

# TAILORED FOR PANAMA: OFFSHORE BANKING AT THE CROSSROADS OF THE AMERICAS

by  
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**ABSTRACT.** With the steady integration of a deregulated world of hypermobile capital, offshore banking has become an increasingly significant part of the geography of international finance. Many interpretations tend to treat offshore banking centres as identical sites of investment that can be easily substituted for one another by completely mobile, fungible capital. This paper explores the nature of offshore banking in one largely overlooked centre, Panama. It charts the historic context that led to the creation of Latin America's most important centre of international banking, emphasizing the unique qualities that stand in contrast to hyperglobalist interpretations, including the Canal and the role of the US dollar. Second, it summarizes the regulatory changes initiated in the face of global neoliberalism, including the absence of a central bank and recent reforms designed to attract foreign capital. Using primary and secondary data, the paper maps Panama's growing role as a net capital exporter, charting domestic and foreign loan markets. Finally, it also addresses the trade-offs between confidentiality, and transparency in the context of illicit activities frequently alleged to occur in offshore banking centres, which in Panama revolve around drug trafficking and money laundering. It concludes by noting that even in an ostensibly seamless world, offshore banking exhibits the place-based embeddedness of financial capital within local institutional relations.

Within the growing literature on the geography of money (Leyshon and Tickell, 1994; Leyshon, 1995, 1997, 1998; Corbridge, *et al.* 1996; Leyshon and Thrift, 1997; Cohen, 1998;), the globalization of finance has received pride of place. Few industries are as internationalized as banking and securities, industries that have exhibited enormous technical and institutional changes over the past two decades. While a considerable literature has focused on the role of global cities in this regard (Daniels, 1986; Sassen, 1991), others have pointed to the steady emergence of small, often marginal places – offshore banking centres – hitherto sequestered on the peripheries of international money markets that have gained steadily in stature and importance (Roberts, 1994).

Harvey's (1982) famous work *The Limits to Capital* unearthed the ways in which money and social power are deeply intertwined, highlighting the importance of finance as a means of reproduc-

ing uneven development, attenuating the spatial and temporal crises of capitalism, and accelerating the turnover time of capital. Such work spurred an on-going interest among geographers in the ways in which money circulates at several spatial scales ranging from the local to the global. The globalization of finance has focused in large part on deregulation and the erosion of national monetary controls (Gill, 1992; Swyngedouw, 1992; Agnew, 1994), the ways in which nation-states have surrendered much of their authority to international corporate elites through the adoption of neoliberalism in various forms, what Rosenau and Czemieli (1992) term 'governance without government'.

The globalization of finance has helped to spawn various myths about the relations between capital and space. Castells' (1995) work on the 'space of flows' contributed significantly to a reorientation of theorizations of money as part of a broader web of social relations that at first glance appear to be placeless. What may be termed 'hyperglobalist' interpretations of international financial flows (cf. Held *et al.* 1999) centre largely upon the putative irrelevance of place in a seamless, borderless world in which electronic funds dance from centre to centre without obstacle, the ultimate annihilation of distance (Ohmae, 1990, 1995; O'Brien, 1992). Such views tend to portray regions as passively accommodating to the global prerogatives of capital rather than actively shaping those forces at the local level. Between these two poles of money as place-bound and money as placeless lies an intermediate scale of analysis that incorporates aspects of each, a term Swyngedouw (1992, 1997) coined 'glocalization'.

This paper explores the origins and changing status of one largely overlooked centre of international banking, Panama. The historical geography and institutional dynamics of banking in this nation are closely bound up with the geopolitics of Panama at several scales, from its long subordination to the USA to its emerging role as the premier banking centre of Latin America. The paper invokes the lit-

erature on the contemporary geographies of global finance from several distinct theoretical angles, refuting simplistic 'hyperglobalist' assertions that the fluidity of international money renders all local banking centres identical. Rather, it emphasizes the comparative and local topographies of regulation that underpin the formation (and occasionally dissolution) of offshore banking centres. Thus, despite the extreme liquidity of global capital, place still matters, and profoundly. Drawing upon interviews with bank managers, financial advisory services firms and government officials in Panama, the paper seeks to explicate the unique characteristics that differentiate Panama from its competitors, including the presence of the Canal, the role of the US dollar and the absence of monetary controls, and its evolving set of banking laws designed to attract foreign firms. Primary data are supplemented with information, largely unpublished, provided in corporate publications and by the US Embassy in Panama. The paper charts the origins of the nation's banking sector, the reasons underpinning its success, regulatory changes that facilitated the growth of offshore banking, and the principal sectoral and geographic loan markets of Panamanian banks. Finally, the paper confronts the 'hidden ghost' that frequently haunts the analysis of offshore banking – money laundering of illegal, largely drug-related funds, as well as private foundations to shelter family assets – which forms a particularly important dimension in the context of Panama. In this context, it explores the knife-edge between confidentiality and transparency that offshore banking centres are forced to negotiate in order to lure investors and yet remain sufficiently legitimate in the eyes of the global banking community.

### **Offshore banking and the global financial system**

The emergence of contemporary geographies of offshore banking can be traced straightforwardly to the global sea-change in capitalism that began with the traumatic petro-crises of the 1970s and massive restructuring of industrialized economies, in which the relatively stable world of Bretton-Woods gave way to what Strange (1994, 1998) calls 'casino capitalism'. This transformation included a fundamental worldwide renegotiation of the relations between financial capital and space, including the explosive growth of 'fictitious capital' largely divorced from production and oriented instead to speculation (Harvey, 1989). Freed from many of

the technological and political barriers to movement, capital has become not merely mobile, but *hypermobile* (Warf, 1995a). As Castells (1996, 1997) emphasized, all around the world the 'network society,' dominated by a 'space of flows' rather than a 'space of places,' has generated new political formations, forms of identity and spatial structures.

A key part of this new order was the emergence of 'stateless money' (Martin, 1994), which originated in its contemporary form through the Euro-market. Originally the Euromarket comprised only trade in assets denominated in US dollars but not located in the US; today it has spread far beyond Europe, and includes all trade in financial assets outside of the country of issue (e.g. Eurobonds, Eurocurrencies). One of the Euromarket's prime advantages was its lack of national regulations: unfettered by national restrictions, it has been upheld by neoclassical economists as the model of market efficiency. Indeed, US banks invested in the Euro-market in part to escape the restrictions of the Glass-Steagall Act, which prohibits commercial banks from buying and selling stocks. Further, the Euromarket lacked any reserve ratio requirements until 1987, when the world's central bankers met at the Bank for International Settlements in Basle, Switzerland, to agree on global reserve standards.

Capital markets worldwide were profoundly affected by the digital revolution, which eliminated transaction and transmission costs for the movement of capital much in the same way that deregulation and the abolition of capital controls decreased regulatory barriers. Banks, insurance companies and securities firms, which are generally very information-intensive in nature, have been at the forefront of the construction of an extensive network of leased and private telecommunications networks, particularly a skein of fibre optics lines (Graham, 1999). Electronic funds transfer systems, in particular, that form the nerve centre of the international financial economy, allow banks to move capital around at a moment's notice, arbitraging interest rate differentials, taking advantage of favourable exchange rates and avoiding political unrest (Warf, 1995b). Travelling at the speed of light, as nothing but assemblages of zeros and ones, global money dances through the world's fibre optic networks in astonishing volumes. The total volume of electronic financial transactions worldwide exceeds \$516 trillion annually, including, in Europe, the Belgian-based SWIFT, the Society for Worldwide Interbank Financial Telecommunications,

which now extends into 130 countries (Teitelman and Davis, 1996). The US Federal Reserve Bank's Fedwire system transfers \$223 trillion in the balances among private bank deposits annually, while the Clearing House Interbank Payments System (CHIPS), a consortium run by private firms to clear international transactions, processes \$310 trillion annually (Solomon, 1997). Private firms have analogous systems. Citicorp, for example, erected its Global Telecommunications Network to allow it to trade \$200 billion *daily* in foreign exchange markets around the world. Reuters, with 200,000 interconnected terminals worldwide linked through systems such as Instinet and Globex, alone accounts for 40% of the world's financial trades each day (Kurtzman, 1993, p. 47). Other systems include SEAQ in London, Soffex, the Swiss Options and Financial Futures Exchange, the Computer Assisted Order Routing and Execution System at the Tokyo Stock Exchange, and TSE and CATS in Toronto. Such networks provide the ability to move money around the globe instantaneously: subject to the process of digitization, information and capital become two sides of the same coin.

The ascendancy of electronic money altered the impacts of financial instruments on local economies. Foreign investments, for example, have shifted increasingly from Foreign Direct Investment (FDI) to intangible portfolio investments such as stocks and bonds, a process that reflects the securitization of global finance (Kahler, 1998; Friedman, 1999). Unlike FDI, which generates tangible levels of employment, facilitates technology transfer and alters the material landscape over the long run, financial investments tend to create few jobs and are invisible to all but a few agents, acting in the short run with unpredictable consequences. Further, such funds are provided by non-traditional suppliers: a large and rapidly rising share of private capital flows worldwide is no longer intermediated by banks. Thus not only has the volume of capital flows increased, but the composition and institutions involved have changed.

Globalization and electronic money had particularly important impacts on currency markets. Since the shift to floating exchange rates, trading in currencies has become big business, driven by the need for foreign currency associated with rising levels of international trade, the abolition of exchange controls, and the growth of pension and mutual funds, insurance companies and institutional investors. The world's currency markets trade approximately \$1.6 trillion every day, dwarfing the

\$25 billion that changes hands daily to cover global trade in goods and services (Solomon, 1997). In the 1990s, the vast bulk (72%) of foreign exchange transactions included only three currencies, the US dollar, German mark and Japanese yen (Laulajainen, 1998, p. 104). London remains the premier world centre for this practice, exchanging \$465 billion in currencies annually, followed by New York (\$250 billion), Tokyo (\$185 billion) and Paris (\$75 billion). The market opens each day in East Asia while it is evening in North America; funds then travel east, bouncing from city to city over fibre optic lines, typically from Tokyo to Hong Kong to Singapore to Bahrain to Frankfurt or Paris to London.

Electronic money may be exchanged an infinite number of times without leaving a trace, making it difficult for regulatory authorities to track down transactions both legal and illegal. The intermediaries that now serve as checkpoints for recording such transactions are eliminated by peer-to-peer transactions (Kobrin, 1997). The opportunities for money laundering are thus made all the more attractive. Tax evasion has become increasingly serious as electronic money has become the norm; moreover, the jurisdictional question – who gets to tax what – is vastly complicated. Digital counterfeiters can also take advantage of this situation, working anywhere and using the Internet to spend currencies in any other place.

The neoclassical case for capital mobility holds that such fluidity allows countries with limited savings to attract financing for domestic investment, that it allows investors to diversify their portfolios, that it spreads risk more broadly and that it promotes intertemporal trade. Capital mobility implies that firms can smooth consumption by borrowing money from abroad when domestic resources are limited and dampen business cycles. Conversely, by investing abroad, firms can reduce their vulnerability to domestic disturbances and achieve higher risk-adjusted rates of return. The major problems concerning capital mobility in this view centre around the asymmetry of information in financial markets and 'moral hazard,' reliance upon the state (or IMF) to bail them out during crises. Yet neoclassical theory is flawed in several respects, not the least of which is an inadequate appreciation of politics and space, the ways in which national, class, gender and other non-market relations shape and constrain flows of money, even electronic money, and how the intersections of capital and nation-states play out unevenly across the globe.

A key part of the new geographies of global finance has been the emergence of small centres of offshore banking (Gorostriga, 1984; Roberts, 1994, 1995; Hampton, 1996b; Palan, 1998a, 1998b). Roberts (1994) identified five major world clusters of offshore finance, including the Caribbean (e.g. the Cayman Islands, Bahamas, Panama); Europe (e.g. Isle of Man, Jersey, Luxembourg, Liechtenstein, Andorra, San Marino); the Middle East (Cyprus, Lebanon, Bahrain); Southeast Asia (Hong Kong, Singapore); and the South Pacific (Vanuatu). Offshore banking centres offer regular commercial services (i.e. loans), foreign currency trades and speculation on both the spot and forward markets, access to electronic funds transfer systems, asset protection (insurance), investment consulting, international tax planning and trade finance (e.g. letters of credit). The emergence of such places reflects the intersections of electronic money and the global topography of financial regulation as large financial institutions used their enhanced ability to shift funds to take advantage of lax regulations, taxes, and other restrictions to be found on the periphery of the global financial system.

As the digital revolution allowed global capital to circulate more freely and rapidly, the technological barriers to moving money declined dramatically. Accordingly, spatial variations in the nature and degree of regulation rose in importance. Even small differences in regulations concerning taxes or repatriated profits may be sufficient to induce large quantities of capital to enter, or exit, particular places. Thus, many small states have opted to attract finance capital by deregulating as much as possible, lifting controls over currency exchanges, investment, repatriated profits, and eliminating taxes in the hope that global money, with the world as its oyster, will select their locale. As Hudson (2000) points out, offshoredness also reflects a reworking of the notion of sovereignty – the central ordering principle of international political economy – as a historically specific set of institutionalized authority claims. By retaining political sovereignty but sacrificing its financial counterpart, offshore centres uncouple the historic suturing of power and territory.

'Offshore' is as much a process as a place. Yet place still matters, in the forms of locally embedded social relations that shape local policy. Perhaps given the extreme fungibility of financial capital, particularly in its electronic, digitized form, the literature on offshore banking has tended to treat the plethora of places that have carved out this niche as

essentially the same, if for no other reason than through the lack of attention paid to their fundamental differences. Part of the purpose of this paper is to correct this misconception by emphasizing the locally unique nature of offshore banking in Panama, its distinctive qualities that render money, even in its most liquid form, place-bound. Yet such a move inevitably raises the question of how to interpret the human actors who construct and reproduce such systems, to which this paper now turns.

### Origins and growth of the Panamanian banking complex

As with many successful developing nations that have carved a competitive advantage in the contemporary world system (Porter, 1990), Panama's economy is characterized by a dichotomy between a large, internationally oriented service sector and a small, inward-looking goods-producing sector. In 2000, services comprised 75% of the national GNP (\$10 billion); manufacturing, in contrast, gradually declined to 15% of national output and employment. By far the leading edge of the Panamanian services sector is its financial services complex, which is the largest and arguably most important international banking centre in Latin America.

Panama's success reflects several features that are unique to its historical trajectory and geographic location at the crossroads of the Americas. One important reason underpinning the original emergence of Panama's banking centre is the Panama Canal itself, the nation's *raison d'être* since 1903, when the US essentially constructed the nation as a flag of convenience for its imperial intentions. The Canal had long-lasting impacts that continue to shape Panama's economy and banking system; for example, because Canal workers were paid in US dollars, dollarization in Panama began with its construction. More generally, the Canal helped to instill a broader culture of globalization. Today, with 14,000 ships passing through it annually, 9 400 employees, and generating 6% of the nation's GNP, the Canal is still one of the country's largest sources of foreign revenues. Because ships in transit pay fees and purchase supplies locally, and are prohibited from doing so on credit, banks in Panama (both foreign and domestic) historically enjoyed close linkages to clients in maritime trade. In addition, the Colon Free Trade Zone, established in the 1950s and today the world's second largest (after Hong Kong), generates \$10 billion annually in re-exports and formed a secondary site of bank invest-

ments. So close were the original relations between banking and shipping that it is impossible to conceive of the emergence of Panama as a financial centre in the absence of the Canal. Such a feature distinguishes Panama from other offshore centres such as the Cayman Islands, in which trade figures minimally in attracting foreign capital.

However, the Canal's significance has dwindled gradually compared to banking, which now employs more people in Panama (12,800) and generates a larger share of its GDP (11% in 2000, compared to 2.5% in 1960 and 4.1% in 1970). Changes in the technology of maritime trade, particularly the introduction of 'post-Panamax' ships too large to use the canal, as well as 'doublestacking' of railroads to generate economies of scale in land transport across North America, have limited growth in maritime traffic through the Canal. Panama remains the world's second largest home to foreign-registered companies, with 350,000 such firms (including many shipping companies), behind only Hong Kong. Competition with other centres of ship registration, particularly Cyprus and the Bahamas, has led to stagnant revenues from fleet financing, ship mortgaging and maritime insurance (*Offshore Outlook*, 2001). Since the return of the Canal to Panama at the end of 1999, the legally autonomous Canal Zone Authority has sold securities and entered into direct negotiations with shipping companies, bypassing the banks. Accordingly, the primary growth in recent banking clients has been non-Canal related, and shipping forms a negligible source of banking income at present. Although the Canal has diminished greatly over time as a revenue source for banks, the linkages between the two point to the complex ways in which the nation's historical legacy shapes its contemporary economic landscape: far from constituting a set of perfectly mobile firms with unalloyed power to locate at will in some nebulous cyberspace, Panama's banking complex in fact comprises a palimpsest in which earlier rounds of production shape decisively the nature and location of the present (cf. Massey, 1984).

A second factor of major importance is Panama's dollar-based economy, which it has had since its inception (the Balboa is on a par with the US dollar, which is also legal tender). Lacking a central bank and prohibited by its Constitution from printing paper money (the only country in the world to do so), Panama has since its birth effectively surrendered monetary policy to the US Federal Reserve. Panama is the only nation to have a monetary

treaty with the USA (Ecuador and El Salvador recently adopted the US dollar, but without such a treaty). Thus its interest, inflation and exchange rates have historically moved in close tandem with those in the USA. The nation's only publicly-owned commercial (as opposed to savings) bank, the Banco Nacional, acts as the legal 'fiscal agent' of the US Federal Reserve in Panama, existing primarily to exchange worn-out dollars for new bills; since 1979, as a result of the Carter-Torrijos Agreement returning the Canal to Panamanian control, it has been the only foreign member of the New York Federal Reserve Bank that is not a central bank<sup>3,4</sup>. However, while Panama largely accepted the American model of corporate law (based on the well-known model of Delaware's 1927 statute for legal incorporation, for example), it did not adopt the American style of financial regulation (e.g. Glass-Steagall restrictions between commercial and investment banking).

Because Panama has what is locally described as a 'private monetary system,' (i.e. there is no federal reserve bank to serve as lender of last resort), banks there typically stay very liquid to compensate for the higher risk levels they face, prepared for financial difficulties without appeal to national discounts of failed loans. Similarly, depositors lack any sort of deposit insurance. Panamanian banks are typically more cautious (risk averse) than their counterparts elsewhere in Latin America.<sup>4</sup> Thus, total bank reserves in Panama in 2000 amounted to \$5 billion, equivalent to approximately half of the national GNP, and total bank assets (\$36 billion) were 3.6 times GNP, the highest such ratios in the world. However, without a central bank to print money, this Faustian bargain with the USA sharply limited Panama's rate of inflation (in contrast to most of Latin America), annihilated currency fluctuations relative to its largest trading partner, allowed it to avoid IMF-mandated devaluations commonly part of austerity restructuring plans and enhanced foreign investors' confidence in the economy. Excesses or shortages of liquidity within the country traditionally have been resolved of necessity through private capital flows into or out of the country, not central bank interventions. Thus bankers argue typically that the gains to efficiency exceed the associated loss of national seignorage. The 'dollarized economy' unique to Panama is one of its primary assets attracting foreign banks, who often prefer it to the overly regulated and bureaucratized public banking systems common in much of Latin America (Jenkins, 1991) and has been her-

alded by neoliberals as a prime example of a deregulated 'balance of payments' approach to macroeconomic management, in which every exogenous shock is translated directly into employment effects without the mediating role of a central bank to dilute such disruptions through inflationary monetary policies.

In addition, Panama has enjoyed relative political stability. Due to the considerable history of US presence, Panama has long served as a magnet for capital flight in Latin America. Mexico's near-default on foreign loans in 1981 and subsequent collapse of the peso precipitated a hemispheric-wide financial crisis in Latin America when American banks withdrew funds to the USA in order to declare their losses as tax deductions, a blow from which it took Panama's banking community several years to recuperate. The American invasion of 1989, 'Operation Just Cause' that overthrew General Manuel Noriega, induced the exodus of \$13 billion in bank deposits (two-thirds of the previous year's total). In large part this round of capital flight started because in 1988 the USA froze \$56 million in Panamanian assets held in the Federal Reserve Bank of New York, causing the national banking system to halt completely for ten weeks, initiating a liquidity crisis that reduced Panama to a barter-based economy. However, because of its close association politically and economically with the USA, Panama's status has long made it an attractive investment site for Latin American capital. Cultivating this image through regulatory reform became a key prerequisite to the establishment of a banking complex, a step undertaken aggressively in the 1970s in the context of global financial deregulation and internationalization.

### **The regulatory structure of Panamanian banking**

With the substantive foundations laid through its historically and geographically unique position, all that remained to initiate a banking complex in Panama was a catalyst. In realist terms, the necessary conditions already existed; to activate them contingently required an actor with foresight and initiative. Such a perspective is necessary if the growth of 'regional worlds' (Storper, 1997) such as came to exist in Panama City is to be understood as something other than a teleological necessity driven by the prerequisites of global capital but rather as a human product embodied in individual actors.

The origins of Panama's status as a magnet for

international banking lay with the Torrijos administration of the 1970s, which sought to diversify the national economy from its historic dependence on agriculture, the Canal Zone and the Colon Free Trade Zone (Johnson, 1976). In large part, the impetus to create an offshore banking centre was the brainchild of Torrijos' Minister of Planning, Dr Nicholas Ardito Barletta. With a doctorate in economics from the University of Chicago, an institution that has enjoyed a significant influence over monetary policies of Latin American governments, Barletta played the pivotal role in the development of a Panamanian banking complex in the late 1960s. Extensive interviews with Barletta for this paper revealed the powerful influence of the Chicago School's ideology as well as the complex negotiations that led to the regulatory changes which launched the banking complex. Barletta himself studied with luminaries such as Nobel laureates Milton Friedman, George Stigler and Theodore Schultz, and formed part of an important generation of Latin American economists who initiated a long campaign against traditional Latin American economic policies such as import substitution. As Barletta noted, 'if I had not studied at the University of Chicago, I would have advocated the creation of a central bank'<sup>5</sup> instead of the much more complex – and interesting – policies and products that resulted from his efforts.

Essentially, Barletta identified the need to develop a 'cushion' against unfettered liquidity that existed in the absence of a central bank, seeking to leverage the nation's greatest monetary weakness into a competitive strength (Barletta, 1998). To overcome the opposition of conservative local banks, he offered repeal of the national usury law that placed a 9% ceiling on interest rates. Barletta hoped the incipient banking community would attract investment capital to finance national development projects, particularly the Colon Free Trade Zone.<sup>4</sup> Indeed, because trade through Colon is credit-driven and a source of significant revenue for banks, he noted that 'the Free Trade Zone and the banking system are totally symbiotic'.<sup>5</sup> Thus it is highly ironic that although 'Chicago School' economics has long been synonymous with Friedmanian monetarism and neoliberal *laissez-faire* doctrines, Panama's banking complex was engineered quite consciously, by the state, to facilitate a growth pole in Colon and as a growth pole itself in Panama City, a strategy much more in keeping with that of European regional science than North American neoliberalism. The strategy enjoyed a fortunate

nexus of circumstances internationally: the Euro-market was surging far beyond Europe itself, massive volumes of petro-dollars were being recycled in search of overseas outlets, and capital flight and tax evasion by US and Latin American investors had reached new heights. In the 1980s, Japanese banks – flush with income from the long since deflated ‘bubble economy’ – made Panama their Latin American headquarters. Barletta himself highlighted the contingent nature of this process, noting, for example, that ‘We were lucky. We happened to be in the right place at the right time with the right idea, not that we were geniuses.’<sup>5</sup>

The initial banking legislation studiously sought to avoid small, potentially unreliable banks in favour of large, well-established ones with a history of international operations. Unlike offshore banking in many comparable centres such as the Cayman Islands (with 1 000 banks employing 500 workers), ‘brass plate’ banking is illegal in Panama, a form of banking popularly dismissed as ‘post office banks’ or ‘closets with computers’. As Barletta noted, ‘we would not accept fly-by-night banks’<sup>5</sup>. Unlike brass plate banks, financial markets in Panama rely heavily upon a high degree of uncodifiable tacit knowledge, which is socially embedded and articulated through localized agglomeration economies (Dicken and Malmberg, 2001). Foreign firms must maintain offices and physical addresses that employ a minimum of three people, including a CEO, treasurer, and secretary who serve as compliance officers responsible for ensuring that regulatory controls are enforced.

In 1970 Barletta’s vision materialized in practice: banking laws were liberalized, secrecy guaranteed, currency controls abolished and most restrictions removed from bank transactions. For example, banks were not allowed to disclose information concerning their clients, leading to claims that the nation offered more secrecy than did Switzerland<sup>1</sup>. The founding legislation set up the licences required by foreign and offshore banks and established the regulatory authority that governed Panama’s banks for the next three decades: from 1970 to 1998, Panama’s banks were essentially ‘self-governing’ through a National Banking Commission composed mostly of bankers.

At this juncture it is important not to reiterate the common error of equating foreign banking with ‘offshore’ finance. Offshore banking refers specifically to financial operations designed to avoid regulatory and tax restrictions generally imposed by home governments. Many banks establish offices

in the nation to provide access to the Panamanian domestic lending market itself. The distinction between foreign and offshore banking is reflected in the licences required by the Panamanian government: foreign banks seeking business with Panamanian clients must obtain a general licence and pay national income taxes, whereas offshore banks obtain an international licence, serve only foreign clients and avoid taxes of any sort.

The 1970 legislation also sought to turn Panama into a tax haven for foreign investors. Because the income tax system of Panama is constituted strictly along territorial lines, all offshore business is exempt from national taxes, including profits, capital gains, and interest on domestic savings and time deposit accounts. (The use of territorial income, rather than citizenship, for purposes of taxation is common throughout Central America.) Thus banking and brokerage business conducted in Panama by non-resident Panamanian corporations is not considered by the government to be trade within Panama, creating a ‘100% tax haven’. The fact that Panamanian taxes are based on the locale where earnings are generated, rather than on citizenship (as in the case of the USA), helped to create incentives to invest abroad, one factor that has made the country a net capital exporter. Further, the nation abolished all exchange controls and currency restrictions, and Panama lacks any tax treaties with other nations with regard to repatriated profits.

Panama’s government has continued to work overtime to accommodate the requisites of global neoliberalism. In the late 1990s, concerned about the competitive pressures of global neoliberalism, and with the transfer of the Canal imminent, the Panamanian government embarked on another bout of privatization and deregulation. In 1997 Panama joined the World Trade Organization and initiated across-the-board reductions in tariffs, quotas and export subsidies, curbs on anti-monopoly practices, and ensured intellectual property rights. The government pursued several free trade initiatives with its neighbours, including investment protection measures, and initiated the privatization of several public assets (e.g. sewage treatment plants). In 1997, the government passed legislation that permits the privatization of pension funds. This round of liberalization also produced a comprehensive banking law designed simultaneously to attract more firms and to quash the country’s persistent and debilitating reputation as a haven for South American drug traffickers (about which more below), a problem the banking community conceived

of and portrayed discursively as one of inadequate transparency. The 1998 law created a powerful Superintendent of Banks to oversee the banking community, run by a committee of five that excludes bankers, and increased the overall level of supervision, including audits, licences, sanctions and liquidation of insolvent institutions. Private banks acquiesced to these measures in the hopes of improving the nation's reputation internationally as a nation with high legal standards.<sup>4</sup> Concerns over money laundering led the government to raise the minimum assets for domestic banks from \$1 million to \$10 million (\$500 million for foreign banks), encourage inter-bank lending, and to lend no more than 8% of reserves when weighted by relative risk, steps that brought the nation into conformity with the guidelines of the Financial Stability Forum of the Basle Committee on Banking Supervision as well as OECD benchmarks.<sup>4</sup>

### The bankers of Panama: empirical patterns

Panama's changing global context and local regulatory structures have been manifested empirically in the size and composition of its financial community. The number of banks in Panama reflects a sequence of increases and decreases over time (Table 1). A decline subsequent to the American invasion in 1989 was followed by a gradual rise, reaching a peak of 110 banks in 1997, including 70 foreign banks. However, since then, a wave of consolidation among Panamanian banks, stimulated in part by government hopes of achieving economies of scale, has led the total number of such firms to decline to 83 in 2000 (Table 1), including 53 foreign banks. For example, in 2000 HSBC Bank (Hong Kong and Shanghai Banking Corporation) purchased the Panama subsidiary of Chase Manhattan. This contraction in the number of banks mirrors a global process of consolidation through mergers and acquisitions (Fauli-Oller, 2000). Total deposits, however, remained constant, and the average bank size measured in assets increased. Few bankers interviewed for this study expressed concern over these changes.<sup>3</sup>

The entry of foreign banks into Panama, penetrate both to the domestic and offshore markets, has been uneven over time (Table 2). Following the initiatives of the Torrijos administration, a wave of 19 banks arrived in the 1970s, followed by a smaller group of 13 in the 1980s; in the 1990s, however, relatively few opened new offices there. In 2000, foreign banks in Panama originated in 25 foreign na-

Table 1: Banks in Panama, 1987 to 2001.

	Deposits Number (\$ billions)	
1987	110	21.7
1988	96	24.3
1989	89	11.5
1990	110	12.7
1991	104	17.1
1992	104	19.0
1993	106	21.2
1994	109	26.0
1995	108	25.2
1996	109	25.2
1997	110	27.5
1998	101	26.8
1999	92	26.9
2000	83	27.3

Source: Superintendencia de Bancos de Panama.

tions (Table 3), including most commonly the USA, several Latin American nations (Colombia, Ecuador, Venezuela), and Western Europe (France, Spain, Switzerland). The Japanese presence is notably small. The ten largest foreign banks in Panama include several from the US and Europe, as well as one each from China and Argentina (Table 4).

The largest privately owned bank in Panama (in contrast to the nationally owned Banco Nacional) is BLADEX, or Banco LatinoAmericano por el Desarrollo de Exportes, founded by Dr Barletta in 1978.<sup>5</sup> BLADEX was established with the intent of using Panama's competitive position in financial services as a source of funds to finance Latin American exports. With \$5 billion in assets, its shareholders consist of the central banks of all Latin American states (class A stockholders), 285 commercial banks (class B), and a few non-Latin American banks (class C), as well as the International Finance Corporation of the World Bank. Thus, with approximately two-thirds of its equity privately held, it operates much like a public-private partnership to facilitate export financing in 20 countries. Since 1992, when BLADEX began to sell shares on the New York Stock Exchange, it has generated most of its funds from outside of Latin America; indeed, through this vehicle the enormous bull market on Wall Street served as a source of investment funds for much of the region.

Panamanian banks cater to several sector and geographic markets within the nation and abroad. Domestically, Panamanian banks tend to emphasize commercial clients, mortgages, retail banking and consumer credit, while their foreign counterparts,

Table 2: Foreign banks entering Panama.

1904–1969	5
1970–1979	19
1980–1989	13
1990–1999	8
2000	2

Source: compiled by author from data from Superintendencia de Bancos de Panama.

Table 3: Origins of foreign banks in Panama, 2000.

USA	6
Colombia	5
Ecuador	4
Venezuela	4
France	3
Spain	3
Switzerland	3
Argentina	2
Costa Rica	2
Dominican Republic	.2
Great Britain	2
Israel	2
Japan	2
Bolivia	1
Brazil	1
Canada	1
Cayman Islands	1
China	1
El Salvador	1
Germany	1
Italy	1
Netherlands	1
Peru	1
South Korea	1
Taiwan	1
Total	52

Source: compiled by author from data provided by Superintendencia de Bancos de Panama.

which generate 40% of investment funds nationally, are concentrated primarily within the commercial lending sector and securities (Table 5). One substantial market for domestic and foreign banks alike is trade in Panamanian government debt, which in 2000 amounted to more than \$7.5 billion. Few domestic banks invest in the Panamanian stock exchange, the Bolsa de Valores de Panama (established in 1990), despite its steady growth (\$1 billion in capitalization in 2000), the introduction of electronic trading of stocks and recent legislative changes permitting the participation of foreign firms. Spatially, domestic bank loans are concentrated overwhelmingly in Panama City, the locus of the vast bulk of foreign and domestic investment and commercial activity in Panama, reinforcing the country's traditional primate city structure. Surprisingly, few banks in Panama engage in currency transactions or speculation, despite the huge tides

Table 4: Ten largest foreign banks in Panama, 2000

Bank	Country	(\$ millions)
HSBC	USA	593.6
Citibank	USA	473.9
Banco Bilbao Viscaya	Argentina	285.5
BankBoston	USA	211.6
Dresdner Bank	Germany	194.7
Banco Sudameris	Italy	140.4
Banco Atlantico	Spain	138.5
International Commercial Bank of China	China	95.3
Banco Santander	Spain	85
ABN-AMRO	Netherlands	73.8

Source: Superintendencia de Bancos de Panama.

of funds that bounce among the world's global cities in this sector; several bankers expressed skepticism of the nation's ability to compete with New York and London in this arena.

Foreign loans by Panamanian banks reflect the nation's status as an emerging centre of capital exports, although only two have foreign offices (in ten countries). Panamanian banks generate around \$180 million annually in net external interest earnings. The outstanding loans owed to Panamanian banks reflect the industry's close ties to Latin America (Fig. 1), which, with close cultural and linguistic ties, comprises the overwhelming bulk of its client base. North America and Europe comprise a distinctly secondary nexus, and the rest of the world hardly appears at all. Such a distribution hints at the close ties between banks and their clients – manifested, for example, in airline trips by banking executives – and is a far cry from naive assertions that financial capital is automatically capable of moving to any place, any time around the world (see e.g. O'Brien, 1992); rather, capital is bound closely by the historical legacies of colonialism, neocolonialism, and its contemporary cultural and geopolitical aftermath.

Panama's strategic position in Latin American financial markets is closely associated with its growing telecommunications infrastructure. The microelectronics revolution, the digitization of capital, and an emerging global telecommunications infrastructure centred upon fibre optics lines became increasingly vital to the liquidity of global capital and hence to the competitive position of governments attempting to court it. Thus, in Panama, boosting the corporate telecommunications network was undertaken by the state in conjunction with its studied efforts to retain banks. For exam-

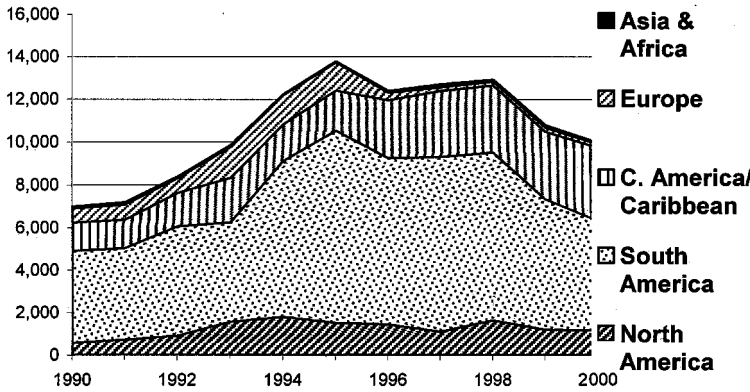


Fig. 1: Regional distribution of foreign loans extended by Panamanian banks. Source: Superintendencia de Bancos de Panama

Table 5: Sectoral distribution of bank loans within Panama, 2000.

Market	Panamanian banks		Foreign banks	
	\$ millions	%	\$ millions	%
Securities	174	3.0	658	16.4
Agriculture	136	2.3	55	1.4
Fishing	20	0.3	3	0.1
Mining	0	0.0	10	0.2
Commercial	2 109	35.8	1 887	47.0
Industrial	137	2.3	361	9.0
Mortgages	1 754	29.8	531	13.2
Construction	177	3.0	70	1.7
Personal	1 383	23.5	442	11.0
Total	5 890	100.0	4 017	100.0

Source: Superintendencia de Bancos de Panama. Notes on major interview sources:

ple, as part of its deregulatory reforms, the government dissolved the state-owned telephone monopoly INTEL in 1997 and sold its shares to the British giant Cable and Wireless. Because banks and securities firms are information-intensive in nature, they have been at the forefront of a global network of fibre optic lines used to move funds electronically. Panama, in part because of its legacy as the crossroads of the Americas, has become an important hub in this regard with an infrastructure that is attributable originally to the American military presence. For example, a consortia of telecommunications firms led by AT&T has build the MAYA-1 and ARCOS-1 fibre rings through Central America and the Caribbean, and the Bermuda-based fibre giant Global Crossing has used Panama as its hub for a cable ring around South America. Recently, Cable and Wireless entered a joint venture with Microsoft, called WebStation Alliance, to promote e-commerce in the country.

Panamanian bankers are highly conscious of

their intense competition with other parts of the world. Several remarked upon the competition with the remnants of the British empire for offshore funds, and expressed hope that new restrictions on secrecy imposed by the European Union would provide an impetus for investors to divert funds elsewhere. As one bank claimed on its website:

The British Government, for its part, has forced changes in the regulations and standards of supervision in its two Crown Dependencies of the Channel Islands and the Isle of Man and also its 5 Overseas Territories in the Caribbean, namely, Anguilla, the British Virgin Islands, Montserrat and the Turks and Caicos Islands. The aim of the British Government, as stated by its Foreign Secretary, Robin Cook, is to see that all these Caribbean offshore finance centres have levels of supervision and control similar to those already found in Europe, whilst the OECD has declared that it wants to see tax havens stamped out. ([www.trustserv.com/](http://www.trustserv.com/)).

Others expressed the opinion that because most Latin American banks have yet to liberalize, Panama's major source of competition remains Miami.<sup>4</sup>

The employment dimensions of international banking in Panama deserve a mention. In 2000, the industry generated 12 800 jobs (compared to 7 000 in the Canal), almost all of which were concentrated in the financial district of the capital, Panama City. Employment data from the Superintendent of Banks indicate that in 2000, 5 153 foreigners – about 35% of the banking employment – worked in this sector. National labour regulations stipulate

that no more than 10% of positions in corporations may be occupied by foreigners unless adequately skilled Panamanians cannot be found; further, firms are required to attempt to train Panamanians for such positions and reduce their foreign employment over time. Thus, interviews with numerous banking officials revealed that managerial positions in many foreign banks are filled with Panamanians, many of whom spent years working their way up the corporate hierarchy. Typically, whereas low-level employees are frequently women, managers and skilled professionals are overwhelmingly male.

### **Silence of the scams: confidentiality, money laundering, and Panamanian financial services**

Offshore banking centres have long suffered from the cloud of suspicion that they constitute little more than havens for tax evasion and money laundering of illicitly obtained funds (Hampton, 1996a; Hampton and Christensen, 1999). As electronic money has come to dominate global finance, the use of offshore banking centres for illegitimate purposes has grown apace. As Wechsler (2001, p. 43) notes, 'Thanks to globalization and advances in banking technologies, distant countries are now just a mouse-click away'. Indeed, just as large corporations can use the Internet and fibre optics to move funds from place to place, so can actors on the 'dark side' of the global economy, including tax evaders, drug cartels, arms traffickers, terrorists and corrupt government officials. The presence of such individuals and organizations has played a key role in structuring offshore banking in Panama and its international competitive position as defined by local differences in regulation.

A key issue in the success or failure of offshore banking centres is the degree of confidentiality that investors feel they can obtain. Indeed, the quality of offshore banking centres is often judged by the quality of laws protecting the privacy of investors. In Panama, numerous private and corporate investors make use of a complex web of holding companies, including ready-made shelf companies provided by Panamanian legal services firms. The use of shell companies, including holding corporations and, increasingly, foundations, blurs legal lines of liability, keeping insurance rates low, and protecting assets (both legal and otherwise) from public scrutiny through deliberately impenetrable webs of cross-ownership that typically deflect even the most dogged of auditors. It is important to note that

while the intent behind such a strategy may be illegitimate, the path taken is not technically illegal. In Panama, unlike the USA tax evasion, unlike fraud, is a penal, not a criminal offence, punishable only by fines, not imprisonment.

Distinct from commercial banking markets, common clients of offshore investment banking services often include High Net Worth Individuals (HNWIs), persons with large assets (generally inherited), often in the range of \$50 to \$100 million, who seek to shelter their funds using lax tax laws overseas and complicated mazes of holding companies to minimize legal liability (Cobb, 1998). Interviews with several members of the Panamanian banking community indicated that while there are some wealthy foreign families that use the nation in this way, HNWIs appear to be less significant in Panama than in, say, the Isle of Man. However, most wealthy Panamanian families are legally 'offshore' in their own country, typically using shell banks incorporated overseas (a favourite is the Cayman Islands) to avoid taxation on their assets and income. Panamanian HNWIs make common use of private foundations, which may own assets but, unlike a trust, not commercial income-producing activities. Panama's recent (1995) private foundations law, based on the well-known model of that in Liechtenstein, allows for estate planning for individuals, in essence importing a corporate model of fiduciary confidentiality to protect the assets of wealthy families by distinguishing legally between the settler's and trustee's assets.

The deregulation of finance globally has accelerated the globalization of mutual funds, many of which are important to offshore banking centres (Graves, 1998; Bogle, 1999). Globally, Luxembourg is a dominant player in this regard, although Ireland and Guernsey have made major inroads into this market (*Offshore Outlook*, 2001), one that Panama would dearly love to enter. The legitimacy of Panama's status as an enclave of offshore banking has been clouded by the presence of several predatory investment trusts, unlicensed by the state, that carry out fraudulent activities designed to milk mutual funds investors of their funds. Promising unrealistically high rates of return, such firms have stolen billions of dollars worth of assets from individuals, a process facilitated by the use of the Internet. Concerned about the impact on its reputation, such firms have been the target of stringent, if often unsuccessful, legal prosecution in Panama.

With the growth of illegal drug exports from

Latin America, primarily to the USA, Panama has long suffered for its reputation as a haven for laundering 'narcodollars' (Robberson, 1993). Given the secrecy of its banking legislation, such charges have been difficult to substantiate or refute. Some sources claimed that allegations of money laundering were simply attempts by Western banks to discredit their competitors in the developing world, an ironic position that turns the margins of the global banking world into a position from which to critique the centre.<sup>2</sup> Others pointed out that money laundering as a global predicament was minimal until the 1980s, when the US declared a War on Drugs.<sup>5</sup> None-the-less, a long history of corruption, with allegations stretching to the President's office, and Panama's proximity (physically and culturally) with neighbouring Colombia, by far the world's leading exporter of cocaine, have led to continued widespread concerns about this issue.

The US Department of Treasury estimates that Colombian narcotraffickers launder more than \$600 million through Panama's offshore banking system annually (Meditz and Hanratty, 1995). The preferred medium for laundering narcodollars has traditionally been the purchase of US Postal Service money orders, which many Panamanian banks now refuse to accept<sup>3</sup>. Faced with high costs of monitoring an overwhelming number of cash deposits in an economy with a weakly developed credit system, many banks opted to pay the minimal legal fines associated with money laundering. In response to continuing suspicion that the nation was little more than a conduit for the legitimization of illegal drug-generated wealth, including, in 1989, General Noriega himself (Dinges, 1990), the USA pressured Panama to sign the Mutual Legal Assistance Treaty (MLAT), which lifts confidentiality in the case of suspected money laundering; other participants in the MLAT include the Cayman Islands, the Netherlands Antilles, the Turks and Caicos Islands, Turkey, and Switzerland. In 1998, Panama conceded to US demands in the form of new legislation increasing penalties for drug trafficking, establishing extradition procedures, and officially making money laundering a crime. These measures included subscribing to the dictates of the Caribbean Financial Action Task Force erected by the USA to combat money laundering. Under this regime, legal requirements to open retail bank accounts were increased, suspicious deposit activity (i.e. repeated large cash deposits) must be reported by law, funds in bank accounts suspected of holding laundered funds may be frozen, and con-

fidentiality privileges suspended. The 1998 reforms also mandated a 'know your customer' provision that requires banks to obtain considerable personal information about their depositors' backgrounds and prohibits anonymous accounts, a measure sanctioned by the US Internal Revenue Service<sup>2</sup>. Generally narcotraffickers use banks without their knowledge that funds are being laundered; however, should the government suspect bank complicity, the bank can be sent down permanently. Several bank officials complained in interviews that these measures are cumbersome to comply with and may frighten away potential investors.

Panama's case is illustrative of a delicate balance between secrecy and transparency that many offshore banking centres are forced to strike. Should their laws and regulations offer too much secrecy, the centre may suffer as reputation as a haven for illegal funds, a force that may discourage legitimate investors (McKee, *et al.* 2000). Conversely, should the centre prove too transparent to auditors and international watchdogs, even investors with legal assets (e.g. HNWI) may be frightened off. Thus, offshore banking centres are continually poised at the knife-edge of marginal legitimacy. In this way, the topography of regulation and the geography of offshore finance become simultaneously determinant phenomena.

In their self-defence, Panamanians pointedly contrast their financial situation with other, even more notorious havens of narcodollars by comparing total bank assets to the size of national economic activity: in Panama in 2000, aggregate bank assets (about \$36 billion) were three times the size of GNP (\$10 billion), whereas in the British Virgin Islands, with \$50 billion in bank assets, GNP totalled only \$0.5 billion. In short, the size of banking assets reasonably reflects the size of Panama's economy rather than the hidden wealth of foreign investors.

## Conclusion

Money, Harvey (1989, p. 167) argues, exhibits the curious property of being 'everywhere but nowhere in particular'. Oscillations in global financial markets over the past three decades – propelled by the ascendancy of neoliberalism, worldwide deregulation, a broad network of telecommunications, and the heightened mobility of capital – have raised greatly the number and importance of offshore banking centres. As Roberts (1994) and Cobb (1998) note, small island states have carved a com-

petitive niche out of this environment by relaxing markedly their regulatory requirements, forming small 'black holes' in the topography of regulation through which large sums of money flow.

Contrary to much received speculation, capital does not flow across some mythical, seamless cyberspace, but is still very much bound up with locally determined social relations. Caution about exaggerated globalization is thus warranted, for such tendencies are inevitably mediated at the local level; that is, globalization cannot productively be viewed in simplistic 'top-down' terms since it proceeds through the integration of the actions of those who view their worlds at both global and local level. As this paper has sought to demonstrate, the dynamics of global money in the specific case of Panama are unique. With the legacy of the Canal, the early dollarization of its economy, the Colon Free Trade Zone and its long-standing prohibition against brass plate banking, Panama differs significantly from other offshore banking centres. Whereas many offshore centres are little more than collections of 'brass plate banks,' in Panama local regulatory restrictions have created a bona fide commercial centre that has become the nation's largest single source of employment and foreign revenues.

Further, as Thrift (1994) and Budd (1999) have argued persuasively, the telescoping of scale from global to local inevitably conjures up the embeddedness of actors in specific constellations of legal and cultural relations. Thus both the Bretton-Woods system and the globalized neoliberal regime that followed relied heavily upon a pastiche of local regulatory structures that placed some localities at the centre of global finance and others at the periphery. Such a view eschews the mechanistic determinism that underpins much literature on finance in favour of one that puts actors first. In Panama, there was nothing inevitable about the emergence of a banking complex; the seminal role of Dr Barletta was instrumental in importing Chicago School neoliberalism and activating the regulatory context that facilitated the emergence of Latin America's most important banking centre. Given widespread concerns about crime, particularly narco-traffickers and money laundering, the regulatory structure of Panama has been forced to negotiate the knife-edge between credibility and secrecy, a trade-off made by investors legitimate and otherwise. When examined within the local institutional light, subject to the contingencies of actors embedded firmly within webs of cultural relations, money

loses much of its abstract qualities and becomes humanized and place-bound.

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### Notes on major interview sources

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3. Ricardo Cucalon, Vice President, BAC International Bank, Panama.
4. Gustavo Adolfo Villa Jr. and Miguel Lee, Division of Economic Studies and Financial Analysis, Superintendencia de Bancos de Panama.
5. Dr Nicholas Ardito Barletta. Barletta's status in Panama and in international economic policy circles deserves brief elaboration. Following his doctoral degree from the University of Chicago, he served as Planning Minister for the Torrijos Administration, Chair of the Banking Commission, during which he started BLADEX. Subsequently, he served as Director of Economic Affairs for the Organization of American States (1970 to 1973), Vice-President of the World Bank for Latin America during the debt crisis of the 1980s, and as President of Panama from 1984 to 1985. During the 1990s he managed to effect the return of Canal Zone territories to the government of Panama.

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