Cambridge Journal of Regions, Economy and Society 2009, **2,** 143–148
doi:10.1093/cjres/rsp019
Advance Access publication 15 June 2009

Editorial: Spatial circuits of global finance

Harry Garretsen[a], Michael Kitson[b] and Ron Martin[c]

[a]*Department of International Economics and Business, Faculty of Economics and Business, University of Groningen, PO Box 800, 9700 AV, Groningen, The Netherlands, j.h.garretsen@rug.nl*
[b]*Judge Business School, University of Cambridge, Trumpington Street, Cambridge CB2 1AG, UK, m.kitson@jbs.cam.ac.uk*
[c]*Department of Geography, University of Cambridge, Downing Place, Cambridge CB2 3EN, UK, rlm1@cam.ac.uk*

Money and space

Traditionally, the geography of money has been a topic of only marginal or peripheral interest to economists. To be sure, economists have long studied banking, the operation of national financial and monetary systems, international capital movements and the like; but in typical economics fashion, the spatial frames and contexts within which banking, financial systems and capital markets operate have not of themselves been of interest and have typically been considered as exogenous and pre-given. Even geographers tended largely to ignore the spatialities of finance. Admittedly, in the 1970s and 1980s, there were some studies of regional banking structures, urban mortgage markets, regional credit availability and regional interest rate differentials; but the studies that appeared hardly added up to a substantial or coherent body of theoretical or empirical research.

During the 1990s, however, the relationship between money and space began to attract increasing attention, with a succession of books and papers by economists and geographers (for example, Cohen, 1998; Corbridge et al., 1994; Dow, 1990; Eichengreen and Flandreau, 1996; Laulajainen, 1998; Leyshon and Thrift, 1997; Martin, 1999; O'Brien, 1990, 1992; Porteous, 1995). Ironically, this flurry of publication occurred at the very time that developments in the world of finance were leading some of the new commentators to argue that if geography had once been of relevance for understanding money, it was rapidly becoming irrelevant. O'Brien (1990, 1992) in particular claimed that various processes, especially technological advances in information and communication technologies (ICT), the wave of financial deregulation that had begun in the 1980s in the USA and UK and a new trend of financial innovation, were together facilitating—indeed promoting—accelerating financial integration at a global scale, rendering geography and location of rapidly declining significance for financial firms, financial flows and access to financial products and services. The globalization of money, it was contended, was annihilating space. Not only was financial globalization undermining national economic sovereignty (Cohen, 1998), by going global banks were free to locate wherever they chose, and money having become electronic, and hence hyper-fungible and hyper-mobile, could now move anywhere almost instantaneously. In this brave new world of global finance, money had escaped space.

© The Author 2009. Published by Oxford University Press on behalf of the Cambridge Political Economy Society. All rights reserved. For permissions, please email: journals.permissions@oxfordjournals.org

Downloaded from http://cjres.oxfordjournals.org/ at UniversitaetsbibliothekMarburg on May 29, 2012

Geographers on the whole have been much more cautious in pronouncing what O'Brien called the 'end of geography' with respect to finance. While they acknowledge that distance may have become irrelevant in financial transactions and operations, they have argued that location and place remain of crucial importance (see Leyshon, 1995, 1997, 1998; Martin, 1994, 1999). The spatial concentration of banks, investment houses and other financial institutions in the major national (and global) financial centres has not dramatically lessened: indeed in many respects it has increased, as has the financial specializations of those centres and the competition between them. The outsourcing and offshoring of certain financial functions and services (such as call centres), themselves developments facilitated by ICT and related 'globalization' processes, have been highly geographical in their locational dynamics and impacts. Global and national financial centres may be linked together in worldwide networks of financial flows and transactions that ignore national borders, but in so doing they also function as the portals through which monetary fluctuations, perturbations and shocks originating elsewhere are transmitted down through their domestic financial systems and economies, with highly geographically differentiated effects on the economies of different regions and cities (Tobin, 1984). In the other direction, local and regional economic imbalances within nations can trigger off inflationary pressures and house price bubbles that then not only disturb national domestic monetary conditions and management, but through the global interconnections that link financial institutions in world markets can even trigger off global monetary instabilities. And while the banking and financial systems of individual countries have become increasingly and inextricably interconnected, most retain a local or regional dimension in their organization and operation. How these local circuits of money relate to and are entwined with global circuits has major implications for the propagation and impact of financial shocks and perturbations. In short, contrary to what some argued, money remains highly geographical, even in today's globalized world. This special issue of the *Cambridge Journal of Regions, Economy and Society* brings together a number of papers on this issue, ranging from the geographical organization of financial centres in pre-industrial Europe to the geographical dimensions of today's global 'credit crunch'.

The Geographies of finance

The four papers in this issue that deal with the geographies of finance each offer a different perspective on the spatiality of financial markets and financial transactions.

By taking an historical perspective and by using mid-18th century data that precede the Industrial Revolution, Flandreau et al. (2009) explore the spatial linkages of financial transactions across Europe, circa 1750. The central unit of observation is the city, so that in effect the paper is really about the monetary geography of European cities and in particular about the extent to which 'local' or own-city currencies circulated 'abroad', that is in other cities. The mapping of the monetary geography of Europe in the paper of Flandreau et al. is inspired by three interdisciplinary approaches. The first concerns the role of states. History shows that before the ascent of the nation state, there was an intricate and almost seamless web of financial relations across Europe. With the rise of nation states, however, the monetary and financial space of Europe was progressively nationalized and compartmentalized into sovereign territories. The second approach upon which the paper builds is economic geography. The description of intra-city linkages across the Europe of the mid-18th century clearly point to the relevance of agglomeration forces. The main financial centre at that time was the city of Amsterdam, though other financial hubs or agglomerations in the European network of currency transactions are also clearly discernible. In southern Europe, the city of Genoa was for instance very important and likewise the city of Hamburg in Northern Europe. But in the hierarchy of financial centres, Amsterdam dominated, with London and Paris also being very important. A third and final approach that can be used to understand the network of financial connection across European cities is (of course) economic

Downloaded from http://cjres.oxfordjournals.org/ at UniversitaetsbibliothekMarburg on May 29, 2012

history. Here, the authors argue that their main result can be interpreted through the lens of modern or new institutional economic history. Whatever the analytical approach used, however, the main finding of the paper is that in pre-modern Europe, that is prior to the Industrial Revolution, there was already a dense and quite distinct spatial urban network of financial connections in Europe. Local currencies or bills of exchange circulated widely outside their own locality or city. At the same time, not all cities or bills of exchange were equally widespread: the monetary geography of Europe in those days was one in which a few cities dominated, much like in the modern monetary geography of Europe.

In the literature on 'money and space', the geographical role or relevance of financial intermediation and banks in particular is emphasized. The claim by O'Brien (1992) that geography has become irrelevant in the modern financial system applies most to public capital markets. When it comes to the supply of and demand for bank loans, however, even casual observation suggests that proximity still matters. At the same time, in many countries the banking sector has seen structural change at an unprecedented scale in the last few decades. Banking has gone 'global' and this has been accompanied by a very substantial (spatial) concentration of banking. This leads to important questions about the interrelationship between global banking and local credit markets. This interrelationship is at the heart of the paper by Alessandrini et al. (2009). Using O'Brien (1992) as a point of departure, Alessandrini et al. seek to establish if and how distance still matters in the case of the Italian credit and banking market. Distance is a multi-faceted concept and the authors come up with two ways to define distance, namely 'operational' and 'functional distance', that are subsequently used in their empirical analysis. Three findings stand out. First, geography (still) matters when it comes to the Italian credit market and the way in which firms and banks interact (locally). Second, the impact of distance on the interrelationship between global banking and local credit markets is not unambiguous. This then leads to the third finding or probably more accurately an agenda for future research: geography matters when it comes to local banking structures, and banks' own territorial strategies, as well as the relevance of the banks' headquarters for regional development.

In these first two papers on the geographies of finance, financial centres play a key role. In his paper, Wójcik (2009) takes the location of financial centres as given and tries to find out whether (non-financial) firms that are located in financial centres are more likely to go public than similar firms that are located in the financial periphery. Going public means taking the firm to the stock market via a so-called 'initial public offering' (IPO). Using firm-specific data for 32 countries, Wójcik shows that there is indeed a strong positive correlation between the location of firms and their IPO activity. Firms that are located in financial centres are more likely to go public. Given the high degree of (international) capital mobility and the current technological possibilities for both investors and firms to inform themselves about each other and the functioning of the stock market, one may wonder why in this case geography still matters. The author points out, for instance, that closeness to financial intermediaries may make it easier for firms to go public and also that the specialized labour that is needed for an IPO process is more readily available in financial centres. In this way, it appears that the geography of financial centres influences the capitalization process (via IPOs) of businesses.

All three papers introduced so far suggest, somewhat contrary to what O'Brien (1992) claimed, that even with unhampered capital mobility geography is still relevant for many financial transactions. Even with capital free to move within or between countries, the bulk of financial transactions is or remains spatially bounded and has a distinct geographical footprint. From an international macro-economic perspective, the idea that free international capital mobility does not seem to go along with a de-nationalization of capital flows is known as the Feldstein–Horioka paradox. More specifically, the paradox here is that with free capital mobility, one would expect that national savings and national investment are no longer positively correlated. Without capital mobility,

Downloaded from http://cjres.oxfordjournals.org/ at UniversitaetsbibliothekMarburg on May 29, 2012

national investment is inevitably constrained by the amount of national savings. But with capital mobility, this is in principle no longer the case. However, following the seminal study by Feldstein and Horioka (1980), scores of researchers have found that for almost every country national savings and national investment are still strongly correlated. The paper by Kool and Keijzer (2009) throws new light on this issue. Using new (panel) estimations and estimation techniques for a sample of 23 countries for the period 1973–2003, they find that the Feldstein-Horioka (FH) coefficient that measures the relationship between savings and investment has in fact dropped significantly in recent years. Indeed, around the year 2000, the coefficient is no longer significantly different from zero. This suggests that economic and financial integration has increased markedly in recent years. As to the reasons behind the de-coupling between national savings and investment, the authors single out increased trade openness and especially a fall in the so-called 'home equity bias'. The latter refers to the stylized fact that investors typically have a tendency to underinvest in foreign equity. According to Kool and Keijzer, with this bias getting weaker, the correlation between national savings and investment also has weakened. Since it is only fairly recently that the FH coefficient has fallen so strongly, it remains to be seen if this is merely a temporary phenomenon or if national savings and investment have really started to move independently of one another. The current financial crisis is a first real test in this respect.

Geography and the global financial crisis

The spatial dimensions of finance have been highlighted by the current financial crisis—where a shock ostensibly emanating from the US housing market was rapidly transmitted into a global recession. In their paper, O'Brien and Keith (2009) argue that the crisis has been facilitated by the 'end of geography' with ICT and lightly regulated finance enabling ultra-rapid and highly complex flows of financial capital across borders. However, when reviewing the future of finance, O'Brien and Keith suggest that it is likely that the drive towards the 'end of geography' will be slowed by the crisis; as the level of financial regulation is likely to increase, developments in ICT may help improve the management of information, a feature that has been manifestly lacking in modern global financial markets.

In any case, as discussed above, the 'end of geography' thesis should not be exaggerated: deregulation and ICT may promote and facilitate the movement of money and capital across space, but they do not necessarily result in a 'geography-free' world of finance. Furthermore, it can be argued that globalized financial markets have intensified geography by sustaining and, in some cases, intensifying spatial differences in economic prosperity and social welfare. Global capital markets have enabled countries such as the USA and the UK to run persistent balance of payments deficits by facilitating circulation of finance from those countries that have maintained persistent balance of payments surpluses. And within both the USA and UK, the recession that the credit crunch sparked off has been anything but spatially even in its impacts.

The notion of the 'end of geography' is subject to a powerful critique by Dymski. Tellingly, Dymski (2009) argues that O'Brien's argument is a repackaging of efficient markets theory—a theory that has been left in tatters by the recent behaviour of financial markets. Dymski constructs an alternative counter-narrative where government policy is fundamental to the construction of financial markets—not only through the regulatory framework but also through the macroeconomic and industrial policies which shape the opportunities for doing business and generating profits. Furthermore, Dymski argues that global finance has not led to the emergence of a 'global banking customer' but has instead created a spectrum of different financial customers, which has contributed to the global divisions in income and wealth. Customers from poorer parts of the spectrum are charged higher interest rates, are more likely to suffer from foreclosure and are the first to be deprived of liquidity when crisis strikes. But, of course, the most

Downloaded from http://cjres.oxfordjournals.org/ at UniversitaetsbibliothekMarburg on May 29, 2012

impoverished, such as many of those in Africa, are completely disconnected from the financial system.

According to French et al. (2009), the credit crunch is a 'very geographical crisis'. They argue that the crisis has arisen from an active use of space at a range of scales and along networks of varying length which connect individuals and institutions to the financial system. Thus, the crisis has been characterized by different geographies of financial flows, wealth effects and impacts. It should also be emphasized that the financial crises has led to an economic crisis—and the geographies of the two crises are likely to be different and will be determined by the mechanisms through which the former is transmitted to the latter—as the decline in world income and trade and the inability of producers and consumers to borrow to invest and consume will have different spatial impacts and amplitudes.

The paper by Bieri (2009) also counters the O'Brien position, on the grounds that the globalization of financial markets has led to a change in geography rather than its demise. Bieri contrasts the 'old' geography characterized by competing nation states with the 'new' geography comprising globally dispersed creditors and debtors with both strong local and global connections and drivers. Furthermore, such bi-polar processes will continue in the future and global financial markets will become more 'curved and spiky, not flat'. This will create challenges for regulation and global financial architecture: the Bretton Woods system, which was established after the Second World War in the era of dominant nation states, largely remains in place today. Thus, there is a need to re-evaluate the global financial architecture and balance the need for decentralized local regulation and centralized interventions and coordination.

The issue of the relationship between financial liberalization and poverty is analysed by Arestis and Caner (2009). The conventional focus is on the link between financial liberalization and growth and how the latter may influence poverty through 'trickle down' effects. Arestis and Caner analyse three further channels: the crises channel, the access to credit and financial services channel and the income share of labour channel. They show that although the relationships between financial liberalization and poverty are complex, the former often causes increases in the latter.

Conclusions

Although the paper of O'Brien and Keith provides an updated view of the 'end of geography' thesis, the majority of papers in this issue suggest that to characterize the contemporary global financial landscape in such terms is to capture at best only certain facets of today's monetary reality. There is in fact considerable evidence that 'money and space' are still closely intertwined—geography has evolved and changed but its 'end' is not in sight. This will become even more apparent as the fallout and complex repercussions of the current financial crisis continue to feed through to the real economy throughout the globe: including house repossessions across numerous cities in the USA and UK; major plant closures, job losses and unemployment in many local communities; future major cutbacks in public sector spending programmes, to help reduce the government debt incurred by bailing out failed banks and mortgage lenders; the collapse of the Iceland economy and the need for IMF support; and the contraction of world trade, which is affecting the German and Japanese economies to such an extent that these two countries are forecast to have much deeper recessions than those countries from where the crisis emanated in the first place (IMF, 2009, 10). What recent events demonstrate so clearly is that finance may have gone global but its complex circuits are profoundly spatial in their operation and impact.

References

Alessandrini, P., Presbitero, A. F. and Zazzaro, A. (2009) Global banking and local markets: a national perspective. *Cambridge Journal of Regions, Economy and Society*, **2**: 173–192.

Arestis, P. and Caner, A. (2009) Final liberalization and the geography of poverty. *Cambridge Journal of Regions, Economy and Society*, **2**: 229–244.

Bieri, D. S. (2009) Financial stability, the Basel Process and the new geography of regulation. *Cambridge Journal of Regions, Economy and Society*, **2**: 305–333.

Cohen, B. J. (1998) *The Geography of Money*. Ithaca, NY: Cornell University Press.

Downloaded from http://cjres.oxfordjournals.org/ at UniversitaetsbibliothekMarburg on May 29, 2012

Corbridge S, Martin RL, Thrift N. (eds). *Money, Power and Space*. Oxford: Blackwell.

Dow, S. C. (1990) *Financial Markets and Regional Economic Development*. Aldershot: Avebury.

Dymski, G. A. (2009) The global financial customer and the spatiality of exclusion after the 'end of geography'. *Cambridge Journal of Regions, Economy and Society*, **2**: 267–285.

Eichengreen, B. and Flandreau, M. (1996) The geography of the gold standard. In J. Braga de Macedo, B. Eichengreen, and J. Reis (eds.). *Currency Convertibility: The Gold Standard and Beyond*. London: Routledge.

Feldstein, M. and Horioka, C. (1980) Domestic savings and international capital flows. *Economic Journal*, **90**: 314–329.

Flandreau, M., Galimard, C., Jobst, C. and Noguès-Marco, P. (2009) Monetary geography before the industrial revolution. *Cambridge Journal of Regions, Economy and Society*, **2**: 149–171.

French, S., Leyshon, A. and Thrift, N. (2009) A very geographical crisis: the making and breaking of the 2007–08 financial crisis. *Cambridge Journal of Regions, Economy and Society*, **2**: 287–303.

IMF. (2009) *World Economic Outlook: Crisis and Recovery*. Washington, DC: International Monetary Fund.

Kool, C. J. M. and Keijzer, L. M. (2009) International capital mobility: linking the Feldstein-Hoioka puzzle to the trade and equity home bias puzzles. *Cambridge Journal of Regions, Economy and Society*, **2**: 211–227.

Laulajainen, R. (1998) *Financial Geography*. Göteborg, Sweden: School of Economic and Commercial Law.

Leyshon, A. (1995) Geographies of money and finance I. *Progress in Human Geography*, **19**: 531–543.

Leyshon, A. (1997) Geographies of money and finance II. *Progress in Human Geography*, **21**: 381–392.

Leyshon, A. (1998) Geographies of money and finance III. *Progress in Human Geography*, **22**: 433–466.

Leyshon, A. and Thrift, N. (1997) *Money/Space: Geographies of Monetary Transformation*. London: Routledge.

Martin, R. L. (1994) Stateless monies, global financial integration and national economic autonomy: the end of geography? In S. Corbridge, R.L. Martin, and N. Thrift (eds.). *Money, Power and Space*, pp. 253–278. Oxford: Blackwell.

Martin, R. L. (ed). (1999) *Money and the Space Economy*. London: Wiley.

O'Brien, R. (1990) The end of geography? The impact of technology and capital flows. *The AMEX Bank Review*, **17**: 29 May.

O'Brien, R. (1992) *Global Financial Integration: The End of* Geography. London: Royal Institute of International Affairs, Pinter Publishers.

O'Brien, R. and Keith, A. (2009) The geography of finance: after the storm. *Cambridge Journal of Regions, Economy and Society*, **2**: 245–265.

Porteous, D. J. (1995) *The Geography of Finance*. Aldershot: Avebury.

Tobin, J. (1984) On the efficiency of the financial system. *Lloyds Bank Review*, **153**: 1–15.

Wójcik, D. (2009) Financial centre bias in primary equity markets. *Cambridge Journal of Regions, Economy and Society*, **2**: 193–209.

Downloaded from http://cjres.oxfordjournals.org/ at UniversitaetsbibliothekMarburg on May 29, 2012