From proprietorship, public companies to pyramid ownership and control: The evolution of the Financialisation of the South African Economy

Introduction

The significance of South Africa's capital markets in the economy is substantial. The country's stock market is valued at twice the value of output as measured by the Gross Domestic Product. It is also larger than the bourses of Mexico, Indonesia and Turkey, whose economies are slightly larger than South Africa (Hassan, 2013). But how did an economy down in the South of the African continent and far away from the dynamic and diversified economies of the east, north and west?

South Africa has historically been integrated into global trade and financial systems since 1652. As it changed hands of political control from the Dutch to the English, Batavia, the English, and the Union that integration had continued. The 1948 National Party victory and the introduction of apartheid resulted in the isolation of the South Africa and capital flight. In this paper it is argued the finance was central to South Africa's integration in the global economy. Proprietors, corporates, private and public account for the development of the South African economy from, agriculture, mining, manufacturing and the tertiary sector.

Economists refer to the deepening of finance in the South African economy from financial institutions, financial markets, and firms to households as financialisation (van der Zwan, 2014). In the South African historiography very little has been written on the foundation of the financialisation of the South African economy and how it has transitioned throughout the period. While there is political commentary on scholarly accounts on financialisation, there have been very few attempts to explore the meaning of such phenomenon in the economy (See Ashman, Mohamed, & Newman, 2013; Pons-Vignon & Segatti, 2013). For example, during the transition period of the 1990s when the South African economy permitted corporates to internationalise and dividends paid to international investors, and the subsequent balance of payments instability and currency volatility, very few studies have researched the phenomenon (Chabane, Goldstein, & Roberts, 2006).

In this paper financialisation is broadly defined. It includes an outcome of intensified intercapitalist and interstate competition during periods of hegemonic transitions (Arrighi, 1994). It also includes the long-term shifts in the underlying structure of the economy that rely on changes in employment and the basket of goods and services produced (Castells, 1996). Finally, financialisation is defined as a pattern of accumulation in which profits accrue primarily through financial channels rather than through trade and commodity production. In this definition financialisation refers to activities relating to the provision (or transfer) of liquid capital in expectation of future interest, dividends or capital gains. The question is what constitutes the relevant evidence for financialisation and how this evidence should be evaluated?

In the paper, Section One presents the transformation of the financial sector in the 1860s. It is argued that the development of the primary sector in South Africa was underpinned by financial inflows raised from London capital markets by entrepreneurs (proprietors) based in London in partnership with South African entrepreneurs who formed part of a network. These networks of merchants provided opportunities in the colonies, such as South Africa for London proprietors who were looking for higher returns elsewhere. The objective is to show that entrepreneurs (proprietors) through networks are able to mobilise finance for investments in new sectors of the economy that can lead to economic change. The paper argues that changes in English Company Act in the mid 1800s allowed sole proprietors to diversify their risks into joint stock companies and thus enabled risk taking in new ventures, particularly in the colonies. The evidence is supported by a case study of the Standard Bank of British South Africa.

In Section Two, the paper presents the changing sources of finances from proprietors to public financial institutions. It is argued that there was a structural shift in the financing of the post-war reconstruction away from entrepreneurs to official (public sector) sources of finance such as the International Bank for Reconstruction and Development (IBRD), commonly known as the World Bank. The paper shows that because of the long-term nature of infrastructure projects such as roads, railways and electricity generation, private financial institutions needed the public sector to guarantee and partner in financing of economic infrastructure, which the IBRD provided in the reconstruction period. Furthermore, the paper suggests that South Africa's role in the formation of the World Bank enabled it to invest in assets in the transport and electricity generation sectors that offered lower returns before 1966.

In Section Three, the paper present the impact of the National Party victory and the isolation of South Africa after the Sharpeville massacre of 1961 and the banning of political organisations such as the African National Congress (ANC) and the Pan Africanist Congress PAC). It is argued that the decision by the apartheid government to go it alone rather than reform apartheid policies led to capital flight was and an misallocation scarce capital. Furthermore, it is argued that the sanctions and foreign exchange controls limited access to international capital and resulted in the prescription of investment in the retirement and life assurance industries. This view in the paper is supported by the evidence that shows how the apartheid state provided tax incentives such as the depreciation allowances to industries and car allowances deductions to corporates and households and various other tax deductions for savings in retirement annuities. In return, the state prescribed what assets should the retirement industry investment in. The paper argues that the excess liquidity in the retirement sector encouraged the pyramid shareholding by corporate and the growth of non-voting shares which were held by the retirement industry ensuring control of the company by few shareholders.

Finally, in Section Four, the paper presents the foundations of the Growth, Employment and Redistribution (GEAR). It is argued that the ANC's resentment of pyramid ownership and control structures (monopoly capital) may have clouded their views of corporate restructuring in a democratic South Africa. As a result what many critics have argued as selling out to corporates by allowing them to internationalise could have been a compromise by the ANC were they sold the view that such an action would lead to foreign direct investment and new competitors in the domestic market. The ANC in return by embarking of fiscal and monetary discipline foresaw the rapid decline of the government debt and service costs, which in turn would allow it to invest on critical infrastructure and social welfare. The paper concludes that what the ANC had perceived that introduction of global competition as an instrument would discipline "monopoly capital and power", would have unintended consequences.

Section One: From proprietorship to banks, financial markets and corporates

The London capital markets remained an important source of funds and skills for the development of the banking industry, particularly in the 1860s prior to the boom of the 1870s. For example, in 1862 the Standard Bank of British South Africa (now Standard Bank and trading as Standard Bank Investment Corporation in the rest of Africa) led by a Port Elizabeth merchant, John Paterson, raised capital in the London Stock Exchange. It was well received because of higher levels of liquidity, which Amphlett (1914) call "easy money and active speculation. The Money Market Review of the 18 October 1862 commented on the capital raising as follows:

> "Scarcely any Colony of the British Crown is advancing more satisfactorily in material prosperity than South Africa, and numerous particulars demonstrating the lucrative nature of the field there presented for capital and enterprise have from time to time been laid before the readers of the Money Market Review. The rate of discount of first-class bills in the Colony ranges from 8 to 12 per cent.; the local Banks divide at rates varying from 12 to 22 per cent, per annum, and the local journals not merely vouch for their solidity, but express wonder that Home capital does not flow more freely to so promising a Colony" (Amphlett, 1914, pp. 6)

The Eastern Province Herald of the 23 December would not have put it better:

> We shall, in fact, be brought into closer and direct contact with monied men of the old world, who will soon find that the South African Colonies offer a fine field for legitimate trading,

> and especially for the profitable employment of surplus capital, coupled with undoubted security (Amphlett, 1914, pp. 8).

The Standard Bank of British South Africa and the London and South African Bank were beneficiaries of the abundance of money and active speculation in London, which led to unprofitable investments in certain cases. However, because of their London shareholders and strong balance sheet the two institutions were able to absorb a number of banks in South Africa that collapsed due to the drought and resistance struggles with the local communities. This resulted into a concentration in the financial sector as players became fewer. These lessons were employed in the development of the diamond industry.

The discovery and development of the Diamond Fields led to a rapid expansion of the Standard Bank of British South Africa. As a result in 1875 the bank became the sole bankers to the Government of the Cape Colony until the absorption of the Colony into the Union in 1910. The Diamond Fields brought a number of challenges to the banking sector in the Cape Colony. The London and South African Bank was absorbed into Standard Bank of British South Africa. However, the Oriental Bank, which had loss making branches in India could not absorb the loss and were taken over the Standard Bank of British South Africa in London through a new vehicle called the London Bank of Africa. The British Special Commissioner annexed the Transvaal Province in 1877 and the bank expanded into the Province rapidly. The banking account of the new Transvaal Government was entrusted with the Standard Bank.

Insert: The Balance Sheet of Standard Bank 1870 -1879

The discovery of diamonds was followed by the discovery gold in the Witwatersrand in 1886, which to an extent overshadowed the importance of diamond mining. However, the experience gained on the diamond-mines and in the diamond company boardrooms proved invaluable in the Witwatersrand. The low ore grade, access to cheap coal and the exploitation of African labour enabled the ores to be mined profitably. In certain cases, the low-grade ore necessitated other sources of finance. In 1887 the Johannesburg Stock Exchange (JSE) was started with the primary aim of mobilising finance for the mining sector. Today, the JSE (now referred to as the JSE Securities Exchange) is one of top twenty largest stock markets in the world and is the sixth largest among emerging markets (after China, Brazil, India, Taiwan and South Korea).

Standard Bank was a catalyst for the consolidation of various Diamond Fields and it was Cecil Rhodes in 1889 that founded De Beers Consolidated Mines who ended up owning most of the output. It is estimated that in 1890 De Beers accounted for about 90 percent of domestic production and the bulk of world production (Gerson, 1992, pp.11). Standard Bank was also instrumental in financing Goldfields of South Africa, a competitor to the Anglo-American Corporation which was established in 1917 by Sir Ernest Oppenheimer through British and American proprietor funding. Sir Enerst Oppenheimer represented A Dunkelsbuhler and Company of London, small member of the syndicate through which De Beers marketed its production, when he immigrated to South Africa at the age of 22 (Gerson, 1992). This signified a shift from proprietors to banks to financial capital markets and big corporations.

Section Two: From Private to public finance in the Reconstruction and Development Period

In the section it is argued that South Africa's participation in WWII cemented its role not only in economic and financial flows but also in international affairs when General Smuts joined Churchill's War Cabinet in 1942. During the period General Smuts met President Roosevelt in Cairo where post war reconstruction and development were also discussed. While World War II was still in an early phase, British and American government officials had begun thinking about arrangements for post-war international economic cooperation (Horsefield & de Vries, 1969).

The Union of South Africa's integration into the global economic and financial system and its participation along the allies in WWII put it at the centre in the envisioning of the post-war reconstruction and development. Schuler & Rosenberg, (2012) argue that the allies wished to prevent the "unrestrained economic fighting of the 1930s," in which economic crisis and lack of international cooperation had led countries to take steps that were politically popular in the short term but destructive to international trade and, in the long term, to domestic markets. They also wished to spur post-war economic rebuilding (Schuler & Rosenberg, 2012). In the plenary session a Statement by President Franklin was read reiterating the purpose of the Conference.

> "It is fitting that even while the war for liberation is at its peak, the representatives of free men should gather to take counsel with one another respecting the shape of the future which we are to win.... [The program you are to discuss constitutes, of course, only one phase of the arrangements, which must be made between nations to ensure an orderly, harmonious world. But it is a vital phase, affecting ordinary men and women everywhere. For it concerns the basis upon which they will be able to exchange with one another the natural riches of the earth and the products of their own industry and ingenuity. Commerce is the lifeblood of a free society. We must see to it that the arteries, which carry that bloodstream, are not clogged again, as they have been in the past, by artificial barriers created through senseless economic rivalries. Economic diseases are highly communicable. It follows, therefore, that the economic health of every country is a proper matter of concern to all its neighbours, near and distant. Only through a dynamic and a soundly expanding world economy can the living standards of individual nations be advanced to levels which will permit a full realization of our hopes for the future." (Roosevelt, 1944)

General Smuts' interactions with Churchill and Roosevelt not only did it lead to the Union of South Africa participating in the United Nations Monetary and Financial Conference in Bretton Woods, which resulted in the formation of the International Monetary Fund (IMF) and International Bank for Reconstruction and Development (IBRD) it also had immediate economic benefits to the Union's economy.

The Union of South Africa team was led by S. Frank N. Gie, the Minister to the United States and participated throughout the Conference proceedings. Other Union delegates included John Edward "Jack" Holloway, the Secretary who was a top career official for Finance and previously a Lecturer and Professor of Economics, Gray University College (1917-1925); later Governor, IMF (1946, 1948); Governor, World Bank (1946); Alternate Governor, World Bank (1948); Alternate Governor, IMF (1949-1951, 1954); South African Ambassador to the United States (1954-1956). Also in the delegation was Michiel Hendrik de Kock, the Deputy Governor of the South African Reserve Bank; author, Central Banking (1939); later Governor, South

African Reserve Bank (1945-1962); Alternate Governor, IMF (1946-1948); Alternate Governor, World Bank (1946-1948, 1949-1963); Governor, World Bank (1948) The were advised my a team of adviser led by Willem Christiaan Naudé who was the Attaché, in the South African Legation, in Washington and later South African Ambassador to the United States (1960-1965) (Horsefield & de Vries, 1969).

Another economic benefit came from Churchill's who initiated in October 1941 that the British government proclaimed that British citizens holding South African paper should surrender them to the British Treasury for settlement. This transaction wiped out most of South Africa's external debt. As a result by 1945 only \$14 million of external debt was outstanding. How did the South African government cut a deal with their British counterparts? First, the South African Reserve Bank sold gold to the tune of \$70 million. The proceeds were transferred to the British Treasury who then returned all the issue paper to the South Africa Reserve Bank. Second, The South African Treasury then issued paper in the domestic market at a coupon of between 2,75 -3 percent to settle the Bonds from Britain, which were now held by the South African Reserve Bank.

Furthermore, the Union of South Africa issued a twelve-year bond with a coupon of 3,25 percent was issued to cover any shortfall in the conclusion of the transaction. Holders of the consolidated stock who were domiciled in South Africa were permitted to hold local stock. The transaction in general benefited both countries by contributing gold to the British war effort and not stirring domestic concerns on the cost of the transaction. Moreover it also ensured that South Africa retained its membership of the Sterling Area and that the country accepted the exchange control arrangements pertaining to Sterling Area countries. Domestic monetary policy was also supplemented by an extensive system of direct control measures to curb inflationary pressures during the war.

At the end of World War II South Africa became part of the international exchange rate system agreed upon in terms of the Bretton Woods agreement, which implied that the external value of the currency and exchange rate stability remained the primary focus of monetary policy, but at the same time retained its membership and the exchange controls of the Sterling Area. In terms of the Bretton Woods agreement of fixed (but adjustable) exchange rates, the US dollar served as anchor currency for the international exchange rate system. The value of currencies was linked to the US dollar, which was, in turn, linked to gold at a fixed price of US$35 per fine ounce (South African Reserve Bank, 2012).

As a result the South African economy came out of the war in 1945 in great shape. The banking system was very liquid and reserves were solid. However, there was an investment and consumption backlog. The discovery of new gold mines in the Orange Free State provided further opportunities for an investment led growth. The low levels of savings in South Africa meant that both the investment and consumption were to be funded by external borrowings. The boom was accelerated and facilitated by huge capital inflows from the UK and expansion of credit between 1947 and 1948. Between 1946 and 1949 the deficit in the current account of the balance of payments widened to £515 million and the foreign exchange reserves shrunk from £266,8 million to £104,6 million during the period (IBRD, External Debt of the Union of South Africa, 1950).

In the face of an investment and consumption backlog, South Africa knew that it needed international capital to prosper. International private banks are comfortable with short-term lending in the form of loans and overdraft facilities. For private international banks to finance long-term investments, knowledge of the sector is critical since it provides the risk profile and expected returns in the sector. However, financing railways and electricity generations where the payback period is longer is unattractive without guarantees from a robust financial institution.

The IBRD saw itself as distinct from private banks with specific characteristics as a partner for development at a Conference of the bank held in Savannah, Georgia in 1946. This view was emphasised by the US Secretary of the Treasury Fred M. Vinson in a debate on the location of the IBRD in New York or Washington D.C. with Lord John Maynard Keynes from Britain.

> “The Fund and the Bank are not business institutions in the ordinary sense…they are cooperative enterprises of governments and their chief business is with governments… The

> business of the Fund and Bank involves matters of high economic policy. They should not become just two more financial institutions." (Asher & Mason, 1973)

It can be argued that Vinson had an understanding of the importance of the financial sector in economic development by channelling resources from sectors where there is a surplus to where there is a deficit (See Arestis & Demetriades, 1997; Weiss, 1995; World Bank, 1988). In these early years of the IBRD based on Vinson's view it appeared as though it was understood, particularly in the US representation what role and position where a development financier such as the IBRD could play when compared to a commercial bank. Since commercial banks tend to follow, instead of leading developments in the real economy. Crucially, commercial banks also rely on information to assess risk and this means that it tends to fund projects in sectors, which are well developed in the economy, on which much is known, and where there are readily available examples.

At its formative years, a number of Americans working for government were skeptical of the IBRD. For example, at the first meeting of the Executive Directors of the IBRD, Henry Morgenthau, the ex-secretary of the Treasury vetoed President's Truman's choice of the IBRD President Lewis D. Douglas in favour of Emilio Collado, the Executive Director of the US, who became the head albeit temporary until Eugene Meyer, was appointed in June 1946.

In Morgenthau's view, Lewis D. Douglas was too connected "with big business and Wall Street, his tie-ins with international financiers, and his general point of view" (Asher & Mason, 1973). A sceptic could argue that Morgenthau was concerned with institutional capture. Eugene Meyer reiterated the role of the IBRD as that of reconstruction and development with a focus on agriculture to address famine and structural change of the primary sector into manufacturing.

Early in 1950, the Vice President of the IBRD, Robert L. Garner visited the Union of South Africa at the invitation of the Union government and conferred with principal official on the reconstruction developmental needs of the Union. A visit by the IBRD Mission soon followed. The Minister of Finance presented the investment requirements in the electricity and transport sectors in an attempt to protect its foreign exchange reserves in the importation of capital equipment.

After the deputy President's visit, an IBRD mission visited the Union of South Africa to conduct a due diligence. The Mission observed that the structure and composition of Union South Africa's economy had changed dramatically between 1939 and 1949. For example, manufacturing grew rapidly from SA£69.7 million in 1938/39 to SA£145 million in 1945/46, representing an increase in its contribution to national income from 18 percent to 21 percent. The structural transformation of the economy and the post-war devaluation of the pound throughout the sterling area in September 1949 resulted in an increase in commodity exports and exacerbated the shortage of electricity. For example in 1949, the Rand electrical system reached critical points between 09:30 and 13:30 when the demand matched the entire available capacity, with no reserve at hand. In 1949 work had been carried out on ten power stations simultaneously

Escom was obliged to explore the possibility of raising loans outside South Africa. Subsequently, the Union of South Africa approached the IBRD initially for a loan of \$60 million. However, only SA£50 million was approved at the request of the Union since it had sourced in additional capital from private international investors. The IBRD in its credit analysis of the Union of South Africa had high fives for the Union's ability to service the debt but was worried about the inter-racial tension simmering to undermine its potential economic performance and therefore its ability to repay the loan. At the IBRD Board of Governors Meeting held in Paris in 1950, the Minister of Finance, N.C. Havenga, made a request for \$60 million or the equivalent in other currencies to finance transport and Escom projects. In January 1951, the IBRD granted Escom a 20-year loan of £30 million with a coupon rate of 4 percent (IBRD, 1951).

<u>Table 2</u>

Present Financial Position of ESCOM

9. The following summarized balance sheet shows the financial position of ESCOM at December 31, 1952, with the 1951 totals shown for comparison.

Balance Sheet

Assets	£SA 000 1951	£SA 000 1952	Liabilities	£SA 000 1951	£SA 000 1952
Expenditure on Capital Account	68,641	88,280	Loan Capital	66,968	84,065
Movable Plant and Equipment (Less Depreciation)	600	705	Interest Accrued on Loan Capital	315	490
Stores and Materials	4,555	5,008	Creditors and Credit Balances	3,296	5,244
Debtors and Debit Balances	1,453	1,488	Temporary Advances Amount due to Bankers Less Cash on Hand Advances at Call	4,302	5,728
Investments (Housing Loans)	204	294	Redemption Fund	15,734	18,302
Investment of Redemption Fund	15,249	17,661	Amount Amortized on Account of Deferred Liabilities for Assets and Rights Acquired	194	217
Investment of Reserve Fund	2,421	2,407	Deferred Liabilities for Assets and Rights Acquired	172	150
Balance on Revenue Accounts of Undertakings (Deficit)	128	546	Reserve Fund	2,271	2,192
Totals	93,251	116,389		93,251	116,389

10.(a) The loan capital shown above at December 31, 1952, consisted of the following:

	£SA 000,000
Local registered stocks	76.82
Amount drawn down from IBRD loan	6.48
Amount drawn down from £ 7 million Exim-Bank loan	.77
	84.07

(b) The redemption fund is a fund created for the redemption of ESCOM's loans in not more than thirty years from their issue, on a sinking fund basis at 3-1/2% compound interest, as required by the Electricity Act. ESCOM's present practice is to provide for

The loan provided for part of the imported equipment for the seven new power stations, the installation of additional capacity in existing power stations, and for the construction of high-voltage transmission lines. These projects required total expenditure of £59 million during the years 1950-1955. In order to ratify the loan agreement, Parliament passed special Act, the Electricity Supply Commission Loan

Agreement Act of 1951 (Christie, 1978). The Act guaranteed Escom loans, meaning that should Escom default the Union Of South Africa would step in and make good.

> "Minister of Finance may, on behalf of government, on such terms and conditions as he may deem fit, guarantee the repayment of any loan…."

This did not mean that Escom could pass on all its liabilities to the state but only after it exhausted all its revenues and assets would the state step in. South Africa was the second African borrower after Ethiopia. Egypt, Ethiopia and South Africa were the only African countries that took part in the formation of the International Monetary Fund and the IBRD in 1944 (Kritzinger-van Niekerk, 2016). This marked the beginning of a long-term mutually beneficial relationship between the IBRD and Escom. Both institutions focussed on reconstruction and development dominated and controlled by engineers, thus facilitating Eskom's easier access to the IBRD and three additional loans were approved in each of the three years after the first loan of 1951.

> "Over a short span of eight years from 1952 to 1959, Escom started the construction of eight new power stations of its own and added boilers and generators to six existing stations. Stations rose almost overnight like mushrooms in fertile soil" (Conradie & Messerschmidt, 2000).

Conradie & Messerschmidt (2000) argue that the early of the 1950s wer globally challenging. Many countries including the Union were characterised by a shortage of electricity, skilled labour and raw materials such as copper, steel, cement and bricks, inputs in the reconstruction and development effort. This problem was also exacerbated by a shortage of capital. Delays in the production of heavy machinery forced engineers to be innovative. The second half of the decade was characterised by economic growth in which Escom and IBRD played an important part.

During the decade of the 1950s Escom's generating capacity increased from 1514 MW to more than £479 MW – an increase of 130 percent (Conradie & Messerschmidt, 2000, pp. 125).

Escom's capital investment in power stations and transmission and distribution sytems amounted to just over £188 million in 1960. About £35 million came from international funders and the rest from domestic sources indicating the deepening of domestic capital markets. Escom's revenue alos increasd from £9,5 million to almost$41 million per annum between 1950 and 1960. The revenue was driven by supply of of power to ventures such as the Western Deep levels Mine and bulk sales to municipalities.

Section Three: Apartheid Self-sufficiency and Going It Alone

The defeat of General Smuts by the National Party in 1948 indicated that the post-war political settlement would be vulnerable under Nationalist rule. In 1960, a referendum to establish a republic was supported by 52 percent of the white electorate. Prime Minster Verwoerd led the new Republic out of the Commonwealth because of its anti-apartheid stance. Traditional allies also distanced themselves from the republic. In April 1961, at the UN, Australia, and the UK aligned themselves with a US resolution calling about the end of apartheid.

In 1961 led by Robert Mangaliso Sobukwe, a Pan Africanist Congress march by 20 000 people led to a massacre of 69 people on the 21 of March. The government declared a state of emergency but failed to prevent mass protests around the country. This prompted the state to introduce legislation to limit freedom of speech, press freedom and the freedom of movement. The state jailed many leaders forcing the ANC and the PAC to go into exile to wage guerrilla warfare against the apartheid regime.

It was during this period that Eskom undertook studies to determine the optimal configuration of a national integrated system (Conradie & Messerschmidt, 2000). Building power station became more expensive that transmission lines between the Cape and the Transvaal and as well as the cost of coal. Moreover the economical sizes of power stations and their turbo-generators grew even larger because of the pooling of all power and demand sources. This resulted in better economies of scale, and help reduced the unit cost of electricity nationwide. This enabled Eskom to fulfil its ambition for a power network to interconnect the whole of the sub-continent of Southern Africa.

However, this required an amendment of the Electricity Act authorising Eskom to supply electricity in bulk to its neighbours. Eskom was authorised and ventured into the mountain kingdom of Lesotho in 1967. In 1969 Eskom started a cross-border supply to the border of Ressano Garcia in Mozambique and the supply to Swaziland was finalised in 1973.

In 1966 the Apartheid government had decided “to go it alone” than reform in the face of criticism against apartheid policies after the Sharpeville massacre of 1961. In this paper it is argued that the relationship between the IBRD and South Africa given South Africa’s role in its formation ensured access to private capital that latter enabled the capturing of key ANC leaders and the subsequent financialisation of the South African economy.

These actions by the apartheid state intensified isolation closing the doors of international lenders and the after effect of the post-war boom of the 60s led to a competition for capital pushing interest rates up. Eskom focussed in managing escalating costs by forecasting demand and planning raising its first bond of R175m in the domestic market. Steyn (2006) argues that the forecast of a 10 percent increase in Eskom capital expenditure for the next ten years (1971 – 1981) was wrong since it assumed the continuation of increase in electricity demand, which had grown over 105 percent between 1961 and 1970. Eskom could only borrow locally for long-term investment.

In the 1970s it became apparent that investment in electricity infrastructure had not kept up with growing demand as the reserve margin dropped below 15%. In addition, core to industrial policy was to leverage Eskom to beneficiate coal into electricity so as to enable the development of a range of other mineral processing activities such as steel production, aluminium smelters. The result was an extremely energy intensive growth with demand in electricity more or less double that of GDP growth. Figure One shows Eskom’s capacity additions that added 26GW between 1976 and 1993 of generating capacity to the network. The build program was characterized by the construction of very large "six pack" generators in proximity to coal mines to realize large economies of scale.

Figure One Capacity Additions in the 70s and 80s (Eberhard, 2007)

Table 6.1. *Dates of commissioning of major Eskom power stations*

Name of power station	Date of commercial service First–Last unit	Net maximum capacity MW
Komati	1961–1966	906
Camden	1966–1969	1520
Grootvlei	1969–1977	1130
Hendrina	1970–1977	1900
Arnot	1971–1975	1980
Kriel	1976–1979	2850
Koeberg	1976–1985	1840
Matla	1979–1983	3450
Duvha	1980–1984	3450
Tutuka	1985–1990	3510
Lethabo	1985–1990	3558
Matimba	1987–1991	3690
Kendal	1988–1993	3840
Majuba	1992–2001	3843

Source: Eskom Statistical Yearbook, 1995.

Eskom has been roundly criticized for the apparent over-investment in infrastructure during the 1980s build program as shown in Figure Two below. However, this must be seen in the context of an economy that grew on average at 0,7% annually between 1980 and 1992 compared to an annual average growth rate of 3,5% between 1970 and 1980. Energy growth decreased annually from 9,3% on average between 1970 and 1980 to 4,8%, a decline of nearly 50%. Had growth been sustained at the previous rates in this period, Eskom would have required additional build during the 1980s (over and above what was actually built in that period).

The over-investment was also a result of how managerial incentives were structured. Steyn (2006) points out that a key finding of the De Villiers' Commission of 1986 was that ESCOM's excessive investment decisions lay with a "distortion in managerial investment incentives." The De Villiers' report suggested:

"That for ESCOM managers the route of minimum risk involved the avoidance of public and political criticism about the utility's possible inability to supply power… This resulted in "over insurance" and unnecessary costs which could in turn be automatically recouped by increasing prices". (Steyn G. , 2006)

Figure Two: Overinvestment in Capacity in the 70s and 80s (Steyn G. , 2006)

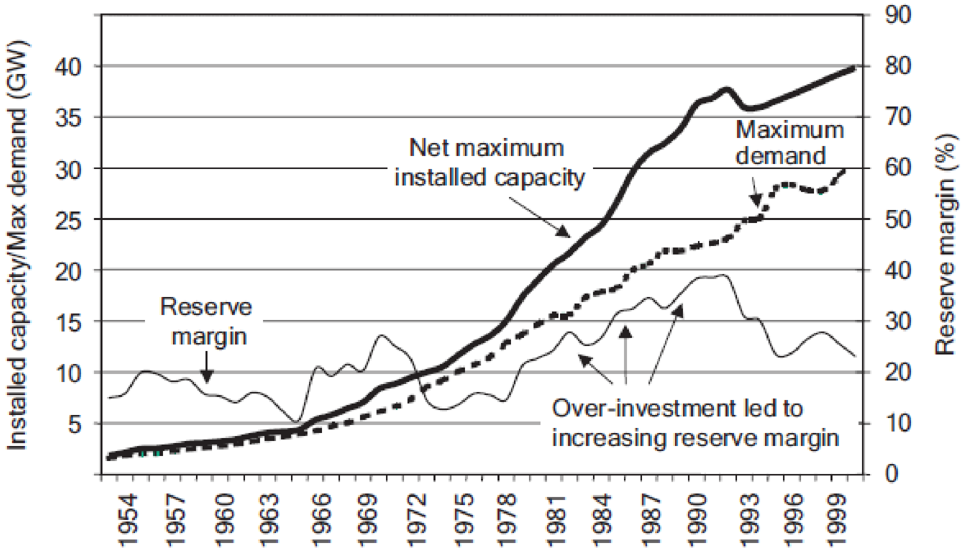


Figure 6.1. Historical growth in maximum demand and capacity at Eskom
Sources: Eskom Annual Reports, 1980–2002; Eskom Statistical Yearbooks, 1985–1996

Figure three shows the link between the tariff and capital investment program. Figure Three shows that the consequence of the build program with minimal economic growth was not just over-capacity, but also required major price spikes in order to meet the interest and capital repayments associated with the new assets. These price spikes were severely exacerbated by a price determination methodology based on historical costs, rather than a methodology that smoothens the tariff process such as a current cost methodology (i.e. a replacement value that indexes the assets against inflation), although both approaches provide the generator with an identical return over the life of the asset. As part of the fall-out associated with the price spikes the De-Villiers Commission of Enquiry was convened that resulted in 1986 that ESCOM became Eskom, in Eskom being corporatized and paying taxes and in Eskom being run under much more commercial disciplines.

By 1991, it was recognized that there was scope for significant efficiency gains in Eskom that would enable a reduction in the electricity tariff and Eskom entered into a compact with government to reduce the tariff by 15% in real terms between 1992 and 1996 so as to leverage electricity as part of an investment promotion strategy. An additional deal was done in 1995 to reduce the tariff by a further 10% by 2000 for a total real price reduction of 25% compared to 1991. This put the Eskom tariff beneath either a historical or current asset cost tariff determination methodology.

Figure Three: The Link between the Tariff and the Capital Investment Program (Eberhard, 2007)

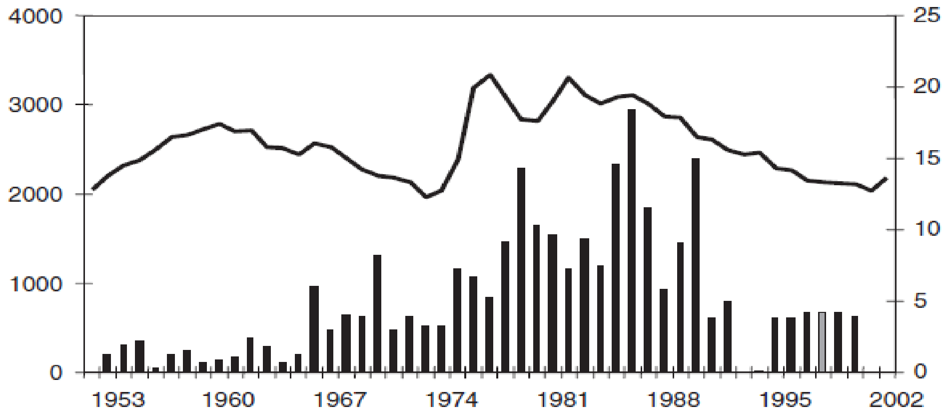
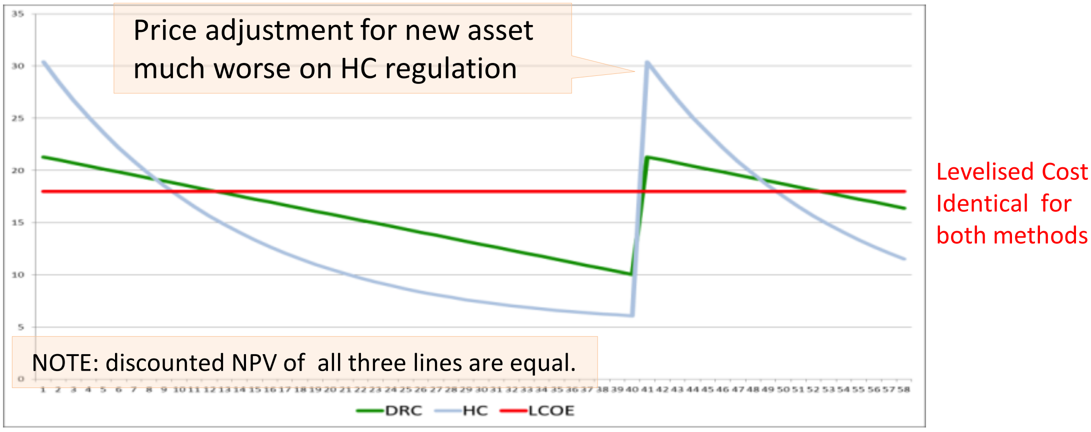


Figure 6.2. Eskom capacity expansion in MW (*bar*) and electricity price in SA cents/kWh (*line*), 1950–2000
Sources: Eskom Annual Reports, 1980–2002; Eskom Statistical Yearbooks, 1985–1996.

Figure Four: Comparison of Historical Cost and Current Asset Cost Tariff Trajectories



HERE I NEED TO TALK ABOUT PRESCRIBE ASSETS. THE DOMINANT ROE OF THE RESERVE BANK AND ITS RELATIONSHIPS WITH THE SWISS BANKS AND HOW THESE FLOWS WERE TRANSFERRED FROM THE SOUTH AFRICAN RESERVE BANK TO THE BANKING SYSTEM. THE SOURCES OF SAVINGS AND HOW THEY WERE DEPLOYED. THE GROWTH OF PYRAMID COMPANIES AND THE ESCALATING DEBT OF SOUTH AFRICA AND DEBT STANDSTILL. THE PRIVATISATION OF ASSETS

Section 4: From Isolation to Period 1990 - 1994

In the period between 1966 and 1990, the South African corporate landscape changed dramatically. There were about five to six large diversified group of companies that were structured in the form of a pyramid. Distinction should be made between a conglomerate and a pyramid. In a conglomerate the top holding company owns claims to dividends in several diverse operating companies. The shareholders of conglomerates all have the same pro rate claim to dividends in its various branches or subsidiaries. This condition, however, is not met with respect to the various shareholders involved in broader pyramid groups (Gerson, 1992).

HERE I WILL FOCUS ON TWO OF THE CONGLOMERATES THE REMBRANDT GROUP AND THE ANGLO-AMERICAN/ DE BEERS GROUP.

FOCUS ON THE TRANSITIONARY PERIOD AND MANDLA'S VISITS TO THE OPPENHEIMERS AND HASHING OF THE "ALLEGED COMPROMISE". INTRODUCE THE ANC ECONOMIC POSITIONS LEADING TO GEAR ECONOMIC POLICY. THIS WILL FLOW NICELY TO THE DEMOCRATISATION OF THE SA ECONOMY.

THEN I WILL LOOK INTO THE DATA: FOLLOWING GREAT KRIPPNER'S APPROACH TO TEST THE HYPOTHESIS OF THE FINANCIALISATION OF THE SA ECONOMY IN THE PAST TWENTY-TWO YEARS.

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