Will Brexit Reverse the Centralizing Momentum of Global Finance?

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The UK's EU referendum, in calling for separation from cross-border entanglements, marked a caesura in the intensive integration project of the European Union (EU). A key facet of this three-decade-long effort has been the integration and harmonization of financial trading and services at EU international financial centres (IFCs). The process of harmonizing global finance – that is, those financial activities that involve counterparties in two or more countries – has been occurring worldwide, compelled both by the increasingly severe financial crises of recent years and by these centres' exponentially rising financial volume/capacity.

The Brexit vote has generated substantial uncertainty about the future of global finance in Europe. Yet does this vote constitute the beginning of a reverse trend away from the globalization of financial activities?

No aspect of the worldwide trend toward financialization has grown faster than global finance, which encompasses flows of credit, remittances and earnings, and capital, as well as insurance, hedging, and other services. The growth of global supply chains in goods and services markets, together with heightened exchange-rate volatility, have multiplied the risks of cross-border trade. Many of the instruments used in cross-border financial provision are exploited to offset some of these risks, and thus augment economic growth. At the same time, the steady expansion of global financial activity has spawned new forms of financial speculation and led to more frequent and deeper episodes of financial instability.

The sometimes-volatile instruments involved at the heart of global finance are provided primarily through specialized firms clustered in financial centres. Geographically, global finance forms a deep-rooted archipelago-economy. That is, a dense web of high-speed financial flows materialising only in specific locations endowed with distinct regulations and clusters of dense skill and competition (cf. Hall and Wójcik). European financial centres have taken leading roles in this web of flows. For example, London is an explicitly strong wholesale banking centre, which comprises investment and merchant banks, capital brokers and dealers, etc. Wholesale banking links issuers – that is, corporations of all sizes, governments, banks and insurers – with investors, such as asset managers, hedge funds, insurers, pension funds, to name but a few. These financial entities have intensified not just the volume, but also the frequency and complexity, of their activities. This has generated the requirement for sophisticated financial infrastructure (stock exchanges, clearing houses, etc) – embedded in highly competitive regulatory

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environments. While global finance has the appearance of an archipelago, its activities are deeply intertwined with macroeconomic processes and outcomes. The governments responsible for stabilizing macroeconomic growth paths must also defuse financial crises when they occur; this, despite megabanks' continuing efforts to escape regulatory oversight and to retain freedom of action in IFC. Indeed, the micro-meso-macro connectivity enabled by global finance but punctuated by occasional deep crises give global finances its special character.

Since finance has become a more important part of national output and employment, the uneven distribution of global financial gains is a geo-economic issue. Moreover, as resolving financial crises in any one nation now frequently requires policy interventions in other nations, finance also holds a geo-political dimension. The US Federal Reserve (Fed), assisted by the Bank of England (BoE), demonstrated its willingness and capacity to backstop global finance in the 2007-08 financial crisis. This permitted European banks to turn for liquidity to the wholesale US money-market after the collapse of European inter-bank lending. The European Central Bank (ECB), strait-jacketed by its overly restrictive charter, stepped into the subsequent Eurozone crisis late and reluctantly, ultimately orchestrating the shifting of sovereign-debt losses from lenders to European taxpayers and to residents of crisis-affected nations (Varoufakis, 2017). So, while globally-active UK and European banks' asset sizes remained largely unaffected by this dual crisis, they had to focus on recapitalization and have remained dependent on US money and capital markets (Dymski, 2017). Consequently, their retail lending fell dramatically and they have lost ground to global US banks in some global European financial markets – especially in investment banking (cf. Pollard's questioning how fit for purpose the UK's financial landscape is to finance local SMEs). In effect, this dual crisis demonstrated that the global European banks active in IFCs in Europe and elsewhere are operating in an environment of hierarchically-distributed risk and underwriting.

London has been Europe's leading financial powerhouse for decades, building on intricate economic and financial relationships with continental Europe and heavily nurtured by the policies of the EU single market. The picture that appears to be emerging from the recently launched divorce process between the UK and the EU is clear: State governments have been fighting tooth and nail to attract large stakes of London-based business to their financial centres, and the fight for the prestigious European Banking Authority is now a politically sensitive deal-making. Examples that give a taste of what might follow in the EU's complex geo-political environment includes resolving the two currencies-one market taxonomy of the lucrative euro clearing business in London (Dörry, 2017). Another illustration is the collapsed merger between Deutsche Börse and the London Stock Exchange, which sought to create a European counterweight to America's powerful stock exchanges, but faced political interference from governments and regulators in Brussels, Rome, and Hesse/Germany.

The pressure on financial businesses in London is on, and the Bank of England urged UK based financial businesses to present contingency plans in July this year to ensure access to the European single market, a market of 500 million people that topples the US' 323 million inhabitants. Co-location of vital business operations to the EU27 remains the prime, though costly, solution for now. Ricocheted by aggressive media campaigns and other promotion channels, Europe's most important, competitive financial centres – Amsterdam, Dublin, Frankfurt, Luxembourg and Paris – have been succeeding in attracting financial activity from

London. Many see Frankfurt the winner, but the Brexit-business race has hardly begun. Germany's leading financial centre attracted four of the five largest investment banks and other global lenders so far, thus seeking to gain up to 10,000 additional jobs. Competition with Paris, France's powerful banking centre, is fierce, but the French Bank Association believes to benefit from up to 1,000 jobs shifted to Paris in addition to jobs created by re-located operations from banks like HSBC. Amsterdam, Dublin and Luxembourg, IFCs of much smaller size and less capacity to absorb large job influxes than their French and German counterparts, vie more for special commercial and reinsurance business – with "the 'London market' … worth an estimated GBP 60 billion in gross written insurance premiums" (European Parliament, 2016, p. 7) – and asset managers than for banks, because skill, infrastructure and competitors are already bustling in each of these specialized finance hubs. The post-Brexit EU financial centre architecture may still find London to be a finance hub of global importance, yet, the gap to its European rivals may well dwindle. Still, at what cost?

Turning to the geo-political dimensions of banking, Brexit threatens to expose an unresolved structural weakness of European finance. Its leading banks are now sustaining their asset positions with leveraged offshore liquidity. As such, they are fully incorporated into the cross-border architecture of global non-bank financial entities, and in any crisis, will depend on the US Federal Reserve (Dymski, 2011). The Fed's willingness to play a global lender-of-last-resort role again, as it did in 2008, is now in question, as is the effectiveness of the 2010 Dodd-Frank reforms in reining in US banks' speculative impulses. President Trump has championed a roll-back of Dodd-Frank, despite the new wave of subprime lending now taking shape. Large European banks have been caught in a peculiar trap since the creation of the Eurozone: they have been competing in the single financial market with UK banks. However, unlike UK banks, they lack a central bank willing and able to act as a lender of last resort; and both UK and EU banks compete with US banks, behind which stands the Fed. A precautionary response to the withdrawal of UK banks from the single market, given the constraints on ECB action, would be to tighten financial regulations. But instead, financial centres in Europe are bidding for business that falls off the London table. The fragility of this approach is not evident if 'normal expectations' prevail. That Brexit may disturb expectations is evident, as is the unreliability of the post-Obama US as a backstop for global finance. In sum, there is a growing centralization and reiterative multiplication of high-volume, risk-related financial services. So long as sophisticated financial instruments are needed as offsets to the financial risks associated with global supply chains, and/or to smooth return-risk exposures for global wealth portfolios, this centralizing tendency – with its consequential spatial and functional power discrepancies – will remain.

The controversies now roiling academia and the news media about what Brexit means for IFCs and global finance creates important opportunities for new research in economic geography. The analysis we have unfolded here suggests that such research must merge geographic (location) with economic (creation and transfer of wealth) analysis (cf. Lai and Pan's call to incorporate global trade and investment patterns), an appreciation of these centres' function (trading, finance, brokering, etc.) with agency (firms, governments, etc.), paying special attention to the nexus between micro, meso, and macro dynamics. There is much to be understood in these supremely uncertain times.

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