatory bodies for banking, insurance and securities, as well as SAFE for foreign exchange and the PBOC (central bank). Communication across all these organisations is far from seamless. Sometimes foreign banks found that they even contradicted one another in terms of specifying requirements and application process; better coordination and clarity were clearly needed. Regulatory procedures for daily reporting and common transactions also need to be simplified so as not to impede on business activities.

On the industry level, more needs to be done to improve the professional standards of the securities market, in terms of implementing stricter rules governing the behaviour of brokerage houses and security companies, improving accountability and upgrading the skills and knowledge of workers to cope with new ideas and products. This is of particular concern to the Chinese government as well as foreign investors in the light of scandals involving Chinese securities companies, accounting firms and listed companies over the past few years, which have increased calls for tighter rules and punishment.[7] In Shanghai, for example, there are two types of brokers dealing with local and foreign shares respectively. The existence of two share markets, a domestic A-share and an international B-share, has led to a divergence in professionalism between the two markets. They differ significantly in their information requirements in that issuers of B-shares have to meet higher standards of disclosure, according to international accounting standards, compared to issuers of A-shares. The continued existence of two parallel and divided markets, one strictly controlled by state-planning mechanism while the other is encouraged to introduce market forces and international standards into its operations, may not be sustainable. Part of the on-going share reforms is meant to address this divergence in standards between the parallel stock markets by closing the gap between A and B share requirements but only time will tell how successful these reforms will be.

[7] See BBC NEWS, 15 February 2002; Chung, 2005; Sun, 2005.

8.4.2 Raising Legal and Accounting Practices to International Standards

Many of my respondents (particularly the foreigners) suggested that the management and operation of the market economy system must change in ways that were consistent with normal international practices in order for the financial markets to be fully developed and Shanghai's aspirations to be realised. Although China's centrally-planned system has changed significantly since the adoption of Open Door policies, there is still substantial political motivation in governmental economic management functions. Since the mid-1980s, China has been gradually building a legal infrastructure, expertise and instituting legal procedures towards international standards, but the nature of Chinese legal and regulatory practices, as well as approach to enforcing regulations, still differ markedly from that of more open industrialised countries. Banking regulations in China are divided into 'published laws' and 'regulations', in which Beijing publishes the law while regulations are interpreted and implemented by local entities. This creates uncertainty, inhibits business dealings and raises transaction costs, particularly for foreign investors (Yusuf and Wu, 2002: 1222). Yatsko (2001: 77) relates how local investors' focus on anticipating government actions explains some of the volatility of China's capital markets. Instead of focusing their investments on companies with long-term prospects, most individual investors in China buy for short-term gains based on government policy changes, rumours, and the behaviour of particular government-backed market participants. There is a paucity of reliable information about public companies for investors to make informed decisions. With the government's unwillingness to promote an independent press, and the poor standards of disclosure of listed companies, it is unsurprising that local investors prefer to speculate rather than depend on unknown company fundamentals.

A foreign manager of a foreign bank gave an example of the difficulties of assessing a potential Chinese client as the numbers and accountancy data they provided proved to be unreliable:

> [This company was] selling to one of our very big clients in Italy, an Italian group that has production in France and Germany and so on. And we said, that's interesting, we'll go talk to them. We talked to them and we looked at the numbers. The numbers were OK. They had a parent company and the municipal government had about 40 percent ownership here, you know, the numbers were OK. There was a rating, a double-B plus or triple-B minus, around that level, sort of top end of non-investment grade. […] We've haven't actually done any dealings because they haven't actually exported any. And I went up there one day and had a look around and I said, 'Where is everyone?' And he said, 'Oh, we sent them all home'. 'Why is that then?' 'Because we're not producing at the moment.' 'Why not?' 'Oh, there's some problem with the parent company… issues.' […] And then a couple of days later it was out in the papers that there was some accounting scandal in the parent company. We would have been OK because we have the Italian company to finance but it's just, you just really don't have a clue what's going on. (#37, 19 October 2006)

The caricature of the Chinese company with three different accounts books (for the tax bureau, for the bank, and for themselves) is a real and persistent problem. This form of 'accounting with Chinese characteristics' is problematic in hindering accurate assessment of accounts and valuation of companies especially on the part of foreign banks who are unfamiliar with the local environment and frameworks. The Chinese MOF, which has the responsibility for regulating accounting matters in China, has set itself the objectives of fostering investors' confidence in financial information, increase transparency of financial reporting, and harmonising Chinese national accounting standards with International Financial Reporting Standards (IFRS), so as to reduce the costs of raising capital by enterprises and alleviate the risks of financial crisis. In 1993, with funding from the World Bank, the MOF engaged Deloitte Touche Tohmatsu as consultants to develop a body of Chinese Accounting Standards (CAS) broadly in line with accounting and financial reporting practice used internationally. Progress was slow up till the late 1990s due to the lack of perceived urgency at that time and the MOF has since adopted a 'need-based' philosophy of standards issuance. Since 2001, however (possibly due to the influence of WTO accession), efforts to further develop and implement CAS have stepped up. On 16 February 2006, the MOF announced that it had adopted a new basic standard and 38 new CAS that were substantially in line with IFRS, with a few exceptions. The MOF now requires all listed companies to start using the new CAS in their 2007 annual financial statements and the new CAS will be expanded to all SOEs starting in 2008, and then to all large and medium-sized companies in China starting in 2009.[8]

However, there are still particular obstacles as China develops and improves its national accounting standards to international requirements. A very significant portion of the economy is dominated by SOEs. Even after enterprises are restructured into joint stock enterprises and branched out from the government structure, functional or regional government that remain stakeholders still exert significant influences over the enterprises and their trading partners and their transactions. Unsurprisingly, many transfers of assets are government driven rather than motivated by pure business considerations. Financial statements are multi-functional, serving not only the needs of the investors but also other interested parties including the state and local government for supervisory and management purposes, which are not

[8] See http://www.iasplus.com/country/china.htm

accounted for in the IFRS. Enterprises and professional intermediaries such as auditors and valuers are also at the developing stage and will take time to mature.

8.4.3 RMB Convertibility

The convertibility of the RMB and relaxation of foreign exchange controls was another issue frequently cited as being crucial to further development of the banking products and financial markets in Shanghai. Although the RMB is no longer fixed to the US dollar and is now weighted against a basket of currencies, the margin within which it is allowed to float is very small. It is also so tightly controlled that most in the industry do not see it as really a floating currency – "It's not 'floating', it's 'jiggling'" (foreign chamber of commerce: #18, 14 March 2006).

Without full convertibility of the RMB, the banks are restricted not only in terms of derivatives and treasury products that they could offer (which restricts the development of capital markets) but are also limited in the more mundane business of loans and trade financing. SAFE is indirectly regulating the amount of foreign currency and RMB-denominated business that financial institutions as well as companies can conduct by controlling their individual licenses and foreign exchange quotas that each are subjected to individually, so as to manage the impact on RMB appreciation or depreciation. Foreign banks and other companies that wish to expand their operations in China are prevented from simply bringing money in from their headquarters or transferring from other operations in their global company network as foreign exchange controls limit the amount of money that they can bring in from abroad each year as well as remit back to their home countries. A foreign respondent was adamant that it is only when the RMB is fully convertible that treasury products and capital markets in Shanghai will take off and enable it to achieve the aspiration of becoming an international financial centre. Until that moment, everyone is just waiting and preparing for that day with under-utilised dealing rooms and having their treasury desks operating out of Hong Kong where there are no such restrictions:

> Actually there is only one moment when the financial markets in China can really take off and that is when the RMB becomes convertible, fully, freely convertible. Until that time, it's all lip service and it's all a little bit experimenting left and right but it's extremely annoying that for [some] financial products it's no longer possible because SAFE decides the impact is too big on the exchange rate… It's all 'Mickey Mouse' until the RMB becomes convertible. So when it becomes convertible, then treasury [business] becomes interesting. Until that time, everyone is building up dealing rooms to prepare for that moment. How long it will take? Hard to say. Five to 10 years…? (Foreign manager of foreign bank: #43, 27 October 2006)

There was also some concern about the transparency of the process through which the exchange rate was set. A Chinese respondent related how, in spite of the best efforts of his team, they could not figure out how the RMB exchange rate was determined, even using the set basket of currencies stated by the SAFE. This was problematic for the bank's own projections and business planning:

> Because although we have taken a small step, although now we have moved towards floating, I think it is quite difficult for [the RMB] to free float and the change is very small. They say it's linked, or pegged to a basket, but when we calculate it, we say it cannot be a basket because the weighting cannot be calculated! [laugh] We can't solve this problem, very difficult to tell how… what is the mechanism to determine the exchange rate. At the same time, not only the foreign exchange rate, but also the conversion, when corporates or customers, when they come into the bank to convert RMB into US dollars or back into RMB, a lot of… they still need to provide supporting documents to the banks, which means so many things [to be done]… (Local deputy head of capital markets for foreign bank: #15, 7 March 2006)

The tight restrictions surrounding foreign exchange also require a lot of documentation on the part of customers and the bank for every foreign currency transaction. The onerous reporting and documentation requirement is a recurring complaint for businesses in China in general; a freely convertible RMB would allow SAFE to do away with many of the documentation requirements and quotas which are currently limiting financial and non-financial institutions in their daily business transactions as well as expansion plans.

8.4.4 Greater Role for Foreign Banks

The foreign banks that I spoke to, in particular, were eager to push for regulatory changes to open up the finance sector further to foreign competition as well as a lighter regulatory touch on existing business sectors. A local interviewee who worked for a foreign bank (#15, 7 March 2006) expressed the frustration faced by others in the industry:

> China is really a highly regulated market. Without the approval or policy from PBOC, CBRC, or other regulators you *just cannot* do it! It's only with the introduction of new regulations, with the opening up, with the further liberalisation, that we can have access to certain markets. Even these markets, when we do some business, we are subject to some kind of restriction [… So the question is] when, how and to what extent will they release these kind of restrictions. The whole market is still under the full control of the regulators' side. (Original emphasis)

Foreign banks are required to establish a representative office for two years before they could upgrade to branch status; during that period, they have to pour large sums of money into the country under the minimum capital requirement. The minimum 'tier' of license that they can hold is foreign currency business with foreign corporate customers; to move up the 'tiers' to RMB-denominated business and

Chinese retail customers would require more capital commitment for each level of business license. The most recent requirement for local incorporation and the significant increase of registered capital to 1 billion yuan (to offer RMB banking services to the Chinese retail market) is a case in point (see section 5.5). Banks face no such restrictions in Hong Kong while they are severely restricted in Shanghai and other parts of mainland China. One reason for this is to restrict foreign competition until local banks have shaped up and can compete on better terms (see section 7.4.2), otherwise they are more than likely to collapse, and bankruptcy is unacceptable due to local social and political implications. A foreign respondent acknowledged that regulatory restrictions could not be removed all of a sudden but believed that they also could not continue without hindering Shanghai's development:

> Restrictions have to be taken away, but they can't do that suddenly, but that's what has to happen. We were saying at the meeting today, the European banks representation, there are so many rules and regulation on the banking industry and that's what's got to go away to create a free market. You have to have a free market for it to be a commercial, for a true financial centre. You've got all these regulation, a lot of which are geared clearly to keep the foreign elements out, therefore the competitive element out. Then you're not going to have a true financial centre. No way, cannot be. (Foreign president of foreign bank: #20, 11 April 2006)

Due to the various restrictions and difficulties for foreign banks, many were now less optimistic than before about the prospect of the financial sector in Shanghai/China; the initial euphoria has dissipated, especially over the past three years. When asked about foreign sentiments, a foreign respondent replied that, "people in the banks will, in public, still chant the mantra of Shanghai as an international financial centre, because to do otherwise would be political suicide. But in private, they know that it is not 'there' yet and will take another 20 years" (foreign chamber of commerce: #2, 17 August 2006). The Chinese regulators cannot force the local banks to undergo reforms on their own and need the help of foreign banks to raise the standards of local banks through competition. This means they have to be careful not to drive the foreign banks away through too much regulatory bias. Restrictions on products and services permitted for foreign financial institutions will have to be relaxed in order for the latter to have more influence in quickening the pace of marketisation and improving the finance sector through competition or joint ventures. This will be of particular benefit to Shanghai which already has the largest concentration of foreign bank presence in China.

8.4.5 Shortage of Skilled Labour

In terms of labour requirement, the local Chinese labour market has not kept up with the rapid growth of the finance industry. A number of local and foreign interviewees pointed out the problem of labour shortages particularly for local Chinese middle-managers. Over the past few years, salaries have spiralled ever upward in the search for Chinese workers with the necessary financial knowledge, language skills and professional experience. A local Chinese (not necessarily Shanghainese) with about five years' experience in the industry *and* English language skills could expect to earn almost as much as expatriate staff. Both local and foreign banks were also facing the problem of high staff turnover as people hop from one lucrative position to another in the tight labour market.

Table 8.5 shows the requirements posted by a foreign bank in a job advertisement for a relationship manager and credit analyst. The demand for English language skills is similar to other foreign banks that I have spoken to. However, this is not an issue only for the foreign banks; many domestic banks are increasingly looking to overseas markets and also need workers with English and other foreign language skills on board. A local respondent who was working in a financial institution as a result of a foreign-Chinese joint venture explained some of the problems faced by Chinese workers in a new environment where they had more responsibilities than they were used to and had to catch up on language and technical skills. He pointed out that this would not be a persistent problem as each generation attained more skills suited to the marketplace than those before but that it would be a slow process that takes time to develop:

> Actually there are many such finance managers in China who are very experienced and knowledgeable but they are unable to do all these things [… mainly due to] language, and also some technical skills. For example we are now using some IT systems from the foreign partners and for those that are around 40-50 years old, those who have never encountered these things before, they may find it more complicated. […] So if you go into a new company and want to learn something, the instructions are all in English and this can be difficult for those people. You need to have the professional knowledge, to be able to communicate, do presentations, travel and so on […] But I think things will get better. [Another interviewee in the same company] is a little younger than me, and their English is already much better than ours, and we are also better than those before us. For example when I am on business travel, most people cannot immediately tell that I am Shanghainese. If I am 10 or 20 years older, a Shanghainese on business travel, I may not even speak Mandarin, China's language, very well. This is a slow process. (Local analyst for joint-venture fund management company: #48, 3 November 2006; translated from Mandarin)

Table 8.5 Lists of skills requirements in a job advertisement from a foreign bank in Shanghai (Source: Bank website; emphasis added).

Relationship Manager
▪ Knowledge of the local market (customers and products)
▪ University bachelor degree in finance and accounting or related disciplines
▪ At least 4 years working experience in international bank, with marketing, credit knowledge and relationship with medium sized companies; or at least 6 years working experience in local bank, with solid credit knowledge and know SMEs market very well.
▪ Must be detail-oriented, with good analytical, interpersonal, communication and sales skills
▪ Possess personal qualities of independence, integrity and professionalism
▪ Self-motivated, hard-working, willing to travel
▪ ***Fluency in spoken and written English are mandatory***
Credit Analyst
▪ University bachelor degree in finance, accounting or related disciplines
▪ Minimum 3 years solid experience in credit analysis or risk management in banking sector with sound knowledge of bank products
▪ Solid knowledge of credit assessment for corporate customers with industrial background, familiar with SMEs is an advantage
▪ Familiar with techniques of quantitative analysis
▪ Familiar with regulations of CBRC,PBOC and SAFE
▪ Must be detail-oriented, with good analytical, interpersonal, communication and presentation skills
▪ Possess personal qualities of independence, integrity and professionalism
▪ Self-motivated, hard-working
▪ Need to travel occasionally
▪ ***Fluency in spoken and written English are mandatory***

A regulatory official pointed out that language skills were important not only to facilitate business communication on a purely transactional basis, but was also significant in learning and professional education, in the transfer of particular concepts and philosophies that were not present in the local languages. He described how English language skills had become important for promotional prospects even in the regulatory and government departments as they were seen as an indicator of the candidates' open-mindedness and grasp of foreign ideas and concepts. He described a recent recruitment drive for a new department in the Beijing office:

> They also used English during the interviews. So even if we are very good in our knowledge, if we can't get past the English language barrier, it is useless. We have

> many friends and colleagues who are very good but because they are not very good in their English, they have been passed over, which is a shame. Because language is not just a tool for communication, it also has cultural significance, it affects how you think, your ideology. If you can speak a particular language, it does not only involve a grasp of the language but also ideas, ways of doing things, all these things have to do with the language as well. (Local regulatory official: #25, 16 April 2006; translated from Mandarin)

As pointed out by Thrift (1994, 1998), the continued success of international financial centres such as the City of London is sustained not only by its geographical location, urban infrastructure and regulatory environment; its competitive edge is also constituted and sustained by communities of practice as highly skilled finance workers form a network of information, knowledge and interpretation that is crucial to the workings of a financial centre as it relies on the generation and interpretation of monetary information. The social and cultural constructions of a financial centre, particularly in terms of labour markets, need to be further developed. This situation should improve over time as the local labour force gain more experience, language skills and technical expertise. New graduates from Chinese universities are increasingly trained in English language communication. However, the pace of development in labour skills can also benefit from more resources and attention being put towards professional education and enrichment for those currently in the industry, to improve their skills and knowledge of new financial products and systems as well as a renewed emphasis on bilingualism in English and Mandarin. At the moment, there is little evidence of that happening in terms of professionalisation of the industry except on an *ad hoc* and individual (or bank-specific) basis.

8.4.6 Other Considerations

Corruption was not seen as particularly problematic in comparison to issues listed above. However, it was raised a couple of times as an issue generic to the Chinese business environment and not just for the finance sector or as a problem in Shanghai. One of my foreign respondents spoke of his occasional encounters with corruption in Shanghai and highlighted it as an area of reform that requires government attention:

> I think… giving someone particular favours or to speed up the process, that's bribery, that's corruption. And that does exist here. And that is something that I'm not familiar with. I'm not familiar with it in Hong Kong and I'm not familiar with it in London where I've worked. But I am beginning to be aware of that in China… I mean, it's not a big… it doesn't affect us hugely but I am certainly aware of that. And again sometimes as a foreign entity, you're not sure… […] In the environment where I'm at, no, it's not across the board, but I have come across it. And I've gone ooh…! [expression of surprise and aversion] It's a bit like being touched by a very cold poker, not sure that I like that very much! (Foreign representative of foreign bank: #16, 9 March 2006)

The Chinese government has certainly been very aware of the negative impact of corruption not only on international perceptions of China but also of costs to business and the social and political implications within its domestic sphere. In recent years, there have been many high profile charges and court rulings against characters such as the former head of China's food and drug administration, Zheng Xiaoyu (CBS News, 29 May 2007), the Vice-Mayor of Beijing (responsible for completing construction of sporting sites for the 2008 Olympics), Liu Zhihua (*Financial Times*, 11 June 2006), and the former Vice-chairman of the Bank of China in Hong Kong, Liu Jinbao (*China Daily*, 14 July 2005), on charges of embezzlement and taking bribes. According to the Xinhua news agency, almost two percent of the Chinese Communist Party, around 115,000 people, has been indicted and jailed for corruption and related charges.[9] The Chinese government has clearly indicated tackling corruption as a priority and some headway has been made. However, it will take time to resolve such a deeply rooted and pervasive practice and efforts at eradicating corruption and related practices must not slacken just as investors are gaining confidence of the government's determination to root out and punish perpetrators.

Other issues that could affect Shanghai's aspiration to be an international financial centre and continued development of its finance sectors include the sustained growth of the national and regional economy in order to sustain demand and growth for financial products and services, and political stability of the country. These are areas that the Chinese state is keenly aware of due to implications on its own political legitimacy and are addressing even now with national policies directed at resolving the income and regional inequalities, under President Hu Jintao's goal of developing a 'harmonious society'.

8.5 CONCLUSION

> *A lot of issues are… I won't say being written off, but looked through a lens that is quite rosy in terms of the long term. I think that in itself has worked very much in China's favour. People are very hopeful, and because they are very hopeful, they are willing to be very patient and that's something that other developing countries have not had that kind of chance. (Foreign director of foreign bank: #23, 14 April 2006)*

While almost all my interviewees were optimistic about Shanghai's future and eventual success, most of them agreed that the success of Shanghai as an international financial centre will be a long-term process and unlikely to happen for another two to three decades as there were numerous issues still outstanding and

[9] http://news.softpedia.com/news/Chinese-Vice-Mayor-Fired-Following-Corruption-Charges-26287.shtml

regulatory frameworks, skilled labour and market infrastructures to be developed. In this chapter, I examined the factors contributing to Shanghai's success, from narratives of historical success and eminence and central government policies to geographical location and cultural factors. Shanghai's achievements to date have also raised the issue of competition with other Chinese cities, primarily Beijing and Hong Kong. My research revealed a qualitative distinction in the roles of these cities, with Beijing as a 'political centre', Shanghai as a 'business and commercial centre' and Hong Kong as an 'offshore financial centre'. This was reflected in the operational structures and business strategies of financial institutions that I interviewed and suggested some form of functional coordination and complementary roles played by these top Chinese cities. In the second edition of *The Global City*, Sassen (2001) focuses on inter-city relations as "the emerging transnational urban system" (p. xvii) in which "specialised service firms need to provide a global service which has meant a global network of affiliates or some other form of partnership. As a result we have seen a strengthening of cross-border city-to-city transactions and networks (Ibid.: xxi). This idea of connections and systemic linkages is reiterated in her other writings (e.g. Sassen, 2000, Sassen, 2002) as she argues that global cities must engage with each other in fulfilling their functions, whether at a global or regional level, which gives rise to complementary forms of relations and alliances:

> In the initial stages of deregulation in the 1980s there was a strong tendency to see the relations among the major centres as one of straight competition among New York, London and Tokyo […]. But in my research on these three centres I found clear evidence of a division of labour already in the 1980s. What we are seeing now is an additional pattern whereby the cooperation or division functions is somewhat institutionalised: strategic alliances not only between firms across borders but also between markets. *There is competition, strategic collaboration, and hierarchy* (Sassen, 2002: 24, emphasis added).

Castells (2000) also argues that "the global city phenomenon cannot be reduced to a few urban cores at the top of the hierarchy" (p. 380) and postulates a global network that connects centres with different intensity and at different scales, integrating them at a global level. He provides a new context through which to view global cities: cities are a part of a space of flows that, in turn, constitutes the new network society. This approach has inspired geographers such as Peter Taylor (Knox and Taylor, 1995) and others at the Globalisation and World Cities (GaWC) Network and Research Group (Beaverstock, 2002). Taylor (1995), for example, assesses global cities in terms of their network connectivity by sector and by regions by analysing the location strategies of 100 leading global service firms across 315 cities. Instead of economic date, Smith and Timberlake (2001 [1995]), on the other hand, utilise data on flight connections between various cities as a tool to conceptualise inter-city linkages. All these points to the necessity of thinking about cities relationally, as the product of networking activities (Knox and Taylor, 1995: 27). The international financial system has reached levels of complexity that requires the existence of a cross-border network of financial centres to service the operations of global capital. This network of financial centres around the world is increasingly fulfilling gateway functions for the circulation of national and foreign capital. The incorporation of a growing number of financial centres is one form through which the global financial system expands; each of these centres is the nexus between the economic development of that country and the global market, and between foreign investors and that country's investment opportunities.

There will be an increase in specialised collaborative efforts between financial centres as the globally integrated financial system is not only about competition between centres. Nobody would really gain from crushing Hong Kong or Shanghai or Shenzhen. The ongoing growth of London, New York, or Frankfurt is in part a function of a global network of financial centres. Take Sassen's global cities, for example. New York, London and Tokyo are very similar in terms of their roles and functions as major hubs within the global financial network, but it is the differences that connect these cities in meaningful ways and integrate them into a network of capital, labour and information flows. A simple and obvious example is how their location in different time zones enables them to operate as a 24-hour unit. Their different geographical locations also offer different strategic advantages in terms of the products and services they can offer to the global market. These cities are highly interdependent and differentiated from one another at the same time. It is the very differences that make the networks/networking desirable and worthwhile in the form of "antagonistic cooperation" (Friedmann, 1995: 21).

The idea of flows and networks is vital in conceptualising global city networks but the place-based geographies of such flows are also important. Cities accumulate and retain wealth and power because of what flows through them and embedding cities in a space of flows thus directs our attention beyond simplistic concerns for what they contain to their *connections* with other cities. But by denying the global city the status of a place, Castells' view of a global city as "not a place, but a process" is in danger of abstracting it from its real geography (Knox and Taylor, 1995). We should not neglect the 'grounding' of flows, which is what transforms these cities, and is made possible only because global cities are also *places*. Sassen's (2000) "strategic places" and Storper's (1997) "privileged sites" are just two of many conceptualisations that view global cities as localised knowledge complexes based upon their particular mixture of innovation potential and capacities. London and New York are becoming more integrated, not only in terms of economic flows but also in terms of social and cultural linkages, into what has been called the "NY-LON phenomenon" (*Newsweek*, 13 November 2000). However, this is not so much the effect of a general death of distance, but an indication of how the space of flows connects places to one another and is actively reconfiguring the space of places. This perspective highlights the importance of historical, geographical and cultural contexts in explaining why particular 'marketisation' processes are taking place in Shanghai instead of other Chinese cities.

In the last section, I discussed the top cited concerns of my respondents regarding possible obstacles and future challenges for Shanghai in its aspiration to become a financial centre for China, if not the wider region. Top of the list were improvements to the regulatory environment, raising legal and accounting standards, relaxing controls on the RMB and the activities of foreign financial institutions. The shortage of skilled labour with the necessary language skills, financial knowledge and experience, issues of corruption and wider concerns about economic sustainability and political stability also need to be addressed. As stated in the opening quote to this chapter, most foreign investors in China, and even the locals, were very optimistic due to the enormous potential and opportunities available. This optimism had coloured their perspective such that they tended to be rather forgiving and patient and more willing to bear with what they saw as temporary obstacles in the hopes of future gain. However, if the above issues are not resolved in near future, the Chinese government and regulators may run the risk of using up this well of optimism and damaging business sentiments and its international reputation.

Chapter 9

Conclusion

Opening the Black Box of 'Markets'

> *The fundamental difference between socialism and capitalism does not lie in more planning or more market. Planned economy does not equate with socialism – capitalism also has planning. Nor does market economy equate with capitalism – socialism also has [a] market. Both planning and market are economic means… Planning and market that serve socialism are socialist; whereas planning and market that serve capitalism are capitalist… The essence of socialism is to liberate and develop the productive forces, to maintain the public ownership system as the mainstay of the economy, to eliminate economic exploitation, to avoid polarisation of rich and poor, and to achieve ultimate common affluence. (Deng Xiaoping, quoted in Yao, 1998: 27)*

9.1 INTRODUCTION

China has undergone enormous transformation since the Open Door policy in 1979. As one of the most open cities in China, Shanghai's economy has been at the forefront of those changes. Shanghai's state-sanctioned role as the 'dragonhead' to connect China to the global economy is best exemplified in the development of its financial sector. While expectations were high, particularly in the early 1990s with the opening of the first stock exchange (the SSE) in China, the process of developing financial services, products and markets in Shanghai had been fraught with difficulties and contestations over the form, structure and pace of reforms. Recent efforts at share reforms, further relaxation of rules regarding foreign participation and investment in the financial sector and China's WTO accession have provided a unique opportunity for using the changing empirical reality to critically interrogate the extant literature on the geographies of money and finance and conceptualisations of markets.

In this chapter, I reflect on the theoretical and empirical strands of the thesis as I situate my research within broader debates in geographies of money and finance and the literature on 'markets' in the wider social sciences. In section 9.2, I analyse the different approaches to 'markets' presented in the preceding chapters and highlight their empirical and theoretical significance. I also consider what might be the 'right' approach from the perspectives of different actors involved, such as foreign financial institutions and investors, domestic financial institutions, local investors, the central Chinese government and local governments. Section 9.3 reflects on and justifies the major strengths and weaknesses of the research as a whole and suggests ways in which it might be extended empirically, to include comparisons and co-analysis with other Chinese cities and international financial centres, and theoretically, through developing a research agenda centring on the complex and contested nature of market formation and issues of global standards and governance. Finally, in section 9.4, I reflect on how deconstructing markets, market relations and market ideologies can enrich our understanding of the processes taking *place* in financial centres and the spatialities of global capital, and challenge the neoliberal market discourse.

9.2 ANALYSING APPROCHES TO MARKETS

The central aim of this thesis has been to critically engage with the concept of 'markets' and 'from-plan-to-market' economy in order to expose its multiple identities and conceptualisations and the contested nature of the 'marketisation' process. The tendency to treat market exchange as the atomic structure of all economic processes and as the *default* form of economic coordination is problematic as other forms of organisation become marginalised or treated as problematic exceptions. The market optic (Sayer, 2003) and its normative presumption mystifies capitalist dynamics and social relations without actually examining how they operate in different historical and geographical contexts. This is particularly significant given the prevalence of neoliberal dogmatism and fatalism, which hails a particular model of economic development as the only workable model. The assumed progression of market practices in socialist economies is a case in point. During the post Cold War period, governments, economists and commentators often focused on the privatisation of formerly communist economies and policies aimed at a transition from planned to market economy. This approach, however, neglects the complexity of institutional legacies that differ across Eastern Europe and China and assumes a form of market essentialism that forecloses alternative forms of exchange relations and structures.

9.2.1 States and Markets

In the opening quote of this chapter, Deng Xiaoping demonstrates particular insights into the mutually constitutive roles of planning and market mechanisms in economic development. In this thesis, I have used the term 'marketisation' to refer to the on-going process of instituting market-led practices into the Chinese economy. Instead of an unproblematic and progressive journey from centrally-planned to market economy, China's experience demonstrates the complex and highly contested nature of market systems and practices. Rather than the wholesale adoption of neoliberal market practices and principles, the Chinese state continues to exercise considerable control over the pace and structure of reforms with clear political and social objectives in mind. In this thesis, I have therefore sought to highlight the unique conceptualisation and utilisation of 'market' practices by the Chinese state and institutions and to distance myself from the conceptual baggage often implicated in popular discourse about market-based economies and practices.

In acknowledging that markets are the products of social relations that vary across time and space, my empirical research in Shanghai examined how financial markets were being constructed, regulated and reproduced in a complex and highly contested process. China's experience of developing financial regulatory standards, in particular, demonstrated how different interpretations and agendas affected the process and outcome of re-regulation. According to the concept of hegemonic stability, a particularly strong state is likely to impose order on international financial system according to its standards. In the case of China, however, there appears to be no one 'preferred' system for financial regulatory standards and control. Although there seemed to be a preference for London's model à la the FSA[1], China was also developing its financial regulatory framework by incorporating expertise and elements from other financial centres such as Hong Kong and Singapore. In developing the CAS, for example, it also drew heavily from the IFRS championed by the US. This cherry-picking demonstrated how China was developing standards and frameworks unique to its economic environment and political context. Clark et al.'s (2001) study on the adoption of international and US financial accounting standards by German corporations revealed that the process of harmonisation to international accounting standards is not one of complete submission to the forces of global finance and economic logic. Instead, they highlight the coherence and persistence of German institutions and traditions and how new methods and systems are often accommodated within these institutions rather than overwriting them. The importance of 'difang hua', or localisation, as a guiding principle was echoed

[1] On 13 September 2007, Northern Rock received an emergency bank loan from the Bank of England due to the tightening of inter-bank lending over fears of the sub-prime market in the US. The following four days saw the first bank run in the UK for decades and doubts were raised regarding the regulatory division of labour between the Bank of England, the Treasury and the FSA. It remains to be seen whether this have had any impact on the desirability of the UK's mode of financial regulation to counterparts in China.

throughout interviews with government officials and local respondents, and provided a strong critique of the market optic that prescribes a unidirectional journey from 'planned' to 'market' economy. China's experience demonstrates a world of 'post-hegemony', whereby different state actors are linked into different policy communities as they increasingly operate within transnational networks, with the agencies such as the CBRC and PBOC establishing networks with counterparts abroad as well as with multinational financial institutions to access particular knowledge networks and develop the necessary skills and expertise for an international financial centre in Shanghai.

In response to the common critique of a lack of administrative transparency and 'fuzziness' in Chinese regulatory standards, many of my respondents pointed out it was a misconception that there were *insufficient* laws in China to govern property rights and rules of exchange; the real problem lie with their *execution and enforcement*. Their characteristic vagueness allowed for more specific treatment and interpretations by local authorities according to local contexts, but the lack of clarity proved highly confusing and frustrating for foreign investors who might not understand their rationale and mode of operation. Through consultations, working groups, position papers and training programmes, foreign financial institutions and regulatory bodies had contributed to greater clarity of new and existing regulations with some success as seen from the on-going drafting and re-drafting of laws and policies to govern new and existing products and markets. However, the Chinese regulators clearly valued the ability to control market activities through an opaque system that granted them the power and flexibility to quicken, interrupt or slow down the process of 'marketisation'. It also allowed for adaptation to local needs by local branches in the context of a large country with varied regional and local political economies. As such, the ‘fuzzy’ characteristic of Chinese laws and regulations is likely to continue while particular areas within are refined in response to changing local, national and international considerations.

In examining the role of the state in the process of ‘marketisation’, it is interesting to note the extent to which the views and perceptions of my Chinese respondents appeared to be strongly influenced by state actions. This was particularly evident in the view of local respondents that Hong Kong as an international financial centre and its dominant role in the Asian region would eventually give way to Shanghai as the former was too dependent on Chinese IPOs, which had to be approved by the Chinese state. By that extension, the success of Hong Kong becomes dependent on the ‘approval’ of the mainland government who will surely not jeopardise the success of Shanghai as an international financial centre on the mainland – at least from the perspective of my Chinese respondents. This ‘patriotic’ reading of the future of Hong Kong and Shanghai reflects more than the cultural bias of mainland politics; it reveals how the dominant role of the state in the finance sector is such that its actions or policies are seen as determining possibilities and likelihood of success or failure for what are commonly seen as ‘market’ decision. Likewise, even foreign banks have taken on the ‘state’ lens in believing that the SOEs are too big and too important to fail because they have government backing, and are thus ‘good investments’. The Chinese state, I would argue, is central to the operation and development of financial markets in Shanghai, not only in terms of allowing products and services to be offered (especially for foreign financial institutions) but also in terms of being an important actor in financial markets (by controlling the amount of shares being offered in the primary market and liquidity in the secondary market) and by being a key consideration for business strategies for both local and foreign financial institutions. Therefore, if one considers the argument of neoliberal market capitalism, that the 'rolling back' of the state is necessary for the development of successful 'market' conditions, there are undeniable contradictions in the Chinese context where the 'markets' are *made possible* on account of the strong role of the state. If the state should completely withdraw its influence and control over the SOEs, for example, that could trigger a massive loss of confidence as foreign and local investors have few other reliable criteria to judge these companies with.

9.2.2 Contested Visions of Markets

In this thesis, I have sought to incorporate issues of power and conflict in examining the socially constituted economic systems and practices, following Sayer's (2003) critique of the tendency to produce an overly benign view of economic relations and processes in theorising about embeddedness, networks and trust. This idealistic and 'soft' conceptualisation of networks downplays issues of power and inequality. In this vein, my research reflects Fligstein's (2001) conceptualisation of market institutions as emergent and forged through political contestation. In my research, I have highlighted the variety of actors and interests within a market setting and emphasised the importance of power, conflict and processes of negotiation and resolution in understanding 'markets' in Shanghai. The development of the Shanghai stock market demonstrated how the concept of a stock market presented different opportunities and different purposes to different groups of actors. The different perspectives of foreign and Chinese actors in the banking market regarding financial sector reforms were reflected in their business strategies in Shanghai, which varied from an aggressive move towards offering comprehensive banking services, to selective joint-ventures with local financial institutions (in areas such as securities, asset management and insurance), to focusing on niche markets.

More significantly, there were multi-scalar dimension to these contestations over the structure, direction and pace of financial sector reforms, between central government, local municipalities and regulatory bodies, between foreign and local financial institutions, between financial institutions and Chinese regulatory bodies, and even within financial institutions themselves. While the central government and regulatory bodies in Beijing might be keen on maintaining a slower pace of reform for fear of creating social and political instability, local officials and regulatory bodies who were in more frequent contact with the finance and business community might be in favour of further and more rapid regulatory changes that would allow for higher levels or more innovative forms of business activities to boost local economies. Foreign financial institutions were understandably frustrated at having their business growth curtailed due to the many tiers of licensing and capital requirements meant to limit their 'threat' to domestic financial institutions and viewed such restrictions as unfair. Domestic financial institutions, on the other hand, were adamant that they should have enough time to develop their own capacities before being subjected to foreign competition due to different conceptualisations of 'fair competition'. Both groups of actors were constantly pressuring regulators to act in their favour as regulatory standards and reforms were being developed and implemented. Organisational politics were also implicated in the 'marketisation' process as foreign banks within Shanghai and their head offices situated elsewhere had different visions of the Chinese 'market'. Therefore, an analysis of the development of 'markets' in Shanghai needs to be embedded in a network of political power, interests, and capital flows that extends not just to rest of China but also transnational actors beyond. Developments in Shanghai are arguably the outcome of political and economic processes elsewhere, with institutional forces in Beijing still determining the pace and process of 'marketisation' in Shanghai, and the influence of the international business community on developments in Shanghai depending on how Shanghai (or China as a whole) fits into their globalisation strategies.

9.2.3 Placing Markets

In this thesis, I have argued for a geographical sensibility to the treatment of market relations and processes. The world of money and global finance has a distinctive geography, particularly in terms of its multi-scalar and place-based nature. In the preceding chapters, I have shown how the development of financial markets in Shanghai was driven and influenced by processes elsewhere (be it in Beijing, Hong Kong or other financial centres in Europe) and this process was negotiated amidst contesting perspectives regarding the form, structure and pace of these market reforms. Sensitivity to the importance of scalar politics in such processes is a useful geographical contribution to the money and finance literature as these flows and processes operate at a number of different spatial frames or scales.

The place-based geographies of such flows and processes are important as they do not simply occur 'out there' in electronic space. The 'grounding' of capital or knowledge networks, which is what transforms these global financial centres, is made possible only because financial centres are also places. Sassen's (2000b) "strategic places" and Storper's (1997) "privileged sites" are two such conceptualisations that view global cities or international financial centres as localised knowledge complexes based upon their particular mixture of innovation potential and capacities. In the case of Shanghai, the 'marketisation' process was enabled by a variety of place-specific factors that led to its government sanctioned role and current development as an international financial centre for China, ranging from its history, geographical location, state support and business culture (as discussed in Chapter 8). There were geographically specific reasons for why such processes were happening in Shanghai rather than, for example, Beijing or Shenzhen. The historical image and contemporary branding of Shanghai as a cosmopolitan world city and international financial centre played a particularly significant role in its development strategies as seen in its prominence not only in official discourses and (state-controlled) media representations, but also in the expectations of foreign investors. These expectations, in turn, influenced the business practices and activities of financial institutions. The 'market' in Beijing, for example, was concerned with research activities, lobbying and regulatory matters, while the 'market' in Shanghai dealt with actual business transactions such as trade financing, commercial lending, and foreign exchange. Distinctive roles were thus carved out for each city with Beijing being a political centre, Shanghai as a business centre and Hong Kong performing the role of an offshore financial centre. This regional division of labour was reflected in the operations of the financial institutions located there, such as representative offices and investment banks in Beijing, commercial lending and trade financing in Shanghai and treasury business in Hong Kong. The socially inflected approach that I have taken in teasing out the motivations, rationale and practices of market actors in Shanghai has thus contributed to a more nuanced understanding of the 'marketisation' process taking place in Shanghai. A geographical sensibility in analysing market structures, relations and processes is vital to our understanding of the international financial system, relationships between state actors and global capital and how financial centres operate within international monetary networks.

Shanghai's experience also highlights the importance of context in the critique of neoliberal conceptualisation of market reforms. History matters; there is a need to understand the past in order to explain present phenomena and processes. In terms of policy-making and recommendations, this has implications for the transferability of solutions; the same rule or solution may not create the same type or magnitude of development in different places due to their specific historical experiences and institutional configurations. In the formation and adoption of regulatory standards and frameworks, for example, the Chinese authorities were keenly aware of such constraints in economic and political models and their relevance in cross-applications, even as they were eager to learn from the experience of other regulatory regimes. In contrast to models of stage-by-stage linear economic development with the input of the requisite economic factors, the 'marketisation' process in China pointed to the possibility of alternative approaches to markets and highlighted the importance of contextualising such approaches to local historical, geographical, social, cultural and political circumstances.

9.2.4 The 'Right' Approach to Markets?

In the response of my interviewees – particularly foreign respondents but also some of my Chinese respondents in regulatory capacities who had overseas experience – there seemed to be an implicit assumption of what is the 'desirable' or 'right' approach towards 'marketisation' of China's finance sector. A foreign president of a foreign bank (#20, 11 April 2006) in Shanghai, for example, insisted that:

> You have to have a free market for it to be a commercial, for a true financial centre. You've got all these regulations, a lot of which are geared clearly to keep the foreign elements out, therefore the competitive element out. Then you're not going to have a true financial centre. No way, cannot be.

From the perspective of foreign investors in the banking or securities sectors, the right approach would be to remove regulatory restrictions and barriers to entry. This would enable foreign financial institutions, most of whom have more experience and expertise in financial products and systems that China was just starting to develop, to have greater influence in quickening the pace of marketisation and improving the finance sector through competition or joint ventures. Without restrictions on foreign exchange or capital requirements, for example, they would be able to expand their business activities in China much more quickly, which would increase the growth of financial markets as well as the China business of their clients in manufacturing and other sectors. For local financial institutions, however, the right approach would be to restrict the activities and expansion of foreign financial institutions in order for the former to develop their own skills and capacities so as to avoid being overwhelmed by foreign competition. While domestic banks were mostly keen to learn and adopt new techniques and systems, there was widespread concern about the time it would take for them to be brought up to par with foreign financial institutions (be it in terms of credit systems, customer service, or international experience and networks). Joint ventures and other limited forms of participation for foreign financial institutions was seen as helpful for knowledge transfer to domestic banks and buying them time for implementing reforms and improving skills and standards, so that they could then compete 'fairly' with a strong domestic financial sector.

To the central government and regulatory authorities, the right approach towards 'marketisation' was to develop a 'socialist market economy' that would uphold the principle of preserving 'public ownership' (by the state) and 'cooperative ownership' (based on contractual arrangement among the employees, enterprise, and the state) as the mainstay of China's economic system. This was reflected in the practices of a quota system for the primary equity market, segmented share structure, restrictions on the trading of shares held by the state (and its affiliates) in the secondary stock market, and significant state influence over the activities of state-owned banks such that it resulted in the dominance of state ownership amidst private ownership. Controlling the structure and pace of reforms to the finance sector such that it limited foreign participation and the implementation of new financial products and services might restrict the growth potential of this sector and the development of Shanghai as an international financial centre. But this cautious approach enabled the central government to observe the impacts of new market systems and practices, to limit negative externalities that might have social and political consequences. From the perspective of local government and regulatory officials, having the freedom to interpret broad and 'fuzzy' guidelines from the central government and implement them according to local contexts was highly useful. This freedom to interpret and implement specific regulations could be abused to satisfy personal agendas (such as favouring particular individuals or local institutions over other Chinese or foreign counterparts) but such a multi-tiered system of governance helped to avoid the problem of inappropriate policies for a country with enormous social and economic disparities. Therefore, while foreign financial institutions might complain that regulatory 'grey areas' and 'fuzziness' were obstacles to developing robust, transparent and efficient markets, these characteristics offered enormous flexibility to local officials in ways that took into account local contexts and interests, to develop market systems and practices that were appropriate for local economies.

In this thesis, I have highlighted the multiple and contested visions of markets in the banking and stock markets from the perspective of different actors. In this vein, the 'right' approach to markets very much depends on whose vision of 'markets' is more persuasive, or rather, who has the power to determine or influence the version(s) of markets that is implemented, even though this process is fluid and unstable and subject to constant negotiation. Therefore, there is nothing 'natural' or 'unstoppable' about the move towards market-based economic structures and activities, at least in the neoliberal conceptualisation most commonly represented in the media. In the preceding chapters, particularly in terms of the responses from my foreign interviewees, there seemed to be an implicit assumption that China must inevitably embrace a neoliberal agenda, to remove regulatory restrictions and open up its financial markets to foreign participation and competition, if it is to develop further. This thesis has thrown doubts on that assertion by showing how the process of developing market systems, structures and practices is far from straightforward and fraught with the difficulties of balancing different visions and agendas, and by highlighting the dominant role of the Chinese state, which, to some extent, might even be necessary for the success of Shanghai by providing a source of investor confidence and the basis upon which actors in the market assess market conditions and opportunities (or lack thereof) and adjust their business strategies and activities accordingly.

In *The Writing on the Wall*, Hutton (2007) argues that China has no choice but to complete the full transition to capitalism that it has embarked on, that it cannot continue with its current model of market socialism due to inherent contradictions.

The past two decades of reforms have been extraordinary as China introduced what Hutton calls the 'hard' processes of a market economy, such as free movement of prices, wages and rents, permitted (albeit limited) ownership of private property, and opened up to overseas investors. But he argues that the 'soft' institutions of capitalism are as integral to growth and sustainability as the hard processes and these have been neglected thus far by the CPC leadership due to its formal adherence to the doctrines of Marxism, Leninism and Maoism and emphasis on political control. Examples of the soft institutional infrastructure that are lacking include "impartial courts, clear property rights, commercial processes for bank lending, independent auditors, accountability to a free press, independent trade unions, effective corporate governance, transparent anti-monopoly rules, free intellectual inquiry and even a properly functioning welfare system" (p. 6). He highlights the delicate balance being maintained at the moment between reform and control and argues that the Chinese economy is in danger of being upset by a banking crisis, or a crisis of excess supply (thus the recent concerns regarding an overheated Chinese economy), which will provoke social reactions that might endanger the political status quo. As such, the current situation of trying to maintain political control over what might be seen as only half a market economy is unsustainable. The only way a market economy can flourish, he argues, would be for China to accept and develop institutional infrastructures that promote economic pluralism and confer political pluralism.

Sayer (1995, 2003), on the other hand, argues for a more nuanced approach to markets in terms of its characteristics, and as systems and practices. He points out how 'the market' has become something of an icon, fetishised as having powers and authority of its own, to which people and institutions must conform. More importantly, the pervasiveness of the 'market optic' (Sayer, 2003) has led to the normative treatment of capitalist social relations of production and neoliberal systems of regulation. In the former socialist countries, for example, 'markets' (in the neoliberal sense) have been treated as a panacea even though their recent experience is already demonstrating the inadequacy of liberal market theory. Sayer (1995) is particularly clear regarding the importance of *multiple* conceptualisations of markets and the dangers of conflating market and capitalism: "markets can exist outside capitalism, and hence they should not be seen as equivalent" (p. 81).

Finance capitalists (be they individuals or institutions) have come to wield considerable power due to the amount of capital they control and the ability to switch the location and direction of capital flows in acts of regulatory-spatial arbitrage. This has led to speculations about the imperative of financial power overtaking the state as the latter becomes caught up in the desire to attract and retain these capital flows. This decline in state power vis-à-vis finance capital is not readily evident in the case of China's approach to 'marketisation' and the development of Shanghai as a financial centre; state control is still undeniably dominant at the central and local levels of governments and state institutions continue to play vital roles in the financial markets. Perhaps this particular approach to markets will limit Shanghai's success in a global financial architecture where the rules governing monetary flows are structured according to neoliberal market principles different from its own (such as the IAS, systems of determining foreign exchange and interest rates, and prudential regulation). On the other hand, if one considers the benchmark for success from the perspectives of the Chinese state and state institutions and domestic financial institutions, Shanghai's success could also be measured by the willingness of foreign financial institutions to play by the Chinese rules of limited engagement and activities while allowing for the continued dominance of Chinese financial institutions, 'public ownership', and state control in the financial markets. The findings of this thesis highlight the politics of market systems and practices and the limits of financial power vis-à-vis the state. Just as 'the market', as conceptualised by the far right and neoliberalists, is shown to be contested and unstable 'markets' with multiple interpretations and identities, the 'state', so often thought of as a monolithic entity particularly in a socialist regime like China, needs to be acknowledged as a fragmented entity with different agendas and visions at the levels of the central, regional, and local governments, and within the regulatory bodies spread across different spatial scales. Research on geographies of finance and regulation, therefore, needs to go above as well as below the 'state' (in its conventional conceptualisation) to examine supra-national and sub-national networks and processes of governance, through the roles and actions of transnational and local agents.

9.3 REFLECTIONS ON THE RESEARCH

Having highlighted the empirical and theoretical strands of the thesis and identified its contributions to a geographical perspective on 'markets' in understanding financial centres and global capital flows, this section reflects on some weaknesses and limitations of the research. Given the complex economic geographies of 'marketisation' as identified in the preceding chapters, some facets have invariably been overlooked in writing up the research to product a logical argument within the time constraints of a PhD programme. It is not my intention in this thesis to produce an assessment of which approach to 'markets' is the most desirable or 'best practice'. Instead, my aim has been to highlight the multiple conceptualisations of markets, and the contested process of instituting reforms driven by a variety of actors with differing politics, agendas and power.

Empirical research undertaken for this thesis took place at a particular time when the Chinese stock markets were undergoing major reforms, when IPOs were recently halted on the mainland with major listings turning to Hong Kong and other overseas markets, and when China was in the final stage of fulfilling its WTO commitments. If this research had taken place in the 1990s, it might have taken a different direction in focusing on the success of the newly established SSE, when the stock market was on a bull run and expectations were high on the part of both foreign and local investors. During the course of my research, the Chinese stock markets were just recovering from a slump and new IPOs were suspended as share reforms were carried out to erase the division between tradable and non-tradable shares and to allow for greater participation by foreign and domestic investors in previously restricted segments of the stock market. During this sensitive stage of reforms, it was impossible to obtain interviews from people working in the SSE as they were unwilling to speak in an official capacity. Due to the timing of the research as well as lack of personal contacts that could connect me directly with specific people in the SSE, I was not able to undertake any participant observation within the SSE that could have enriched my understanding of the practices and perspectives of this group of actors from within this particular financial market. Following the snowballing method, interviewees who mentioned that they have friends working in the SSE were asked if they could put me in touch with those contacts. Invariably, however, those contacts declined to be interviewed as they felt uncomfortable about having an outsider enter their premises and scrutinise their operations in the light of on-going reforms. However, I was able to interview some locals from domestic financial institutions and a government official who used to work for the SSE, who did not feel the same constraints in sharing their views and experience.

Another limitation of the field research relates to the selection of actors interviewed. My ideal sample would have been an even number of respondents from three groups: Chinese government and regulatory bodies, foreign financial institutions, and domestic financial institutions. In the end, I was only able to conduct three interviews with government and regulatory officials and I had greater success contacting foreign respondents compared to local ones. Reasons for this include the specific Chinese environment of information dissemination and my positionalities as a not-quite-Chinese scholar (read differently by different respondents), as detailed in Chapter 5. I have tried to overcome this under-representation of government and regulatory actors by actively seeking the views of other respondents from financial institutions on local regulatory processes and frameworks and their encounters and interaction with officials and regulators. I also tapped into the expertise of some Chinese respondents who used to work for regulatory bodies. This provided a means of triangulation and helped me to corroborate what I read from official or publicly available reports with a spoken discourse. My interview success with individuals from foreign financial institutions meant that I was able to obtain unexpectedly detailed accounts of the experience and perspectives of this group of actors, which enabled me to learn more about their strategic practices and business activities in the face of regulatory bias, internal politics regarding conflicting visions of the Chinese 'markets' within transnational organisations and their geographical readings of markets in Beijing, Shanghai and Hong Kong.

Beijing and Hong Kong were initially considered as additional fieldwork sites, especially in the light of the significant regulatory and operational linkages between Shanghai and these important centres. Unfortunately, they had to be excluded primarily due to issues of practicality and time constraints. The importance of regulators and decision-makers in Beijing was evident from my field research in Shanghai and in research by other scholars, but the difficulty of obtaining interviews and useful information during meetings with officials in Shanghai raised doubts about the usefulness of such interviews in Beijing. Given the reluctance of government and regulatory officials to grant interviews and their taciturn approach when such permission was obtained, I concluded that my limited time and resources in the field would be better spent obtaining richer and more in-depth accounts in Shanghai rather than spreading myself too thin by adding Beijing as another case study. My experience in Shanghai has revealed a very steep learning curve upon arrival into a new environment and it took a long time to establish local contacts that have proved vital in fieldwork. In the case of Hong Kong, while I already had a couple of contacts and anticipated less difficulties in obtaining interviews and materials such as reports and other published information, the relevance of a trip there seemed less important as my research focus shifted in the course of fieldwork to analysing developments in Shanghai itself, rather than a comparative study with Hong Kong's experience. However, I have not ignored the important linkages between these cities and included them in my analysis by using interview data from respondents based in Shanghai to examine the different roles played by Beijing, Hong Kong and Shanghai in the development of financial markets in China, and to investigate how Beijing and Hong Kong are viewed by actors based in Shanghai in terms of competition or complementarities with Shanghai. In order to maximise resources at hand with the objective of enriching empirical data, I conducted some interviews in London, following up on pilot interviews as well as contacts obtained from foreign respondents in Shanghai. This included banks with operations in Shanghai and the FSA, who provided advice and consultations to the Chinese regulators. The inclusion of London as an additional field site proved useful in obtaining feedback on preliminary findings, providing an alternative perspective on events and processes in Shanghai and acting as a check for possible bias in interpretation and highlighting issues relevant to those in the industry.

There is clearly scope for further research in interrogating actors based in Beijing and Hong Kong to compare their perspectives on the roles of those respective cities and relationships with other financial centres in the region. An in-depth study on Hong Kong could focus on its regulatory environment, expertise and the networks of regulatory cooperation between Hong Kong and Shanghai. Having two rich case studies will provide a solid basis for comparing processes of 'marketisation' in different contexts to enrich our understanding of multiple conceptualizations of markets. Instead of studying markets in one locality, further research could also employ a network approach to examine how groups and individuals negotiate, circumvent, challenge, and re-create the complex webs that entangle them in the production of market ideologies, systems and practices. Future studies could trace flows of capital, people and knowledge as they touch down in particular localities such as Hong Kong, Shanghai and Beijing to investigate how regulatory, institutional and financial capacities are enacted through the entanglement and negotiation of market discourses and practices, and how such ideas and practices are circulated, adapted and implemented in specific localities even as they traverse geographical space and boundaries.[2] The ways in which financial institutions with operations in both cities use these locations in strategies of spatial-regulatory arbitrage, how they visualise the functions, advantages and future direction of both financial centres will

[2] For more on multi-sited approach to fieldwork, see Burawoy (2000).

also address business and policy concerns of the financial and regulatory communities.

9.4 Conclusion

Deconstructing markets, market relations and market ideologies means confronting the messy reality of economic behaviour and economic structures instead of assuming them away in the tradition of orthodox economics or impoverished accounts of the economy. In this thesis, I have sought to open up the black box of 'markets' in the context of Shanghai's experience to examine the underlying processes taking place in the city, as well as across spatial scales, in order to elucidate the complex processes of market making. In doing so, my intention is to undermine the power of a seemingly unified (neoliberal) market discourse. Although the 'black box' metaphor alludes to the increasingly popular SSF approach to markets, I have chosen instead to highlight the political economy aspects, broader structural issues and the nature of regulation pertaining to financial markets. The political economy approach is less popular now compared to the 1980s and early-1990s but, as I have demonstrated in this thesis, it can be particularly useful for understanding specific local or national scale phenomena by embedding them within an international context that emphasise flows, interconnectivity and power – aspects of which tend to be neglected in the micro- and meso-level studies of the SSF.

At the same time, I am also mindful of the social and cultural embeddedness of finance capital and financial markets. In the introduction to a collection of papers on the 'cultural economy', Amin and Thrift (2004) argue for a hybrid model of culture and economy in which the two terms are dispensed with as separate categories. Instead of an add-and-stir approach of adding cultural overtures to an economic core, or examining how the economy is culturally embedded or how culture is mobilised for profit, “the pursuit of prosperity must be seen as the pursuit of many goals at once […] through hybrid and temporary coalitions […] set against the background of various kinds of ordering frames (*ibid.*: xiv) (see also Zelizer, 1988, Krippner, 2001). By emphasising the variety of actors involved in economic transactions, organisational arrangements and the development of regulatory standards, rules and practices in market-building, I argue for a more variegated account of what constitutes economic practice and the construction of values by focusing on multiple approaches to markets.

This thesis also emphasised the importance of embedding concepts of power and governance into the theorisation of markets and how they not only enrich accounts of market formation and processes but are crucial to their explanations. Rather than harmonious cooperation ensured by the invisible hand or the coercive power of the state, concrete social groups construct ‘markets’ through power struggles against other groups and other possible forms of markets (see Lie, 1993, Lie, 1997, Fligstein, 2001). This recognition of the variety of actors and interests within a market setting and an emphasis on power and conflict and processes of negotiation and resolution has been central to my research. The form, structure and pace of market formation taking place in Shanghai is a contested process that has to be negotiated amongst the different interests of incumbents and challengers, involving a variety of actors including local firms, foreign firms, national and local state bodies, foreign state institutions and transnational organisations. My research has also taken Fligstein’s (2001) political-cultural approach further by highlighting the distinctive geographies of global finance and the development of financial markets that operates at a number of different spatial frames or scales, such as how the development of financial markets in Shanghai was driven and influenced by institutions and actors based elsewhere (e.g. Beijing and other international financial centres) with different understandings and interpretation of 'markets' and power to influence that process. The 'marketisation' process in Shanghai was also enabled by a variety of place-specific factors such as its history, geographical location, state support and business culture.

The key role of states and state institutions in the process of market building is another important aspect. In theorising about conceptions of control, governance structures and rules of exchange, Fligstein (2001) demonstrates how issues of governance and regulation are central to market enquiries. The question should thus be: how and with what methods does the state contribute to the performance of calculative agencies and the organisation of their relations? This implies the existence of a wide range of possible configurations. The term 'transitional economy' reflects the old paradigm; there is nothing of a transition in the developments observed or in the diversity between countries such as Poland, Ukraine or China. It is more useful to conceptualise them as reconfigurations, combinations and re-arrangements peculiar to their historical contexts. In these rearrangements, the state often plays a crucial role and the dynamics in place, in turn, impact on its own position and contribution to the economy. The case of Shanghai should therefore not be seen simply as a transition 'from plan to market' but a process of reconfiguration specific to its historical and geographical context, of which the constitutive role of the state is crucial. The experience of market building in Shanghai illuminates how different constructions of capitalism evolve, how they intersect, and how a geographic sensibility makes a difference to the form and function of variegated capitalist economies. The world, therefore, remains a patchwork of different financial spaces or systems; the patchwork that is the nation-state, to a certain extent, represents changing geographies of capitalisms. In the face of neoliberal fatalism, the active construction of neoliberal market ideology needs to be exposed through theoretically informed empirical research and this thesis is a contribution towards that effort.

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Appendix A

Profiles of Interview Respondents

#	Date	Venue	Institution (Country)	Position
1	10 December 2004	Nottingham	Private Chinese property group	Chairman
2	17 August 2005	Shanghai	Foreign Chamber of Commerce	Executive Director
3	12 December 2005	London	UK-based international bank	Director
4	11 January 2006	London	UK-based international bank	Chief economist, head of global research
5	13 January 2006	(Via email from Hong Kong)	UK-based international bank	Associate Director
6	21 February 2006	Shanghai	TNC (France)	Director
7	22 February 2006	Shanghai	Foreign bank (UK)	Economist
8	23 February 2006	Shanghai	TNC (Netherlands)	Regional manager, Asia
9	27 February 2006	Shanghai	Chinese private financial institution	Executive manager
10	28 February 2006	Shanghai	UK Consulate-General	Trade and investment officer
11	6 March 2006	Shanghai	Foreign bank (UK)	Head of operations
12	6 March 2006	Shanghai	TNC (Netherlands)	Finance manager
13	7 March 2006	Shanghai	Foreign bank (UK)	Corporate relations manager
14	7 March 2006	Shanghai	Foreign bank (UK)	Vice-president of corporate relations
15	7 March 2006	Shanghai	Foreign bank (UK)	Deputy head of capital markets
16	9 March 2006	Shanghai	Foreign bank (UK)	Country representative
17	9 March 2006	Shanghai	Foreign bank (UK)	Country head, China and branch manager
18	14 March 2006	Shanghai	Foreign Chamber of Commerce	Executive Director
19	10 April 2006	Shanghai	Lujiazui Finance Zone	Deputy Director
20	11 April 2006	Shanghai	Foreign bank (Germany & Thailand)	President
21	11 April 2006	Shanghai	Foreign bank (Germany & Thailand)	Board of Management
22	12 April 2006	Shanghai	Chinese securities company	Research analyst
23	14 April 2006	Shanghai	Foreign bank (Germany & Thailand)	Board of Management
24	15 April 2006	Shanghai	Chinese private financial institution	Consultant
25	16 April 2006	Shanghai	China Banking Regulatory Commission	Legal Counsel
26	18 April 2006	Shanghai	Chinese fund management company	Vice-director
27	19 April 2006	Shanghai	Chinese state-owned bank	Secretary-General

28	20 April 2006	Shanghai	Office for Financial Services	Deputy Director-General
29	12 October 2006	Shanghai	Foreign bank (UK)	Chief Representative
30	12 October 2006	Shanghai	Foreign bank (UK)	Deputy Representative
31	13 October 2006	Shanghai	TNC (France)	Chief Executive
32	13 October 2006	Shanghai	Foreign bank (Germany & Thailand)	President
33	13 October 2006	Shanghai	Foreign bank (Italy)	Deputy General Manager
34	17 October 2006	Shanghai	Chinese securities company	Analyst
35	18 October 2006	Shanghai	Chinese securities company	General Manager, M&A Department
36	18 October 2006	Shanghai	Foreign bank (Netherland)	Senior Manager
37	19 October 2006	Shanghai	Foreign bank (Italy)	Deputy General Manager
38	20 October 2006	Shanghai	Foreign bank (Germany & Thailand)	Regional Marketing Head
39	24 October 2006	Shanghai	Foreign bank (Belgium)	General Manager
40	25 October 2006	Shanghai	Foreign fund management company (France)	Deputy General Manager
41	27 October 2006	Shanghai	Foreign bank (Germany)	General Manager
42	27 October 2006	Shanghai	Foreign bank (Germany)	Head of German Desk
43	27 October 2006	Shanghai	Foreign bank (Netherlands)	Branch Manager & Head of International Clients, China
44	27 October 2006	Shanghai	Foreign bank (Australia and New Zealand)	Business Development Manager
45	1 November 2006	Shanghai	Foreign bank (Germany)	Chief Representative
46	2 November 2006	Shanghai	Foreign bank (Belgium)	Senior Account Manager
47	3 November 2006	Shanghai	Fund management company (Chinese and foreign joint venture)	Marketing Officer
48	3 November 2006	Shanghai	Fund management company (Chinese and foreign joint venture)	Investment Analyst and Advisor
49	3 November 2006	Shanghai	Foreign bank (UK)	Head of Cash Management China
50	12 March 2007	London	UK-based international bank	International Advisory Services
51	10 April 2007	London	Financial Services Authority	Manager

Appendix B

Glossary of English and Chinese Terms Used During Interviews

English term	**Mandarin**	***Pinyin***
‘Marketisation’, transformation into a market system	市场化	*Shichang hua*
‘Stockification’, transforming (SOEs) into a shareholding form	股份化	*Gufenhua*
Adjustment (period of)	调整（阶段）	*Tiaozheng (jieduan)*
Administrative regulation	行政管理	*Xingzheng guanli*
Advantage	优势	*Youshi*
Chairman of the board	董事长	*Dongshizhang*
Challenges	挑战	*Tiaozhan*
China Banking Regulatory Commission	中国银行业监督管理委员会	*Zhongguo yinhangye jiandu guanli weiyuanhui*
Client	客户	*Kehu*
Competition	竞争	*Jingzheng*
Contracting out	承包	*Chengbao*
Contradictions	矛盾	*Mao dun*
Exchange (stock or futures)	交易所	*Jiaoyisuo*
Financial Administration and Regulation Office	金融行政管理处	*Jinrong xingzheng guanlichu*
Financial centre	金融中心	*Jinrong zhongxin*
Flexible, flexibility	灵活（性）	*Linghuo (xing)*
Fundamental analysis	基本分析	*Jiben fenxi*
Futures	期货	*Qihuo*
Hardware	硬件	*Yingjian*
Interfere	干涉／干预	*ganshe/ ganyu*
Internationalise	国际化	*Guojihua*
Liberalisation	自由化	*Ziyou hua*
Market analysis	市场分析	*Shichang fenxi*
National State Assets Administration Bureau	国家国有资产管理局	*Guojia guoyou jichan guanli ju*
Non-governmental organisation	民间机构	*Minjian jigou*
Not-for-profit organisation	非盈利机构	*Fei yingli jigou*
Official	官方	*Guanfang*
Operate/control	操纵／作	*Caozong/ zuo*
Participate	参与	*canyu*
Policy	政策	*Zhengce*
Power, authority	权	*Quan*
Price differential	差价	*Chajia*
Private enterprise	私有企业	*Siyou qiye*
Progress	进展	*Jinzhan*
Quality	素质	*Suzhi*
Regularise, normal	规范（化）	*Guifan, guifanhua*
Regulate	监督管理	*Jiandu guanli*
Relax/ loosen (a policy)	放松	*Fangsong*
Reputation	名气，声誉	*Mingqi, shengyu*

Risk	风险	*Fengxian*
Shanghai Foreign Investment Services Centre	上海市外商投资服务中心	*Shanghai shiwaishang touzi fuwu zhongxin*
Shanghai Securities Regulatory Commission	上海证券管理委员会	*Shanghai zhengquan guanli weiyuan hui*
Share reform	股改	*Gu gai*
Short-term/long-term	短期 / 长期	*Duanqi/changqi*
Software	软件	*Ruanjian*
Special	特殊	*Teshu*
State Council Securities Policy Committee	国务院证券委员会	*Guowuyuan zhengquan weiyuanhui*
State-owned enterprise	国有企业	*Guoyou qiye*
Stocks	股票	*Gupiao*
Strategy	策略	*Celüe*
Systemisation	制度化	*Zhiduhua*
Technical analysis	技术分析	*Jishu fenxi*
Turnover rate	成交量	*Chengjiao liang*

Appendix C

Equity Structure of Listed Companies in China, 2006

	Absolute numbers	Percentage
I. Number of Listed Companies		
Shanghai Stock Exchange	886	58.79
A shares	832	55.21
B shares	54	3.58
Shenzhen Stock Exchange	621	41.21
A shares	566	37.56
B shares	55	3.65
Total	1507	100.00
II. Number of shares (in billion)		
Non-tradable shares	925.98	72.40
State shares	522.13	40.82
Legal person shares	11.59	0.91
Others	392.26	30.67
Tradable shares	352.98	27.60
A shares	330.08	25.81
B shares	22.90	1.79
Total	1278.96	100.00
III. Market capitalisation (in US$ billion)		
Non-tradable market capitalisation	825.34	72.05
Shanghai Stock Exchange	707.19	61.74
Shenzhen Stock Exchange	118.15	10.31
Tradable market capitalisation	320.22	27.95
Shanghai Stock Exchange	210.40	18.37
Shenzhen Stock Exchange	109.81	9.58
Total	1145.55	100.00
(Source: CSRC, 2007)		