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An empirical assessment of the Istanbul International Financial Centre Project

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ABSTRACT

This paper tests the determinants of establishing a financial centre in the city of Istanbul by analyzing the results of a questionnaire survey which was conducted to elicit the perceptions of people working in the Turkish financial industry. We find that Istanbul has the potential to become a regional financial centre; however, the city, though improving, does not yet meet the criteria of being a financial centre. The city has a long list of issues to address, from Economic Conditions to Public Services and Social Environment, before its problems are solved. Until completion of all these tasks, the Istanbul International Financial Centre Project announced by the government will end up only being a much-publicized prestige project.

1. Introduction

Cities have been at the centre of urban studies since the early twentieth century. Early studies in urbanization (Gras, 1922; McKenzie, 1927) have analyzed the influence of cities and the concept of dominance by focusing on the social and geographical facets of world cities. Subsequent studies have theorized about the factors which give rise to a city's influence and the forces behind city growth (Hall, 1966). During the 1970s and 1980s the conceptualization of city systems emerged, as a major shift moved the world towards a global structure. The focus moved to the nature of world cities and the emergence of financial centres, with consideration of their relationships with each other and with the world economy. This was evidenced in the study of Friedmann and Wolff (1982), who saw world cities as the control centres of the global economy; of Friedmann (1986), who first proposed the world city hypothesis; and of Sassen (1991), who posited a triad of global cities. One of the main themes of these studies was to identify the taxonomy of cities, and it was argued that the world system and cities are interlocked by global flows of capital, information and telecommunication. In recent years, studies have instead analyzed specific cities and their influence in the world economy: e.g. New York, Chicago and Los Angeles (Abu-Lughod, 1999); Paris (Higonnet, 2002); London (Hamnett, 2003); Shanghai (Cai & Sit, 2003); Hong Kong (Meyer, 2006); and Tokyo (Waley, 2007).

One aspect of urban studies has been competition, with inquiries into whether cities do indeed compete. According to Buck, Gordon, Hall, Harloe, and Kleiman (2002), city competition is not new, but has become more severe and widespread because of the globalization which has accompanied the emergence of financial centres. In this new economic era, competition between cities has been more open and it is obvious that cities increasingly tend to compete and market themselves as attractive locations for inward investment. They compete to promote themselves as financial centres able to attract consequent advantages, in terms of new jobs, high incomes and wealth concentration. Cassis (2006) refers to growing competition between cities, in particular in Europe, where Paris and Frankfurt, while competing against each other, have long endeavoured to also supplant London. In Asia, both Hong Kong and Singapore are rivals of Tokyo. Cities such as Istanbul, Moscow and Johannesburg, which have important representation within a host country in terms of economic power, financial and services industries, manufacturing, contributions to the national GDP and hosting of the largest stock exchanges in the country as well as the headquarters of the largest banks and companies, are in competition to become regional hubs, since being a financial centre has come to be their dominant project in pursuing their aims.

In this paper, we first define the forms of International Financial Centres (IFCs) for the purpose of our analysis. Second, the vision, strategy and action plan of The Istanbul IFC Project (The Project)

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declared by the Turkish government are reviewed. In the main, we aim to be in a position to assess if Istanbul meets the criteria of being a financial centre by analyzing the perceptions of the people working in the Turkish financial industry. The paper concludes with the main outcomes of the analysis and proposals to encourage the success of Istanbul as a financial centre.

2. International financial centres

An IFC is a hub where financial transactions of considerable volume and variety take place. It could be a city, or a district within one, which has heavy concentrations of financial institutions offering products on a regional level or globally. The term has been used by several scholars; e.g. Johnson (1976), Heenan (1977), Reed (1981), Gorostiaga (1984), Jones (1992) and Cassis (2006). Financial centres for Reed (1981) mean centralization: such places contain concentrations of institutions which are capable of easing the flow of financial services and capital between their national economy and those of other countries. An IFC is assumed to have major stock exchanges, capital markets, financial institutions and to be the main host of regulators and central banks. With regard to their impact, a striking point is made by Jacobs (1984), who argues that the key drivers of global economies are not nations, but cities with financial centres.

Bearing in mind that not all cities are the same and that there are varieties and different types of cities in the development of IFCs, for the purpose of this paper we classify IFCs as Global Financial Centres (GFCs) and Regional Financial Centres (RFCs). For instance, cities in a third group are neither global nor regional centres, since this category consists of urban areas in national economies, such as Istanbul in Turkey and Moscow in Russia. In this paper, we do not refer to more specific debates within urban studies on categorizing different types of cities, as we solely aim to focus on whether Istanbul can be an RFC.

GFCs are key sites for economic and financial industries serving as market places. These hubs are characterized as command and control centres in the global economy and of banking, finance and other services, such as accounting and consulting. Among others, the increase of transnational corporations (TNCs) and global financial institutions is considered to be evidence for a city as a GFC (Saito & Thornley, 2003). Shin and Timberlake (2000) support the argument that GFCs serve as the nodes through which capital and information circulate and in which multinational corporations are concentrated. Knox (1995) illustrates these hubs as centres of transnational corporate headquarters, of their business services, international finance and telecommunications and of information processing. London and New York are widely seen as the only GFCs. They function as key locations for finance and service companies, for the production of innovations and as markets for these products, in addition to managing huge amounts of funds.

RFCs are defined by their concentration of broad financial services and transactions; they interact vigorously either with GFCs or their counterparts. RFCs are distinguished from GFCs in that a centre is called regional if it derives its main role from its geographical proximity to the combination of countries in which its customers operate (Johnson, 1976). They are hosts to foreign financial institutions which have found them convenient for locating offices, rather than magnets of financial power. GFCs, on the other hand, serve as hubs for TNCs with worldwide financial activities. RFCs have developed markets with good infrastructures and intermediate funds in and out of their region, where they provide favourable regulations, an enhanced legal framework and secure conditions for doing business. They have become globally more prominent as their relations with other cities have extended. Singapore and Hong Kong are mere RFCs compared to London and New York. Frankfurt, Paris and Amsterdam in Europe and Chicago in North America are other examples of RFCs. Hong Kong has one of the largest stock exchanges in Asia by market capitalization and the world's second-highest value of initial public offerings. Singapore is a significant market in foreign exchange and derivatives trading and real estate investment trusts; however, there are definite differences between the GFCs and the second group. As argued by Sassen (1999), only a few cities have the resources to be dominant within the international network of financial centres and first among them are London and New York, with their enormous concentrations of capital and financial flows. GFCs function as hubs where huge volumes of transactions are managed between TNCs across the world by using financial instruments, whereas the RFCs are the spokes in these complicated transactions with financial flows going through these centres from the global hubs.

3. The Istanbul IFC Project

The Turkish government wants to pour resources into Istanbul to allow it to become an IFC, rather than into the capital city, Ankara. This is because Istanbul is the premier city in Turkey in terms of its economic power, financial and services industries and manufacturing. There are also other reasons; Istanbul has a rich cultural and historical background and is a cosmopolitan city. With its lifestyle and culture, it meets the expectations of people from many different countries.

A new central business district is under construction in Atasehir–Istanbul and will host the headquarters of various financial institutions upon completion. In addition, the Turkish government has decided to move the banking regulator and state-owned banks from the capital city to Istanbul as part of a strategy to promote the latter as an RFC. However, the government had to put the Central Bank of Turkey's (CBT) move on hold in the face of resentment and resistance from political opponents and some public institutions. It is argued that the CBT should be located in the capital city, close to the government and the treasury, to better coordinate the monetary policy in times of economic crisis. Political opponents, on the other hand, see relocating the CBT as a first step in a bid by the government to move the capital from Ankara to Istanbul, since the CBT is seen as a symbol of national sovereignty and some consider that moving it out of the capital city of the country could damage the Republic. Such opposition is seen as ideological, as it has no basis in economic realities.

Istanbul is the command and control centre of the country, having huge revenue-generating potential. It generates 27% of the country's GDP, 47% of its total exports and 54% of its imports, and handles 46% of its air traffic (TurkStat, 2013). With a population of 14.1 million, 18.5% of the national total, Istanbul is the largest city in Turkey and with its significant contribution to the Turkish economy, it is responsible for 40% of the nation's total tax revenue.

Playing host to the largest banks and headquarters of companies and the Borsa Istanbul (BIST), the sole exchange entity of the country, which combined the former Istanbul Stock Exchange, the Istanbul Gold Exchange, and the Derivatives Exchange of Turkey, in addition to the fixed income, foreign exchange and money markets, the city's command and control status is unequalled in the country. Among the emerging markets, BIST has the 7th largest traded value in equities, with a total of USD 419 billion, and is the world's 8th largest bond market, with USD 521 billion as of 2013. Equity portfolio holdings by international investors represent 62.5% of free float capitalization. Non-residents' share in the government bond market stands at around 25%. The total trading value of the debt securities market