The City and finance: changing landscapes of power

Book Section

Chapter 4
Changing landscapes of power: The City and finance

John Allen

Aims

- To introduce and describe the dominant role of the City of London in the context of the UK economy.
- To explore how the City of London has reproduced this dominance and whether the 2007-9 economic downturn signals its decline.
- To examine the basis of the City of London's power and its contested nature.

4.1 Introduction

At the end of the first decade of the 21st century, the landscape of financial and economic power across the UK economy looked markedly different from that at the turn of the century. Back then, the business of banking, broking and insuring, fuelled by deregulation and the globalisation of capital flows, accounted for a growing proportion of the UK's wealth and profitability. The sense in which the UK economy could turn its back on its manufacturing past and embrace a more weightless, financially-driven future spearheaded by the City of London's financial institutions looked not only convincing - among policymakers, at least - such a belief had assumed the status of an economic creed. The City, a shorthand for the UK's financial sector (although see Chapter 5), represented the money-making future that was to cement the UK's role in the global economy. Fast-forward to the end of the noughties, such beliefs not only looked far from convincing, they also drew into question the very basis upon which the UK economy rests.

Amidst the battered landscape of London's financial sector, the once mighty banks, investment houses and trading firms struggled to come to terms with the financial storm that had wrecked their businesses. The subprime crisis in the United States, the trigger for the enveloping storm, inflamed by a culture of excessive risk taking, had altered the financial landscape almost beyond recognition. Job losses in the City, from a peak of 360,000 in 2008, looked set to shrink by a third, cumulative losses and write downs for the world's largest financial institutions predicted to reach $1000bn and the contribution of London's financial services to the nation's wealth forecast to be slashed from 9 to 6 per cent of GDP. The dominance of the City looked to be over: its power greatly diminished, its authority and influence no longer recognised. Or so it seemed to some at the time.

Opinion is divided on the matter, largely over how best to interpret the 'highs' and 'lows' of power when the economy changes abruptly and business shrinks in both scale and volume. What significance should we attach to the changing momentum of the UK economy for, say, the big banks as a dominant force in economic markets and beyond? In such circumstances, what happens to their power and influence over the government's longer term economic strategy. When, for example, the US bank, Lehman Brothers slid into bankruptcy in September 2008 after 158 years of trading, did its power simply evaporate? And if so what about the other big overseas investment houses still trading in London's Canary Wharf? Has their authority simply taken a knock, only to be restored in an economic upturn when their 'reserves' of power can be drawn upon once again? Or has the City of London's power and influence diminished irrevocably in the financial crisis of the late 2000s?

As ever, it depends. It depends upon how financial and economic power is understood; how the way that power 'works' is read. In this chapter, we look at two contrasting interpretations of power and finance, each resting upon a particular view about how the economy changes and how it is organized. The first, broadly *structural* explanation of events, focuses upon the financial system as a whole, where the power of City institutions stems from their distinct position in the circuits of credit, finance and capital. In direct contrast, the second account rests upon a more *networked* account of events which draws attention to the largely expedient actions of financial elites in skewing rewards of power and wealth to their advantage. Where one would consider the latest financial crisis as a periodic punctuation in the City's dominance, the other would see the evident loss of the City's authority as the result of over-reach and misdirection with no guarantees as to the future abilities of its financial institutions.

Before we look at each 'reading' of power and finance in turn, we consider the broad historical shifts in the City's ability to reproduce itself as a powerful force, in relation to both economic markets and the state.

4.2 From dominant to bankrupt force?

Whilst there is disagreement over *how* the City has reproduced its dominance over time, there is broad agreement over the fact of that dominance - for the time being at least. What is meant by power in this context is the ability of the City to bend or influence the will of others to gain advantage. The nature of that advantage is implicitly financial: to profit at the expense of industry and shareholders, or consumers and taxpayers, and the like, by forcing a redistribution in the City's favour. In short, it comes down to the ability of the City to skew the system to its advantage by ensuring that others have no choice but to fall into line. Notwithstanding the fact that the City has altered in both its economic character and size over the past two centuries, the extent to which it has maintained its dominance over time is often attributed to its core commercial activities: the ability of its institutions to place themselves in the 'middle' of all kinds of complex financial activities and to benefit disproportionately from that role.

With respect to this commercial dominance, there has been a longstanding debate about the 'exceptional' character of the UK's economy which resurfaced in the late 1980s with an even stronger emphasis upon the pre-industrial stamp of the nation's ruling block and the hegemonic role of the City. Also at issue in this debate, however, was the precise role that the City performed in relation to the 'real' economy of the UK, in particular its disappearing manufacturing base. In opposition to those who portrayed the City as a type of 'finance capital', orientated to global markets and largely separate from the domestic parts of the UK economy, Geoffrey Ingham (1984, 1989) argued pointedly that the City's earnings came predominantly from its commercial role.

By this, he meant that the City's profits from the 1830s onwards stemmed overwhelmingly from the ability of its institutions to act as 'middlemen' or brokers within the financial system. By inserting themselves in the middle of the foreign exchange and money markets, commercial brokers profited from their role as intermediaries on a fee or commission basis. As traders of capital, stocks, bonds and securities, City firms built up an historical advantage in the exchange and distribution of economic resources that witnessed their ever growing significance to the UK economy. The economic historian C.H. Lee, in his study *The British Economy since 1700* (1986), charted the rise of this commercial significance, dating back to the mid-nineteenth century, which showed a southern service economy, centred on London and commerce, consistently generating around half the national rate of economic growth and the bulk of the employment growth (see Figure 4.1). Economic significance, however, is not the same as economic dominance, and although work by other economic historians such as Cain and Hopkins' (1987) account of 'gentlemanly capitalism' point towards the dynamic role of the City of London in the national economy from the 1850s through to the Second Wold War, the argument does not amount to a justification of the City's *persistent* dominance. The ability of the City to skew the economic system to its advantage, to shape the conditions of existence for everyone else, as a continuous feature, sits uneasily alongside just some of the historical, global events of the last century which damaged its fortunes: the devastating impact of the First and Second World Wars, for example, or the demise of the gold standard and the 1930s global depression.

Ingham acknowledges the significance of these events to the shifting fortunes of the City over time, yet he still wishes to maintain that the commercial dominance of the City remained throughout the twentieth century despite the obvious economic difficulties it faced, including the growth of opposition from industry and manufacturing. His claim is not that the UK had grown a top-heavy financial system at the expense of industry, but rather that the network of institutional relations between the City and government, in essence the relationships between finance houses, the Treasury and the Central Bank, worked in favour of the City's commercial interests over time. Ingham is at pains to point out, however, that this state of affairs was not down to any capability on the part of the City to wield power 'over' the state, but that the different interests of all those involved coalesced around a relatively stable monetary system. While, from the City's standpoint, instability can lead to speculation and short term gains, in the long run the stability of monetary system engenders trust and confidence in the commercial markets.

Another way of saying this is that despite the often divergent agendas of government and financial bodies, effectively they all enjoyed the benefits of a positive-sum game. Yet if that interpretation is correct, to what extent can the City be said to have forced a redistribution in its favour by bending the will of others? If the City has been able to reproduce its dominance throughout the twentieth century, and indeed before that, then its role as commercial broker and clearing house should have had some bearing upon its ability to skew rewards in its favour. From the late 1950s and early 1960s on, with the shift in the character of the City towards a more supra-national orientation, that ability became markedly evident

In the latter part of the twentieth century, a number of developments served to reproduce the City's privileged position in the UK economy, the most significant of which spoke to the increasing internationalization of the City's activities and the rise of a certain kind of commercial expertise and professionalism quite different from earlier forms of 'gentlemanly' conduct (Thrift, 1994). The internationalization of bank lending, via the Euromarkets, together with the development of the euro currency markets, witnessed a rapid increase in the number of foreign banks operating in the City. Alongside the internationalization of London's equity markets brought about by the Big Bang reforms of 1986, and the relaxation of barriers to trade within the financial markets, the liberalization and deregulation of the City's activities saw an unprecedented explosion in the flow of funds and capital through the City. Changes of this magnitude and scale were reflected in the ballooning global transaction figures where those mediating these voluminous financial transactions found themselves enjoying positions of considerable power and advantage.

The power in question arose from the role performed by commercial brokers and financial traders, but to refer to that role as one of straightforward domination and control is perhaps to miss the point. In many respects the advantages enjoyed by financial intermediaries are not particularly new; it concerns the unequal access to the quantity and quality of information available to them, in contrast to industrial corporations and pension funds, as well as other investors such as mutual funds, university endowments and public sector agencies. With the routine allocation of capital and the management of risk, such basic asymmetries are not necessarily an issue, but in the increasingly volatile international financial environment of the 1970s and 1980s the diversification of risk, rather than its elimination, introduced an element of uncertainty and financial innovation in the system that favoured those best able to engineer financial solutions (Pryke and Allen, 2000).

One of the effects of this environment was to produce 'new' and restructured financial instruments that were suitably tailored to the uncertainties of the monetary system taking shape. The use of such instruments, the ability to bundle up products to distribute risk and leverage future income streams, has been a key driver of the growth of 'financialization' over the past two decades. Financialization, according to Robin Blackburn (2006), can be defined as 'the growing and systemic power of finance and financial engineering' (p39) and although not a novel phenomenon it differs from previous rounds of financial innovation in the sheer scale and expansion of its engineered 'products'. Almost anything it seems can be turned into a bond-like security - mortgages, student loans, credit card debt, health insurance, toll road fees, utility bills, and the like - sold on and used as collateral to generate further speculative activity and risk abatement (Leyshon and Thrift, 2007).

The growth of 'secondary trading' and the ability to engineer ever more elaborate instruments to repackage loans has led to significant economic gains for those dealing with the risks, but a disproportionate share of those gains, as Blackburn points out, has been swallowed by those actively managing and trading the risks. Those in the 'middle', the traders and brokers, exploited their informational advantage to skew financial rewards in their favour. Financialization, it seems, is but the latest move by which the City has been able to reproduce, if not its straightforward dominance, then its ability to engineer outcomes which disproportionately benefit its institutions.

That is, until recently, when the actions of those very same institutions brought the financial system to the edge of collapse and bankruptcy (Blackburn, 2008).

As in previous eras, it is difficult to suggest that the City, in getting its way on financial remuneration, exerted power 'over' the institutions of the state. Recent governments have supported the view that the UK had a comparative advantage in financial services and that a competitive, risk-taking City was a central component of that economic policy (see Table 4.1). The relentless expansion and profitability of the UK's financial sector from the 1960s and 1970s on, reinforced by the deregulation of the City, was not out of line with the Central Bank's inflationary concerns, nor at the expense of the Treasury's interests. But that expansive growth was also accompanied by an institutional momentum and economic volatility that ushered in a culture of risk-taking which, in hindsight, favoured the City at the expense of just about every other stakeholder - shareholder and taxpayers alike. That that heady momentum came to an abrupt halt in 2008, and with it the bewildering array of risk-taking gains, has left the City in a position where its dominance is once again in question. If its moment of financial hubris is over, does the City's nemesis spell out its inevitable loss of leverage and authority? Or are we simply witnessing the latest bout of market readjustment after the bursting of a financial bubble?

Put another way, is this the upending of the City's established dominance, when a broken industry comes to terms with its demise as a powerful economic force? Or is its dominance merely on hold, whilst its banks sit out the cycle of blame and await the next upturn in its business and economic fortune? How you answer these questions turns upon how you read the landscape of economic and financial power.

4.3 The City as a systemic bloc of power…

One reading, which reaches back to various Marxist accounts of the basis of power in capitalist economies like the UK, focuses upon the ability of the City to reproduce its power through a pattern of *structural* dominance. By structural in this context is meant that the City, as an institutional bloc of power, is able to place limits upon what is and what is not possible in the economy as a whole. Whilst there may be periodic shifts in the ability of bankers and other financial actors to shape the surrounding business environment, the existing structures of the UK's capitalist economy reproduce the power of the City over time. The enduring, yet changing pattern of the City's dominance, on this view, operates as a *systemic* feature, independent of anybody's will.

This bring to the fore the notion of financialized capitalism. Earlier I mentioned the ability of the City to skew the system to its advantage by ensuring that others have no choice but to fall into line. The ability to constrain the free choice of others by leaving them no room for manoeuvre is the defining characteristic of domination. When that dominance is structural it implies that whilst government bodies and regulating authorities may curtail, say, the most recent excessive risk practices of the City, it can only do so within an economic framework that leaves the financial system as a whole broadly intact. With finance in private hands, bankers and financiers operate the economy's money and that very fact places them in a structural position quite different from manufacturing or retail firms, for example. The power of the City in this sense, according to Lawrence Harris (1988), stems from its distinct position in the international circuits of capital, first, through its control over the use of money as a means of circulation and, second, through its control over highly mobile, supra-national financial assets.

In relation to the first point, we are close to Ingham's stress upon the commercial role performed by the City, whereby the distinct position occupied by financial traders and brokers places them in the special role of buying, selling and transferring the economy's money. Effectively, their power is exercised by dealing in money, credit and financial instruments, not merely as a monopoly provider of such services, but as the point through which such practices of money-dealing have to pass. They are able to skew rewards in their favour through their ability to appropriate profits from the spread on the buying and selling prices of foreign exchange, equities, and bonds, as well as from the fees and commissions charged for the transfer, exchange and management of money balances.

From one viewpoint, this simply amounts to a bundle of lucrative trading practices. But when considered from the vantage point of the financial system as a whole, rather than, say, through the eyes of dealers and investment managers at the US giant, Citigroup, or the Swiss Bank, UBS, this advantageous structural position is precisely what has enabled the City to reproduce its dominance over time. Foreign banks in the City are not powerful simply because of their international reach; they are powerful because of the position they occupy in the circuits of capital.

This is not to deny that individual investment managers are able to exercise power at the expense of savers or trust funds, for example, but that they do so as part of a financialized form of capitalism which has benefitted the City disproportionately. Over time, on this view, the development of London as an international financial centre, through its accumulated expertise and innovative edge, has enabled it to be at the forefront of the recent wave of financialization which has spread risk across the globe. This supra-national growth of the financial system, with the City as one of its chief engineers driving liquidity and mobility, witnessed the gains from dealing with risk rise exponentially to a level where those positioned to skim the rewards enjoyed extravagant remuneration. That is, until the momentum in the system stopped in the late 2000s.

When the power of the City is thought of as systemic, the implication is that the structures of financialized capitalism reproduce its dominance despite fluctuations in the fortunes of its banks and finance houses. There is, in effect, a systemic-bias in favour of the City as a whole. This bias, crucially, is not one that can simply be challenged and overruled, but is part and parcel of the way that the UK's capitalist economy operates; the way that its economic relations are structured and organized. If this sounds a little rigid, the intention is not to suggest that government authorities, for instance, are powerless to counter the dominance of the City; rather it is to point out that economic growth and profitability within this framework is *constrained* by the powers of finance.

Money is the bedrock of the whole economic system and those in a position to control it - the banks, the investment houses, and especially those who allocate capital and manage risk - operate it largely to their advantage. Moreover, they do so as part of a structural configuration which situates them, as well as governments, industrial corporations, pension funds and other institutional actors, within a pre-existing set of economic relations that constrain and sets limits upon what can change. Even if the whole banking system becomes more regulated and less lucrative as various financial 'bubbles' burst, the underlying imperative of financialized capitalism - that finance becomes ever more liquid and independent from production - enables the City to enjoy a dominant economic position that others are forced to confront.

On this interpretation, the economic system itself confers power and resources upon some actors, but not others, and likewise is capable of forcing a redistribution in favour of some interests at the expense of others. The latest go-getting, deal-making culture of excessive risk may be discredited for now, but the structural imbalance of power between finance and the rest of the economy remains in place.

4.4 … or a more tenuous, networked power?

Critics of a systemic view of the City's power point to its over-blown character, where it would seem that little can ever dent the ability of its financial institutions to grasp the lion's share of economic gains. This overly deterministic view is countered by one that stresses the *tenuous* nature of the City's powers; that whatever dominance its banks have been able to enjoy represents an achievement, not a given. Dominance, on this view, is something that is made and remade; a precarious achievement subject to the networked abilities of a multitude of bankers, brokers, dealers and investment managers which hinges upon their own sense about how it is put together . If, until recently, the City has been seen as a financial powerhouse, that is not because of any enduring quality, but rather because its financial elites have, over time, been more or less successful in engineering outcomes to suit their interests. The leverage of such elites is largely expedient: it stems from a practised ability to manipulate financial transactions to their advantage or risk losing that power and advantage in the process.

If the power of the City's traders is more tenuous, less substantial, than often perceived, that is because it is what they *do* that matters, rather than any reserves of power that may be called upon because of their economic position. Embedded position is still significant to those who draw attention to the *exercise* of power and authority, but primarily because it points to the networked role performed by brokers, bankers and the like. With the onset of financialization, such individuals found themselves well placed as intermediaries to exploit resource asymmetries to their advantage. But such potentially rewarding roles, as noted earlier, are not new to the City. What is new, each time, is their achievement; that different financial elites have been able to skilfully exploit whatever advantages arise to enrich themselves at the expense of others.

Understood in this way, the power of the City from the nineteenth century onwards is not one thing; it comprises a variety of financial elites, both old and new, who have been able to use their trading roles to skew rewards in their favour. At times, this has been achieved through acts of domination, where investors have no choice but to pay exorbitant fees and commissions; at other times, the engineering of financial deals and the temptation of rewards too great not to want speaks more to an agenda of manipulation and inducement. Different registers of power and influence, in that sense, have come into play at different historical moments, and are enacted by diverse financial elites. Cain and Hopkins' gentlemanly elites shared a common educational and class background based upon personal ties, whereas today's professional elites, according to Savage and Williams

(2008), operate in a looser, networked fashion, often connected through a third party than any direct tie.

For Savage and Williams, the direct personal ties which characterised the old established City elites are of secondary importance in today's global networks, where the ability to broker or bridge the 'holes' in monetary networks holds the key to a profitable performance. Separate professional intermediaries working at, say, the German bank, Commerzbank, or the French bank, Societé Générale, may 'work' the net in similar ways putting together innovative financial deals around the globe that, for example, connect previously unrelated investors through the secondary trading market. The ability of such professional elites to enrol institutional investors, as well as wealthy individuals, to translate and align their different interests, and to 'fix' an overall orientation is, on this account, a form of net*work*ed power (see Allen 2009).

Such mediating elites do not compel others to enrol in such networked ventures. In recent years, the win-win situation that securitized loans and the sophisticated management of risk presented to players was, in itself, a sufficient inducement. The fact that such gains turned out to be illusory for some, if not most of the investors, merely points to the contingent nature of the City's power. When the networks start to fall apart, so too does the power and influence of those who previously held them together. The loss of authority experienced by investment bankers and financial analysts after the recent meltdown in the City's fortunes is, in that sense, following Bourdieu (1989), a loss of symbolic power, where trust and social recognition simply disappear.

Of course, such groups continue to occupy a distinct position in the circuits of capital, but there is no guarantee that their future actions will do anything other than confirm that loss of power. Money may be the bedrock of the economy, but if risk is mismanaged and capital misallocated on a grand scale, as happened in the 2000s, the gains and influence achieved in an earlier period simply fade away. In that respect, the expedient actions of financial elites, in hindsight, turned out not to be quite so conducive to the needs and demands of the moment.

The implication of this is that power of the City, on this view, turns out to be a tenuous achievement; it is not something held by financial institutions, rather it is produced through networked forms of interaction. Such powers of finance may be generated by the application of resources and skills over tracts of space and time, and expand or contract in line with the monetary resources available *and* how they are used. There is a pragmatic side to things, in so far as financial elites may misuse or simply waste resources, or fail to recognise that what works well in one context may fail in another, and in so doing find that their power and influence shrinks in both scope and scale (see Allen, 2008).

On this interpretation, the ability of bankers and brokers to over-reach themselves in a moment of financial volatility and excessive momentum may or may not upend the established City order, but it does spell out an evident loss of authority - for now at least. As for how long, that is a contingent question, as there is no guarantee that in any future economic upturn City bankers will be able to enrich themselves to such an extraordinary degree as over the past two decades. The provisional and contextual nature of their power means that it is simply not possible to know in advance whether the City of London's power and influence diminished irrevocably in the financial crisis of the late 2000s.

The issue is further complicated by the fact that, for much of the time, what actually passes for power in the City is not the kind that bends the wills of others, to gain advantage. In no small part this is because the power exercised by financial elites is largely directed at working the networks: forging connections, bridging the gaps, and stabilizing interests so that associations hold together. As such, it is more about exercising power *with* rather than *over* others, holding out the prospect of positive gains that are too great to pass up. Positive-sum gains, however, do not equate to equal-sum gains and some gains turn out to be illusory, as noted, and in this way skewed reward structures may be 'masked' by the exercise of quieter register of power: through persuasion, inducement and manipulation. On this view, the 'power to' engineer financial solutions to their advantage is an apt description of what financial intermediaries attempt to do. And, in the last resort, it is what they do that is said to matter.

4.5 Conclusion

In contrasting a broadly structural account of power, where the City reproduces itself as a dominant force over time, to a more provisional, expedient landscape of the City's achievements, I inevitably run the risk of overstating the difference. But the difference, even if drawn a little too starkly, rests upon divergent assumptions about how finance and the UK economy is organized and how open it is to change. How we 'read' the basis of the City's power matters because it spells out the room for manoeuvre that there is to see things differently.

If the City's dominance is more or less systemic, then the argument for a more regulated, less lucrative, financial sector is subject to structural constraints that may well reassert themselves after several lean years. Derivatives and securitization are, after all, not processes that can simply be wished away and nor necessarily should they be. A more provisional account of the City's powers, however, one which emphasizes the 'produced' nature of those powers under contingent circumstances, offers greater room for manoeuvre about what state regulation can achieve and what role the City and finance should assume in the UK economy going forward. This is not to imply some kind of voluntaristic action directed at the worst excesses of financialization, but rather that such a reading opens up more of a space for political engagement. An engagement, that is about what kind of economy the UK should be if, as is now evident, the notion that the country could survive on finance alone has gone the way of much of the City's speculative gains pocketed in recent years.

Further Reading

- For an 'insiders' view of the City's growth and future (just prior to the global financial crisis), see Sir John Gieve's account 'The City's growth: the crest of a wave or swimming with the stream' in the *Bank of England Quarterly Bulletin*, 2007 Q2.

- A more critical account of the rise of the City and its distortion of the UK economy can be found in Doreen Massey's *World City*, 2007.

- For an historical account of the City's dominance, see Ranald C. Michie's *The City of London: Continuity and Change 1850 - 1990*

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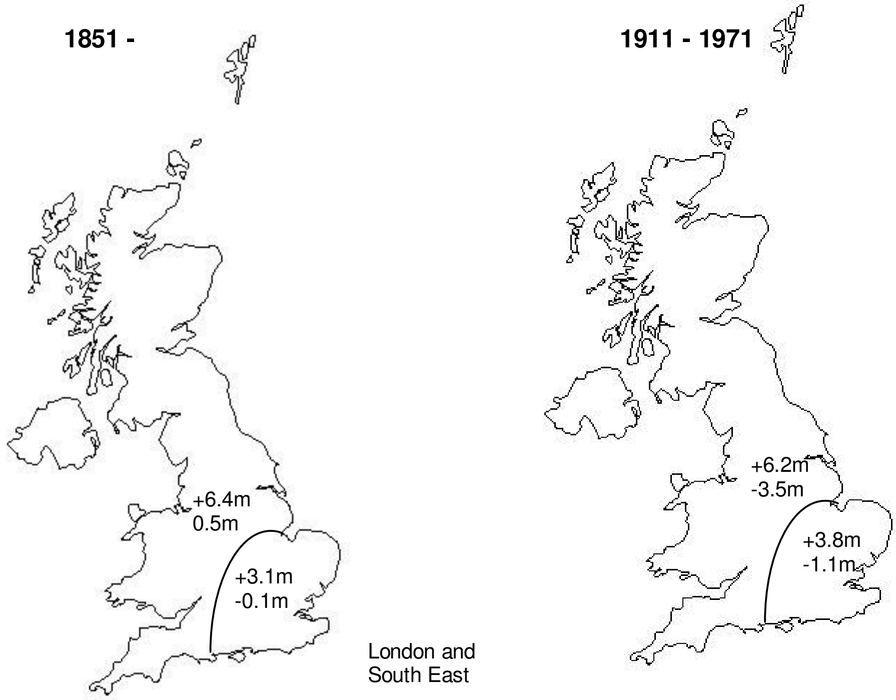
Figure 1: London and the South East's Regional Pre-eminance



Employment Change 1851 – 1971

Source: adapted from Lee, C. H (1986), 264/5

Table 1 Selected Financial Indicators – Top 10 Cities 2008

Total Value of Equities Trading	Total No. Contracts of Derivatives	Total No. of Commodities Contracts
1 New York	Seoul	New York
2 London	Chicago	London
3 Tokyo	Frankfurt	Chicago
4 Frankfurt	London	Shanghai
5 Shanghai	Philadelphia	Tokyo
6 Singapore	Mumbai	Mumbai
7 Paris	Sao Paulo	Osaka
8 Milan	Johannesburg	Kuala Lumpar
9 Hong Kong	New York	Sao Paulo
10 Shenzen	Mexico City	Johannesburg

Banking/Financial Services companies	Investments/Securities firms	Total value of Bond Trading
1 London	New York	London
2 New York	London	Copenhagen
3 Tokyo	Tokyo	Madrid
4 Hong Kong	Hong Kong	Moscow
5 Frankfurt	Singapore	Bogota
6 Singapore	Chicago	Istanbul
7 Paris	Paris	Seoul
8 Shanghai	Seoul	Frankfurt
9 Milan	Frankfurt	Milan
10 Madrid	Madrid	Tel Aviv

Source: adapted from Sassen 2009. Mastercard Worldwide Centres of Commerce Report 2008