THE ORIGINS AND IMPLICATIONS OF SOUTH AFRICA'S CONTINUING FINANCIAL CRISIS

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When in the latter half of 1985 South Africa was struck with a shocking debt crisis which forced the government to declare a temporary moratorium on all short-term debt repayments, some economic commentators said the crisis derived largely from the careless policies of the South African Reserve Bank. The deregulation of exchange controls had gone too far between 1983 and 1985, and the SARB had encouraged reckless borrowing overseas. A period of monetary stringency and fiscal restraint should restore South Africa's foreign accounts, which had always been considered very sound.

Four years later, however, there are no signs of a return to what once was considered normality. Foreign reserves are lower than they were after the Sharpeville massacre, when the country was considered on the brink of insolvency. After Sharpeville American loans restored confidence in the economy, and South Africa entered a period of very rapid growth, especially in manufacturing. In 1989, four years after the current debt crisis broke, the South African government is scratching for foreign exchange, and capital is draining from the South African economy almost as fast as it poured in during the 1960s.

The peril of insolvency casts a shadow over South Africa's growth prospects, and over every government activity, or plan, from attempts to finance the privatisation of Eskom (*Sunday Star*, 6.6.88), through plans for upgrading black townships (Boraine, 1988), to the pursuit of war in Southern Africa (*Cape Times*, 5.8.88; *New York Times*, 8.7.88). Moreover, every time the economy begins to boom, the government is forced to turn it off because of balance of payments pressures arising primarily out of the debt crisis. Periodic interest rate hikes and credit restrictions since 1985 illustrate the severe constraints placed on the South African economy in large measure because of its current position in international capital markets.

Today both liberal incrementalists and Nationalists push for socio-economic improvements in the black communities as a prelude to, or substitute for, political change. The government believes that black political demands can be softened if the socio-economic needs of the advanced sectors of black communities are given greater attention (Boraine, 1988). The incrementalists, in the liberal tradition, believe that 'what lies ahead is a slow and often painful path in which economic advance will often be the forerunner of political advance' (Godsell and Berger, 1988; *Cape Times*, 28.7.88). For these prognoses to be feasible the economy would have to grow at a rate of well over three percent per year, yet the Reserve Bank is forced to constrict the supply of domestic credit and restrain demand long before this level of growth is reached.

Why did the 1985 credit crisis tilt South Africa into this economic and political predicament, how has the crisis affected South Africa and its relations with its trading partners in the years since 1985, how have creditors and debtors responded to the difficulties, and what are the economic and political implications of the continuing crisis? (see Lind and Espaldon, 1986; Harris, 1986; Martin, 1986; Padayachee, 1988). I will argue, against some recent writers, that external economic pressure, to which sanctions have contributed, has pressurised the apartheid regime, in part through the politicisation of the financial crisis (see Lipton, 1988, for one differing perspective; Kaplan, 1986 for another). I will also argue, against the incrementalists, and in accordance with some Latin American experiences (see, for example, *Politics and Society*, 1988; Stepan, 1985), that economic vulnerability and weakness, rather than economic growth, can force the state to shift into a serious reformist mode.

The Roots of the Financial Crisis

The reason for the government's apparently counterproductive behaviour in turning off the boom just when it appears to be lifting South Africa out of crisis is simple: South Africa has to compensate for the export of capital which takes the form of compulsory debt repayments, royalties, interest and dividend payments, and unrecorded or illicit flows.

South Africa has always experienced an excess of imports over exports during domestic booms, mainly because of its dependence on imported machinery, technology, and intermediate goods like oil and chemicals (Kahn, 1987a, 1987b). The trade account deficit had to be financed through capital inflows of various kinds — a condition typical of the balance of payments constraint that limits the options of many developing countries. If South Africa runs a deficit on the capital account (if investment and financial flows are negative) as it has since late 1985, it must run a surplus on the current account to balance international transactions. This means cutting down on the kind of imports that could sustain the boom, by cutting off the boom through fiscal and monetary actions (Kahn, 1987b; Black and Stanwix, 1987; Jenkins, 1987).

Under such conditions growth is cut short, and investment will fail to materialise. As Anglo American Corporation chairman Gavin Relly put it, 'Our heavy commitments for repayment of external debt, inability to raise long term loans, and limited access to overseas trade credits oblige us to forgo or divert very substantial resources that were formerly available for productive investment' (*Cape Times*, 26.7.88).

During the 1970s, as was true for many other capital importers, foreign direct and indirect investment from abroad slowed and credit took its place in the capital account of the balance of payments. At the same time, savings declined to a very low level, reflecting the onset of stagnation and the continued escalation of poverty and unemployment in South Africa. Medium- and long-term credit was required to finance the projects of parastatal companies such as the monopolistic Electricity Supply Commission (ESKOM) and the gas-from-coal corporation, SASOL, and was also used by government departments, such as the Department of Posts and Telegraphs (*ICABA*, 5, 1987/88). In the 1980s private companies inside and outside the banking sector became increasingly dependent on foreign loans for financing their capital expenditure (Padayachee, 1988).

At first longer-term syndicated loans were most common, but later the securities market was tapped more often, and private domestic firms as well as public corporations became dependent on credit which South African banks raised abroad (see Tables 1 & 2). The structure of South Africa's foreign liabilities altered well before the debt crisis surfaced. The composition of South Africa's debt changed in three important ways. In the early 1980s the proportion of the debt that was short-term (maturing in less than one year) rose rapidly. As Table 1 indicates, short-term debt rose from 49 percent of total debt in 1980 to 72 percent in 1985. Factors contributing to this development include transnational banks' (TNBs) fears after the Mexico default in 1982, uncertainty about South Africa's economic and political future, the growing sanctions movement, and the willingness of South African borrowers to accept relatively unfavourable terms. The very high levels reached by South African interest rates drove borrowers abroad for short-term loans, largely in the form of interbank loans. Politically sensitive lenders, particularly those in the United States where the sanctions movement was growing, found that 'lending to South Africa through the interbank market provided a near perfect disguise, since transactions through the interbank market are never published' (*Daily Telegraph*, 7.9.85).

Table 1:

South Africa's Foreign Debt 1980-1986

	For. Debt US$ million	For. Debt SA Rand million	F. Debt as % of GDP	Short-term For. Debt	Short-term Debt as % of Tot. For. Debt
1980	16 890	12 595	20,3	6 188	49,1
1981	18 889	18 081	25,5	10 573	58,5
1982	22 609	24 249	30,4	13 725	56,5
1983	23 954	29 116	32,5	19 169	65,8
1984	24 294	48 230	45,7	32 804	68,0
1985	23 473	60 142	50,0	43 273	72,0
1986	22 593	49 513	35,2	35 816	72,3
1987	22 618	43 593	N.A	N.A.	N.A

(Source: South African Reserve Bank *Quarterly Bulletin*, December 1987)

Table 2:

Percentage Structure of South Africa's Foreign Liabilities

	1970	1980	1983	1984
Equity capital including shares reserves & undistributed profits	60,1	48,6	34,7	27,2
Loans to private sector	23,6	22,6	29,1	37,1
Loans to public corporations & local authorities	5,2	16,5	13,7	11,5
Loans to central government & banking sector	11,1	13,7	22,5	24,2
Total	100,0	100,0	100,0	100,0

(Source: Pamela Freer, *South Africa into the 1990s: Growth for Survival*, Economist Intelligence Unit, 1986.)

Table 3

South African International Borrowing 1974-1987(1)

(all in millions of U.S.Dollars)	1	2	3	4	5
1974	774,8	50,0	—	724,8	
1975	944,4	308,4	88,5	547,5	
1976	826,9	25,0	59,5	742,4	
1977	33,2	33,2	—	—	
1978	481,9	143,9	338,0	—	
1979	270,7	11,0	232,6	27,1	
1980	750,0	172,2	192,8	385,0	
1981	403,0	92,0	271,8	39,2	
1982	1 333,4	153,9	160,2	1 008,8	10,5
1983	768,3	329,1	203,2	136,0	100,0
1984	1 233,0	618,3	395,6	187,8	31,3
1985	849,5	745,3	56,9	47,3	—

1. Funds raised on the Int. markets. (i.e. total cols 2+3+4+5 see (1))
2. Int. issues of Bonds by SA borrowers.
3. Trad. Foreign Issues of bonds, SA borrowers
4. Int. medium and long-term bank loans.
5. For. Med. & Long Tm Bnk Loans

(1) The data is drawn from OECD *Financial Market Trends*, Vol 27, March 1984; OECD *Financial Statistics Monthly*, 1987, No 10. Note that an international (or 'Euro') bond is one that is placed simultaneously on the market of at least two countries and is not necessarily denominated in the currency of either. A 'traditional' foreign issue is one that is placed, generally by a domestic syndicate, on the market of a single country. Similarly, an international loan is a Eurocurrency loan, while a traditional foreign bank loan is a domestic currency credit extended by a bank or group of banks in one country to a non-resident borrower. All the items in the table are for periods greater than one year.

A second change in the composition of South Africa's debt was the movement from conventional long- and medium-term loans to securitised borrowing. Table 3, which summarises the composition of South Africa's revealed borrowing between 1974 and 1985, shows an unmistakeable trend away from medium- and long-term loans and into bonds. From 1983 the inflow of capital in the form of longer-term loans and securitised debt was not, however, great enough to compensate for the outflow of funds in the form of licensing, royalty, interest, dividend payments, and investment. The gap between savings and investment, as noted, was bridged with short-term loans. The trend *towards* securitised debt matched international trends, as did the trend *away* from long-term loans. But, certainly in the case of US banks which switched earliest into short-term loans, the latter trend had political precipitants too.

Thirdly, it appears that South Africa's major creditor nations have shifted relative positions since the debt crisis of 1985. US and UK banks have been repaid the soonest and the most, increasing the relative importance of continental European banks as South Africa's creditors, rather than the traditional UK and US banks. Most important would appear to be banks in the Federal Republic of Germany and Switzerland.

The trend towards obtaining longer-term financial capital from continental Europe, especially Germany and Switzerland would appear to have begun some time before the credit crisis. In 1984 three of the top five lead-managers in South African international bond issues were banks of the Federal Republic of Germany. In 1983 all four top international South African bond issuers were FRG banks, and in 1982 the three top banks were German (*Euromoney International Bond Annual*, 1985). *Euromoney* surveyed twenty top international bond issuers in 1986 and found that of the four banks to have lead-managed South African debt issues in 1985, two were German and two were Swiss (*Euromoney International Capital Markets Annual*, 1986).

But the services of the European banks could not offset the outflow of capital. While the South African economy had experienced net capital inflows during the course of its great post-war boom in import-substituting manufacturing (except during the immediate aftermath of the Sharpeville massacre), the periods 1977-80 and from late 1983 onwards have been characterised by capital outflows. In the late 1970s the economic difficulties, including severe domestic inflation, brought about by the oil price rise, combined with the political turmoil of the Soweto uprising in 1976 to discourage investors. The economy experienced negative growth in 1977, none in 1978. The crisis was ended by the second international oil crisis which helped rocket the price of gold in 1979 and 1980 and relieve the South African economy (see Table 1). In 1983 the loosening of exchange controls by the South African government was accompanied by chance by a South African recession brought on by declining inflation in the West and a falling gold price. As a consequence of this coincidence, disinvestment escalated.[1]

Though the 1970s recession hit it like it did other countries, South Africa profited from the oil price crises and Western stagflation through a rise in the price of gold sparked by inflation and world-wide fears of further inflation. Gold had been freed from the fixed rate of $35 per fine ounce when US President Nixon dissolved the Bretton Woods agreement in December 1971. The metal hit a peak of $194 per fine ounce in December 1974, and another in late 1979 and early 1980 when the price of gold rose to $850. But by mid-1984 oil prices had declined and, as inflation eased off in the advanced industrialised countries of the West, the dollar rose, the gold price drifted downwards, and with it fell the South African rand (*Financial Mail*, 6.5.88). While a decline in the rand allowed the rand price of gold to increase, though its dollar price fell, the weakness of the rand undermined South Africa's ability to repay its debts (*International Currency Review*, 18 (1), 1987).

The currency collapse in 1985 precipitated the credit crisis and the withdrawal of short-term credit. This exacerbated South Africa's capital account deficit and forced the government to restrict imports and currency flows so that an adequate current account surplus might allow the repayment of loans.

In sum, South Africa's foreign debt has tended to rise since 1970, slowly at first, then dramatically during the early 1980s, before stopping with the 'freeze' in 1985. As Table 1 indicates, in 1980 South Africa's total foreign debt stood at $16 890-million which, in rand terms, was 20.3 percent of the country's GDP. By 1984 foreign debt reached a peak of $24 298-million which in rands was 45.7 percent of the GDP (reflecting in part the decline of the rand against the dollar). In 1985, though the dollar value of South Africa's debt declined slightly, the continuing depreciation of the rand took the debt up to 50 percent of its GDP at about the time that South Africa stopped payment on short-term debts. By June 1986 principal of nearly $500-million in short-term and 1.5-billion in longer-term debts had been repaid. However, in mid-1989, in spite of the repayment of some of the principal, the debt remained at about $22-billion. This was higher than might have been expected because some of South Africa's debt is held in hard non-dollar currencies such as Swiss francs and Deutsche marks, which appreciated against the dollar after 1985.

The financial crisis

At the end of August 1985 the South African government closed the foreign exchange market for three trading days. Shortly before it reopened, the government imposed a unilateral moratorium on South Africa's short-term international debt, as a response to US banks calling in their loans. Short-term debt had reached over 70 percent of South Africa's total foreign debt of $24-billion. By February 1986 a South African negotiating team and the creditor banks had come to an interim agreement about repayment, but confidence in South Africa's economy was shaken.

In August 1984, in an attempt to counteract persistent double-digit inflation which put South Africa increasingly out of step with its major trading partners, the South African Reserve Bank pushed the prime lending rate up to 25%, way above the inflation rate and much higher than US rates, even though US interest rates were regarded as high at that time. The South African prime interest rate first rose above 20% in 1981. Interest rate differentials and the absence of controls enticed South African banks to borrow short-term funds abroad, especially in the US, and to re-lend it for longer periods in South Africa on the expectation that the differential would allow repayment. Two South African banks, Barclays National and Nedbank, opened branches in New York. The Nedbank branch in particular was very active in interbank borrowing in London and New York (*Euromoney*, December 1985).

Nedbank, the largest South African controlled bank at that time, was freer to expand internationally than the British controlled Barnat and Stanbic (*Euromoney*, December 1985). The *Financial Mail* commented that Nedbank, whose short-term interbank loans were re-lent as longer term domestic loans, 'had been thought by U.S. banks to be travelling in dangerous waters'. The *Financial Mail* also reported that some 50 percent of Nedbank's foreign borrowings had been re-lent to the South African public sector and parastatal corporations (*Financial Mail*, 9.9.85).

The overborrowing of short-term interbank funds that created the preconditions for the credit crisis of 1985 was also in some measure the consequence of weak administration of the South African treasury (*Financial Mail*, 10.7.87). In its application of a 'liberal attitude' to overseas borrowing in the early 1980s, the South African Reserve Bank failed to keep track of the transactions that took place. International borrowing was encouraged without the Reserve Bank paying attention to the nature of the accumulating debts incurred. As the managing director of a South African bank put it: 'The Reserve Bank's reporting systems were inadequate. Its free market philosophy seemed to extend to its not requiring information' (*Euromoney*, December 1985). Moreover, 'adjusted' forward rates quoted by the Reserve Bank to South African banks 'that were repaying foreign credits too soon' (in the words of Reserve Bank governor Gerhard de Kock) encouraged the banks 'to take the gap and increase foreign debt' (*Financial Mail*, 10.7.87). Indeed, six months before the crisis broke, a Citibank report on the South African rand observed that 'South Africa's external finances are in total chaos'. The South African Reserve Bank, it noted, paid 'no regard whatsoever... to the maturity structure of the debt', allowing more or less uncontrolled short-term interbank borrowing by South African banks (Citibank, 1985).

As the dollar continued to rise against all currencies and the rand continued its decline begun in 1983, the interest rate differential on South Africa's short-term overseas borrowings, especially those denominated in dollars, failed to compensate for the rapid growth in the rand value of the loans. While the US dollar value of South Africa's debt grew by 34 percent between 1980 and 1985, its rand value grew by 293% (derived from Table 3). The Reserve Bank struggled to shore up the rand's value first by shifting the payment to the gold mines for gold from US dollars into half-and-half in dollars and rands, then selling almost all South Africa's foreign reserves, and 'mortgaging' much of its gold holdings through gold swaps (Citibank, 1985). (A gold swap is an exchange of a quantity of gold for finance at an agreed rate of interest, for an agreed period of time. South Africa's gold swaps are normally arranged by Swiss banks.)

When these measures failed, South Africa's credit-worthiness was called into question. A Citibank report noted in March 1985 that 'with the country's credit rating having deteriorated, it is difficult to see how debt refinancing on the scale required... can possibly be achieved' (Citibank, 1985).

On 20 July 1985, after ten months of almost continuous unrest in the Transvaal and Eastern Cape, the South African government declared a State of Emergency in 36 magisterial districts, and detained hundreds of anti-apartheid activists. A few days later the government of France announced restrictions on French investment in South Africa. In the week after the emergency measures were announced the market value of shares on the Johannesburg Stock Exchange fell by R11-billion. Brokers described the wave of selling, mainly by US, UK, and French shareholders as a 'bloodbath' (*Star*, 28.7.85, cited by Harris, 1986). In the same week there were rumours that Chase Manhattan, Citibank and some other banks would refuse to renew short-term loans to South Africa, many of which were to fall due at the end of August (*Evening Standard*, 31.7.85, cited by Harris, 1986).

On 31 July it was announced that Chase Manhattan Bank would neither extend credit on maturing short-term loans to South African borrowers, nor advance credit to South African new private borrowers. The next day Chase Manhattan's lead was followed by the Security Pacific Corporation, and during August other American banks took the same path (*New York Times* and *Wall Street Journal*, various issues, 8 & 9.85).

Since the last quarter of 1980, US banks had increased lending to South Africa nearly five-fold. By August 1985 interbank lending made up roughly two-thirds of all US bank lending in South Africa, and 85 percent of all US loans to South Africa were short-term. In contrast, about 57 percent of British loans to South Africa, and 31 percent of German loans, were short-term (Lind and Espaldon, 1986:2). British banks began to follow suit in mid-August and withhold new credit, and even German and Swiss banks soon refused to fill the breach left by the American banks (*New York Times*, 15.8.85). A British banker claimed 'that whatever pressure American bankers put on South Africa, Japanese banks take off... South Africa's a good investment for people who can stand the political heat' (*New York Times*, 1.8.85). It would appear, though, that the Japanese were less heat-resistant than the Swiss.

On August 15 State President PW Botha delivered a major policy speech, the 'Rubicon', which offered nothing in the way of concessions to the rightless black people of South Africa, nor did it point to any alternative way out of the crisis. Instead Botha lashed out at overseas pressure for reform. The following morning the rand fell by 20 percent on the Johannesburg foreign exchange market. On August 27 the rand reached a record low of $0.35, and the government suspended all trading on the Johannesburg Stock Exchange, and in foreign exchange. The Governor of the Reserve Bank, Gerhard de Kock, flew to London, New York and Washington to negotiate relief, but failed.

On September 2, the day before the exchanges reopened in South Africa, the government announced a three-part package of measures to relieve the debt crisis. Firstly, the repayment of the principal of a large part of the debt, \$10-billion of the \$14-billion that was short-term, was suspended until December 30, and during the intervening period debtors and creditors would negotiate revised mutually acceptable terms of repayment. Several categories of loan, including government guaranteed loans, trade credits, and loans from the IMF, were excluded from the moratorium in South Africa's attempt to retain some credibility as a borrowing nation and to encourage the continued flow of essential credits (Martin, 1986; *ICABA*, 3, 1986).

Secondly, the two-tier currency system that had been abolished in 1983 was reimposed. The two tiers consist of a 'commercial rand' with which most transactions are undertaken and the exchange rate of which is managed by the Reserve Bank, and a 'free-market determined' 'financial rand' which has to be used in foreign investments in South Africa, and disinvestments. The supply of financial rands is limited and its value depends on the volume of investment. If the demand for financial rands for investment is low, the price of the financial rand is low, and if investment increases, it rises. In a disinvesting climate the value of financial rands would be very low, and would diminish returns on the sale of South African assets, while at the same time making foreign investment in South Africa seem very attractive financially (Harris, 1986:800). The financial rand has been discounted at rates of more than 40 percent off the commercial rand. Such a two-tier structure had been abandoned in 1983 in an attempt to induce foreign investor confidence, but this action, combined with political and economic crises, had encouraged massive disinvestment, especially in 1985.

The third measure was the alteration by the South African government of the mechanism which determines the value of the rand. The free-floating exchange rate, under which the rand had lost almost a third of its already much-diminished value in little over a month, was converted into a 'managed float', subject to greater Reserve Bank intervention.

After South Africa declared a payments moratorium, the creditor banks set up a committee to negotiate repayment terms. The committee of 29 banks, representing 233 creditor banks, chosen partly from amongst South Africa's biggest creditors, and partly to ensure geographic representation. South Africa appointed a mediator who was acceptable to the banks: Mr Fritz Leutweiler, chairman of Brown Bovieri and former chairman of the Bank of International Settlements. It also set up a standstill coordinating committee under the leadership of Dr Chris Stals, the Deputy-Governor of the South African Reserve Bank. The two committees met for the first time in London in October 1985. A second meeting scheduled for November was cancelled, apparently due to political pressure. In December South African anti-apartheid clerics Archbishop Desmond Tutu, the Reverend Allan Boesak, and the Reverend Beyers Naude called on the country's creditors not to reschedule outstanding loans unless fundamental political reforms were undertaken by the government.

South Africa's once secure position in international capital markets had been badly eroded. Late in 1985 the US Interagency Country Exposure Review Committee lowered its rating of South Africa's credit-worthiness to having 'transfer risk problems'. The Swiss Board and the Bank of England similarly saw lending to South Africa as more risky. The *Bank Credit Analyst* declined to recommend South Africa on political and economic grounds, and South Africa's credit rating in the annual *Euromoney* listings fell from 31st place in 1985 to 60th in September 1986 (*ICABA*, 6, 1988).

South Africa was forced to extend its unilateral moratorium until the end of March 1986. A meeting eventually took place in February 1986 and the parties present arrived at an interim agreement in terms of which South Africa undertook to pay an initial instalment of 5 percent ($500-million) of the outstanding funds to be paid in instalments (to be negotiated between individual debtors and creditors), and to reschedule the remainder of the debts by March 1987. A technical committee of 12 major banks, three each from the US, the UK, Germany and Switzerland, would oversee the process (*Financial Times*, *Wall Street Journal*, 21.2.86).

At a meeting with the technical committee in March, though the banks apparently attempted to increase the initial instalment to be paid by South Africa, the 5 percent level was accepted, but a larger proportion was to be paid up-front by mid-1986. US banks were apparently exerting pressure on South Africa to pay up more quickly. The interim agreement was to last until June 1987, at which point South Africa would have to renegotiate the remainder of the outstanding frozen loans (*Financial Times*, 17.3.86). The rolled-over loans would earn rates between 0.5 and 0.75 percent higher than LIBOR (the London interbank offered rate), or 1 to 1.25 percent over the pre-moratorium rates (*South African Digest* 18.4.86, for the first version; *Wall Street Journal*, for the second).

It should be noted that South Africa was obliged, in theory, to repay the full amount on the loans which fell outside the net — the long-term loans, IMF loans, government guaranteed loans and trade credits. South African bankers estimated that about $3.6-billion in debt excluded from the original repayments squeeze was due to be repaid by July 1987. However, South African officials said that only about $2-billion of this amount was repaid, indicating that TNBs must have rolled over, or renewed, loans outside the net to the value of about $1.6-billion (*Euromoney*, December 1986). In February 1986 South Africa withdrew its SDR 70-million deposit from the International Monetary Fund, but it had to repay IMF loans amounting to SDR 950-million by November 1987 (*International Financing Review*, 608, 8.2.86; *Euromoney*, December 1986).

Rescheduling negotiations were due to be resumed in September 1986 but were preempted when the South African Ambassador to London, Dr Dennis Worrall threatened Western governments that South Africa might renege on the agreement if the governments of creditor nations imposed sanctions on South Africa (*International Financing Review*, 629, 5.7.86). This failed to stop the passage of the Comprehensive Anti- Apartheid Act in the U.S. which prohibited the extension of certain new loans. South Africa repeated the threat to renege after Commonwealth leaders (but not Britain) agreed to an import ban on South African coal, steel, and several other products (*International Financing Review*, 634, 9.8.86).

For a time it appeared as if Dr Leutweiler had resigned his mediating post in anger at South Africa's policies, and he was absent from negotiations in September 1986 between the South African government and the technical committee of the creditor banks (*Financial Times*, 8.9.86). But negotiations continued. The banks sent a team of economists to South Africa to establish whether South Africa's balance of payments would permit it to step up the first year's repayments to the creditor banks to above 5 percent. The bankers concluded that the country's economic situation would not permit it to increase payments and agreed to defer further negotiations until April 1987 (*Financial Times*, 8.9.86; *International Financing Review*, 641, 27.9.86).

Discussions in fact took place in March 1987 when South Africa came to a new agreement with 34 banks representing its creditors. In the lull after the Comprehensive Anti-Apartheid Act and major banking disinvestments, and with the State of Emergency suddenly cutting television coverage of South Africa, the banks apparently made no political demands and agreed to a package which was very gentle to South Africa. Large parts of the credits were to remain frozen, unless they were converted into another form of asset such as long-term debt repayable over 10 years, deposits, or equity investments. Only 1.5-billion of the frozen loans had to be repaid for the duration of the new accord, which was to last for three years until June 1990 (*ICABA*, 6, 1988).

Politicising the crisis

When the TNBs refused to roll over their South African loans in August 1985, their primary motive was, no doubt, concern about the recoverability of the loans. The fact that it was American banks that acted first, and that American banks had shifted most definitively into short-term loans, indicates the importance of political considerations. American banks had long been under pressure to cut ties with South Africa; the bank that pulled the plug, Chase Manhattan, had disinvested from South Africa a decade-and-a-half earlier under domestic political pressure, though it continued to serve South African borrowers — especially American transnational corporations in South Africa (Wilson, 1986).

American banks were more sensitive to domestic political pressure, which broadened dramatically after the South African army was called in to stem a new wave of revolt in the Vaal triangle in September 1984. Such pressure, often exerted through student/church coalitions, and coordinated by anti-apartheid organisations, also existed in Britain, and to a lesser extent on the continent of Europe (see Hirsch, 1989). These organisations, such as the British End Loans to South Africa campaign, and the German Kein Geld fur Apartheid were able to further politicise an already unusually political debt crisis. In South Africa church leaders Dr Beyers Naude and Archbishop Tutu called on the TNBs to refuse to reschedule South Africa's debt until major political reforms were undertaken by the government. In response, though creditor banks were unwillling to define exactly what steps South Africa needed to take to restore creditworthiness, they said political reforms had to be enough 'to satisfy public opinion in the West, and lift pressure from lobby groups on bank creditors, particularly in the US' (*Financial Times*, 17.6.86).

South African business groupings responded to the crisis with unusually extensive reform proposals, and were eventually followed by the government which promised several reforms in January 1986. Shortly before the final part of the first rescheduling negotiations in March 1986, South Africa lifted its limited State of Emergency. Not long after the negotiations were completed the South African government imposed a new more comprehensive State of Emergency, and several business groups retreated from their reformist positions (see Hirsch, 1989).

By early 1987 pressure on South Africa had eased somewhat with the passage of the US Anti-Apartheid Act the previous October, and with the effectiveness of the 1986 Emergency as regards both the suppression of protest, and the muzzling of the local and international press. The South African government wisely rushed the debt negotiations to completion before the effects of the swing to the right in the May elections could be felt internationally.

South Africa's financial links post-crisis

Since the debt crisis South Africa has found it difficult to raise any new loans, though new finance has entered the country. South African borrowers and their creditors take great pains to keep their transactions secret. In a 1987 *Eurobank* survey of South African banks, 'none was prepared to give even the slightest detail' of their international operations (*Euromoney*, Special Supplement, 'South African Banking', April 1988, pp 34, 27).

In the past, major syndicated loans or bond issues in favour of South African clients were publicised in the form of 'tombstones' in financial publications. Since 1986 all financial publications have recorded zero public loans and bonds in favour of South Africa (reflected in Table 3), yet there is ample evidence that funds have been made available to South African borrowers. As early as February 1986 it was announced that ESKOM — the parastatal electrical supply utility — was seeking R300-million ($120-million) abroad that year and expected to have little difficulty obtaining it (*Financial Mail*, 14.2.86). In the first quarter of 1987, according to Nedbank, South Africa 'reported a net inflow of R533-million, the first net inflow in ten quarters. This can be attributed to improved overseas sentiment, reflected in a preparedness to roll-over debt *and grant new loans* (own emphasis), as well as to the debt standstill' (Nedbank Bulletin *Guide to the Economy*, August 1987). Later that year the bank reported that 'public corporations were successful in raising new loans abroad and contributed just under R700-million ($340-million) in the first half of the year (1987)' (Nedbank *Guide to the Economy*, November 1987). In March 1988 the South African Reserve Bank reported that 'fairly substantial net drawings of R817-million ($380-million) were made in 1987 by public corporations on new and existing loan facilities for project financing' (South African Reserve Bank *Quarterly Review*, March 1988).

In March 1989 the government's Finance Department announced that it was confident of negotiating R200-million in new foreign loans in the current financial year, and that it had received 'R195-million in new finance through private placements in the previous financial year' (*Business Day*, 17.3.89). Lenders were expected to be Swiss based. These sums are very small relative to South Africa's foreign debt, or to its budget deficit, but they indicate that the government still has access to discreet sources of foreign finance.

Lenders avoid the public gaze by using interbank loans,[2] private 'on shore' and off-shore banks to channel funds, manipulating short-term trade credits, rolling over existing loans. Foreign exchange reserves are replenished through the use of discreetly arranged gold-swaps. Small private banks in Switzerland, the Federal Republic of Germany and the Benelux countries are 'known to be involved in gathering finance for South Africa, often through hidden complex deals' (*ICABA*, 5, 1987/88).[3]

Access to credit does not necessarily entail new loans, or even the rolling over of loans falling outside the net. Within the net the interim repayment agreement is not compulsory if the creditor does not enforce it, and roll overs might appear attractive to some lending banks, especially at rates of interest 1.0 to 1.25 percent above LIBOR (*South African Digest*, 28.2.86, 18.4.86). By late 1987 the German Deutsche Bank, unlike most banks in the US and UK, had received *no* repayments from South Africa since the rescheduling agreements. There was no overall reduction in the exposure of banks from the Federal Republic of Germany to South Africa and Namibia (*ICABA*, 5, 1987/88). As noted above, outstanding loans were rolled over.

Money is also still available on the interbank market, at a price. For instance, secret documents leaked through the End Loans to South Africa campaign in mid-1986 showed that the Toronto Dominion Bank was offering credit up to $24-million to two South African banks, Standard and Volkskas, at a premium of up to 1.25 percent over the charge on previous interbank loans to South Africa (*Guardian*, 1.8.86). Since the embarrassing disclosure, political pressure forced the bank to cut its South African ties (*ICABA*, 4, 1987).

Some banks have recently made equity investments in South Africa. The Scheizerische Gesellschaft fur Kapitalanlangen bought the Bata Shoe Company in South Africa after its Canadian owners were placed under great pressure to disinvest (*ICABA*, 5, 1987/88). The Swiss bank renamed the company Futura Footwear. The bank had probably taken up the South African offer to convert outstanding debt into equity, announced early in 1987.

As political pressure on TNBs dealing with South Africa has grown in the USA and the UK, banks in the Federal Republic of Germany, Switzerland, Belgium Luxembourg and France have taken an increased proportion of the South African business. A report in 1986 noted the important role played by Swiss banks in financing South Africa before and after the credit crisis. The three big Zurich banks — Union Bank of Switzerland, Credit Suisse and Swiss Bank Corporation — all have representative offices in Johannesburg, and 'at least one of them is reported to have been far more accommodating to South Africa on loans than any of the other major banks' (*Euromoney*, December 1987). At the time of the debt crisis about 80 percent of the giant parastatal South African Transport Services' borrowings were denominated in Swiss francs and Deutsche marks (*Financial Mail*, 16.10.87). In late 1986 the managing director of a major South African bank remarked:

> The U.S. and Japanese banks are very conscious of their governments' sanctions against South Africa and are mostly uneasy about, even opposed to, dealing with us. But the Europeans are more relaxed. They admire what we have done repaying debt (*Euromoney*, December 1986).

Dr Chris Stals, then director-general of the South African treasury noted more recently,

> There are regional differences in the attitudes of banks in the world, which one can understand. The political pressure in all countries is not the same. In the U.S. there is now legislation against apartheid and so you cannot expect much activity from there. But it is not the same for German, French or Belgian banks and investors (*Euromoney*, April 1988).

More recently, partly as a consequence of the 'internationalism' of the Dellums/Cranford sanctions bill currently before the US Congress, business and government in Japan and the FRG have shown increasing sensitivity to sanctions calls. The slow but steady growth of sanctions movements in these countries and in Switzerland, France and Belgium, were boosted, especially in Europe, by the murder of ANC representative Dulcie September in Paris, and promise to gather strength in the near future. These anti-apartheid groupings, still rooted in the churches and in student movements, are not yet as strong as similar organisations in the UK and the USA.

On the question of raising new loan finance, Department of Finance director Stals noted that 'One must be modest in one's expectations, but there are possibilities, maybe more from the providers of capital equipment than loans initially, but all this counts as finance' (*Euromoney*, April 1988). This is critically important for it points to the central significance of trade finance in South Africa today as the major form of new credit.

When South Africa declared a unilateral moratorium on short-term debt in September 1985 it specifically excluded trade credits from the standstill net. Trade credits, largely short-term, were to be repaid on schedule so that new credits would be made available for South African imports. Most banks that declared that they would end loans to South Africa specifically excluded trade credits from the ban. The United States 1986 Comprehensive Anti-Apartheid Act, like similar measures elsewhere, excludes trade credits from the the US loan ban (see United States, 1988). Similarly, long-standing Japanese restrictions on credit to South Africa exempt trade credits from the ban. The Federal Republic of Germany in 1977 set a DM 50-million ceiling on the size of trade credits to South Africa that would be guaranteed under its Hermes credit guarantee programme. However, the ceiling was high enough to guarantee most trades with South Africa, and 'it is probable that the German government has occasionally permitted exporters to link DM 50-million guarantees to cover larger transactions', such as in the case of the export of capital equipment a SASOL coal liquification plant in 1979 (Spindler, 1984:46-48).

Most of South Africa's trade, which amounts to $10-12-billion per year, is financed through trade credits. As South Africa's director general of finance put it:

> If the world banking community should effectively exclude South Africa from international trade and payment systems, it would be a much more effective sanctions measure than trade sanctions applied by governments. It would put us on a barter system overnight (*Euromoney*, March 1987).

Approximately $3-billion of the $10-12-billion annual trade credits is insured by government export credit organisations, of which the biggest insurers are the UK and Japan (Lind and Koistinen, 1988). The United States, though it still allows credits, no longer insures them through its Eximbank.

Since they again became freely available to South Africa in 1987, trade credits have played a critical role in South Africa's international credit structure. Not only do they make it possible to import products, including capital goods for expansion, but they allow long-term borrowing to take place. Trade credits can extend for as short as 3 to 6 months for consumer goods, but as long as 5 years for capital goods. In effect it is possible to convert trade credits into loans; how much this is happening is impossible to say as 'both borrower and lender observe a strict code of secrecy' (*Euromoney*, March 1987). The Governor of the South African Reserve Bank exhorted importers to use foreign credit during foreign exchange crunch periods, and made special arrangements to cheapen its cost, in order to bring in foreign loans, however small, for however short a time (*Finance Week*, 27.4.89).

A notable new development in recent years has been the increased involvement of South African companies in off-shore trade financing for South African importers. Two companies, GDM and Sasfin, recently reported very rapid growth in business, profits and earnings (*Cape Times*, 2 & 16.8.88) Sasfin reported pre-tax income growth of 201 percent for its financial year ended June 1988. As the managing director of Sasfin explained:

> The credit squeeze being applied to importers through the reluctance of overseas suppliers to extend trade finance to SA importers has increased demand for our off-shore finance facilities — a trend we see increasing in the future, particularly with political pressure on foreign credit insurers and suppliers to apply sanctions against SA (*Cape Times*, 16.8.88).

Though companies like Sasfin may attempt to fill the gap created by trade finance sanctions, it is doubtful that they could fully make up for the loss of foreign supplies of finance. Both companies cited are still very small. Also, as the market narrows, the cost of trade finance will inevitably rise. This points to the ultimate effect of most sanctions: even if they cannot completely cut off supplies or markets, they do make business more difficult, and more expensive.

Resurgence of the crisis

In mid-1988, South Africans were sharply reminded about the sensitivity of the economy. A relative gold glut brought the price of gold down in early 1988, and made it difficult for South Africa to sell its gold. As the 1987 mini-recovery encouraged import growth the rand declined, leading the economy to lapse into a balance-of-payments deficit. Fears soon surfaced that South Africa would be unable to repay the close to $1-billion scheduled for the year, and bankers called for austerity led by higher interest rates (*New York Times*, 1.7.88). In spite of measures taken by the Reserve Bank to contain credit, by the end of July 1988, gold and foreign reserves, measured in US dollars, had fallen by 28 percent since December 1987, at which point they stood at a critically low \$2.3-billion (*Argus*, 8.8.88).

After a temporary recovery, the reserves resumed their decline in 1989 in dollar terms, because of the rise of the dollar, the fall in the price of gold, and the continued rush of capital out of the South African economy. The capital account continues to lose the equivalent of 4 percent of the GDP annually, making up a net outflow of about R25-billion since 1985. Part of the capital outflow is debt repayment, within and outside the net, some of it foreign investment by South African companies, perhaps for sanctions busting, but a good deal of it flows through irregular channels. Foreign exchange fraud is estimated to account for at least R1-billion out of South Africa's 6.5-billion capital outflow in 1988, and the Reserve Bank recently undertook a major staffing reshuffle to try block foreign exchange leaks (*Finance Week*, 4.5.89).

The next three years will be particularly tough because of South Africa's debt repayment obligations outside of the net — longer-term loans and bonds. South Africa is obliged to repay \$1.7-billion in 1989, \$2.1-billion in 1990, and \$1.5-billion in 1991. The next round of short-term debt rescheduling talks are due to be completed in 1990, and promise to be even more politicised than before because of a campaign to put political pressure on South Africa through its debt crisis orchestrated by the Commonwealth. Some banks with outstanding short-term credits in South Africa have recently converted as much as \$3.5-billion to longer-term obligations, presumably to avoid political embarrassment during and after the rescheduling talks. The banks known to be involved in such conversions are significantly the American banks Manufacturers Hanover Trust and Citibank (*Business Day*, 26.4.89; *Finance Week*, 20.4.89).

Representatives of capital are increasingly anxious about the economic dangers of isolation. A confidential ASSOCOM report in 1988 warned that the government had to 'encourage the process of political change' to avoid further sanctions (ASSOCOM, 1988), and the director general of the South Africa Foundation made a series of public appeals along similar lines (*Argus*, 16.4.89). Moreover the Governor of the Reserve Bank made an unprecedentedly strong intervention in the political process when he warned that any amount of economic reform would be useless without political reforms 'and a consequential easing of stresses and strains in South Africa's relationships with other countries.' If the current rate of capital outflow continued, he warned, South Africa could expect a GDP growth rate of no higher than 2 percent (*Finance Week*, 18.5.89).

* * *

The debt crisis will remain with us as long as South Africa remains in a state of relative instability, and it consequently contributes to that instability. There will not be a miraculous recovery as in the early 1960s, for two reasons. Firstly, the government has not proved it knows a way out of the political crisis; repression has not worked as efficiently as it did in 1960-61. Secondly, and more importantly, South Africa presents no great investment prospect today, with gold in the pits, high inflation, and a stagnant domestic and regional market.

As the recent church delegation to the United States (Tutu, Boesak, Naude and Chikane in May) clearly recognised, the continuing debt crisis represents both disaster and opportunity. Pressure on South Africa's balance of payments has immediate effects through the deflationary policy the government is forced to pursue. The political connections are not difficult for the Governor of the Reserve Bank to draw, and this is increasingly true for the business sector and the white population at large. The September elections are likely to revolve around economic issues, as white living standards (and black) continue to plunge. Political pressure through the financial crisis may turn out to be a powerful lever in the struggle against apartheid.

Notes

1. The wave of disinvestment of the 1980s thus seems to have preceded the resurgence of the sanctions movement in late 1984 and reflected primarily the private calculations of firms. See, for example, the report of the Stamberger Institut 'The Economic Impact of Sanctions Against South Africa', Tables 18 & 19, with regard to investments by firms from the Federal Republic of Germany (where sanctions movements were relatively weak).
2. Nedbank, one of South Africa's most active traders in the interbank credit market, now has offices in London, New York, Frankfurt, Hong Kong, Zurich, the Cayman Islands and Jersey (*Euromoney*, Special Supplement South African Banking, April 1988, p7).
3. It has also been noted in the financial press that two South African Deutsche Mark issues took nearly three years to be listed on German exchanges. Normally listing take less than one year (*International Financing Review*, No. 705, 02.01.88).

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