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A COMPARATIVE ANALYSIS OF EMERGING FINANCIAL CENTERS: THE CASE OF SHANGHAI, ISTANBUL AND DUBAI

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AUTHOR DECLARATIONS

1. The material included in this thesis has not been submitted wholly or in part for any academic award or qualification other than that for which it is now submitted.

2. The program of advanced study of which this thesis is part has consisted of:

i) Research Methods course during the undergraduate study

ii) Examination of several thesis guides of particular universities both in Turkey and abroad as well as a professional book on this subject.

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ABSTRACT

Xin Zhao **January 2013**

COMPARATIVE ANALYSIS OF EMERGINGFINANCIAL CENTERS: THE CASES OF SHANGHAI, ISTANBUL, DUBAI

Many newly emerging financial centers rushed up to the world stage after the financial crises of the last two decades; although the competitive rating has not changed significantly for the positions of top global financial centers like London, New York, Hong Kong and Singapore, emerging financial centers have gained a lot of power, developed rapidly and become more competitive, examples of which include Shanghai, Dubai, and Istanbul. China, Turkey and UAE all have set the goal to turn Shanghai, Istanbul and Dubai into truly global or international financial centers in a foreseeable future. In this thesis, we have first reviewed and summarized the historical experiences of development of international financial centers in general and Shanghai, Istanbul and Dubai in particular. Then we have concluded some common developmental preconditions for IFC formation through synthesizing theories and reviewing academic studies, and we have developed some special instrumental factors to evaluate potential powers of Shanghai, Istanbul and Dubai as emerging international financial centers. This thesis tries to make a comparative analysis to increase the persuasiveness of our evaluation. Finally, we have drawn some conclusions and policy evaluations about the strengths and weaknesses of Shanghai, Istanbul and Dubai to become international financial centers.

Key words:

Shanghai, Istanbul, Dubai, International financial center, comparative analysis

KISA ÖZET

Xin Zhao **Ocak 2013**

Yükselen Finansal Merkezlerin Mukayeseli Analizi:

Şangay, İstanbul ve Dubai Örneği

Birçok yeni finans merkezi son yirmi yılda meydana gelen ekonomik krizler neticesinde dünya sahnesine çıkmıştır. Londra, New York, Hong Kong, ve Singapur gibi zirvedeki küresel finans merkezleri için rekabet hızı pek değişmese de Şangay, Dubai ve İstanbul'da yeni ortaya çıkan finans merkezleri güç kazanmış, hızlı bir şekilde gelişmiş ve daha rekabetçi olmuşlardır. Çin, Türkiye ve UAE Şangay, İstanbul ve Dubai'yi öngürülebilir bir gelecekte gerçek bir uluslararası ve küresel bir finans merkezi haline getirmeyi amaçlamışlardır. Bu çalışmada genel itibariyle uluslararası finans merkezlerinin tarihsel gelişimleri; özel olarak ise Şangay, İstanbul ve Dubai'deki finans merkezlerinin gelişimleri incelenmiştir. Teorileri sentezleyerek ve akademik çalışmaları inceleyerek IFC formasyonu için kalkınma amaçlı bazı ortak önkoşulları sıraladık. Bu tezde yeni araçsal faktörler geliştirilmiş olup; Şangay, Dubai ve İstanbul'un potansiyel güç olabilirlikleri değerlendirilmiştir. Çalışmada yer alan analizin daha inandırıcı olması için mukayeseli çalışmalar yapılmıştır. Son olarak ise Şangay, İstanbul ve Dubai'nin uluslararası finans merkezleri olabilmeleri için bazı politika değerlendirmeleri yapılarak bu yerlerin güçlü ve zayıf yönleri ortaya konulmuştur.

Anahtar Kelimeler

Şangay, İstanbul, Dubai, Uluslararası finans merkezi, karşılaştırmalı analiz

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LIST OF ABBREVIATIONS

CAI	Capital Access Index
CDI CFCI	CDI China's Financial Center Index
CHA	China
CSRC	China Security Regulatory commission
DB	Doing Business
DIFC	Dubai International Financial Center
EFW	Economic Freedom of World
EIU	Economist Intelligence Unit
FDI	Foreign directly investment s
FDR	Financial Development Report
FDR	Financial Development Report
GCI	Global Competitiveness Report
GFCI	Global Financial Center Index
GFSR	Global Financial Stability Report
Gov.	Government
HD	human capital development
HDI	Human Development Index
IFC	International Financial Center
IPO	Initial public offerings
ISE	Istanbul Stock Exchange
M&A	Mergers and acquisitions
MNCs	Headquarters of multinational corporations
NPC	National People's Congress
NYSE	New York Stock Exchange
QFII	Qualified Foreign Institutional Investor
QLI	Ferrans and Powers Quality of Life Index
RMB	Renminbi Chinese currency
SSE	Shanghai Stock Exchange
TR	Turkey
TTC	Travel& Tourism Competitiveness Report
UAE	Unit Arab Emirates
WEF	World Economic Forum

INTRODUCTION

Financial centers have always been in the center of very hot debates in the world. Although the competitive rating has not changed significantly for the top positions of global financial centers like London, New York, Hong Kong and Singapore, after the financial crisis in the last two decades, emerging financial centers have enhanced their competitive power and gained more power to rush up the league tables.

In terms of emerging economies in the world, three cities in particular have attracted attention in the financial press for incorporating IFC aspirations into their development agendas: Shanghai, China; Istanbul, Turkey; and Dubai, Unit Arab Emirates (UAE). They have made a strong improvement since 2007, raised their global centers competitiveness rating by 16%, 15% and 12% for Shanghai, Istanbul and Dubai, respectively. [1]

However, little has been done by way of a systematic attempt to gauge their current status or compare their processes. Shanghai, Istanbul and Dubai share several features that make such research important to undertake. In addition, China, Turkey, and United Arab Emirates have great ambitions to turn these three cities into regional international financial centers (IFC) and, eventually global financial centers, and they incorporate the project into a national strategy and take a lot of measures to improve from all aspects to achieve their aims. Therefore, it is very meaningful to make a comparative analysis of the three cities to evaluate their potential strengths to develop into an IFC and find the weaknesses and rooms for further improvement.

The government of the People's Republic of China has set a goal of turning Shanghai into a truly global financial center by 2020, a target with which the municipal government of Shanghai is in enthusiastic agreement.

[1] Data from Global Financial Center Index 2007-2012, calculate by author.

This objective is a highly desirable one for Shanghai, and China as a whole, because financial centers would bring substantial economic gains, increase “soft” geopolitical power, and create many good opportunities in many social aspects. Empirical studies have shown that well-functioning financial centers contribute positively to the national economies that have these financial centers (Elliott, 2011). there is a great opportunity for Shanghai to shorten the distance to be a global financial hub, and regain the IFC position.

Shanghai has a lot of potential: it is one of the biggest cities in China, a historical IFC in the world, and stood as the Asia Pacific’s undisputed financial hub in the 1930s. The “Paris of the East” has not only hosted opium dens and cabarets, but also the world’s third largest stock market in terms of capitalization. Shanghai had the world’s second-largest bank building after the Bank of Scotland in London. The number of foreign banks in Shanghai (33) even overtook Hong Kong (21) and Singapore (17) in 1934. Although for some reasons it lost this competitive position for many years until 1980s, after the open policy reform in China, it developed fast and regained its competitive power in finance and became an economic hub. Shanghai’s port is the world’s busiest, measured by cargo tonnage.

Shanghai benefits from being located in the Yangtze River Delta Economic Region which accounts for 19% of China’s GDP, 37% of its exports and 49% of foreign investment, providing strong economic backing for Shanghai. Shanghai’s financial sector is leading in domestic financial markets, and it hosts the mainland’s key trading markets for futures, gold and foreign exchange. It’s a fashion capital for young people with large cameras and small cell phones. All this economic activity creates demand for credit, insurance, trade finance as well as stock and bond markets (Tong, 2009). In addition, manufacturing, logistics, economic and financial advantages, accompanied by a budding entrepreneurial culture in neighboring provinces and increase Shanghai’s potential as an IFC.

The GFCI does note that, Shanghai, along with Singapore and Dubai, is likely to become "more significant" in the next few years, and Shanghai has most potential to become the third truly global financial center after London and New York.

Istanbul is the largest and most cosmopolitan city in Turkey (TR), which centralizes the great majority of manufacture, service and financial activities of TR. The city accounts for the 20 % of the total population, 27% of economic output, 40% of tax revenues and half of Turkish exports and imports. Historically, Istanbul was the center of the country's economic artery due to its location advantage as an international junction of land and sea trade routes and has always been the country's "financial capital". In 2007 the ruling Justice and Development Party government set "developing Istanbul into an IFC" as one of its major long-term economic goal. This long term goal is planning to develop Istanbul as regionally dominant within 10 years and to be one of five or six most important international centers within 30 years.

Turkish economy's growth performance and great ambition and efforts provide solid foundation and opportunity to Istanbul as an IFC. Turkey is the 15th largest economy in the world. At the end of 2011, its GDP reached to $1,288 trillion, with 9.49 of GDP growth rate, per capita is $10,498 billion, and the unemployment rate descended to 7.8% under control (Oct.2012). Turkey benefited a great deal from participating in the financial globalization and from integration with national financial markets; thus attracting greater internationally mobile capital and creating a freer financial environment.

The opening of specific markets in the city during the 1980s further strengthened this status. Istanbul Stock Exchange (ISE), established in 1986, is the sole securities market of Turkey; it provides trading in equities, right coupons, Government bonds, Treasury bills, revenue sharing certificates, bonds issued by the Privatization Administration and corporate bonds, and it carries out overnight transactions. In 1993 the ISE decided to liberalize the gold market, and in 1995 the Istanbul Gold Exchange was established, which ended the gold bullion imports monopoly of the Turkish Central Bank and transferred it to the private sector members of the gold exchange.

UAE government also aims to capture the global opportunities to develop Dubai into an IFC. In 2004, the UAE constitution was amended to allow an emirate to establish a "financial free zone," a separate legal, geographic and judicial jurisdiction. Federal Decree No. 35 in 2004 then established the Dubai International Financial Center (DIFC).

Dubai is a monarchy, Sheikh Mohammed bin Rashid Al Maktoum being the present leader of the UAE. Dubai is located in the Persian Gulf and surrounded by oil and gas reserves. In its thirty years of development, Dubai has been synonymous with luxury and richness. It is a leading international trader in the world, one of the trade hubs worldwide with very developed shipping and airline centers. Due to Sheikh Rashid's foresight and long term national development plan, Dubai has been a trade hub from pearls to textiles since its earliest history. Therefore, many of Dubai's prominent families built their financial empires not on oil (like neighboring Abu Dhabi) but on successful trade with Europe, Middle East, and South Asia (Matly and Dillon, 2007).

Dubai was the third most important re-export center in the world in 2004 trailing Hong Kong and Singapore with imports more than doubling between 1998 and 2004; one fourth of the world's global 500 companies were located in Dubai in 2006. Over the past decade, Dubai has recorded significant GDP and economic growth, primarily driven by the non-oil sectors. Dubai represents approximately 29% of the UAE's GDP in 2005 with a recorded nominal growth of 27%. The finance sector represents almost 10% of Dubai's GDP and has been growing strongly.

In addition, Dubai also wished to position itself as the financial service hub of the Middle East and the DFM (Dubai Financial Market) commenced operations on March 26, 2000. The UAE's capital markets have also undergone rapid growth and development in recent years. The DIFC launched the Dubai International Financial Exchange (DIFX) in September 2005 and the Dubai Gold and Commodities Exchange (DGCX), the Middle East's first gold exchange, was started in November 2005.

Moreover, Dubai has enough economic and financial freedom, the most favorable tax regime in the world, high quality and luxury of life, big confidence for investors from the pegged exchange rate etc. All of its economic and financial powers create a big potential for Dubai as an IFC.

In this study, this paper will use comparative analysis and take Shanghai, Istanbul and Dubai as the examples of emerging financial centers. The main methodology is instrumental factors analysis. We also investigate the best practiced official indexes and reports along with books and articles. Through analyzing the three cities' economic conditions, historical factors, potential abilities, post-crisis opportunities and so on, we will conclude with the strengths and weaknesses of Shanghai, looking into its feasibility and competitiveness position as well. Finally, the author will propose some suggestions for further improvement.

This paper explores the dynamics of Shanghai, Istanbul and Dubai's competitiveness. The structure of the paper is as follows. Chapter 1 states some basic and necessary information about financial centers: the definition, classification, characters, functions, benefits and cost and so on. Then it delves into several existing theories about financial centers: place theory, scale economies, geography theory, time-zone and global cities theory.

The section following that will summarize preconditions and common requirements for a city to become a global or international financial center. According to those summaries, furthermore, we construct the evaluation instrumental factors structure to make a comparative analysis. The categories of instrument have 4 major indicators, namely human capital, business environment, regulation and legislation, and financial potential. It includes the macroeconomic and microeconomic environment together with many other indexes and reports or academic frameworks. We will try to make the analysis as comprehensive and concise as it can be.

Chapter 2 explores Shanghai's potential as IFC and evaluates it by instrumental factors built in the chapter. After a dynamic lateral comparison of the city alone, it is more meaningful to have a vertical comparison among the cities with other developed financial centers. Therefore, chapter 3 is spared for a comparative analysis of the three cities, using the same instrumental factors. Every city is unique, and it must build on its own strengths and work to shore up its own weaknesses; these strengths and weaknesses are themselves often a reflection of the time in history and the larger world and local circumstances.

However, a comparison among them and other developed financial centers still yields a number of useful clues (Elliott, 2011). After that, we will draw conclusions about the strengths and weaknesses of Shanghai and foresee the feasibility of Shanghai as an IFC. Finally, the paper will propose some recommendations for further improvement.

CHAPTER 1

AN INTRODUCTION TO FINANCIAL CENTERS AND INSTRUMENTAL FACTORS

1.1 Introduction to Financial Centers

1.1.1 Definition Of A Financial Center

There are many different ways to define financial centers based on their functions; however, a unified definition for financial centers has not been achieved yet.

A financial center of any kind is a city in which there are concentrated financial activities - banking, insurance, and ancillary types of financial business-which cater to a region outside the city itself, which may include other cities as well (Harry,1976). A financial center is simply a location where a substantial amount of financial business is conducted (Elliott, 2011). Jarvis (2011) defined such a center by stating 'common definition of financial center thus normally highlight their roles as place of intense exchange relations which exhibits a dense clustering of a wide variety of financial business in one centralized location.'

Generally speaking, a financial center is a city or a district that has a heavy concentration of `financial institutions', plays a financial intermediary function of financial flow, facility financial service, offers a highly developed commercial and communication infrastructure, and where a great number of domestic and international trading transactions are conducted. Therefore, we will see the categories of the financial centers as follows.

1.1.2 Hierarchy of Financial Centers

There are many different classifications of financial centers depending on diversity of functions. This thesis uses the classification from GFCI, which classifies financial centers into five hierarchical categories based on their financial activities scales.

Global financial centers that have truly global foci: where only a few can claim that role such as London and New York; International financial centers conduct a significant volume of cross-border transactions such as Hong Kong and Singapore; Niche financial centers that are worldwide leaders in one sector, such as Hamilton in reinsurance or Zurich and Edinburgh in fund management; National financial centers are often within federal countries that act as the main financial center for financial services within one country such as Toronto or Frankfurt. Regional financial centers conduct a large proportion of regional business within one country, e.g. Boston or Vancouver (GFCI, 2007).

These centers come in different sizes and levels of capability, with no clear dividing line. A successful financial center can and do fulfill more than one role. For instance London and New York, both considered as the only two truly global financial centers, can implement all the other functions that lower hierarchy financial centers' functions.

1.1.3 Main Characters and Functions of Financial Centers

Generally, when a city functions as a financial hub, it could be called as a financial center. Therefore, to some extent, the characters of the financial centers are their practical functions.

In summary, we can identify some common characteristics of financial centers: A financial center is the place that agglomerate financial institutions, and centralized-decentralized center of funds; it must be a clearing center, with high quality of financial service systems; it must encourage financial innovation, and it has a standard and transparent financial regulation environment.

Besides, a financial center is a desirable place that attracts talents and professionals. Its location is close to other key areas such as economic, trade, shipping centers and so on. High-developed communication and net system infrastructure are the basic conditions for such centers.

The main functions of a financial center are to optimize the allocation of resources, as a financial information hinterland, to decide the goods prices in the market and to arrange capital raising and financial risk management transactions for firms around the world.

1.1.3.1 Optimizing the Allocation of Resources

A financial center owns special financial markets and achieves optimum allocation of resources according to supply-demand regimes. In order to meet the demands for funds of the institutions with high profit and development, it makes use of price-decision and adjusts direction of fund flows. In a financial center, a fund supplier invests with financial instruments that they choose by themselves; however, fund demanders can finance funds according to their operational conditions and financial status. They can choose suitable financial instruments to get the quality and quantity of the funds they need. Therefore, a financial center acts as a financial intermediary that can raise capital and make effective allocation (Pan *et al.*, 2010).

1.1.3.2 Financial Information Agglomeration, Distribution Function and Price Discovery Function

A developed and well-operated international financial center is a place which agglomerates and distributes financial and economic information as an information hinterland. It could provide references for local and periphery financial institutions and offer financial information for government regulation of the macroeconomics. In addition, a financial center should decide market price according to the supply and demand for fund (Pan *et al.*, 2010).

1.1.3.3 Risk Management

A financial center is not only necessary for raising capital but it is also necessary for risk management. A financial center provides many instruments for investors by providing mechanisms of realization, evaluation, dispersion and transformation of the risks. Investors can select features, options, interest exchange rates to diversify investment risks and enhance the security level. In addition, a financial center is a concentration place of transactions with very high daily volume and turnover transactions.

Therefore, it can ensure high liquidity of financial capital for the investor. Moreover, financial centers generally possess relatively complete financial regulations and experienced financial supervisors. Such institutions and professional individuals depend on diversity on-site or off-side methods to supervise traders, and they follow financial laws seriously in order to create smooth transaction and enhance the security of financial transactions (Pan *et al.*, 2010).

1.1.4 Benefits and Costs Of Financial Centers

1.1.4.1 Benefits

A larger body of economic literature supports the premise that the performance and long-term economic growth and welfare of a country are related to its degree of financial development (Čihák *et al*. 2012). The link between financial development and economic growth is now well established in terms of empirical evidence, and it can be traced back to the work of Joseph Schumpeter in the early 20th century, and more recently to Ronald McKinnon and Edward Shaw..

World Bank "Financial systems around the World" (Čihák *et al*. 2012) points that: Financial intermediation and financial markets contribute directly to economic growth and aggregate economic welfare through their effect on capital accumulation and on technological innovation. Well-developed financial centers direct capital to the right investment projects and promote sound corporate governance and they could make microfinance more efficient by diversification of savings and portfolio choices, and they can increase the return on savings and create more opportunities.

Kaufman (1999) believes that most benefits for the city as a financial center are that a financial center could enhance the value of the city, promote economic development, decrease fixed assets and pollution, and create more effective banks in the competition environment. Elliott (2011) argues that the cities fight for IFCs because of the perceived advantages including high added value, quick development, and low fixed-cost plant and equipment.

1.1.4.2 Costs

Although being a financial center seems to be very appealing, there are also costs, including high fragility, spillover of problems from the center to the domestic economy, and quick departure of footloose human capital (Kaufman,1999). We can classify the cost as sensitivity, fragility, and complexity of financial regulations.

The sensitivity of the financial center stems from its functioning as an information hinterland. The financial market indexes interact with economic and political changes. Therefore, markets may sometimes overreact, exaggeratingly and they might signal distortion. In case this situation is discovered and manipulated by the speculators, then, probably it will result in a wider range of panic and more serious distortion. If and when this happens in a financial center, it can lead to a multi-market uproar, and a source of financial turmoil. This is mainly because of the fact that a financial center is fragile and finance is a service industry which lacks the entities like the industry sector instead relying on financial institution agglomeration.

If a city loses its function as a financial center, the finance industry of this city will shrink quickly, and this will lead to a series of problems such as economic loss, increase in unemployment, loss of clients in many related industries etc. All in all, it is a big threat to this city’s economy, and it is impossible for a city which loses its financial position to attract enough resources, rebuild its industry and expect an advantage in certain aspects.

Financial development should be based on economic entity but because of its independency to economics and its autonomous operation in the meantime, it has its own rules for movement. Obviously, we can claim that the higher the level of the financial institutions, the more the level of independence. In addition, the relatively small investment in fixed capital in financial centers is offset by a relatively large investment in human capital. But unlike fixed capital, human capital is highly mobile. Thus, financial centers are relatively footloose and what is attracted easily can be lost just as easily and quickly.

1.2 Theoretical Bases

The emergence of financial centers was far from being random events; they were supported by theories including section-chosen and place theory, economics of scales, finance geography and global cities theory. It is obvious that all of these theories have some relations with each other; in other words, they are not independent but have some overlaps.

1.2.1 Section-Chosen and Place Theory

Davis' (1990) section-chosen theory applies industrial place chosen theory to financial area, using the demand-supply microeconomic way and economic externality to discuss the inner decision of the formation of the financial centers. In his paper, Davis also claims that it is the principle of profit maximization.

From the supply aspect, the following elements are to considered: the availability of skilled personnel, degree of difficulty in market access and openness of enterprise, ancillary activities and market scope, supply of suitable office instruments, steadiness of economic and political conditions, laws for protecting profits of consumers and investors and cost of operations which are related with fund supply and demand, tax regime and sorts, efficiency of payment and clearing systems, and complicated financial regulations.

From the demand aspect, the ability of access to the market and acquisition of clients are the main elements to be considered by financial institutions.

Place theory, represented by Walter Christaller (1966), claims that the spatial inequities result in urban hierarchies. Producers consider that the boundary of the demand should be at the minimum scale which meets the normal profit because the range of the market has geographical limitations: if the place is far, the consumer and producer prefer to close it, so the hierarchy range of the market depends on the distance and size. In some certain ranges, the distinctive space is only one with high-value goods and services, but minor centers have many locations producing lower-value goods and services.

The less the hierarchy is, the more the center locations and the smaller the sizes are. The importance of the center place is due to the products value. In Christaller's work, how far the distance consumer could bear is decided by the degree of the requirement of the products, namely, the "thresholds" of goods. The higher the value of the goods, the bigger range and far more distance the consumers could tolerate.

Thus, it produces a spatial configuration of urban centers that disperses them hierarchically relative to the value order of the services and goods they produce (Jarvis, 2011). Then, the more concentration of the urban center and the volume of high-value goods and services it could provide, the higher the economic thresholds intensify; that's why, the absolute size of the center place grows into an urban setting as a result of an economic hinterland.

1.2.2 Scale Economics

Jarvis puts forward the main content of the scale economics as follows:

" Scale economics result from clustering which arise from the efficiency gains and reduction in costs associated with financial agglomeration, where the density of financial services firms not only reduces barriers to transaction facilitation but creates information symmetries and knowledge economies that reduce operating

and transaction costs. Clustering, for example, produces allied markets and agglomerates skills capacity in financial management, engineering, legal and settlement systems which reduces collective industry costs and allows competition in the provision of services because of market size and specialization. It also provides employment pools of highly skilled labor that would otherwise require large upfront sunk costs for training and skills development. Further, scale economics and clustering allow for the emergence of trust relationships and of transactional norms that become institutionalized" (Jarvis, 2011).

1.2.3 Geography of Finance

Geography of finance provides advanced proof by applying asymmetry of information and path dependence theory to analysis formation, development and vicissitudes of financial centers.

The main ideas about the financial geography focus on information hinterland and information center (Gordon *et al.,* 2003, Porteous 1995). Porteous (1995) defines information hinterland as 'a region for which a particular core city, acting as that regional center, provides the best access point for the profitable exploitation of valuably information flows.'

As for the key role of the information, the effect of information asymmetry had driven the financial institutions approach to the information hinterland as close as possible to consuming the least. There is a clear asymmetry in the reality of financial markets. The regulatory information is not available and it is the same between the policy maker and taker. Limited by the distance and relationship, the pathway of getting the same and accurate information for different participators is distinctive with the quality and cost.

The asymmetry of information makes fair competition more difficult for foreigners who typically cannot understand the local market regulations and many policies as accurately and efficiently as the domestic state-owned companies. The costs of collecting and verifying the information become very high, thereby approaching information hinterland has a strong impact on profit especially for the remote party.

It is well known that financial profits are very sensitive to policy information, and distance to information source plays a key role for the information users because acquiring the useful information has a high cost. Accessibility, accurate and fast spread of information can save a lot of cost, enhance the profitability, and find potential opportunities. The sensitiveness of information generates geographical proximity to the sources of policy information due to cost saving and as a result overcomes information asymmetry problem.

In addition, the size of the information hinterland is an essential factor to attract financial firms. Therefore, geography of finance could agglomerate the amount of quantity combined with high quality information as a hinterland and make the financial center develop strongly in economic and financial aspects with the political protection (Zhao *et al*. 2004:579).

With the development of the new technology and a number of innovations in telecommunication, many scholars have argued that geography is not important anymore; however, geography of finance still matters in finance and financial centers. Furthermore, financial centers have clearly demonstrated that the forces of spatial agglomeration remain powerful and positively impact the financial sector (Elliott, 2010).

Compared to neo-classical economy, geography of finance is close to spatial agglomeration and transportation cost theories, and accordingly it emphasizes the scale of economics, conjunction effect, market thickness, knowledge spillover and other external effects. Additionally, , immobilization of production elements, rent for lands, transportation cost and other external uneconomic factors all have influence on spatial economics. The geography of finance's characteristic quality and contribution lies in using the concepts "increasing returns" and "imperfect completion" as its assumptions.

1.2.4 Global City Theory

From the 1970s on, new technologies, telecommunications and information technology have led to both decentralization and agglomeration of economic activities. The global flows of goods, capital, information and personnel have grown rapidly and beyond the state boundaries. The network between the cities began to dominate the world economy.

All of these intensified the international metropolis to play an increasingly important role in control and management of the center of global economic activities. Therefore, since 1980s many scholars have done extensive research on the world or global cities in the background of globalization. Hence, it can be said that the world cutting edge cities are global financial centers as well. From this perspective, the world city theory could explain the formation of global financial centers. The representative works are Friedman (1986, 1995), Sassen (1991, 1994, 2001), Castells (1996) and British Loughborough university's GaWC group.

Friedman (1986) argued that key factor for a world city is the international professorial human capital that is in the dominant position in the world. The flow of international professional talent is both the reason and result of the world city formation. City is an organization that caters for their requirements in all aspects. In Friedman's hypothesis, the world city should function as a headquarter, a financial center and an articulator city (that link a national or regional economy to the global economy).

According to Sassen (1991, 2001), economic globalization and modern telecommunications are two factors contributing to the agglomeration of the new urban service economy that is based on cross-border networks as well as strategic locations with vast concentrations of competitive resources. To develop their global empire, MNCs tend to locate their headquarters in global cities where, under the global telecommunication network, their affiliates and subsidiaries around the world can be effectively controlled and coordinated.

Specifically, MNCs seek competitive locations that are underpinned by many factors, including sufficient transportation and communication infrastructure, high quality of professional services such as legal, accounting, and financial services, rich social and cultural amenities, and good institutions rooted in the rule of law (Petter, 1998). Therefore, MNC headquarters and high-end financial services are inextricably concentrated in the same key locations. This pattern of spatial co-location has contributed to the making of a global city or a global city region (Tong, 2001).

The world and global city literature advance the notion that as economic production intensifies worldwide, only a few cities are able to coordinate and control complex, particularly product-oriented functions, such as financial functions, that support the expansion and construction of the world economy (King 1989; Clark 1996; Knox 1995; Sassen 2001). Alongside the world city hypothesis, there are other workswhich view world cities as epicenters of global financial transactions (Reed 1981; Goldberg et al. 1988; McGahey et al. 1990).

However, as Poon (2003) said these two lines of work are not mutually exclusive. London, New York and Tokyo (Big-3) in the global city system have been the central themes of these two major strands of literature. Ben Edwards in the Economist (1998) has called this "Capitals of capital".

Sassen (2001) argued that world, particularly global, cities are the primary agents in the production of financial services. These services provide transnational corporations with the necessary capabilities to conduct their global operations. In viewing world cities as central production sites of complex financial activities, supply-driven factors underscoring the construction of the global urban system have emerged as popular explanations in the formation of international financial centers.

To sum up, although in terms of the world city theory, different scholars have their own ideas that emphasizes different aspects, their conclusion share many common characteristics about financial center formation. If one city is a global financial center, it must be a global city, but it may not be true the other way around.

1.3 Methodology Issues and Comparative Analysis of Instrumental Factors

1.3.1 Methodology Issues

The main methodology of this thesis is to apply the instrumental factors that are developed by the author to make comparative analysis and investigation of indexes & reports.

Compiling a city-level comparable data is somehow impossible for the data is not available in some indicators at the city level. Most of the famous professional official research reports and indexes only focus on the country-level, but it is reasonable and appropriate to use country level data to represent the city-level indicators for Shanghai, Istanbul and Dubai which are the outstanding cities in their countries.

This is possible because these three cities' performances overtake their countries' levels in almost all aspects. The approach taken in this paper is to use the data specific to the city level wherever possible; however, in some cases data availability dictates that state or national-level data be used.

In order to make the study comprehensive, this thesis used all of the data dynamics. They cover at least 2 years, most of them covering more than 5 years. Therefore, the reports and indexes are reliable and comprehensive. The principle adopted when choosing indexes and reports is to focus on the institutions' best practice aspects and on their professional and special fields.

1.3.2 Instrument Factors Literature Review

In this section, we developed the comparative instrument factors by reviewing the main indexes and reports and other preview studies about financial centers.

Global Financial Center Index (GFCI) is the most authoritative index study about global financial centers, which was originally sponsored by the City of London in 2007 and published biannually. Until 2012 there had been 12 reports and covered 77 cities already. GFCI is a ranking of the competitiveness of financial centers based on over 26,000 financial center assessments from an online questionnaire survey together with over 80 subjective instrumental factors indexes from organizations such as the World Bank, the OECD and the Economist Intelligence Unit.

GFCI divided 77 indicators to 6 categories: people, business, environment, Market access, infrastructure, general competitiveness and reputation. GFCI examines what decision-makers think, both the senior executives who make such decisions and the other professionals whom executives wish to lure to or retain at their firms.

"Xinhua-Dow Jones International Financial Centers Development Index, published by Xinhua News Agency, is linked up with the Chicago Mercantile Exchange (CME) Group, in 2010. It includes subjective indicators evaluation of and in-depth interviews with experts such as senior government officials and senior managements of financial industry familiar with global financial markets with authority in local regions to measure the IFC development. This index designed three levels of indicators.

CDI China's Financial Center Index (CDI CFCI), published by China, is about the formation and development of other financial centers to design an evaluation system to evaluate 31 cities which participate in the completion of building a financial center. It shows the strength and weaknesses of all of the 31 cities. This index also references to GFCI, and it was adjusted to comply with Chinese cities. In all of the indexes and reports, there are some instrument factors with different aspects and foci.

Economic Freedom Index, published by the Wall Street Journal and Heritage Foundation,uses 10 economic measurements to evaluate 179 countries' degree of economic freedom. There are four main indicators:rule of law, limited government, regulatory efficiency, and open market, which are divided into 10 broad factors of economic freedom. For each factor, a country receives a 0 to 100 percentage score, indicating the degree of economic freedom in the country. The higher scores indicate higher degree of economic freedom (Heritage, 2012).

The Economic Freedom of the World (EFW), published by the Fraser Institute,covers 42 variables which are divided into five broad areas: size of government. legal structure and security of property rights, access to sound money, freedom to trade internationally, regulation of credit, labor, and business. Each component and sub-component is placed on a scale from 0 to 10 that reflects the distribution of the underlying data. A higher value signifies greater economic freedom.

Economic freedom of the world measures the degree of supporting economic freedom from the countries' policies and institutions. It is different from "Economic Freedom Index" which focuses on the performance in economic freedom. These two indexes evaluate economic freedom from two different perspectives (freetheworld, 2012).

Global Competitiveness Index, published by the World Economic Forum, measures the productivity and competitiveness of a country which is determined by the country's policies, institutions and other factors. It states the productivity level and determines the rates of return of investments in an economy which derive growth rate. This index classifies economies as factor-driven, efficiency-driven and innovation-driven at three levels. Calculated from a mixture of survey and hard data, it covers 12 pillars and the data for each pillar is converted into a scale from 1 to 7. Higher values indicate greater competitiveness (Weforum, 2012).

Ease of Doing Business (EDB), published by the World Bank, it measures business regulations and enforcement for 185 economies. EDB is designed to indicate the regulatory costs of business and can be used to analyze specific regulations that enhance or constrain investment, productivity and growth. The index is calculated by ranking the simple averages of country percentile rankings on each of the 10 topics covered (Doingbusiness, 2012).

The Human Development Index (HDI) is a comparative measure of life expectancy, literacy, education and standard of living for 177 UN member states. The index converts the HD level into a scale of 0 to 1. The higher the score is, the higher the human development level (HDI, 2012).

The Transparency International Corruption Perception Index (CPI) ranks 176 countries in terms of the degree of perceived level of public sector corruption. The CPI Score relates to these perceptions of the degree of corruption as seen by business people and country analysts from around the world, including experts who are citizens in the countries evaluated. The score ranges between 100 (highly clean) and 0 (highly corrupt) (Transparency, 2012).

Quality of Life Index (QLI), developed by Carol Estwing Ferrans and Marjorie Powers in 1984, measures both satisfaction and importance regarding various aspects of life. It covers four sub-indicators which are health and functioning, psychological/spiritual domain, social and economic domain, and family.

In addition to these indexes and reports, there are quite a few academic papers and scholars studying the conditions and indicators that play an important role ina city’s development into an international financial center. For example: Elliott (2011), Simon X.B. (2002), Aniyand (2011), James and Kam (2005) and so on. All of these studies propose a number of important factors which describe those conditions and indicators; and use those factors as criteria to evaluate the level of financial centers.

FIGURE 1.1 COMPETITIVENESS FACTORS RANKING IN GFCI 2012

Competitiveness factors	Rank
The availability of skilled personnel	1
The regulatory environment	2
Access to international financial market	3
The availability of business infrastructure	4
Access to customers	5
A fair and just business environment	6
Government responsiveness	7
The corporate tax regime	8
Operational costs	9
Access to suppliers of professional services	10
Quality of life	11
Culture and language	12
Quality /availability of commercial property	13
The personal tax regime	14

FIGURE 1.2 FACTORS INFLUENCING IFC DEVELOPMENT

Macroeconomic environment	High GDP per capita and growth High trade and investment intensity Sound macroeconomic policy Low business costs (office rental, corporate taxes, wages, etc) Significant domestic market and growth potential Rule of law and the absence of corruption and red tape
Microeconomic business environment	Highly developed physical infrastructure (communications, transpiration, etc.) Adequate human capital (availability of finance, accounting and legal professionals. etc) Livability (low pollution, affordable housing, access to high quality health, education, entertainment and supervisory practices) Political and economic freedom
Financial market efficiency	Low transaction costs (taxes, brokerage fees, etc.) International standards of accounting, legal and supervisory practices Large variety of financial products and services

Source: Laurenceson and Tang 2005

There are other criteria to classify the indicators; for example the criteria of LAURENCESON & TANG (2005) in figure 1.2. They only have two levels of indicators; the first level consists of macroeconomic environment, microeconomic business environment, and financial market efficiency; while the second level covers 13 small options.

Elliott (2011) stated 10 important factors shown in figure 1.3. after analyzing the theories and other materials about the formation and development of financial centers.

FIGURE 1.3 CRITICAL ATTRIBUTES NECESSARY FOR SUCCESS

Critical attributes necessary for success
• Availability of high quality finance professionals Quality of life English speaking staff • Rule of law • Appropriate regulation (financial stability, toughness, predictability, speed) • Avoidance of excessive taxation • Proximity to customers • Core infrastructure • High quality support services • Reasonable operational costs • Openness to foreign entry • Favorable time zone

(ELLIOTT, 2011)

IMF (The key building blocks of world class financial centers) shows 10 factors which are: open and fair financial markets, free flow of capital and a convertible currency, skilled workforce/flexible labor laws, prevalent use of globally familiar language, fair, transparent, efficient legal and regulatory regime, sound and fair tax regime, implementation of international standard and best practices, low cost of doing business, high quality, reliable and appropriate physical infrastructure, and stable political and economic environment.

Xinhua-Dow Jones IFC evaluation framework has five main indicators: first, financial markets which focus on capital, foreign exchange, banking, insurance market; second, growth and development of capital market, economics, and innovation outputs and potential; third, industrial support that includes business environment support, basic urban conditions, and urban infrastructures; fourth, service level including government service, intellectual capital, and urban living conditions; fifth, general environment which refers to economic, political situation and openness.

1.3.3 The Explanation of Instruments and Factors

There are many papers mentioning amplefactors from their own aspects, we could not indicate all. However, we could combine and synthesize them, we find the common points, depend on them and other theories reviewed in previous sector 1.2; thereby we may create our own instrumental factors for competitiveness.

We create two levels of indicators demonstrated in table 1.1. The main factors include 4 elements: human capital, business environment, regulation and legislation and financial potential. The second level indicators encompasses 19 sub-factors. The detailed explanation for the factors is in the following section.

TABLE 1.1 THESIS COMPARATIVE ANALYSIS INSTRUMENTAL FACTORS

Human capital	The availability of skilled personal
	Quality of life
	Culture and language
Business environment	High quality reliable and appropriate infrastructure
	Economic and financial freedom
	Market access
	Taxation regime
	Stability of political and economics
	Reputation of the city
Regulation and legislation	Rule of law
	Fair, transparent efficient legal and regulatory regime
	Government responsive
	Institutional effectiveness
Financial potential	Financial performance

The instrumental factors framework above is author’s own contribution to this thesis. Thefactors cannot be considered in isolation, because they are all necessary conditions; therefore, the combination of the factors has a greater impact on a financial center’s competitiveness than that of the individual elements.

1.3.3.1 Human Capital

1.3.3.1.1 Availability of High Qualified Financial Professionals

It is obvious that the qualified professionals working in financial institutions are critical hidden values who have immeasurable impact on increasing wealth and diminishing costs. Usually, they are familiar with clients, and their expertise, knowledge of previous transactions and relationships with the investors could bring a great value to the institution and much of that value could be transferred to another firm if the employee becomes dissatisfied and leaves the company. Attracting, retaining, and motivating the professional staff is one of the most critical tasks performed by the top management of any investment bank (Elliott 2011).

In addition, it takes long time and an abundance of resources or high costs to train new experts in this field because being an expert requires significant experience and diverse skills from broad aspects. Therefore, the cost of the professional human capital is the most important factor. Human capital plays essential role in financial markets and services; nothing could be done without people. This is also the top factor in both McKinsey's survey and in the GFCI surveys; and is ranked very highly by all the surveys and commissions. McKinsey survey also lists separately, as the fifth and sixth most important factors, the "reasonable compensation levels to attract quality professional workers" and the "availability and affordability of technical and administrative workers,".

Moreover, to the quantity of the talented people and the quality of the talent, in this thesis the educational situation will be compared for education plays essential role in providing high quality workforce and professional talents.

1.3.3.1.2 Quality of Life

Higher quality of life is a source of attractiveness for professional staff. The simple reason is that CEOs or top executives are all human beings in the end; they hold their own preferences about where to live. Therefore, finding and keeping good professionals is easier if the firm can offer employment in a place where successful professionals want to live (Elliott, 2011).

Furthermore, the preferences of CEOs usually determine the firm's overall location decision. Elliott (2011) also stated some common characters of the subjective assessment of quality of life, although the criteria vary for different people. There is a number of common attributes: first, there should be attractive houses and apartments; secondly, it should offer good cultural, entertainment and sports facilities; thirdly, there should be excellent restaurants, good quality and internationally accredited schools; fourth, there should be low levels of pollution, fifth, there should be low levels of noise pollution; and finally, the commuting should not take excessively long.

1.3.3.1.3 Culture and Language

Culture does not only relate to the humanistic quality, overall life and work environment, but also improves work efficiency. Efficiency is critical for financial services due to the information issue; therefore, culture is a matter of quality in financial environment.

Language is an irreplaceably important factor in human capital, and it is the most efficient means of communication in human activities like financial services. So far, English has become a global language, especially the global business language. Many business transactions and the majority of world trade are very largely conducted by English. From the legislation and contract perspective, English is even more necessary and important. The global deals conducted by standard laws are written and interpreted based on English. In addition, the critical disclosure documents describing a transaction are also generally in English (Elliott, 2011).

Therefore, language has a significant relationship with information hinterland and asymmetry, regulation and legislation, information accuracy and worldwide international customers. Translation costs time and decreases the efficiency of information flow. Multiple languages will bring some misunderstanding during transaction or trade, and any small mistakes could result in substantial losses in business. As a result, a truly global financial center needs a large number of fluent English-speakers. Furthermore, for higher levels of hierarchy, sophisticated use of English is more important.

Language also has effects on the life quality of staff, especially expats, because it is related to all aspects of an individual's daily life, including entertainment, children's education, eating, shopping and so on. It is harder to persuade CEO's to move to a country where only a few people could speak English fluently and even harder to persuade the couples.

Culture and language do not generally show up in quantitative surveys, but several reports indicate these concepts as an advantage for London, New York and Mumbai and a potential constraint for some of the growing Asian centers. The GFCI survey lumps the factors together and ranks culture and language 12 out of 14 most important factors.

1.3.3.2 Business Environment

1.3.3.2.1 Efficient, Reliable and Modern Core Infrastructure

Efficient, reliable and modern infrastructure are not only crucial for attracting investment and increasing international competitiveness, but also they serve to boost economic growth and job creation. The core infrastructure facilitates transaction and financial services, and is positively related to the quality of life. In terms of financial services, global financial institutions require a well-structured, broad network of physical infrastructure to work properly. As for the cities, basic infrastructure ranges from the power network, the telecommunication network, the water system, road constructions, and sanitation services to modern buildings available and high-end technology.

In particular, traders will only live at stable and reliable environments with high quality basic infrastructures. The cost of lacking high quality infrastructure is expensive in terms of opportunity cost. The global city theory and geography finance theory have reached the same conclusion about infrastructure. Insufficient roads, ports and power generation all can act as chokepoints that diminish the attractiveness and economic potential of a city. It is hard to attract talents without efficient and reliable modern infrastructure.

The GFCI survey shows "availability of business infrastructure" as the fourth most important factor, while the McKinsey survey locates "high quality transportation infrastructure" in the middle of the list of factors. Defining infrastructure more broadly than just transportation would almost certainly raise the ranking more.

1.3.3.2.2 Freedom of Economics and Finance

As the world heritage institution states: 'economic freedom is a condition or state of being in which individuals can act with autonomy while in the pursuit of livelihood'. They define economic freedom this way: "should encompass all liberties and rights of production, distribution, or consumption of goods and services. The highest form of economic freedom should provide an absolute right of property ownership; fully realized freedoms of movement for labor, capital, and goods; and an absolute absence of coercion or constraint of economic liberty beyond the extent necessary for citizens to protect and maintain liberty itself" (Freedom of Economics).

To achieve the goals of economic freedom there should be a three-pronged approach: from individual, government and society. Firstly, it should empower the individual and assure non-discrimination. The individuals should be able to pursuit their dreams based on their effort and ability without being exposed to any discrimination arising from race, ethnic background, gender, class, family connections, or any other factors unrelated to individual merit. Their property rights should be protected properly and respected by the state and society; all of their economic activities such as work, produce, consume, and invest should take place in a free environment, they should be able to choose everything and any method they prefer under the rule of law.

Second, in terms of the government, they should guarantee the openness and fairness of decision making process and a competitive environment. The political and economic theories accept that government could supply public goods more efficiently than privates. However, if the government imposes a separate constraint on economic freedom -beyond those clearly considered public goods-, it may supplant private-sector activity and usurp resources that might otherwise have been available for private investment or consumption. The result is lower productivity, economic stagnation and declining prosperity.

Last but not the least, the overall society should make every effort to maintain the freedom for the individual and the government, respecting the rules and government supervision. The society is responsible for protecting the investors' and consumers' profits, and preventing speculative and other similar activities which distort the natural order of economy and finance.

1.3.3.2.3 Market Access

We consider the market access the capital access and cost of doing business. The higher levels of capital volume and the ease of doing business, the much more attractive a financial center.

1.3.3.2.3.1 Operational Cost

The GFCI shows operational cost as the ninth most important factor and McKinsey shows "reasonable commercial real estate cost" as the 12th most important factor. Both "World city" and "geography of finance" theories consider the operational cost. It is obvious that profit equals revenue minus cost; therefore, operational cost is the fundamental factor that must be considered in a financial center. Usually there are two types of cost: soft and hard cost.

Soft cost usually means personnel costs which make up the largest non-financing expense for investment banks by a considerable margin. However, the hard cost is very significant and relatively more expensive than personnel costs. For example; real estate, technology instruments, official equipment, local services etc. Tax should be included into the hard cost as it is the compulsory consumption of a financial center and also a large payment.

Operational cost varies among different cities which have different quality of life, regulation processes, tax regime and scare resources. London and New York are the good examples to verify this. New York has a restively low operational cost while for other things the conditions are similar with London, which is a significant advantage when the investors engage in financial activities (Elliott, 2011).

1.3.3.2.3.2 Open and Fair Financial Market

The precondition for being an IFC is to have an open and fair financial market; none of the foreign companies would like to invest in a place full of discrimination and restrictions. An open and fair market could ensure whether public or private the domestic and foreign companies share the same and have equal footing rather than being discriminated or having limited rights.

Moreover, such an environment will attract best practices in the world, cutting edge technology, and render the financial sector more efficient and productive. Overall, such open and fair financial markets result in a strengthened institutional capacity and enhance the quality and transparency of regulation and supervision, reinforce the market attractiveness for investors and intermediaries in the international demand market (SIA).

1.3.3.2.4 Sound and Reasonable Tax Regime

Tax regime is essential for an economic and financial center, it is a critical matter for business environment. The size and regime of tax impact many aspects of investment and growth. Anyone doing business must consider the tax regime, because it is a part of cost, and avoidance of excessive taxation is important for business. Corporate and personal tax regimes play an important role on determining the cost structure and overall profitability of financial firms.

In GFCI 12 the corporate tax regime ranked the 8th, and the personal tax regime ranked the 14th. Tax regime has a serious effect on the growth of different financial centers and on determining the location of headquarters. In the GFCI 12 questionnaire about the most important factors for competitiveness, taxation ranked no.2, and it is mentioned 138 times.

Moreover, keeping a reasonable level of tax could encourage the development of the private sector and the formalization of business. Efficient tax administration can help encourage business to become formally registered and the economy to grow, to expand the tax base and increase tax revenues. The high tax rate does not equal to high revenue, because collecting tax consumes time and resources. Both private business and government can benefit from tax systems which are simply to administer and where levels of compliance are high. Where taxes are high, businesses are more inclined to opt out of the formal sector.

The empirical studies show that higher tax rates have negative impact on formal businesses and private investment. "A 10% increase in the effective corporate income tax rate is associated with a reduction in the ratio of investment to GDP to 2% and a decrease in the business entry rate of about 1%. A tax increase equivalent to 1% of GDP reduces output over the next 3 years by nearly 3%." (World Bank, 2010).

1.3.3.2.5 Stability of Political and Economics

Political and economic stability is the basic and necessary pre-condition for the formation of a financial center. The stability could ensure the rights and profits of the investors and institutions. Finance is a very sensitive sector, any adverse news could lead to inestimable results. Therefore, a steady political and economic environment could increase the investor confidence; attract more talents and more cooperators in the markets. No one likes to work in a place surrounded by conflicts and war troubles, and not a single company could afford the loss arising from an unsteady economy. Therefore, it is one of the most basic and important elements that the individuals and companies consider while they choose the place to live, work and do business.

1.3.3.2.6 Reputation

Reputation is getting more and more important in real life apart from the financial and economic activities. When the GFCI 2012 questionnaire asks about the most important factors for competitiveness, reputation is mentioned 127 times and its ranking is no. 3 in all factors, just behind business environment (1^{st}) and taxation (2^{nd}). One could be very rich but may have a bad reputation, the same is valid for financial centers.

Consequently, reputation is the long term credit, it is more reliable than money and other things, and it could not be attained by money. A good reputation is related to many aspects, and it could measure the real power of a city or country. The higher the reputation of a financial center, the more attractive financial institutions and talents.

1.3.3.3 Regulation and Legislation

1.3.3.3.1 Rule of Law

Like everything in the world must follow some rules, the financial activities also require the rule of law, without laws a financial center could not exist. Elliott (2011) pointed: "business cannot thrive unless there are predictable and reasonable rules under which it can operate". This is particularly important for the type of financial transactions one finds in a global financial center, since their complexity could produce a great deal of ambiguity if the laws were not clear. Of course, it is not sufficient for the written laws to be acceptable, they must also be enforced in a predictable and reasonable manner.

In addition, the commercial law is not only necessary to the individual but also to those working in the firm must have the personal security knowing that they work under reasonable laws which will not be enforced in an arbitrary or corrupt manner. The rule of law will protect both investors' and demanders' rights as well as those of the working staff (Elliott, 2011). The McKinsey survey of senior executives ranked "fair and predictable legal environment" as the second most important factor and the GFCI surveys show "the regulatory environment" as the second most critical factor which effectively presupposes the rule of law.

1.3.3.3.2 Fair, Transparent, Efficient Legal and Regulatory Regime

A successful IFC could not develop without a fair, transparent, flexible, and efficient legal and regulatory environment combined with characteristics such as being independent, ordered, reasonable, economical, efficient and so on; otherwise, morbid legal and regulatory regime will result in lower investor confidence, investment rate, productivity and overburden in financial sector. However, it is not enough to own a regime of laws and rules if they are non-transparent and unfair, uneven or inefficient. The enforcement and implementation play essential role. The sound legal and regulatory regime must protect market participants from risk at the highest level, ensure accurate and rapid market direct, insulate from governmental and political intervention, and be free from corruption (SIA).

SIA Key Building Blocks in the paper: "The Key Building Blocks Of World Class Financial Centers" states that:

> A fair, flexible, and transparent legal system that is attractive to global investors and intermediaries will demonstrate the following characteristics: 1) wide latitude for private parties to contract; 2) a non-approval based

regulatory system; 3) qualified regulators; 4) strong, consistent and predictable legal standards and remedies; 5) expeditious and transparent enforcement; 6) a well-trained, ethical judiciary and local bar (including a sufficiently large number of local lawyers); and 7) a legal system open to foreign legal practitioners.

1.3.3.3.3 Government Response

Regarding the formation and evolution of financial centers, there are two major types: one of them develops naturally based on economic and trade centers, for instance: London and New York; the other one is dependent on the government support in which case the advantages of the city are combined with the pushing of the native government. The most successful example for this type is Singapore, so we called this pattern the Singapore pattern.

Government policy plays a very important role in many aspects of financial centers, such as, the financial regulation; the way of making laws, the supervision of financial activities, the resistance to financial crises, attitudes towards the domestic and foreign companies. Especially, within the beginning phase of the development of a financial center, it is necessary to have some preferential policies and institutional environment provided by the government, which can attract investors and set up institutions.

Otherwise, the formation process of agglomeration may accelerate slowly. There are many examples arising from the case of Singapore. Although Singapore implements pure market economic system, in the formation process, it still took positive impetus measures, to make sure Singapore currency establishes its status in the straight regulation in the Asia area.

1.3.3.4 Financial Potential

1.3.3.4.1 Economic Foundation

Financial services sector constitutes a relatively higher stage in the development of a society. It must be based on real economics because, as the theory has stated before, economic clustering attracts financial institutions agglomeration, impetus financial services and also attributes to the formation of international financial centers. The steady and rapid increase of the income level and GDP growth rate play an essential role on the formation of international financial centers since GDP growth rate not only reflects the short-term economy but also the dynamism of long-term income level.

The higher growth rate reflects the long term potential and how vibrant the domestic financial market of the country is, because the domestic demand for sophisticated financial products and services is closely related to domestic savings per capita and, hence, GDP per capita. The higher level of income, the higher level of investments (Meyer,1998). The attractiveness of investing is positively influenced by higher economic growth rate and higher volume of international trade.

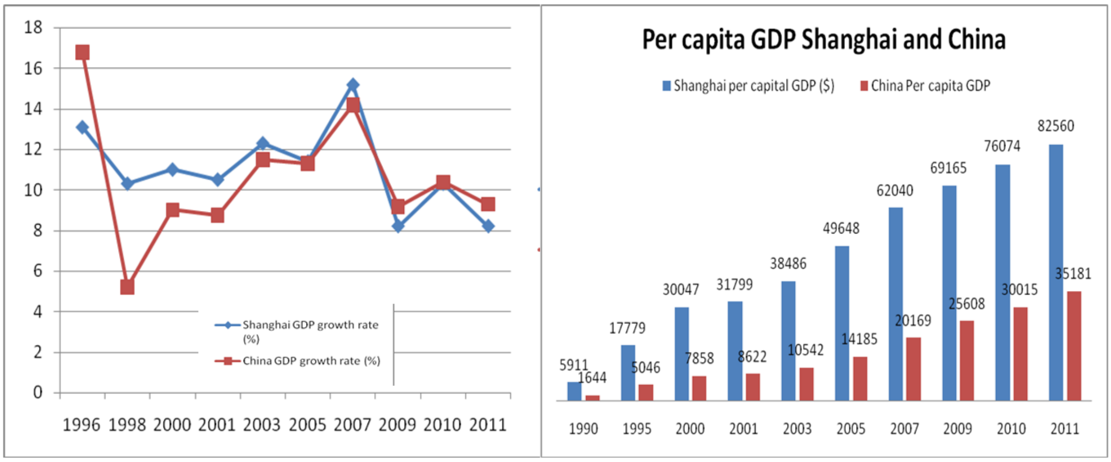
A city is more likely to emerge as an IFC when the real sector is both dynamic and internationally orientated. As Meyer stated, an IFC is essentially en exporter of financial and related services. The trade activities of merchandise goods and direct investment also make use of these services. In particular, exports and imports provide opportunities for the financial sector to underwrite trade through the provision of credit, and if domestic firms expand into other countries through foreign direct investment, then financiers can follow firms with the provision of financial products and services (Meyer,1998).

Thus, the foreign direct investment (FDI) is a sign of the development of the economy and finance. The more developed the economy, the more FDI coming into the country. Therefore, when we compare the cities we must consider these entire economic bases which determine, in a certain extent, the long-term development.

Financial centers could not establish without a high quality finance sector potential. This thesis will study banking market, bond market, capital market and insurance market, and compare them in terms of the real volume of trade and also use some indexes to come up with comprehensive and concise factors to evaluate the development of the financial market and services. High quality service is essential to the financial center development. The investors and customers are sensitive to service quality for the high quality and efficient services could decrease the cost of doing business as well as standard service processes could eliminate the barriers between different places. The GFCI survey ranks the "access to suppliers of professional services" the tenth.

1.3.4 Relationship between City-level and Country-level

FIGURE 1.4 GDP GROWTH RATE AND PER CAPITA GDP OF SHANGHAI AND CHINA



Source: data from Shanghai Statistic Yearbook 2011

In figure 1.4, we could see Shanghai's development is faster than China as a whole. GDP growth rate is higher or equal to China mainland and per capita GDP is almost double. Not only in terms of economic indicators, but regarding many other indicators the results are similar. Shanghai is also one of the most important economic, financial and trade centers in China. In the following chapter we could see the details.

TABLE 1.2 PROPORTION OF ISTANBUL TO TURKEY IN MANY SECTORS

Ratio of Istanbul to Turkey %	GDP	Population	Labor	Industry	Services	Export	Import	Bank deposits	Bank loan	Tourism	Tourism income
2008	21.7	17.75	12.4	27.7	22.2	55.39	55.09	45.5	42	22.8	26.8

Table 1.2 illustrates the proportion of Istanbul to Turkey in terms of some major economic and financial indicators in 2008. Istanbul accounts for 21.7% GDP and around 18% of the total population in Turkey. More than 50% international trade and more than 40% of bank deposits and loans concentrate in Istanbul, and almost one third of the tourists are attracted by Istanbul.

Figure 1.5 SECTORAL PROPORTION OF DUBAI TO UAE NORMINAL GDP 04-05

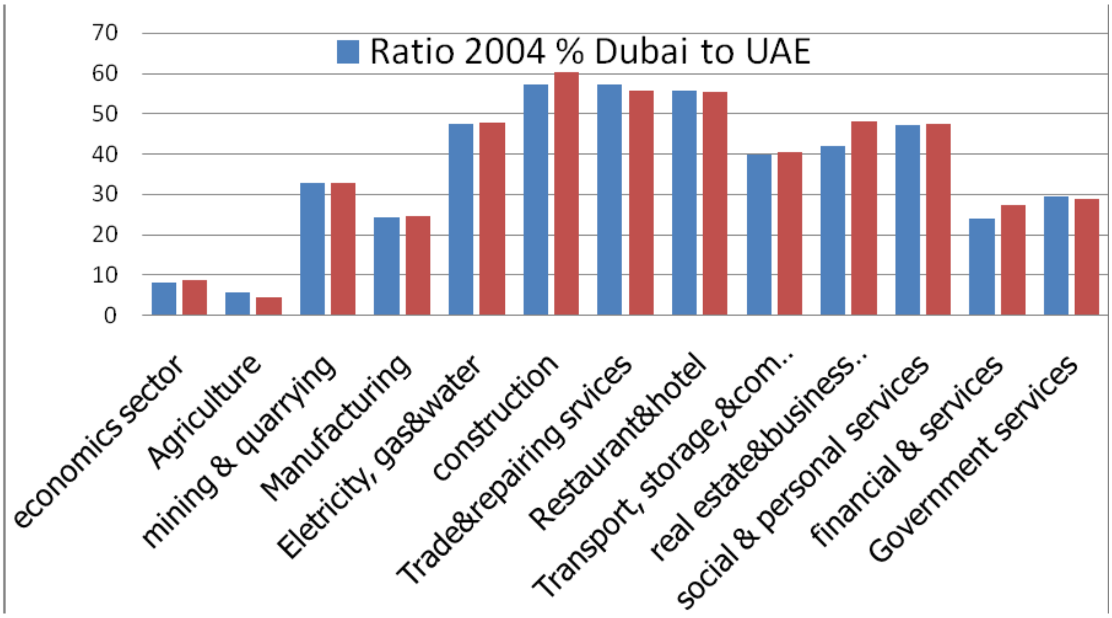


Figure 1.5 shows the ratio of Dubai to UAE GDP in many sectors in 2004-2005. Except the agriculture sector, Dubai accounts for a large ratio in all other sectors. In terms of financial sector, the ratio is approximately 30%.

In sum, the data derived from the analysis of the three cities and countries shows that Shanghai, Istanbul and Dubai are the most outstanding cities in their countries. After the states engaged in national projects to develop these cities as IFC's, the development speed and the share of country in nearly all aspects increased significantly. Shanghai and Istanbul do not exist as independent governments; the political, micro and macroeconomic environment is same with the country.

Although Dubai has separate and independent laws and administration system, the leader of Dubai and UAE is the same person under the UAE monarchy system. Therefore, in economic, financial and political aspects, city and country are in the same situation. It is reasonable to apply country-level data to represent city-level; however, in the thesis, the author will use city data wherever available.

CHAPTER 2

SHANGHAI'S POTENTIAL TO BECOME AN INTERNATIONAL FINANCIAL CENTER

2.1 Introduction of Shanghai

2.1.1 Shanghai's the Historical Role as an International Financial Center

From a historical perspective, Shanghai has the potential to be at the forefront amidst the world's international financial centers. In the early 20th century, around the 1920s to the 1930s, Shanghai has been the largest financial center in the far-east – which could be traced back during the time of the Opium War. Nonetheless, Before the Opium War Shanghai had a well-developed domestic trade center which was owing to its superior geographical position.

In 1850, Shanghai became another Foreign Trade Center and exceeded Guangzhou soon after. In 1861, Shanghai's export constituted 50% of the entire country's revenue, and during 1871 – 1873, the foreign trade proportion saw an even higher increase which amounted to 64.1% of its exports. Trade expansion has been a leading force in the financial sector's development, and since Shanghai was the biggest commodity distribution center, it certainly needed a lot of provision for its financial institutions, (e.g. such as fund turnover and other financial services).

Consequently, overtime Shanghai became the most pivotal financial center. By 1858, the number of banks in Shanghai was more than 100, and until the early 1880s, Shanghai had a large-scale ticket number semicolon of 24, which retained a relatively strong force considering the total amount earned by the banking house had reached 300 million taels of silver.

Ever since the beginning of the 20th century, Shanghai's financial industry had reached a new climax. After 1897, the Commercial Bank of China established its head office in Shanghai. The Ministry of the government-run banks and the Bank of Communications also established branches in Shanghai. In addition, there were exclusively only private capital operational banks that opened in Shanghai.

In the late 19th century the Qing government borrowed a huge foreign debt and the XinChou indemnity, which required a repay installment, first remitted to Shanghai and then to the foreign banks. Until 1911, payments on this channel ticket amounted to over 9,400 million taels of silver. A lot of money pooled into Shanghai, financing activities progressed rapidly. Loans to foreign banks saw a significant increase, and the foreign exchange market turnover increased manifold. Even the government reserve, which never dealt with interest, started to lend loans to the banking house in order to make a profit on interest.

After World War one and the proceeding years was a period for Shanghai for which further development of the financial sector and the building of its foundational period. Although under the Northern Warlords, known as the warlordism governance, the production for many provinces and territories declined, the market depressed, but Shanghai's industrial, commercial and financial sector has immensely developed due to the war.

From 1913 to 1921 there were 26 new banks established, the total bank deposits rose from a mere 1 billion dollars in 1912 to nearly 500 billion dollars in 1921. The Chinese Security Exchange was established in Shanghai in 1920, the standard gold exchange market in 1921, and furthermore the loan market and the exchange market were much more active. Chinese banks began concentrating on foreign exchange businesses and the bank credit market trend also witnessed a significant expansion.

After the foundation of the Nationalist government in Nanjing, the financial industry developed in an unprecedented fashion. This was not only due to the good relationship between Shanghai bourgeoisie of the financial industry and Chiang Kai-shek regime, but also by virtue of Shanghai's close proximity to the political center. During The late 1920s, and early 1930s, Shanghai's financial industry funds distribution role reached new heights due to the increase of social currency capital collected by the bank.

In Shanghai, it was estimated that by 1935 a total of 42 billion deposits from 27 major banks were made which accounted for 47.8% of deposits in China. North China, mainland China and China's Industrial Bank's head offices or management, along with transportation, salt, and Jincheng, all successively centralized to Shanghai and formed a financial network center. Consequently, China's radiation issue significantly improved, and various regions' interest rates and other financial market price transfers to Shanghai and other large commercial ports within the exchange market was now based on Shanghai's market standard.

In the 1930s, Shanghai stood as the Asia Pacific's undisputed financial hub. The "Pairs of the East" hosted not just opium dens and cabarets, but also the world's third-largest stock market by capitalization. In 1931 China's total foreign trade reached 3.51 billion yuan (each Customs taels equivalent to 1.50 yuan), has an increase of which increased five times more than the beginning of the 20th century. At this time in Shanghai the domestic import value is about three times more than Hankou, four times than Tianjin, five times over Guangzhou and six times over Qingdao.

In the 1934, thirty-three foreign banks were operating in Shanghai, more than in Hong Kong (21) or Singapore (17). Bond turnover was up to 47.7 billion in 1934. The Securities Building, which was built in Hankou Road, is located in the central area of Shanghai where International bankers exchanged foreign currency. They lent money to British property investors and Japanese cotton factory owners. They financed government railways, and military campaigns by the then-ruling Kuomintang (KMT).

At the time, the neoclassic, domed headquarters of the Hong Kong and Shanghai Bank (since renamed HSBC) stood out as the most visible presence of the foreign banks. The ionic-columned structure anchored Shanghai’s riverfront boulevard, the Bund, and was the world’s second–largest bank building after the Bank of Scotland in London (Tong, 2009). Therefore, Shanghai's financial industry and trade facilities are evidently exceptionally broad.

Shanghai is also the largest investment market; it holds funds from all over the country, moreover, its Stock Exchange business is far more than Beijing's Stock Exchange. The broad absorption and concentration of funds are not only due to the role of financial markets in Shanghai, but also because it led to capital flows, and resulted in good economic returns from its enterprises and industry. Shanghai expanded its financial center location from China to the Far East.

Shanghai's massive gold market trading volume, which is only behind London and New York, is larger than France, Japan and India. Due to the huge throughput of HSBC Bank's Foreign exchange market, the volume of transactions also increased. At that time, it was discernible that the financial position of all other cities in the Far East could not match up to that of Shanghai.

Shanghai lost the IFC position quickly due to arduous reasons such as government default, global currency crisis, wartime inflation, Japanese invasion and new China “seal policy” which pushed entrepreneurs, bankers and capital out of mainland of China, which thus led many banks to flee to Hong Kong.

Although, from Shanghai’s financial center position in history, we should not draw a conclusion that Shanghai must become an IFC in the future, we can however attempt to illustrate that Shanghai has a considerable amount of power potential to become an IFC. Today it is time for Shanghai to restore its IFC position.

2.2 Present Shanghai

Shanghai is one of four central municipalities of the People's Republic of China and also the biggest city of mainland China; it occupies an area of approximately 7,037.50 square kilometers, with a population of twenty million. Located at the Changing River mouth, which is in the middle of the country's continental coastline, it owns the biggest industrial base and the biggest seaport for foreign trade in China (CDI). It is central to China's economy, finance, trade and shipping. From 1978, with the "opening up reform" in China, Shanghai began to recover its strength and regain its glorious position.

The GFCI has noted that in the next few years Shanghai will probably become more prominent and that if there were to be another global financial center, it would most certainly be in Shanghai.

Shanghai is the economic center in mainland China; considering the population factor, we chose per capita GDP, which comparatively reflects a country's real economic power. Shanghai's per capita GDP is much higher than the entire country's average level. From a dynamic aspect, Shanghai's GDP grows rapidly and substantially faster than that of the country's. Therefore, Shanghai is in a leading economic position within China, and assuredly the economic base as a prospective financial center.

TABLE 2.1 GDP GROWTH RATES OF SHANGHAI AND CHINA

	1996	1998	2000	2001	2003	2005	2007	2009	2010
Shanghai GDP growth rate (%)	13.1	10.3	11	10.5	12.3	11.4	15.2	8.2	10.3
China GDP growth rate (%)	16.8	5.21	9.02	8.77	11.49	11.3	14.2	9.2	10.4

Source: data from Shanghai Statistic Yearbook 2011

China is unequivocal financial center, an appropriate epithet for the city of Shanghai. Overall, Shanghai ranks number-one in China in terms of the financial sectors' overall economic output as well as in the number of private banking headquarters. Furthermore, Shanghai also serves as a leading domain for the majority of foreign banks in addition to the big banks within China such as ICBC, the Bank of Agriculture, and the Bank of Communications; consequently they prefer taking Shanghai as their primary headquarters. The financial market factors of Shanghai are the most accomplished and developed throughout the nation. More than half of the management companies are located in Shanghai, and the direct total for financing accounts to one fourth of China as a whole.

In addition, Shanghai takes approximately two-thirds the amount of headquarters of foreign capital banks, accounting for 85% of total asset within China. In China, five-sevenths of the headquarters of legal persons of foreign-invested property companies concentrate in Shanghai. In addition, 60% of headquarters of Chinese-foreign joint venture insurance companies and management companies of joint venture funds are located in Shanghai (CDI, 2010).

Shanghai is the second biggest global center of the stock market, ranking third among the global stock exchanges, only next to NYSE and NASDAQ, surpassing those of London and Tokyo. Shanghai is the second biggest global center of the futures market, only next to that of Chicago, simultaneously taking a place in the center of the ten global biggest derivatives markets. Besides, Shanghai is the global center and biggest gold spot transaction and the second biggest center of diamond spot transactions (CDI, 2010).

2.2.1 The Opportunity and Blueprint for Shanghai

Chinese government unveiled a national strategic plan for establishing Shanghai as an international financial and shipping hub by 2020, compatible with the country's economic strength and the RMB's international status. The IFC should be a multi-functional and highly internationalized financial market system, a pool of internationally competitive financial institutions and financial professionals and a compatible system of taxation, credit, regulation and law (CGS, 2009).

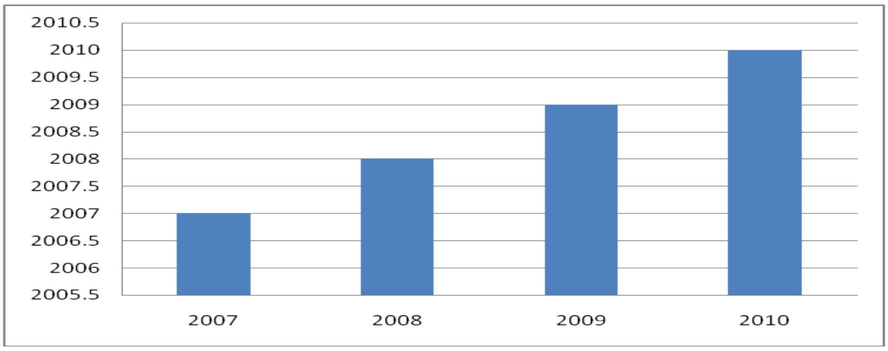
2.3 Evaluations by instrumental Factors of Shanghai

2.3.1. Human Capital

2.3.1.1 Quantity of Professional Staff

Shanghai developed a high quality of professional staff. The employees in the finance sector have increased significantly from 49.8 thousand in 1993 to 231.9 thousand in 2008, an average growth rate of 10.3%. Figure 2.1 shows the quantity of employees in the finance sector from 2007 to 2010.

FIGURE 2.1 QUANTITIES OF WHOLE SOCIAL EMPLOYEES IN FINANCE SECTOR (2007-2010) 10,000persons



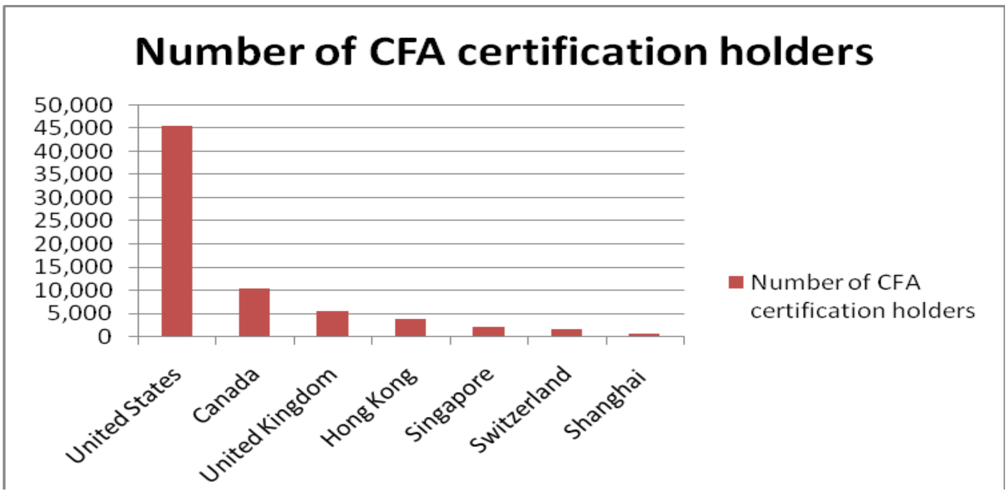
Source: data from Shanghai Statistic Yearbook 2011

Regarding the education structure aspect, the vast majority of staff members had obtained a bachelor's degree or higher. In terms of industries, a master's degree in securities, insurance and fund proportion is higher than most traditional banking sectors, especially with respect to being the master of the technical backbone of the securities industry, which can be as high as 81.5%.

Although the absolute number of professional staff has increased immensely, there exists a big gap in terms of quality when compared to other developed financial centers. For instance, the number of international professional qualification certificates and their incremental facets could not meet the current demand. Take CFA certificate as an example, until August 2008 (see Figure 2.2) there are 80,000 CFA charters all over the world. The number of the top six countries are: United States (45,700), Canada (10,500), United Kingdom (5,500), Hong Kong (3,800), Singapore (2,100) and Switzerland (1,600); whereas Shanghai currently only has 615, far less than Hong Kong and Singapore, accounting to 0.77%, which is even less than 1% of the world.

In addition, new added number of certificate holders still has a big difference compare to other countries. The incremental numbers are 2,610 in the U.S., 746 in Canada, 519 in the U.K, and 483 in Hong Kong. The total in Mainland China is only 326 which accounts for 0.265% of the employees amongst the entire financial sector.

FIGURE 2.2 NUMBER OF CFA CERTIFICATION HOLDES 2008



2.3.1.2 The Talent Shortages Hit Shanghai

An extensive training of good business leaders is indeed required due to the fact that Shanghai is obliged to finance the cultivation of the competitive environment and an increased amount of experienced individuals for practical operations. With the rapid expansion of financial enterprises, the number of senior management personnel could not keep up with the demand. Moreover, there is a bigger gap in the senior business management talent, especially an imbalance of the demand and supply in the professional staff who are experienced and familiar with international financial processes, and moreover those who are competent in managing business operations and are capable of resisting financial risks.

Top talent shortages are prevalent in various financial industries such as: banking industry research and analysis, risk control and personal finance; the insurance industry is much-needed in terms of risk management and investment analysis, actuarial and IT personnel; the securities industry has a great demand of risk management, sponsor of the domestic and foreign markets business, strategic research and financial engineering and other areas of expertise; the fund industry demand relatively concentrates on research talent, and general researchers focus more on the economic and political situation.

The basic talents of operations personnel just about meet China's demand, and when it comes to oversupply, the future objective is to enhance the efficiency which is essential in reducing the unnecessary allocation of resources. Support for technical personnel is relatively high, but there is some discrepancy in the structure of knowledge and skills, and the complex financial and legal talent and complex financial operational talent which are all but sufficient.

Professional in general, the growth cycle of the salesperson is relatively in surplus, which basically matures after two to three years of cultivation. However, the growth cycle of investment research staff is longer, usually five to eight years, or even longer, and the total supply is by comparison not enough. However, risk control and actuarial, and professional staff in other relatively newly developed technology are sorely lacking in various financial enterprises.

2.3.1.3 The Education Situation in Shanghai, China

Shanghai has one of the best education systems in China, and it is the first city in the country to implement a nine-year mandatory education. By the end of 2011, the Shanghai Statistic Yearbook data shows that Shanghai has sixty-six universities and colleges in which twenty-five are higher education institutions. These establishments include fields such as science and engineering 18 of which are economics and finance, 3 of them include politics and law.

Additionally, there are 1,337 kindergartens, 764 primary schools, 94 whole secondary schools, 134 senior high schools, and 358 junior high schools, 149 system schools of 9 years and 19 system schools of 12 years. Approximately 591.7 thousand regular second school students and 791.1 thousand primary students are taught by 75.3 and 48.2 teacher staff respectively. The 2010, based on the total population in Shanghai, shows that 21.9% had a college education, double the level from 2000, while 21.0% had high school, 36.50% middle school, and 13.55% primary school education. A mere 2.74% of residents age fifteen and older were illiterate.

Shanghai is a major center for higher education in China. A number of China's most prestigious universities are based in Shanghai, including Fudan University, Shanghai Jiao Tong University, Tongji University, and Shanghai University of Finance and Economics. The Chinese Executive Leadership Academy, a cadre school in Pudong, is also located in Shanghai.

Shanghai's publicly-funded education has the highest educational quality in the world. In 2010, Shanghai took the top spot[2] in the latest round of the most comprehensive assessment of the world's state schools. According to

[2] http://www.time.com/time/world/article/0,8599,2035586,00.html

the Program for International Student Assessment results, Shanghai students, including migrant children, scored highest in the world in all aspects—mathematics, reading and science, all of which outperformed the second best state school in the world by 17 scores. Particularly in mathematics, Shanghai students' average score was 600, which is 100 times greater than the average score of 500 (Dillon, 2010).

With regards to the quality of life in Shanghai, one of the advantages is the relatively low cost of living compared to Hong Kong and other IFCs. We will discuss this in detail in the following chapter.

2.3.2 Business Environment

2.3.2.1 High Quality, Reliable and Appropriate Infrastructure

Communication and transportation infrastructure

TABLE 2.2 SHANGHAI INFRASTURCTURE OF INFORMATIZATION IN MAIN YEARS

Indicators	2005	2009	2010
Long-distance Cable (km)	5,141	4,297	4,670
Length of Information Communication Pipeline (channel km)	1,621	5,354	5,821
Users of Internet (10 000 persons)	803	1,250	1,560
Users of Internet per Hundred People (%)	45.2	65.1	68.1
Broadband Access Users (10 000 households)	247.40	470.32	517.40
# Household Users of broadband access	222.66	423.28	440
Popularity Rate of Mobile Telephone (%)	81.0	109.6	103.1
Average Population Served by Every Post Office (10 000 persons)	2.99	3.04	3.86

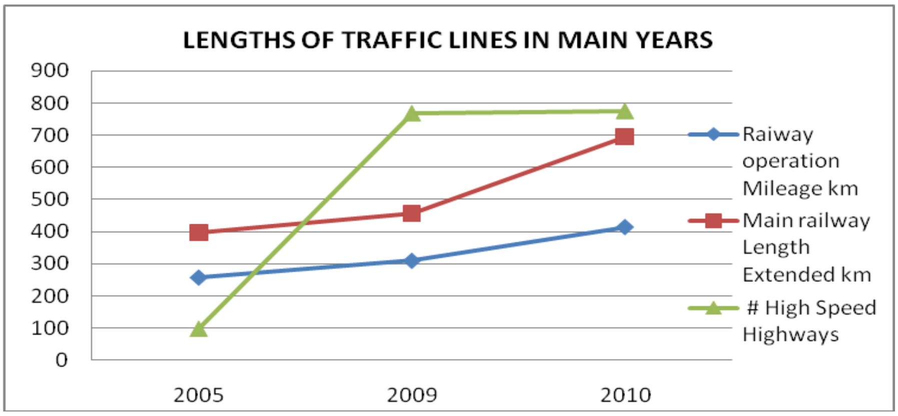
Source: Data from Shanghai Statistics Yearbook 2011

The length of long-distance Cable has reached 4,670 km, and the length of information communication pipelines now extend to 5,821 channel km, which is 3.6 times longer than 2005. The number of Internet users increased steadily; the availability of broadband throughout households has also increased, and digital cable TV users nearly tripled in five years. With more users of the Internet and advanced-technology products, the faster the speed of information disseminates. This could evidently show the development of a higher level of communication infrastructure.

It is not surprising that the popularity rate of the telephone line and the household usage has decreased. This is owing to the widespread usage of mobile devices, considering its portability and access to the Internet. The service provided by the post office has played an important role more than ever before. It was not the sending letters that thrived the industry, but it was rather due to the rapid development and popularity of online shopping which expanded commerce.

2.3.2.1.1 Transportation Infrastructure

FIGURE2.3 LENGTHS OF TRAFFIC LINES IN MAIN YEARS



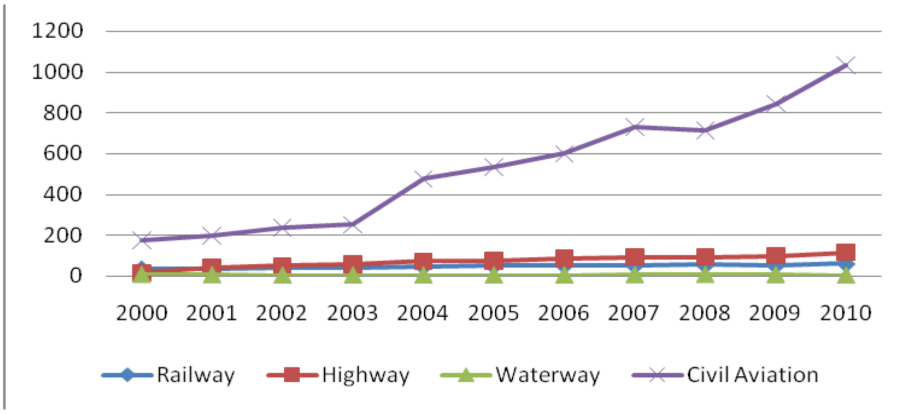
Source: Data from Shanghai Statistic Yearbook 2011

Figure 2.3 shows the length of traffic lines for railway, highway and navigable transportation in the main years. Although the development of the high-technology and telecommunication shortens the distance of the world, it could not shorten the real distance from the places for the transportation and delivery of the goods. Therefore, the importance of the transportation infrastructure never reduced but rather increased. The operation mileage of the railway increased by 37.9% in five years, and the length extended to 697 km. Highway infrastructure has been the most important transportation in the main cities.

Shanghai's number of high speed highways jumped nearly eight times from only 98 in 2005 to 775 in 2010, and the operation mileage extended more than double. Shanghai's port is one of the most important ports of mainland China; the importance of navigable transportation is self-evident. It affords more than 10% cargo trade. From 2005 to 2010 whatever length of harbor, berths of which tonnage and container berths, increased significantly. This shows the potentiality of Shanghai's port and how it has enhanced and improved over the years. The number of berths has had a significant jump from 1990 to 2010, increasing almost five folds. From sea, air, and land-way, Shanghai's transportation condition and basic infrastructure has seen big improvements in recent years.

Figure 2.4 illustrates the turnover volume of passenger traffic of Shanghai in the main years. The most significant jump was in civil aviation, showing that the transportation is not necessarily a monopoly entity for China; moreover, the competition will enhance the service and benefit consumers.

FIGURE 2.4 TURNOVER VOLUME OF PASSENGER TRAFFIC IN MAIN YEAR



Source: Data from Shanghai Statistic Yearbook 2011

From communication, transportation, and the arduous infrastructure improvement, we could see that the Shanghai government has invested huge resources to enhance the difficult conditions of Shanghai in order to match the IFC development scheme. The government investment on the basic urban infrastructure increased from 8,435 million yuan in 1992 to 115,734 million yuan in 2011 a 13.72 fold increase. All of the investments for the improvement of power generation, transportation, communication, facilities for public and civil construction of Shanghai’s stricken urban infrastructures, are undoubtedly a notable achievement.

2.3.2.2 Freedom of Economic and Finance

2.3.2.2.1 Ease of Doing Business

China’s performance in terms of ease of doing business is not quite satisfactory, although Shanghai is more open than all of China, but it still restricted by the Chinese government's control and the frequent enactments of special laws. The overall rank of China with respect to the “ease of doing business” is 89 out of 183 countries, which is far behind the U.S, the U.K, Hong Kong and Singapore, and even worse than Turkey and UAE. The starting or and closing of businesses takes up a lot of time and assumes strenuous procedures. Shanghai ranks last in the world wide when it comes to dealing with construction permits; it includes 37 procedures and takes 336 days on average.

In terms of the financial sector, time and information are money, the efficient procedure could attract more prospects and more opportunities, and otherwise, it will increase costs and lost chances. The employment of workers rank is not desirable either; the rank is 140, but only the rigidity of hours index is within 50. The rank of registering property is 32; which only requires four procedures and takes one month. This index in particular is quite competitive.

In the fields of finance and economy, getting credit is important for doing business; the bank for China is 61 in the world. It is not very easy to get credit somehow which reflects the lack of freedom for business ventures. The next rank is about protecting investors, where profits and rights are crucial. The more profit, thus the higher the protection, which consequently more investors prefer. However, the rank of protecting investors is 93, which again, is considerably behind other developed countries. For example, the

United States and the United Kingdom, Hong Kong and Singapore are 5, 10, 3 and 2 respectively.

Shanghai's rank of paying taxes is also very low at number 130 out of 183 counties. For trading across borders China ranks 44, which although it is behind Hong Kong and Singapore, it is basically satisfied with its standing. China ranks 18 with respect to practical enforcing contracts, requiring thirty-four procedures, which on average takes 406 days to finalize. The last rank in this report is about closing a business, and in this term, China ranks 65, which on average takes 1.7 years and the recovery rate is 84.2% in dollars.

TABLE 2.3 EASE OF DOING BUSINESS

		Singapore	HK	U.S.	U.K.	China
Ease of doing Business	Rank	1	2	4	7	91
Starting a Business	Rank	4	5	13	19	151
Dealing with Construction Permits	Rank	3	1	17	22	179
	Procedures (Number)	11	6	15	9	33
	Time (days)	26	67	26	99	311
Registering Property	Rank	14	57	16	68	40
	Procedures (Number)	3	5	4	6	4
	Time (days)	5	36	12	29	29
Getting Credit	Rank	8	4	4	1	67
Paying Taxes	Rank	4	3	72	24	122
Protecting Investors	Rank	2	3	5	10	97
	Disclosure	10	10	7	10	10
	Investor Protection Index	9.3	9	8.3	8	5
Trading Across Borders Rank		1	2	20	13	60
Enforcing Contracts	Rank	12	5	7	21	16
	Procedures (Number)	21	26	32	28	34
	Time (days)	150	280	300	399	406
Closing a Business	Rank	2	16	15	6	75
	Time (days)	0.8	1.1	1.5	1	1.7
	Recovery Rate (cents/dollar)	91.3	81.2	81.5	88.6	36.1

Source: World Bank: Ease of Doing Business 2010

In summary, the overall situation for China about "Ease of Doing Business" is very lagged in comparison to other developed economies. In many aspects, it ought to take more measures to improve the business environment.

2.3.2.3 Economic and Finance Freedom

Freedom of economics and finance is one of the important factors to evaluate the possibility of a city to be a financial center. Firstly, a complete financial regime in relation to financial transactions, regulation, and judiciary and information flow, could ensure the development of financial markets and institutions in an apple-pie order.

Secondly, with proper, well-balanced regulation regime openness, this can surely contribute to investment freedom and bring about a sufficient financial market by stimulating the financial scale and expanding capital flow. Overlooking the Chinese government's similar scale size, a massive gap still exists when compared to the United States, the United Kingdom, Japan, Singapore and Hong Kong in foreign investment, banking, property rights, regulation and market information.

TABLE 2.4 ECONOMIC FREEDOM INDEX CHINA 2012

<table>
<tr><th colspan="2">Rule of law</th><th colspan="2">Limited government</th><th colspan="2">Regulatory efficiency</th><th colspan="2">Open markets</th></tr>
<tr><td>property Right</td><td>20</td><td>Government Spending</td><td>84.1</td><td>Business Freedom</td><td>46.4</td><td>Trade Freedom</td><td>71.7</td></tr>
<tr><td rowspan="2">Freedom From corruption</td><td rowspan="2">35</td><td rowspan="2">Fiscal Freedom</td><td rowspan="2">70.4</td><td>Labor Freedom</td><td>55.4</td><td>Investment Freedom</td><td>25</td></tr>
<tr><td>Monetary Freedom</td><td>74.2</td><td>Financial Freedom</td><td>30</td></tr>
</table>

Source: data from heritage 2012

From table 2.4, we could see that the freedom of China leaves much to be desirable. The overall world rank is 138 out of 184 countries in the 2012 report. Hong Kong, Singapore, the United States and the United Kingdom rank 1, 2, 10, and 14 respectively. In particular to Hong Kong and Singapore, which are in the Asian region, possess more freedom than China. In China, except for trade, monetary, and government spending freedom, all of the freedom indicators in the four categories are very low. The overall score is only 30 out of 100; it is very limited in terms of its financial activities which consequently has a great deal of impact on the financial scale.

The rule of law which includes property rights and freedom from corruption is the worst item on the list. The property right is "the ability to accumulate private property, and wealth is understood to be a central motivating force for workers and investors in a market economy" (Heritage, 2012). It is the vital feature of a fully functioning market economy. Secure property rights give citizens the confidence to undertake entrepreneurial activity, save their income, and make long-term plans because they know that their income, savings, and property are safe from unfair expropriation or theft (Miller and Kim, 2012).

For China, the property right score is so low due to individuals not trusting the government; there are perilous problems with inefficiency, corruption, the judicial system and problems of the government, and above all, China's score for freedom from corruption confirms these assertions. However, the independence, transparency and effectiveness of the judicial system have proved to be the key determinants of a country's prospects for long-term economic growth and to maintenance of peace and security and the protection of human rights (Miller and Kim, 2012).

Economic freedom is not only about the attractiveness of the financial center, but also to how easy it becomes to access the market. Especially for the foreign companies, if the financial environment is too limited, attractiveness inevitably diminishes.

2.3.2.4 Tax Regime of Shanghai

China's tax regime is complicated and is seen as an overburden for domestic and foreign companies. The structure of the Chinese tax authorities depends on the different service objects which are classified as two systems: National Tax Bureau and the Local Tax Bureau. They are responsible for enterprises and corporations assessing and collecting taxes and individual income and property taxes, respectively.

Foreign invested enterprises which includes equity joint ventures, cooperative/contractual joint ventures and wholly foreign-owned enterprise, and foreign enterprises which include representative offices and branches doing business in China are liable to the following types of taxes: (1) Income tax; (2) Transaction tax: Value added tax, Consumption tax, Business tax; (3) Other taxes: Vehicle and Vessel license tax, Stamp tax, Property tax, Deed tax (KCSL, 2007).

In addition, custom duties are levied on imports and exports and individuals working in China are liable to individual income tax. For the non-resident enterprise without a permanent establishment in China are subject to a withholding tax of 20% on its profits, interests, rentals, royalties and other income sourced in China. Double tax agreements (DTA) may reduce the rate.

Shanghai has a lot of concessions of the tax regime to attract foreign investment. Foreign enterprises engaged in manufacturing in Shanghai pay income tax at a reduced rate of 24%, moreover, if they are established in Pudong New Area which are economic and technological development zones of Shanghai such that the income tax is at a reduced rate of 15% instead of 33%. In some areas, tax holidays still apply to foreign enterprises engaged in preferred industries. As the permission to WTO, all business entities in China have to pay the same rates of taxes, therefore, all entities enjoy the lower tax rate in the special zone.

Property tax is levied at an annual rate of 1.2% on the original value of the real estate, after 20% is deducted from it. The tax rate is 12% for the rental income. However, if newly constructed houses are built or purchased by the foreign-invested enterprise in Pudong New Area and Economic and Technological Development Zones, shall be exempt from real estate tax for five years as of the month of completion of construction or purchase. Withholding tax on profit, interest, rental and royalty are 20% for foreign enterprises that have no establishments in China. However they enjoy a reduced withholding tax rate of 10% in Shanghai (KSCL, 2007).

Shanghai's government made many encouraging policies in order to make Shanghai more attractive. However, tax is still an obstacle compared to Hong Kong and other financial centers. Shanghai’s personal income tax rate tops out at 45%, compared to 17% in Hong Kong (Tong, 2009). In China, the statutory rate is 20%, but the effective rate of corporate income tax paid is lower at 16.9%. The proof from paying taxes report has verified the inefficient tax regime and process in China mainland.

Take Hong Kong SAR as a comparison, the ease of paying taxes rank 3 and 121 for HK and China out of 186 economies, respectively. The difference lies on all the procedures and time consuming items. Total tax rate is very high in mainland China, 63.5%, almost higher than three times to that of Hong Kong which is only 23%, furthermore, it is 18.7% higher than the world average level at 44.8%. Time to comply taxes in HK only takes an average of 80 hours per year, but China took five folds more time which consumed 398 hours per year.

In terms of tax payment, rank is 7 and 3 for China mainland and HK respectively. High tax rate and complicated procedures of collecting taxes have an inverse impact with respect to the attractiveness of the city. From all of the data, we could arrive at the conclusion that the taxation regime for Shanghai is a big disadvantage for an IFC (pwc, 2012).

2.3.2.5 Reputation of Shanghai

Shanghai has a good reputation, standing 20th out of 77 in the GFCI 2012. The method used in GFCI is by checking the difference between the average assessments given to a center and its overall rating. For Shanghai, the average assessment is 693 and 37 higher than GFCI 12 rating, therefore, the reputational advantage of Shanghai is 37, which indicates that respondents’ perceptions of Shanghai are more favorable than the quantitative measures alone would suggest.

2.3.2.6 Stable Political and Economic Environment

In recent years, the global economic and financial environment has been more complicated and unpredictable, and the recent financial crisis also impacted investors’ confidence of the financial centers. Although the Chinese economy's immunity from the financial crisis, for which they had even gained more power, as the World Bank financial stability report stated: "China's Economy continues to intend and its financial sector developed in the deepening level, stronger resilience of the sector against shocks, stable financial markets performance between financial conditions of the government, corporate and household sectors, progress in financial infrastructure construction, and the overall soundness of the financial system.

There are still a lot of hidden problems such as imbalances and unsustainable problems in economic growth remains pronounced, with downward pressure in economic growth, upward pressure in price movement, and potential risks in the financial sector, there are new challenges in the maintenance of financial stability.”

2.3.3 Regulation and Legislation

2.3.3.1 Law and Legal System

The legal system of China is similar to the European Code Law System. There are three levels of regulation in China, the highest levels is The National People’s Congress (NPC) or its Standing Committee which includes the Securities Law and the Fund Law. NPC has the ultimate law making body. The second level is the State Council together with its various administrative departments which authorized and promulgated administrative regulation and measures that as long as they are not contravening the relative laws such as the Constitution; which is an important source of laws in China. The administrative bodies are the sole interpreter of the administrative regulations and measures. Their power to interpret the laws is only limited, or subject to the adjustments of its supervisory bodies and the court.

The third level is China's Security Regulatory Commission (CSRC) in accordance with (and subordinate to) the laws and regulations of the Stated Council, and they are developed and promulgated rules and regulations. However, the CSRC rules and regulations may be described as "Tentative" or "Trial" where they are new regulatory requirements or they relate to innovations, but they have the same status as other rules or regulations promulgated by the CSRC and are enforceable as such (KCSL, 2007).

To conclude, the characters of China's laws and regulation could be summarized as numerous regulations and implementations; arbitrary changes, tentative, privileged first, mutually restriction, power struggle and confusion.

There are many reasons for the chaos of laws and regulation. One of the problems about laws is that China does not apply the standard law which is generally applied. Until 1994, China only has the first company law, however, which is a very "General Law", which was not valid in some special issues and was simply enacted. In order to deal with the specifics, the government made some special laws which, briefly speaking, depend on the circumstance when the special laws could not be applied, the general laws play a minor role.

In addition, China owns a large amount of state-owned companies, therefore, government's essentially control the content of the laws when taking into account the government and state-owned companies and their opinions.

There is another obstacle for which there is limitation for the branches of foreign companies registered in China, due to the Company Law defects. Since there is no implementation of regulation when it comes to registration in China and its administration of branches, therefore, only certain industries are allowed to set up branches in certain locations in China. For instance, the administration of the branches of foreign banks in Shanghai all belong to the central bank of China, The People's Bank of China, which is governed by a special set of regulations.

The next most common attributed affair to that of Shanghai and all of China is the regulation feature and its aspect of non-transparent and obfuscation regulation environment. Much of this is due to the rapid rate of development of regulation systems, such that many intuitions make a lot of regulation. There are some overlapping financial sectors, and since none of them have absolute decision power, in some instances, they have regulation competition (Jarvis, 2011). As China's financial stability report, which is developed by the IMF, states that: "There are various levels of law making within China."

Another important reason for regulation uncertainty is the competing political interests (Jarvis, 2011). Shanghai is more open than many other cities of China; the local government prefers higher liberalization and greater foreign bank participation as a tool to rapidly transform China's banking system. While the decision right not belongs to Shanghai instead of Beijing. The alleged professional protectionists worry about the situation getting out of control and that if there exists too much shares of the foreign companies then the power of Shanghai may overtake Beijing's. Therefore, they will not accept some useful and beneficial regulations or policies which may promote the development of Shanghai's financial center (Jarvis, 2011).

Present Shanghai has a more transparent regulation and legislation system than ever before, especially after China joined the WTO, China's law and regulation environment made progress. For example, if someone were to be doing business in Shanghai, all applicable laws and regulations can be download from the government’s official website. The People’s Courts are the judicial organs of the state, which are able to exercise independent power in accordance to the law.

The People’s Courts and their judges are appointed by the NPC and its Standing Committee. When a person believes that his/her right has been infringed by any administrative body, he/she can normally complain to its supervisory body, or resort to a review by the court under the administration law (KSCL, 2007).

Without a transparent regulation and legislation environment, the efficiency of the institution will have a great reduction in terms of quality. Lacking in powerful and efficient laws and rules, the competition of different political powers will add excess burden and stress to the financial system, resulting in inefficiency.

2.3.3.2 Government Responds

High-quality corporate governance is believed to encourage financial development, it has a positive impact on economic growth and financial developed (WEF, 2008). Although the Chinese government supported Shanghai in developing into an IFC, the main problem of Shanghai is that the local government's political leadership has no independent decision-making authority about the timing, policies, pace and economic and spatial configuration and styles of Shanghai’s development. However, this national development strategy is substantially controlled by Beijing (Jarvis, 2011).

The regulation of China is very complicated between state and market imperatives. The government – Beijing, capital city of China, has the right for ultimate control, nonetheless this government control is not always accurate and efficient. Sometimes it makes a lot of oversights in development, mismatches the market demand and national ambitions, resulting in missed opportunities. Shanghai faces a high location risk coming from Beijing's intervention. Therefore, Shanghai's greatest challenge from the domestic aspect is to secure the consensus and commitment of policy makers in Beijing (Laurenceson, 2005).

Another obstacle is that Shanghai suffers from a lack of political and economic freedom which is reflected as non-transparent when dealing with officialdom, as well as the government's direct and discretionary control over the national economy (Laurenceson, 2005). This shortcoming in the rule of law makes many observers remain skeptical about Shanghai's capacity to become a credible international financial centre in the near future.

2.4 Financial Potential of Shanghai

2.4.1 Overview Development of Financial Industry

Shanghai has a steady higher economic growth rate which could provide a strong economic basement for the financial development. In only ten years, the per capita GDP increased by 60.5% from 2000 to 2010.

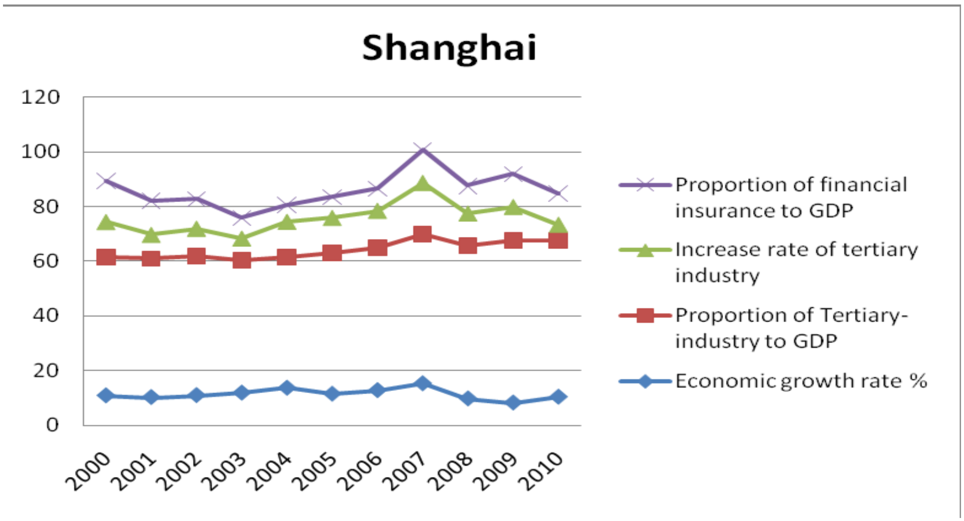
TABLE 2.5 SHANGHAI PER CAPITAl GDP AND ANNUAL GROWTH RATE OF PER CAPITAL GDP%, AND THE PROPORTION OF CHINA

(unit: 100 Million Yuan)	1990	1995	2000	2001	2003	2005	2007	2009	2010	2011
Shanghai Per Capital GDP	5,911	17,779	30,047	31,799	38,486	49,648	62,040	69,165	76,074	82,560
Shanghai PPP Growth Rate (%)	-13.2	28.1	11.0	5.84	13.33	11.89	18.56	5.06	10.99	13.76
China Per Capita GDP	1644	5046	7858	8622	10542	14185	20169	25608	30015	35181
China PPP Growth Rate (annual %)	8.23	24.77	9.77	9.00	12.17	15.00	22.24	8.01	17.21	17.21
Ratio of Per Capita GDP Shanghai to China	3.60	3.52	3.82	3.69	3.65	3.50	3.08	2.70	2.53	2.35

Source: Shanghai Statistic Yearbook (2012); China Statistic Yearbook (2012)

Shanghai's financial industry developed rapidly from the opening policy in China. The development speed of Shanghai is faster than that of mainland China and also higher in quality. However, the financial sector proportions is approximately only 10%, far less than the government plan which aims to take 15% of Shanghai's GDP.

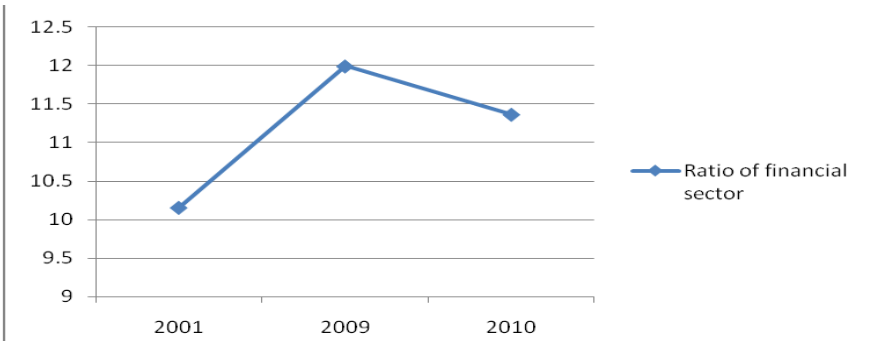
FIGURE 2.5 SHANGHAI



Sources: Data from Shanghai Statistic Yearbook 2011 Unit: 100 million yuan

Shanghai's tertiary develop is very steady, the average increase rate is over 10% throughout, and the proportion to Shanghai's total GDP is more than 60% from 2000 until now. Although during 2000 to 2005 the tertiary industry had a slight decrease, but after 2005, the proportion of the tertiary industry steadily rose, and it accounted to more than half of the GDP of Shanghai at almost 60%.

FIGURE 2.6 RATIO OF SHANGHAI'S FINANCIAL SECTOR TO TOTAL GDP IN MAIN YEARS



Sources: Shanghai Statistic Yearbook 2011

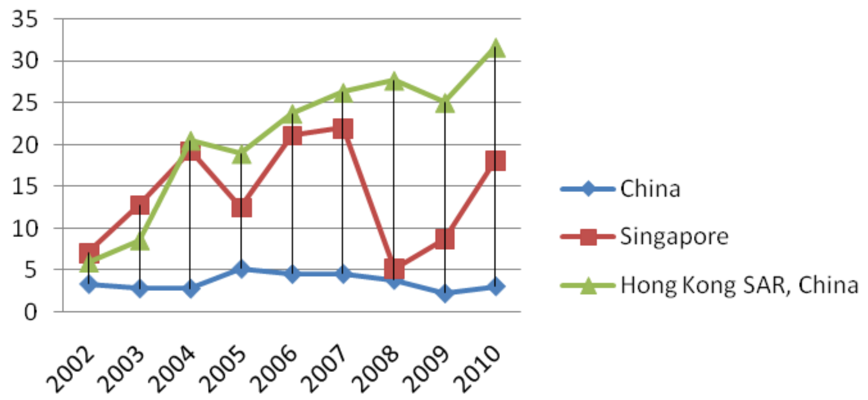
From table 2.5 we could see the scale of the financial center of Shanghai. The total value added and financial industry value added in the absolute value are increasing, but the proportion of the value added of GDP and the financial sector value added of the total value added decreased from 31.4% in 2000 to 21.9% in 2010. This indicates the weight of contribution in the financial center and how it decreasing overtime, thus the scale of the financial center has limited expanding potential. The scale of finance is one of the indicators of financial power. The more quotas, the greater the power, otherwise, it is not so promising for securing funds within and out of the country.

The financial industry is one of the most important pillar industries which contribute to Shanghai's value added, and it accounted to 31.4%, 23.0% and 21.9% in 2000, 2009 and 2010, respectively. Before 2009, the financial industry was the biggest contributor to Shanghai's GDP value added. Shanghai was thriving in 2010, where it was No.2 in the six pillars by means of the trading and industry.

FDI has a very important impact on the financial market and economics of China. In the past twenty-five years, attractive foreign direct investment was the key strategy for China, like its reform and opening up policy. FDI contributes to the host country's economy which has been one of the more important questions for the MNCs headers. American scholar Cave (1996) promoted the eight contributions of the FDI to the economic development of the host country: improved labor productivity, technology transfer, introduction of new methods, management experience and methods, the domestic market know-how, staff training, international production networks and international market channels. The World Investment Report 1999 concludes the function of FDI: promote capital formation, enhance the ability of technology to improve export competitiveness, create jobs and enhance the skills bases as well as environmental protection (UN, 1999).

Figure 2.7 illustrates that China's FDI has a huge difference to Hong Kong and Singapore, and the difference is getting bigger. There are a lot of reasons on why one should respond to that. Due to the irreplaceable role of FDI, the Chinese government should take some measures to encourage FDI its employment.

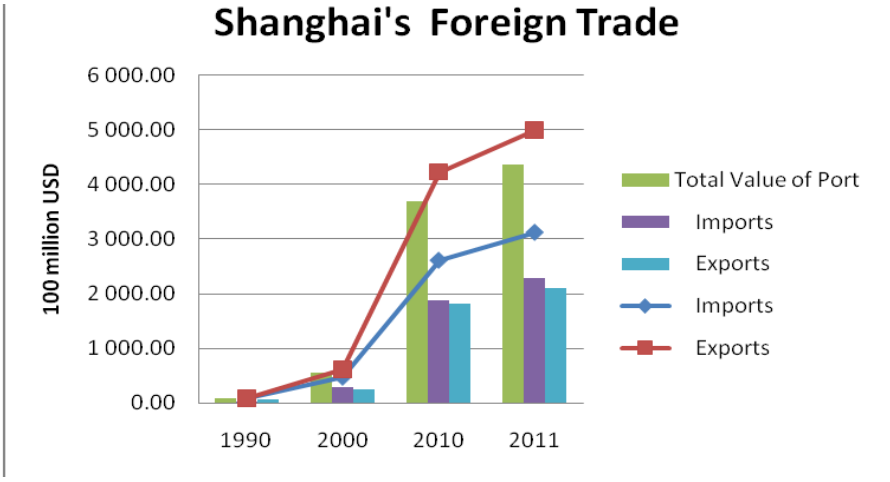
FIGURE 2.7 FDI INFLOWS OF GDP%



Source: Data from World Bank

In Shanghai's financial aspect, through twenty years of hard work, in the end Shanghai became the nation’s financial center. Shanghai's financial service function and position enhanced significantly. Deposits into financial institution and the loan scale have grown rapidly, the financial market financing function has continually enhanced, and the insurance industry developed steadily. The proportion of the National inter-bank bond market, the ability of enterprise to raise capital, and the financial value added has improved a lot. All of these factors play an essential role for Shanghai by overcoming the impact of the financial crisis, and by maintaining steady and rapid develop.

FIGURE 2.8 SHANGHAI'S FOREIGN TRADE IN MAIN YEARS



Sources: Shanghai Statistic Yearbook 2012

International trade plays an essential role to the economic growth and in the raising of funds and capital. A trade center is a solid base and which is a driven force for the financial center, it serves as a pivot for information, funds, and capital flows which are gathered and spread throughout. Figure 2.8 shows the international trade of Shanghai and how it has had a significant increment from 1990 to 2011. Although foreign trade has shrunk in recently years, the absolute values kept its increase and maintained its status in a relatively high level.

The scale of Shanghai's financial market transactions has continually increased, and its global ranking has enhanced steadily. We could see the financial market's overall performance and ranking has been better than before. Total volume trading in the Shanghai Stock Market is second to the Chicago Mercantile Exchange Holdings ranked second in the global security market.

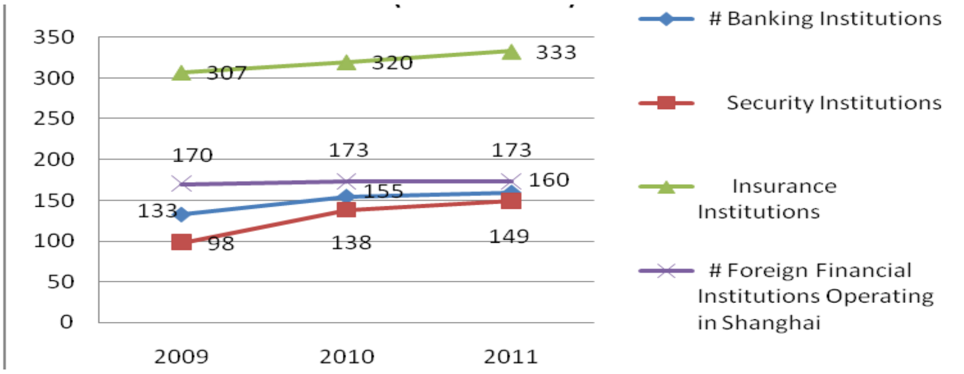
Total volume trading of the Shanghai stock market ranked third in the global market, and increased 4 ranks since 2008. The gold market has performed outstandingly, in 2009 the total gold turnover reached 1,101,063 million Yuan, the annual growth rate has been 22.62%, and moreover, in 2011, the turnover of gold has had a breakthrough of 4,441.23 billion Yuan, fourfold than 2009. The diamond turnover increased threefold in 2011 compared to 2009, which reached 4,707 million Yuan.

The total Shanghai financial derivative market has been ranked the first in the world market in 2009.

2.4.1.1 Financial Institution Agglomeration

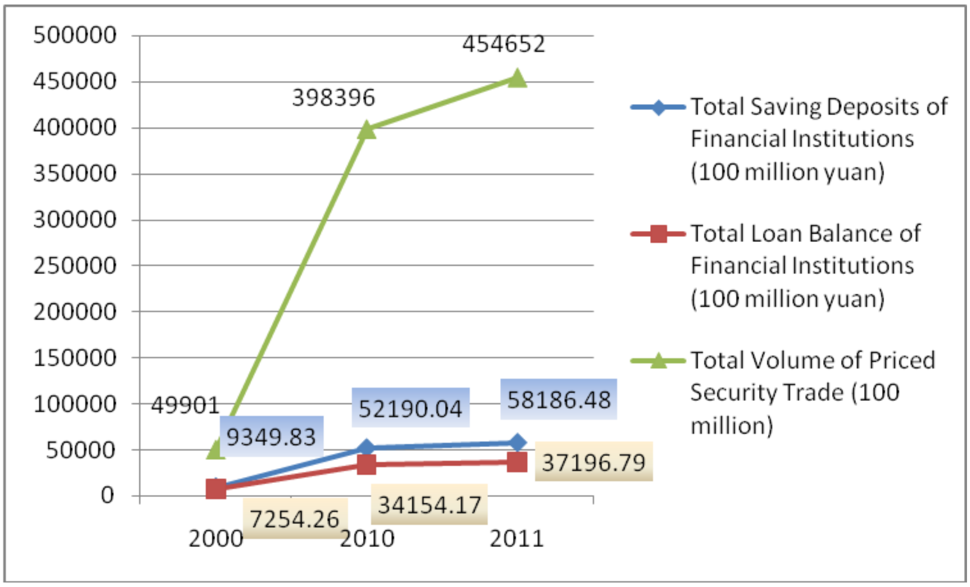
Figure 2.9 reflects the agglomeration of Shanghai's financial institutions. The total financial institutions attained 910 in 2010, increasing to 12.7% compared to 2009, and attained 1,048 in 2011. The banking institution comprises of 140, security 138, and insurance has 320, and moreover, the number of institutions in the financial sector has increased compared to 2009. The total number of financial institutions in Shanghai has increased from 794 in 2009 to 1,048 in 2011, a 32.0% increase, in which the security institutions increased by 52% from 98 in 2009, to 149 in 2011. The banking institution has increased by 20.3%, and the number of insurance institutions increased by 25 and reached to 160 by 2011. The least expansion was in the foreign financial institutions, which only added three new foreign institutions. This apparently shows that Shanghai's attractiveness to international firms is not up to standards. One of the reasons is that regulation for foreign and domestic companies is different, and the cost of opening a new financial institution for foreign firms is higher than that of domestic companies. To a certain extent this reflects an unfair business environment.

FIGURE 2.9: QUANTITY OF FINANCIAL INSTITUTIONS OF SHANGHAI (2009-2011)



Sources: Data from Shanghai Statistic Yearbook 2011

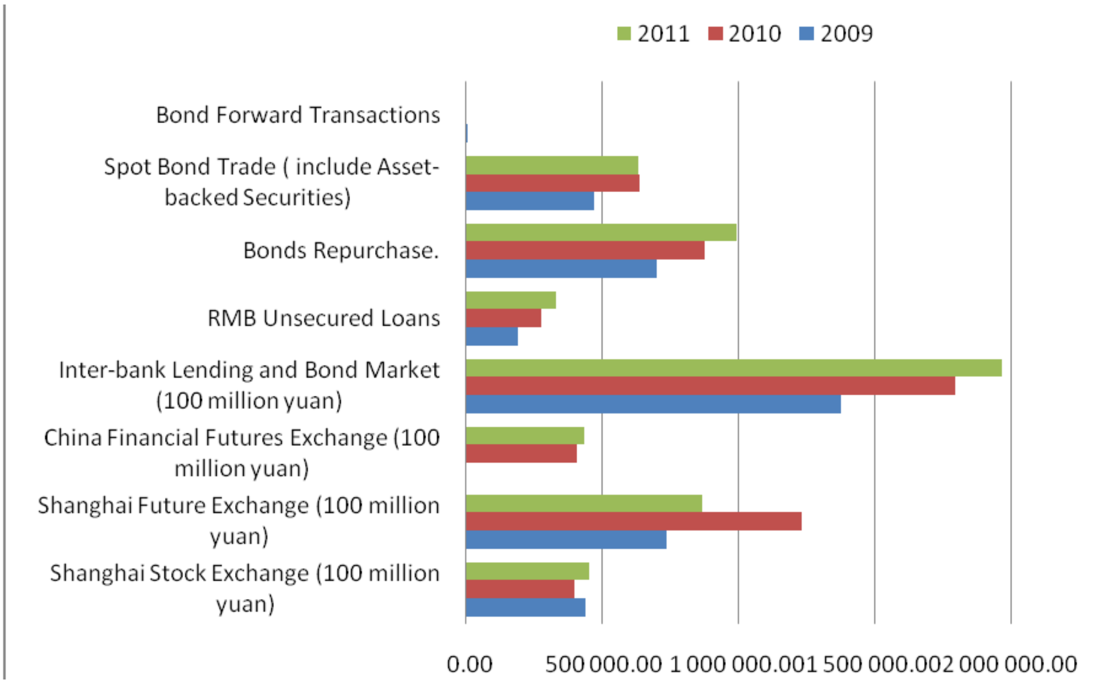
FIGURE 2.10: FINANCE AND INSURANCE INDICATORS IN MAIN YEARS



Shanghai statistic Yearbook 2012

Figure 2.10 illustrates the main indicators of development in the financial sector. Total savings deposit of domestic and foreign institutions attained 4,472,027 million Yuan, and the annual growth rate at 25.39%, in addition to the 8% increase in the speed of growth rate. Newly added domestic and foreign savings deposits reached 901,088 million Yuan, for which the added amount is equal to 375,856 million Yuan. The loan balance of domestic and foreign institutions is 2,968,410 million Yuan, an increased rate of 22.92%. Financial institutions and enterprises financed in the Shanghai Stock exchange market is 386,786 million Yuan, and the annual growth rate is 17.39%. The number of stocks has reached 237,560 in 2011 which demonstrates the big vitality of stock market. Equity financing reached 334,315 million Yuan, which had a huge growth in rate, almost reaching 50%. Shanghai enterprises involved in direct financing is 193,230 million Yuan, which is more than 1.5 times than last year. Insurance market performance is also, quite impressive considering how the premium of primary income reached to 75,311 million Yuan by the end of 2011, which was more than five times of an increase compared to 2009.

FIGURE 2.11 DEAL STATISTICS OF MAIN FINANCIAL MARKET (2009-2011)



From the deal turnover in figure 2.11, we could see the financial market size and scale. The Shanghai Stock Exchange Market is the strongest stock market in China; the turnover is number 1 in mainland China, and until 2011 the turnover of the Shanghai stock exchange has attained 454,651.56 100 million Yuan. The Shanghai Stock Exchange placed 6th in the top 20 in 2012 for trade value and market capitalization in the world (Relbanks, 2011).

The Shanghai Future Exchange in 2010 was at its peak, although there was a slight decline, it still kept a big turnover. Total gold turnover increased from 11.03 trillion yuan to 44.41 trillion yuan, keeping the first gold trade position in the world. The diamond turnover increased from 1,521 in 2009 to 4,707 million USD in 2011.

2.4.2 Financial Industry Overview: Shanghai Is the National Financial and Economic Centre

In this section, first we will compare Shanghai's financial market with other potential cities within China. Since China's Economy has grown rapidly, many cities which developed fast proposed to develop financial centers within China, for that reason competition spread throughout various cities in China. For example, Beijing is the capital city of China and Shenzhen, one of the coastal and rapidly developed trade cities; in addition to many other major cities and big provinces in China. Therefore, it is necessary to have a lateral comparison between Shanghai and other potential cities within China.

Shanghai is far below the average level of the national financial center in relation to employed persons in the financial system to all locally employed persons and also to the yearly growth rate of the number of employed persons in the financial system.

2.4.2.1 National Comparative Study

A comparative study and its results regarding the banking development status of China's financial city-centers suggests that Shanghai has some edge in banking development, with its balance development. In terms of local bank businesses, Shanghai's deposit balances is more than 5 trillion Yuan and has more than 3 trillion Yuan loan balances, which ranks 2nd in China, which is right behind Beijing. Shanghai has more than 2,000 bank outlets; it has a considerable advantage in the number of local business institutions of foreign-funded banks.

By the end of 2010, the number reached 152, which was even more than Hong Kong who had 135 foreign-funded banks. The drawback of the banking sector is on the total of assets of the local commercial bank of legal representative. Beijing is far more than Shanghai, almost fourfold. One of the important reasons is that Beijing is the capital city of China, and the political, cultural, and economic center. China's five biggest state-owned banks have their headquarters located in Beijing, and thus the scale of assets of the local commercial bank of legal representative towers above other financial city-centers. In addition, by the end of 2011, New York's scale of assets of local commercial bank of legal representatives is more than 5.1 trillion USD, which is the same level of Beijing, although much higher than Shanghai (CDI, 2012).

2.4.2.2 Comparative Study on Securities Market

The number of local securities corporations is led by Beijing (18), Shenzhen (16) and Shanghai (15). In comparison, Hong Kong has 431 licensed corporations participating in the stock exchange. The gross asset value of local securities corporations of Shanghai is more than 250 billion RMB, which clearly has an unyielding edge. The gross broking volume of local securities corporations of Shanghai, Shenzhen and Beijing are all more than 1,500 billion RMB, and in the leading position. Referring to this indicator, Hong Kong in 2010 accrued 1,710 billion HK$, so the National financial centers in mainland China and Hong Kong are shoulder to shoulder.

Additionally, Shanghai has a strong advantage in terms of the number of business networks of local securities corporations. The number of branches of securities corporations in Shanghai has reached 467 units by the end of 2010. The second ranking city is Beijing, which is only half of Shanghai. However, in terms of proportion of aggregate domestic stock financing value to GDP, in 2010 Beijing was 67.81% higher than other cities, due to the big state-owned enterprises always having their headquarters in Beijing; and when they go to IPO, the stock financing value is large.

2.4.2.3 Comparative Study on Insurance Market

The Shanghai local Insurance Corporation is far more than other region financial cities. It has 35 units of local insurance corporations and places 2nd in China, just behind Beijing at 40 units. However, the asset value of the local Insurance Corporation between these two cities has a big gap. Beijing has highlighted more than 2,700 billion RMB in 2010, while Shanghai was just around one-third of Beijing, at only 900 billion RMB.

In terms of premium income Shanghai exceeded by 80 billion Yuan and ranked second following Beijing which has 996.46 billion RMB—however, there is still a big gap if compared to Hong Kong who had a premium income of 191.2 billion HK$ in 2010 which is about 1.5 times of Beijing. Shanghai and Beijing are far-and-away leaders in terms of local insurance compensation payout; with close to 20 billion Yuan in 2010, which was more than two times than that of other cities. Insurance penetration is one important indicator with regards to the development level of the local insurance market.

In 2010, Shanghai's insurance penetration was 4.8% less than 6.85% of Beijing, and only ranked fourth in China. Insurance density is another important indicator for insurance markets which subsequently reflect the position of insurance to a country's economy, as well as the development level of the insurance in the country. Insurance density is the average insurance premium according to the total population in the country. Shanghai and Beijing have the obvious edge, whose insurance density well above 3,000 Yuan per person, whereas Beijing is far more than Shanghai. Shanghai’s insurance density, and penetration are below average, but the asset value of local insurance corporations has lagged tremendously compared to the average level in other cities (CDI, 2012).

After this comparative study within China, we could conclude that Shanghai is indeed a leading national financial center in China withstanding competition from other potential financial cities such as the likes of Beijing.

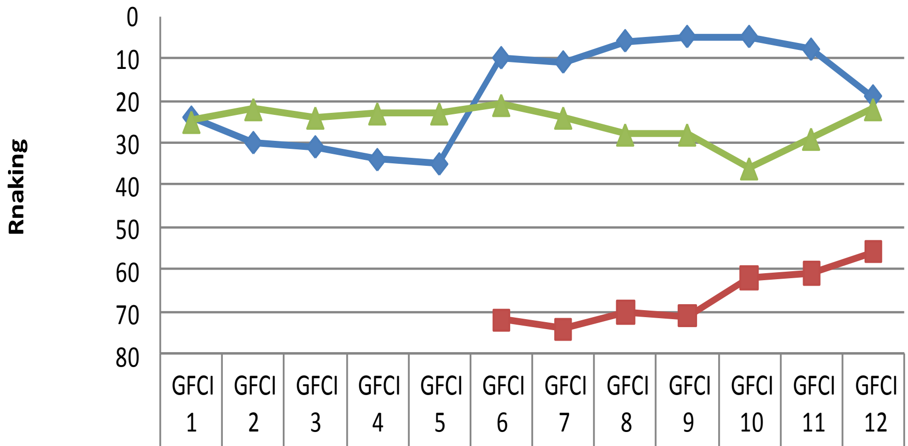
CHAPTER 3

COMPARATIVE ANALYSIS OF EMERGING FINANCIAL CENTERS: SHANGHAI, ISTANBUL AND DUABI

3.1 The Potential Power of Three Cities Overview

Figure 3.1 exhibits the GFCI ranking for Shanghai, Dubai and Istanbul. It illustrates that Shanghai and Dubai are ranked remarkably higher than Istanbul. Before 2009 Dubai was above Shanghai, after that Shanghai improved its position rapidly and overtook Dubai. It was even among the top 10 for 5 years, but there was a big fluctuation, by the end of 2012 and Shanghai had a sharp fall to the rank 19th. Dubai looks steadier and has small fluctuations , it merely moves between the ranges 20 and 30. Although Istanbul entered the list in GFCI 6 (2009), later than the other cities, it displays a strong and significant increasing trend.

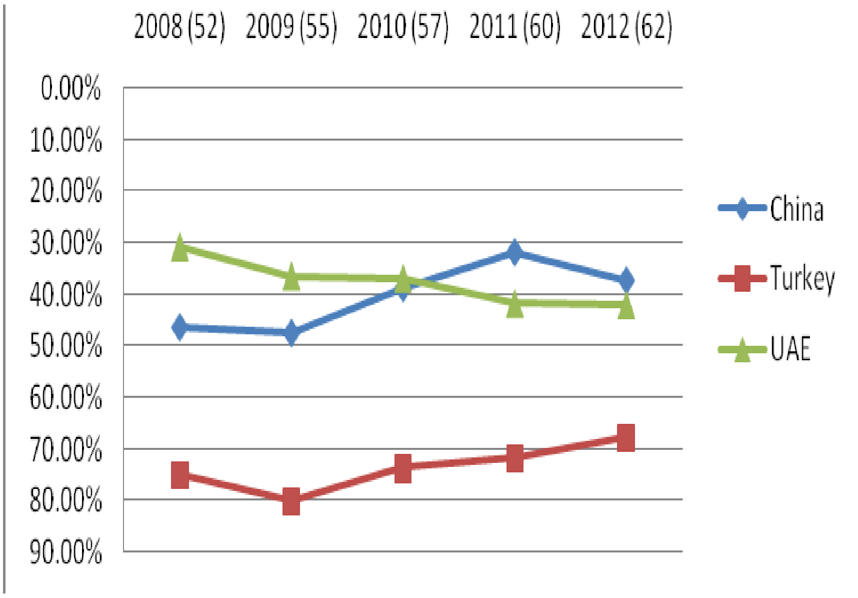
FIGURE 3.1 GFCI RANKING OF SHANGHAI, ISTANBUL AND DUBAI



	GFCI 1	GFCI 2	GFCI 3	GFCI 4	GFCI 5	GFCI 6	GFCI 7	GFCI 8	GFCI 9	GFCI 10	GFCI 11	GFCI 12
Shanghai	24	30	31	34	35	10	11	6	5	5	8	19
Istanbul						72	74	70	71	62	61	56
Dubai	25	22	24	23	23	21	24	28	28	36	29	22

WEF's FDR has represented the similar positions of China, Turkey, and UAE in terms of financial development. Figure 3.2 shows the relative positions of the three countries from 2008-12, because the total numbers increase annually, the relative position is a more accurate indicator to reflect the situation . Figure 3.2 illustrates that China and UAE are in a similar position and are both ahead of Turkey; however, Turkey has a significant increasing trend from 2008 to date.

Figure 3.2 WEF FDR RELATIVE RANKING OF CHINA, UAE, AND TURKEY 2008-2012



Source: The Financial Development Report (2008-2012)

TABLE 3.1 WEF GLOBAL COMPETITIVENESS REPORT 2011-2012

Country or Area	overall index		Sub indexes					
			Basic requirements		Efficiency enhancers		Innovation and sophistication factors	
	Rank	Score	Rank	Score	Rank	Score	Rank	Score
China	26	4.9	30	5.33	26	4.7	31	4.15
UAE	27	4.89	10	5.84	25	4.78	27	4.43
Turkey	59	4.28	64	4.61	52	4.22	58	3.62

Table 3.1 shows the global competitiveness of China, Turkey and UAE, and their overall ranks are 26^{th}, 27^{th} and 59^{th} respectively. China's and UAE's scores have a slight difference of 0.01. It depicts that China and UAE are at similar levels in overall power both of which are quite ahead of Turkey. On the other hand, in terms of the basic requirements sub-index, which includes institutions, infrastructure, macroeconomic environment and health and primary education, there is a significant difference between China and UAE.

If we look the at details, we see that institutions and infrastructure cause the basic requirements rank to lag behind.

In sum, from those three official reports, we could reach a general conclusion that Shanghai, China, Dubai and UAE are at the similar phases of development, all of which are more competitive than Istanbul, but Istanbul has a powerful increasing trend and has been improving its financial competitiveness.

The following part will compare these three emerging financial centers by the instrumental factors which were developed by the author in Chapter 1.

3.2 Comparative Analysis Study by Instrumental Factors

3.2.1 The Economic Base of Three Cities

TABLE 3.2 MAIN ECONOMIC INDICATORS FOR SHANGHAI, ISTANBUL AND DUBAI 2010

	Population (Millions)	GDP (Billions, PPP)	GDP Growth Rate (%)	GDP per Capital (PPP)	Unemployment (%)	Inflation (%)	FDI Inflow (Millions)	Public Debt (% of GDP)
Shanghai	23.03	$272.48	10.3	$7,518.7	4.3	3.326	$105,735.0	33.8
Istanbul	13.5	$188.2	8.2	$13,463.7	11.7	8.566	$9,071.0	42.2
Dubai	1.9	$79.9	2.8	$48,820.9	2.4	0.897	$3,948.3	21.0

World Bank; Shanghai statistic yearbook 2010;

Table 3.2 reflects the macroeconomic environments of Shanghai, Istanbul and Dubai in 2010. In terms of GDP growth, Shanghai is the clear leader among the three cities. Meanwhile Istanbul is also experiencing significant growth and its rank in recent years was higher than Shanghai. Dubai's GDP growth rates are much lower compared to Shanghai and Istanbul. However, it should be kept in mind that the GDP growth rate is likely to overstate the growth advantage of Shanghai and Istanbul compared to other established IFCs.

Primarily because there is a large gap between Shanghai and Istanbul and other highly developed cities, such as high income cities as Dubai. Looking at the GDP per capita, we could see the real difference among cities. As a matter of fact, there is still room for them to grow rapidly in time and attain the similar level with richer economies. So, the GDP growth rate cannot reflect the panoramic view, but it gives away a certain extent to forecast the long term tendency.

However, even though Shanghai's and Istanbul's current levels of GDP per capita lay well behind of Dubai and other developed countries, they can still sustain high rates of growth in the foreseeable future. . High inflation is one of the primary disadvantages of Istanbul. Despite the fact that it is already under control in recent years, it still high to in comparison to other emerging cities. Shanghai has an absolute advantage in attracting FDI, it is almost tenfold higher than Dubai and 26 times than Istanbul. The positive impact of FDI on the development of financial sector has been discussed before. Another obstacle for Istanbul is the high ratio of public debt to GDP.

3.2.2 Human Capital

3.2.2.1 Skilled Labor Force and Human Capital

Shanghai's financial sector is currently suffering a talent shortage; it has been an extreme bottleneck for Shanghai's development as a financial center. Talent shortage directly and negatively affects Shanghai's overseas capital investment, the ability of financial innovation, the supervision of the increasingly complicated and its globalized and highly risky financial industry (ChinaStakes, 2008).

Shanghai's local government has taken many measures to attract financial talent, such as "Thousands of talent plans" and taxes subsidy and many other favorable policies in order to attract foreigners or domestic professional elites. Such actions gained initial success; that is to say the number of employees in financial sector has increased significantly, but it is still insufficient.

As for now, the overall performance of the financial sector in Shanghai still falls behind due to the fact that the required level of financial talents is still not reached compared to other international financial centers. The main reason is that the city lacks senior and mid-level managers and talented individuals familiar with new financial products and services. It is forecasted that the number of financial jobs in the Shanghai will increase by 39.13% over the next five years, from 230,000 to 320,000.

In New York's Wall Street and the City, London's financial hub, there are 400,000 and 300,000 financial practitioners, respectively; however, there are only 100,000 specialists working in Shanghai. The Chairman of the Chinese Banking Regulatory Commission pointed out that although the quantity of financial staff has increased, they still have a long way to go in many aspects; such as the quality of professional talents, the degree of globalization and employee dedication (ChinaStakes, 2008).

Although there are relatively enough graduates from the economics, finance, management and other finance related departments, the graduates cannot play a direct role in increasing the financial talents due to the fact that educational level of finance sector in China could still not catch the latest financial developments and the financial service requirements. These graduates need professional training to qualify in financial service after graduation.

Moreover, although not only Shanghai but also Chinese government has taken many actions to improve the human resources environment to attract the talented, most of the talents are scholars without experience in operation and they are not competent enough in the practical financial sector. There are enough talents in Hong Kong SAR; however, the survey shows that most of them do not want to work in Shanghai; one of the most important reasons is that tax levels in Shanghai are much higher than Hong Kong. Some foreigners prefer to live in Hong Kong despite the higher living cost compared to Shanghai which has much lower living cost, just because to evade higher income tax rates. According to Chinese Tax Law, if residents stay in China mainland over 183 days, they need to pay an income tax, otherwise they don't.

One of the most important advantages of Turkey is the adequate level of skilled labor force supply, especially in the field of retail banking. Skilled labor force of Turkey is highly competitive when compared to that of the region, and the IT structure and level are at global levels. The Istanbul IFC feasibility study 2009 argued that, as of 2009 Turkey's workforce is around 23.5 million, and it has ample potential for labor force since 40% of its total population is less than 18 years old, which accounts for approximately 30 million people.

Therefore, the potential of retain home-growth talent is considerably high. In addition, Turkey has skilled labor together with lower wage rates, and located in the center of time zones it has accessibility advantage thanks to its geographical location, thusshould have a strong vision (Consultancy, 2009). However, there are many expatriates outside the country, and they should find a way to bring them back. For example, the country has a remarkably large number of highly qualified labor force working in finance sectors in London and NY. Comparing with the industry volume, the HR profile of the staff employed in industry is very high. The senior and lower levels of management in local banks acquired by foreign banks remained 90% the same.

Although Turkey's labor force has some advantages, there is shortage in financially skilled talents especially in the middle and back office operations. Employees in financial sector in Turkey are usually occupied with front-office operations, and the country lacks sufficiently skilled vocational school graduates for back office functions. Capital market professionals are supervised and it is required by Capital Markets Board that they pass a number of exams to obtain a license to qualify in most of the fields of finance in Turkey. Turkey offers improving levels of business education, including top quality MBA programs, one of which was selected as "one of the best MBA programs in Europe" by Business Week and Frankfurter Allgemeine (Consultancy, 2009).

The structure of the financial sector still concentrates on the university level, that is, the number of post-graduates and higher level talents is relatively low with a rate of less than 10%. For instance, among the banking employees in Turkey, 70% of the labor force employed in banks is college graduates, while only 6% of that has a master's degree. There is a lack of depth, very few lawyers with international connectivity are working for 'recognizable' firms. The Big 4 accountancy firms have a presence, but offices are small and the employees don't have adequate specialist expertise. There is an opportunity to hire high skilled and experienced people from the market or with Ph.D on part-time or full-time basis (at least 10 years) since at present it is still hard to attract those people due to the limited salaries offered.

The best financial sector professionals are employed in Dubai thanks to the power of money, but Shanghai and Istanbul cannot offer the same level of high salaries and zero tax. Professionals expatriate for the luxurious life in Dubai. However, Dubai has its own problems. It has shortage of local skilled labor, as the majority of talents are foreigners. In Dubai the female participation in labor force is very low, they are discouraged to work because of the culture and religion. While only 24% of the females are active in the workforce in Dubai, this number is approximately 50% in Turkey. Labor force of Dubai is the hidden obstacle against the long-term development. Dubai's local labor pool is very small, and it relies on expatriate to support its financial center. While it is possible to 'buy in' skill sets, this is unlikely to be sustainable, and may set Dubai at a cost disadvantage in the future.

TABLE 3.3 HDI 2010

HDI Rank	Country	Level of HD	Human Development Index 2010							
			HDI score	Life expectancy at birth	Expected years of schooling	Mean years of schooling (years)	Education index	Income index	Health Index	Gender Inequality Index
30	UAE	Very High HD	0.846	76.5	13.3	9.3	0.741	0.916	0.892	0.234
92	TR	High HD	0.699	74	11.8	6.5	0.583	0.689	0.851	0.443
101	CHA	Medium HD	0.687	73.5	11.6	7.5	0.623	0.618	0.843	0.209

Table 3.3 represents the human development index, which is one of the well-known indicators to measure the human capital at the country level. UAE is in the leading level among the three countries, its world rank is 30 and HDI is 0.846. It has a very high level of human development, Turkey is in the middle, but there is large gap between Turkey's and UAE's ranks and the HDI scores. Turkey's rank is 92 and HDI score is 0.699. China is only at the medium level of HD. The difference with Turkey is not very large. In addition, table 3.3 illustrates the education, income, and health indexes. They are the important HDI aspects; the results are similar with the ones before.

However, a better city performance than the country level is one of the important aspects we could not ignore. From the EIU global city competitiveness index "human capital" result, we could see Dubai is in the leader position among the three, even among the 120 economies, its rank is 37th. Shanghai at the middle stage, its rank is just the medium, the 60th. Istanbul's score is much lower with only 48.5, thus it still has much room to improve. It is normal that contradiction exists to a certain extent between the country and city levels, for the objects being investigated , the cover range and the population are different and many other reasons.

TABLE 3.4 HUMAN CAPITAL RANK FOR SHANGHAI, ISTANBUL AND DUBAI IN EIU 2012

Human Capital	Shanghai	Istanbul	Dubai
Score /100	63.7	48.5	69.1
Rank/ 120	60th	n/a	37th

Source: The Economist Intelligence Unit Limited 2012

3.2.2.2 Quality of Life

Quality of life is a considerable element for the individual and companies. Quality of life index is defined as the satisfaction with life; that is, "a person's sense of well-being that stems from satisfaction or dissatisfaction with the areas of life that are important to him/her."

The table 3.4 shows the overall scores for Shanghai, Istanbul and Dubai which are -17, 66.1 and 175.3, respectively. There are large gaps between these three cities. As a matter of fact, Shanghai is the worst one, the score is even minus; while Dubai is the best one, nearly three times higher than Istanbul.

Dubai has emerged as a regional hub in the Gulf region over the last two decades. It aims to be an international city, and is rapidly developing as a tourist, business and leisure destination. It has world leading shopping, hotels and restaurants, but limited historical or cultural heritage. Its harsh climate is also a restriction for much of the year. Dubai has the lowest level of costs and is the safest city compared to Shanghai and Istanbul. The purchasing power of Dubai is very high, there is low pollution, low traffic commute time and the price houses are reasonable.

Shanghai's overall score is only -17, the level is too low in comparison with the other two cities. The purchasing power is quite low; the health care is at the lowest level among the three cities. The most unfavorable factor is the high estate prices; the ratio of house price to income is 30.08, however, in Istanbul and Dubai the same ratio is merely 7.14 and 4.52 respectively. This means house prices are much higher in Shanghai than those in Dubai and Istanbul. Therefore, the cost of living is much higher in Shanghai whether you rent a house or buy a house. The level of pollution in Shanghai is not acceptable, either.

As for Istanbul, safety is a shortcoming compared to Shanghai and Dubai, because it is a highly important factor when individuals or companies opt for a place. Another drawback of Istanbul is the traffic problem. There are very serious traffic jams, the public transportation is not developed sufficiently. For instance, most of the buses are very old and out of date, expiration takes too long. The public buses commute rarely which makes it hard to catch them, besides, the duration of commute is too long. There is not much order in bus stops, the private buses could stop anywhere even in the middle of the road, this is one of the reasons that cause traffic jam.

More seriously, there are not any clear signs at the bus stops and information tables about how many stops there are, where the bus will pass by or even where it is could not be found. It is very inconvenient for foreigners, or even for the citizens who are not familiar with the place. Therefore, for further development Turkish government has to engage in every effort to improve transportation facilities.

TABLE 3.5 QUALITY OF LIFE SCORE OF SHANGHAI, ISTANBUL AND DUBAI (2012)

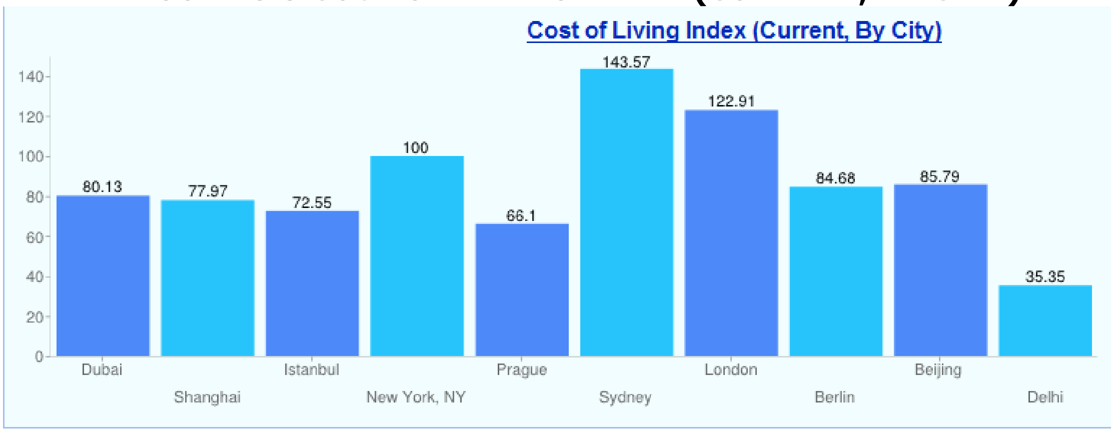
City, country	Shanghai	Istanbul	Dubai
Purchasing Power Index	43.81	60.73	114.4
Safety Index	56.25	42.88	75.34
Health Care Index	34.72	79.51	69.86
Consumer Price Index	77.93	72.91	80.37
House Price to Income Ratio	30.08	7.14	4.52
Traffic Commute Time Index	34.33	78.22	25
Pollution Index	92.45	63.57	57.4
Total score	-17	66.1	175.83

Source: Quality of life index city comparison

3.2.2.3 Cost of Living Index

You would need around 21,626.78¥ (3,462.33$) in Shanghai or 4,340.66$ in Dubai to maintain the same standard of life that you can have with 2,800.00$ in Istanbul, (assuming you rent in three cities).

FIGURE 3.3 COST OF LIVING INDEX (CURRENT, BY CITY)



Source: NUMBEO. 2012

From the cost of living index in figure 3.3, we may see that Shanghai, Istanbul and Dubai's cost of living levels compared to other popular cities. In this index, we use New York as a 100 base, and other cities are all compared with NY, for example, Dubai is 80.13. This means that in Dubai if you want to enjoy the same standard of living of NY, the cost is 80.13, which is less than NY. In London the index is 122.91. This means in London an individual must pay 22.91% more to acquire the same level of life in NY which shows the cost of living in London is higher than New York. Therefore, cost of living in Istanbul is the least, in Dubai it is the most, and in Shanghai it is little less than that in Dubai.

3.2.2.4 Culture and Language

Social and cultural environment is one of the important factors determining a place's livability, which impacts the vibrancy of a city. As EIU city report wrote: "Cultural vibrancy of the city has an additional benefit: the potential to develop the creative industries' cluster, which in turn generates greater economic benefits through the multiplier effect."

Chinese culture is diligent and thrifty; the workforce is willing to work longer hours to create more social wealth. As the huge population ends up in a harsh competition in the society, people must strive hard to make a living. The efficiency is also one of the crucial qualities for work. Overtime work in most companies is a common thing, sometimes even during holidays or important festivals many workers keep working. Another characteristics of China is that Chinese people are very organized and they prefer to well organize all things.

Being at the crossroad and the cradle of civilizations, Istanbul is a unique city in many respects. It has been the capital city of three important empires, namely Romans, Eastern Romans (Byzantine) and the Ottomans. Located at the crossing point between two continents, Europe and Asia, Istanbul is also the seat of the Patriarch, the spiritual leader of the Eastern Orthodox Church. Besides Muslim majority, there are Christian, and Jewish minority settlers in the city. The Hagia Sophia and the Blue Mosque are just two of the most important historical monuments among the many others (eNewsletter, 2008).

UAE does not possess such an old and deep history and civilization heritage like Turkey and China. There are some common points for Dubai and Istanbul. Most of the people are Muslim, they prefer spending their free time with friends, sharing food and tea no matter how busy and hardworking they are. They are used to having their private life separate from work. So they do not have a strong time perception. However, this does not necessarily mean they do everything ineffectively or worse. In opposite, thanks to their culture, their system and procedures are more effective than those in China in many aspects, thus this could make up for the differences between the countries and cultures.

In terms of culture, we cite the index from EIU, the indicator of Social and Cultural character which takes into consideration the freedom of expression and human rights, openness and diversity, presence of crime in the society and cultural vibrancy to measure the social and cultural performance. Human capital city score illustrates that Istanbul’s cultural and social character is more attractive than Shanghai and Dubai, the rank in EIU is 55th in 120.

As for the language indicator, Dubai has the best performance. Dubai's official language is English. Shanghai and Istanbul in terms of the level of fluency in English lag behind Dubai.

3.2.2.5 Education of English and Culture

UAE government has extended instruction in English, they have hired approximately 500 native English speakers to teach in public schools. Problems with English teaching at government schools in general have delayed pupils' admission to the universities where English is the primary language of instruction. UAE has also lengthened the school day to come closer to international standards and is also investing heavily on professional development of principals and teachers, as well as working towards teacher certification. In 2009, Abu Dhabi Education Council announced that it would replace 100 old school buildings with new and environmentally sound designs over the next decade.

Chinese government also recognizes the importance of language, so the English teaching starts even from kindergarten level until the post gradual level. The government also hires native English speakers to teach English, but there is large variation in China. The quality of education varies remarkably between different regions and cities.

Turkish government has devised elaborate strategic plans to improve the education of English due to the criticism that foreign languages are not taught well in the country. In the "STRATEGY AND ACTION PLAN FOR ISTANBUL AS AN INTERNATIONAL FINANCIAL CENTER" see figure 3.4. The plan focuses on wide extensions, from the basic education level, primary and middle school, to higher education level, university and graduate school. Furthermore, Turkish government plans to spend an estimated TL 1.5 billion and run a five years project that aims to 'hire 40,000 native English speakers as guest teachers' to lay solid foundation for the English teaching. "English cafés" will be opened, popular cartoons and children's shows will be aired in

English with Turkish subtitles and foreign language education sets will be distributed to students' (Today's Zaman, 2011).

FIGURE 3.4 TURISH STRATEGIES AND ACTION PLAN FOR ISTANBUL AS AN INTERNATIONAL FINANCIAL CENTER

55	Enhancing foreign language education at primary and secondary schooling	Ministry of National Education (R) YOK (C)	2010-2011 Academic Year - Continuous	Practical knowledge of English to the extent needed at the financial center shall be provided intensively at primary and secondary schooling, and the existing content of foreign language courses shall be revised.
56	Enhancing foreign language education at higher education	YOK (R) Ministry of National Education (C)	2010-2011 Academic Year - Continuous	Professional knowledge of English to the extent needed at the financial center shall be provided at university level, and options shall be considered to make foreign language competence at a certain level mandatory for graduation.

With the project, a total of 40,000 English teachers will arrive in Turkey over the next four years and activities will be held during weekends and the summer vacations with the participation of Turkish teachers of English and native English-speaking teachers. In English classes, native English-speaking teachers will accompany Turkish teachers and take part in extra curricular activities. The native teachers will also hold speaking classes for both the students and the Turkish teachers of English.

3.2.3 Business Environment

3.2.3.1 Infrastructure

Shanghai government infuses huge amount of money to develop the basic hard infrastructure of Shanghai, the details of which we already stated in the previous chapter.

Istanbul has sufficient level of support services, such as health services, education and cultural background which are at global levels. However, the only problem is the traffic issue. Within the last decade, especially in the last 5 years, Turkish government made affordable and serious investments on highways, underground and maritime lines. Information technology, telecommunication and air access services are strengths whereas road transportation is still the weakness of Istanbul. In order to improve the traffic problem, TR government has planned to invest minimum 16 billion USD.

TABLE 3.6 INFRASTRUCTURES RANKING FROM TTC 2011-2012

	China		Turkey		UAE	
	Rank	Score	Rank	Score	Rank	Score
T&T business environment and infrastructure	64	3.8	55	4	9	5.3
Air transport infrastructure	35	4.2	37	4.2	4	5.8
Ground transport infrastructure	59	4	60	4	31	4.9
Tourism infrastructure	95	2.6	54	4.4	22	5.8
ICT infrastructure	73	3.1	59	3.4	18	5.2
Price competitiveness in the T&T industry	24	5.1	108	4.2	4	4.9
WEF Financial Development Index 2012	45	-	43	-	23	-

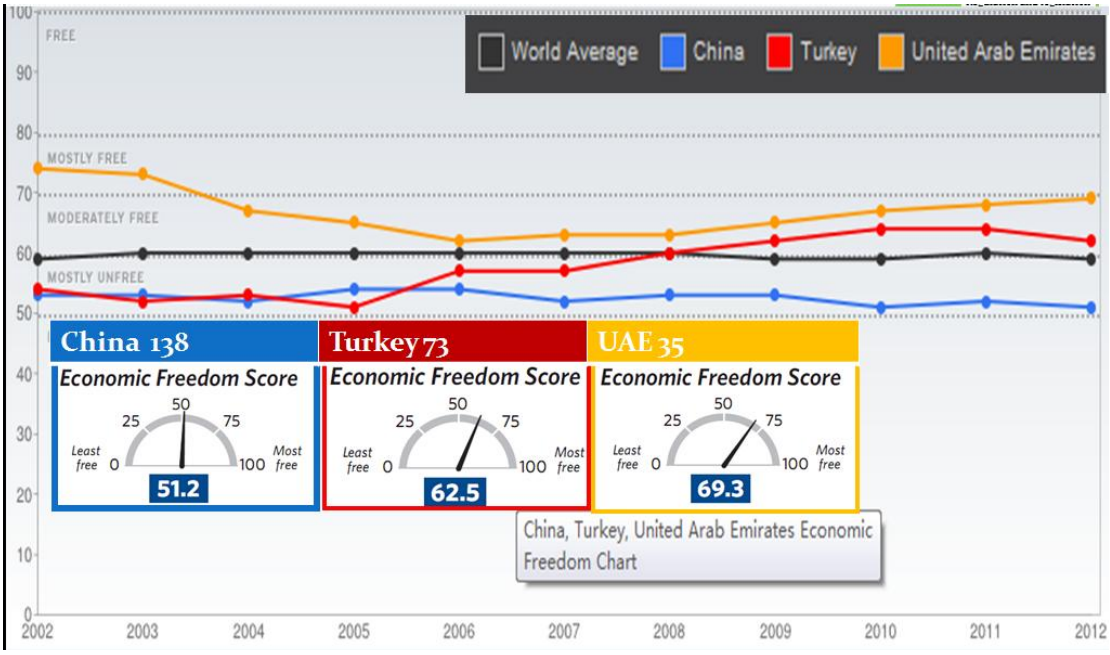
Source: the Travel &Tourism competitiveness Report 2011 © 2011 World Economic Forum

In the infrastructure indicator seen in table 3.6, three cities all have good performance; the government has employed considerable amount of people and invested funds to develop hard infrastructure. However, UAE has the best development level; its rank is 9 out of 139 countries, just behind the highly developed countries. UAE keeps the leading position in all aspects of infrastructure: air transport infrastructure, ground infrastructure, tourism and ICT infrastructure. UAE has high-quality roads and airports infrastructure, Dubai airport is a major airline in the Middle East, and it is the 4th busiest airport in the world in terms of international passenger traffic. Convenient transportation facilities could increase cites' attractiveness. In WEF's FDI ranks the same for three countries.

3.2.3.2 Economic and Financial Freedom

In the figure 3.5 we could see a picture of basic freedoms for three countries. In this case, the country level could represent the city level, because the freedom policies applied within the city are the same with the country. Although regarding some areas of freedom or trade zones, there is more freedom, the overall trend does not tend to change.

FIGURE 3.5 ECONOMIC AND FINANCIAL FREEDOMS



Source: data from heritage foundation. 2012. Figure by author.

Figure 3.5 illustrates the economic freedom in China, Turkey and UAE from 2002 to 2012. The overall economic freedom scores of China, Turkey, and UAE are 51.2, 62.5 and 69.3 out of 100, making their economies the 138th, 73rd, and 35th freest in the 2012 index of 179 economies, respectively. Chinese economic freedom performance is the worst among the three, its overall score is even lower than the global and regional average. Among the Asian-Pacific region's 41 countries, China takes only the 30th place. Chinese government has not made efforts on changing the economic freedom so far.

In contrary, Turkey's economic freedom has experienced significant improvement after the Turkish government engaged in a national project to establish Istanbul as an IFC. Although its overall score is 1.7 points lower than 2011, which is due to the explosive growth in government spending, the financial freedom has a notable improvement. Turkey's overall score is higher than the world average.

In terms of The United Arab Emirates' economic freedom is higher than the world and regional average. Among 17 Middle East/North Africa regions, UAE stands as the 4th clearly leading position. In 2012, there were some improvements in property rights, monetary freedom, and labor freedom so that the overall score was 1.5 points higher than 2011 (Heritage, 2012).

For China the problem is the vulnerable judicial system which is not independent from government, Communist Party intervention and fragile foundations, and if the widespread corruption is not avoided, it will constitute a serious obstruction. Although communist party is composed of a small leading group, it holds the ultimate authority, and makes the final decisions on many aspects of economy and politics. Too much governmental and Party-wise intervention has slowed or stopped to some extent the pace of genuinely liberalizing economic reforms. Chinese government has engaged in expansionary fiscal and monetary interventions in order to impede the reduction of global demand (Heritage, 2012).

Government intervention in the market dynamics has disrupted market efficiency and long-term competitiveness, and it has also been distorting the economy to a certain extent. Chinese government lacks the appropriate political measures and the motivation to restructure the fundamental domestic economic structure. Therefore, adverse conditions and inefficient structure has distorted economic growth and development, and made them depend on exports, public investment and government support extremely.

Excessive dependency on government subsidies and credit control continue to undermine the efficiency and productivity of the state-controlled financial sector. The private investors and companies have more difficulties in participating in the competition and thus take seldom share of the whole economy. The gap between the poor and the rich gets much bigger.

The corruption leads many bureaucracies to collect excessive money which should be used on behalf of society and "table culture" wastes huge amount of resources and society's wealth. That so-called "table culture" is one of most important aspects of Chinese officialdom. After meeting or any activities the officers are invited to a luxurious dinner to have a conversation.

They discuss the problem at hand in the table, usually after drinking and eating.

Turkish economy is one of the most dynamically developing markets in the European region. Although government intervention has still impact on the economy, the private sector is expanding considerably. The banking sector is more independent from the government control and has weathered the financial turmoil well. The regulatory environment has improved and open market policies that encourage global trade and investment have enhanced the competitiveness of Turkey essentially (Heritage, 2012).

The biggest obstacle for Turkey is the inefficient judicial system. The State has overtaken the judicial power and has bad influence on the general judicial order, which hinders judicial fairness. The absence of fairness in regulation and weak judicial system result in corruption inevitably. Chronic fiscal deficits highlight the need to enhance public finance management and restructure public-sector programs (Heritage, 2012).

UAE has an positive trend in improving the economic freedom. Economic restructuring has been underpinned by efforts to strengthen the business climate, boost investment, and foster the emergence of a more vibrant private sector. The generally open trade regime has helped to sustain the momentum for growth while controlling the costs. The UAE aims to be a regional financial hub, and its banking sector has handled the recent financial turmoil comparatively well.

The corruption rate is very low compared to China, Turkey and even the other countries in the region. The weakness of UAE which harms the overall economic freedom is the drawbacks in legal system and the oppressive investment framework. There are still various restrictions on foreign investment, and the political intervention in the judicial system makes it vulnerable despite some progress (Heritage, 2012).

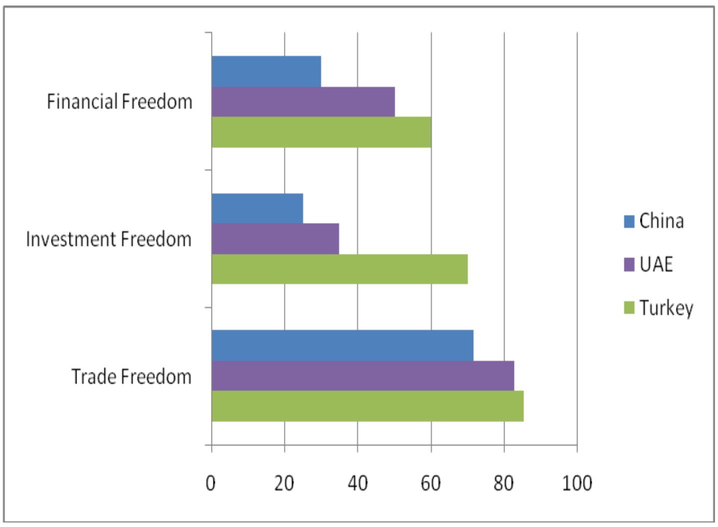
The freedom trend in figure 3.6 shows that freedom in China is more limited. Turkey is getting more open. Even though they have narrowed down the freedom due to the financial crisis lasting from 2011 to 2012, the overall trend is increasing. UAE is getting more and more free in economics. This is an action that the UAE government took to attract in more foreign investment.

FIGURE 3.6 FREEDOM TREND

Source: Heritage foundation, 2012

3.2.3.2.1 Open Market Freedom

FIGURE 3.7 FINANCIAL, INVESTMENT AND TRADE FREEDOM



Source: data from heritage 2012

Looking at the figure 3.7 we could see Turkey has the most freedom in trade, investment and financial sector in 2012. UAE takes the second rank among these three countries; however, in China, apart from a comparable trade freedom, freedom in all other aspects is very limited.

Despite the fact that the trade environment in China is relatively more free, the weighted tariff rate is 4.2%, with layers of non-tariff barriers adding to the cost of trade. The investment freedom is ranked as the 146th out of 179 economies and has only a score of 25, due to the non-transparent and inefficient investment regime. Chinese government has tight control of the financial system and market access. The fact that government holds many rights with its authority causes unfairness to small and private enterprises, because the government has the right to control the direction of the funds flow, lend according to state priorities and favor particular enterprises, which usually turn out to be the large state-owned enterprises.

As for Turkey, the trade weighted average tariff rate is 2.3% which is relatively lower, but non-tariff barriers constrain the freedom to trade. The government takes action to attract foreign investment, but there are still restrictions in a number of sectors. Excessive bureaucracy and frequent changes in the legal and regulatory environment shake the confidence of the investors. The financial system has undergone a rapid transformation with greater transparency and competitiveness.

UAE has a modest trade weighted average tariff rate of 3.7% which is between those of China and Turkey, but lingering non-tariff barriers add to the cost of trade. Only in the "Free Zones" the domestic and foreign investors could be treated without discrimination. The government has some power policies in order to control the economy; for instance, except the free zones, at least 51% of a business must be owned by a UAE national. The state possesses strong controlling power over the companies and investors. However, UAE financial sector provides a full range of services, though the state presence is prevalent. In addition, the capital markets in UAE are open and vibrant (Heritage, 2012).

3.2.3.3 Market Access

In terms of market access, two reports are used to compare the countries. One is "Doing Business (DB)" (Table 3.7) to measure the market access, another is Capital Access Index. "Doing Business" sheds light on 'how easy or difficult for a local entrepreneur to open and run a small to medium-size business when complying with relevant regulations' (IFC&WB, 2012).

TABLE 3.7 EASE OF DOING BUSINESS

2012	China	Turkey	UAE
Ease of doing business rank/**185**	91	71	26
Starting a business (rank)	**151**	**72**	**22**
Procedures (number)	13	6	6
Time (days)	33	6	8
Cost (%of income per capita)	2.1	10.5	6
Minimum capital(% of income per capita)	85.7	7.2	0
Dealing with construction permit (rank)	**181**	**142**	**13**
Procedures (number)	28	20	14
Time (days)	270	180	46
Cost (%of income per capita)	375.3	164.3	9.2
Getting electricity(rank)	**114**	**68**	**7**
Procedures (number)	5	5	4
Time (days)	145	70	40
Cost (%of income per capita)	547	517.9	19.3
Registering property(rank)	**44**	**42**	**12**
Procedures (number)	4	6	2
Time (days)	29	6	10
Cost (%of income per capita)	3.6	3.3	2.3
Getting Credit (rank)	**70**	**83**	**83**
Strength of legal rights index(0-10)	6	4	4
Depth of credit information index(0-6)	4	5	5
Public registry coverage (% if adults)	27.7	23.5	5.9
Private bureau coverage (% of adults)	0	63	31.7
Protecting investor (rank)	**100**	**70**	**128**
Extent of disclosure index(0-10)	10	9	4
Extent of director liability index(0-10)	1	4	7
Ease of shareholder suits index(0-10)	4	4	2
Strength of investor protection index(0-10)	5	5.7	4.3
Paying taxes(rank)	**122**	**80**	**1**
Payments (number per year)	7	15	4
Time (hours per year)	338	223	12
Total tax rate (% of profit)	63.7	41.2	14.9
Trading across borders (rank)	**68**	**78**	**5**
Documents to exports (number)	8	7	4
Time to export (days)	21	13	7
Cost to export (US$ per container)	580	990	630

Documents to imports(number)	5	7	5
Time to import(days)	24	14	7
Cost to import(US$ per container)	615	1235	590
Enforcing contracts (rank)	**19**	**40**	**104**
Procedures (number)	37	36	49
Time (days)	406	420	524
Cost (% of claim)	11.1	24.9	19.5
Resolving insolvency (rank)	**82**	**124**	**101**
Time (years)	1.7	3.3	3.2
Cost (% of estate)	22	15	20
Recovery rate (cents on the dollar)	35.7	23.6	29.4

Data source: Doing Business 2012 arrange by author

The overall ranks for China, Turkey and UAE are 91, 71 and 26 out of 185 countries. For starting a business, China ranks far behind Turkey and UAE. The number of procedures are twice as much, and it takes five times longer than Turkey. The minimum capital accounts for 85.7% of income per capita. In terms of this indicator, Turkey and UAE have the same number of procedures which is only 6. The time required for Turkey is 2 days less than that of UAE; however, the minimum capital for UAE is 0 and the cost is only 6% of the income per capita.

In terms of dealing with construction permit, UAE has the best performance in comparison with the other two countries. Having access to reliable and affordable power is vital for doing business as the modern industry and services cannot operate properly without power. The cost of self-supply power is at a prohibitively high cost especially in the developing economies (IFC&WB, 2012). Whether power is reliably available or not is crucial because a customer always looks for to gain uninterrupted access to power as the first step.

Table 3.7 illustrates the clear leading position for UAE in providing power, and China lags behind significantly. Although Turkey is ranked in the middle, the cost is very high. Ensuring formal property rights is also fundamental. The process of registering property is evaluated to measure this index. Effective administration of land is a part of that. If formal property transfer is too costly or complicated, formal titles might go informal again. If property is informal or poorly administered, it has little chance of being accepted as collateral for loans—limiting access to finance.

In this element, UAE has the highest rank and the least number of procedures, less time consumption and cost. Turkey ranks still in the middle; however, China is the last one among the three. Especially the cost of income per capita is 547% , and it is almost 25 folds of UAE's rate. One of the important reasons for this is that, all the land in China is state-owned. If the individuals or companies want to use the land, they need to apply to upper governmental administration.

Protecting investors matters for the ability of companies to raise the capital they need. Investors may be reluctant to invest unless they feel confident with the protections provided by strong and reasonable laws or they could become the controlling shareholders. In terms of protecting the investor, Turkey's overall rank is better than China and UAE. The countries rank the 70th, 100th, and 128th respectively, but compared to other developed IFCs, all of them are weak in terms of this indicator. because their common problem in regulative environment and judicial system is that the fairness and openness are limited.

Paying taxes is an essential element in doing business. UAE has the absolute advantage in tax regime; their world rank is No.1 in Doing Business Index out of 185 countries for 2012. The number of payments per year is only 4 in UAE, 15 in Turkey and 7 in China. The time consumption is only 12 hours per year and it is much less than China with 338 hours and Turkey with 223 hours per year. The total profit tax rate is only 14.9%, but in China it is 63.7% while in Turkey it is 41.2%.

Trading across borders in today‘s globalized environment, especially for China, Turkey and UAE, plays a key role in promoting the economic growth, because these three countries rely on exports and trade to a certain extent. Therefore, the easiness of trade between economies is increasingly important for business. The traders prefer lower cost and highly efficient trade procedures, any complicated processes such as excessive document requirements, extended time of waiting, burdensome customs procedures, inefficient port operations, low quality of service and inadequate infrastructure all lead to extra costs and delays for exporters and importers, hindering the trade potential.

Research shows that 'exporters in developing countries gain more from a 10% drop in their trading costs than from a similar reduction in the tariffs applied to their products in global markets' (IFC&WB, 2012). In trading across border category, UAE has greater advantage than China and UAE although these two countries have better performance in this indicator compared to their performances in other indicators.

The enforcing contracts and well-functioning courts help businesses expand their network and markets. Effective contract enforcement ensures people's legal right and protects employees even they do not have good relationship with the businessmen. The efficient contract enforcement could enhance the reputation, widen the access credit of the firms and is more likely to attract new borrowers or customers. China stands as the 19th in the ranking of 185 economies on the ease of enforcing contracts, and it is ahead of Turkey and UAE, which stand on the 40th and 104th ranks respectively.

An efficient bankruptcy system is beneficial for firms and society. A well-functioning insolvency system, proceeding like a filter, could protect the firms in the maximum degree, reallocating the resources reasonable, ensuring the firms a fast returns at lower costs, and increasing the returns to creditors. 'By improving the expectations of creditors and debtors about the outcome of insolvency proceedings, well-functioning insolvency systems can facilitate access to finance, save more viable businesses and thereby improve growth and sustainability in the economy overall' (World Bank, 2012). For this indicator, China stands as the 82nd out of 185, and Turkey and UAE stand as the 124th and 101st respectively.

3.2.3.3.1 Capital Access Index: Alternative Way to Measure Market Access

There is another index named Capital Access Index (CAI) compiled by Milken Institute to evaluate the market access from 7 components. The detailed performance of three countries is presented in table 3.8. Overall ranking illustrates that UAE has the broadest capital access among three economies, and China has made significant progress from 2008 to 2009, thus the distance between China and UAE has got smaller. Turkey is far behind these two economies.

TABLE 3.8 CAI RANKING 2008-09 OF CHINA, TURKE AND UAE

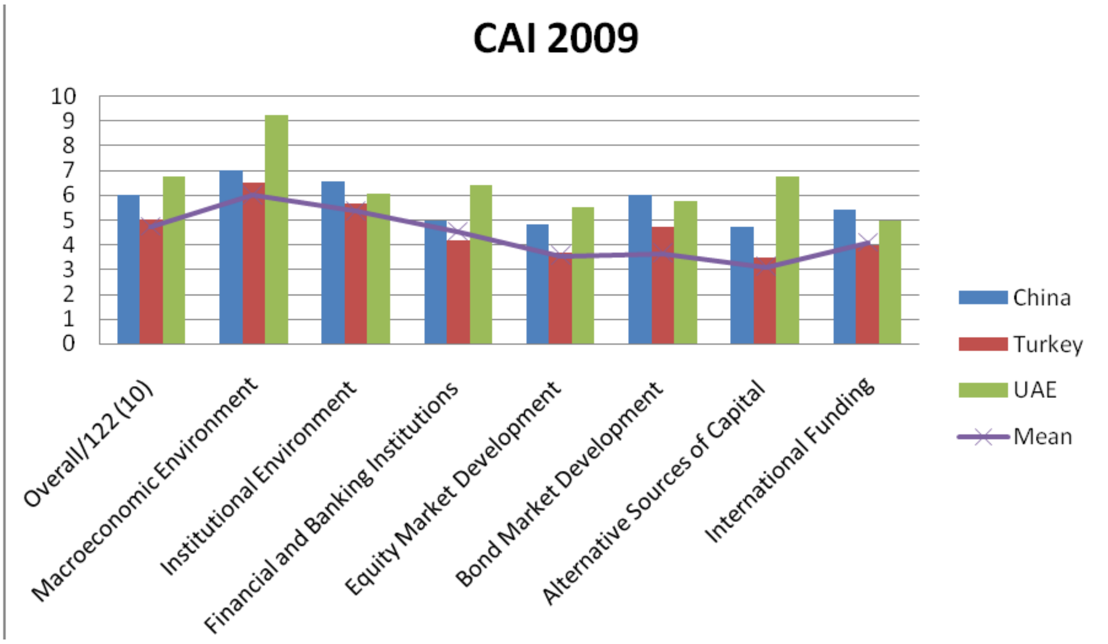
Country	Rank 2009 (122)	Rank2008 (122)	2009 Score (average: 4.73)
China	32	45	6.00
Turkey	52	50	5.02
UAE	22	19	6.77

Source: CAI 2009

Figure 3.8 shows the capital access for the three countries. In seven aspects, China and UAE perform much higher than the world average, Turkey performs worse than them.

In the CAI 2009, China is one of the largest leaping countries among 122 economics; it has jumped 13 ranks, with improvements in all subcomponents except for the bond market and alternative sources of capital (Barth *et al.*, 2010). Although China's trade surplus started to shrink due to the crisis in the world, sound economic growth and a robust banking sector have stabilized the economy and has been keeping the credit inflow. The reliance on exports has alleviated to some extent. While the country's institutional environment continued to improve, there is still a large gap between China and the well developed economies. The absence of a meaningful corporate bond market has to an extent limited Chinese businesses' access to capital (Barth *et al.*, 2010).

FIGURE 3.8 CAI RANKING



Source: data from Capital Access Index 2009.

3.2.3.4 Tax Regime

Tax system and regulation have vast impact on business environment and economic growth. A case study run by p&w company covering all around the world reveals that there are on average 28.5 tax payments in a year, it takes 277 hours to comply with tax practices and the tax cost accounts for 44.8% of the commercial profits (PWC, 2012). As discussed previously, tax rates and regime are critical for business environment. The tax volume and the tax regime impact many aspects of investment and growth, especially for the private sector which has an important position in the economic and financial sector.

Therefore, keeping a reasonable level of tax could encourage the development of the private sector and the formalization of business. Efficient tax administration can help encourage businesses to become formally registered and the economy to grow, expand the tax base and increase tax revenues. The study shows the higher the tax rate is, the more the companies opt out of formal sector.

In world economics, the trend of reducing tax payment is wide spread. In the past 7 years, 40 economies have eliminated or merged some taxes to simplify tax compliance and reduce costs for firms (PWC, 2012).

TABLE 3.9 RANKING PAYING TAXES

Economy	Overall Rank	Tax Payments	Time to Comply	Total Tax Rate Rank
China	121	11	155	161
Turkey	75	54	90	102
UAE	6	49	2	7

Source: Doing Business 2012 report

Table 3.9 shows China's, Turkey's and UAE's overall ranking in paying tax among 183 countries in 2012. UAE has absolute advantage in tax regime, it stands as the 6th out of 183 economies, although China surpasses in tax payments category, the time to comply is very short for UAE. The efficient tax system enables UAE to rank as the 2nd in the *time to comply* category; and the total tax rate is considerably lower than that of China and Turkey.

TABLE 3.10 TAX PAYMENTS AND RATES 2012

	China	**Turkey**	**UAE**
Total tax payments	7	15	14
Profit tax payments	2	1	0
Labor tax payment	1	1	12
Other tax payments	4	13	2
Tariff Rate (%)	4.2	2.3	3.7
Income Tax Rate (%)	45	35	0
Corporate Tax Rate (%)	25	20	0
Tax Burden % of GDP	17.5	24.6	1.8
Gov't Expenditure % of GDP	23	37.2	25.8
Total Tax Rate	63.5%	41.1%	14.1%
Profit Tax	6.0%	17.9%	0
Labor	49.6%	18.8%	14.1%
Other taxes	7.9%	4.4%	0
Rank	161	102	7

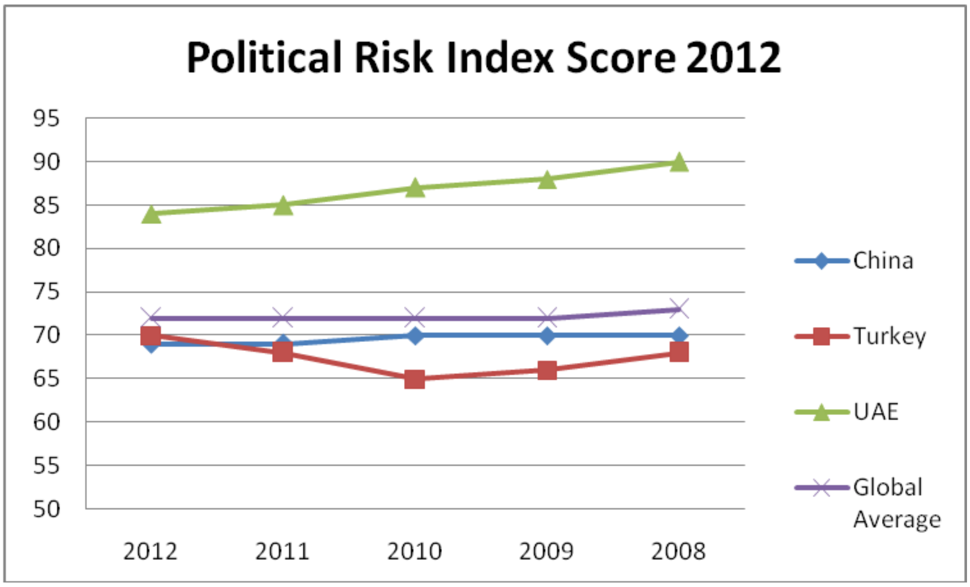
Source: Paying Taxes 2012

Table 3.10 illustrates the details for China, Turkey and UAE considering tax payment and rates. UAE is absolutely in the leading position worldwide in terms of paying tax. This is a critical strength for Dubai which enables it to attract investment and encourage private sector to promote economic and financial development. China and Turkey impose heavy tax burdens, higher costs and much complicated processes to collect taxes and the administration of tax is not transparent.

3.2.3.5 Stability of Politics and Economics

3.2.3.5.1 Political Stability

FIGURE 3.9 POLITICAL RISK INDEX 2012



The Global Political Risk Index (GPRI) is a compound measure of a country's governmental, social, security-wise and economical risks. Figure 3.9 exhibits the average political risk scores for China, Turkey and UAE. The ranks for them are 12, 58, and 62 out of 100 countries in 2012, respectively. China and Turkey have similar positions, but Turkey has improved a lot in 4 years, increased its rank from 68 to 58. China has had some improvements as well, although it is behind Turkey. UAE's political risk level is much less than those of the other two counties. From this aspect, the UAE has a strong advantage.

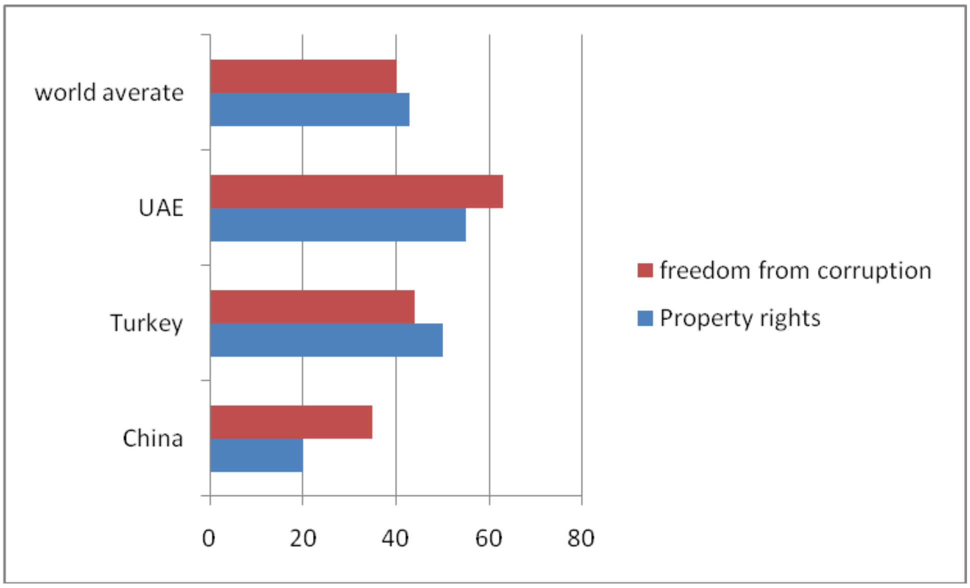
3.2.3.6 Reputation

In GFCI they use a different scoring for assessment and expectation to measure the reputation of the cities. Shanghai, Istanbul and Dubai's scores are 37, -19, and 18 respectively. Shanghai's reputation is in the first position among these three cities, and it is just behind Seoul, Singapore and Toronto. Dubai is in the 19^{th} position out of 79 cities, the reputation advantage has raised rapidly. However, Istanbul, in terms of this indicator, does not possess any advantage, the reputation score is -19 which means people's level of confidence in Istanbul is quite low. Istanbul has to make effort to improve its reputation.

3.2.4 Regulation and Legislation

3.2.4.1 Rule of Law

FIGURE 3.10 RULE OF LOW



Sources: Data from Freedom index 2012

Figure 3.10 shows the overall scores of property rights and freedom from corruption. In terms of property rights, China's rank is 143 out of 177 countries, the score is only 20 out of 100. It shows private property is protected weakly and corruption is widespread in many aspects. Judicial system could not work in order, court system is inefficient, and outside settlement and arbitration is common (Heritage, 2012). There are many reasons for this result. The main reason is that all of the land in China is state-owned; that is, the individuals and companies could only attain short or long-term leases with strict constraints and many restrictions are imposed by the government.

In this process, the corruption is an inevitable phenomenon which results in a highly vulnerable judicial system. Bribe, corruption and public drinking have been a general social atmosphere that wastes huge amount of social wealth and money of the taxpayer. Government's meddling in the judicial processes and predilection leads to unfair competition. Intellectual property rights are not protected effectively and infringements on copyrights, patents, and trademarks are quite common.

Property rights in Turkey are better than China, although the infringement remain high; the intellectual property rights regime has improved. The property rights are generally in enforcement, but the government's interference in the judiciary system makes it unfair and inefficient. The courts in Turkey are overburdened and slow, and judges are not well trained for commercial cases.

The rule of law is relatively well maintained in UAE, but due to monarchism, the ruling families have been exerting considerable influence on the judiciary system. All of the land in Abu Dhabi, largest of the seven emirates, is government-owned. According to a new resolution concerning property ownership in 2010, non-citizens are given the right to own, buy, sell, rent, and mortgage property and invest in special areas (Heritage, 2012).

Judicial system of China and Turkey are not independent from government. Government interference plays an important role, and the procedures within the judicial system are not transparent enough. Governmental institutions hold too much power; therefore, corruption cannot be avoided. This results in ill conditions in the system and institutional structure. Various forms of corruption severely affect banking, finance, government procurement, and construction in China. In Turkey bribery is outlawed, and some officials have been prosecuted for corruption, but corruption continues to undermine perceptions of government integrity. UAE the level of corruptions remains at a modest level, it is much better than those in China and Turkey.

3.2.4.2 Fair, Transparent Efficient Legal and Regulatory Regime

TABLE 3.11 REGULATORY EFFICIENTR

	REGULATORY EFFICIENT					
	Business freedom		Labor freedom		Monetary freedom	
	Score	Rank/179	Score	Rank	Score	Rank
China	46.4	149th	55.4	115th	74.2	112th
Turkey	67.1	87th	40.0	164th	71.9	134th
UAE	68	83rd	78.8	35th	80.9	40th

Source: data from heritage foundation 2012

In the regulation efficiency indicator table 3.11, UAE and Turkey are seen at the same stage and they have better performance than China with a remarkable difference.

Corruption is one of the biggest obstacles that hamper the efficiency in institutions. Table 3.12 measures the corruption rate and transparency levels of the countries. The results show that UAE has a much lower corruption rate than that of Turkey and China. The rankings are 27th, 54th and 80th out of 176 countries, respectively. UAE government's control of corruption rate is 80%' however, in China it is only 33% and in Turkey it is just 58%. These show that corruption in China is a very severe social problem and widespread in almost all aspects. Too much corruption make the legislation inefficient, the regulation processes untransparent and hamper economic and financial development.

TABLE 3.12 CORRUPTION PERCETPION INDEX

	Corruption perceptions index 2012		Bribe payers index 2012		Control of corruption 2010		Open budget index 2010	Press freedom index 01-02	Judicial independence 01-02		Rule of law 2012		Voice & accountability 2010	
	Rank/176	Score/100	Rank/28	Score/10	Percentile rank	score	openness	Rank/179	Rank/142	Score	Percentile rank	score	Percentile rank	score
China	80th	39	27th	6.5	33%	-0.60	None	174	63	3.9	45%	-0.35	5%	-1.6495
Turkey	54th	49	19th	7.5	58%	0.01	some	148	88	3.3	58%	0.10	43%	-0.1593
UAE	27th	68	23rd	7.3	80%	0.98	18/71	112	34	5.1	63%	0.39	24%	-0.8885

In terms of judicial independence indicator, Turkey has the worst performance with a ranking of 88th out of 142, China stands in the middle with a 63rd position, while UAE is ahead of them with a ranking of 34th. Turkish and Chinese judicial systems have problems, they are not independent enough, and some stronger powers could intervene with the judicial system or even control it. This is quite a risk for investors and customers as in that case they will consider protection by laws and legislation is not strong enough.

The freedom of press and voice & accountability all refer to the right of individuals to know and the transparency of the government. If the government holds substantial power to control the media and the news, the transparency degree is very low. Government can control the news to impact on people and companies. As for companies, they cannot receive accurate information from public to base their decisions on. In terms of these indicators, China is quite behind, almost the worst in the world, the 174th out of 179 countries. Voice & accountability in China is only 5%, and in UAE it is 24%, Turkey is relatively higher, with a rate of 43% in 2010 database.

3.2.4.3 Government Responsiveness

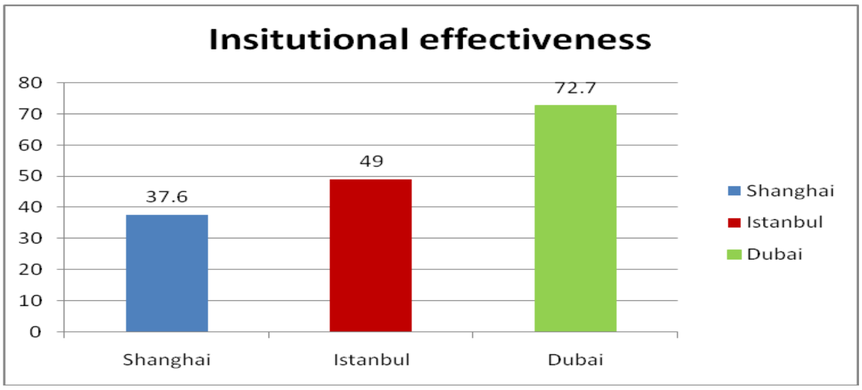
High-quality corporate governance is believed to encourage financial development, which in turn has a positive impact on growth.

In terms of this indicator; China, Turkey and UAE's governments have all developed Shanghai, Istanbul and Dubai into an international financial center by taking many measures to improve the condition from all aspects. China, Turkey and UAE stand as the 31st, 43rd, and 16th respectively in FDR 2012.

3.2.5 Institutional Effectiveness

To assess cities' institutional effectiveness, we use the data from EIU "Global City Competitiveness 2012", in which they examined indicators that "encourage stability of regulations, predictability and fairness of political processes and effectiveness of the system." Local government's fiscal autonomy and government effectiveness were weighted relatively higher within this category. Shanghai's overall score is 37.6 out of 100, Istanbul's is 49, and Dubai's is 72.7. Dubai's institutional effectiveness is higher than that of Istanbul and Shanghai, although Dubai only ranks the 40th out of 120 cities. See figure 3.11.

FIGURE 3.11 INSTITUTIONAL EFFECTIVENESS



3.3 Financial Potential

3.3.1 Overall Financial Development

To compare China, Turkey and UAE's financial potentials, we employ The Financial Development Report (FDR) 2012, which is annually published by the World Economic Forum starting from 2008 and provides a score and rank for the breadth, depth, and efficiency of 62 of the world's leading financial systems and capital markets. This index aims to measure the financial development of the national economy and thus compares the overall competitiveness of financial systems. Ultimately, this report serves as a tool for both advanced and emerging economies to benchmark themselves, thereby allowing them to identify and prioritize areas for reform.

Therefore, the data that we apply from this report could provide some financial development degree for China, Turkey and Shanghai. We can compare them to other well developed economies so that in order to they can catch up with the advanced economies; such as Hong Kong SAR, and then detect their current position, strengths and weaknesses for further improvement.

We will analyze the three countries using the FDR structure by the factors policies and institutions that lead to effective financial intermediation and markets, as well as deep and broad access to capital and financial services.

Figure 3.2 shows the relative position of the three economies in Financial Development Report. China fell down by four spots in the 2012 report, standing at the 23rd rank overall. The decline can be attributed to a decreasing scores in banking financial services and financial access pillars. These changes are in part due to an increasing banking system instability and also due to the weak results in both commercial and retail access sub-pillars. China scores particularly high in non-banking financial services (4th), with IPO (1st) and M&A activity (5th) being especially robust. Still, there is considerable room to improve China's business environment (47th), which remains the country's worst-performing pillar (WEF, 2012).

Turkey showed considerable strength in the financial markets pillar (30th), particularly in equity market development (20th). However, on the negative side, Turkey is experiencing greater financial instability (58th). Both Turkey's currency (56th) and banking systems (50th) have become more unstable (WEF, 2012).

UAE (26th) has declined by one spot since last year. UAE took hits in the banking financial services pillar 31st, because its banking system became less efficient (43rd), falling down by ten spots, The UAE experienced declining results in the IPO activity (48th), securitization (51st), and retail access (26th) sub-pillars. Despite these weaknesses, the Gulf States benefit from strong factors, policies, and institutions. UAE benefits from efficient tax regimes (2nd and 1st, respectively), generally strong corporate governance mechanisms (16th) and highly stable banking systems (4th) (WEF, 2012).

3.3.2 Comparative Sector Analysis

"Emerging market banks, emerging giants" (WEF, 2012).

Although, in the West, many are unfamiliar with emerging market banks, they are by no means small. In fact, the world's biggest bank in market value is China's ICBC. The global top 25 currently includes eight emerging market banks. Among these 4 are Chinese banks (ICBC, China Construction Bank, Agricultural Bank of China, and Bank of China). All these four Chinese banks were in the top 10 worldwide in 2012 (Taylor, 2012). In 2010, emerging market banks as a group accounted for roughly 30 percent of global profits, a third of global revenue, and half of tier 1 capital. In 2011, these numbers only increased. Not only are emerging market banks already substantially large; but also they are growing fast.

In terms of market value, the share of emerging market banks in the industry's total worldwide almost doubled between 2005 and 2010. In addition, asset growth has been impressive in many emerging markets. Although China again tops the ranks, other emerging markets have seen impressive increases in bank assets as well while maintaining adequate capital ratios and ample deposit funding. Loan growth was strong in many emerging markets in the period leading up to the financial crisis (WEF, 2012).

3.3.2.1 Countries Profiles

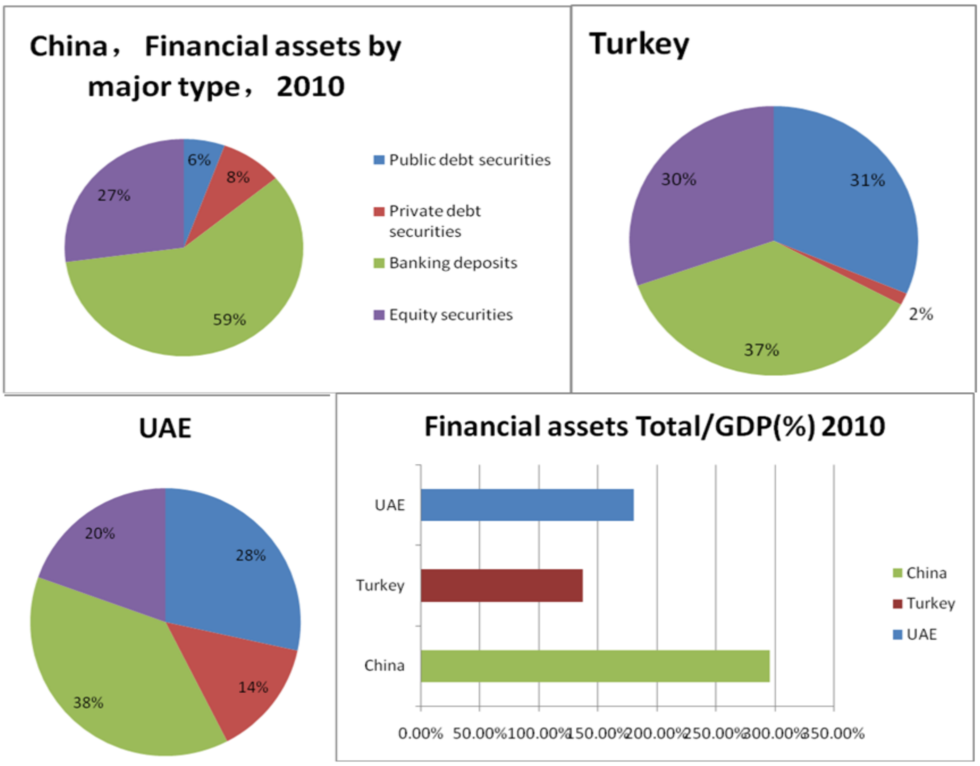
China leads the total financial assets of GDP with the the ratio of 296%, roughly accounting three fold of its GDP; UAE is in the middle of the three with 180.1%; Turkey, on the other hand, has the ratio of 137% in financial assets to GDP. So the size of the financial market and contribution of financial sector to GDP of China is the biggest.

The major types are different for three countries. China, Turkey and UAE's financial assets ratios are all dominated by banking sector, 59%, 37% and 38%, respectively, and private debt securities are relatively the smaller than other financial assets. In Turkey and UAE, public debt security accounts for one third of the total financial assets; in China it only takes 6%. Therefore, the size of public debt security is very small relative to other financial types in China.

The banking financial service rank for China, Turkey and UAE are 17, 35 and 31, respectively. China's banking sector development has significant advantage than Turkey and UAE in size, efficiency and financial information disclosure aspects.

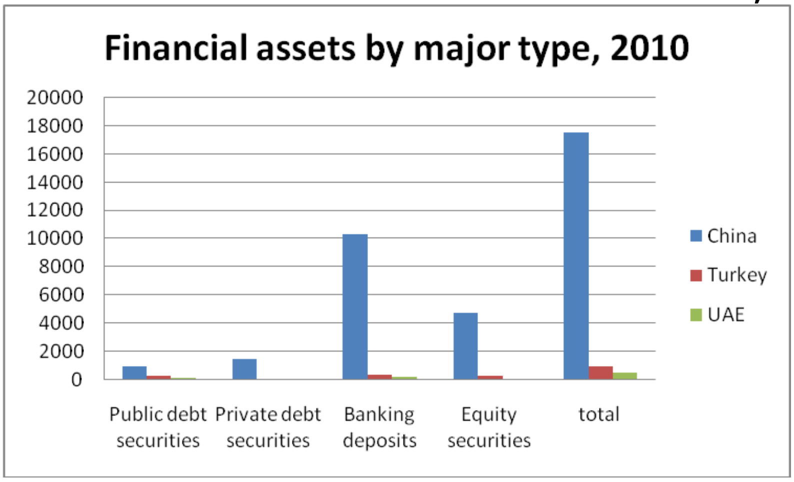
Non-banking financial services: China has absolute advantage than Turkey and UAE. Especially in IPO activity, it ranks 1st out of 62 economies; however, Turkey and UAE are far behind in this indicator; their rankings are 45 and 48 respectively. M&A activity is also another strength of China which stands the 5th out of 62 economies. The non-banking performance for Turkey and UAE do not have competitive strength.

FIGURE 3.12 FINANCIAL ASSETS BY MAJOR TPYE OF CHA, TR AND UAE



Source: Data from Financial Development Report 2012

FIGURE 3.13 FINANCIAL ASSETS BY MAJOR TYPE, 2012



In terms of financial market part, data for UAE is not available, but the overall rank for China, Turkey and UAE are 21, 30 and 47 respectively. Obviously China's performance is better than the other two. However, the derivatives markets development has big room to improve. Bond market development is a disadvantage for China too.

TABLE 3.13 FINANCIAL SECTORS RANKING IN FER 2012

	Hong Kong SAR	China	Turkey	UAE
Banking financial services	1	17	35	31
Size index	2	21	47	n/a
Efficiency index	1	21	22	43
Financial information disclosure	21	19	20	39
Non-banking financial services	10	4	45	48
IPO Activity	2	1	23	48
M&A Activity	14	5	43	47
Insurance	9	15	35	28
Securitization	25	32	54	51
Financial markets	4	21	30	47
Foreign Exchange Markets	5	20	25	n/a
Derivatives markets	11	25	21	n/a
Equity market development	1	11	20	49
Bond Market development	27	24	40	n/a

Source: WEF Financial Development Report 2012

3.3.2.2 Banking Sector

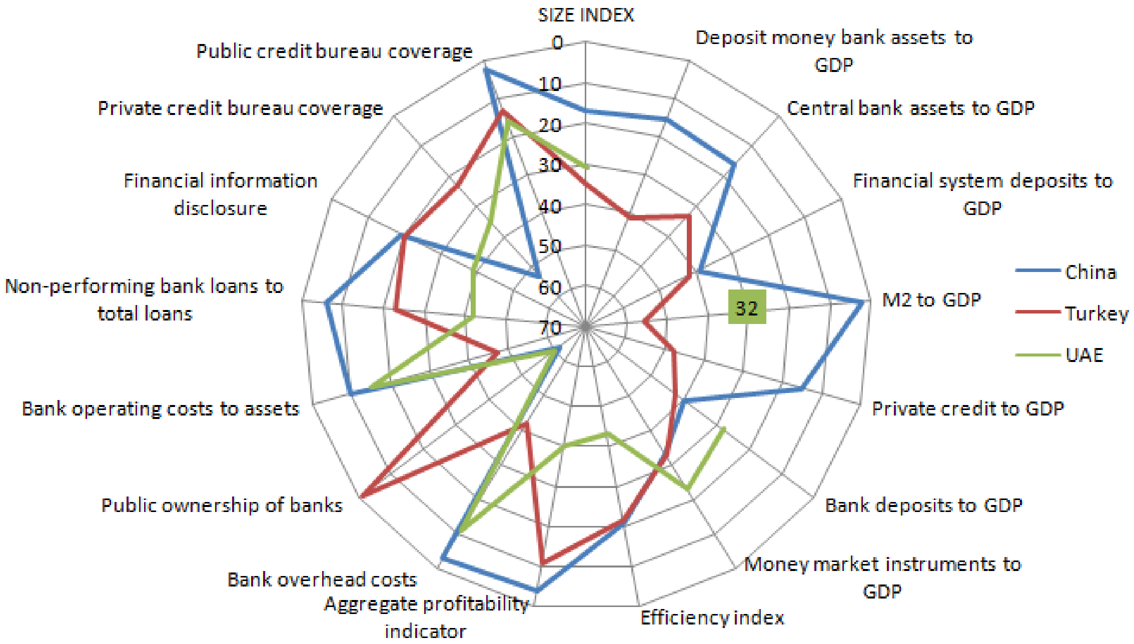
Banking sector could be analyzed from size, access, efficiency and stability aspects. According to the size indicator in Table 3.13, China has a significant advantage in deposit money bank assets to GDP, Central bank assets to GDP, M2 to GDP and Private credit to GDP; Turkey in these indicators is the smallest of the three countries. Since some data is not available for UAE, it is not comparable. All in all, the banking sector size of China is much bigger than Turkey and UAE, which is an advantage for China. Figure 3.14 shows banking-sector performance for China, Turkey and UAE.

In Efficiency index indicator, China (21st) and Turkey (22nd) has some strength, but UAE (43rd) is very weak.The aggregate profitability, and non-performing bank loans to total loans are the common advantages for China and Turkey. Their ranks in these indicators are in the very forward positions. Turkey has an absolute strength in public ownership of banks and is listed in the 1st position in all 62 economies; however, China and UAE have worse performance in this indicator. China ranks the last in all economies, and UAE takes the 60th place only. Bank overheads cost for China (3rd) and UAE (11th) are more efficient than Turkey, which is a weakness for Turkey.

In sum, except its obvious weakness of public ownership of banks,China has competitive strength in efficiency of banking sector. Placing right behind China in overall ranking, Turkey has also certain advantages, yet UAE has to take some measures to improve its efficiency. A third key aspect of the efficiency of the banking system is the role of financial information disclosure within the operation of banks. Policies that induce correct information disclosure, authorize private-sector corporate control of banks, and motivate private agents to exercise corporate control, tend to encourage bank development, operational efficiency, and stability (WEF, 2012).

Private credit bureau coverage variable is the percent of adults covered by a private credit registry. Public credit registry coverage is the percent of adults covered by a public credit registry. In this indictor, China and Turkey have better performance than UAE; the overall rank is 19th, 20th, and 39th, respectively. Public credit bureau coverage is the common advantage for three countries, especially in China which places 2nd out of 62. However, only Turkey has a good rank in private credit bureau coverage indicator; for China this is a weakness as the value is 0.

FIGURE 3.14 BANKING SECTORS RANK OF CHA, TR AND UAE



Source: Data from Financial Development Report 2012

3.3.2.3 Non-banking Financial Services

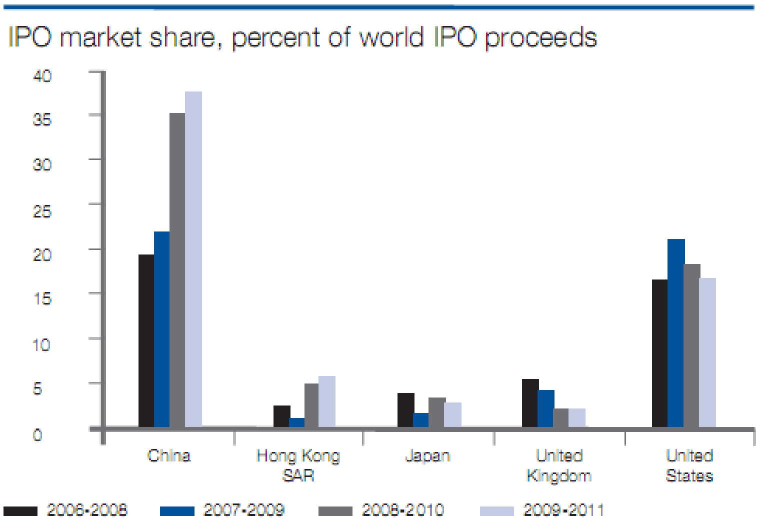
Non-banking financial service of China is in the absolute leading position and it stands 4th out of 64 economies, much ahead of Turkey (45th) and UAE (48th). Except securitization, China has strengths in IPO activity, M&A activity and Insurance sectors.

3.3.2.3.1 IPO Activity

Initial public offerings (IPO) are used by companies to raise expansion capital and transfer private to public enterprises. China's IPO market share and share of world (30.2%) are in the best position in the world. IPO activity for Turkey is strong too; the rank is 23 out of 62 countries in FDR 2012.

Figure 3.15 shows a decline in the top stock market situation except China and Hong Kong which increased their IPO market shares, while the other three Japan, United Kingdom and Unit States declined. China experienced a slight decline of four percent in the IPO proceeds amount, while Hong Kong saw an increase of 81 percent. From the figure 3.16 we could see that China's IPO has increased more than double, while Hong Kong decreased by 32 percent.

FIGURE 3.15 IPO ACTIVITY INDICATORS ACROSS TOP 5 STOCK EXCHANGES



Source: Financial Development Report 2012

3.3.2.3.2 M&A Activity

Mergers and acquisitions (M&As) activity benefits mainly from the economics scale such as taking more market share, generating cost efficiency and tax gains. China has a stronger position than Turkey and UAE in the three sub indicators of M&A except transaction value of GDP.

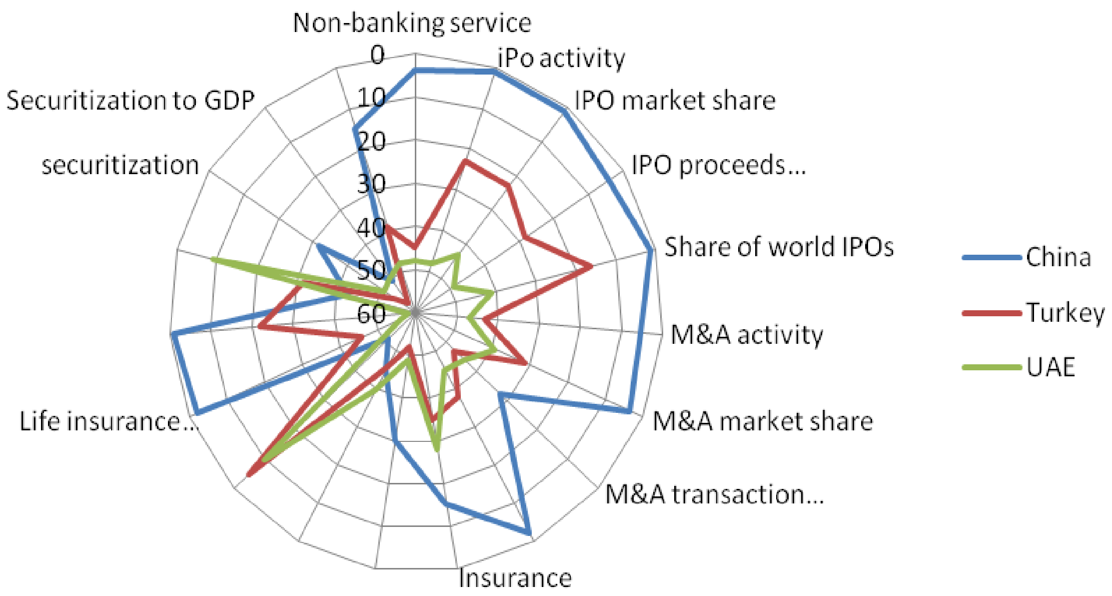
3.3.2.3.3 Insurance

Insurance market overall performance ranks for China, Turkey and the UAE are 15, 35 and 28, respectively. Compared to Turkey and the UAE, China has a relative advantage. In life and non-life insurance density items, China has an absolute advantage; however, the penetration and real growth of direct insurance premiums have big room to improve. Turkey and UAE are opposite, in real growth of direct insurance premium indicator, their ranks are 5th and 10th, and average growth rates from 2009 to 2011 are 14.2% and 10.3%, respectively.

3.3.2.3.4 Securitization

Security markets of the three countries are not well developed; they all rank behind 50. Although China has a relative advantage in share of total number of securitization deals (15th), the overall securitization needs to develop further.

FIGURE 3.16 NON-BANKING RANK SECTORS OF CHA, TR AND UAE 2012



Source: WEF Financial Development Report 2012

3.3.2.4 Financial Markets

TABLE 3.14: FINANCIAL MARKETS PERFORMANCE

Financial market	China (21st)		Turkey (30th)		UAE (47th)	
Foreign exchange markets	20	3	30		47	1.6
Spot foreign exchange turnover	18	0.5	22	0.3	n/a	n/a
Outright forward foreign exchange turnover	16	0.6	18	0.5	n/a	n/a
Foreign exchange swap turnover	24	0.3	26	0.3	n/a	n/a
Derivatives markets	25	2.5	21		n/a	n/a
Interest rate derivatives turnover: Forward rate agreements	n/a	n/a	29	0	n/a	n/a
Interest rate derivatives turnover: Swaps	31	0	40	0	n/a	n/a
Interest rate derivatives turnover: Options	10	0.6	25	0	n/a	n/a
Foreign exchange derivatives turnover: Currency swaps	41	0	11	1.6	n/a	n/a
Foreign exchange derivatives turnover: Options	33	0	14	0.4	n/a	n/a

Equity market development	11	4.5	20		49	17.3
Stock market turnover ratio	5	186.5	1	237.9	n/a	n/a
Stock market capitalization to GDP	17	83.8	42	37.1	n/a	n/a
Stock market value traded to GDP	5	145.8	23	46.1	26	0.1
Number of listed companies per 10,000 people	55	0	39	0	n/a	n/a
Bond market development	24	2.8	40		n/a	n/a
Private domestic bond market capitalization to GDP	21	22.7	40	0.6	n/a	n/a
Public domestic bond market capitalization to GDP	35	21.9	29	26.9	n/a	n/a
Private international bonds to GDP	49	1.4	47	1.7	22	23.1
Public international bonds to GDP	51	0.1	23	5.8	31	2.9
local currency corporate bond issuance to GDP	3	2.3	n/a	n/a	n/a	n/a

Source: WEF Financial Development Report 2012

In order to compare financial market development of the countries, we will analyze foreign exchange markets, derivatives markets, equity markets and bond markets. The financial market performance of China has a relative advantage compared to Turkey and UAE. The ranks of the three countries are 21, 30 and 47, respectively. As for the data acquisition problem, UAE lacks a lot of data; that's why we just obtained its rank from FDR to compare.

3.3.2.4.1 Stock Exchanges

Shanghai Stock Exchange (SSE)

Shanghai Stock Exchange (SSE), established in 1891, has a long history. Until May 2012, there were 932 listed companies with the volume reaching US$0.5 trillion (Dec. 2009), and combined market capitalization was US$2.3 trillion by Dec. 2011 (WFE, 2011). SSE is the 6th largest stock market in the world. SSE is based in the city of Shanghai, China, and it is the biggest stock exchange within China where only two stock exchanges are independently operating.

In June 2008, China's authorities opened the gates of the securities industry and allowed foreign investors who are among the Qualified Foreign institutional Investors as permitted by the Chinese government. These investors can take A shares in non-tradable State shares. However, such A shares are now closed to most foreigners (ChinaBriefing, 2008). The disadvantage of Shanghai Stock Exchange is that it is not entirely open to foreign investors and that there are many limitations and massive changes and tight capital account control by the Chinese government. These factors make the foreign investor reluctant to invest.

The top 10 largest stocks are all state-owned companies because the requirements are very strict in Securities Law of China and Company Law of China in terms of share base, total share capital, company scale and experience and so on (SSE, 2008). Therefore, such a big threshold blocks off many private companies and foreign companies. From 2003 until January 2012, there had only been 40 foreign enterprises in the QFII Qualification list.

In SSE, securities market stocks, bonds, and funds are the three main categories. Bonds traded include treasury bonds (T-bond), corporate bonds, and convertible corporate bonds. Stock market includes "A" share, which is traded with the RMB currency, and "B" share, quoted in U.S dollars and issued by SSE. Only B shares are available to foreigners since 2001.

Istanbul Stock Exchange

Istanbul Stock Exchange (İstanbul Menkul Kıymetler Borsası, İMKB) was founded on Dec 26 1985 by the Turkish Government as an autonomous entity. There are 371 companies on the listing, and market capitalization reached to US$662 billion with US$ 4879 billion volume until 2012. The biggest disadvantage of ISE is that there is no foreign company in its list; there are only domestic companies which are incorporated banks and brokerage houses (IMKB, 2012).

NASDAQ Dubai

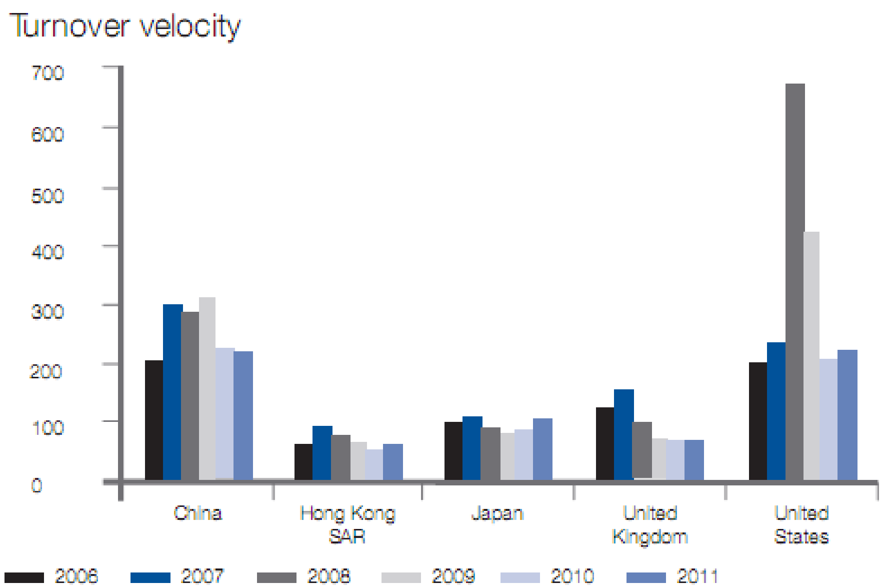
Dubai stock exchange was established in September 2005 as DFIX , Dubai International Financial Exchange. The securities include equities, derivatives, structured products, Sukuk (Islamic bonds) and conventional bonds (NASDAQ Dubai). The biggest advantage of DIFX is that it does not have many restrictions for foreign investors.

The value of shares trading to GDP has increased substantially in China and Hong Kong since 2006, (109% and 49%, respectively), but from 2010 to

2011, domestic market capitalization to GDP has fallen; China and Hong Kong experienced the largest decline at 34 percent and 11 percent respectively.

This is a matter of potential concern given the current environment and the need for sustainable growth. Empirical evidence suggests that stock market liquidity is positively and significantly correlated with current and future rates of economic growth, capital accumulation, and productivity growth (WEF, 2012). Figure 3.17 shows the turnover velocity of five main stock exchanges. Accordingly, China has a good performance in the liquidity of stock, and it clearly has the leading position in the world.

FIGURE 3.17 TURNOVER VELOCITY OF FIVE STOCK EXCHANGE



3.3.2.4.2 Equity Market Development

China is very strong in equity market development with overall rank of 11th out of 62 economies. Turkey also performs well at this indicator, taking the 20th place. UAE, however, ranks 49th in 62 in equity market development. In the stock market turnover ratio, Turkey has the absolute advantage, standing in the first position worldwide. Its stock market turnover ratio is as high as 237.9. On the other hand, China reached to 186.5, and it ranks 5th in 62 economies. Stock market capitalization to GDP of China and Turkey are

83.1 and 37.1, and they are placed in the 17th and 42nd ranks, respectively. China has an obvious advantage over Turkey in this indicator.

The stock market values traded to GDP for China, Turkey and UAE are 145.8, 46.1 and o.1, and the ranking is 5, 23, and 26 respectively. China is stronger than Turkey and UAE in this aspect (WEF, 2012).

UAE Equity Market

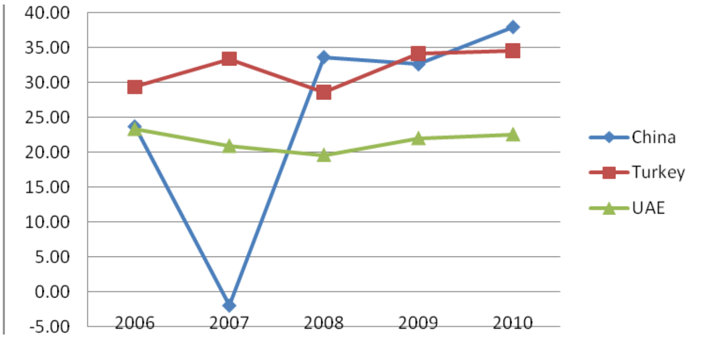
"The value of equities traded on NASDAQ Dubai in 2011 was 674 million dollars, down 48% from 1.3 billion dollars in 2010. The drop was in line with other exchanges in the region, reflecting the capital markets challenges experienced during the year. Equities traded value in December 2011 was 28.1 million dollars, down 22% from 35.8 million dollars in November 2011 and down 74% from 107.9 million dollars in December 2010 (NASDAQ DUBAI, 2012).

3.3.2.5 Financial Stability

Figure 3.18 shows Bank Z-score, which is one of the indicators to measure the stability of the banking sector. It captures the probability of default of a country's banking system, calculated as a weighed average of the Z-scores of a country's individual banks. Z-score compare a bank's butters with the volatility of those returns.

In this indicator, before 2008 Turkey was ahead of China and UAE and in a relatively high level. Since 2008, the three countries' bank z-scores have all had a rising trend, especially China's performance has skyrocketed, and it even overtook Turkey. After that, China and Turkey's bank z-socres broke even and remained much higher than that of UAE.

FIGURE 3.18 BANK Z-SCORE



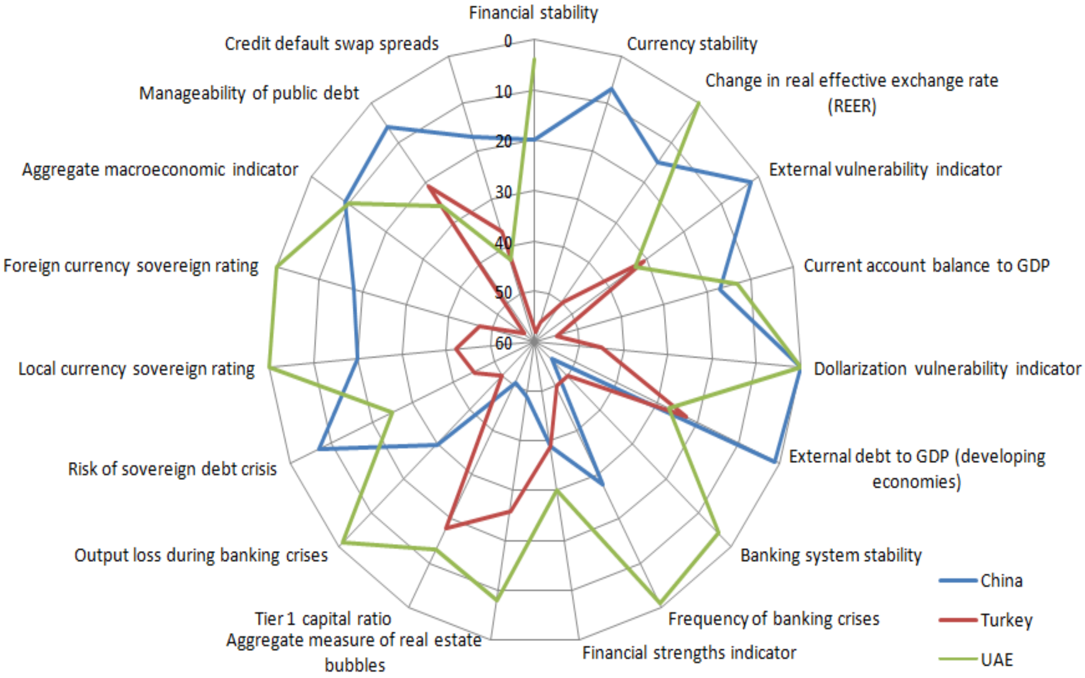
Source: Data from World Bank 2011

In terms of financial stability, we will compare the three countries from following aspects: currency stability, banking system stability and risk of sovereign debt crisis. The overall situation points to the fact that UAE (4th) has more financial stability than China (20th) and Turkey (58th). While China is relatively steady, Turkey's stability performance is not good enough.

In the first sub indicator currency stability, China is in the best position, Turkey the worst, and no data available for UAE. Considering its fixed exchange rate and lower inflation rate, we could conclude that its currency is more stable than Turkey's. In the external vulnerability indicator, China ranks the 2nd out of 62 economies, and it is strong. The outstanding performance of China is based on its external debt to GDP. It has an absolute advantage over the other two with only 9.6% and No.1 position. Turkey and UAE's ratios of external debt to GDP are as high as 40.9 and 48.7, which stems from the weakness in the currency stability.

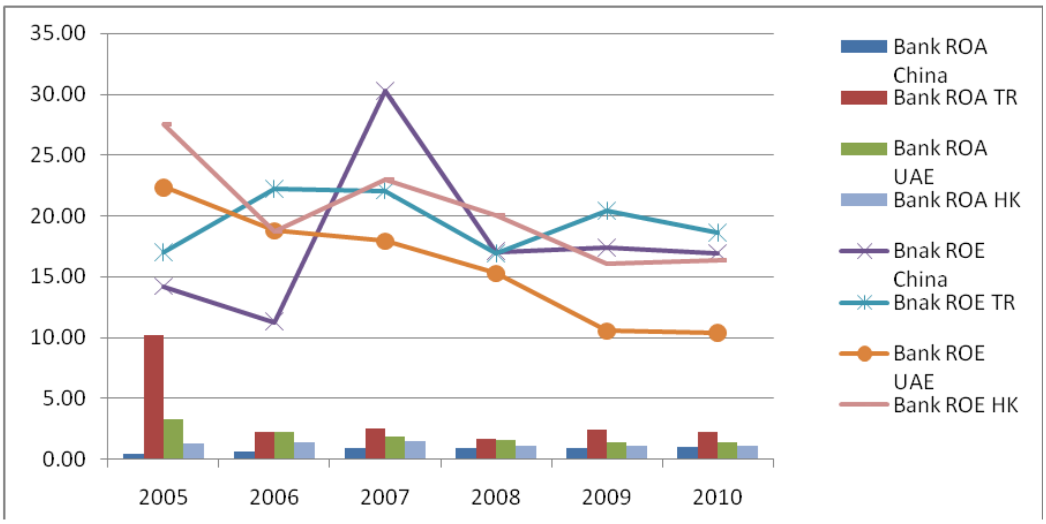
However, in terms of banking system stability, China (55th) and Turkey (50th) has a big disadvantage while UAE has very steady banking system, ranking the 4th out of 62 ecnomies. There is not frequently banking crises, hence no output loss. Financial strengths indicators show that China and Turkey have the same power, ranking 39. Although UAE is better than these two countries in this respect, it only ranks 30th, just in the middle of the 62 economies. China faces a threat from the real estate bubbles, the price of house is too higher to be considered reasonable. After the crisis and real estate bubble, UAE has improved this item. Tier 1 capital ratio is strong for Turkey and UAE, but obviously it is weak for China. The gap between them is very significant. Risk of sovereign debt crisis is one of advantageous indicators of China in all aspects; however, for Turkey it is a big weakness.

FIGURE 3.19 FINANCIAL STABILITY



Source: Financial Development Index 2012

FIGURE 3.20 BANK ROA AND ROE OF CHINA, TURKEY AND UAE

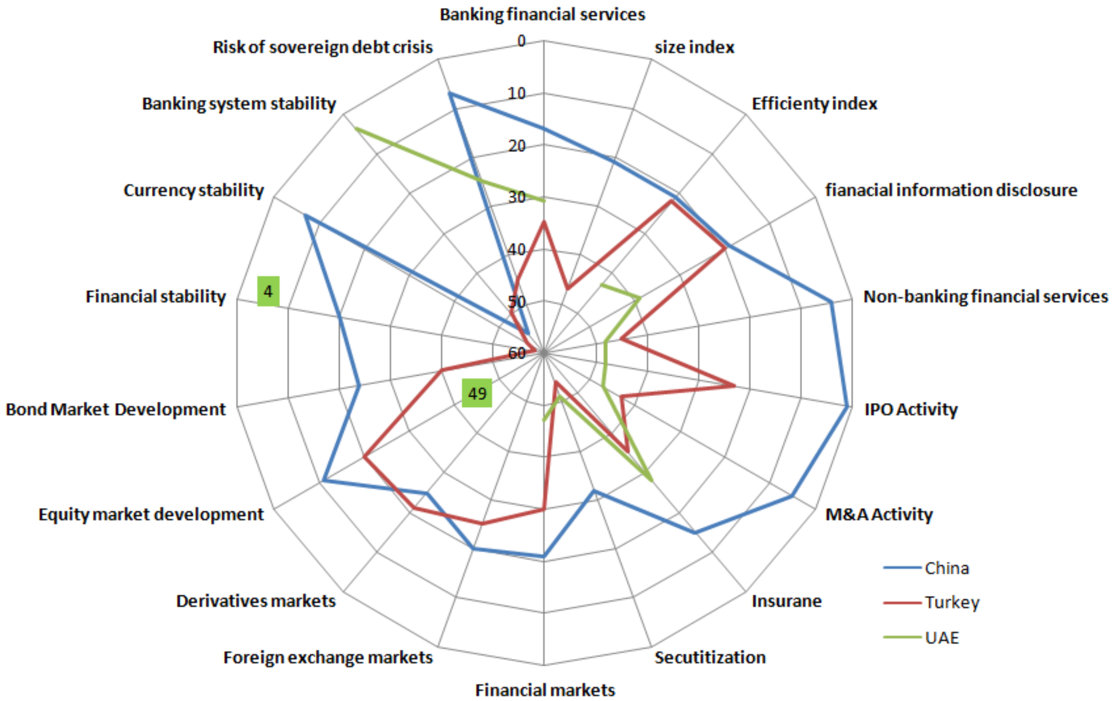


The figure 3.20 reflects the bank return on asset (ROA) which is the commercial banks' net income to yearly averaged total assets and return on equity (ROE) which is commercial banks' net income to yearly average equity. Both are the commonly used indicators to compare the probability of the bank. However, it does not mean the higher the more efficient. From the figure 3.20 we could see Turkey's ROA is very high, even higher than Hong Kong SAR, while China's ROA is in the lowest level. UAE's ROE has a significant decreasing trend. China reached to the peak and overtook Turkey in 2007, then stayed steady around 17%. From this two indicators, it can be said that Turkey's banking is more profitable than UAE and China's.

3.4 Overall Comparative Analysis

Figure 3.21 illustrates the overview in terms of the financial potential of the three economies. Except derivative market and banking system stability, in all other indicators China has obvious advantages and potential. Turkey has to develop its non-banking financial service, security market and financial stability. In terms of financial potential, UAE does not have any significant strength except its financial stability.

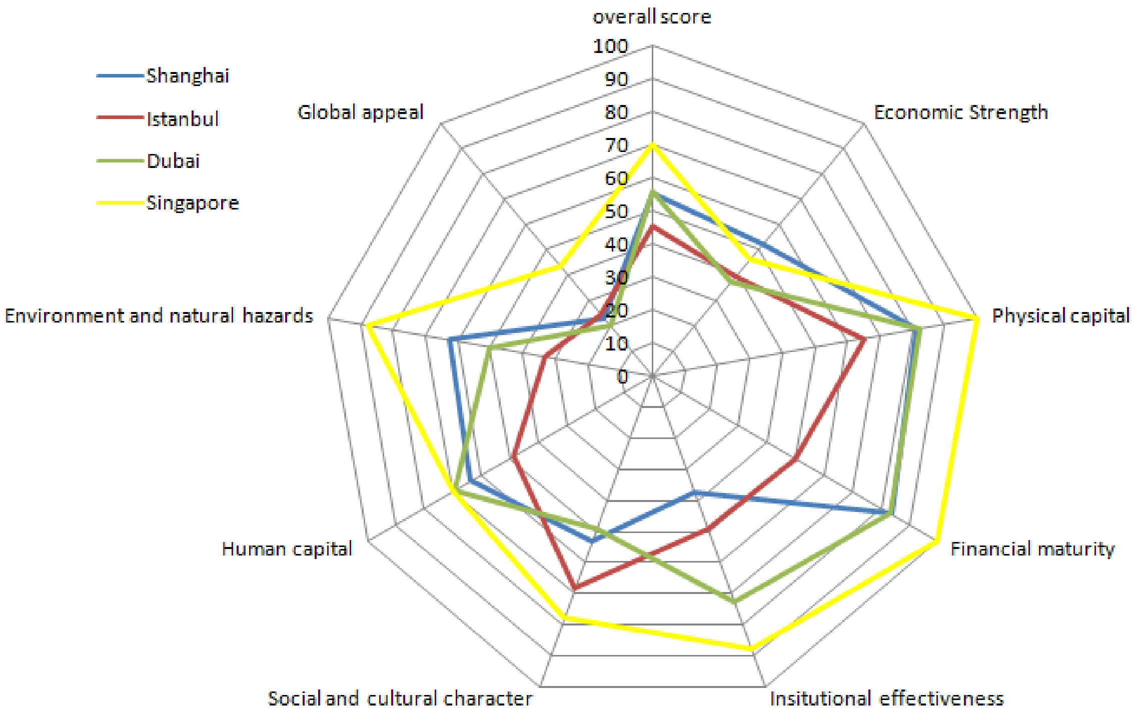
FIGURE 3.21 OVERVIEW OF FDR OF CHINA, TURKEY AND UAE



Source: WEF 2012

The figure 3.22 shows the four cities' competitiveness from EIU global city index 2012. Although Shanghai and Dubai placed very ahead of Istanbul in many aspects, we could see how big is the difference from a very developed city like Singapore, which is said to be the most competitive city of Asia. Except its economic strength, Shanghai lags far behind Singapore in all other indicators. On the one hand, there is big gap, but on the other, there is a big potential. Shanghai's government has to focus on institutional effectiveness and global appeal in these two terms, and they need to enhance Shanghai's attractiveness and efficiency.

FIGURE 3.22 GLOBAL CITY COMPETITIVENESS OVERALL SCORE OF SHANGHAI, ISTANBUL, DUBAI AND SINGAPORE



Source: EIU 2012

CONCLUSION

4.1 Comparative Analysis Conclusions

The rapid growth in GDP rate, international trade and financial services led Shanghai, Istanbul and Dubai develop into international financial centers in different regions. Especially after the financial crisis, emerging economies gained a lot of power to compete in the global stage. Shanghai, Istanbul, and Dubai rely on their countries' support, driven by the national strategy, have big potentials to transform into real international financial centers from national or domestic financial centers.

After the comparative analysis from the perspective of instrumental structures, this paper can conclude these countries' strengths and weaknesses. They have potential and obstacles in different aspects and long way ahead to become real global or international financial centers when compared to the present well-developed international financial centers.

There are several findings in the paper with regards to Shanghai, Istanbul and Dubai's potential and disadvantages to become international financial centers. Table 4.1 shows the overall rank or score by evaluating instrumental factors. Although it does not reflect the real situation completely, it is still meaningful, and it has many implications.

TABLE 4.1 OVERALL INSTRUMENTS FACTORS INFORMATION

		Shanghai, China	Istanbul, Turkey	Dubai, UAE	Source
Global city competitiveness		43rd	74th	40th	EIU 2012
GFCI mean	City Rank	18.2	56.6	22.1	GFCI 2012
	GDP growth	10.3	8.2	2.8	2010
GCI *2011-2012*	Overall index ranking	26th	59th	27th	World Economic forum 2012
Human capita	The availability of skilled personal	101st	92nd	30th	HDI 2010
	Quality of life city	-17	66.1	175.83	QLI 2012
	Culture and language city	53.3	68.3	49.2	EIU 2012
	Human capital city score	63.7	48.5	69.1	EIU /100 2012

Business environment	High quality reliable and appropriate infrastructure	48th	51st	8th	GCI 12-13
		45th	43rd	23rd	Financial development Index 2012/139
		64th	55th	9th	Travel tourism competitiveness /139
	Economic and financial freedom	138th	73rd	35th	heritage
	Market access	91st	71st	26th	Ease of doing business
	Capital access index	32nd	52nd	22nd	CAI 2009
	Taxation regime	121st	75th	6th	Paying tax2012
	Stability of political and economics	62nd	58th	12th	Political Risk index 2012
	Reputation of the city	37	-19	18	GFCI 12
	Rule of law: Property right and freedom from corruption	143rd 80th	53rd 57th	49th 30th	Heritage
Regulation and legislation	Fair, transparent efficient legal and regulatory regime	80th	54th	27th	Corruption index 2012
	Government responsive	31st	43rd	16th	FDR 2012
	Institutional effectiveness city	37.6	49	72.7	EIU
Financial potential					

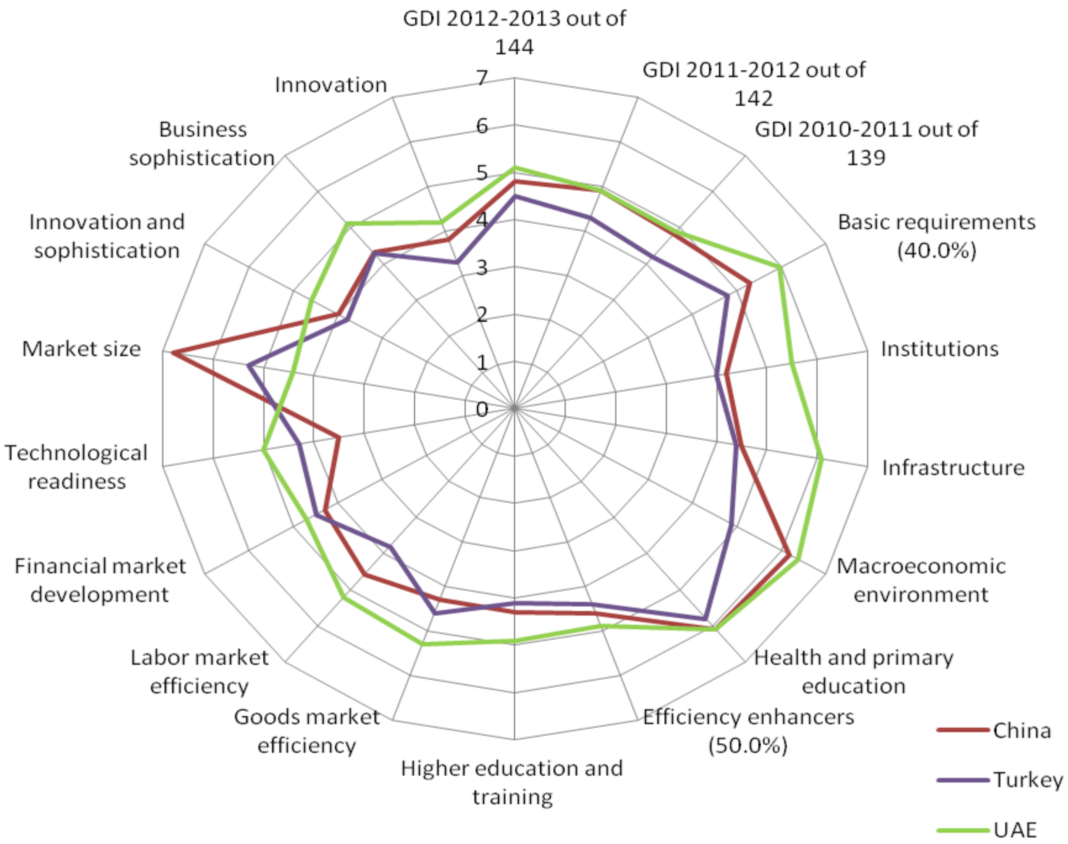
Author arranged

According to the Global Financial Index, Shanghai and Dubai have stronger potential than Istanbul; however, Istanbul has a significant upward trend. Shanghai and Istanbul share several strengths: both are domestic financial centers, the size of their financial sectors are already comparable with established international financial centers such as, Hong Kong, Singapore and Tokyo. Moreover, their market sizes, depending on their huge national markets, are the common advantages for Shanghai and Istanbul. The literature shows that financial sector can not prosper without a strong economic base, and the aggregation of financial institutions contributes to financial development. So the economic scale and potential of Shanghai and Istanbul play essential role in promoting financial centers' development.

In addition, Shanghai and Istanbul are historically regional financial centers and located in favorable geographical locations, and they held strong economic and financial power or had been vibrant domestic financial centers in the past. Dubai does not have such a historical advantage;by contrast, it is a contemporary financial center, supported by the UAE government which relies on natural resources to some extent.

Figure 4.1 illustrates overall results from Global Competitiveness Report. China and Turkey only overtake UAE in terms of market size. However, all other indicators' scores are less than UAE's. Obviously, China and Turkey still lag behind UAE, not to speak of other established IFC, such as London, New York, Hong Kong, Tokyo, Singapore, etc.

FIGURE 4.1 GDI OVERALL OF CHINA, TURKEY AND UAE



WEF Global Competitiveness Report_2010, 2011, and 2012

4.2 Strengths and Weaknesses of Shanghai

4.2.1 Strengths of Shanghai

- ✓ Shanghai is the historical international financial center in the Asia region, and the national blueprint focus.
- ✓ Shanghai has been the domestic economic and financial center already, and it has a favorable geographical location.
- ✓ Shanghai has a sound economic base, combined with rapid and steady GDP growth rate which overtook China as a whole after "the reform and opening-up policy".
- ✓ Shanghai has an international orientation.
- ✓ Shanghai, influenced deeply by the Chinese diligent and hard-working culture, has a highly educated workforce that is willing to work long hours.
- ✓ Shanghai possesses high quality, reliable and appropriate hard infrastructure. Shanghai has invested in massive construction of infrastructure in recent years, the communication and transportation condition and infrastructure have made great progress. Shanghai has two world-class airports, a high-speed modern airport train, the longest metro network in the world, and six toll-free elevated expressways (Elliott, 2011).
- ✓ Shanghai is a vibrant and diverse city of China, besides being one of the most open cities in China with a lot of business opportunities. In addition, this city has good quality infrastructure and diversified entertainment, and is relatively a higher educated region of China.
- ✓ Shanghai has a strong backing of the national and municipal government support. Shanghai is to be developed into an IFC and international shipping center. Chinese government and Shanghai's municipal government enacted many favorable policies in many aspects to encourage domestic and foreign investors and companies to develop in Shanghai, such as Tax subsidies.

- ✓ China entering WTO provided many chances and channels for Shanghai.
- ✓ With good reputation, Shanghai is believed to have the most probability to be the third Global Financial center in the world by many people.
- ✓ Access to a huge and growing Chinese financial market (Elliott, 2011). Shanghai has big potential ability to function as the access point to China. If sizable fraction of needs for Chinese capital and risk management products are met through Shanghai, it will assure a very significant role, at the least, a major regional financial center with the potential to be a truly global one (Elliott, 2011).
- ✓ Shanghai hosts the mainland's key trading markets for futures, gold and foreign exchange. It is the fashion capital for young people with large cameras and small cell phones. All these economic activities create demands for credit, insurance, trade finance, stock and bond markets (Tong, 2009).
- ✓ Shanghai has a relative high agglomeration of financial institutions, and the amount increases rapidly.
- ✓ Market size of Shanghai, supported by China's big market, is in big scale.
- ✓ Big scale of International trade volume provides many opportunities and raises a lot of capital and funds.
- ✓ Shanghai has big potential in terms of financial market. It is the second biggest global center of stock market and the third global Stock Exchange, only next to NYSE (New York Stock Exchange) and National Association of Securities Dealers Automated Quotations (NASDAQ), even surpassing those of London and Tokyo. In addition, Shanghai is the second biggest global center of futures market, only next to that of Chicago, simultaneously taking a place in the center of the tenth global biggest derivatives markets. Besides, Shanghai is the center of global biggest gold spot transaction and the second biggest center of diamond spot transaction.

4.2.2 Weaknesses of Shanghai

- ◆ Shanghai's municipal government is not independent from Chinese government, Beijing, and has too little authority to make decision about the development plan and policies.
- ◆ The speed of GDP growth has slowed down which has negative impact on economic long-term development.
- ◆ China’s international trade has shrunk, and its world factory advantage will lose due to labor shrink.
- ◆ Shanghai's competitiveness and openness need further improvement. Since the reform and opening-up policy, Shanghai economic structure has changed along with the rapid development of economy. Although the proportion of tertiary industry has been gradually enhanced, there is still a big gap compared to the developed countries.
- ◆ Shanghai's regulation and legislation environment is in confusion. There are serious regulation competition between different political groups. In addition, corruption happens everywhere.
- ◆ The shortage of financial talents has been the bottleneck of Shanghai's financial development.
- ◆ Higher education is too conservative to integrate with the world's high and standard level.
- ◆ Opaque political decision making process of Chinese government impedes Shanghai's financial environment progress, which often leads to unfair treatments to domestic and foreign companies.
- ◆ Renminbi, Chinese currency, is not available and convertible worldwide.
- ◆ Chinese government concerns with political favoritism (Elliott, 2011).
- ◆ Lack of rule of law, and lack of transparency when dealing with officialdom, as well as the government’s direct and discretionary control over the national economy are all perceived as obstacles to Shanghai (Laurenceson and Tang, 2005).
- ◆ Economic and financial freedom is very limited, which restricts

Shanghai's further development.

- Shanghai's estate price is too high to afford, which impacts the attractiveness negatively.
- Most significant Chinese banks—the locus of corporate Finance—remain state-owned. Stock market regulators pick which companies go public, and when. "The market doesn't have much say in who gets capital; the government does," says independent economist and Morgan Stanley alum Andy Xie. For now, he says, Shanghai's notion of becoming a free-market, international financial center "is still a concept" (Tang, 2009).
- Domestic competition is very intense from Hong Kong, Beijing, and Shenzhen, etc. Especially Beijing, which threats Shanghai to some extent, is the capital city of China. Due to government favoritism, political control of power, and information asymmetry, Beijing is more attractive to financial institutions than Shanghai. Such contests weaken cities' financial sector, because the present China has not such strong market and enough demand to develop more than one IFC simultaneously, even U.S and U.K could not. Therefore, Shanghai is suffering from complicated political struggles and domestic competitions.
- The financial product portfolio of Shanghai's markets is still comparatively narrow. Wealth management and private banking, for example, has just started and investment-banking activities like M&A, IPO's, and asset management are still concentrated in Hong Kong. Moreover, the corporate bond, the money, and the foreign currency exchange markets are still immature (Loeche and Quelch, 2011).
- The ability of financial market risk management is relatively weak. It affects the investors' confidence and limits financial products diversification.
- Shanghai's industrial structure is rigid, inflexible and not sound. It relies on state-owned and big & medium-sized enterprises too much. Industrial sector development is related to economic growth's speed and scale,

financial income increase rate, degrees of socio-economic and financial stability. It is well-known that private and non-state-owned enterprises are more active, efficient and competitive. They encourage innovation and apply new technology to decrease the cost. However, state-owned enterprises develop slowly, inefficiently, and costly, especially, in China where such a social environment exists with high corruption, asset control and a lot of interest groups fighting (Zhang and Daogeng, 1995).

- The Chinese government protects state-owned big and medium-size enterprises. There are a lot of restrictions on private and non-state-owned firms, for example, in the areas of the minimum assets for registration, minimum employees, open experiences and so on. Such conditions cannot be met by a small-size and new enterprise at all. Therefore, they cannot participate in a fair competition.
- Foreign trade development is way behind other coast cities such as Shenzhen, Guangzhou, Jiangsu and Zhenjiang.
- There is too much limitation on the sophisticated financial products in Shanghai (Elliott, 2011). This is also due to the fact that Shanghai has no authority to make decisions. The Chinese laws and regulations have been quiet conservative about what financial products should be available in the financial market, for some sophisticated financial products are risky. Therefore, many sophisticated products especially in the derivatives area, are not allowed in China. This makes it very difficult to capitalize on Shanghai's potential to dominate Chinese derivatives transactions by building on its commodities exchange (Elliott, 2011). In addition, it is hard for Shanghai to connect the diverse financial markets of the world.
- Shanghai's related service is still modest (Elliott, 2011). Shanghai does not yet have the volume or level of expertise in its service industries that a global financial center will need. The reason is that usually the process of growth of expertise happens gradually following the expanding of the financial market itself. However, the present Shanghai is not developed

into an IFC by itself but applying the "Singapore way" with government ambitions and supporting. Therefore, Shanghai need to find a way to be more attractive and outstanding, then it could draw more world class service firms and talents.

- Shanghai's internationalization is not enough. It seldom applies world class sophisticated and standardized laws and regulation legislations, which block many foreign investments.
- The tax rate is very high, and the spending of the collected taxes is very uncompetitive compared to the other centers in the world. The tax regime is very complicated. The whole tax issues is one of the biggest obstructs which has limited Shanghai's development as a financial center.
- Shanghai has to attract more regional headquarters of foreign banks and MNCs from Singapore, Hong Kong and even Beijing.
- The laws and rules in financial sector are not at the level of international standards.
- Stock market is not efficient because the majority players are state-owned firms. Add to this the higher trading cost and insider trading. Also governance structue is traditional and non-profitable (Laurenceson and Tang, 2005).

4.3 Some Proposals

- Authorize Shanghai's municipal government more border right to make their own decisions.
- Adjust the industrial structures and encourage non-state-owned enterprises.
- Increase economic and political freedom.
- Modify the law of rule and legislation system to avoid interest group competitions.
- Encourage innovation and apply new technology and advanced ideas of management, and increase the insider competition within state-owned

enterprises in order to lower the operation cost, save resources, enhance efficiency and make them more vibrant.

- ✧ Enhance the degree of punishment to control corruption, actually it is a system problem, adjust system as well as expose corruption at the same time.
- ✧ Put more effort to develop Shanghai's international trade to strengthen economic solidity.
- ✧ Deal with competition and cooperation in relation with other potential financial centers within China mainland. While encouraging competition to speed up the development cooperate instead of seizing resources.
- ✧ Take action to attract and train more professional talents, do not only focus on quantity but also quality and skill.
- ✧ Education should more open, provide as many opportunities for students as possible to participate and practice. It should work to motivate them and make them realize the function and application of their studies.
- ✧ Government should provide more trading programmer without too much fees to educate especially skilled persons, for example, CFA, CPA etc.
- ✧ Spread financial knowledge to attract investment, and enhance the awareness of risk control of investors.
- ✧ Reduce insider transaction, limit the government intervention.
- ✧ Nondiscrimination for domestic and foreign firms, and create fairness and justify environment.
- ✧ Try to improve the life quality essentially, the hard infrastructure is further than enough.
- ✧ Abolish government capital control and liberate private investment to encourage more market participation and attract more funds and capital.
- ✧ Control estate price in a reasonable range to encourage consumption and investment from people.
- ✧ Reduce the tax rate of firms and individuals.
- ✧ Diversify financial service and products to disperse risk.

- Apply standard international rules in accounting and auditing.
- Implementation and supervision are far more important than proposals, if the government could implement the present laws efficiently, it could improve the situation.

4.4 Conclusion

From the comparative analysis of the three cities, we could sum up that there are more weaknesses than strengths to the present day Shanghai. Moreover, many questions are historically handed down, and the system or structural problems cannot change in a short time. Therefore, if Shanghai wants to achieve its ambition, it should work substantially harder and regularly to deal with the above mentioned questions step by step. It has a long way ahead.

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