

SPATIAL RESTRUCTURING OF FINANCIAL CENTERS IN MAINLAND CHINA AND HONG KONG

A Geography of Finance Perspective

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The rapid progress of globalization and information technology has stimulated profound changes in the global financial landscape and attracted growing interest in the geography of finance. Although there is apparently remarkable stability in the ordering of financial centers over time, the spatial changes of regional, national, and even global financial centers are an ongoing process. The newly developed subdiscipline of the geography of finance examines and evaluates these spatial changes among financial centers. This study explores the possible changes in China's information hinterland and the spatial restructuring of financial systems in the region, including the spatial switching in importance among the financial centers of Hong Kong, Beijing, Shanghai, and the major Guangdong cities of Guangzhou and Shenzhen. China's landmark World Trade Organization accession will certainly have a tremendous impact on China's information hinterland and induce profound organizational and spatial restructuring of the financial systems in the region.

Keywords: *geography of finance; spatial restructuring; financial centers; China; Hong Kong*

In this era of the Internet and globalization, financial markets have become increasingly volatile and crisis prone. Accompanying this financial market volatility, individual financial centers are also increasingly becoming

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unstable and unpredictable in terms of their relative importance in their regions. Although there is considerable stability in the ordering of financial centers over time—as New York and London demonstrate—significant changes in the rankings of financial centers at national, regional, and global levels do occur. The spatial switching of financial dominance from place to place can be seen all around the world: For example, Sydney has replaced Melbourne in Australia, Toronto has overtaken Montreal in Canada, São Paulo now dominates Rio de Janeiro in Brazil, and Johannesburg has succeeded Cape Town in South Africa. In the United States, Chicago gave way to New York early in the past century, and Los Angeles is now surpassing San Francisco. Nowadays, due to the power of globalization and information technology (IT) innovation, the speed and scale of the changes have been increasing, and many financial centers, including the strongest ones such as New York and London, have been under tremendous pressure to maintain their dominance. For instance, the virtual market of NASDAQ now posts a fresh threat to the Dow Jones, and the City (London) had to join forces with Frankfurt to form a new stock exchange market iX to counter the challenge from Euronext, another newly born stock exchange market jointly formed by Brussels, Amsterdam, and Paris. Hong Kong, as a preeminent financial center in Southeast Asia, is no exception, as Singapore and Shanghai are threatening to take over. It is not surprising to learn that many municipal governments of international or regional financial centers have begun to establish special task offices, such as London First for the City, to shelter their financial centers from the worst effects of such changes.

Although many “technical” or “sectional” measures can be adopted to strengthen the competitiveness of a financial center—including deregulation, transparency, pegged exchange rate systems, and technological and institutional innovations—the spatial evolution of a financial center is effectively beyond the power of the financial sector itself. Recent developments in economics and geography, particularly the emergence of the new subdiscipline of the geography of finance, have provided some powerful tools to account for the spatial changes among financial centers. For example, the theory of path dependence offers a much better account of the persistence and dominance of a particular center, and the theories of asymmetric information and the information hinterland allow us to answer why path-dependent

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dominance can be undermined and challenged (Porteous 1995). These new theories address the most important concepts of information externalities, asymmetric information, path dependence, and the information hinterland, which help us to understand the forces behind the development of financial centers, including the rise and fall of their relative importance in the region. China's landmark accession into the World Trade Organization (WTO) will certainly create tremendous impacts on China's economic development and its landscapes of finance. It will change China's information hinterland and induce profound organizational and spatial restructuring of the financial systems in both Mainland China and Hong Kong. Within the theoretical framework of the geography of finance and based on surveys of multinational corporation (MNC) headquarters locations, this study analyzes and forecasts the possible changes and spatial restructuring of financial centers in Mainland China and Hong Kong. The result of the study should allow researchers to predict some of the growth trends likely to affect China's major financial centers in the near future.

THEORETICAL FRAMEWORK

INFORMATION FLOW AND FINANCIAL CENTER DEVELOPMENT

A financial center is an area in which high-level financial functions and services are concentrated. It can be defined multidimensionally: Functionally, a financial sector includes industries of banking, investment banking, insurance, security and exchange, and brokerages; it is also closely associated with accounting, auditing, lawyer, and other professional services. Spatially, a financial sector is usually a city but is more often a localized area within city boundaries, for example, New York's Wall Street or the City in London. Rather than providing retail services such as branch banking, a financial center focuses on providing a high-level financial service that serves a much larger area at regional, national, and even global scales. The relative importance of a particular financial center can be measured by various indicators, for example, total employment in the financial sector, check clearings, stock exchange volumes, the presence of local banks and financial institutions and their head offices, and the presence of head offices of foreign banks and financial and nonfinancial institutions. The last item—the presence of foreign corporate head offices—provides the most accurate indicator for the ranking of international financial centers. This is not only because these foreign corporations have a relatively high capacity and important position in the global economies but also because the place they occupied/located

also presents a strategic locational importance in the domestic economy. In short, a financial center is an agglomeration of financial and service enterprises and corporate headquarters, particularly the foreign ones.

It is recognized that some agglomerating (centripetal) forces contribute to the establishment and development of a financial center. Four of the most notable of these are labor market externalities, demand for intermediate services, technological spillovers, and informational spillovers (or externalities) (Krugman 1991). All these forces imply that the establishment of any financial firm requires a certain amount of information attachment. A financial firm will probably choose a locale where a large local pool of labor (especially highly skilled personnel); abundant specialized producer services, including sophisticated communications; and complex legal services and rapid technological innovation can be found. Also, to benefit from their ability to process information more efficiently and to maximize access to information flows (thereby increasing profits), financial firms are most likely to locate in a place where the largest volume of informational spillovers can be found.

According to the theories of the geography of finance (Porteous 1995, 1999; Martin 1999; Thrift 1994; Corbridge, Martin, and Thrift 1994), financial centers in general and banking systems in particular provide specialized and high value-added intermediate services and rely almost entirely on information flows and IT innovation. A financial center is an information collector and user that lives off of the existence of information and simultaneously functions to "add high value" to the information. In other words, information is the crucial prerequisite for the development of financial centers, and in this sense, the financial sector can be conceived as a "super value-added" information service industry. Porteous (1995) has stressed the importance of information externalities, asymmetric information, information hinterland and heartland, international attachment, and path dependence as forces that help to shape and develop financial centers and determine the rise and fall of their relative importance within their regions, and it is useful to consider each of these terms in some more detail.

First, information externalities refer to the information spillover effect that accrues in the presence of existing financial enterprises. It is suggested that the nature of financial production adds significant value to existing information, and as a result, information externalities (or spillover effects) from the presence of agglomerated financial enterprises are often huge and instantaneous. There are three types of information—namely, trading (the flow of goods), financial (the flow of capital), and regulatory (policy-making) information. A particular city may be specialized in producing a certain type of information; in China, for example, Shanghai is rich in trading information,

Hong Kong has sophisticated financial information, and Beijing specializes in obtaining regulatory information. This exactly exemplifies what Dunning (1998) has suggested: that the locational choices of MNCs have been influenced by “the growing importance of intangible assets—and particularly intellectual capital—in the wealth-creating process, and of the need of companies to harness, as well as to exploit, these assets from a variety of locations.” Firms would be able to tell what kind of information they wanted to exploit and choose the location where they could exploit the most information.

Second, asymmetric information refers to problems in interpreting the value, background, or culture of information. In this context, there are two kinds of information: standardized and nonstandardized information. The former refers to the “hard” data that are publicized and transmittable through common media, and the latter refers to “soft” data that are localized and untransmittable through common media, such as rumors, the undercover credibility and liability of companies, and so on. The nonstandardized information causes problems for the precise interpretation of the value of the information, which in turn determines the viability of any financial enterprise (e.g., rumors about corporate mergers, acquisitions, or takeover bids). In some extreme cases, rumors such as the news that Deng Xiaoping had died or Zhu Rongji had been sacked have a significant impact on financial markets with unpredictable and instant volatility. To accurately interpret the value of the nonstandardized information, one must understand the broad background or culture of such information. Mainstream media such as television, newspapers, and the Internet can transmit data or information but cannot transmit the background or the culture of information. Thus, the asymmetric characteristic of information requires financial enterprises to locate close to the sourcing area of the heartland of information. To tap useful information and develop the business optimally in the region or the country as a whole under the consideration of efficiency, most foreign companies have to set up their subsidiaries and head offices in the information heartland. In this particular locale, a financial center will most probably emerge, assuming a sufficient number of other corporations make similar decisions.

Third, information *hinterland* and *heartland* refer to the best access point for the profitable exploitation of valuable information flows within a region. This best access point is normally a core city of a region, in which information is produced or generated, collected, and disseminated. Hence, this best access point or core city can be referred to as the information heartland. The difference between a traditional economic heartland/center and an information heartland is that the former refers to the agglomeration of economic activities that characterize the production of goods, whereas the latter refers

to the clustering of knowledge/information activities that feature deals and services production. The "heartland" can also be referred to as a particular transaction/deal-making area or an information generation field. In a dynamic sense, a financial center is expected to grow from this information heartland, which will move and change as its information hinterland moves and changes. An information heartland may move among the economic centers in the hinterland but will most probably be located in the best access point for the most profitable exploitation of the valuable information of the region or country.

Last, international attachment refers to the openness and accessibility to the outside world, and path dependence relates to the past successful track record of a firm/sector that has been able to establish supremacy over others and thus requires all others to follow. As there is an increasing emphasis on the globalization of capital, international linkages are particularly important in boosting the financial role of a city, and the city must be well functioning as a "point of attachment" through which foreign capital is channeled into the local economy. By and large, the evolution of any financial center must undergo two stages: The first is the formation of an immediate hinterland adjacent to the center, and the second is the formation of a region interacting with other hinterlands and heartlands and fitting itself into the global or regional patterns.

The first precondition for financial center development is, therefore, to form an information hinterland and heartland in which financial firms can find the most accessible point for the exploitation of information flows. Similar to serving as the most accurate indicator for the ranking of international financial centers, the presence of a foreign head office also serves as the most reflective indicator to reveal the "most accessible point" for the exploitation of information flows. This is because foreign corporations have less locational constraints compared to the domestic ones and are more purely market oriented and profit driven. They will select, locate, and agglomerate in a place (the best access point) that has strategic importance for their business development, as well as for the country/region as a whole. Thus, this study will focus on the foreign head office survey in searching China's most accessible point—the best location for China's financial center development in the face of China's imminent WTO accession.

METHOD

According to studies conducted by Porteous (1995), the presence of head offices of foreign banks and financial institutions, as well as large nonfinancial

corporations such as global MNCs, provides the most accurate indicator for the overall assessment and ranking of international financial centers. This is because the easy accessibility and accurate interpretation of information are the key factors affecting the location of headquarters of foreign MNCs and the agglomeration of headquarters of foreign MNCs. As for information itself, it is difficult to quantify the measurement even for the standard information and the accessibility to it, and it is even more difficult to place the value in monetary terms. As for the nonstandardized information such as rumors and "informal information," according to the assumption of asymmetric information, the quantification and "monetarization" of them are virtually impossible. Therefore, the qualification and accessibility of information need to be substituted with factors that could be tangible and able to be quantified. Hence, the locational choice of foreign MNCs' headquarters is probably the only way to suggest the importance of information itself and the correct interpretation of it. As a result, the location of foreign MNCs' headquarters is perhaps the only practical as well as effective factor differentiating the cities in China currently, as well as facilitating the display of the significance of the information and its effects on cities.

It is necessary to distinguish the locational choice of the headquarters of multinational corporations, as well as the locational choice of their production bases and the foreign direct investments as they are not necessarily located in the same city. The firms located in the financial centers of London and New York are classic examples of the separation between the location of headquarters and the location for production and operation, as both London and New York facilitate the access of information. Dunning (1998) attempted to identify the differences in the factors affecting the locational decisions of MNCs from the 1970s to the late 1990s, and he concluded that one of the main changes of the locational needs of corporations is the shift "from those to do with access to markets, or to natural resources, to those to do with access to knowledge-intensive assets and learning experiences." That is, he concluded that firms have been increasingly choosing to locate where information and knowledge can be obtained.

A very recent example of such separation is the relocation of the headquarters of Boeing, the internationally renowned aircraft manufacturer, from Seattle, where its production plant is located, to Chicago in 2001. Although Seattle is its founding city, the company is even more "determined that our headquarters needs to be in a location central to all our operating units, customers and the financial community—but separate from our existing operations," and it is emphasized that the relocation "is a fundamental element of our business strategy" (Boeing chooses Chicago 2001). The new location shall "offer ready access to global markets, provide a strong pro-business

TABLE 1: Realized Foreign Direct Investment in Beijing, Shanghai, and the Guangdong Province (in U.S. \$100 million)

Year	National	Beijing		Shanghai		Guangdong	
		Amount	% of National	Amount	% of National	Amount	% of National
1995	378.0	27.3	7.2	32.4	8.6	121.0	32
1996	418.7	15.5	3.7	39.4	9.4	117.5	28
1997	523.8	20.6	3.9	36.3	6.9	150.9	28.8
1998	452.8	21.6	4.8	36.0	7.9	120.1	26.5
1999	452.8	19.7	5.0	28.3	7.1	116.5	29
2000	407.1	16.8	4.1	31.6	7.8	112.8	28

SOURCE: Compiled from *China Statistics Yearbook*, various years; *Guangdong Statistics Yearbook*, various years; *Beijing Statistics Yearbook*, various years; *Shanghai Statistics Yearbook*, various years.

environment, and allow easy access to major Boeing operations and customers” (Boeing chooses Chicago 2001).

In China, although foreign direct investment (FDI) concentrated in the Guangdong province during the 1990s (see Table 1), the number of headquarters of companies located in the province is minimal, whereas Beijing shares most of the headquarters, although it has the least FDI among the three places surveyed (this will be further explained later).

It is important to emphasize these differences of locational choices (between headquarters of the multinational corporations and their production/manufacturing bases as well as their actual location of foreign direct investments) because the former is led essentially by information and the latter through physical resources and other factors of production (Dunning 1998). All of the above examples illustrate the point that the easy accessibility and interpretation of accurate information lead to the concentration of headquarters of the MNCs in certain city centers, but their manufacturing bases can spread widely across the country according to specific required resources and factors of production.

The exploration of the city-based agglomeration of solely foreign-owned companies and their headquarters in China and Hong Kong is one of the key objectives of this study, in addition to making an attempt to explore the underlying reasons for their locational choices and project or predict future locational trends within the region. As the headquarters of foreign companies in Hong Kong are mostly regional headquarters, which directly report to the global headquarters of the company, they oversee the businesses in the Asia Pacific/East Asian region without frequent supervision from the global

headquarters. There are essentially two different levels of headquarters. We noticed that in most cases, the headquarters of foreign companies in Chinese cities often have to make contact or report to the regional headquarters in Hong Kong. Therefore, the “headquarters” in China and the regional headquarters in Hong Kong are often closely linked with each other. This study focuses on the location of headquarters of foreign businesses in China but also discusses briefly the impacts and implications of foreign corporations’ headquarters located in Hong Kong.

The survey’s sample targets and framework will be selected from the *Directory of Standing Representative Organizations of Foreign and Territorial Companies in China* (Lotus Trade Centre 2000), compiled and published by the Lotus Trade Center. We have selected 7 categories (out of 18 categories in the directory) of industry and five cities for the analysis—namely, Hong Kong, Beijing, Shanghai, Guangzhou, and Shenzhen—as our sample base. The 7 industries are the most important to the economy in general and most relevant to financial center development in particular (for details on the 7 industries, see the appendix), and the five cities are chosen because they are the major financial centers in the region. There are about 6,000 foreign companies and offices (out of 9,946 in the directory) of the 7 industries in the mainland four cities, of which about 1,000 firms commit in double counting because of overlapping (for any enterprise that has a subsidiary, only one of them is surveyed). So, we shall select 5,000 foreign companies and offices in the mainland and 1,000 in Hong Kong (those companies that do business in China)—a total of 6,000 as our survey sample. This is a twofold investigation: The first part is composed of a locational survey of foreign-owned headquarters; the second part is an investigation of the underlying locational factors.

The survey was conducted by Lotus Trade Centre in Beijing, with the help of some investment banks and financial institutions, including Morgan Stanley Dean Witter and the Hong Kong General Chamber of Commerce in Hong Kong. The Lotus Trade Centre is a Beijing-based and well-established publishing house of business directories that compiles and publishes the *Directory*. The questionnaire survey consisted of in-depth interviews with selected senior officers, chief executive officers (CEOs), and the chief representatives of major banks and MNCs. The questions asked in the survey include general enterprise information, the existing and future office/premise locations in China and Hong Kong, locational preferences for branch/offices in China, and the reasons behind their locational choices. The survey was mainly completed by phone and fax (one set of questions had been set for all interviewees) and was supplemented by some interviews conducted in person. Due to its affiliated relationship with the Ministry of Foreign Trade and Economic

Relations, China's central governing body for trade, the Lotus Trade Centre has the authority to collect data and information from every MNC in China. In other words, every MNC in China is obliged to provide its basic company data to the center. Thus, the response rate of the survey is very high—92%.

The information about locations of foreign firms and offices will be further supplemented by another survey from a global perspective—the survey of regional headquarter locations of 1,000 *Fortune* MNCs in Mainland China and Hong Kong. *Fortune Global 1000* (2000) is an authorized listing of the world's top MNCs ranked by revenue. The existing locations and locational propensity of regional headquarters or the first-level subsidiaries of the world's largest MNCs will provide an indicator of the overall attractiveness of the region for financial center development. This is a Web-based survey, and all of the information sources can be explored from the *Fortune* Web sites and the corporation Web sites of the *Fortune Global 1000* corporations. We have chosen Internet sourcing because it provides accurate and up-to-date information about the locations of such corporations. Again, the Web survey will concentrate on the locations of the highest administrative unit of each surveyed corporation in the five largest Chinese financial centers.

On the other hand, the survey of locational factors involves interviewees from 2,498 foreign corporate headquarters in China. Again, the interviews were conducted by phone and fax, supplemented by some in-person interviews, and the response rate was also as high as 90%. This is because the services and financial sectors in China are just in their “infant” stage. We assume all other factors affecting business locations, particularly noneconomic factors such as expertise, professional know-how, labor forces, banking and financial operation systems, and infrastructure, to be equal among China's major cities, such as Beijing, Shanghai, Guangzhou, and Shenzhen. They are all situated more or less at the same starting point in financial and service sectors development. Rather, we focused on asking the chiefs/CEOs to answer why they had or intended to locate their headquarters in their locating cities, and four locational factors were specifically selected. They are as follows: proximity to the central governmental units in China (factor A), the government's preferential business policies that are designated to the region (factor B), the superior business environment and culture (factor C), and the superior urban infrastructure (factor D). Moreover, two choices of factors, factor A and factor B, are critically designed and planned. In the first place, the designation of factor A is to testify to the spatial effect of “asymmetric information” generated from Beijing, the traditional and contemporary central governmental base in China, as well as the location of the highest administrative organs of state-owned enterprises. It is understandable that Beijing-based corporations can possess spatial advantages in the aspect of gaining better

access to such “regulatory information” that is substantially essential for doing business in China. Apart from Beijing, access to such information becomes weaker, though there are still substantial government agents in the region possessing certain forms of administrative linkages to Beijing. In other words, it implies that factor A is particularly designated to Beijing.

Factor B is specially designated to testify to the spatial effect of the center’s special or preferential business policies that attract MNCs’ headquarters to the region. It particularly refers to Shanghai, as the Pudong District in Shanghai has emphatically developed to be an economic center and a hub for other parts of the country since Jiang Zemin, the party secretary of Shanghai municipality at that time, emphasized this development in 1988 (Zhao 1994). Ten preferential business policies¹ for the development of Pudong were announced when Pudong was declared a special development area on 30 April 1990. In a few coastal open cities (namely, special economic zones [SEZs]), including Guangzhou and Shenzhen, there are also preferential policies similar to those in Shanghai. Therefore, factor B is particularly designated to investigate the impacts of the preferential policy on Shanghai, as well as the coastal open cities of Guangzhou and Shenzhen. The other factors—factor C and factor D—are the two most essential components that are commonly requested to constitute a well-functioning financial center. This part of the survey will investigate which factor is most important to determine headquarter locational preference in the respective city and industry.

FINDINGS: AN OVERALL ASSESSMENT OF REGIONAL DISTRIBUTION OF FOREIGN COMPANIES AND THEIR HEADQUARTERS IN CHINA AND THE UNDERLYING FACTORS

DISTRIBUTION OF FOREIGN-OWNED COMPANIES AND CORPORATE HEADQUARTERS IN CHINA

In All Industries and in Seven Selected Industries

The dominant position of Beijing in agglomerating foreign companies and representative offices compared to the three cities of Shanghai, Guangzhou, and Shenzhen is obviously recognized (see Table 2). Among nearly 10,000 foreign companies of all (18 categories) industries, more than 4,000 firms (44%) located in Beijing, contributing the largest share. Shanghai took the second largest share, but the share was only about half of Beijing’s share. Guangzhou and Shenzhen share 8% and 2% of the total,

respectively, but their shares were not significant when compared to the largest two cities. This figure showed that foreign investment in China was substantially uneven, with Beijing and Shanghai taking up 70% of total foreign company settings in China; however, the part shared by Beijing was larger than that of Shanghai by a substantial margin.

The investigation of seven specific industries shows a similar picture. Whether we focus on the total number of companies or the total number of headquarters of foreign companies, it is obvious that Beijing has a leading and dominant position in foreign business agglomeration. Comparing the four cities, it is possible to make the following observations.

First, in terms of foreign companies, Beijing accounted for the largest share: 44% of the national total. The second largest share was Shanghai, with only 25% of the total establishments. The rest of China, including Guangzhou and Shenzhen, only occupied 31%, still less than Beijing's share (see Table 3).

Second, in terms of the number of foreign corporate headquarters, among the total 2,498 establishments in China, Beijing's share was also overwhelmingly large among China's cities (57%), with Shanghai's share only about half of Beijing's (31%). The shares of Guangzhou, Shenzhen, and other places made up only diminutively more than 10% of the total (see Table 4).

Third, in terms of China's regional headquarters and Pacific-Asia regional headquarters, the central role played by Beijing was also illustrated in foreign business agglomeration. In terms of these two categories, Beijing performed the most significant role (its shares were 62% and 50%, respectively). In comparison, Shanghai not only performed a secondary role but was also lagging far behind Beijing (Shanghai occupied 33% and 40%, respectively), with Guangzhou and Shenzhen occupying only an insignificant part (see Table 5). It is clear that Beijing is dominant in the mainland as a preferred location for foreign business locating its Pacific-Asia regional headquarters there, but Hong Kong has the overwhelming share of headquarters of foreign businesses. In 2001, 944 foreign companies chose Hong Kong as their regional headquarters, an increase of 10.4% compared to the same figures for last year of 855. This reflected the increasing significance of Hong Kong as the hub for regional headquarters of foreign corporations and justified Hong Kong's role as the "information hinterland" with Beijing. Among those headquarters, 83% of them were supervising the business operations in the mainland, and 24% were supervising the business operations in the Pacific-Asia region as a whole (Census and Statistics Department 2001). Consequently, Hong Kong is undisputedly the most important center for locating headquarters of foreign corporations (especially multinational corporations) in China.

TABLE 2: Number of Solely Foreign-Owned Companies and Representative Offices for All Industries in Various Cities by Mid-2000

<i>Industry</i>	<i>Regions (%)</i>					<i>Total Number</i>
	<i>Beijing</i>	<i>Shanghai</i>	<i>Guangzhou</i>	<i>Shenzhen</i>	<i>Others</i>	
1. Advertising, news, gifts, consultancy, information, services	53	27	9	2	9	918
2. Finance, insurance, negotiable securities, law, banks	44	30	8	4	14	593
3. Construction, engineering, decoration, hardware building material, real estate	42	27	10	2	17	642
4. Machinery equipment, processing, and manufacturing industries	44	23	6	1	26	1,220
5. Post and telecommunications, computer, high technology, electronics	46	21	8	3	23	1,366
6. Culture and education, trademark and patent, office equipment, printing and paper making, exhibition	54	28	7	1	10	232
7. Health care, medical products and raw material, biology	49	23	10	< 1	18	407
8. Garments and dress, textile, food processing, tobacco, beverage, and entertainment	36	29	10	< 1	23	631
9. Commerce, trade, investment	42	24	11	2	20	1,156
10. Transportation, freight forwarding, automobile, aviation and space flight, shipping, tourism	35	26	7	3	29	960
11. Chemical industry, metal, plastic, rubber, ceramics, mining industry	41	29	9	2	19	719
12. Instruments and meters, fire-fighting and security equipment, mechanical and electrical industry	42	32	7	1	18	471
13. Animal husbandry, agriculture, aquatic products, forestry	67	14	5	0	14	86
14. Electrical household appliances, articles of everyday use, photograph and equipment	32	28	11	2	27	224

(continued)

TABLE 2 (continued)

<i>Industry</i>	<i>Regions (%)</i>					<i>Total Number</i>
	<i>Beijing</i>	<i>Shanghai</i>	<i>Guangzhou</i>	<i>Shenzhen</i>	<i>Others</i>	
15. Environment protection, energy resources	63	17	4	4	12	284
16. Chamber of commerce, member organization, news organization	60	28	8	4	0	25
17. Business service, maintenance, leasing	40	40	0	0	20	5
18. Other classifications	14	71	0	14	0	7
Total number	4,366	2,557	827	204	1,992	9,946
Percentage share	44	26	8	2	20	100

SOURCE: Compiled from Lotus Trade Centre (2000).

TABLE 3: Foreign Companies in China by Mid-2000

	<i>Number of Companies</i>	<i>(%)</i>
Beijing	2,738	(44)
Shanghai	1,541	(25)
Guangzhou	507	(8)
Shenzhen	141	(2)
Other regions	1,311	(21)
Total	6,238	(100)

TABLE 4: Foreign-Owned Corporate Headquarters in China by Mid-2000

	<i>Number of Headquarters</i>	<i>(%)</i>
Beijing	1,429	(57)
Shanghai	773	(31)
Guangzhou	72	(3)
Shenzhen	41	(2)
Other regions	183	(7)
Total	2,498	(100)

TABLE 5: Number (%) of China and Pacific-Asia Regional Headquarters in China by Mid-2000

	<i>China Regional Headquarters</i>		<i>Pacific-Asia Regional Headquarters</i>	
		<i>(%)</i>		<i>(%)</i>
Beijing	1,419	(62)	10	(50)
Shanghai	765	(33)	8	(40)
Guangzhou	70	(3)	2	(10)
Shenzhen	41	(2)	0	(0)
Total	2,295	(100)	20	(100)

These findings showed a similar picture: namely, that Beijing was overwhelmingly predominant in agglomerating foreign companies/offices in all categories of industry, especially for the seven selected categories that were closely related to the major service, manufacturing, hi-tech, and telecommunications industries. In foreign business agglomeration, Shanghai can only present its secondary role to Beijing, but when compared to the minor role performed by Guangzhou and Shenzhen, Shanghai is still an important financial center in eastern and southern China.

In general, the four cities—Beijing, Shanghai, Guangzhou, and Shenzhen—are altogether controlling the lion's share of China's economy and financial networks. From the findings reported here, the "big four" represented the total of foreign investment in China, with 79% of total foreign company establishments and 93% of total headquarter establishments in the seven categories. Among the big four, the largest two were Beijing and Shanghai, with an agglomeration of 69% of total foreign companies and 88% of total headquarters in China.

In the Service and Manufacturing Sectors

The regional distribution of foreign businesses in the seven particular industries can be shown clearly in Table 6. Among the seven industries, categories I, II, V, and VII are in the "service sector," whereas categories III, IV, and VI are in the manufacturing, hi-tech, and telecommunications sectors. For illustrative purposes, we have arranged the seven industries into two groupings, but whether we look at the either sector, Beijing remains the preferred location for foreign companies and headquarters offices.

In the service sector, 46% of the 2,692 total foreign company establishments in China located in Beijing. Shanghai came second with 27%, which was approximately the share of the rest of China, including Guangzhou and Shenzhen (28%). In the same grouping, Beijing also presented an overwhelming dominance (58%) in foreign companies' headquarters in China; Shanghai came second with 31%, and Guangzhou and Shenzhen have an insignificant score. Again, the two cities of Beijing and Shanghai were the homes for more than 70% of the nation's total foreign companies and headquarters.

The manufacturing sector also shows a similar pattern. Beijing, with 42%, was superior in agglomerating foreign companies. Shanghai, with 23%, and Guangzhou and Shenzhen had a negligible amount. It is important to observe, however, that the role of "other regions" (26%) in this grouping of industries surpasses that of Shanghai, showing that companies in the manufacturing sector had spread more in geographical terms (hence, they are more diversified). However, for the spatial spread of headquarters, Beijing and Shanghai remain the most favorable locations (56% and 30%, respectively). It is worth noting that Beijing is superior to Shanghai in agglomerating manufacturing firms by a substantial margin, despite the common perception that Shanghai is China's largest industrial and manufacturing hub.

TABLE 6: Number (%) of Foreign Companies and Headquarters of Service and Manufacturing Sectors in China by Mid-2000

<i>City/Industrial Sector</i>	<i>Service^a</i>				<i>Manufacturing^b</i>				<i>Total</i>			
	<i>Companies</i>	<i>(%)</i>	<i>Headquarters</i>	<i>(%)</i>	<i>Companies</i>	<i>(%)</i>	<i>Headquarters</i>	<i>(%)</i>	<i>Companies</i>	<i>(%)</i>	<i>Headquarters</i>	<i>(%)</i>
Beijing	1,247	(46)	657	(58)	1,491	(42)	772	(56)	2,738	(44)	1,429	(57)
Shanghai	714	(27)	357	(31)	827	(23)	416	(30)	1,541	(25)	773	(31)
Guangzhou	260	(10)	37	(3)	247	(7)	35	(3)	507	(8)	72	(3)
Shenzhen	68	(3)	13	(1)	73	(2)	28	(2)	141	(2)	41	(2)
Others	403	(15)	77	(7)	908	(26)	118	(9)	1,311	(21)	183	(7)
Total	2,692	(100)	1,141	(100)	3,546	(100)	1,369	(100)	6,238	(100)	2,498	(100)

a. Service sector includes industry categories I, II, V, and VII (see appendix).

b. Manufacturing sector includes industry categories III, IV, and VI (see appendix).

TABLE 7: Distributions of Foreign Bank Branch^a and Representative Offices of Foreign Institutions^b in China (1998)

	<i>Number of Foreign-Owned Bank Branches</i>		<i>Number of Representative Offices</i>	
		(%)		(%)
Beijing	16	(11)	122	(44)
Shanghai	45	(30)	68	(25)
Guangzhou	15	(10)	23	(8)
Shenzhen	23	(15)	10	(4)
Other regions	53	(35)	54	(19)
Total	152	(100)	277	(100)

SOURCE: Compiled from Association of China's Finance and Banking (1999).

a. Solely foreign owned.

b. Solely foreign owned or foreign-China joint venture.

In the Banking Sector

The administrative status of Beijing can be further emphasized by official data in the financial sector. Table 7 is compiled from the official data from the *Almanac of China's Finance and Banking* (Association of China's Finance and Banking 1999) and shows the number of foreign bank branches and representative offices of financial institutions among the four cities in China. In terms of bank branches, Shanghai had 30% of the total, ranking number one, whereas Shenzhen had 15%, Beijing had 11%, and Guangzhou had 10%, ranking second, third, and fourth, respectively. This finding shows that Shanghai remains the largest financial retailing outlet in China.

However, in terms of the representative offices of foreign financial institutions, which are on a higher level in the hierarchies of institutions, Beijing was the most popular choice (44%), whereas Shanghai accounted for only 25%. The shares of Guangzhou, Shenzhen, and the rest of China altogether were only 31%, even less than those for Beijing alone. This finding shows that Beijing is already in a leading position in terms of agglomerating the administrative foreign financial settings in China.

The findings in sectoral distribution lead to a profound consideration: Shanghai has been China's traditional industrial and manufacturing center for the past century. The city has been designated as China's number one financial center and is even supposed to become Asia's number one financial center, taking over Hong Kong's position in the near future. However, we need more information before we can predict or speak with confidence on the reasons why most foreign companies and offices choose to agglomerate in Beijing rather than Shanghai. In the financial services—the manufacturing and service sectors in general and the hi-tech and telecommunications

industries in particular—Beijing gains its superiority as the most favorable location for foreign companies in China.

GLOBAL PERSPECTIVE OF HEADQUARTER LOCATION IN CHINA

HONG KONG'S ROLE IN FOREIGN BUSINESS IN CHINA

A tight business relationship between Hong Kong and China can also be observed (see Table 8). About one-third of the headquarters of foreign-owned companies in China have senior-level administrative offices in Hong Kong. Moreover, among the upper offices, nearly 90% of them function as China–Hong Kong headquarters. This reflects the fact that a substantial number of foreign companies still like to use Hong Kong as springboard for opening up China's business. It shows a strong relation between Hong Kong and China, as well as Hong Kong's significant role for China's economic development.

In fact, information and capital flows between the mainland (especially Beijing) and Hong Kong are frequent and huge in volume. By November 2000, more than 6,000 companies in Beijing were set up by Hong Kong businesses, and their investment volume amounted to 115 billion Hong Kong dollars. They accounted for 39% of the total establishments of foreign-domestic joint-venturing corporations and 50% of total investment volume in Beijing, making Hong Kong the largest incoming investor in the capital (Gansheng touji Beijing 2000; Guoji jinrong gikou zhai gang qidang 2000). Furthermore, in regard to Hong Kong–mainland business relation, it is interesting to note that not all the Hong Kong offices function as the upper-administrative office to the mainland offices. One of the notable examples is the International Monetary Fund (IMF), which has its regional headquarters in Beijing and a branch office in Hong Kong. By and large, a tight business relationship between the mainland and Hong Kong is clearly recognized.

DIFFERENT ROLES OF BEIJING AND HONG KONG IN CHINA'S INFORMATION HINTERLAND

From the data collected in Table 9, when comparing among Hong Kong, Beijing, Shanghai, Guangzhou, Shenzhen, and the rest of China, Hong Kong has the largest cluster of local/regional offices of the top *Fortune* 500 corporations (in other words, the 500 largest U.S.-based corporations in terms of revenue). Of the local/regional offices in China, 40% were concentrated in Hong Kong. Also, Hong Kong is the place for Pacific-Asia headquarters

TABLE 8: Number of Foreign-Owned Corporate Headquarters Having Upper-Administrative Offices in Hong Kong (in Seven Selected Industries) by Mid-2000

Industry/ Headquarters	Foreign-Owned Corporate Headquarters in China (Total)	Headquarters Having Upper Offices in Hong Kong (Total)	Administrative Function	
			China– Hong Kong Regional Headquarters	Pacific-Asia Regional Headquarters
I	446	134	119	16
II	169	75	68	8
III	582	123	112	16
IV	492	163	149	22
V	501	168	149	25
VI	295	111	98	19
VII	13	2	2	0
Total	2,498	776	697	106

TABLE 9: Number (%) of Headquarters/First-Level Subsidiaries of Fortune 500 Companies in China (2000)

Region	Regional/ Local		China Regional		Pacific-Asia Regional		Total
	Office	(%)	Headquarters	(%)	Headquarters	(%)	
Hong Kong	57	(40)	28	(30)	17	(94)	102
Beijing	25	(17)	34	(37)	0	(0)	59
Shanghai	25	(17)	19	(21)	1	(6)	45
Guangzhou	11	(8)	5	(5)	0	(0)	16
Shenzhen	8	(6)	0	(0)	0	(0)	8
Others	17	(12)	6	(7)	0	(0)	23
Total	143	(100)	92	(100)	18	(100)	253

SOURCE: Compiled from *Fortune* 500 (www.fortune.com/fortune/fortune500/).

NOTE: For a single company, more than one office may be counted among the selected regions. Also, when the headquarters and the first-level subsidiary of the same multinational corporation locate in the same region, only one is counted; when the multiple first-level subsidiaries locate in the same region, also only one is counted.

agglomeration, with 94% of them set up in Hong Kong. But in terms of headquarters for China, more *Fortune* 500 corporations had chosen Beijing as the business base over Hong Kong (Beijing had 37% of the total, whereas Hong Kong only had 30%). In the same category, Shanghai ranked third, followed by Guangzhou and Shenzhen.

TABLE 10: Number (%) of Headquarters/First-Level Subsidiaries of *Fortune* Global 500 Companies in China (2000)

Region	<i>Regional/ Local</i>		<i>China Regional</i>		<i>Pacific-Asia Regional</i>		Total
	Office	(%)	Headquarters	(%)	Headquarters	(%)	
Hong Kong	89	(40)	38	(26)	15	(100)	142
Beijing	36	(16)	71	(48)	0	(0)	107
Shanghai	35	(16)	29	(19)	0	(0)	64
Guangzhou	15	(7)	5	(3)	0	(0)	20
Shenzhen	4	(2)	0	(0)	0	(0)	4
Others	46	(20)	6	(4)	0	(0)	52
Total	225	(100)	149	(100)	15	(100)	389

SOURCE: Compiled from *Fortune* 500 (www.fortune.com/fortune/fortune500/).

NOTE: For a single company, more than one office may be counted among the selected regions. Also, when the headquarters and the first-level subsidiary of the same multinational corporation locate in the same region, only one is counted; when the multiple first-level subsidiaries locate in the same region, also only one is counted.

The investigation of the headquarter locations of *Fortune* Global 500 corporations in China showed many aspects of the same trend (see Table 10). Hong Kong had the highest share of all local/regional offices (40%) and Pacific-Asia regional headquarters (100%). However, in terms of the agglomeration of China headquarters, Beijing was the most preferred location (48%), with Hong Kong's share only about half of Beijing's (26%) and Shanghai having even less (19%). Guangzhou and Shenzhen ranked fourth and fifth, respectively; their shares were relatively insignificant.

These findings indicate that despite Hong Kong being the preferred place for establishing Pacific-Asia business bases, its attractiveness of being the location for the headquarters of business in China is still inferior to Beijing's. In our finding, more top global corporations, especially the MNCs from the United States, prefer to set up headquarters in Beijing to conduct their China business rather than in Shanghai. This finding contradicts the prevailing public perceptions. In our assertion, Beijing is the most likely city to be developed as an international financial center, as well as a global city. In the near future, if China is able to develop a better economic infrastructure and encourage more business opportunities, Beijing will present a potential threat to Hong Kong as the chief financial center for the country, even for the Pacific-Asia region.

FACTORS DETERMINING DECISIONS OF LOCATING HEADQUARTERS

The above findings suggest that Beijing and Hong Kong are the chief financial centers within the information hinterland of China presently and will probably remain in their positions for the immediate future. It is obvious that Beijing has overtaken Shanghai—a traditional industrial and commercial base—as the largest agglomeration of economic activities in the country. We suggest that this is because Beijing is traditionally the central governmental base in China. It is well known that Beijing-based corporations have spatial advantages in the sense that they have better access to “regulatory information,” which is essential for doing business in socialist China. The further the one moves from Beijing, the more difficult it becomes to gain access to such information, even though there is quite a number of government agencies in the region with administrative linkages to Beijing. The preferential and special business policies pursued in Shanghai may help to explain the common misconception about the geography of finance in contemporary China. However, despite the preferential business policies that have existed in Shanghai since the early 1990s, Shanghai still lags behind Beijing in attracting foreign business to locate their “China headquarters.” The following empirical analysis further supplements the above findings by investigating the factors that are the most likely to determine locational decisions of headquarters of foreign companies in China.

As Table 11 shows, in different cities, different factors are considered in the locational decision of individual foreign corporations. For instance, in Beijing, 37% of “selections” were based on the proximity to the central policy-making unit (factor A). This implies that the city is chosen as a location of corporate headquarters because of the efficient access to regulatory information, which should be helpful for doing business. In addition, a substantial portion of locational decisions are made on the basis of business culture and environment (factor C) and urban infrastructure (factor D) (with 24% and 22%). On the other hand, preferential business policies pursued in the region (factor B) is the least likely factor to be selected, making up only 17% of the total. In sum, these findings are consistent with our early findings that Beijing, as the location of the highest governmental and administrative units, has a built-in advantage by virtue of its “regulatory” function, something that is of the most significance for attracting foreign investment into China.

On the other hand, the locational factors chosen by the Shanghai-based interviewees show a very different pattern. The accessibility variable (the proximity to the central policy-making unit [factor A]) is the least likely to be identified, with only 11% of the “selections” from the Shanghai-based

TABLE 11: Weighing of Different Factors of Locating Corporations' Headquarters, by City (2000)

<i>City/Factor</i>	<i>A</i>		<i>B</i>		<i>C</i>		<i>D</i>		<i>Total</i>	
	<i>n</i>	<i>(%)</i>	<i>n</i>	<i>(%)</i>	<i>n</i>	<i>(%)</i>	<i>n</i>	<i>(%)</i>	<i>n</i>	<i>(%)</i>
Beijing	436	(37)	202	(17)	285	(24)	256	(22)	1,179	(100)
Shanghai	52	(11)	77	(16)	173	(36)	177	(37)	479	(100)
Guangzhou	12	(15)	7	(9)	35	(43)	27	(33)	81	(100)
Shenzhen	11	(24)	9	(20)	14	(30)	12	(26)	46	(100)

NOTE: Choices of locational factors are as follows: A = The geographic location is in proximity to the central policy-making unit, which is advantageous to business development. B = The business policies pursued by the government of the People's Republic of China for sustaining regional economic development. C = An ideal business environment in the region. D = Better infrastructure and overall environment in the region than those in other regions.

corporations. This implies that, in general terms, Shanghai does not possess the sort of spatial advantages that would be beneficial to its business. In contrast to Beijing, the city's infrastructure (factor C) and business environment (factor D) are the two most important inherent advantages that Shanghai possesses and are detrimental to the establishment of headquarters. The combined factors add up to more than 70% of the total. The remaining 16% of the "selections" chosen by the corporations were associated with preferential business policies (factor B), which was similar to the case in Beijing. This implies that preferential policies specially designated to attract foreign corporations to Shanghai may not have much actual impact on the business leaders of foreign-owned enterprises in China.

We can find a similar pattern in Guangzhou. Most interviewees who were based in Guangzhou felt that the business environment (factor C) in the city was the most important factor in determining the decision-making process (43%). The infrastructure (factor D) in the city, which ranked second, also made up a substantial part of the pattern, as 33% of the foreign enterprises in Guangzhou chose this option. On the other hand, because Guangzhou seldom functions as a policy-making center, very few Guangzhou-based corporations locate their headquarters there, presumably for the reason suggested above (see factor A). It is also clear that preferential business policies (factor B) were the least significant consideration for locating headquarters in Guangzhou, with only 9% of the total. Although the Lotus Trade Centre has long emphasized economic development by pursuing several special business policies, it cannot effectively determine the channeling of foreign investment to the region.

In another city in the Guangdong province, Shenzhen, the share of the four locational factors was spread more evenly than in the other three cities. This suggests that, similar to its neighboring city, Guangzhou and Shenzhen are also attractive cities for locating headquarters because of their business environment (factor C) and infrastructure (factor D). The two factors constituted 30% and 26% of the total selections in Shenzhen. The third ranked factor is the city's proximity to the central policy-making unit (factor A), and the fourth ranked is the preferential business policies (factor B) that are pursued in this city. Although these two factors are not highly ranked, they are clearly important in making decisions to establish headquarters in Shenzhen.

In summary, most of the Beijing-based foreign corporations locate in the capital mainly to take advantage of its proximity to the central policy-making unit. This implies that most of these corporations should be sensitive to regulatory information that is offered by the Lotus Trade Centre (Beijing). It is obvious that this factor is not significant in the other three cities because they do not (or seldom) perform such a regulatory function. Instead, as most interviewees mentioned, these cities are chosen as the location of corporations because of the infrastructural advantages and generally positive business environments, rather than the preferential policies pursued there. This implies that the preferential policies designated by the central government do not effectively motivate businesses to locate their headquarters in the SEZs or the Free Trade Area, particularly in Shanghai. In other words, it is believed that the entire issue of locational decision making needs to be reexamined and reevaluated by policy makers and other researchers.

Table 12 shows the weighting of factors, which are chosen by foreign-owned corporations in the seven industrial sectors. It shows that different factors can affect the decision of locating headquarters in China, depending on the types of industry. In general, for all seven industries, the factors of proximity to the central policy-making unit (factor A), business environment (factor C), and infrastructure (factor D) were dominant, representing 29%, 28%, and 26% of the total, respectively. These three factors represented more than 80% of the total, whereas preferential business policies (factor B) only had 17% of the share. This implies that regional business policies in China do not appear to determine the locational decision making of corporations.

Among the four major factors, factor A (proximity to the central policy-making unit) makes up the largest part of the composition. In terms of investigating the individual categories, factor A made up more than 30% of the total "selections" of the respective industries of commercial and financial sectors (categories II and V), telecommunications and hi-tech industries (category IV), and transportation and heavy industry (category VI). As for the service and information industry (category I) and manufacturing industry (category

TABLE 12: Weighing of Locational Factors of Foreign Corporations' Headquarters in China, by Industry (2000)

<i>Industry/ Factor</i>	<i>A</i>		<i>B</i>		<i>C</i>		<i>D</i>		<i>Total</i>	
	<i>n</i>	<i>(%)</i>	<i>n</i>	<i>(%)</i>	<i>n</i>	<i>(%)</i>	<i>n</i>	<i>(%)</i>	<i>n</i>	<i>(%)</i>
I	156	(24)	95	(15)	204	(32)	189	(21)	644	(100)
II	45	(34)	23	(18)	36	(27)	27	(21)	131	(100)
V	81	(33)	44	(18)	60	(25)	57	(24)	242	(100)
VII	1	(6)	1	(6)	11	(65)	4	(24)	17	(100)
III	78	(27)	49	(17)	79	(27)	86	(29)	292	(100)
IV	89	(30)	50	(17)	82	(28)	75	(25)	296	(100)
VI	61	(37)	33	(20)	35	(21)	34	(21)	163	(100)
Seven industries	511	(29)	295	(17)	507	(28)	472	(26)	1,785	(100)

NOTE: For definitions of factors, see Table 11.

III), factor A was not ranked first in locating headquarters, though it still appeared to play an important role in determining the decision of the location. For these two industries, this factor accounted for a 24% and 27% share, respectively. This demonstrates again that the convenient accessibility of "regulatory" information is essential to most of the business in China and thus implies that Beijing has the upper hand in attracting foreign investment in China.

Among the seven industries, only category VII involves the activities of the chamber of commerce and related organizations. The locational preference had been dominated by factor C (business environment), which had recorded a share of 65%. It is reasonable to conclude that an ideal business environment fosters and sustains healthy business. In this industry, factor D (infrastructure) was also significant, with 24% of the total. These two factors are also significant for other industries and in fact appear to be important for all seven industries in determining locational decision making. It is important to note that factor B (regional business policies) does not seem to play an important part in locational decision making. Similar to the conclusion drawn earlier, it is apparent that preferential business policies cannot effectively determine the locational decisions of foreign corporations.

To summarize the above findings, it is obvious that foreign corporations in China are more likely to locate in close proximity to the central governmental unit. This is consistent with our proposition that gaining access to regulatory information is of utmost importance when foreign companies decide to locate in socialist China. It is also consistent with the earlier findings that Beijing, as the center of governmental power, has the highest density of

TABLE 13: Comparison of Cost of Living in Selected Cities

<i>Ranking in 2001</i>	<i>Ranking in 2000</i>	<i>Cities</i>
1	1	Tokyo, Japan
3	4	Hong Kong, China
5	8	London, United Kingdom
7	7	New York City, United States
9	12	Singapore, Singapore
10	16	Beijing, China
14	16	Shanghai, China

SOURCE: Compiled from The Economist Intelligence Unit (2000, 2001).

headquarters of government departments and higher administrative units. Another two factors, superior business environment and urban infrastructure, are also attractive to foreign corporations. These two factors are effectively significant in Shanghai and Beijing, which have only weak linkages with the central government. Within China, only Beijing has the ultimate spatial advantage of being able to generate and process regulatory information. This explains why Beijing's leading financial status remains "unchallengeable," even as the leaders of China from the center intend to develop Shanghai as the national number one financial center.

NONECONOMIC FACTORS

There are some noneconomic factors affecting the locational choice of headquarters. These noneconomic factors, such as infrastructure, expertise, and professional know-how, as mentioned earlier, are assumed to be equal among all Chinese cities because service and financial sector development is just in their initial stage. Although most noneconomic factors do not account for the measurement of the spatial restructuring of financial centers in China, the cost of living is an exception. Although it is highly perceived that Hong Kong has one of the highest costs of living for expatriates in the world, and although Hong Kong is ranked the world's 3rd most expensive city (just after Tokyo and Osaka of Japan) by the twice-yearly survey conducted by the Economist Intelligence Unit, it does not mean that Beijing and Shanghai have a low cost of living. As the result, the survey ranked Beijing 10th and Shanghai 14th (see Table 13). Consequently, although Beijing and Shanghai do have a relatively low cost of living compared to Hong Kong as a whole, both of them are actually situated at the same cost-of-living level for expatriates compared to Hong Kong and other "world cities" such as Singapore, New

TABLE 14: Ranking of Hong Kong and China in the Index of Economic Freedom of Various Years

<i>Year</i>	<i>Hong Kong</i>	<i>China</i>
2000	1	100
2001	1	114
2002	1	121

SOURCE: Compiled from Heritage Foundation (2000, 2001, 2002).

York, and London; both of them have shown an increase in their cost of living (especially Beijing). As a result, Beijing and Shanghai are not necessarily superior to Hong Kong in terms of cost of living with reference to location of headquarters of MNCs.

Another major indicator of the noneconomic factors affecting the restructuring of financial centers is the *Index of Economic Freedom*, compiled and published annually by the Heritage Foundation, a world-renowned think tank based in Washington, D.C. The index quantifies economic, noneconomic, and institutional indicators on every nation in the world. These indicators include the level of income and corporate taxation; government expenditures and government intervention in the economy; the level of openness of the government in terms of its trade, monetary, finance, and wage policies; the level of protection of property rights and capital flow; and the level of corruption and other black market practices. In short, it provides a comprehensive overview of the competitiveness and openness of a place in the world. Hence, it could serve as an important criterion for financial center development. Table 14 indicates the ranking of Hong Kong and China between 2000 and 2002.

Hong Kong has been maintaining the top position in this three-year span, indicating a state of almost full economic freedom, but in China, the ranking has declined from 100th in 2000, to 114th in 2001, and finally to 121th in 2002. This indicates that China is worsening in its openness toward the world economy. Although Hong Kong has been crowned as the "world's most free city in economic freedom," this indicates that Hong Kong is still the true "global city for business" in the region. China's low ranking in the index also indicates that its development of financial centers is still in the primitive stage of development. Therefore, it justifies our assumption mentioned earlier that all other factors, whether economic or noneconomic, are about the same among China's major cities due to their "infant" stage of development in the financial sector.

Perhaps the most important institutional factor influencing China's financial center development could be China's landmark accession to the WTO in 2001. The entry to the WTO implies that MNCs and FDI will play a much more significant role in China's financial markets. Along with the big surge of trade volume and FDI, the immediate implication of China's WTO accession is the creation of three "grand waves": The first is a grand wave of business and investment in the manufacturing, telecom, Internet, and IT sectors. The second is the grand wave of business and investment in the financial and service sectors. The third is the grand wave of government policy, rules, and regulations (for details of these three waves and their justification, see Zhao, Tong, and Qiao 2002).

As the three grand waves are in essence the waves of information flows (news, business deals, regulatory policy and rules, etc.), the most immediate implication is that the volume of information will literally explode, effectively establishing a new information hinterland and several heartlands in China. The second and the third waves directly demand massive and immense services of financial centers. The spatial impact of these three waves shall result in a set of new national financial and service centers, with one being the number one or dominant. Thus, China's WTO accession will provide a starting point for major Chinese cities to compete for the first position of the new financial and service centers. The question of where this financial center will be would be better answered by asking another question: Where would the headquarters of MNCs be most likely to locate? This study, by focusing on the regional distribution of corporate headquarters in China, particularly the foreign-owned ones, will offer some insightful indications.

OVERALL IMPLICATIONS OF THE FINDINGS

With China's successful WTO accession and its induced emergence of the three grand waves, it is foreseeable that the process of agglomeration of corporate headquarters, particularly for those financial ones, to Beijing via Hong Kong will be accelerated (Hong Kong will still be China's most important gateway and springboard). As a result of this process, a new pattern of China's information hinterland and heartland will most likely be born or emerge. This new pattern (see Figure 1) will determine the spatial development or restructuring of China's financial systems, including Hong Kong. As shown in Figure 1, the area between Hong Kong and Beijing presents an information-rich hinterland, and the axis connecting the two cities will form a super-information corridor, with Hong Kong and Beijing serving as the information heartlands. The two economies will appear to be more interdependent,



Figure 1: Hong Kong–Beijing–Hong Kong Information Corridor and China's New Information Hinterland and Heartlands After China's Accession to the World Trade Organization

with information and capital flows being more intense, frequent, and huge in volume. Thus, with China's historical accession into the WTO, Hong Kong and Beijing look likely to become China's primary financial centers, whereas Shanghai might, in relative terms at least, benefit less from the financial center restructuring induced from China's WTO accession. The impacts on the Guangdong cities of Guangzhou and Shenzhen are most likely to be neutral. Shanghai does not locate in the center of the new round of information explosion. However, due to the positioning and designation from the Chinese government, Shanghai will continue to play an important role in China's overall economic development, including the development of financial centers.

Hong Kong seems likely to benefit greatly from its "path dependence" and the "thickness" and "richness" of the financial information, and it will advance its dominance in financial and service industries. It will maintain itself as an important center of trade, transportation (port and airport), and tourism. In the global context, Hong Kong will possibly grow into the world's top international financial center, after New York and London, Frankfurt, and Tokyo. Within China, Hong Kong might well rise above Shanghai and increasingly become the most important domestic financial center for China.

Currently, Hong Kong houses several hundred H-share companies (state-owned enterprises in China) and red-chip companies (companies originating from China that operate their businesses in Hong Kong). With listings in Hong Kong's stock market, China's largest and most important companies may be able to serve as "window" companies for both central and provincial/local governments. Hong Kong will continue its advancement and prestige in finance and increasingly become the chief listed stock market for China's major companies and corporations. This is evidenced by the fact that the Hong Kong Stock Exchange houses the absolute majority of Chinese stocks listed overseas; includes renowned companies such as China Unicom, China Mobile, and Sinopec; and is equivalent to one-tenth of the total number of stocks listed in the domestic stock exchanges and a quarter of the total market capitalization. At the same time, Hong Kong has always been the single largest investor in China, as FDI from Hong Kong alone has been continually accounting for 60% of the total of China's FDI inflow from the early 1980s to the early 1990s and continues to contribute half of total FDI inflow of China from the early 1990s onwards. Foreign investments, as a whole, have accounted for 35% of China's gross domestic product (GDP) in the past decade. Therefore, Hong Kong has always been an important engine of economic growth and transformation for China as a whole. As it has benefited from being the world's focal investment and trade in Southeast Asia for the past 30 years, Hong Kong will most likely continue to benefit from the new round of the world focal investment and trade in China, induced by its WTO accession, for the next 30 years.

Beijing seems to benefit greatly from the explosion of its "regulatory" information and will most likely become one of the most important information heartlands in the foreseeable future. It is not entirely impossible for Beijing to take over Shanghai's current predominant position and to emerge as China's number one financial center. Thus, it is reasonable to predict that in addition to its supreme political status, Beijing will also likely become China's most important financial center in the future. The rapid development of Beijing's Financial Street, as well as Chaoyang District, has long attracted many domestic and international banking firms and foreign firms from other sectors to establish regional headquarters offices there. Beijing traditionally has been the chief political center for the nation, and its financial sector is of no exception. China's central governing bodies for finance, securities, and insurance are all in Beijing and are mostly located in the city's Financial Street. For example, the China Securities Regulatory Commission and the China Insurance Regulatory Commission, the headquarters of the People Bank (China's central bank) as well as the four major industrial and commercial banks, China International Capital Corporation (China's first and largest

investment bank joint ventured by China's Construction Bank and Morgan Stanley Dean Witter), the Everbright Securities (one of the largest stock brokerage firms in China), and many other financial institutions and organizations all cluster in this area. Furthermore, by 1999, Beijing had already become the home of headquarter offices for 6,000 foreign corporations, including the largest MNCs in the world (companies appeared in the *Fortune* 500 and Global 500 list). Beijing is also the home for most headquarters of red-chip and H-share companies (China's largest companies listed in Hong Kong and overseas stock markets; most of them are subsidies or affiliations to the State Council and various central governmental ministries). In the near future, because of the city's regulatory and governmental functions, it is likely that Beijing will surpass Shanghai as the largest financial center of the nation. In the long run, Beijing may also present a real challenge to the position of Hong Kong as the chief global financial center in China, as the findings above suggested.

As noted earlier, Shanghai may be overshadowed by other cities in the competition for economic and financial supremacy. In terms of the information requirement for establishing a number one national financial center, Shanghai seems unlikely to be able to benefit greatly from China's accession to the WTO. Although it will benefit from an expansion of its textile production and exports, as well as high value-added and large-scale manufacturing such as cars and the airplane industries, it is becoming increasingly clear that the dominance of the manufacturing sector in a city will not be important for China's future financial center development. Although one of the biggest stock markets in China is currently located in Shanghai, the physical location of the stock market will no longer be important in this Internet era. For example, the virtual stock market of NASDAQ has increasingly challenged the New York-based Dow Jones Stock Exchange. Shanghai has obviously suffered from the loss of its significance in China's financial development, in addition to which it only has a minor role in terms of regulatory/governmental functions. It has also been undermined as China's number one merchandise trading hub, mainly because of the natural constraints associated with its development as a large-scale container port. As both requirements are crucial for China's information and trading sector developments, it is reasonable to anticipate that Shanghai may benefit less from China's entry into the WTO as compared to Beijing because Beijing possesses the sources of the acquisition of regulatory information and other nonstandardized information the foreign businesses need. It is difficult for Shanghai to find firsthand reliable regulatory information from the central government, and there is a lack of correct channels to interpret nonstandardized information such as rumors. This disadvantage or weakness of Shanghai is quite critical, as MNCs are

increasingly led by the knowledge-based and information-rich economy (Dunning 1998). Second, as the key focus of the developmental area in China's WTO accession shall be on the financial and service sector, Shanghai, which is a traditional and contemporary manufacturing center, is likely to profit less from China's WTO accession than the academics and businesspeople worldwide have been anticipating. Also, compared to Beijing, it suffers from a lack of development in transportation and hi-tech industries, such as IT and telecommunications, which will continue to be the most strategic and lucrative sectors in the new millennium.

Shanghai also suffers from the unprecedented bust of its real estate development, which has severely undermined the city's financial vitality in terms of both municipal government fiscal ability and private-sector financial strength. Shanghai's average annual output of completed office buildings (1991-1995) was equivalent to that of the 10 years' output of Hong Kong during the 1980s. In just an 8-year span, from 1991 to 1998, Shanghai's total stock of office buildings exceeded what Hong Kong had built in the past half century. As a result, the vacancy rate in Shanghai is extremely high—in Pudong, it was 60% (all grades) in 1996, and 73% (all grades) and 70% (prime) in 1997, which suggests one of the world's largest real estate "bubbles" (Haila 1999; Jackson 1997). Shanghai also suffers from long-term strict central control, which so far has not been relaxed much. Meanwhile, Shanghai has been long known for its famous "Shanghainese culture": When Shanghainese deal with non-Shanghainese, they will assume a "sure-win" situation for themselves and a corresponding "sure-lose" situation for the counterparts. In many situations, Shanghainese businessmen are regarded as being too "smart" or too "skillful"; in fact, they are often criticized as being too "cunning." This unique aspect of Shanghainese culture will impose a long-term negative effect on the general business environment in Shanghai. In addition to Hong Kong's and Beijing's domination in the nation's financial and regulatory landscapes, the adverse business culture in Shanghai partially suggests at least, if not in full, why so many foreign big corporations choose to set up their regional headquarters in Hong Kong and Beijing.

CONCLUDING REMARKS

The newly emerging discipline of the geography of finance addresses the importance of information flows in modern financial center development. The theories on information externalities, asymmetric information, and information hinterland/heartland help to explain the underlying forces behind the location and agglomeration of head offices of MNCs and banking

and financial institutions. The new subdiscipline provides a better account of the formation of financial center systems, including the new growth of a particular center and the possible rise and fall in relative importance of regional urban areas. China's landmark WTO accession will certainly have a tremendous impact on China's economic development and its information landscape. It will also transform China's information hinterland and induce profound organizational and spatial restructuring of the financial systems in the mainland as well as in Hong Kong. From the perspective of the geography of finance, this study has assessed the impact of these possible changes—the changes in information flows, information hinterland/heartland, and hence the financial system—on the spatial structure of the landscapes of finance associated with China's accession to the WTO.

On the basis of the head office survey of about 5,000 foreign companies and offices in seven major industries, as well as the locational survey of *Fortune* 500 and *Fortune* Global 500 corporate subsidiaries in Mainland China and Hong Kong, this study reveals some striking findings that may come as a surprise to policy makers in Mainland China. Proximity to central policy-making units appears to be the most significant factor. In other words, the location of China's central government apparatus is very influential. That is why Beijing is overwhelmingly favored by foreign companies as their head office locations in the secondary level within the mainland, whereas Hong Kong is fulfilling a similar function for Pacific-Asia business development. Beijing excels in the category of regulatory information flows, whereas Hong Kong is paramount in the case of financial and, to some extent, trade information flows. Both flows of information, particularly the regulatory type in Beijing, imply that huge profits can be made under the assumption that the new information can be correctly interpreted. This requires regional head offices of MNCs in general and financial firms in particular to be close to the sources of the information, so they can understand the background or culture of the information.

More specifically, the findings of this study maintain that in the process of China's accession to the WTO, Hong Kong and Beijing will become among the largest international and national financial centers. Furthermore, Hong Kong, together with its neighboring cities (e.g., Guangzhou and Shenzhen), will advance as the largest financial center in the Asia-Pacific Rim and as an important node in the international money landscape. Beijing, rather than Shanghai, will become the largest financial center in the mainland with its dominant policy-making and regulatory functions due to its higher administrative capability. It will continue to be the most desirable place for the MNCs to set up their head offices in the mainland. Shanghai, on the other hand, will become (or remain as) the largest industrial and commercial trade center in

China because of the presence of many large production bases of corporations, as well as its century-long tradition of manufacturing and export and its continuing ability to attract a large number of foreign manufacturing investors. However, in terms of the development of a national financial center, it is interesting to raise the question about whether China's top leaders, such as Premier Zhu Rongji, and those central policy makers in the financial sector will be forced to change their original assumption that Shanghai will be China's number one financial center. They may indeed need to reconsider their original policy and positively develop Beijing as China's national number one center. In addition, maybe the newcomers of MNCs should also reconsider the location of their headquarters when entering China's vast market, following China's WTO accession.

However, I would like to stress that it is dangerous to generalize this Chinese model of spatial development of financial and service centers. It is definitely different from the Western model, and the key difference lies in the extent and pervasiveness of the state control and the openness and transparency of the systems. Although both Chinese and Western models prioritize the role of information (externalities and asymmetric nature), the Chinese state, with its overwhelming controls over its economy and society and with its relatively untransparent system, could control and regulate information. This has exacerbated the role of asymmetric information and has much more impact to service and financial industries in general and MNC headquarter locations in particular. The finest example can be seen in the format of the stock exchange market. A stock exchange market is normally constituted by three functions: listing approval and monitoring, stock trading/transactions, and the central registry of stock. In Western or market systems, all three functions are housed within the stock exchange market (under one building physically). However, the Shanghai Stock Exchange in China only holds the middle function—the stock trading/transaction—with the other two more important functions held in Beijing by the China Securities Regulatory Commission, which is the central government's ultimate governing body. That is why Beijing appears to be so predominant in terms of attracting MNC headquarters. Nevertheless, this Chinese model is definitely applicable to the former socialist systems and developing countries with totalitarian and untransparent regimes.

This study has spelled out one exciting and profound meaning in theoretical contexts: the power of the geography of finance—a very new discipline or subdiscipline that crosses economics, finance, geography, and information technology and that can interpret and explain the spatial restructuring of financial centers in modern times. This study has also created tremendous room for the further development of the geography of finance. With the

recognition of the power of information as a new determinant for economic and financial development and with the approach of the information hinterland and heartland, a more comprehensive theoretical framework and applicable analytical modeling for the further development of the geography of finance will certainly be an important extension to the theory of Porteous (1995). Accomplishment of such a new development would also be possible to open another chapter for growth theory in both economic and urban and regional development in the new ages, such as the theory on new determinants and new growth poles in new economy (I will discuss this in later papers or monographs). Finally, this study echoes many influential scholars who have been arguing that “geography still matters,” but I would like to stress that a modern discipline of geography must be equipped with new perspectives in the age of information technology.

APPENDIX

The Seven Categories of Industry in the Headquarter-Location Survey

Seven categories of industry have been chosen for the investigation because they are most likely to cover the service, manufacturing, hi-tech, and telecommunications industries, which are the most related to the important components of a financial center. They are as follows:

- I. Advertising, news, gifts, consultancy, information, and services
- II. Finance, insurance, negotiable securities, law, and banks
- III. Machinery equipment, processing, and manufacturing industry
- IV. Post and telecommunications, computer, high technology, and electronics
- V. Commerce, trade, and investment
- VI. Transportation, freight forwarding, automobile, aviation and space flight, shipping, and tourism
- VII. Chamber of commerce, member organization, and news organization

Among the seven industries, the grouping of industry categories I, II, V, and VII are included in the “service sector”; categories III, IV, and VI are included in the “manufacturing sector.”

NOTE

1. The 10 preferential policies are related to the following: income tax of foreign investors; custom duties and tax for equipment, vehicles, and building materials related to foreign

investment; export-oriented foreign investments shall dominate the area; foreign investors are allowed to invest in infrastructure projects; foreign investors are allowed to operate tertiary industries; foreign banks are allowed to open foreign branches in Shanghai, including the Pudong New Area; a free trade zone will be established in the Pudong New Area; preferential treatment in terms of income tax reduction will be given to enterprises complying with industrial policies and those that are beneficial to Pudong development; land leasing for 50 to 70 years will be used in Pudong (foreign investors may contract large tracts of land for development); and the Pudong New Area can keep the revenue for further development. (The policies were approved by the State Council on 30 April 1990. For details, see Pudong Development Office of Shanghai Municipality and People's Construction Bank of China 1990; Shanghai Pudong New Area Administration 1992; Pudong Development Office of Shanghai Municipality, 1990.)

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