Financial Globalization:
Taking Your Business Elsewhere?

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Effects of financial globalization

- Financial integration is higher than ever
- Increasing number of financial centers that can attract global business
- Greater opportunities to “take your business elsewhere”
Focus today:

- Changes in the geography of global financial business?
- What are the most prominent markets of destination?
- Impact for the U.S.?
Why does it matter?

- **Stability issues**
  - Markets less affected by shocks to one financial center
  - Regulatory intervention more difficult

- **Efficiency of capital markets**
  - Barriers removed, competition enhanced, liquidity improved

- **Impact on the “local” economies**
Two main take-aways

- Learning something new about key financial markets:
  - Corporate bond markets
  - Primary equity markets (IPOs)
  - Secondary equity trading

- Focus on *measurement*
Bond issuance

- Global corporate bond market dominated by U.S. and Eurobond markets
- Combined market share in 2006: more than 90% of global issuance
EMU made Eurobond issuing less costly

- Reduced currency risk
- Eliminated cross-country investment restrictions
- A new “broader” market made it more attractive to non-Europeans
Eurobond much more costly...

Gross Spread (Underwriting Fees) 1996-2006

Underwriting cost in Eurobonds

Underwriting cost in US Bonds
...but costs have converged

Gross Spread (Underwriting Fees) 1996-2006

Underwriting cost in Eurobonds

Underwriting cost in US Bonds
U.S. market losing EU firms ...

- European firms issuing U.S. bonds
- U.S. firms issuing Eurobonds
... and losing U.S. firms as well

Eurobond market gaining as U.S. market loses
IPOs and secondary equity trading

- Most companies still issue on domestic exchanges
- More and more firms are choosing to go abroad
Growing **network** of cross-market IPO activity
Network Analysis
to measure market “prestige”
Measure based on three criteria:

1. More prestige if more foreign firms are coming in
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2. More prestige if foreign firms come from prestigious markets
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1. More prestige if more foreign firms are coming in

2. More prestige if foreign firms come from prestigious markets

3. Loss of prestige if domestic firms go to foreign markets
Google’s Web Page Ranking uses similar algorithm!

1. More prestige if more foreign firms are coming in

2. More prestige if foreign firms come from prestigious markets

3. Loss of prestige if domestic firms go to foreign markets
Actual network of cross-exchange IPO issues, 2004 – 2006 average
Rankings in market prestige. IPOs.
Rankings in market prestige. IPOs.

1. U.S. dominance through 1990s
Rankings in market prestige. IPOs.

1. U.S. dominance through 1990s
2. Negative trend in 2000s

Net receiver

+ 0 -

Net giver


U.S.

Europe

U.K.

China - HK
Rankings in market prestige. IPOs.

1. U.S. dominance through 1990s
2. Negative trend in 2000s
3. Three-market core now

Net receiver
+
-

Net giver


U.S.
Europe
U.K.
China - HK
IPO activity only part of the story

- IPOs are one-time events
- A dominant exchange should provide an efficient and liquid environment for subsequent trading
Same **network** analogy applies

Arrow lines capture trading volumes instead of IPO proceeds
Rankings in market prestige. Secondary trading.

Net receiver

U.S. dominance unchanged

Net giver

1995 1997 1999 2001 2003 2005
Summary

- U.S. bond market has lost part of its dominance
- U.S. stock exchanges share top rankings in global IPO activity with London and other European exchanges
- U.S. stock exchanges still leaders in overall trading activity of global listings
Open questions

- How will international ranking continue to evolve in the future?
- Are U.S. regulatory agencies losing “control” of markets?
Reference Slides
U.S. Bond and Eurobond Corporate Market Issuance

Source: Securities Data Corporation
Market Share of Investment-Grade Bond Issuers From Different Regions

Source: Securities Data Corporation
Market Share of Below-Grade Bond Issuers From Different Regions

Source: Securities Data Corporation
Prestige of IPO Listings Across Regions, Adjusted for Turnover

Net receiver

+ Net giver

1995 1997 1999 2001 2003 2005

U.S.

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Europe