FINANCIALISATION IN SOUTH AFRICA: EXAMINING THE FINANCIAL CONDUCT OF NON-FINANCIAL ENTERPRISES, BANKS AND HOUSEHOLDS

NUNO JORGE RODRIGUES TELES SAMPAIO

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Department of Economics
School of Oriental and African Studies
University of London

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Abstract

Financialisation addresses the rising importance of the financial sphere in contemporary capitalist economies, but the concept has remained theoretically vague, often failing to go beyond the narrow confines of the rise of finance and to examine the broader interaction of finance with the rest of the economy. Furthermore, scarce attention has been paid to the relevance of financialisation to developing countries, particularly to middle-income countries. South Africa is an important case-study that enables a stronger conceptualisation of financialisation, encompassing its relation to developing countries.

The thesis first develops a political economy approach to the concept of financialisation by drawing on recent work that stresses the changing conduct of non-financial enterprises, banks and households. A theoretical framework for financialisation is developed and is then set against the empirical reality of South Africa. To be specific, the thesis examines the evolution of financial flows as well as of the financial position of different sectors – focusing on non-financial enterprises, banks, and households - during the post-apartheid period, thus testing the relevance and applicability of financialisation to South Africa.

The thesis shows that the South African economy is indeed a financialised economy, but which nevertheless presents a number of distinguishing features for each sector due to the specific domestic historical context and connections with the world market. Non-financial enterprises have become increasingly engaged in debt and equity markets, but still rely on traditional sources of funding, such as bank credit. Banks have targeted households as a rising source of income, but investment banking activities have remained marginal. Finally, households have accumulated increasing volumes of debt, although with unequal distribution and cost, reflecting the extreme inequality of the South African society. The results presented contribute to a more robust understanding of financialisation in developing counties showing its variety of form as a phase of capitalist development.

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Acronyms and abbreviations

ANC	African National Congress
APR	Annual Percentage Rate
ATMs	Automatic Teller Machines
BEE	Black Economic Empowerment
Bn	Billion
BRICS	Brazil, Russia, India, China and, depending on the account, South Africa
CAPM	Capital Assets Pricing Model
CDO	Collaterized Debt Obligations
CEOs	Chief Executive Officers
CMBS	Commercial Mortgage Backed Securities
CME	Coordinated Market Economy
EU	European Union
FDI	Foreign Direct Investment
FIRE	Financial, insurance and real estate
FoF	Flow of funds
GDP	Gross Domestic Product
GEAR	Growth, Employment and Redistribution
IMF	International Monetary Fund
IT	Information Technology
JCI	Johannesburg Consolidated Investment
JSE	Johannesburg Stock Exchange
K	Thousand
Km2	Square kilometre
PIH	Permanent Income Hypothesis
LCH	Life Cycle Hypothesis
LME	Liberal Market Economy
LSM	Living Standards Measure
M&A	Mergers and Acquisitions
MEC	Mineral-Energy Complex
MERG	The Macroeconomic Research Group
Mn	Million
MVBS	Motor Vehicle Backed Securities
NCDs	Negotiable Certificates of Deposit
NEPAD	New Partnership for Africa's Development
ODC	Other Deposit Corporations
OECD	Organisation of Economic Co-operation and Development
PIC	Public Investment Corporation
PNs	Promissory Notes
RiY	Reduction in Yield
RMBS	Residential Mortgage Backed Securities
ROA	Return-on-Assets
ROE	Return-on-Equity
SARB	South African Reserve Bank

SDRs	Special Drawing Rights
SNA	System of National Accounts
SSA	Statistics South Africa
TNCs	Transnational Corporations
UK	United Kingdom
UN	United Nations
UN-HABITAT	United Nations Human Settlement Program
US	United States of America
VoC	Varieties of Capitalism
WAAPR	Weighted Average Annual Percentage Rate

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1. Introduction

1.1. Crisis and financialisation

The past five years have been marked by the biggest world recession since the Great Depression of the 1930s. The world economy has been going through a long period of economic crisis and financial turmoil. Having begun in 2007 with the rise of subprime defaults in the US, this crisis reached its pinnacle with the bankruptcy of the American investment bank Lehman Brothers in September of 2008, causing an international financial panic and subsequent collapse in international trade. Economic growth plummeted and unemployment rose around the world. After the massive injection of public funds into the economy, and particularly the financial system —an intervention which prevented another major depression—the centre of the crisis has now shifted, toward sovereign debt in Europe and the euro, and geographically from the major financial centers—the US and the UK—to the periphery of the eurozone.

As in the Great Depression, this crisis had its origins within the financial sphere. However, two important differences apply. The first is the new global economic context out of which this crisis originated. On the strength of the technological progress, market liberalisation and privatisation of the economy that have driven public policies around the world in the last three decades, financial markets became highly integrated—constituting probably the only truly globalised market—and their size and power grew to an unprecedented level. The second major difference is the crisis's epicentre. The financial crisis was launched not by a stock market crash, but by the increasing household defaults of a particular new credit market, the subprime. This market, targeting poor households with no previous access to credit, was more risky but also more profitable. This process unveiled the recent transformation in the operations of banks: the new relative weight of households as their debtors.

Nonetheless, this ongoing crisis unfolded amid a chorus of warnings, starting with the mid-1990s financial boom, from the margins of the economics profession and the alter-globalisation movements. A stream of research had been produced on the rise of the financial sphere and its implications for job creation, income distribution and increased economic instability. Attention was devoted not only to the inner mechanisms and impacts of finance, but also to its profound implications for the functioning of the economy and related transformations in social life, from labour relations — under the pressure of demands for shareholder value — to the financially mediated access to essential goods such as housing or retirement pensions (Plihon, 2001). This new financial hegemony has been identified in political economy as “financialisation”.

This concept of financialisation has, however, proved elusive. Gerald Epstein (2006) argued that it is difficult to have a narrow concept of financialisation, since the term is used in quite diverse ways: the ascendancy of shareholder value in corporate governance; the dominance of capital-based financial markets over bank-based ones; the explosion of financial trading; a new pattern of accumulation where financial profits dominate; the rise of a rentier class, etc. Epstein offered abroad definition, which has since proven recurrent in academic research: “the increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of the domestic and international economies” (2006: 3). In another popular definition, Gretta Krippner described financialisation as a “pattern of accumulation in which profits accrue primarily through financial channels rather than through trade and commodity production” (2005: 174)[1]. Although these definitions point to the capitalist nature of this transformation, they point to its application in a wide variety of contexts.

While these definitions are easy enough to accept, in their breadth they leave the mechanisms behind the emergence of financialisation largely unspecified. They are compatible with various interpretations of the roots and meaning of this new capitalist phase. The operational use of financialisation as a concept seems to be lost at this degree of generality—the rising importance of the financial sector—which even raises the question of whether the use of this concept to describe the dominant configuration of contemporary capitalism is justified. After all, financial hegemony is far from being a new development in the history of capitalism (Arrighi, 1994).

On my view, financialisation needs to be conceptualised through a more substantive analysis of the transformations at the heart of this process. Hence, the first question that frames this dissertation: what is the content of financialisation in a modern economy? Financialisation has been the object of research in number of different theoretical currents within political economy (post-Keynesianism, Marxist political

[1] A definition close to the one used by Arrighi (1994), for which she finds empirical evidence in the U.S. — both for rising portfolio income and for the ratio of portfolio income to profits (three to five times greater than in the 1950s and 60s).

economy, regulation school, etc.) as well as in other social sciences, such as geography and sociology. My research thus begins with an overview of theoretical debates around the concept.

Contemplating the most recent theoretical contributions, produced in the wake of the current international financial crisis—which, given its scope, necessarily changed the way financialisation is to be understood—I broadly base my theoretical framework on the most recent efforts in Marxist political economy, as presented by Lapavitsas (2009, 2012), Dos Santos and Lapavitsas (2008) and Dos Santos (2009). Put briefly, on this account, financialisation is the result of major non-financial corporations' increasing degree of direct access to money and capital markets in their search for funding. It is contended that banks reinvented their operations, directing their operations to financial mediation between corporations and financial markets (a reinforcement of investment banking activities) and redirecting credit to households (where new information technologies would play a crucial role in creating the trust and confidence necessary for the banks' expansion into this new market). These transformations, on this analysis, are possible only thanks to the neoliberal processes of liberalisation, deregulation and privatisation that swept capitalist economies during the last decades, putting households in a new, asymmetric, vulnerable position vis-à-vis of the financial sector.

Having established my theoretical framework, to be used critically, I can move on to the research question that this dissertation tries to answer: Is South Africa a financialised country? Given its presentation as a structural transformation of contemporary capitalism itself, research on financialisation in geographical settings that lie outside the international financial centers is of paramount importance to establish its specificities and variations. More generally, the attention devoted by Marxist political economy to the historical and social character of economic processes raises the question of the specificities of financialisation in different national settings. Only through the comparative study of specific national settings, which are prone to have their own "theoretical generative properties" (Peck and Theodore, 2007), can new theoretical contributions be made to research on financialisation. Hence, given South Africa's particular history and integration into the international economy, does financialisation carry some explanatory power with regard to the country's path during recent years?

Given the stress put on the weight of the financial sector, attention in financialisation studies has been devoted mainly to the most developed countries, where the financial sector is more mature and powerful. This bias has been reinforced by the developed-country focus of the current financial turmoil[2]. Moreover, despite being affected by the related collapse of international trade, a number of large middle-income economies—the so-called BRICS: Brazil, Russia, India, China and, depending on the account, South Africa—have been acknowledged as having enhanced the resilience to external shocks in recent years (Rodrik, 2011). These countries have even been presented as emerging economic powers, capable of replacing the traditional economic centers as the powerhouses of the world economy. The historical, economic and social realities of these "emerging" countries varies widely, and the causes of their recent economic flowering differ greatly, from state-led processes of industrialisation during recent decades (as in China) to reliance on commodity boom prices over the second half of the 2000s (Brazil, South Africa). Nonetheless, if financialisation is to be part of a systemic approach to contemporary capitalism, research is needed on its origins, content, and impacts, in light of the current financial turmoil, in countries that lie outside of the international financial core.

1.2. Financialisation in South Africa?

The South African economy, having embarked on the international liberalisation and deregulation of finance beginning in the 1980s, has witnessed a profound restructuring since the end of the apartheid era. Characterisations of the South African economy have normally pointed to its dual reality, with a modern economy centred around capital-intensive sectors such as mining and energy production and an underdeveloped informal economy on which large swathes of its population remain dependent. Understandings of this dual nature vary, from the official stance of Thabo Mbeki (2003) of the existence of a successful first-world economy that lives beside a third-world economy, with the fostering of the former to compress and trickle down its successes to the latter, to Marxist political accounts that identify South Africa as an example of "uneven and combined"[3] development where in large informal and backward sectors reproduce the inexpensive labour force that

[2]This focus contrasts with the interest dedicated to so-called "developing countries" and financial crisis during the 1980s, 90s and early 2000s — from the "debt crisis" of the eighties to the Asian financial crisis in 1997 that subsequently affected countries such as Russia (1998) and Argentina (2001).

[3] The "uneven and combined" nature of capitalism was first theorised by Trotsky (1906) with regard to Tsarist Russia's combination of and unevenness between capitalist industry and serfdom. It has since been used to explain the persistence and deepening of differences in capitalist development (Ashman, 2009).

feeds the success of the more formal economy, eventually leading to problems of overaccumulation (Bond, 2006).

Aided by the liberalisation and deregulation of markets and strict monetary and fiscal policies during the 1990s, large conglomerates unbundled their activities and expanded their operations internationally. Simultaneously, financial liberalisation enabled the growth of capital inflows and outflows, where the domestic legal and illegal capital flight promoted by these conglomerates was compensated by foreign inflows, particularly in the form of portfolio inflows in search of undervalued post-apartheid South African assets and high domestic real interest rates.

The South African financial sector has risen exponentially, being probably the most dynamic sector in the whole economy. This growth in the importance of the financial sector has led researchers on political economy in South Africa to draw on the concept of financialisation. The recognition of financialisation in South Africa is, however, normally limited either to the assessment of the financial sector as the driving force of economic growth with limited impacts on productive investment and the overall welfare of the population (Southall, 2010) or to its role in serving the South African conglomerates' interest in internationalisation and capital export (Fine, 2008, 2010), being taken in this context as a constraining force on the democratic state's ability to pursue developmentalist policies (Marais, 2011).

Mohamed (2010), recognising the still scarce research on financialisation in South Africa, identified domestic financialisation not only with the growth and influence of the financial sector but also with rising international capital flows in the context of the declining importance of the mineral and energy sectors. Here financialisation is the result of international liberalisation and abundant liquidity on international financial markets, offering the "private sector access to credit (…) associated with increased debt-driven consumption by households and speculation in real estate and financial asset markets" (2010: 22). Ashman, Fine and Newman identify financialisation as the "subordination of real accumulation to fictitious capital" (2011: 176), leading real investments to be reduced in favour of financial speculation. Here, financialisation in South Africa is presented as the result of liberalisation and deregulation of financial activities, enabling the domestic growth of financial speculation and private credit extension, and the growth of short-term speculative financial inflows and long-term outflows. On this view, financialisation has thus had a limited impact on the economic structure of South Africa—with the Mineral and

Energy sectors remaining at its core—but has enabled a post-apartheid class recomposition, with the promotion of a small black elite accommodated in the capital structure of the economy through the financial markets, with the help of state promotion through the "Black Economic Empowerment Program."

These general approaches to financialisation in South Africa rest on the generic association (discussed below) of growth of the financial sector and of financial transactions with poor GDP growth and investment outcomes. This new configuration of capitalist development seems to be driven by a distant inner logic of financial speculation, with tenuous links to the rest of the economy. Finance, on this view, is no more than a functional way for capital to overcome problems of over-accumulation:

"(…) as over-accumulation begins to set in, as structural bottlenecks emerge, and as profit rates fall in the productive sectors of an economy, capitalists begin to shift their investable funds out of reinvestment in plant, equipment and labour power and instead seek refuge in financial assets. (…) financial assets must be increasingly capable of generating their own self- expansion, and also be protected (at least temporarily) against devaluation in the form of both financial crashes and inflation." (Bond, 2006: 11)

Such straightforward recognition of financialisation in South Africa, lacking a more substantive meaning, misses the economic changes that the rise of the financial sphere has imposed across the economy, the varied nature of this process, and the specificities of the financial sector in South Africa, both in its recent international integration and in domestic developments. This generic content in approaches to South African financialisation leads to clearly contradictory analyses of the recent behaviour of the South African financial sector and the local implications of the international crisis. Assessments vary between clear-cut identification of the same processes of household over-indebtedness and default in South Africa as in the US during the financial crisis (Bond, 2010) to appraisals of the South African banking sector's resilience due to the supposed absence of over-lending combined with regulation that prevented the collapse of the domestic banking sector, as argued by Roger Southall:

"A fortuitous combination of the apartheid legacy of control and post-apartheid macroeconomic stringency had ensured that the financial sector had remained quite tightly regulated. Hence the excesses of deregulation and over-lending that brought many major financial institutions to their knees in the west were not repeated in South Africa. No banks collapsed." (Southall, 2010: 8)

These ambiguous understandings of financialisation in the context of South Africa are reinforced by the downplaying of some of the implications normally associated with financialisation that do not seem to hold in this particular setting, namely stagnant economic growth and investment, since the country has benefited from record economic growth and a mild surge of investment in the years that preceded the financial crisis.

The original contribution of this dissertation is thus to provide a thorough account of the nature of financialisation in a middle-income country, South Africa. Critically adopting a substantive theoretical approach to financialisation, the specificities of South Africa and its commonalities with developed countries will be presented. The sectoral meaning of financialisation—in non-financial corporations, banks and households — will be scrutinised, allowing an articulated understanding of the evolution of the South African economy in recent years. Moreover, research on this historically specific geographical setting will contribute theoretically to research on financialisation in general, helping to better identify its salient features.

1.3. Organisation of work

This dissertation starts with a review of the theoretical debates on financialisation and capitalist variation that will frame the research on South Africa that follows. In chapter 2, the epistemological, theoretical and empirical choices that guide this research are presented, along with a brief contextualisation of the case-study, South Africa, with a discussion of recent evolution of the country's economic policy, macroeconomic outcomes, and integration into the international financial sphere through rising capital flows.

Given the theoretical meaning of financialisation from which I depart, my initial research question on the existence and meaning of financialisation in South Africa is to be broken down into a set of questions regarding particular sectors. The sectoral approach of my research entails a division into three broad parts, each one concerning a different sector[4]. For the sake of analytical detail, these sectors are studied in narrower categories. I begin with the private non-financial corporate sector (Chapter 4), since non-financial private conglomerates were the backbone of South African capitalism until the end of apartheid (Fine and Rumstjee, 1996). Its restructuring, transnationalisation and interaction

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[4]This choice leaves behind detailed accounts on sectors such as public corporations (known as parastatals in South Africa), the state (in its different forms, local and central), other financial institutions (such as insurers or mutual funds) and the portion of the households that lives more or less outside the accounting systems of the formal economy. This choice is reached from the theoretical framework of this dissertation, which is focused on the three pointed sectors whose financial interactions make them particularly relevant in shaping the economy.

with other domestic sectors is at the heart of the organisation of contemporary productive capitalism in South Africa. Chapter 5 is dedicated to theoretical approaches to the banking sector and to institutional evolution in South Africa, since the banks are the institutions around which the entire financial sector is organised, being the one that most benefited from the rise of finance in the past decades. An empirical assessment of the financialisation of the South African banking sector follows in Chapter 6. Chapter 7 presents a theoretical discussion on household finance and its financial evolution in South Africa, and Chapter 8 discusses the relation between inequality and debt in the country. Given the approach taken here—based on Marxist political economy—the analytical focus on these sectors does not imply neglect of the rest of economy. On the contrary, my research, despite its focus, is necessarily articulated with a general reading of other sectors in order to establish an understanding of the whole economy.

This dissertation ends with a summary of my overall findings, providing a general assessment of whether and how South Africa is a financialised country, and some tentative theoretical contributions to a more robust theoretical approach to research on financialisation.

2. Financialisation: theoretical debates

2.1. Introduction

The last decades have been marked by the dynamism of financial markets and their hegemony around the world. This is probably the deepest and most sweeping transformation developed capitalist nations have witnessed in recent eras. Finance, benefiting from its intangibility and technological progress, of late, has affirmed itself as the major icon of what has been designated as globalisation.

The exponential growth of finance has been captured by political economists in the concept of financialisation.The theoretical study of financialisation has a brief yet rich history. The concept emerged during the nineties and expanded during the last decade across other social sciences. The meaning and even the use of the expression financialisation varies widely within different traditions of economic thought. The literature review undertaken in this chapter is born from the need to give a more substantive meaning to the label, enabling more precise study of particular cases outside the core of the most developed countries with regard to financialisation.

This review will start with an overview of the competing understandings of financialisation held within the major currents of political economy. The organisation of this review rests on awareness of the two different traditions in political economy which deal with financialisation: Anglo-Saxon and French. The cross-references between these two bodies of thought are scarce[5], even though the cross-fertilisation has been increasing within each cultural bloc However, different key aspects of finance are highlighted in each tradition and merit consideration. Contemporary post-Keynesianism, influenced by economists such as Kalecki and Robinson, beyond Keynes himself, is centred on the dynamics of financial markets, their inner mechanisms, and the implications for the aggregate economy. French Regulationist theory, born out of efforts to understand the global crisis of the 1970s, was originally influenced by Marxist structuralism, however

[5]The fact of different languages and distinct ways, at least until a few years ago, of organizing thought on scientific progress– French economists favouring the publishing of (French) books instead of (English) peer-reviewed journals – may explain partly this lack of communication.

further developments are mainly focused on the central institutions that have driven capitalist accumulation. Finally, Marxist political economy is here also divided between the French and Anglo-Saxon traditions, as distinct paths have been charted for the body of thought on each side, corresponding to cross-fertilisation with other theoretical currents. The first section is dedicated to writings on financialisation from within the Post-Keynesian and Marxist political economy approaches. The second section will be entirely dedicated to French political economy, focusing particularly on its distinct take on the emergence of finance during the last decades, in juxtaposition with certain selections from the literature in English and the signalled shortcomings therein.

This segment ends with a presentation of recent work developed by Lapavitsas (2009) on financialisation which offers a theoretical bridge between the attention to "real" accumulation dynamics characteristic of the Marxist political economy framework, and the more interrelated, institutionalist approach of regulation theory. It argues for a continuing interaction between different sectors and/or institutions in an economy in the emerging of financialisation, and thus a certain flux in the meaning of the latter depending on geographical and temporal settings.

In the second part of this review, the varying nature of capitalism and financial systems is to be critically reviewed (with recourse to the literature on capitalism and economic geography), for extension thereafter to study of financialisation outside the more developed countries. We end with a brief look at literature which tries to capture the specific meaning of financialisation in developing countries, and why further research is needed.

2.2. Theoretical debates on financialisation

2.2.1. Post-Keynesianism

Post-Keynesian theory, owing most to the thought of Hyman Minsky, has been mainly focused on how the growth of financial markets has paved the way for a period of fragility and volatility. Building on the radical, non-probabilistic Keynesian notion of uncertainty, Minsky (1982, 1986) argues that financial transactions are inherently uncertain and follow an endogenous, increasing volatile, path. Periods of financial stability will eventually give way to uncertainty and fragility. The relative weight of the three different income-debt relations in an economy – identified as hedge, speculative and Ponzi – will ultimately be dominated by the latter. The borrower speculates on asset price valuation to pay back his debt, as the cash flows provided by the asset tap neither the payment of interest nor the principal. At some point, such supremacy would lead to a negative revision of expectations, amounting to greater difficulty in refinancing loans and a fall in expected flows (Wray and Papadimitrou, 1997).

Post-Keynesians (Wray, 2007, 2008; Kregel, 2007) employ this theoretical framework to explain recent financialisation (an expression only very recently taken up by these authors and to be narrowly understood as financial sphere growth). Asset price inflation in upturn periods would raise collateral values, allowing corporations to indebt themselves to unsustainable levels. The contemporary financially complex economy, born from financial innovations and liberalisation, would stretch liquidity and increase leverage in such a way that solvency is endangered (Wray, 2007). Finance would thus increase macroeconomic volatility. The growth of the financial sphere is here taken as an endogenous dynamic of "unleashed" capitalist economies. Only strict public regulation, particularly the segmentation between investment and commercial banking which would introduce "de facto maturity matching" (Kregel, 2007), would prevent future crises.

Adopting Gerald Epstein's definition of financialisation (see Introduction), Thomas Palley (2007) takes a broader approach, focusing on the increasing debt volume as the defining feature of financialisation. Palley does not address the causes of this new process. He is mainly interested in assessing its impacts, particularly its power/tendency to "1) elevate the significance of the financial sector relative to the real sector; 2) transfer income from the real sector to the financial sector, [and] 3)…contribute to increased income inequality and wage stagnation" (2007: 1). Three different conduits for the increasing significance of the financial sector in relation to the rest of the economy are identified: firstly, new and growing financial markets; secondly, neoliberal economic policies characterised by abandonment of full employment objectives, trade and capital international liberalisation, privatisation of public assets and labour market reform; and thirdly, new corporate behaviour with the alignment of corporate managers with financial markets (facilitated by eroded union power),most importantly in corporations' use of debt, share buybacks, and transformations of profit streams into interest payments.

For Palley, this new configuration would have resulted in a downward pressure on wages, now detached from productivity growth, and in the rising inequality in the US. New business cycles are based on financial asset booms as they provide the collateral for debt-financed spending, partially counter-balancing the impacts of wage stagnation on aggregate demand. Nonetheless, on top of their regressive income distribution effects, these new business cycles generate mediocre economic growth and increasing instability. Again, the political solution rests in new controls on the financial markets and Keynesian full employment policies.

James Crotty (2000, 2003) stresses not only the endogenous financial dynamics of the past decades but also the profound implications of financialisation for corporations. The second and third financialisation conduits proposed by Palley are here central in the historical comparison between the golden age of the post-war period and the neoliberalism that is the focus of Crotty's work. The golden age of high growth rates and social progress is characterized by partially cooperative behaviour among oligopolistic corporations, worker-friendly labour relations and aggregate demand public management. With the spread of neoliberalism during the past decades, cutthroat global competition would have started to be promoted in key product markets. Coupled with the compression of wages and the dismantling of the welfare state, the result, in this picture, is global sluggish growth and the macroeconomic volatility constrained by the mediocre demand and by the reinforcement of financial rentier interests (such as high interest rates). The opposition between the neoliberal order and the post-war golden age is here reinforced by the general positive assessment of post-war German and Japanese banking systems, as opposed to capital market finance prevalent among national financial systems worldwide nowadays. These (regulated) bank-based models, characterised by few universal and state-supported banks, would engage in long-term industrial investment, allowing the development of industrial policy and economic growth (Pollin, 1995).

Crotty (2005) highlights how "impatient" finance, led by speculation and volatility, forces non-financial corporations to behave differently, shortening planning horizons, paying increased shares of their cash flow to rentier interests and promoting new managerial incentives aligned with shareholders' interests. Still, a major paradox arises in that "destructive competition in product markets in the past quarter century severely constrained the ability of non-financial corporations to earn high profits and cash flow, yet financial markets and managerial incentives demanded ever-rising earnings to support ever-rising stock prices" (2005: 3). At the same time that financial demands on non-financial corporations are reinforced, their productive capacity from which they extract profits would be eroded in an apparent contradiction.

Thought on the effects of financialisation on corporations is further developed by Organzhi (2008). It is acknowledged that non-financial corporations in the US have been increasingly involved with financial markets, from which they gain a rising share of their profits. However, attention tends to be focused on the effects of financialisation on the real investment. Two possible conduits for slower capital accumulation are presented and tested in Orghanzi's study: 1) the possible crowding-out of real investment by new financial profit opportunities; and 2) transfers to financial markets which exhaust internal funds to investment, shortening planning horizons and increasing uncertainty. The author models an investment function in order to account for these potential effects and, using US firm level data, tests a sample regression for its probable cause. Both explanatory hypotheses are proved to have statistical significance, especially for large firms.

Similar work is done by post-Keynesian economists who have tried to formalise the macroeconomic effects of financialisation on capital accumulation (Stockhammer, 2004), on growth using adapted Kaleckian models (Hein, 2008, 2009) and on consumption using Steindlian models (Dutt, 2006). Again, financialisation is here understood as the emergence of the financial sphere (rising financial intermediation, international integration and shareholder corporate governance culture) due to decades of financial liberalisation and technological innovation. Attention is drawn primarily to the effects of financialisation, more than to its origins. The impacts on macroeconomic variables are conceptualized through the rise of a rentier class, whose income comes from dividends and interest, and the consequent rise of income inequality. Three conduits to regressive impacts on accumulation, investment and growth are identified as being 1) different propensities to save and consume of rentiers and workers; 2) shareholder pressure to "downsize and distribute" instead of focus on investment*;* and 3) asset wealth bubbles inducing increased household indebtedness, with implications for propensities to save and consume out of current income in the short term, and regressive distributional effects (due to the rising burden of debt) in the long term.

These different authors have been at the lead of financialisation studies. However, there are some entangled shortcomings that we can identify in this school of thought. While there is wide concern regarding the social and distributional consequences of the changing economy, there has been little or no work on the economic dynamics that lead to the emergence of financial hegemony. The focus of post-Keynesianism is placed on the public policies of liberalisation, privatisation and deregulation generally identified with neoliberalism. Some questions remain unanswered, such as: Why did the political conditions for neoliberalism arise in the 1970s and 1980s? What is the relation between financialisation and the increasing global integration of international trade and production transnationalisation? The neglect of such issues leads these authors to a somewhat romanticized historical interpretation of the post-war period. A golden age of economic and social progress during the post-war period would be completely separated from the economic and political factors of the last thirty years. Such distinction places these authors in a somewhat anachronistic position, defending a return to a particular period of capitalism, with its historical idiosyncrasies, through robust state-led regulation. Moreover, if there is a strong concern for the social implications of financialisation, namely on wage stagnation and inequality, the class analysis here presented is almost exclusively concerned with the rising dominance of the "Keynesian" rentiers generally identified with the top income percentiles. Analysis of the political and social dynamics that gave rise to financialisation is buried in research on its negative impacts on growth and inequality, such that a comprehensive account on how corporations and workers now relate and interact with this financialised economy remains lacking.

2.2.2. Regulation theory

Regulation theory provides a good starting point from which to analyse the heterodox French approaches to the financialisation of the economy, since it is within this theory that we find some of the most influential accounts of finance-led growth regimes. In fact, it is within the regulation school that we find the few references found in the Anglo-Saxon literature (namely Boyer and Aglietta in their English written pieces).

Regulation theory emerged during the seventies with the contributions of economists Robert Boyer (1986) and Michel Aglietta (1976). Influenced by the student radicalisation of the sixties, these young economists tried to depart from the neoclassical approach in favour of a new theoretical framework, in the intellectual tradition of Marx and Keynes, which could endogenously account for the economic evolution of the "golden age" post-war period and the crisis it faced during the seventies. Of a common social origin with the radical American political economists of the same period, the regulationists distinguish themselves from the latter by absorbing the influence of structuralist Marxist thought in post-war France[6].

Indeed, the structuralist influences are apparent in regulation theory as it stresses the role of certain institutions over and above productive forces. A look at five distinct but interrelated socioeconomic institutions and the ways they are organised serves to illustrate the different forms capitalisms have taken, historically and nationally, these five being: 1) the manner in which competition is organised between corporations (price formation, level of concentration, etc.); 2) monetary institutions (foundations of money, functions and circulation); 3) the state and the shape its economic intervention takes; 4) international economy insertion (commercial and investment relations with other countries); and 5) the wage-labour nexus (labour markets and organisation, wage determination, etc.) (Boyer, 2000). It is this last institution that should be placed at the centre of the economic system as it ultimately coordinates the coherence of the other four.

The way these institutions come together and make a coherent whole is designated, within this body of thought, as the 'regulation modes.' More generally, regulationists present the *accumulation regime* concept, which can be defined, coming very close to Marxist insights on material reproduction, as the conditions under which productivity gains are obtained and distributed and demand is generated in a sustainable way (Coriat, 1994). Modes of regulation have thus to prove viable over time in order to be recognised as accumulation regimes. This concept helps to integrate the political and economic determinants within the regulationist framework. Regulation theory diverges from Althusserian Marxism in the way it stresses the plurality of regimes historically observed in each country and does not focus on the invariabilities of capitalism. Different accumulation regimes are recognized to coexist in various geographical locations within the same time span.

This theoretical framework has been particularly useful in explaining the decades of growth that followed the Second World War as a *fordist* accumulation regime. *Fordism*, a concept first coined by Gramsci (2000) in the 1930s, was considered a long-term agreement between workers (organised collectively in unions) and capital in order to share

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[6]Such influence is mainly that of Louis Althusser's structuralism and its underlining of the role of institutions within capitalism.

productivity gains that technical advances and division of labour provided. The oligopolistic mode of competition, the Bretton-Woods monetary system and the welfare state embody the three other regulation theory institutions in this accumulation regime.

After recognizing different "nuances" in fordist regimes in different countries --modified as flexible in Germany, late in Italy, social democratic in Sweden, etc.--, the regulationalists largely abandoned fordism as an accumulation regime *per se* (Boyer, 2000). Instead, the identification of more localised modes of regulation took hold: market-led in the US, meso-corporatist in Japan, state-led in Germany, and Social-Democratic in Sweden. With this turn, regulationist thought converges with the Varieties of Capitalism literature (Hall and Soskice, 2001). However, as stressed by Boyer, the concept of an accumulation regime is not to be entirely dropped. As an alternative:

"the concept of fordism should be located in a series of accumulation regimes by the origin of productivity gains, the principles of division of income and the degree of extraversion of the economy" (Boyer, 2000: 234).

This conception of a core fordist "wage-labour" nexus common to all developed nations is here essential for regulation, since it allows for an account of the 1970s global crisis with one common theoretical framework. Indeed, the crisis and collapse of what was more or less one accumulation regime, and its substitution by another, is at the centre of regulationist theory debates throughout the last decades.

Particularly pervasive and of interest to this review is the emergence of the notion of a finance-led accumulation regime[7], considered to have substituted fordism and expanded in different degrees in all developed countries. Three different sources of destabilization of the fordist regime are identified by Boyer and the regulationist thinkers more broadly (Boyer, 2000): 1) Slowdown in productivity (exhaustion of the technical change potential); 2)inflation and pressures on the profit rate, given the workers' militancy; 3) internationalization of the economy and financial instability (due to end of the Bretton

[7]Even though the wage-labour nexus remains at the centre of regulationist analysis, the rise of finance has forced the integration of a more robust study of money. Guttman (2002) argues that money, as a social and historical institution, has in regulation theory a broader endogenous character than in the post-Keynesian theory. Money is treated as an evolving phenomenon, whose volatile forms have affected the power of national states to take public initiatives to stabilise the credit system.

Woods agreements). These factors are thought to have produced more competition among industries, destabilizing the oligopolistic competition mode. Moreover, increased capital mobility and market-determined exchange rates have pressed for independent monetary policy (focused on the fight against inflation), strict fiscal policy and the privatisation of public firms.

The result is the straining of the wage-labour nexus discussed above. The increased competition and financial volatility are found to have had repercussions on decisions regarding investment and production, putting pressure on the collective arrangements and labour protection laws, now perceived as 'rigid.' Moreover, the reorganisation of labour was facilitated by new difficulties in financing social programs, and as rising unemployment crippled workers' capacity for collective resistance.

Despite the shared recognition of financial hegemony in the main economies, regulationists diverge when analysing the new accumulation regime which has emerged during the last decades. Focusing on the role of collective action and the development and selection of institutions contingent upon its success or failure, Boyer (2000) abandons the centrality of the wage-labour nexus in favour of a more systemic institutional approach. It is argued that the rupture of so-called golden age political alliances and the dynamism of market-led modes of regulation, whereby the US exerts a hegemonic influence over the rest of the world, have produced a race of all different modes of regulation to *flexibility*. This flexibility subdivides into four different aspects: 1) financial innovation and liberalization; 2) international free trade; 3) rising uncertainty in the markets; and 4) state submission to the markets. The emergence of a new financialised accumulation regime is disputed. If a new institutional configuration (market-led) is admitted, some doubts are cast on its viability. The growing influence of finance in firms and in households can be seen to have imposed shareholder value culture on their operations, constraining productive investment (since it must achieve lasting profitability at a higher level than the past) and leading to (credit) consumption volatility. By this picture, aggregate demand is at risk, given the uncertainty of wage income and the volatility that comes with speculative asset bubbles and eroded social policies.

On the other hand, Michel Aglietta (1998) argues for the existence of a new accumulation regime (*regime patrimonial*) wherein a new wage-labour nexus is developed on the basis of a new social compromise. Institutional financial investors (pension and mutual funds) would enjoy a new role in the corporation's governance, but this new power would be balanced by the role of households as new financial assets holders, thus granting this new configuration its social legitimacy. The regulationist discussion of the role of finance in contemporary capitalism is clearly far from closed. The focus in finding new accumulation regimes, the different theoretical influences that have pollinated regulation theory (Post-Keynesian, Institutionalist, Ecological economics), and the current global crisis make it difficult for regulationists to have a homogeneous stance on finance. However, their emphasis on different institutional modes of regulation gives these economists an advantage in contextualizing the emergence of finance in a broader environment of capitalist transformation, particularly against the previously-presented post-Keynesian analysis centred on policy changes. The wage-labour nexus allows for a more robust analysis of the class dynamics and political implications of this new period. There is here no simplistic divide between a golden age of Keynesian regulation, macroeconomic tuning and corporate governance and a new finance-led capitalism. Instead, a systemic approach is presented, analysing the shortcomings of the previous fordist accumulation regime and the dynamics of different institutions in the rise of neoliberalism, with its own contradictions.

The influence of French conventionalists' theories and their work on the inner mechanisms of finance upon regulationist discussions should here be stressed. Born in the eighties, this theory, building on a mainly microeconomic approach, posits the existence of conventions (social norms) in every market relation and the stress the role of these non-market foundations as modes of coordination between agents (Coriat, 1994). Such approaches were, in the beginning of the 1990s, presented as a microeconomic complement to "macroeconomic" regulation theory. Conventions theory would provide the microeconomic theory for the endogenous character of institutions (Boyer and Orlean, 1991).

Although these efforts were not pursued later on, conventions theory, building mainly upon the work of Keynes and the post-Keynesians on conventions and liquidity preference, managed to offer an innovative approach to the functioning of financial markets. Andre Orlean (1989) defines a convention as the way a social organisation endogenously produces a collective representation that orients the action of different agents and determines its expectations. In financial markets, such conventions would provide agents, even if only on a temporary basis, with a model for signal interpretation, overcoming the radical uncertainty they face. These heuristics would provide an historical account for the evolution of stock market booms and busts as the succession of conventions, each one with a dominant variable that structures financial agents‘ behaviour (Orlean, 1999). The "autoreferencial mimetic interactions" (Orléan, 1999: 144) emerging from each one of the conventions act as conduits to the formation of a shared opinion within markets. The self-fulfilment of shared beliefs would thus feed the periods of financial euphoria and depression. The mimetic dimension that Keynes (1973 [1936]) associates with conventional judgement gains here new value as it is essential to explanations of how its reproduction can lead to a crisis. Such analysis of the financial markets provides a sceptical approach to financialised accumulation regime sustainability. Speculative bubbles are to be a permanent characteristic of this period (Lordon, 2000). They respond to the needs of the contemporary capital accumulation, but bring unbalanced impacts since the real economy is unable to sustain the demands of financial markets.

The thinking of French conventionalists can thus be considered to constitute an (ignored) theoretical breakthrough as to how to understand the inner logic of financial markets. While it is true that Anglo-Saxon post-Keynesian economists, such as Davidson (1994), have contributed substantively to thinking on liquidity and radical uncertainty, conventions theory charts an original take on the notion of conventions. If the current periods of instability and stability are to be effectively grasped, one has to incorporate a theoretical framework that explains individual decisions in contexts of radical uncertainty, accounting for how distinct, competing agents build common references that guide their action within the financial markets in order to overcome uncertainty. Nonetheless, this analysis is circumscribed by the dynamics of financial agents, leaving out how other economic agents and sectors interact with this sphere.

2.2.3. Marxist political economy

As in regulation theory, Anglo-Saxon Marxist political economy has directed much of its theoretical effort toward explaining the transition from the post-war period to neoliberalism. However, the causes behind financialisation and its content in varying contexts have been subjected to quite different accounts.

Grouped around the magazine *Monthly Review*, the seminal work on financialisation of Paul Sweezy (1997) and John Bellamy Foster (2006, 2007, 2008) has exerted great influence on Marxist debates. To better understand the approach of this group, one needs to grasp its theoretical origins, namely Sweezy and Baran's seminal book *Monopoly Capital* (1966). Its argument runs that stagnation was the normal state of the monopoly capitalist economy born in the beginning of the twentieth century, as surplus absorption problems started to arise. This tendency towards stagnation was only stopped by the prosperity of the 1950s and 1960s, specifically the following historical factors: rebuilding of the European and Japanese economies, major public investments in infrastructure, and the Cold War arms race and growing US global hegemony. Exhausting such factors, capitalism reached its stagnated monopolist character, whereby a handful of giant corporations controlled industry and competition is not a matter of price, but cost control and sales marketing strategies. The general tendency would seem to dictate a rise in surplus. Yet, as profitable areas for investment become too scarce to absorb the formidable economic surplus gained, economies enter again into stagnation. A severe depression with profound debt deflation becomes inevitable, since, as in an incredibly prescient statement of these authors: “government rescue measures to prevent collapse of the financial system merely lay the groundwork for still more layers of debt and additional strains during the next economic advance” (Magdoff and Sweezy, 1977: 35). Sweezy (1997) later argues that his original analysis failed to take into full account the expansion of the financial sector and its implications, namely, how corporation structure is now subject to change according to the imperatives of financial markets.

Bellamy Foster (2007) argues that if we take capital accumulation not as the mere existence of capital goods, but to include financial assets as well, we’ll have a better understanding of the current period using the same analytical tools as Sweezy and Magdoff. Financialisation would be the natural result of the surplus absorption problems and resulting stagnation pointed to above, in other words:

> “(1) The stagnation of the underlying economy meant that capitalists were increasingly dependent on the growth of finance to preserve and enlarge their money capital. (2) The financial superstructure of the capitalist economy could not expand entirely independently of its base in the underlying productive economy—hence the bursting of speculative bubbles was a recurrent and growing problem. (3) Financialisation, no matter how far it extended, could never overcome stagnation within production” (Foster, 2007)[8].

Financialisation, enhanced by supply-side financial liberalisation, is seen as the systemic fix for capital to escape its accumulation problems. Still, this configuration of the economy would not have eliminated the stagnant tendencies of the 1960s and 1970s.

[8] Retrieved at: http://monthlyreview.org/2007/04/01/the-financialization-of-capitalism

Stagnation would only be counterbalanced by the new and unsustainable rise in corporate and household debt. Moreover, these new avenues of accumulation are only made possible by financial speculation, as nurtured by bubbles wherein capital finds new sources for expansion. The financial structures would become increasingly fragile, as described in Minsky's "financial instability hypothesis" (see above).

A similar argument for finance as the supposed escape valve for stagnated capital is presented by Robert Brenner[9] (1998, 2003). Brenner takes his base, however, in an analytical microeconomic template other than that of the *Monthly Review* editors. Overproduction and overcapacity are stressed as chronic problems of capitalism. Non-innovative firms already present in a certain market would not engage in the Schumpeterian destruction of productive capacity when faced with the competition of new, more cost-effective innovative firms. With immense fixed capital and intangible assets (networks of consumers, brands, etc.) in their hands, it would always be rational for established firms to lower their average profit rates as long as they are still sufficient for circulating capital (the capital needed to put fixed capital in motion). Innovative firms would in turn be incapable of achieving the expected market shares and profits. The aggregate profit rate would tend to be lower, and problems of overcapacity would eventually emerge.

Hence, Brenner develops a framework wherein there is no excess surplus, but a global tendency for profits to fall. These endogenous dynamics of contemporary capitalism would be counterbalanced by the expansion of capitalism to old (Japan and Europe) and new geographical areas where competition was not so fierce – a process exhausted with the expansion of capitalism worldwide and the catching up of major economies as Japan or Germany. The profit rate is then seen to fall in the US during the 1960s, followed by other countries in the 1970s. If the theoretical framework presented by Brenner is not the same as other Marxist approaches, he is in accord with previous authors in explaining the increasing financial sphere (where currency volatility plays a major role) as the answer to the capital accumulation of the 1960s and 1970s:

"In response to the impasse of the international manufacturing sector at the end of the 1970s, resulting from deepening of the crisis of profitability throughout the previous decade, governments

[9] Praised by *New Left Review* editors as Marx's contemporary heir, Brenner's interpretation of the post-war economy has been deeply scrutinized and criticised by Marxist Political Economists (e.g. Fine, Lapavitsas and Milonakis, 1999; Dumenil and Levy, 1999, 2001, 2002).

across the advanced capitalist economies sought to ease entry into financial activities and pave the way for higher returns. To do so they initiated not only a permanent war against inflation, but also far-reaching process of financial deregulation” (Brenner, 2003: 40)

However, for Brenner, the attraction of financial markets is due exclusively to the role of the state in the redistribution of income (lower taxes, welfare state rollback). He grants no autonomy to the financial sphere. As mentioned, Brenner’s analysis and that of the *Monthly Review* editors diverge on many points, but still, they agree that the growth of financial markets has its origins in lasting, unsolved capital-accumulation problems throughout the second half of the twentieth century. However, this analysis is grounded in disputed empirical elements – such as the tendency of profit rate to fall – and ignores the transformations of global capitalism in the last decades (e.g. internationalisation of trade and production, progress in information technologies) that arose as a new configuration distinct in many ways from the capitalism of the immediate post-war period. Moreover, this analysis maintains a very strict distinction between financial and industrial capital, failing to capture their intertwined relationship.

2.2.4. French Marxist political economy

The work of French Marxist Francois Chesnais can be identified as a theoretical link between regulationists and Marxist political economy[10]. He largely follows the work of the regulationists but departs at several points in theorising what he sees as a new financialised accumulation regime (Chesnais, 1997). Three tenets of Chesnais’ thought are nonetheless shared with regulation theory, namely: 1) the notion of an accumulation regime close to the Marxist view of a temporary fix meant to overcome capitalism’s endogenous contradictions; 2) the emergence of financial capital centralisation as the result of a broader context of capital internationalisation, whereby the role of the G-7 states and their liberalisation policies are decisive; and 3) doubts about the existence of a coherent and sustainable financial-led accumulation regime.

Chesnais focuses his research on the dynamics of capital accumulation and reproduction, giving less importance to the five regulation theory institutions meant to compose a mode of regulation. For Chesnais, the theoretical search for new modes of

[10]Chesnais acknowledges his theoretical debt to the regulationists, since he believes that it is thanks to their work that Marxist political economy has managed to survive during the last decades in France.

regulation is bound to fail since the latter are conceptualised against a theoretical and political background of “market superiority” and an “avalanche” of measures that granted capital full liberty to manoeuvre. For Chesnais, the emergence of finance would be impossible without the concomitant liberalisation of trade and foreign investment. By his construction, this new configuration of the international economy has been imposed by the US through international organisations such as the International Monetary Fund (IMF) or the World Bank upon most developing nations. In the case of EU countries, according to the conditions of the Maastricht treaty (1992), financial integration was mandatory and subject to terms imposed by the most powerful nations who benefited from the new configuration.

Financialisation is understood by Chesnais as a process that guarantees the appropriation, under the most regular and safe conditions possible, of financial revenues (interest and dividends) at a global scale, favouring the US economy. In fact, only this country is considered to have a truly financialised accumulation regime, since it is able, through the inflows of capital, to finance its double external deficit (the negative savings rate and current balance) in order to boost internal demand (and speculative bubbles). For Chesnais, the financialised accumulation regime is not the product of the radical autonomy of now free self-referential financial capital towards the real economy (as in Orléan), but the result of international transfers from the peripheries and domestic reinvestment of dividends, household savings and corporations buybacks. He thus recognises a close connection and interaction between the financial sphere and the rest of the economy, with the former able to extract rising income from the latter.

Chesnais (2006) lies within a strictly Marxist understanding of finance, here taken as the institutions which centralise idle money and transform it into interest-bearing capital, where the activist capitalist shares his profits with the passive (lender) capitalist. The interest rate would be the result of the power relations between them. It could not be bigger than the profits of the investment it finances. The transactions between financial institutions would serve mainly as fictitious capital – the capital dependent on future streams of income that do not have any direct relation with effective industrial capital. The fictitious character lies in the illusion that this capital can be sold as securities at any time (‘liquidity preference,’ in Keynesian terms). Finance capital thus presents itself as incorporating the “natural property” of producing long-term gains and, concomitantly, tries to distance itself from the real spheres of the economy. It has its own world representation, wherein the shareholder's only interest is his rent gains. Productive investment is apparently disconnected from his interests (Chesnais, 2004).

Chesnais is sceptical of this understanding of finance capital and critical of an autonomous fictitious sphere. Finance capital grows at the expense of the real economy through interest gains on loans made to the industry and, in a more complex form, through the redistribution of income operated at the state level[11]. In his view, the power restoration[12] of finance capital has, on the other hand, produced/meant two major consequences for long-term capital reproduction: 1) the formidable centralisation capacity that financial agents have. Never was so much capital controlled by so few hands; and 2) subjected to finance capital as the dominant fraction of capital, industrial capital would be conditioned by the demands of the former in its own forms and pace of accumulation (short-term high profitability). Francois Chesnais tries thus to conceptualize a new more fragile and volatile accumulation regime, dominated by finance, built upon both a massive income redistribution that penalizes workers and on increasing imperialistic power relations between states.

Dumenil and Levy (2004, 2006), while sharing Chesnais' Marxist theoretical framework, refuse any regulationist influence in their work. The focus of their assessment of the last one hundred years of capitalism is to be almost exclusively grounded on class struggle. They start their analysis with the "first"[13] period of hegemonic finance during the first decades of the twentieth century as finance becomes, for them, a central actor for the first time in the history of capitalism, imposing a reorganisation of capitalism, notably through the rise of the new managerial class – distinct from corporation owners – which revolutionises the technological and organisational bases of corporations.

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[11]With the rise of public debt since the seventies, around 20% of public budgets in OECD have been allocated to the payment of debt service. The taxes raised from wealth in the form of wages, agricultural incomes and, partially, industrial profits are transferred to rentier (financial) capitalists at a rate of between 2% and 5% of GDP (Chesnais, 1997).

[12] The author uses this term in reference to the hegemony of finance capital in the first decades of the twentieth century.

[13]What qualifies as the first hegemonic period of finance is disputed within Marxist political economy. Using the Braudelian concept of "longue durée," Giovanni Arrighi (1998) argues that financial hegemony is a characteristic of the cyclical path of capitalism, going back to the influence of Genoa as a financial centre in the sixteenth century.

Following further the thought of Dumenil and Levy: the increased financial instability brought on by this hegemony then forces the creation of central banks as a stabilization mechanism since they assure the gold convertibility. These institutions are here perceived as the seed for future public regulation. The Great Depression of the 1930s, the Second World War and the rise of mass socialist and communist movements forces a further containment of the financial sphere through new forms of public intervention in the economic sphere and a new international financial system (Bretton Woods). All these result in a more egalitarian distribution of income and an increasing purchasing power for workers. However, the authors refuse the regulationist idea of a compromise between different classes, favouring the notion that new middle classes arising in this era are inevitably assimilated by dominant classes. They argue against any euthanasia of the superior fractions of the capitalist class and their financial institutions, and for, instead, a mere bourgeois tactical retreat ending with the 1970s global crisis.

The second current hegemony, by this account, emerged from the stagnation of accumulation – with low growth rates – and high inflation of the 1970s that would have opened the way for a brutal ideological offensive, embodied in the notion of neoliberalism, that supported the interests of the upper fraction of the capitalist class. This offensive aimed to end the Bretton Woods agreements and promote liberalisation of financial markets. Neoliberalism is here considered "the ideological expression of the financial power reaffirmation" (2001: 578) with the state to play the pivotal role in advancing this reactionary agenda.

This new period is seen as marked by the prominence of new private (pension and mutual funds) and public (central banks, IMF) financial institutions, the rising profitability of corporations through real wage stagnation and public welfare retreat. A new horizon for international accumulation of capital through the new global financial markets is thus opened, creating "a world favourable to the capitalists" (2006: 169). The Keynesian alliance between workers and the "cadres" of the Post-war period is substituted by the submission of the latter to the new shareholder culture, based on financial incentives.

Dumenil and Levy thus follow Chesnais in his understanding of Marx, but highlight different aspects, such as the separation between property and management of corporations that the new finance hegemony entails. Chief Executive Officers (CEOs) now belong to the capitalist class with their wages exempt from the general logic determining pay rate for the overwhelming majority of the workforce. They would represent a different fraction of the capitalist class: part of the "financial aristocracy". Finally, the authors stress how the separation of property and management in corporations allows a growing socialisation and centralisation of capital (distributed in stock), enhancing the inner contradiction with its private character. Moreover, albeit the promotion of the expansion of productive forces and the creation of a world market entailed by the credit system and fictitious capital, the different pace the financial sphere profit demands compared with the real economy would exacerbate capitalist contradictions and crisis.

French Marxist political economists share the great concern in Marx's own finance-related writings, taking a broad perspective on the world economy and offering careful discussion of abstract and empirical tools, and focusing on the class dynamics behind the last decades of a financialisation. Nonetheless, there is little attention in their writings to the post-Keynesian and conventionalist contributions to how the financial markets work, which leads them to a superficial analysis of the succession of financial bubbles and bursts of the last decade. Moreover, the class analysis here presented gives little attention to how the working class feeds and suffers this cyclical financial euphoria. Centred on the impact of finance on corporations, workers seem to be financialised not so much directly but through their work conditions. Their role as both debtors and financial asset holders in relation to the financial system is neglected.

2.3. Path for a synthesis? The Lapavitsas hypothesis of financialisation

In this overview of the financialisation literature, it was not our aim to argue for the superior relevance of either theoretical bloc, but rather to point to their different contributions and what are understood as the shortcomings of each. Anglo-Saxon accounts of financialisation tend to stress either the role of public policy (post-Keynesianism) or the structural stagnation tendencies of capitalism (Marxist political economy) as the cause for the recent financial hegemony of the upper strata. These diverging foci lead to what James Crotty has noted as Keynesians having historically emphasized finance at the expense of production and Marxists production at the expense of finance (in Henwood, 2003). Francophone contributions try to give a more systemic account of financialisation, integrating different institutions (regulation theory) and the international power architecture (French Marxists). They nonetheless struggle to conceptualize this new phase of capitalist development using their previous theoretical instruments, falling either into approximate accounts of a new accumulation regime or dismissing the current period as the return of prevailing configurations of capitalism found in its history.

The current financial crisis has shed further light on the relations between the financial sphere and the rest of the economy, with household finance at the centre of more recent analysis. Workers are subjected to financialisation not only through their labour relations but also as consumers of and fund providers to the financial system. Any comprehensive analysis of capitalism's current period must integrate the role of household finance in its analysis.

A new focus on the financialisation of workers' income has been put forward by authors such as Marxist political economists Costas Lapavitsas (2009) and Paulo dos Santos (2009, 2010). The fragmented work on the financialisation of individuals becomes here integrated through the extensive study of class and power asymmetries in credit relations. A systemic analysis on how capitalism functions through the interactions between different sectors of the economy is here put forward. Presented against the background of decades of triumphant neoliberalism which deregulated financial markets and imposed a general retreat of the welfare state, this approach rests nevertheless in answering the problems pointed out by Marxist political economy on surplus absorption in contemporary capitalism.

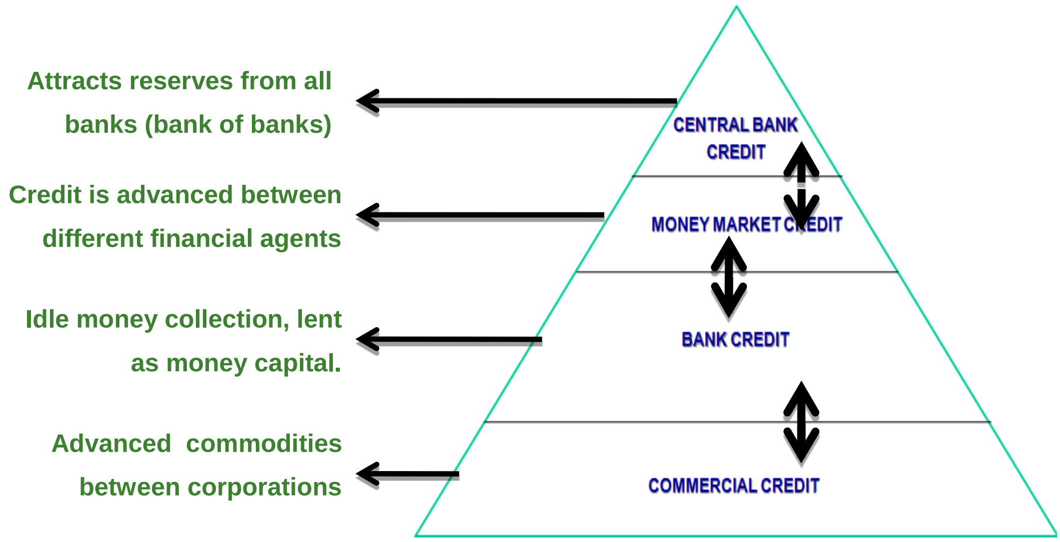
The conceptualisation of financialisation as emerging from the interaction between different sectors of the economy avoids past research pitfalls. It is my belief that this new approach can thus act as a robust theoretical link for further research between the currents of economic thought that have made valuable contributions on the logic of the financial sector (as was the case of Post-Keynesianism and French convention theory) and the centrality of class analysis (Marxist political economy), and finally the ability to consider variation within different institutional settings (regulation theory).

2.3.1. Credit relations

Despite renewed interest in finance within Marxist political economy, little attention has been given by this current of economic thought to money and credit relations in capitalist economies[14]. To understand the Lapavitsas approach to financialisation, it is first necessary to consider his emphasis (2003) on the social meaning of institutional constraints of credit relations, as they provide the analytical base for the study of finance as spontaneous interactions between different sectors.

Building on the work of the Uno Current of Japanese Marxism, Lapavitsas (2003) introduces the idea of the credit system as "an integral, pyramid-like whole, which comprises successive layers of credit relations and is embedded in historically specific conditions" (2003: 71). Households are not yet integrated in this pyramid. Attention is drawn to the role of credit between capitalists. Still, the use of a hierarchical pyramid to characterize the financial system diverges sharply from the mainstream credit relations, pointing to how informal relations of power and trust are endogenous to the financial system and how the financial sector is intertwined with the rest of the economy. Moreover, Lapavitsas argues that it is through consideration of the non-economic foundations of credit relations, namely the condition of trust of repayment between lender and debtor, that relations of power within the hierarchical capitalist credit system can be understood.

Figure 2.1. Credit Pyramid



[14] Suzanne De Brunhoff (1978, 2003) is one of few scholars to study Marx's theory of money. Some insightful institutional constraints and power dimensions in credit relations are presented, such as, for example, the extension of monetary settlements to taxes and rents contracts. Consequently, debt contributes to expansion of the capitalist mode of production. These institutional constraints hint at the existence of social aspects that shed new light on the diverse credit relations – overcoming the narrow understanding of credit as a relation between capitalists.

Lapavitsas (2003) distinguishes four different layers in the financial pyramid: commercial credit, bank credit, money market credit and central bank credit. Commercial credit refers only to transactions among capitalist enterprises, where commodities are advanced without immediate payment. A trade bill is then issued that may or not be monetary credit (depending on if it is sold or not), but that always represents trust and eventual power between the interested parties in their ability to issue, sell or even earn interest. Credit is here only studied as a relationship between capitalists. Even if both debtors and creditors gain from it – the former can buy inputs without using capital, expanding production and raising profitability; the latter can save on the costs of storing and avoid price fluctuations – the creditor must rely on the promise to pay and reduce its capital turnover thus lowering profitability (Lapavitsas, 2003). The creditor must believe in the debtor's potential for profit generation – which amounts to its capacity to relate to labour in a successful (exploitative) way – and access to money. In commercial credit, trust is not the result of any interpersonal altruistic relation but the belief of the lender in the debtor's profit-generation capability or access to liquidity that may derive from class or power positions and not from the efficiency and competitiveness of its industry in the marketplace. The social standing of the debtor is therefore decisive for credit to occur.

In the operations of banking, where credit is mainly the result of the issue of bank liabilities ("promises to pay"), banks need to ensure trust in their own promises based on their access to reserves and the quality and liquidity of their assets. A bank needs to bring:

"(…) together a variety of fields of trust and power across several industries sectors that act as a foundation for trust between in the bank's promises to pay. The particular and private trust between capitalists across a broad swath of industry is subsumed under the bank's own promise to pay" (2003: 80)

These promises have a shorter maturity than their assets (other capitalists' promises to pay). Trust and power have thus a more relevant role here than in commercial credit, since banks have an advantage in collecting and evaluating information about other capitalist sectors and a the same time must project an image of power from the "property relations and social standing of the bank's owners," thus creating the basis for a permanent power asymmetry between banks and the rest of the economy.

It follows that in bank credit, banks perform not only their founding role – to collect idle money from capitalists and transform it into loanable money capital – but also operate in the realms of account management, foreign exchange, assets management, etc., which fall outside lending activities. These money-dealing activities emphasise the information-gathering character of banks and the role that trust plays between borrowers and lenders. Relying on its better information and trust relations this layer will have a better position on their own promises to pay, given the shorter maturity and higher liquidity of their liabilities and their exclusive access to reserves. However, the power relation between banks and the industry is twofold, since, as we have seen above, capitalists use their social standing in order to access bank credit. Hegemony between industry and finance will thus rely on their dynamic relative social standings.

At the third level, we have money market relations, where credit is granted among financial institutions – in the form of short-term financial instruments such as overnight loans, finance bills, financial derivatives, etc.–, which enables them to access reserves. Money markets thus lend homogeneous loanable capital subsumed under the same evaluation criteria of payment probability. Nonetheless, the creditworthiness of each bank is assessed on the basis of the underlying relations in the circulation and production of commodities which support its assets and liabilities. For Lapavitsas (2003), in money markets there is no structural asymmetry between participants. Promises to pay are assessed by financial intermediaries, exclusive participants in these markets, taken as a homogeneous mass. In his words, “the money market cuts across economic and geographical areas and makes it possible for idle money funds to acquire a common and general character across society” (2003: 83). Credit ratings act as a unique set of information wherein all the dimensions are integrated, submitting all the sectors, countries or individuals. This capacity of socializing capital determines its higher standing when compared with the previous pyramid layers. The homogenisation of social relations within this layer allows thus for the money markets to prevail over context-specific realities.

Finally, at the top of the pyramid we find central bank credit: a public bank which only interacts directly with money markets. It thus gathers and analyses information on the whole economy. Its bank notes and reserves serve as the ultimate money in capitalist economies. Its promises to pay support every liability in the economy, given its public (state-controlled) nature and role in each country. The power granted from the state affords it a unique position, influencing the terms of how lending is processed in the economy, as is now clear with the intervention of central banks in injecting liquidity in the economy and acting as a lender of last resort. Without it, trust can be damaged to the point of drying liquidity in money markets and the consequent collapse of the credit system.

The pyramidal scheme Lapavitsas presents has its base in a particular understanding of Marx's concept of interest-bearing capital which departs from the distinction between a "monied" capitalist class who would lend and "functioning" capitalists who would borrow it (Lapavitsas, 2003). Interest-bearing capital is treated as the result of spare funds reallocation among "functioning" capitalists. The credit system "mobilizes the idle money generated in the turnover of capital, transforms it into a homogeneous commodity by giving to it the character of interest bearing and redirects it to toward accumulation" (2003: 91).

This notion offers several conceptual advantages. Two are of special interest to our work since they have particular class analysis implications. Lapavitsas's scheme takes interest payments as a redistribution of surplus value among capitalists and not as the material basis for a specific group of capitalists. In his view, the Keynesian notion of a rising rentier class[15] – wealthy people who get most of their incomes from owning financial assets, rather than working or from owning productive assets (factories, natural resources) (Epstein and Power, 2003) – that benefited from the mere accumulation of financial assets in the last decades should be dismissed, as it gives primacy to the relation between different interested kinds of capitalists from whose struggle arise certain economic dynamics to the detriment of the general class struggle and of the capital accumulation dynamic. The second advantage of this notion is how it accounts for the creation of interest-bearing capital from the idle money of workers and other social groups and for lending to non-productive activities as household consumption. Interest can be extracted from all kinds of revenues across society since it is taken as a "reward for parting with lender's property." It does not need the result of partition of the generated gains of an investment thus opening the path to the integration of worker's income.

[15]Epstein and Power's notion is mainly based on the Kaleckian idea of rentist income that encompasses profits of financial firms, capital gains from asset sales and interest by households. This notion should be distinguished from Engels' definition of rentiers as people who have become "tired of routine exertion in business and who simply want to amuse themselves or pursue only a light occupation as directors of companies" (Supplement to Marx's Capital, 1982).

2.3.2. The financialisation hypothesis

The theoretical contributions of Marxist political economy presented above allow Lapavitsas (2012) to define financialisation as the emergence of number of tendencies at the level of industrial enterprises, financial enterprises and workers in their credit relations[16]. For Lapavitsas, large corporations are financialised as they now have the ability to directly access open financial markets, bypassing any financial intermediation by banks. The modern monopolies (multinationals) have acquired the skills to independently engage in financial operations and trading. This stance is confirmed by the analysis of multinationals by Chesnais (1997), who points out how the financial arms of industrial multinational corporations such as Ford, GM or GE have been responsible for much of the profits gained. They are now autonomous financial agents who interact with money markets, speculating with currencies and derivatives.

Banks have adapted to this new reality, argue Lapavitsas and collaborator Dos Santos, through restructuring their operations, benefiting from the movement of financial liberalisation and deregulation and new information technologies (Lapavitsas and Dos Santos, 2008). According to Lapavitsas (2009), banks have turned toward mediating in open markets to earn fees, and income from trading. They also have turned toward workers to extract income from lending but also from “handling savings and financial assets” (2009). The banking sector in its financialised form would be then less dependent on conceding loans to corporations and more on their preferential position (in terms of skills and reputation) to engage with both financial markets and households. The rise of finance-to-finance and household lending would be thus one of the results.

Finally, and mostly importantly, financialisation is seen to encompass the revenue of workers, both from their financial liabilities and their assets. Workers, and households more generally, are financialised in face of public provision retreat and rising income inequality. The growing neoliberal privatisation of housing, health, education and pensions forces households to resort to the financial sector in order to access such goods, in the form of debt and the channelling of savings (pension, insurance, money market funds). This relation is thus of a different nature than the credit relations described above, since

[16]This approach is itself inscribed in the Marxist tradition as forwarded by Hilferding (1910) and Lenin (1916) in their analysis of finance capital (as the amalgam of banks and industrial capital) and imperialism in the beginning of the twentieth century.

household income does not proceed from profit in the sphere of production. Lapavitsas (2009) presents the concept of "financial expropriation" to illustrate the distinctive character of this relationship and its importance in contemporary capitalism analysis. Banks, and the financial sector more generally, are able to capture rising financial profits from households in the form of interest rates and fees and commission from their money-dealing activities. This concept encapsulates this new asymmetric relation, seen as allowing for "exploitative aspects deriving from systematic differences between financial institutions and workers in terms of information availability, economic and social power, and alternatives in undertaking transactions" (2009: 19)

Class, power and the non-economic foundations of credit systems are thus essential to understand the current trends in the financial markets and their different implications for households. As Dos Santos argues, there is still the "need for robust conceptualizations of credit relations in the process of accumulation, including the distinctive social content of credit to wage earning household" (2009: 28). An analysis on how different economic sectors relate to the financial system should then be adopted. In Marxist political economy terms, one should focus on the circulation of capital. That need not imply the primacy of circulation overproduction, but consideration of the former is a necessary step to understanding the whole economic circuit.

2.4. Variation in financialisation: from the core to the periphery

The theoretical approach presented above draws on the classical Marxist political economy stance of the international financial sphere as an imperialist mechanism that guarantees the regular flow of financial revenues favouring the most powerful economies. It shares with the Marxist tradition, further, the understanding of contemporary financialisation capital as arising from the spontaneous domestic interactions of different economic sectors, allowing financialisation to vary in different spatial settings. Due to the distinct institutional and political histories of different countries, financialisation has varied site to site in its form (Lapavitsas and Powell, 2013).

A flexible theory of financialisation, allowing for variation across different geographical settings is of paramount importance to the research presented in this thesis, as South Africa, a middle-income country which lies outside the group of developed countries where financial hegemony is more salient, has its specificities born both from its international insertion and its domestic dynamics. The theoretical work presented in the group of texts known as the varieties of capitalism (VoC) literature[17] (Hall and Soskice, 2001), including the critique added by economic geographers and the more recent research on the specificities of financialisation in developing countries, is thus key.

2.4.1. Varieties of capitalism

The VoC literature researches the variations of four institutional domains in different national and regional settings: financial and non-financial mechanisms of governance, industrial relations, education and training systems and the competition/cooperation relations between firms. The coordination arrangements within and between firms are at the centre of its analysis. Based on this one-dimensional framework two ideal types of capitalism emerge - liberal market economies and coordinated market economies grounded in the distinction of financial systems into market-based and bank-based (Gerschenkron, 1962, Pollin, 1995). In the first, the financial system would be based on market issuance of securities, multiple and decentralized financial institutions and liberalised, unregulated environments. The coordinated, bank-based economies would be characterised by a small number of universal banks, supported or even partially owned by the state, engaging in long-term industrial investment through conglomerates.

The broader literature of comparative capitalisms provides other nuanced ideal types. Amable (2003) identifies five types of capitalism (market-based, continental European, social-democratic, Asian, southern European) and provides a more comprehensive analysis in order to identify four different types of national financial system – one market-based and three others bank-based. Focusing on Europe, Amable recognizes that a slow convergence to the more liberal-market-based model is taking place: "There are no signs of a complete conversion of Continental financial systems to a market-based system, but there are signs that the systems are changing. Rather than a transformation of European systems into a financial-markets-based system, there is the possibility of a move towards a hybrid system (Deeg 2001), in particular in Germany" (Amable, 2003: 254).

Even though firms' coordination and capabilities are at the centre of its analysis, for the VoC literature economic change is to be explained by external shocks, which result in

[17] More broadly known as Comparative Capitalisms literature.

the adaptation of a different set of public policies. In fact, the role of public policies following from the international Bretton Woods arrangements, the gradual liberalisation of financial markets and the privatisation of firms and essential services play a crucial role in the emergence of financialisation and convergence among different economies. This constitutes a recurrent theme in the literature, as already pointed out.

It is here expected that the national configurations of capitalism are influenced by the institutional, political and social dynamics in each state, assuming some sort of path dependency which resists convergence and maintains the autonomy of national embedded capitalisms. However, the VoC literature, even when assuming hybridisation and new varieties of capitalism, remains grounded in the dual ideal type distinction between LME and CME. Neoliberalism and financialisation are thus identified with the liberal-market economies rather than understood as a global process with its asymmetries and specificities in each setting.

2.4.2. Economic geography and international political economy

Economic geographers Peck and Theodore (2007), Brenner et al (2010), and Dixon (2010) scrutinized the VoC approach and provided important insights into its findings. They praise the VoC's achievements with regard to "the socially and spatially differentiated character of actually existing capitalist formations, and the roles of social choice and institutional agency in guiding and sustaining these systems" (Peck and Theodore (2007: 749). Nonetheless, they criticize its methodological standing as using "nationalist and uniformly territorialist taxonomies," which in their view dismiss evidence of interdependence and continuing convergence in the international arena, and for adopting an equilibrium approach where only "external shocks can disturb the equilibrium conditions that prevail within each national regulatory system" (Brenner et al, 2010: 189). The VoC is thought incapable of incorporating the international restructuring of capitalist production relations, and the contingent aspects produced in national and regional economic blocs. Economic geographers propose instead a "variegated" capitalist approach, born from the synthesis between neo-Marxist concepts of uneven and combined development, Polanyian concepts such as social embeddedness and regulationist geographies of accumulation. The proposed analysis revolves around the "provisional position" of "variegated capitalism" that tries to explain the uneven development of capitalism, where individual cases are chosen according to their "theoretical generative properties" (Peck and Theodore, 2007). The neoliberalisation process and rise of the financial sector is taken as a succession of market disciplinary reforms with asymmetric impacts in different institutional settings (Brenner et al, 2009).

The contribution of International political economy is acknowledged by economic geographers for the identification of supranational capital and institutions in enforcing the modalities of participation of national economies in the international arena. This approach is criticized, however, for having a strict top-down rationale, where national institutional landscapes are not theorized and where a necessarily conflictive interaction with the international economic order is neglected (Brenner et al, 2010).

Despite these criticisms, the importance of the critical literature of International Political economy (Konings (2007), Gowan (1999), Helleiner (1994)) should not be underestimated, particularly when dealing with finance. They provide a theoretical background for the international hierarchy of states and its articulation with the new configuration of global finance. Focusing on the notion of structural power as “power that is exercised indirectly and operates through shaping preferences and influencing the conditions under which other actors make decisions” (Konings, 2007: 37), these authors reject the notion of an homogeneous erosion of state power and, instead, understand the changes in the world economy as the reconfiguration of international power through new rules which have different national and regional impacts. Nonetheless, the causes of the emergence of neoliberalism and financialisation vary in this literature -- from the demise of the Bretton Woods institutional arrangements (Gowan, 1998) to the previous expansion of private global finance that undermines the previous international monetary architecture (Konings, 2007). They converge on how the US economy has acquired a new power position in the international arena through its ability to impose the dollar as world money in a new international monetary system. New avenues of funding were thus opened through the pinnacle role of the dollar in a new non-convertible monetary system. If the US lost its ability to manage domestic dynamics of monetary creation, the power of this country was expanded in what Panitch and Gindin (2005) call the ‘*Americanization* of finance,’ concomitant for them with the globalization of finance, whereby:

“the inflows of capital and imports of commodities to the US have allowed global savings to be channelled and global exports to be expanded, while mobile financial markets have disciplined and promoted the neoliberal restructuring of other economies, reinforcing the barriers to any attempt to delink them from the global system"[18]

The impact of this new structural power is recognised by these theorists as having had immediate impacts on all the other nations, opening space for a more comprehensive analysis of the role and forms of international integration. However, most of these authors, stressing the international power dimension, fail to recognize the specific content of financialisation in each country.

2.4.3. Varied financialisation in developing countries?

The different theoretical approaches presented above, despite their interest in capitalist variation and asymmetric international integration, have dedicated only scarce work to developing countries and their role in the financialisation process. Developing countries are looked to in this context for their peripheral role in global financial markets as they liberalised capital accounts and became reliant on international finance. While it is clear that developing economies are influenced by the international financial processes (through the impact of international capital flows) there has been little effort toward understanding whether these are financialised economies in the sense of having gone through a domestic transformation of their capital accumulation processes, as Lapavitsas has identified it. The structural and historical differences and common trends in the interactions between corporations, households and the financial system in developing countries remain largely unanswered.

Developing countries' integration in world financial markets is far from a recent phenomenon. The various historical debt cycles – where an initial expansion of foreign credits is followed by payment stress and/or default and ends with debt settlement agreements between debtor countries and their creditors – were long ago identified in the cases of these countries. It was the debt crisis of the 1980s that has put these countries under the spotlight when, after benefiting from huge capital inflows provided by both the abundance of petrodollars in the 1970s and the sharp reversal of interest rates in the US, they suffered multiple debt defaults as a result. These were usually followed by structural adjustment programs imposed by international institutions such as the IMF and World Bank which, with their liberalising agendas, brought developing countries into the ranks of those

[18] Retrieved from: *http://actuelmarx.u-paris10.fr/m4panitch.htm.*

fully integrated in international capital markets. If not by direct political means, the internationalisation of production and the capital endemic need of these countries forced developing nations to participate in the global financial arena. These countries have thus been forced to participate in the global finance arena, adopt floating exchange rates, liberalise capital flows and enhance costly measures to avoid the increasing volatility and instability of the system.

They have benefited from growing inflows of capital, but such processes often take the form of short-term flows that benefit small parts of their economy and entail collective costs and income losses for the whole economy as, for example, they are forced to accumulate foreign reserves to stabilize domestic currencies and ease domestic capital flight. The growing transnationalisation of the economy and broader participation in the international financial markets have produced a new power relation between core and periphery. Painceira (2009, 2011) identifies the increasing capital flows from and to these countries as proof of middle-income economies' financialisation. Growing capital flows, coupled with the financial instability of the late nineties – both currency and banking crises affecting regions such as Asia and countries such as Argentina, Russia, Turkey, and Mexico – have forced these countries into a particular insertion in the global financial markets throughout the last 10 years.

The rising importance of emerging markets in the international arena has forced the accumulation, in these countries, of current account surpluses and vast amounts of foreign reserves (where the dollar, as quasi-world money, naturally dominates) in order to prevent any disruptive effects of capital flows volatility, as in the case of the 1990s in a number of countries (Mexico in 1994, Asian countries in 1997-98). Developing countries then have to pay a levy on their participation in international capital markets in the form of low return reserve accumulation in spite of capital inflows, normally related to higher-yield short-term borrowing. This process leads to the growth of public debt as a mechanism to sterilize capital inflows. Domestic and public borrowing is increased in order to comply with the inflation target policies adopted by these countries.

If the hegemonic power traditionally acted as the borrower of funds, exporting capital to new profitable accumulation outlets and creating a relationship of dependency between the core and the periphery, a reversal of such flows is now found. A number of developing nations (such as China, South Africa, Brazil, South Korea, etc.) act as lenders to the hegemonic power, the US. As pointed out by Panitch and Gindin (2005), such reversal should not be understood as the declining role of the US in the world economy[19]. Capital inflows are rather a result of its financial strength. The strong liquidity and relative safety of American assets, with treasury bills acting as world monetary reserves (in the absence of gold), strengthen the role of the dollar as world money.

This structural power coming from the center of the world economy should not however be taken as an immediate and simple mechanism. The insertion of middle-income countries into the international economy and financial sphere varies, and is itself dependent on the domestic interests, state apparatus and historical path of each national setting. The specificity of middle-income countries in the present international financial architecture has been shown, among others, by Becker et al (2011). The authors distinguish two types of financialisation according to different stages of national development. Financialisation as the expansion (and price increase) of fictitious capital – which, being claims on the surplus of productive activities, are here understood generally as financial securities – is hereby prevalent in developed countries. This financialisation configuration is here illustrated by the emergence of strong capital and money markets. The financialisation of developed economies is viewed through a general Marxist political approach as a temporary fix for problems of over-accumulation of "productive" capital (implicitly assuming its declining profitability) and not a transformation of the accumulation process, entailing profound transformations of the accumulation of capital in the whole economy. More interestingly, for Becker et al (2011), middle-income countries exhibit their own variety of financialisation, characterized by the expansion of interest-bearing capital and large interest rates spreads. In the absence of mature securities and equity markets, the banks of these countries are thus the pivotal institution around which the financial sector flourishes. Financialisation is here introduced by the growing dependence of international capital flows in the interest of extraverted domestic elites. Such dependence, on the other hand, would force overvalued exchange rates and high interest rates in order to attract hard currency funding, seen as essential for participation in the world economy. The results are the eroding of productive capacity, a deteriorating current account balance and increasing vulnerability and financial volatility, taking the form of currency crisis.

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[19]While it is true that the current American account deficit has increased from 1.2% of GDP in 1987 to 5% in 2003, this statistic should not shadow the expanding of US exports and foreign direct investment (growing faster than other developed nations) in the international economy.

2.5. Concluding remarks

The brief literature on financialisation of developing middle-income countries shows that general assertions should be taken with caution since experiences vary widely among different countries. Rising capital flows remain one of the common features of this process, but they should not lead us to take financialisation of developing nations as a homogeneous course. The research on financial systems, and particularly financialisation, must recognize the international hierarchical underpinnings of this process whereby the same constraints imposed by international imperialisms are matched by national economic restructurings with deep class implications and interactive transformations among firms, financial institutions and households. The correspondences between the international arena and its global processes of capital accumulation and the individual cases of national/regional trajectories and integration, as presented by economic geography, should thus be part of the research agenda for financialisation of developing countries. Necessary are analyses of both global processes and individual cases from which one draws theoretical inferences about the reality of financialisation.

To study how financialisation impacted these countries already vulnerable to volatile international capital flows and accumulation of foreign denominated reserves is thus key to understanding its more substantive meaning as a systemic transformation of whole economies across their different sectors, and as a hierarchical new international economic order. Country-specific paths need to be more carefully scrutinized, particularly open economies, modern financial sectors, and defy a one-size-fits-all approaches; only through such studies might we generate theory that enables better identification of the properties and specificities of the financialisation in contexts of subordination.The study of financialisation in these emerging economies with modernized financial systems can thus provide additional insight: firstly, it can identify the extent to which financialisation is an increasing international process, not limited to the centre, thus providing further indications of a systemic transformation of capitalism and of its flexibility and plasticity in different contexts; secondly, with certain obvious variations, given their semi-peripheral place in the international economy, marginal cases can lend data to solidify an understanding of financialisation as a sweeping contemporary transformation of the capitalist economy in all its varied forms.

3. Researching financialisation in the South African economy

3.1. How to research financialisation?

Before embarking on the research on financialisation in South Africa, the epistemological and methodological choices that guide this dissertation need to be laid out. The absence of neoclassical (mainstream) theory from the theoretical debates on financialisation in the previous chapter was not a lapse in the review but the consequence of the failure of the dominant theoretical approach to economics to identify the emergence of finance as a defining feature of contemporary capitalism. Given its overwhelming weight in economics, this chapter starts with the reasons behind the methodological refusal of this approach, pointing to its general shortcomings when studying the financial sphere. Alternatively, Marxist political economy, which will frame this research, is presented as a more robust methodological approach. The empirical sources and the descriptive statistics to be developed are presented next.

The second part of this chapter is dedicated to contextualize and characterize the case-study in its recent historical economic evolution. Two themes, recurrent in the financialisation literature, structure the overview of the South African economy during the post-apartheid period. The first is the need to scrutinize the role of public policy and the macroeconomic outcomes in the past two decades. As was already seen, financialisation theoretical accounts stress, albeit having different strength, the importance of neoliberal liberalisation, deregulation and privatization policies in creating the conditions for financial hegemony. The political choices undertaken after apartheid are therefore of paramount importance to offer the political environment within which the financial sector has acquired its reinforced presence. The second theme is the characterisation of capital flows to and from the South African economy in the past years. Liberalisation of capital account and the growing importance of these flows have been pointed as central in the financialisation literature on middle-income countries. Given the focus here undertaken on the domestic sector evolution in South Africa, it is crucial to identify the scale and absorption of capital flows in this country as it affects the dynamics of the domestic economy.

3.1.1. Research design

This chapter presents the methodological choices that have informed the theoretical and empirical research carried out throughout the present thesis. The ultimate goal is to contribute to a comprehensive and in-depth understanding of financialisation, which accounts for the mechanisms behind the emergence of financialisation and addresses the processes of medium-income countries, such is the case of South Africa.

Financialisation is now a recurrent concept within various strands of political economy, notwithstanding it being recently adopted and the coexistence of various, and not always consistent, understandings of its meaning. In its all-encompassing definition it is taken to describe "the increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of the domestic and international economies" (Epstein, 2006: 3). Although this, and other, definitions point to the capitalist nature of the rising importance of the financial sector, in their breadth they leave the mechanisms behind the emergence of financialisation largely unspecified, explaining partly the coexistence of alternative interpretations of the roots and meanings of this new capitalist phase. As underlined in the previous chapter, financialisation needs to be conceptualised through a more substantive analysis of the transformations at the heart of this process.

Financialisation, understood as a particular configuration of the capitalist economy, has been mostly addressed by heterodox currents of economic thought. As presented in some detail in the previous chapter, this has been the case of Post-Keynesianism, the Regulation School, and Marxist Political Economy (French and Anglo-Saxon). Other social sciences have also provided important contributions to this agenda. The work of the economic sociologist Greta Krippner (2005) on the financialisation of the US economy, the work of the economic geographers Jamie Peck and Nik Theodore (2007) and of Neil Brenner and colleagues (2010) are three cases in point. The latter, for example, underline the embeddedness of economic processes in particular in their social, political and geographical contexts, the multiple human motivations and the variegated nature of neoliberalism and financialisation across the globe.

The work of Costas Lapavitsas and Paulo dos Santos (Dos Santos and Lapavitsas, 2008; Dos Santos, 2009; Lapavitsas 2009, 2012), being inscribed in the latter current, is held, in the present thesis, to provide a synthesis between the post-Keynesian focus on the financial sphere, which is found lacking in the Marxist circulation sphere, and the Marxist long-held attention to the production sphere. Marxist political economy is mobilized to stress the prominence of analytically relevant categories such as capital and class, which signal the differentiated access and control of resources from which the exploitative character of capitalism emerges, which must be socially and historically located (Fine and Saad-Filho, 2008). Marxist value theory is, in turn, adopted to provide the analytical tools to the study of finance and money, which are intrinsically associated with processes of capital accumulation and market dynamics (Itoh and Lapavitsas, 1999). Lapavitsas-Dos Santos synthesis is thus taken to be particularly helpful to analyse the specific and historically located dynamics among the different sectors of the economy (corporations, financial sector and households), taking, for example, credit relations as resulting from specific historical processes where class and power emerge as explanatory categories. On this view, financialisation is the result of major non-financial corporations' increasing degree of direct access to money and capital markets in their search for funding, leading to the reinvention of banks' operations towards financial mediation between corporations and financial markets (i.e., a reinforcement of investment banking activities) and the expansion of credit to households. These renewed relations of power are, moreover, originally illuminated by relations of trust and reciprocity originated from other social spheres that embed economic processes in contemporary societies (Lapavitsas, 2003).

To summarize, the Lapavitsas-Dos Santos synthesis is taken to be particularly ingenious in bringing together Marxist political economy and historical, social and geographical specificities, facilitating the dialogue with other social sciences, such as history, sociology, and geography, as well as with other strands within the tradition of political economy. It therefore suggests an interdisciplinary approach that will be pursued, in both theoretical and empirical work, in the analysis of this thesis's research problems: 1) the confrontation of the Lapavitsas-Dos Santos synthesis with a particular historically and geographically located experience in a middle-income country; 2) the scrutiny of the historical and social content of the reorganization of different sectors of the South African economy during the rise of financial sphere.

Based on the theoretical framework just described, this thesis starts off with the following research question: Is South Africa a financialised country? Being a relatively recent subject matter, financialisation studies have been mainly devoted to the most developed countries, where the financial sector is more mature and powerful. This trend has been reinforced in the aftermath of the financial crisis of 2008 and the relative resilience of a number of large middle-income economies, including South Africa. However, if financialisation is to be part of a systemic approach to contemporary capitalism, research is needed on its origins, content, and impacts, in light of the current financial turmoil, in countries that lie outside of the international financial core. Moreover, as the historical, economic and social realities of the "emerging" countries vary widely, the specificities of geographical settings that lie outside the international financial centres need to be taken into account. By bringing the context of a seemingly recent financialised middle-income country, the thesis also offers new theoretical insights to the theoretical framework taken as its starting point.

3.1.1.1. South Africa as a Case-Study

Case-study research is particularly useful "when the researcher is trying to uncover a relationship between a phenomenon and the context in which it is occurring" (Gray, 2004: 127), being especially adequate for the identification of causal relationships through the confrontation of a provisional set of hypotheses to various sets of data (Yin, 1993). This is thus the work to be carried out in this thesis: the confrontation of the hypothesis of financialisation with multiple sources of data about the South African economy and society.

South Africa possesses a number of features that make it a particularly apt for the study of financialisation. First, it is a capitalist economy: the bulk of its gross domestic product originates from market-coordinated private provision and it has a modern private financial sector, relatively unobstructed by direct state intervention. This is a distinguishing feature of South Africa as compared to other emerging capitalist economies as, for example, China where the state plays a central role in regulation, financial repression and general direct intervention in the economy, making comparisons to core financialised countries more difficult. Secondly, its economic scale confers a degree of autonomy to the South African economy, which makes this a particularly adequate study to the identification of both what unites and what distinguishes financialisation processes across national contexts. Of particular interest for the present purposes, the relative autonomy of South Africa makes it particular fit for the examination of the domestic interaction of different economic sectors, which constitute the central units of analysis of the present work, albeit the constraints imposed on them by the evolving international economy. South Africa thus stands in sharp contrast to smaller developing economies, as it is the case of many sub-Saharan countries, with still-dominant pre-capitalist structures, where capitalist sectors are completely dependent on foreign markets. Finally, the exceptional availability of comparable sectorial financial data allows a broad coverage in terms of sector (non-financial enterprises, banks and households) and time span (data available since 1995), which is critical for the empirical exercise to be carried out of confrontation of various sources of data with a theoretical hypothesis taken a as a point of departure: the Lapavitas-Dos Santos synthesis. Given that different units of analysis are examined in the study of financialisation, the thesis rests on what is referred to as 'single case-embedded' study (Gray, 2004).

Since my research intends to be historically embedded, the problem of periodisation emerges. Financialisation has been argued as new period of capitalist development whose origins are normally associated with the neoliberal turn in the US and UK caused by the election of Reagan and Thatcher, respectively. However, recent analysis of financialisation tend to focus on the financial booms and busts of the end of the 1990s, when the liberalisation process had been pushed to new heights – e.g. the Glass-Steagall act in 1999, or even in the building up to the current international financial crisis. In my research, I adopt a middle of the road choice. I generally follow the period between the democratization of South Africa with the end of apartheid in 1994 until the international financial crisis in the end of the 2000s. The choice to have a deep political change as the historical mark for my research is founded in the ensuing transformation of the South African economy in the period that followed, with the opening up to the international economy and domestic restructuring promoted by the new African National Congress (ANC) political power, particularly after the adoption of the Growth and Employment and Redistribution (GEAR) strategy in 1996. It would be a mistake to follow this periodisation in a strict manner as many of the processes identified with the end of apartheid had its historical origins years, or even, decades before. Moreover, the inherited economic structures from the apartheid period explain much of the political and economic path taken afterwards. I will therefore integrate historical analysis that goes back from 1994 whenever it proves critical to explain subsequent economic developments.

3.1.1.2. Quantitative work

Thus, the empirical work generally follows the traditional method of hypothesis testing. Taking the Lapavitsas-Dos Santos synthesis as a starting point, a set of empirical hypotheses was derived to be confronted with empirical data. Given the synthesis' focus on recent interactions among corporations, households, and the financial sector, the examination of the extent to which South Africa is a financialised economy was by and large carried out at the sectorial level, aiming at assessing the degree of involvement of each sector with the financial system. The main research question - Is South Africa a financialised country? - was thus decomposed into various sets of partial questions by economic sector:

1. Financialisation in corporate sector

   1.1. Has the corporate sector been increasingly involved with financial markets? Both as liability issuer and asset buyer?

   1.2. Has the corporate sector increasingly found alternative sources of finance to banking?

   1.3. Has the corporate sector increasingly accumulated financial assets?

2. Financialisation in the banking sector

   2.1 Has the banking sector increasingly relied on finance-to-finance funding?

   2.2 Has the banking sector increasingly oriented its operations towards lending to households?

   2.3 Has the household sector become an increasingly relevant source of revenue (absolute and relative) for the banking sector?

   2.4 Has the banking sector become increasingly involved in financial market mediation?

3. Financialisation in the household sector

   3.1 Has households become increasingly involved in debt and asset markets?

   3.2 What has been the evolution of the service of household debt to disposable income?

Given the nature of the research questions – that aim at assessing the extent and the meanings of financialisation for different sectors of the economy – the bulk of the empirical work consists of gathering and analysing macroeconomic data pertaining to the financial relationships of corporations and households with the financial sector and their respective aggregate financial positions. This work benefited from the public availability, but insufficiently explored, of flow-of-funds data of three major sectors – private non-financial corporations, banking sector, and households. The major contribution of this thesis rests, thus, on the original analysis of secondary aggregated data, especially of Flow of Funds data. As will be explained in greater detail in the next section, Flow of Funds data provide information on financial flows of different sectors of the economy, constituting relevant indicators of the financial uses and sources of funding, as well as the instruments resorted to, while allowing at the same time to trace the balance sheet evolution of each economic sector. Thus, not only do Flow of Funds allow us to measure the extent and the contents of corporations' and household's engagements with finance, but they also allow us tracing these engagements in time.

The goal of the empirical work is not to offer the theory a test within a hypothetico-deductive methodology, as it is still the dominant methodological approach in "mainstream" neoclassical economics. In this latter case, economics remains largely a theoretical enterprise whose main concern is to produce testable predictions, with disregard for the realisticness of its assumptions, still very much along Friedman's (1953) lines. Nonetheless, long ago students of science recognized the difficulties entailed by the Duhem-Quine thesis (Quine, 1951), namely that the confrontation of theory with evidence is not simply a logical exercise. The test of any theory always involves a test system: a conjoint test of a target hypothesis (i.e. the hypothesis derived from theory) together with a variety of auxiliary hypotheses necessary to implement, construct, and execute the test. Thus, when confronted with disconfirming data for the hypothesis under test it is difficult to determine which hypothesis(es) is(are) falsified. This means that a clash between theory and evidence does not have the decisive disproving force as suggested, for example, by falsificationism. By the same token, a confirming test result does not provide definitive support for the target hypothesis, for the positive result may be explained by factors other than the validity of the hypothesis under test. In other words, empirical testing is not merely a logical exercise based on the confrontation of theoretical hypotheses with the hard facts. The construction of test systems and the interpretation of test results require evaluative judgments by researchers, based on the practices, norms, and evolving institutional rules governing the critical interactions of scientists.

Thus, the empirical exercise carried out in this thesis should be instead understood in terms of an on-going dialogue between theory and evidence, more along the lines of Lakatosian methodology of scientific research program (Lakatos, 1970), or within an accepted Kuhnian paradigm (Kuhn, 1969), where the theory provides the viewpoint from which to examine social phenomena, and empirical work feedbacks upon theory, contributing to its extension and better fit to its subject matter. In the context of the present thesis, the goal of the empirical work is to contribute to a more substantive understanding of financialisation that takes into account the mechanisms behind the emergence and the variegated nature of this process. To this end, the analysis of flow-of-funds is taken as insufficient. Other sources of empirical data are required to provide the context and help interpreting the aggregate data.

The empirical work has recourse to publicly available, but surprisingly unexamined, source of data: flow-of-funds between three major different sectors – private non-financial corporations, banking sector, and households. The main empirical contribution of this thesis thus rests on the analysis of secondary aggregated data, taking particular advantage of the availability of flow of funds (FoF) data.

Flow of funds data provide information about the financial uses and sources of funding, the instruments resorted to, as well as a dynamic perspective of the balance sheet evolution of each sector in the economy. These data:

"measure financial flows across sectors of the economy, tracking funds as they move from those sectors that serve as sources of capital (…) to sectors that use the capital to acquire physical and financial assets" (Teplin, 2001: 431).

In national account terminology, they are also called financial accounts. FoF thus measure changes in the stocks of each institution due to transactions, valuation effects or accounting reclassifications of financial assets. Financial assets are defined by the System of National Accounts (SNA) as: "An asset that entitles its owner, the creditor, to receive a payment, or series of payments, from the other unit, the debtor, in certain circumstances specified in the contract between them" (UN et al, 1993: 276). [20] And they are classified under eight major categories: monetary gold and special drawing rights (SDRs); currency and deposits; securities other than shares; loans; shares and other equity; insurance

[20] Any financial asset for a creditor is naturally a financial liability for the debtor (with the exception of monetary gold and special Drawing Rights).

technical reserves; financial derivatives; and other accounts receivable/payable (UN et al, 1993).

Institutional sectors, grouped according to their economic behaviour, are divided in five broad groups by the System of National Accounts: non-financial corporations sector; financial corporations sector; general government sector; non-profit institutions serving households sector; and the household sector. Generally, the presentation among different countries follows the SNA, despite differences in the aggregation in categories of transactions and sectors.

To summarize, flow of funds provide information about financial flows of different sectors of the economy, the asset content of such flows and both the gross and net financial position of different sectors in time, allowing assessing how and when different sectors of an economy interacted. This is the primary source of empirical data of the present thesis, as it aims at better understanding the content financialisation for different sectors of the economy, their financial interactions and overall evolution over the past decades.

In South Africa, flow of funds are compiled and publicly presented by the South African Reserve Bank (SARB). This data is compiled through the balance sheet approach, contrary to the most common transaction approach (De Beer et al, 2006). In the former approach, flows are accounted through changes in the institutions' balance sheets[21], using a double entry system that distinguishes sources and uses of funds. These are computed from thirty two non-financial and financial transaction items contained in five main sectors – Foreign Sector, Financial Intermediaries, General Government, Corporate Business Enterprises and Households – which represent eleven sectors and twenty two different institutions (Table 3.1),from (De Beer et al, 2006). The balance sheets of each institution are first balanced and then consolidated in the eleven sectors in two steps:

[21]The flow of funds compilation can also be made through transaction data. In the case of South Africa, given the absence of balance sheet data from the private sector and households, their positions are derived from the data from the other sectors.

“Step 1 of the processing involves making sure that corresponding sectors have the same sources and uses by using the macro-driven spreadsheet. Since it is impossible to have a perfectly balancing economy due to many factors including timing in reporting and general errors, the data may need to be adjusted using financial market performance trends, source data integrity of the sectors and economic intuition of the compiler(s).

Step 2 of the processing involves incorporating savings and investment data into the final spreadsheet. While step 1 deals with the financial sector data or bottom-up calculation of the net lending/borrowing position, step 2 deals with the real sector data or top-down calculation of the net lending/borrowing position. The detailed data processed in step 1 must therefore agree with the new data brought in during step 2. There are always some minor adjustments made in the balancing items.” (De Beer et al, 2006: 241-2)

The public available data comprises the eleven sectors, thus enabling for breakdown analysis choosing specific sectors. The Flows-of-Funds data for South Africa have been revised and improved for the 1999-2009 period, replacing the previously published annual data, given technical improvements in the compilation of flow of funds since 2006 and a recent revision of national accounts data. Such revision did not entail any major change in the sectorial balance sheets and the revised tables published in 2011 are the data source used in my analysis.

Nonetheless, some caveats apply to the South African flows-of-funds when compared to FoF data presented in developed countries, most notably the US. The South African list of financial assets in the flow of funds differs over the one established by the UN’s System of National Accounts. The number of financial assets/liabilities is more restricted than what is presented in some countries and involve levels of aggregation where important categories of financial assets are amalgamated. Some of the items have a straightforward reading (such as on different government bonds) and go beyond the SNA in detail such as monetary (bank) deposits. However, some of the items explicitly put by the SNA, such as financial derivatives, are prone to be read with ambiguity (e.g. Long-term loans). The second shortcoming of South African flow of funds is the difficult identification of the origin and destination sectors of the flows. In some of the asset categories, the origin sector of the flow is self-evident (e.g. “bank loans”; “monetary deposits”), but categories such as “long term loans”, or the even more broad “amounts payable/receivable” (where derivatives are to be found) introduce a degree of indeterminacy on the origin sector, which can only be partially solved by the intuitive detection of significant sources and uses of every asset/liability for each year. Direct help from the flow of funds division of the SARB clarified the content of a number of items (e.g. the neither non-bank nor bond nature of “long-term loans” and the integration of financial derivatives in the item “amounts Receivable/payable”). In order to make these transaction items intelligible, depending on their significance, I propose my own aggregation of items depending on the analytical interest at play in each of the sectors considered, hence the aggregation that I propose for each sector analysis in the relevant chapters[22].

Table 3.1. South African flow of funds organization

Main Sectors	Sector Breakdown	Institutions	List of financial assets/liabilities
Foreign Sector			1.Gold and other foreign reserves
Financial Intermediaries	Monetary authority	South African Reserve Bank	2. Cash and demand monetary deposits
		Corporation for Public Deposits	3. Short/medium-term monetary deposits
	Other monetary institutions	Land bank	4.Long-term monetary deposits
		Private Banks	5. Deposits with other financial institutions
		Mutual and post office savings banks	6 Deposits with other institutions
	Public Investment Corporation		7. Treasury bills 8.. Other bills
	Insurers and retirement funds	Long-term insurers	9. Bank loans and advances
		Short-term insurers	10. Trade credit and short-term loans
		Public pension funds	

[22]For example, Public debt securities are distributed in a number of different transaction items, which only rise confusion in the reading of the data and are thus aggregated in the analysis presented.

		Private pension funds		11. Short-term government bonds
	Other financial Institutions	Trust companies		12. Long-term government bonds
		Unit trust		13. Non-marketable government bonds
		Finance companies		
		Participation bond schemes		14. Securities of local governments
		Public sector financial intermediaries		15. Securities of public enterprises
General government	Central and Provincial Governments	Central and provincial governments		16. Other loan stock and preference shares 17. Ordinary shares
		Social Security funds		
	Local Governments			18. Foreign branch/head office balances
Corporate Business Enterprises	Public Sector			19. Long-term loans 20. Mortgage loans
	Private Sector			
Households				21. Interest in retirement and life funds 22. Amounts receivable/payable 23. Other assets/liabilities 24. Balancing item

Gross and net flow of funds and the financialisation hypothesis

In the following chapters, I analyse both net and gross sources and uses of the flow of funds for each sector. Such distinction is useful. The use of gross and/or net flows obeyed to the hypothesis testing as was the case of the computation and reorganisation of statistical categories in order to provide an analytical frame that allows the pin down the relevant data for the hypothesis assessment. For example, gross flow of funds provide good measures of the scale of financial dealings evolution for each sector but is insufficient to measure the uses of funding and the financial net position of each sector which measure its solvability. On the other hand, net Flow-of-Funds give us the overall financial position (positive and negative) of each sector in relation with the others as it provides their evolution along the considered period.

The level of detail and reorganisation of the Flow of Funds analysis will nevertheless vary when considering the particular hypothesis to be tested. The chapter on private non-financial corporations discusses different sources of net funding – internal sources, banking, equity, etc. – which presupposed the netting of different transaction items, which involved the aggregation of different Flow-of-Funds items in order to pin down broad categories as of “traditional” banking funding; financial market securities (equity and debt) funding and acquisition and internal resources. The method here adopted followed roughly the one presented by Corbett and Jenkinson (1997) employed to study how the corporate sector physical investment is funded (used in a comparative analysis of non-financial corporate sector of Germany, Japan, the United States and the United Kingdom).

Funding Sources (own savings, bank loans, bond and stock issuance, etc.) and Uses (physical investment and different financial assets) of financial flows are separately scrutinised. Since some funds go to financial assets, if one “subtracts the acquisition of financial assets from increases in equivalent liabilities”, (1997: 72) net categories (sources minus uses) are achieved. The funding sources of physical investment are then discernible. For our purposes, this method allows us to attain all the net financial sources of corporations, enabling the measurement of the net relative weight of each funding source category. For our research, we use an expanded version of the categories used in the original work by Corbet and Jenkinson, with nine instead of five categories (left column of Table 4.1), in order to account for categories that lie outside their original framework but are relevant for South African corporations.

In order to provide a simplified framework for discerning major categories in corporate funding, two accounting steps were required here. First, a few intermediary categories were built (text bold at the right column of Table 4.1), following the SARB flow of funds notes, namely “Monetary Deposits” and “Bills, bonds and loan stock”, so as to discern the aggregate importance of all banking financial deposits and of all debt securities with which the non-financial private sector operates. The second step concerns the construction of the eight net categories: Internal Sources; Net Bank Credit; Net Debt securities; Net Equity; Net Trade credit and Short Term Loans; Net Other Deposits; Net Long Term Loans; Net Amounts Payable/Receivable, Net Other Sources/Uses.

Internal sources are obtained by adding Net savings, Consumption of fixed capital and Net Capital transfers. For Net Bank Credit, the item “Mortgage Loans” was included as a bank credit source since the overwhelming majority of mortgages are issued by banks. The category presented by the SARB Flow of Funds notes as “Mortgage and Long Term loans” was here disaggregated leaving long term loans (issued by agents other than banks, such as insurance companies) as an item of its own. The item “Other Deposits” was not considered as a bank financial use as it concerns deposits with non-financial and financial institutions other than banks (e.g. mutual funds) and, therefore, it rests as a separate category as well. “Net debt securities” is the result of net “Bills, Bonds and Loan stock”[23] sources and uses, resulting in a category that accounts for the weight of marketable debt securities in corporate funding. Net other assets and liabilities is attained by subtracting the item “Interest Paid by Retirement and Life funds” from the net item of Other asset and liabilities (as carried out in SARB flow of funds). “Net amounts of payables/receivables” is taken from the aggregation made in the SARB flow of funds in order to give a more clean depiction of such a generalist category.

Finally, a note must be made on the period taken into account here (1994-2008), which does not fully consider the behaviour of corporations during the current international financial crisis[24]. Given the impact of this crisis, 2009 flow of funds is only to

[23] The name “bond” is used in the South African flow of funds as an item solely for public institutions (Government and local authorities).

[24] With the recent international crisis, the overall South African corporate sector suffered considerable declines in the granted credit (-3.2% in the first half of 2010), which in turn is reflected in the drop of investment (-4%). The SARB (2010) points to the weak household demand as a possible cause for such decline. It should be pointed, however, that following the simultaneous

be included in the differentiated analysis of gross liabilities and assets for each year in the second part of this section.

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decline of profits and credit in 2008, this two indicators began to behave differently in 2009 with soaring profits and stagnated credit and investment pointing probably to a deleveraging strategy of the corporate sector. The ratio of credit as a percentage of annualized profits has gone from 180%, in 2009, to 140%, in 2010, a level never reached during the decade.

Table 3.2. Flow of funds Net Finance source Categories

Net categories	**SARB Flow of funds categories**
Internal	1. Net Savings + 2. Consumption of Fixed Capital + 3. Capital Transfers (Sources-Uses)
Net Bank Credit	17.Bank Loans and Advances + 28.Mortgage Loans **- Monetary Deposits** (10.Cash and demand monetary deposits + 11.Short/medium term Monetary Deposits)
Net Equity	**25.** Ordinary Shares **(Sources – Uses)**
Net Debt Securities	**Bills and loan stock** (16. Other Bills + 24. Other loan stock and preference shares) **– Bills, bonds and loan stock** (15. Treasury Bills + 19.Short term government bonds + 20. Long term government bonds + 21. Non-marketable government bonds + 22. Securities of local government + 23. Securities of public enterprises + 24. Other loan stock and preference shares)
Net Trade credit and short term loans	18. Trade credit and Short Term Loans (S-U)
Net Long Term Loans	27. Long term loans (S-U)
Net Other Deposits	13. Deposits with other financial institutions + 14. Deposits with other institutions (S-U)
Net Amounts Payable/Receivable	30. Amounts Payable/receivable (S-U)
Net other sources/uses	31. Other assets and liabilities (S-U) – 29. Interest in retirement and life funds.

However, in the cases of banks and households such source netting by broad computed transaction items is either impossible to achieve – e.g. banks are overwhelmingly funded by deposits, but its source is not discernible from the FoF data – or unnecessary given the weight of a small number of categories – households have their financial assets mainly either in the form of deposits and interest in insurance and retirement funds and their liabilities in mortgage loans and other banking loans. In the case of banks, the problem is to be addressed by other data sources such as Banks balance sheets. Gross flow of funds divided in both sources (liabilities) and uses (assets) of funds provide a more detailed and straightforward portrait of the absolute involvement of each sector with each particular transaction item and of the pattern changes along time. All the data here presented was deflationed to 1994 prices (the first year of my periodisation) using GDP deflactor with the aim of having comparable real flows along the period here under analysis.

Bank and households balance sheets

As argued above, although the net flow of funds for the private non-financial corporate sector suffices to have a depiction of sources and categories of net funding, in the case of banks such exercise seems more difficult to achieve. The veil posited by items exclusively attributed to banks - liabilities as deposits and assets as mortgage lending and other banking loans – impedes the assessment of the source and recipient sectors of banking flows. Such caveat is to be addressed by the analysis of aggregate bank's balance sheets publicly provided by the SARB through the returns banks are obliged to deliver to the monetary authority. Bank returns on their balance sheet data and the BA 900 returns (which present selected balance items with institutional and maturity breakdown of liabilities and assets), allow me to scrutinize the trends and patterns of both bank funding and bank lending behavior with further detail on transaction item and, more importantly, the sector from and to which the bank flows come and go. Nonetheless, as with the statistical computation of Flow of Funds, the hypothesis testing for banks imply a reorganization of accounting items in order to pin down the different hypothesis to be tested. Hence, analysis of balance sheets, given the sheer number of assets and liabilities present, will involve and exercise of identification and aggregation – with an obvious component of subjective discretionarily - of significant items for my analysis, in order to better indicate how and with which sectors does banking funding and lending relate. For example, involves both a breakdown of deposits in "traditional" retail deposits and money market instruments and the aggregation of loans for a better depiction of the relative importance of financial investment positions relative to the loans granted to corporations and households. Such reorganization and computation of data is explicitly elaborated in the chapter 6 where the empirical analysis is pursued.

In order to better grasp the changing content of the banking business in South Africa, further information on the relation between banks and the rest of the economy can be taken from bank income returns, which, despite having no institutional breakdown, can be of use since particular items are clearly related to specific sectors (e.g. "mortgage loans" with households, "knowledge-based fees" with the corporate sector). Balance sheets provided by the SARB will also be used as a data source for the household sector. However, this data is much less reliable than for banks as there is no direct source of knowledge on the aggregate household balance sheets. Despite its helpfulness in the assessment of general balance sheet evolution (growth or contraction) that illustrates the involvement of households with the financial sector, such data rests on a number of data sources (of which banks balance sheets) and assumptions on the pricing of assets and liabilities that should be taken with some parsimony.

Given the importance of the banking sector in the financial dealings of households, much of the financialisation hypothesis on this latter sector can be assessed from the banking financial data – e.g., increasing bank income coming from households -, however I am here interest also in the weight of financial dealings of households relative to their income. Such verification of hypothesis is to be made through household balance sheet analysis from the SARB and the Flow-of-Funds not only in the gross and net flows (aggregated and computed into relevant categories) as presented for the previous two sectors, but also relative to household disposable income. Such exercise will allow an assessment of financial debt stress and income crucial for the testing of hypothesis subjacent to the Lapavitsas-Dos Santos financial expropriation concept.

3.1.1.3. Qualitative work

The analysis of flow-of-funds is largely insufficient to depict and understand financialisation in South Africa. Other sources of empirical data are required to provide the context and help interpreting the aggregate data. Thus, the analysis of aggregate data is supplemented by various sources of both quantitative and qualitative data.

Depending on the Lapavitsas-Dos Santos's assertions under scrutiny, the theoretical elaborations that have resulted from the confrontation of theory with data have guided the search for additional sources of information. Besides the economic literature on South African economy, and additional sources of quantitative sectorial information, such as the Banking and Financial Stability Reports of the South Africa Reserve Bank, the present thesis relies heavily on secondary literature on the South African recent economic history, from various disciplinary and inter-disciplinary viewpoints, including political economy, history, sociology, anthropology and law. This allowed indirect access to an array of primary qualitative data collected with recourse to various methods, including surveys (particularly pertinent when approaching the financial dealings of households), semi-structured interviews (mainly used in the household sector) and institutional analysis (of legislation, public policy, etc.).

The use of qualitative information has had two main purposes. Firstly, to assist the interpretation of the patterns and trends of the financial behaviour of the South African sectors identified in the quantitative research. Secondly, to account for the socio-economic, institutional and historical specificity of South Africa, which was found critical to further elaborate the concept of financialisation and extend its applicability to countries and regions other than the core capitalist countries.

In the cases of the non-financial corporate and the banking sectors, and given the historic oligopolistic configuration of the South African economy (dominated by big capital conglomerates), particular attention has been devoted to the literature which traces the post-apartheid trajectory, namely the political economy contributions on conglomerates – e.g. Fine and Rumstjee (1995), Chabane et al (2006); Roberts (2010);; Marais (2012) – and banks – e.g. Bond, (1998); Hawkings (2004); Gilbert et al (2009); Singleton and Verhoef (2010). Data retrieved directly from the websites and/or accounting reports of these corporations, as well as from the press, enabled tracing the shareholding structure and changes. Moreover, historical accounts of the evolution of these non-financial and financial conglomerates were introduced in order to identify the evolution of their specificity and idiosyncratic behaviour, from the apartheid to the democratic period, which is the focus of this thesis. Finally, literature on relevant public policy debates and on the mutation of the conglomerates and banks, such as on the legislation and official reports on Growth, Employment and Redistribution or on Black Economic Empowerment were also integrated with a view to identify both political constraints and opportunities presented for these sectors during the last twenty years.

Finally, as regards households, and going beyond the empirical analysis of the financialisation hypothesis from FoF statistics, further information was retrieved from the SARB, the Statistics of South Africa (SSA) and from other official and private agencies, such as the National Credit Regulator (official) and Finmark (private), about the socio-economic evolution of the country, to help interpreting and expand the quantitative account of households financial transactions and wealth derived from the Flow of Funds data. These sources of secondary data, which rely mainly on surveys and semi-structured interviews, were supplemented by academic literature on the relationship between finance and South African households, including the poorest layers.

This wide range of sources and literature mobilized in the context of the present thesis provide the macro social and economic frame for an overall understanding of financialisation from a political economy perspective as it was defined above – a process of capitalist transformation that encompasses whole societies. Such interdisciplinary perspective should thus elucidate particular social phenomena such as financialisation, taking into account the restrictions posed by history and social structures (Lawson, 1997). As eloquently put by Karl Marx in his "The Eighteenth Brumary":

"Men make their own history, but they do not make it just as they please; they do not make it under circumstances chosen by themselves, but under circumstances directly encountered, given, and transmitted from the past. "(Marx, 1868 [1852])

3.2. South African Public Policy: From socialism to neoliberalism

In the midst of a recession between the late eighties and early nineties, the democratic transition was characterized by a debate on what should be the South African economic policy in the following years. South Africa had inherited and uneven economy, centered around the mining and energy sectors in what Fine and Rumstjee (1996) defined as Mineral-Energy Complex (MEC), being the:

"mining and energy sectors and a number of associated sub-sectors of manufacturing, which have constituted and continue to constitute the core site of accumulation in the South African economy. (…) contrary to the popular view that there has been a declining role for mining, the economy's dependence on this MEC core has in fact increased." (1996: 71)

In close collusion with the apartheid political power which provided cheap inputs through its major public corporations – for example, ISCOR in steel and ISCOM in electricity – the MEC was organized around industrial conglomerates (axis of capital) whose activities, forced by the economic isolation of the seventies and eighties, reached most of the sectors of the South African economy. Given its isolation during the final stages of apartheid, coupled with permanent illegal capital flight from the country, which deprived this economy from important resources, this economic model showed signs of exhaustion with very low investment and growth rates and overall stagnation. In the beginning of the nineties investment had collapsed (from 27% to 15% of GDP during the 1983-93 period), with more than 40% of its labour forced ouside the formal sector, although public (52,5% of GDP in 1994) and foreign debt were far from being problematic by international standards (Habib and Padayachee, 2000).

The debate around economic policy for democratic South Africa was first influenced the ruling National Party and the influential capital conglomerates remained influential in the designing of economic policy of democratic South Africa. The initial progressive efforts coming from the ANC were met with plethora of policy documents coming from the private sector – Old Mutual's Prospect for a Successful Transition or the Sanlam's Platform for Investment – and official international bodies as the World Bank or the IMF aligned with the neoliberal Washington Consensus. Such documents, based on trickle-down economics,were to have its highlight with the "The Restructuring of the South African Economy: Normative Economic Model" (NEM) transition program, in 1993. focused on the need of restrictive fiscal and monetary policies coupled with the liberalisation of the economy, particularly in the financial sphere, privatisation and deregulation. The constraints of the South African economy were thus to be found on the supply side, with the state intervention in the economy to be understood as "crowding-out"private investment. These efforts, particularly the NEM "(…) cemented state thinking about the economy in a manner that became exceedingly hard to unstick" (Bond, 2006: 78).

This economic and intellectual hegemony tied with calls for negotiation and consensus for the post-apartheid era resulted in the short life of alternative perspectives for the South African coming from the ANC alliance (compromising the COSATU confederation of Unions and The South African Communist Party).

It is true that he evolution of economic policy of post-apartheid South Africa has been determined almost exclusively the African National Congress (ANC) who has ruled the country since the first democratic elections. However, its economic policy standings rapidly changed from the period it was still an illegal organization to its government period. The foundational Freedom Charter of 1955 stressed economic equality through nationalisation:

"The mineral wealth beneath the soil, the Banks and monopoly industry shall be transferred to the ownership of the people as a whole". A stance continued even in the final stages of apartheid. Driven by strong popular mobilization of the 1980s, Nelson Mandela stated in 1990 that: "The nationalization of mines, banks and monopoly industries is the policy of the ANC and a change or modification of our views in this regard is inconceivable." (1955)

Such socialist proclamations were however rapidly reverted. The ANC lacked a coherent economic program to present to the country during the transition years (Marais, 2011) with the first efforts to be embodied with its Department of Economic Policy Discussion document of 1990 (the year of ANC's unbanning), but inin a context of international turmoil with the collapse of the Soviet Union (discrediting socialist alternatives), the rise of supply-side economics and the new success stories of Japan or

South Korea (Sender, 1994). Two major intellectual efforts from the ANC sphere of influence arise during 1992-93 debates: the collaboration of progressive academics around the Macroeconomic research group (MERG) and the more outward-oriented "flex spec" Industrial Strategy Project (ISP) (Fine, 2008a).

The work of the MERG, published as "Making democracy work – A framework for Macroeconomic Policy in South Africa" (1993), laid out a comprehensive program for ten years, with a subjacent macroeconomic model that favoured public investment of social infra-structure (housing, electrification and "human resource development"), tax reform through the introduction of taxes on wealth, property and capital gains, a monetary policy focused on low real interest rates and an trade and industrial policy that, although not proposing the south African conglomerates unbundling, proposed to "coordinate export support programmes with protection policy" (MERG, 1993: 16). Concerning the financial sector, the proposals were more modest, aiming at financial inclusion and tax incentives and "German" bank-based model where banks and industry work closely, organizing coporate financing and ensuring representation "(..) of banks on the supervisory boards of companies above a certain size (…) (1993: 258). Finally capital markets should be taxed in order to orient investment to "infrastructural ventures" and are perceived as an instrument for the entrance of public funds as new shareholders on the major conglomerates. The MERG, distancing from historic socialist proclamations, tried to establish a "left-keynesianism" approach where discussion on the possibility of a developmental state (Sender, 1994), boosting domestic demand, would attain an economic growth of 5% of GDP and the creation of 300 000 jobs per year. The MERG influence was, however, brief. According to one of its participants (Ben Fine): "Within six months of its having been commissioned and even before it was published, the MERG report was disowned by the leadership of the ANC" (2008: 4).

The ISP (Kaplinsky et al, 1995) was the result of work commissioned by COSATU trade Union and, although often seen as compatible with the MERG work, had a different perspectives on the challenges and objective which was mainly the south African manufacturing revival. Influenced by French regulation School (Fine, 2008), this report focused on the promotion of manufacturing and the promotion of exports through better technology and higher productivity. There is thus more concerns here with potential balance of payments constraints and the dangers of more relaxed monetary policy (Habib and Padayaachee, 2000). Such focus results in scarce proposals concerning the financial sector.

In late 1993, the ANC presented its Reconstruction and Development Program (RDP) with which it came into power in 1994. The program tried to combine the state intervention in the economy, influenced by the ISP in its outward focus, while preserving the recognition of Central bank independence in what seems to have been a condition for Transition by the national Party (Klein, 2007). Assessments of this program differ from the appraisal by Weeks (1999) or Tshitereke (2006) for its commitment to growth through redistribution and fight against inequality to more nuanced analysis of Bond (2006) and Marais (2011) that identify critical elements of macroeconomic restrictive policy, Reserve Bank independence and promotion of international competitiveness as the result of the neoliberal hegemony already enshrined in this document. The document, following in that aspect the ISP, was silent on financial sector proposals. In fact, for Stephen Gelb (2006) the program of financial liberalisation and integration in the international financial markets was already a feature of the ANC prior to arriving in power:

> "Alternative positions – particularly with respect to financial liberalization – were in some sense "unthinkable", because the economy had experienced several years of stagnation and stop-go growth cycles resulting exactly from a closed financial system and the absence of foreign capital inflows due to sanctions, disinvestment and so on. The need for capital inflows to support growth had been strongly argued by the ANC for years – could it now turn around and credibly propose growth policies without encouraging and enabling flows?" (2006: 3)

Nonetheless, the RDP was short-lived, being replaced by the market-oriented Growth, Employment and Redistribution (GEAR) plan in 1996 for the new ANC dominated Government of National Unity (where the Finance Ministry was initially given to the National Party). The plan embraced fighting inflation, guaranteeing positive real interest rates, reducing budget deficit (to 3% of GDP by 2000), liberalizing capital controls, privatizing "non-essential" public companies and enhancing an investment friendly tax system, reducing direct taxes and raising indirect (regressive) ones. Even compared to the more moderate RDP, GEAR was a turn in economic policy, encompassing a core neoliberal agenda. Such turn by ANC elites is to be found the balance of power of the south African economy, namely new found power of the "Washington consensus" institutions in the international sphere, the importance of foreign investment and its gained ability to displace resources and, finally the need to compromise with domestic capital that hegemonised the public debate (Habib and Padayachee, 2000).

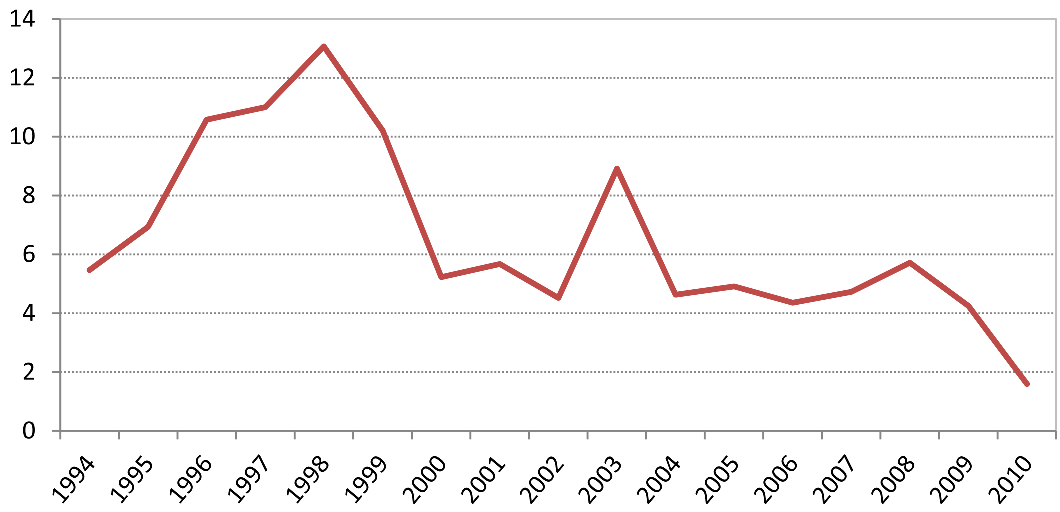
The economic rationale of the adoption of fiscal and monetary restrictive policies was found in the need to attract foreign direct investment to the country in order to boost the small levels of savings and investment that had characterized the South African economy since the 1970s. In an environment of controlled inflation, the liberalisation of trade and capital accounts would enable foreign capital inflows needed to enhance investment:

"To contain inflationary pressures requires concerted implementation of complementary stabilisation measures: accelerated tariff liberalisation, sharper deficit reduction, tight monetary policy, and above all, productivity linked wage increases. (…)As a result of the reduction in government consumption expenditure relative to GDP, and the reversal of government dissaving, gross domestic saving is expected to rise from 18 % to 22 % of GDP. (…) Gross domestic investment is expected to increase from 20 % to nearly 26 % of GDP in the year 2000. This requires capital inflows equivalent to almost 4 % of GDP. The integrity of this growth strategy is therefore dependent on maintaining a favourable investment climate, in order to attract foreign investment. "(South African Treasury)

This market-oriented approach where integration in the international economy was pivotal was to be the cornerstone of public policy in South Africa throughout the whole post-apartheid era. The budget deficit was in fact reduced sharply in the 1990 from 4.9 % in 1996 to 1.9 % in 2000, with public debt to reach 44.4 % for the same year (Table 3.2).

3.2.1. Macroeconomic outcomes

However, as pointed by Weeks (1999), the years that followed this approach until the end of the 1990s had dismal results. Marked by extremely high interest rates (Figure3.1) which prevented investment to grow, strict fiscal policies that limited public intervention and the outflow of domestic capital meant South Africa did not enjoy the international growth of the 1990s.



Source: World Bank development indicators.

Figure 3.1.Real interest rate (%).

Moreover, the Asian financial crisis of the end of the 1990s impacted the South African economy dearly with GDP growth to slow down to negative per capita rates (Figure 3.2). This period was marked by a domestic currency crisis when, following the turmoil of emerging financial markets, particularly in Asia, a sudden halt of short term capital movements led to speculation over the imminent devaluing of the rand, despite previous accumulation of foreign reserves. Such speculation eventually forced a 35 % depreciation of the rand (Mohamed, 2006).The rand depreciation that followed was met by the SARB with a raise of interest rates – to a record high of 13 % of real interest rates - in order to prevent further depreciation and inflation, causing the 1998 recession. The following currency crisis in 2001, again caused by the international turmoil of the time, had a more relaxed reaction from the monetary authority (Bhundia and Ricci, 2005), enabling the economy to adapt in a milder way. However, the financial stress endured by the South African economy continued until 2003 when a banking crisis erupted with the failing of smaller banks (e.g. Sambou), putting stress on the whole financial system.

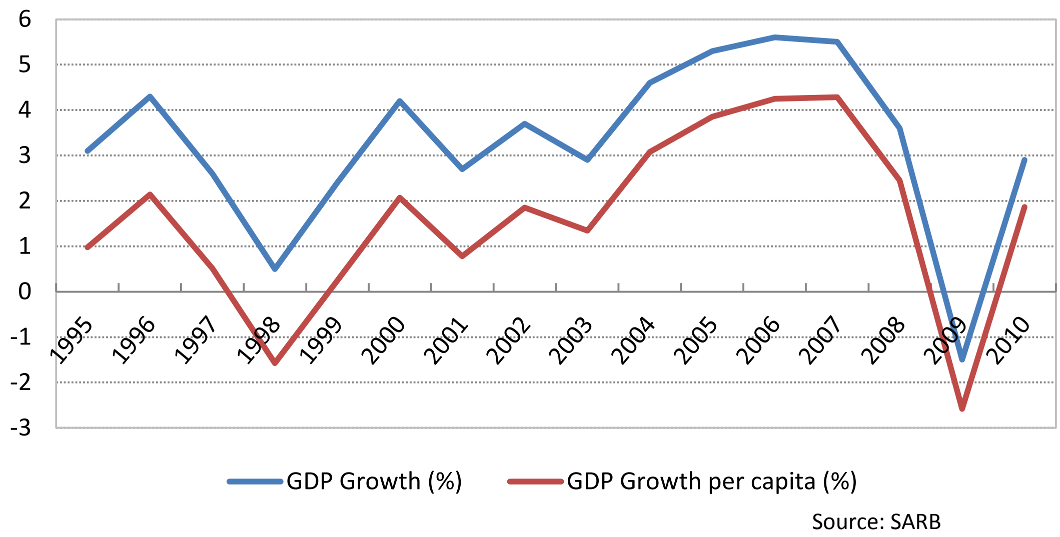
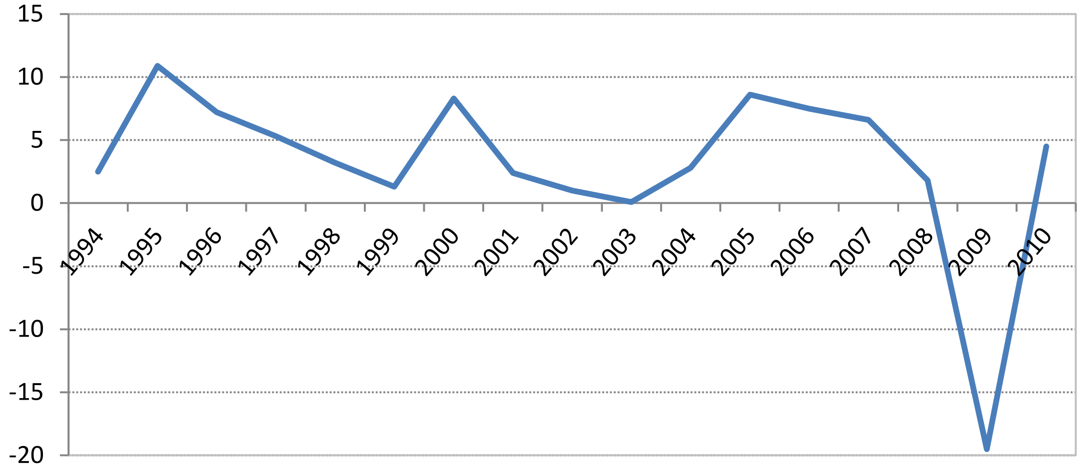


Figure 3.2. Economic Growth

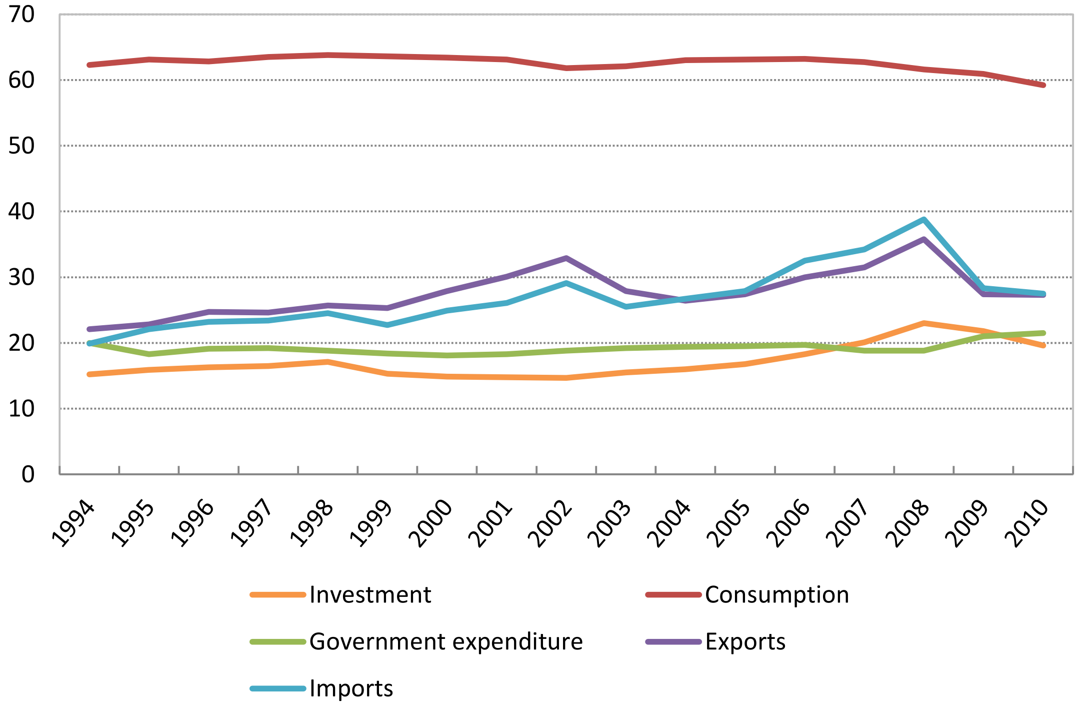
Growth finally picked up in the middle of the 2000s with growth rates to reach between 4.6 % in 2004 and 5.5 % in 2007. This surge can be attributed to a conjugation of different factors. Being still an economy dependent on their mineral and energy sectors exports, South Africa benefited from the rise of commodities prices in the international markets. This was particularly the case for three of the major South African exports: gold (despite declining output), platinum and copper (SARB, 2008b). Exports share in GDP was to surge from 26.4 to 35.6 % between 2004 and 2008 (Figure 3.4), thus becoming one of main drivers of growth during the period (Figure 3.3). However, helped by the valuation of the South African rand between 2003-2005, imports grew at a faster pace than exports for the same period – 26.7 % to 38 % of GDP. These rising imports resulted from a combination of the sustained consumer spending – fuelled by credit extension (Mohamed, 2006) -, the surge in infra-structure investment in the second half of the 2000s and higher oil prices (SARB, 2007b). The result was thus one of fast deterioration of the South African balance of payments from the small deficits of the nineties (between 1% and 2% of GDP), and even surpluses in the beginning of 2000s, to large current account deficits of around 7% of GDP in 2007 and 2008.



Source: SARB

Figure 3.3. Exports (annual growth rate, %).

The acceleration of growth seen in the 2000s was thus not totally dependent on export performance. Contrary to what happened during the increase in exports in end of the 1990s, this later period saw a parallel growth of investment in the economy, growing from the low levels of 14% of GDP in the beginning of the 2000s to 21.4% in 2008 (Figure 3.4), being the second major driver of growth during the period.



Source: SARB

Figure 3.4. GDP composition by expenditure (%).

Despite benefiting all sectors of the economy, this investment growth was to be concentrated in the Finance, Insurance, and Real estate (FIRE) and in the manufacturing sectors – from 41 billion in 2002 to 68 billion rand in 2007 and from 42.5 billion in 2002 to 73 billion rand in 2008 respectively (2005 prices)-, with the mining and quarrying sector to lag its growth until 2006 (Figure 3.5). The greater influx of net capital flows at the during the 2000s enabled the growth of South Africa's financial sector and the private credit extension to households, fuelling the housing market and consumer related sectors, such as wholesale and retail trade.

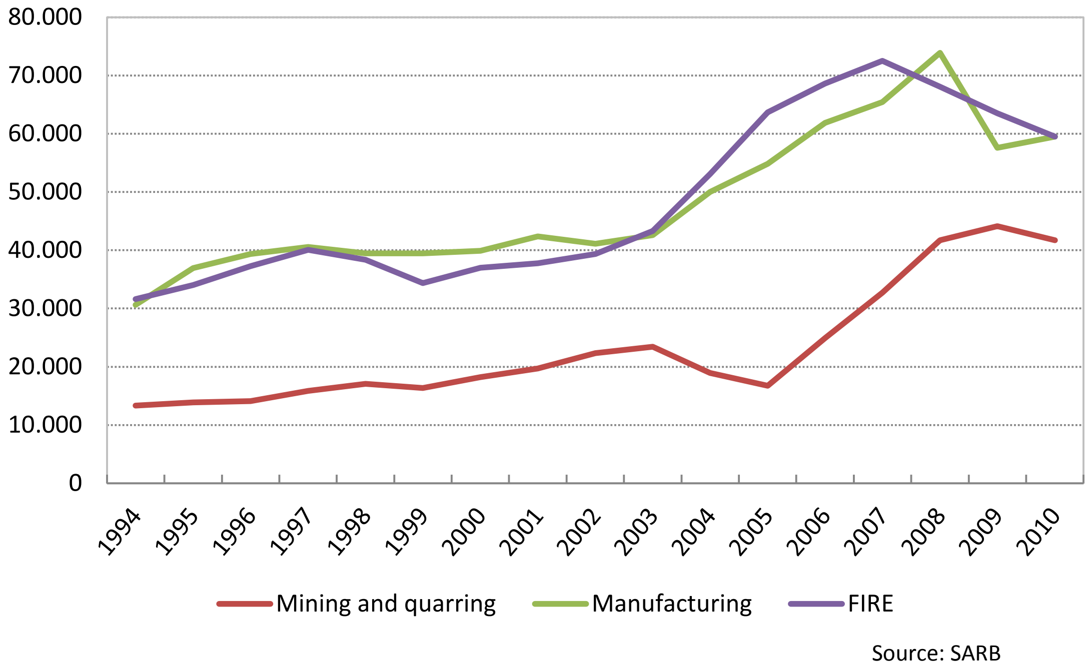


Figure 3.5. Investment – selected sectors (Mn rand).

3.2.2. Searching a developmental state

Fostered by the dismal economic and social results until the mid-2000s, a turn in the political discourse of the ANC from 2005 (Edigheji, 2010) and, more generally, of the South African State seems to have arisen, promoting a new, at least rhetorical, approach for the engagement of the State in the economy. With the *Accelerated and Shared Growth South Africa* (2006) strategy, South Africa embraced infra-structure and energy (capital intensive) public investments, mainly through the "parastatals" ESKOM (energy) and Transnet (transport), and further support for the domestic automobile industry through the

Motor industry Development Programme (Marais, 2011). The positioning of the State, reinforced by the financial crisis of 2008 that highlighted the role of public policy in stabilizing the economy, has been incorporated in the (recovered) notion of a South African developmental state. This became one of the Strategic Priorities put forward by the South African Presidency in its Medium Term Strategic Framework:

"There is an appreciation on a global scale that the markets on their own are incapable of rectifying problems that their own rapacious license has generated in the first instance. The state has a critical role to play in rectifying these weaknesses, particularly in the financial sector, thereby ameliorating the effects of the crisis on the real economy and the conditions of life of especially the poor. (…) At the core of this should be efforts to build a developmental state with the strategic, political, administrative and technical capacity to give leadership to this process, and an active civil society."(Presidency, 2009: 5).

Fostered by political intentions, the academic debate around the possibility of a South African developmental state[25] has known a revival from the debates around economic development of the first half of the 1990s. However, converging with the perspective that given the current international economic architecture the developmental space is shrinking (Wade, 2003), most accounts on South Africa remain skeptical. Southall (2006) points to the perils of replicating the Asian experiences in South Africa, given its current international insertion (highly dependent of resources exports) and an internal political economy that accommodates a "black controlled state, still mainly white owned industry, a black working class, an impoverished black informal sector and propertyless black rural population heavily dependent upon transfers from urban areas for their subsistence" (2010: xli), which hamper the needed embedded autonomy and capacity of the state to pursue long term inclusive development. This is a perspective shared by Terreblanche (2008) who additionally points, on the one hand, to the demobilization of social movements and the capture of black elites by the South African establishment -

[25] The notion of a developmental state was developed theoretically by Peter Evans *Embedded Autonomy: States and Industrial Transformation* (1995), which aims to answer the hegemonic neoliberal notion of state put forward notoriously by Deepak Lal's critique of state intervention in developing countries as always having a distorting effect in the economy and by Anne Krueger's conception of the state as providing incentives for inefficient rent seeking behavior. Put briefly, drawing mainly from the Asian experiences of economic development, Evans presents a typology of three different forms the State can take – Predatory, Intermediate and Developmental, with the later to embody the concept of embedded autonomy. In this case, the state is the result of different interests and networks of the civil society (embedded) and it remains autonomous from the capture of particular sectors in order to pursue long term economic development.

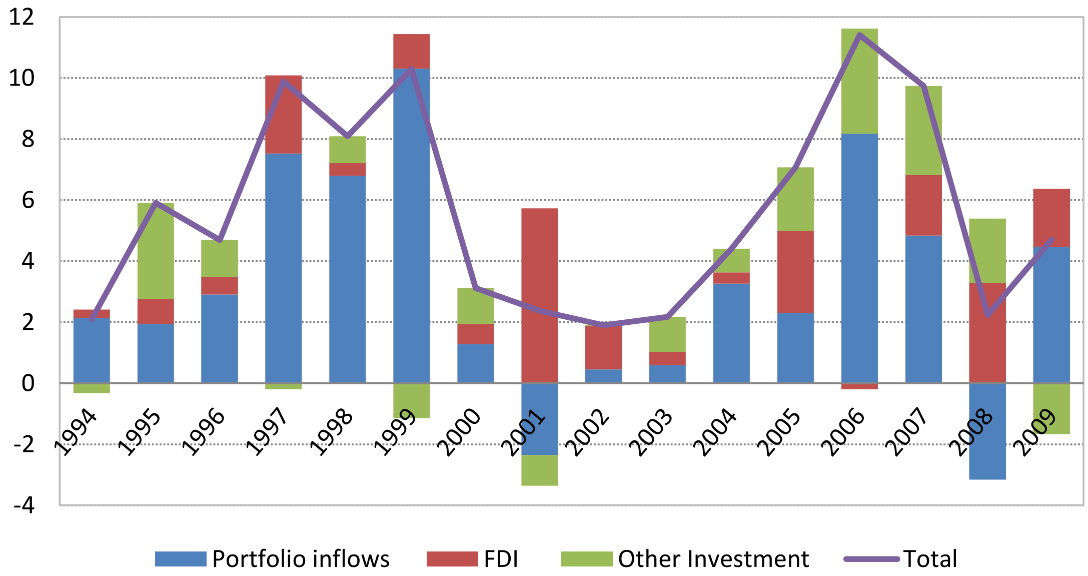
notoriously through the Black Economic Empowerment strategy -, and on the other hand, to the lack of state capacity and powerful economic interests - embodied domestically in local corporations and internationally through the hegemonic Washington consensus institutions (IMF, Word Bank) –, which create a power constellation where “Pretoria” is the weakest link. Fine (2010) notes that such interventionist new stance seems to be a belated recognition of the MERG programme of the beginning of the 1990s, but such intentions are met with suspicion, even arguing that “If South Africa has ever been a developmental state, it might be considered to have been more so in the past than now or in the most immediate future.” (2010: 174). For Fine, with South Africa being characterized by the historical influence of its MEC, where State and big conglomerates converged, the accommodation of Afrikaner interests in the post war period precluded a state-led diversification of the economy out of the MEC and jeopardizing its influence. With post-apartheid liberalisation, internacionalisation and financialisation of the economy, the state remained incapable of coercing and directing domestic industrial investment and diversification at the expense of the new interest of conglomerates to export their resources. Indeed, the new political rhetoric, focused on infra-structure and energy investment, would be mainly to answer the MEC needs. The South African state would be thus unable to have the necessary autonomy from the core sector interests of its economy (Marais, 2011).

It is surprising, however, how the new role of the rising financial sector is commonly neglected in the developmental sate debate both in the official statements and political economy accounts. Approaching finance should be here of paramount importance, given how public policy has been constrained and directed by the importance of capital inflows and outflows as well as the fact that finance is the biggest growing sector of the South African economy and pivotal in the allocation of capital in the economy.

3.2.3. South Africa in the international economy: the role of capital flows

Rising international capital flows have been taken as a popular indicator to assess financialisation in middle-income countries. South Africa confirms the general trend of rising international capital flows, identified for other countries (for Brazil and South Korea, see Painceira, 2011), and has gained an international strategic relevance since it accounts for more than 50% of all capital flows coming to sub-Saharan Africa (World Bank, 2006). The role of rising net capital flows in the second half of the 2000s seems thus of paramount importance to explain the growth surge of the period.

With the end of apartheid in 1994 (and the international economic isolation of the latter decade) and the adoption of the GEAR, the liberalisation of capital flows was understood as an instrument to promote the deepening of financial markets and thus foster foreign direct investment into the South African economy. Indeed, capital inflows skyrocketed with the end of apartheid (Figure 3.6). According to the SARB statistics, capital movement changes in South African liabilities (inflows) went from 2.14% in 1994 to 10.29% of GDP in 1999 (Figure 3.6), benefiting from the large liquidity that characterized international financial markets at the time and the perception of South Africa as an emerging country safe haven in the awake of the Asian financial crisis (Mohamed, 2006).Foreign Direct Investment (FDI)[26] remained however much smaller with its record in 1994 accounting for 3.14% of GDP. Finally, other investment – which accounts mainly for foreign loans – played a considerably minor role during the 1990s.



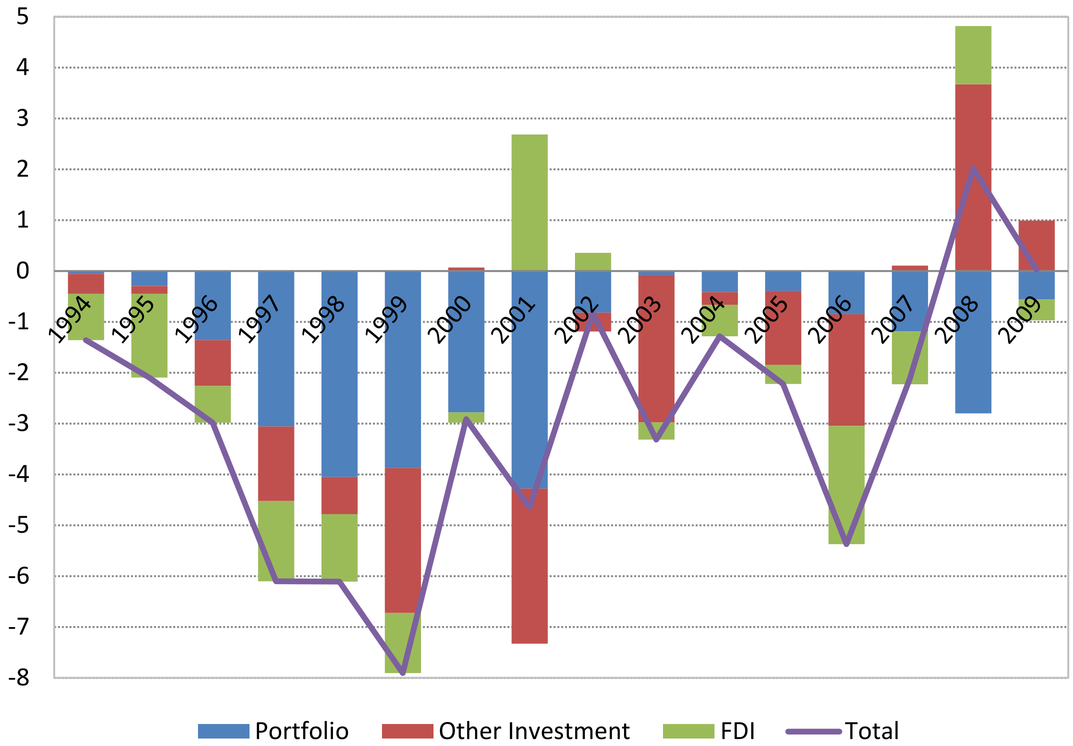
Source: SARB

Figure 3.6.Capital Movements: Change in Liabilities (% of GDP).

This capital flood was however made in the form of mainly short-term Portfolio investment –through the acquisition of equity and domestic bonds. These financial

[26] It should be noted that any acquisition over 10 % of equity of voting rights in a firm is accounted as FDI (IMF, 1993). FDI should not therefore be taken as necessarily involving accrued productive capacity. Furthermore with the listing of South African companies in other countries, FDI may be in fact investment from originally South African companies now accounted as being foreign (Mohamed, 2006).

investments did not have the expected consequences that the GEAR framework had laid down (FDI as 4% of GDP) and it was considerably mitigated by South African capital outflows in the same period (Figure 3.7).

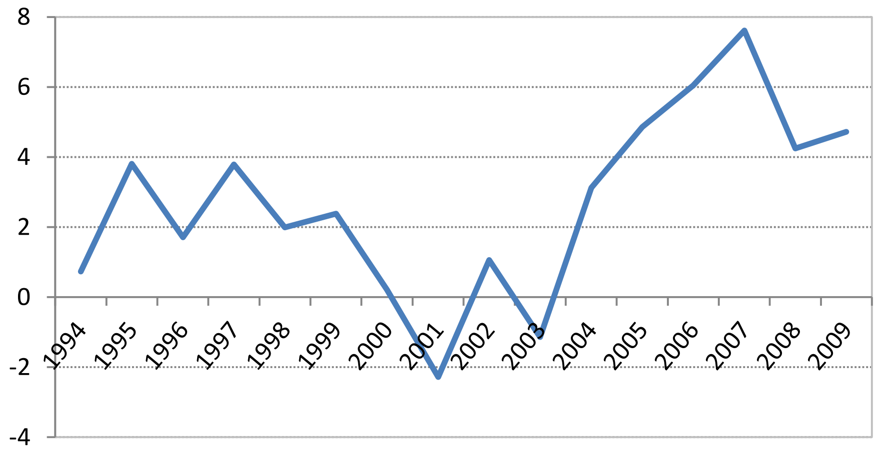


Source: SARB

Figure 3.7.Capital Movements: Change in Assets (% of GDP).

South African corporations started to access international trade and financial markets and expanded their operations worldwide instead of investing in the domestic economy. The net result was, thus, not enough to ensure a rise in domestic real investment and relax the foreign exchange constraints of the South African economy put forward in the GEAR strategy. The total capital flows were under 4% of GDP during the nineties and became negative for the years 2001 and 2003 (Figure 3.8). Moreover, the dependency from short term capital inflows resulted in higher volatility in periods of financial stress, notably during the 2001 currency crisis when rand depreciation was not met with the same interest rate hike seen in the previous currency crisis of 1998. This trend of rising inflows and outflows of capital with paltry net results was reversed during the later years of the 2000s that preceded the international financial crisis. With international abundance of liquidity in financial markets and the good performance of South African exports due to rising commodity prices, the new record heights of capital inflows (11.4 % of GDP in 2006, Figure

3.8) had more nuance equivalence in capital outflows - mainly driven by foreign short-term loans by the banking and long-term loans by the non-banking private sectors (SARB, 2007b). However, the composition of these inflows changed little (Figures 3.6), continuing to be largely short-term flows that tried to profit from the boom in stock market, relatively high interest rates when compared to the rest of the world, and currency stability. The volatility of portfolio investment was to be again confirmed with the international financial crisis in 2007-08 with foreign Portfolio investment inflows to become negative (-3.6% of GDP) in 2008 – leading to a sharp net outflow, with 67 billion rand of foreign funds being withdrawn from the Johannesburg Stock Exchange (leading to 12% drop in FTSE/JSE Index) and a depreciation of the rand of almost 20% (Harris, 2009) - and the banking sector to increase foreign-currency denominated short-term loans (categorised in Other Investment: SARB, 2009b).



Source: SARB

Figure 3.8 Net capital flows (% GDP).

3.2.3.1. Capital flows absorption

The absorption of these financial inflows was mostly made through the private non-banking sector, particularly in the cases of portfolio investment (Figure 3.9) and FDI (Figure 3.10), both highly influenced by the restructuring of the South African conglomerates and foreign purchases of existing South African companies[27]. Other investments (Figure 3.11)

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[27]For example, the impressive FDI seen in 2001 of 5.7 % of GDP is largely the result of buy-out of minority shareholders in the De Beers mining company as part of the corporate restructuring (SARB,

are more evenly divided with the banking sector to profit from short-term loans from foreign lenders.

Mohamed (2006) argues that these influxes of foreign capital had scarce impacts on real investment but had a positive effect on household consumption through increased availability of private credit and associated downward pressure on real interest rates. This consumption level would have sustained its aggregated high levels, that the South African economy had been experiencing since the early nineties (above 60% of GDP), but at the expense of a low savings rate and high indebtedness. Such trend was however to be partially reversed in the years 2005-08. With high commodity prices and high(er) interest rates as "pull" factors and low(er) interest rates in the advanced economies, South Africa showed a new economic dynamism in face of these capital flows. It is true that credit extension continued to grow, particularly for households - causing a housing price boom and a rise imports that ultimately resulted in a current account deficit- , but during this period investment rose above 20% of GDP. The result was thus the record economic growth of the period.

However, it was within the domestic financial sector that this surge of net inflows represented its biggest success. Whilst the liberalisation and deregulation movement started in the early eighties, it was the rising capital inflows that provided the momentum for converting the financial system into the most dynamic sector of the South African economy, with strong capital markets, large internationalised banks and big insurance companies (Hawkings, 2004). Its weight in the economy has evolved along the same lines as in the countries at the forefront of the financialisation process – 21.4 % of GDP in 2009, from 15.3 % in 1994 (computed from SARB statistics), is today accounted for the financial services sector in South Africa, making it the economic sector with the highest growth. The Johannesburg stock market exchange - capitalisation of over 200% of GDP in 2010 (IMF, 2011) - has been buoyant with its main index going from around 8000 points in 2000 to 25 000 in 2010, with a small decline in 2007 and 2008 (SARB, 2005b and 2010b). Resources and industrial sectors are the bulk of market. Eight of the top 20 listed companies[28] by

2002b). The rise in 2005 and 2008 of FDI is mainly due to the acquisition of ABSA by Barclays Bank and of Standard bank by the Chinese IDDC.

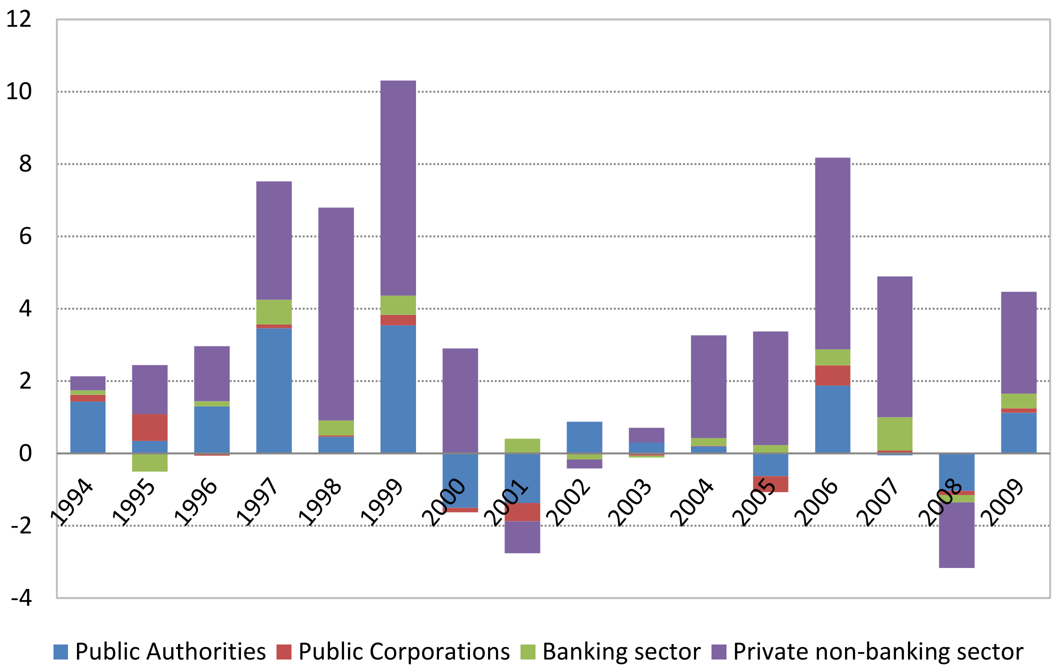
[28] Retrieved from the Johannesburg Stock Exchange website (http://www.jse.co.za/Home.aspx)

market capitalization were mining companies, with the financial sector (insurance and banking) coming in second with five companies), showing their increasing relevance.

Albeit coming in second as direct recipients of foreign capital flows, it is the banking sector that has mostly benefited within the financial sector. These flows have taken the form of rising short-term loans (Other investment in Figure 3.11) during the2004-2007 period thanks to financial and rand stability and relative high interest rates that allowed for South Africa to be one of the most popular recipient of the international carry trade – where international financial agents fund themselves in "low interest currencies" such as the yen and lend to countries with high real interest rates such as South Africa (Gallati et al, 2007). Moreover, the South African banking sector has benefited from fresh inflows of equity capital – accounted as FDI (Figure 3.10) – into two of South Africa's biggest banks (ABSA in 2005 and Standard Bank in 2007). Such scale of such direct inflows explains, however only partially, the intense growing of this sector in the past fifteen years, with total assets increasing from around 60% of GDP in 1994 to over 120 % of GDP in 2008 (see chapter 6).

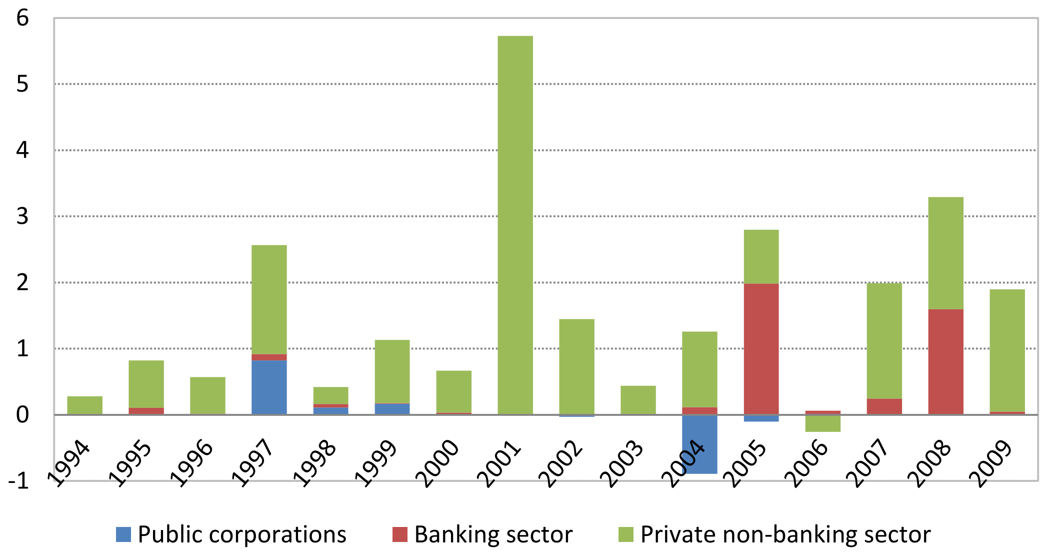
Other financial institutions, as long-term life insurers [29] have remained stable, if not declining, during the whole post-apartheid era with their assets to stay around 70% of GDP. Private and self-administered funds show the same stability - having 21.1% of GDP in 1994 to 24.2% in 2009 – with "Official and provident funds" to have more robust performance growing from 22.5% in 1994 to 37.55%in 2009 (computed from SARB statistics). The surprising stability of these institutions may be explained by the rising importance of new alternative unit (mutual) trusts - in their different forms (money market funds, bonds, and equity) with their assets growing from only 5% of GDP in 1994 to 31% in 2009 –as an recipient of savings from households trusts and by the declining rate of household savings during the past fifteen years.

[29]Long term insurance is highly concentrated within five major companies born from the South African conglomerates (Liberty group, Metropolitan, Momentum group, Old Mutual and Salam) accounting for 68% of total premium income (Hawkings, 2004).



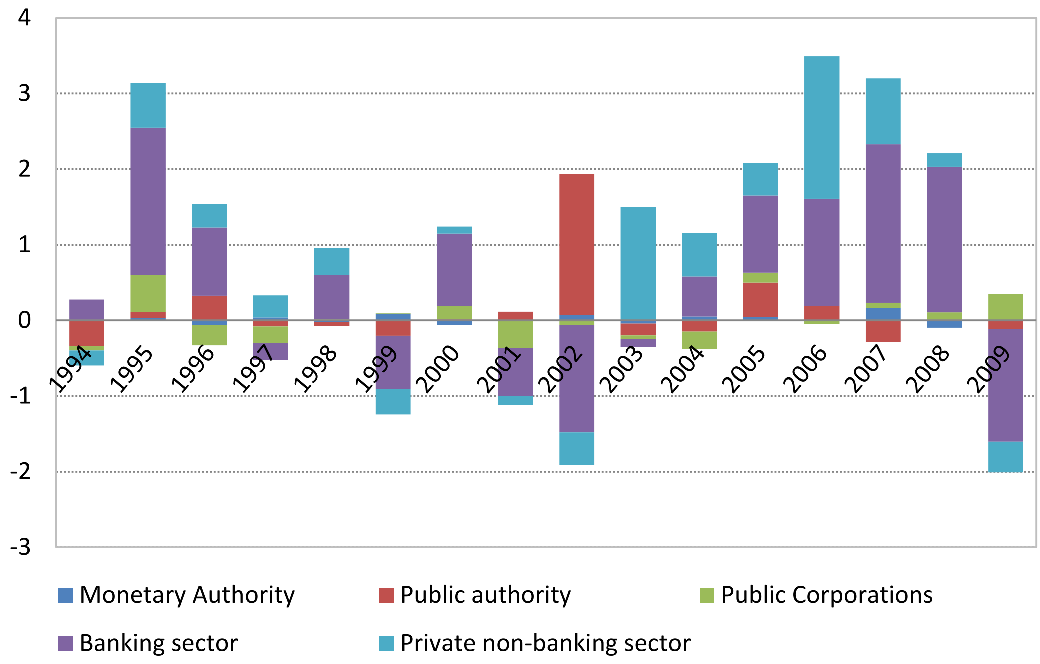
Source: SARB

Figure 3.9.Portfolio inflows by sector (% of GDP).



Source: SARB

Figure 3.10.FDI by sector (%of GDP).

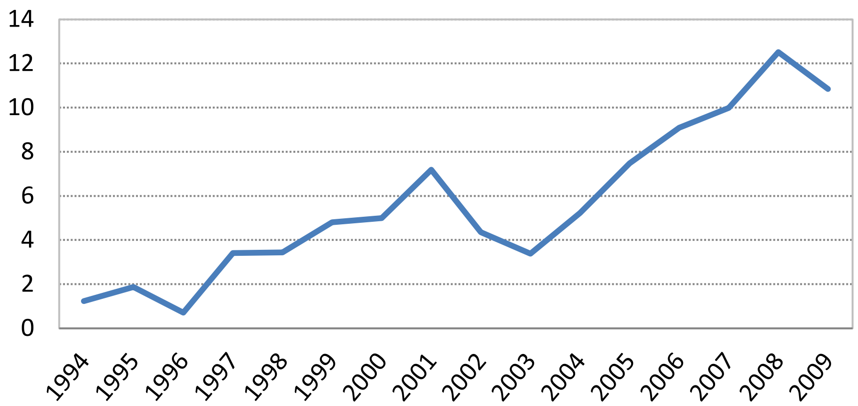


Source: SARB

Figure 3.11.Other investment inflows by sector (% of GDP).

3.2.3.2 The specific case of South Africa as a middle-income country

The case of South Africa in relation to capital flows and the accumulation of foreign reserves is not the same as Painceira (2009) identifies for other emerging/developing countries. It is true that the increasing capital flows have been accompanied by exponential growth of foreign reserves, mainly held by the South African Reserve Bank – from 2% of GDP in 1994 to 12% in 2008 (Figure 3.12). Yet, the source for these reserves lies exclusively in the net private capital inflows and not in current account surpluses. In fact, the external deficit has been rising steadily during the 2000s, with the exception of the period 2008-2010 due to the international crisis. The difference may arise from the non-sterilization of these inflows through rising public debt as credit-based consumption has been growing contrarily to what Painceira (2011) identifies for countries such as South Korea and Brazil, until the international crisis of 2008-2010 when the public deficit had to rise in order to tackle the international recession effects. Sterilization actions of increasing government deposits in the Reserve Bank and the issuance of securities by the SARB during some periods were only partially successful in containing the money supply (M3) growth of these years, which averaged 21.5 % between2005 and 2008 (SARB, 2007b).



Source: SARB

Figure 3.12 Foreign exchange reserves (% of GDP).

Economic isolation and exchange restrictions during the eighties had forced South African MEC conglomerates to expand their domestic holdings to disinvested subsidiaries and the financial sector (Fine et al, 2011). Following the trade and capital liberalisation, South African capital groups created separate companies in order to unbundle their operations, focusing on their core activities and selling other assets (Chabane et al, 2006). A process followed by the foreign listing of major companies and the rise of new firms in non-tradable sectors such as telecommunications, retail and finance and a boom of mergers and acquisitions (M&A). Foreign capital inflows, either strategic or not, were thus instrumental in this reorganization of South African capitalism, allowing a refocus of conglomerates on their core areas of the mineral-energy complex. Such inflow and outflow of capital went well into the 2000s.

Finally, the limited effect of foreign capital flows on South African growth cannot be dissociated from the endemic problem of both legal and illegal capital flight. Such phenomenon has been growing since the end of apartheid. Recent calculations by Fine et al (2011b) put unrecorded capital flows, mainly through illegal miss-invoicing in the ores and metal sectors, at a record over 20% of GDP for 2007, with an average of 12 %of GDP between 2001 and 2007, which compares to an average of 5.4%for the period between 1980-1993. The motivations behind these movements are multiple, ranging from concerns on the political stability of a country to tax evasion. Such increasing capital movements were enabled by the internationalization of the South African economy and its financialisation, namely the liberalization of capital flows. This has clear negative effects on the whole of the economy through its direct impact on the balance of payments and the availability of capital for domestic investment. It crystallizes the uneven and combined development of the country within the world economy, granting a permanent flux of income from a developing country to the more developed havens capital finds in the countries who import from that country and where its major companies are now listed. South African authorities have attempted to minimize the problem through its legalisation both through an amnesty for prior illegal expatriation of capital (imposing a flat fee of 10 % but allowing to keep assets abroad) and a foreseeable complete liberalisation of exchange controls in the "New growth path" public strategy (Fine et al, 2011b), allowing assets to leave the country without any taxation.

4. Financialisation of the corporate sector in South Africa

4.1. Introduction

Research on financialisation has dealt, in its brief history, with the rising importance of the financial sector across the most developed countries and its impacts on the rest of the economy. Non-financial corporations' place in this new context has received some attention by financialisation scholars. Still, this sector is normally assumed to represent only industrial interests, detached from the growing autonomous financial sphere. Hence, research is either focused on the *ex-post* impacts of the finance imperatives in real investment (particularly in post-Keynesian analysis) or in the *ex-ante* accumulation problems in the productive sphere that would have forced an escape of capital to speculative finance. Alternatively, the financialisation approach of Lapavitsas (2009) and Lapavitsas and Powell (2013) sees non-financial corporations and finance as interacting with each other, placing its focus on the increasing ability of non-financial corporations to engage in financial transactions and to earn financial profit in a symbiotic relation between financial and industrial interests that reshapes the rest of the economy.

However, its focus rests in the most developed countries' corporations. Such financialisation hypothesis of the non-financial corporate sector needs to be assessed in different and geographical settings away from the core of developed countries, where corporations are embedded in specific historical paths and potentially more distant from the mature financial markets seen in developed countries. Middle-income countries serve this purpose because they tend to have large homegrown corporations, exposed to increasing international competition, and benefit from modern liberalized financial systems. Market liberalization and international financial integration in these countries opened new avenues for large corporations to change their funding sources, diversify instruments and reduce capital costs. According to the World Bank (2007), from 2002 to 2006, 422 corporations from developing countries issued bonds in the international markets (348 for the first time), 537 resorted to international bank syndicated loans, raising $333 billion dollars in 2006 (upwards from $88 in 2002), and 394 were traded in the major international stock listings, amounting to 29.4% of all foreign companies listed, upwards from just 13.1% in 1998[30]. Such development of private capital flows leads the World Bank to conclude that “the growing profile of such companies, both public and private, in global investment and finance is a defining feature of the current cycle of capital flows to developing countries” (2007: 73). Nonetheless, these corporations have their own particular place in the international economy since they have been forced both to comply with standards of financial accounting and regulation defined in core countries as well as to endure higher interest rate spreads – highly correlated with their sovereign position – than their developed countries’ competitors. The fact that middle-income country corporations are subjected to an international insertion with a clear international hierarchical power structure should thus point to different varieties of corporate insertion within international financial markets.

South Africa, being a middle-income country, should provide evidence, or absence of it, for financialisation of middle-income countries’ corporate sector. South Africa’s historical large domestic industrial conglomerates are suitable examples of major corporations which, initially embedded in a particular setting, have restructured themselves and now operate in a global financialised arena which, in turn, also shapes their structure and behavior. Attention will be dedicated to how corporations funded themselves domestically since the end of the apartheid through flow of funds analysis. Such analysis will enable an examination of the changing interactions of this sector with the rest of the South African economy.

In this chapter, attention will be dedicated to financialisation within the non-financial corporate sector in South Africa, thus assuming both a geographical and sectoral approach that is mostly absent in the financialisation literature. In the first section, I start with a brief critical overview of the neoclassical approach to firms and the prolific literature on corporate finance. I then move on to how corporations are dealt within financialisation studies, laying out the theoretical framework that we aim to assess. The second section analyses the flow of funds of the South African corporate sector in order to identify the different sources and uses of funds and to test the hypothesis of financialisation in this sector. Such empirical assessment is to be contextualized in the third section with the

[30]From this pool of countries, the corporations of twenty middle-income countries account for almost the whole developing world corporations – 95% of bond and equity issuance and 85% of bank borrowing (World Bank, 2007).

recent historical evolution of the domestic and international roles of the large South African industrial conglomerates since the end of apartheid. The fourth and final section of this chapter closes it with the theoretical implications that can be extracted from this case-study.

4.2. From the theory of the firm to financialisation

The theoretical understanding of the firm in neoclassical economics has its origins in Ronald Coase's seminal paper *The Nature of the Firm* (1937). This author poses the question on why firms exist in a market economy. The author tries, in fact, to explain how the collective action of the firm can subsist in an economy coordinated by the market price system where transactions are voluntary. His answer lies in the high transaction costs that a pure market system would entail. The firm is thus an efficient alternative to the market, with its boundary to be determined by where the superior efficiency of its command mechanism surpasses the coordination of markets. The firm would be characterized by its command system where the "master must have the right to control the servant's work" (1937: 13). However, with the post-war dominance of the Arrow-Debreu (1954) general equilibrium, where the economy is based solely on perfect market behavior, the firm was dropped as an economics research topic. Corporations[31] would face few dilemmas in their funding choices in this theoretical framework. The Modigliani-Miller hypothesis (1958) stated that in complete markets different choices of funding (taken as the choice between debt instruments and equity issuances) would be irrelevant in their impact on the value of the corporation.

With the relaxation of some of the neoclassical assumptions (as perfect information and self-interested rational behaviour) arising from the theoretical information asymmetric paradigm and transaction cost literature, Coase's question on the nature of the firm reemerged during the 1970s and 1980s. First, in the work of Alchian and Demstez (1972), which sees the firm as the result of the necessary command structure needed in team work to solve the problem of incentive alignment[32] and then in the Transaction Cost literature

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[31]The distinction between firms and corporations normally falls in the latter's separation between ownership and management.

[32]Recognizing the advantage of team work, the incentive problem arises from the fact that "marginal products of cooperative team members are not so directly and separably (i.e. cheaply) observable" (1972: 780). Since the alignment of incentives and input contribution might be problematic, team

(Williamson, 1975), closely following Coase's perspective. Bounded rationality, uncertainty, privately held information, opportunistic behavior and asset specificity[33] are some of the reasons used in this literature to explain the rising of formal and informal institutions as means to overcome the impossibility of writing complete contracts put by these constraints (Teles et al, 2007). The costs incurred in market exchange may be so high that firms would take the place of markets. According to this approach, the funding choices of corporations may differ in face of different investment projects. Williamson (1988) argues that debt should be used in projects where the specificity of assets is low and, conversely, assets where the specificity is greater and their redeployability limited, increasing the need of monitoring, should be preferentially financed through equity.

Another theory, focused on property rights and sticking to the neoclassical theoretical assumptions core (Grossman and Hart, 1986; Hart and More, 1990), raised substantially different questions (and answers) about the firm. The Alchian and Demsetz "residual claimant" idea is here developed and the firm is defined as being composed of the assets that it owns or over which it has control. The ownership of assets by a single entity may be more efficient than separate ownership depending on the relative costs. The central focus of the theory is to study the optimal assignment of these assets. Workers would not be essentially different from independent contractors. The specificity of the employment relationship is that the employer purchases the residual rights of control over employees' *actions*. Theoretically, close to this approach, the influential agency theories of the firm (Jensen and Meckling, 1976; Gibbons, 1998) focus on the incomplete nature of labour contracts and the need to align incentives between workers and owners. These authors focus on the firm as a nexus of bilateral contracts "under which the *principal* hires the *agent* to perform services on his/her behalf and monitors him/her on a bilateral basis" (Teles et al, 2007:10). Assuming informational asymmetry problems and the self-interested and opportunistic behavior, incentives models must be put in place to ensure that different

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members have an incentive to shirk on their productive efforts. The owner of the resources would act as the monitor of team work, reclaiming the residual of the net earnings of team work, and thus not having any incentive to shirk his own efforts. This hierarchical structure would thus explain the existence of firms.

[33] A specific asset is assumed when its value depends on the continuation in time of a particular relationship. These assets would have a higher value if they were to be deployed in a different transaction setting.

parties in the contract do not shirk. There is here no authority or hierarchical structure. The firm is posited as only a peculiar configuration of market contracts.

It is based in this latter theoretical agency problem approach that we find the vast theoretical and empirical literature of corporate finance that is centred on the choices corporations face for their funding (Bolton and Scharfstein, 1998). The agency problems pointed above are here reconsidered through the lens of the distinction between insiders and outsiders of the corporation, replicating principal-agent incentives mismatch. The first (borrowers, managers or entrepreneurs, depending on the context) would benefit from better information on the corporation than the latter (investors or lenders), creating problems of moral hazard and adverse selection (Tirole, 2006). Corporate finance literature is thus interested in designing contracts that align incentives between the two in the corporation's financial options. Although this literature covers a vast number of topics – from the corporation's capital structure, to pay-out policies and corporate governance - and integrates many of the transformations of financial markets in their framework (e.g. theorizing importance of debt and capital markets), it rests largely in the microeconomic realm and presents a common theoretical background which preserves fundamental neoclassical assumptions such as profit maximization and rational behaviour[34], and with systemic transformations of capitalism and financial markets being integrated as exogenous to the theory. This methodological reductionist stance, and the associated mathematical modeling, implies a rather abstract approach to the corporation, populated by (more or less) rational agents whose actions are guided by clear behavioural patterns detached from the social, historical and political environment within which they operate, neglecting the overall economic in their analysis.

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[34]More recently, the new theoretical contributions of behavioural finance have been added to the corporate finance research. Behavioural finance goes beyond the assumption of rational behaviour and assumes irrational behaviour both from investors (outsiders) in the form of imperfect securities market arbitrage and, to a lesser extent, from managers (insiders) in the form of individual behavior biases, such as overconfidence (Baker et al, 2005). For a more complete discussion complete discussion on behavioural economics contributions and limits see Chapter 7.

4.2.1. Political economy

As was seen in Chapter 2 of this thesis, the focus on the way corporations work nowadays is quite different in the different political economy accounts reviewed in that chapter. Corporations' financial behaviour was here put in the context of the profound transformation of capitalism, with these theoretical approaches focus to be directed to the new demands corporations are now subjected to the financial sphere.

Financialisation within the corporate sector is usually perceived as the imposition of "impatient" financial market imperatives on firm behavior. Corporate financialisation is not studied as a process born endogenously from the opportunities and demands entailed by corporations' new role within the international economic sphere, but as their submission to rising financial power. The shortening of the time horizon for investment –taking the more profitable short-term financial speculation as a benchmark – and the promotion of corporate governance (influence by the corporate finance literature) are some of the effects identified within financialised corporations (Crotty, 2003). Such pressure from the financial markets is said to be responsible for a stagnated real accumulation of capital (Stockhammer, 2004; Palley, 2007; Organzhi, 2008).

In Marxist political economy accounts the focus is not on the abstract theoretical reasons for firms to exist, but on how they represent capital as an "expression of class society, in which one class is able to live off the labour of another class (…) through purely contractual economic basis" (Gosh, 2012: 29)[35]. Marxist political economy accounts place their stress on how production is organized in contemporary capitalism. Financialisation of non-financial corporations is generally understood as arising of a new international organization of production where transnational corporations have a new hegemonic role. Financial operations are here taken as part of the overall restructuring of production that promotes delocalization of production, enhancing new labour disciplinary mechanisms (Chesnais, 1997).

Serfati (1996, 2008) offers a Marxist account on the relation between corporations and finance, arguing how corporations have evolved into industrial-financial groups, where

[35]The capitalist factory system arises as not only a technological development but as a new form of organization of production where labour is subjected to capital and where exploitation (in the form of plus value extraction) takes place (Fine and Saad-Filho, 2008).

a set of companies is owned by a holding company that manages property rights and financial claims, based in transnationalisation of production. The new Transnational Corporations (TNCs), benefiting from the increasing fluxes of intra-firm international trade and Foreign Investment, would have the ability to extract financial profits from financial activities entailed by the transnationalisation of production:

"In their quest for more financial revenues accruing to their corporations, TNCs' managers developed an active management of their assets. They raised more fresh funds (equities and bonds) from financial markets, and less from credit banking." (2008:12)

These new opportunities in the financial sphere, albeit not new in the history of capitalism, would have gained new relevance in the last decades due to the centralization of capital that the transnationalisation of production allowed (George, 1998) and to the deregulation and innovation of financial markets. This theoretical stance is close to the one of Lapavitsas (2009) and Lapavitsas and Powell (2013) where financialised corporations are defined as firms with the ability to engage with financial markets resulting in a turn away from banking sector funding and the accumulation of financial assets. Financialisation is not confined to the mere growth of the financial sphere in developed economies. It is taken as a process resulting from the concomitant development of and interactions between both the non-financial sectors and the financial one instead of the result from the mere submission of industrial interests to financial demands. The financialised corporation emerges from the result of the capital accumulation dynamics, the new close relation with the financial markets and the growing power in relation to the rest of the economy (workers, states, etc.).

Additionally, financialisation should not be understood as an exclusive phenomenon of developed countries, but a global transformation subjected to, and embedded in, a new international monetary hierarchy, where the capitalist center's "structural power" (Konings, 2007) plays a pivotal role. Such force, albeit leading to an increasing integration of international production and of the financial sphere, is far from having homogenous results across the globe. It has asymmetrical impacts with corporations to take "variegated" configurations in particular contexts (Peck and Theodore, 2010) as they are both embedded in national, institutional and historical frameworks and subjected to specific international constraints. Corporate financialisation should therefore be studied outside of the capitalist center, as it is the case for South African major corporations, if one aims to have a more comprehensive understanding of this phenomenon.

4.3. South African corporate sector (FoF analysis)

Following the given definition of financialisation in the corporate sector (Lapavitsas, 2009; Lapavitsas and Powell, 2013), three hypotheses are here adopted in order to recognise a financialised corporate sector in South Africa: 1) increasing engagement of the corporate sector with debt and capital markets; 2) turn away from banking finance; 3) accumulation of financial assets.

Given the financial nature of such assumptions, flow of funds provide a good measure of the evolution of flows from the sector of non-financial corporations to other sectors, namely the financial ones and their content. In the case of the first hypotheses, it can be tested through the evolution of net flows from and to equities and debt securities, as categories aggregated of different flow of funds items (see Chapter 3). Such securities, when used a flow of funds "source", reflect the ability of corporations to fund themselves directly on stock and debt markets where they are bought by other economic sectors. Moreover, when taken as flow of funds "use", these securities reflect the level of financial investment of non-financial corporations and thus what was already mentioned as "active asset management" (Sefarti, 2008).

The identification of gross financial flows from and to securities enables the test of the third hypotheses: non-financial corporations as direct participants of financial markets both as sellers and buyers and thus financialised in the broader sense of the literature of financialised corporations as relevant direct participants in financial markets. The corporation is here not taken as an more efficient arrangement when compared to the market (as it is in neoclassical economics). It is here the primary lieu where production takes place in a capitalist society that reflects both power relations between capital and labour and between capital and the rest of the economy, namely its financial sector. The corporations' funding choices are to be confronted with the more "traditional" channel of funding, namely through banks (Flow of funds categories of bank loans and mortages minus monetary deposits), thereby reaching the relative importance of different funding choices and the second hypotheses of rising market funding relative to banks. The financialised corporation in the narrower sense present in the Lapavitsas analysis can be thus assessed.

In this section, these hypotheses are explored through a flow of funds analysis of the non-financial private sector during the post-apartheid period. Assumption 1) is tested by the examination of the evolution of equities and debt securities, both as net and gross funding sources, of the private non-financial sector; assumption 2) can be tested from the evolution of total banking funding sourced by the private non-financial sector; finally, assumption 3) is tested from the evolution of total financial assets relative to total uses of funds (total flows into assets).

Two empirical approaches are here deployed: an analysis of net categories of flow of funds and a breakdown examination of gross flow of funds (liabilities and assets). The first follows the method by Corbet and Jenkinson (1997) through which net categories (sources minus uses) of total flow of funds are put together allowing the measurement of the net finance sources of corporations. The second approach looks at gross values of liability and asset flows in order to have more comprehensive information on the major funding sources: equities, debt securities, and banking credit. Such approach is complementary to the first one as it results in data on the extent of gross involvement of non-financial corporations with different financial instruments and enables the measurement for the weight of gross financial asset accumulation compared to total assets.

4.3.1.1. Results

The values of the net categories in million rand are presented in Table 4.3, deflated at 1994 prices using the GDP Deflator provided by the World Bank for South Africa[36]. Two findings are discernible: 1- there is a steady decline of real internal sources throughout the period; 2- there is a continuing increase in the total net sources of funding. Other items fluctuate sharply from one year to the next, thus making it difficult to assess any trend. In order to get a more accurate picture, the average relative weight of each category is presented in Table 4.2 for the total period considered (1994-2008) as well as for three five year periods covering the total period considered (1994-98; 1999-2003; 2004-08), in order to facilitate the identification of the evolution of each category.

Table 4.1. Net Finance Sources Averages (%)

	(1994-2008)	1994-1998	1999-2003	2004-2008
Internal (gross savings)	76.3	99.7	86.7	42.4
Net Bank Credit	14.3	1.6	-1.1	42.3
Net Equity	44.8	64.6	49.9	20.0
Net Debt Securities	20.5	1.8	25.9	33.7
Net Trade credit and short term loans	-8.2	-28.0	1.1	2.2

[36] http://data.worldbank.org/country/south-africa

Long Term Loans	3.0	-6.0	-3.1	17.9
Other deposits	-0.8	0.1	12.9	-15.3
Net amounts payable/receivable	-0.4	4.0	-6.0	0.7
Net other assets/liabilities	-49.4	-37.8	-66.4	-44.0
Total	100	100	100	100

Internal resources are found to be the main finance source for the private corporate sector, with an average 76% off all net sources for the whole period. Nevertheless, the share of internal resources has been decreasing to a record low of 42% during the period between 2004 and 2008, confirming the "real" absolute decline reported above.

Table 4.2. Net finance (Mn rand, 1994 prices).

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Internal sources	48193.0	44301.4	41286.4	38049.3	36023.7	33755.5	32221.9	30748.6	28170.9	27138.7	27361.8	26055.1	25133.3	23688.6	22220.4
Net Bank credit	6099.0	-9020.9	4249.5	-2700.8	9310.1	7870.7	8312.9	5623.0	-19524.6	1494.1	9288.9	-3361.1	32398.3	29404.4	79331.4
Other deposits	-1138.0	3237.9	-2373.3	1543.0	-1149.0	1357.8	3983.5	5156.4	9675.4	1150.3	-8757.2	-31844.0	-6138.2	12095.2	3619.1
Net Long Term Loans	244.0	838.2	-1205.1	-5565.7	-10010.9	-2747.1	-3858.2	-1607.2	6261.7	-4727.0	10034.5	955.9	19378.4	20268.0	9700.1
Net Equity	28140.0	16036.0	29000.7	35133.8	24441.4	33483.8	9613.2	25603.5	84.6	22664.0	19003.5	28105.0	22686.0	-7668.2	-17879.6
Net Debt Securities	-11617.0	-763.7	-10247.5	9705.3	32688.2	7170.1	-646.5	7948.3	26245.9	1137.7	11661.4	17422.7	32619.6	42136.7	8524.8
Net Trade credit and short term loans	-13098.0	572.3	-16378.3	-17616.6	-8824.3	-12702.3	-11898.5	-12519.0	-5370.3	36346.4	28001.0	6105.6	-21437.3	-28589.4	-2065.9
Net Amounts Payable/ receivable	2304.0	934.9	1564.2	543.8	4762.1	-14333.9	5451.1	-12109.1	5982.5	813.5	3459.5	26449.1	-5368.0	-6404.4	-29704.5
Net other sources/ uses	-6477.0	-16761.1	-17219.9	-22518.6	-9776.1	-10952.1	-5218.5	-12949.6	-21973.1	-55561.7	-56263.8	-21409.6	-31623.5	8214.5	-6314.5
Total Sources	52650.0	39375.1	28676.7	36573.4	77465.2	42902.6	37960.9	35894.9	29553.0	30456.0	43789.8	48478.6	67648.6	93145.4	67431.2

Source: Computed from SARB, National Financial Account

The engagement with equity markets is considerable, with equity being an important net source of finance for the whole period (45%). Yet, if equities are a considerable finance source for the period between 1994 and 1998 (64%), they decline in importance to 20% in 2004-08. Such decline as a net finance source should not be taken as reflecting a failing stock market. The decreasing importance of equities as a net finance source should take into account the nature of a net category that disguises the absolute involvement of corporations in the equity market as both issuers and sellers.

Debt securities seem a considerable net funding source for corporations with an average of 20.5% of all net sources. Moreover, its importance has grown from residual net impact (1.5%) in 1994-98 to 33% in 2004-2008. This net increase shown by flow of funds analysis should take into account the retreat made by the private non-financial corporate sector from public securities - a major use of funds during the nineties, demonstrated by their negative balance in several years during that decade – and the rise of securities as "loan stock and preference shares". In what concerns bond markets - where the latter category lays - although evidence is found for their importance in corporate funding, they are rather small in South Africa, even by standards of middle-income countries[37].

Although still dominated by public debt, debt markets have been growing for the past decade, particularly in private corporate and financial institutions' bonds. Corporate issuance in South Africa rose from 5,215 to 21,621 million dollars (Figure 4.1). With the macroeconomic stabilization of the 1990s, the consequent decrease in public debt issuances and drop of interest rates (making fixed interest securities more attractive *vis-à-vis* equities), corporations took advantage of their prior relatively underleveraged profile (Rand Merchant Bank, 2001) and increased their debt securities liabilities. However, still high interest rates[38] may explain the parsimony in resorting to such instruments.

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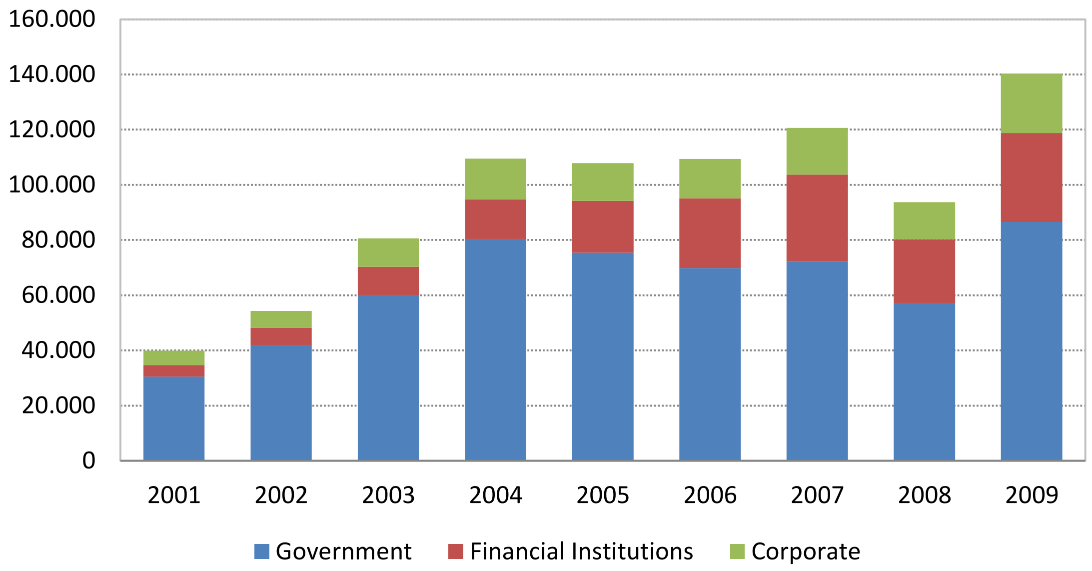
[37] Countries as Thailand, Mexico or Turkey all have larger private debt markets than South Africa (Bank of International Settlements, Quarterly Review, 2010).

[38] For 2006-07, spreads for the South African corporate bonds (including financial institutions) were higher than 400 basis points (only second to Argentina, among middle income countries). Such cost is particularly odd when compared with the low spreads for public debt (less than 100 basis points) (World Bank, 2007).



Source: Bank of International Settlements

Figure 4.1. Debt Bond Issuances (by sector) (Mn US dollars)

Contrary to what might be expected, credit from traditional channels, such as bank credit, continues to have considerable weight as an external net funding source with an average of 14.2% for the whole period. This impact is almost exclusively accounted by the 2004-08 period when it reached an average of 42%. Data for foreign capital raised by developing-country corporations from the World Bank (2007) corroborates this trend, which, although encompassing also financial institutions, shows that more than half of the foreign capital raised in these countries comes from syndicated bank loans, a less demanding funding alternative compared to debt securities.

The transaction items that lie outside our main focus are less relevant as sources of net finance to the private non-financial sector. Their behavior during the considered fifteen years is far from being consistent in their relative net importance for corporations. Trade credit and short term loans were a relevant negative item during the nineties (-28%), but reverted their negative weight to a positive one, even if they remained small for the remaining period (1.1% for 1998-2004 and 2.2% for 2004-2008).

Loans (long term) and deposits with other financial institutions (insurers, life funds, unit trusts) and the foreign sector, have behaved in a seemingly symmetric manner during 1998-2008. The former has gone from a negative net source of finance to positive (from -6% in 94-98 to 12.7% in 2004-08). The latter shows an opposite trend (from 12.9% in 99-03 to -15.3% in 2004-08), thus showing what seems an inversion from a creditor to a debtor position of the private non-financial sector. As a final note, the average weight of the remaining item of "other assets and liabilities" within net sources of finance is striking as a major, albeit negative, net use of funds (-49%). The importance of this transaction item is of difficult examination as it encompasses a number of very different liabilities and assets, like deferred taxes or interest gained from pension and life funds, thus calling for the more disaggregated perspective of the gross liability and asset analysis.

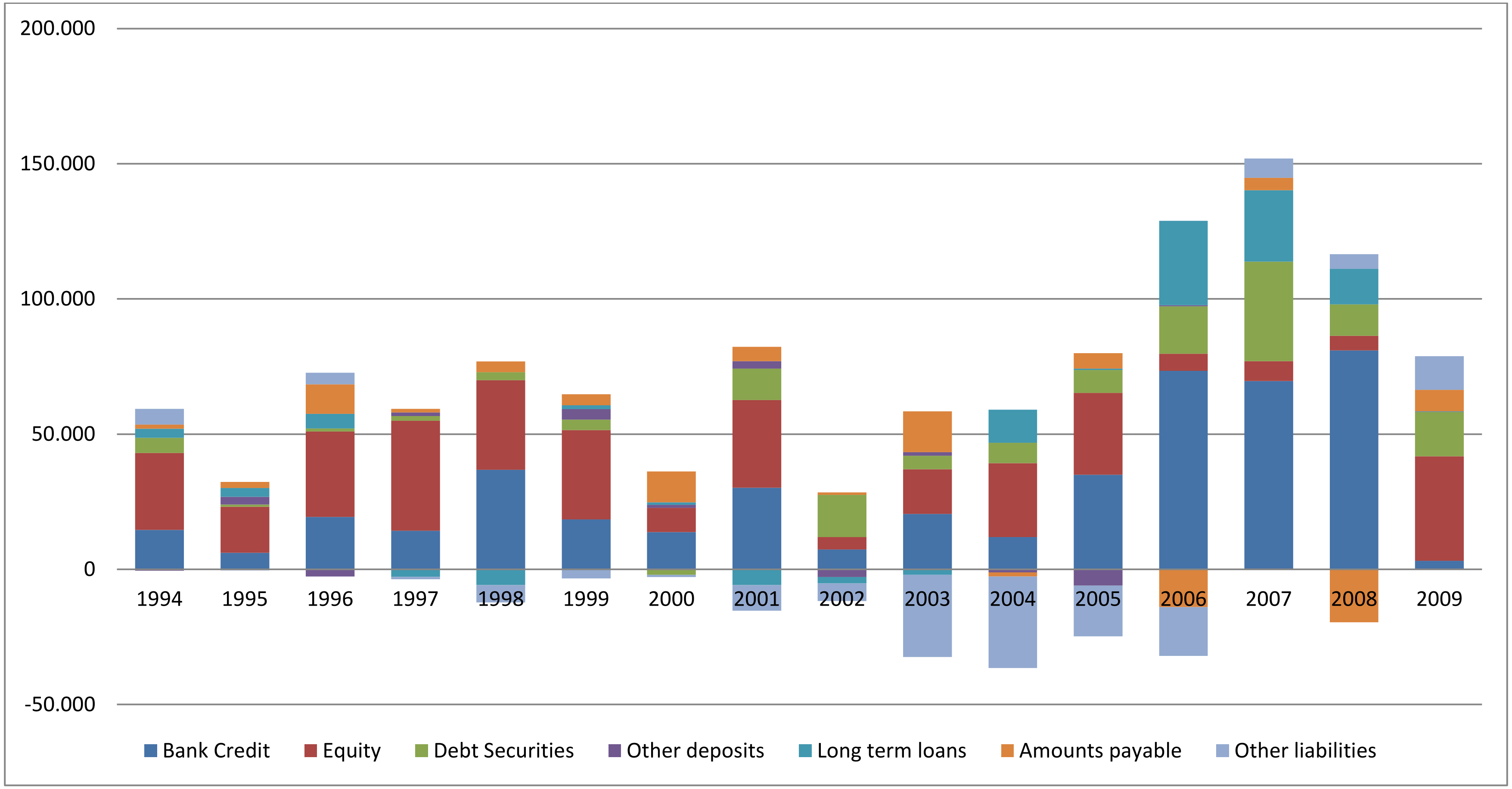
4.3.2. Gross liabilities and assets

Corbett and Jenkinson's net finance method is useful for understanding the net sources of finance used by corporations. Two problems, noted by the authors, arise however: 1- "it implicitly assumes that there is no economically significant difference between an enterprise which has, say, a bank loan of a certain amount offset by bank deposits of the same amount, and another enterprise which has neither (…)"; 2- "we are considering aggregate data, the role of, say, bank loans might be understated if some firms are net depositors and others are net borrowers" (Corbett and Jenkinson, 1997: 72). These two problems gain particular relevance for the research on financialisation of the South African corporate sector since we aim to evaluate the scale of engagement of firms with financial markets. A third difficulty should be added: given the aggregate nature of the method, there is here no distinction to account for different firm size. Yet, only large corporations can access money and capital markets, be it in a middle-income country or in a core one. The large corporations financialised profile may be thus underestimated through this approach.

Such complexity is to be addressed through the flow of funds gross decomposition and differentiated analysis of liabilities and assets. As mentioned, the relative net weights of funding sources may disguise the increase in firms' gross involvement with the financial sphere and with particular financial instruments. On the other hand, given the results presented above, the weight of some of the transaction items for South Africa, such as other assets and liabilities, have a magnifying effect on the importance of different funding sources. Below, the analysis distinguishes the gross liabilities and assets sides of corporate FoF allowing a differentiated assessment of funding sources and uses. The previously built categories are here again applied and all amounts are deflated to 1994 prices.

4.3.2.1. Gross liabilities

From the liabilities items (Figure 4.2), it is apparent that the use of funding instruments has been rising, particularly for the period between 2004-2007, coinciding with growing international liquidity and domestic financial expansion. The corporate sector's funding deficit was covered by an array of financial instruments whose choice and intensity seems to be related with the international economic cycle. The weight of other liabilities in total sources is considerably smaller than what would be indicated by the negative net weight of this item presented above.



Source: Computed from SARB, National Financial Account

Figure 4.2. Flow of funds gross liabilities (selected items) (Mn rand, 1994 prices).

There is a considerable and rising weight of gross bank credit as a funding source of South African corporations, confirming our previous assertion on the continuing importance of this sector for South African corporations. The ratio of all bank funding to all liabilities (internal sources not here considered) shows a permanent relevance of banks funding the private corporate sector throughout the post-apartheid period. It augmented its weight during the last decade, reaching 70% of all liabilities in 2006 and 2007, which coincide with the period of major liability growth.

Table 4.3. Ratios of selected items to total liabilities flows.

	1994	1995	1996	1997	1998	1999	2000	2001
Bank Funding	0.295	0.155	0.313	0.468	0.581	0.304	0.457	0.401
Equity funding	0.575	0.429	0.512	1.328	0.523	0.545	0.301	0.432
Debt securities	0.115	0.021	0.017	0.056	0.047	0.064	0.068	0.154

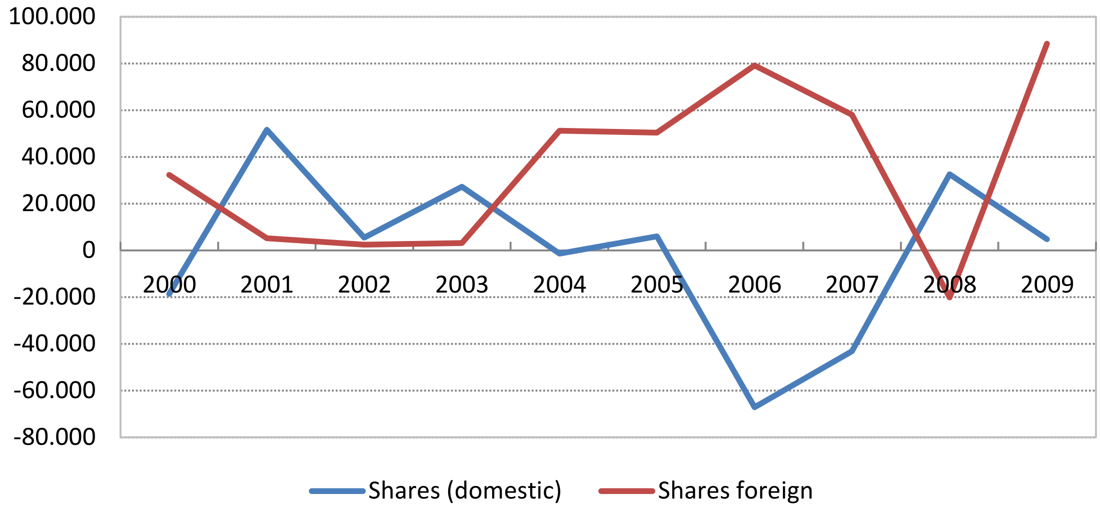
	2002	2003	2004	2005	2006	2007	2008	2009
Bank Funding	0.308	0.407	0.285	0.702	0.771	0.451	0.867	0.04
Equity funding	0.188	0.329	0.652	0.608	0.066	0.047	0.059	0.497
Debt securities	0.655	0.099	0.180	0.168	0.185	0.238	0.124	0.21

Source: Computed from SARB National Financial Account

The increasing relative importance of debt securities as a funding source is again confirmed, thus showing improved access of corporations to debt markets. Not only does the absolute amount of debt securities follow the liability growth of the period, but the ratio of debt securities to liabilities during the last decade also rises when compared to the 1990s.

The importance of equity as a funding source is again more complex to point out. If the issuance of equity was a considerable source of funding during the 1990s and 2000s, peaking at 65% of all liabilities in 2004, the most recent years have however witnessed a decrease in their importance in the flow of funds in both absolute and relative terms: the ratio of equity issuances to liabilities dropped below 10% in the second half of the decade, albeit experiencing again an increase with the international crisis in 2009.

This seemingly contradictory result can be explained by drawing on data from the flow of funds itself. Through the notes published by the SARB for each year, one can distinguish between the shares issued to foreign and domestic sectors (Figure 4.3). The years from 2004 to 2007 are portrayed as years of strong issue of shares for the foreign sector markets and buy-backs in the domestic one, in what might be a strategy to increase the value of their stock and become more attractive to foreign investment. The increasing involvement of corporations with equity markets is thus discernible, even if that translates to small issuances of equity as net funding.



Source: SARB, National Financial Account

Figure 4.3. Issued Shares (Mn rand, current prices)

The financial assets flows (Figure 4.4) of the corporate sector do not provide a complete symmetric perspective. As it is the case with liabilities, firms invest their excess funds in a wide range of financial instruments. However, even if corporations accumulated financial assets particularly for the years 2006, 2007 and 2009, contrary to what might be expected there is no significant growth in financial assets relative to total assets (Table 4.5) throughout the period between 1994 and 2009. There is thus no sustained matching of financial liabilities and assets growth.

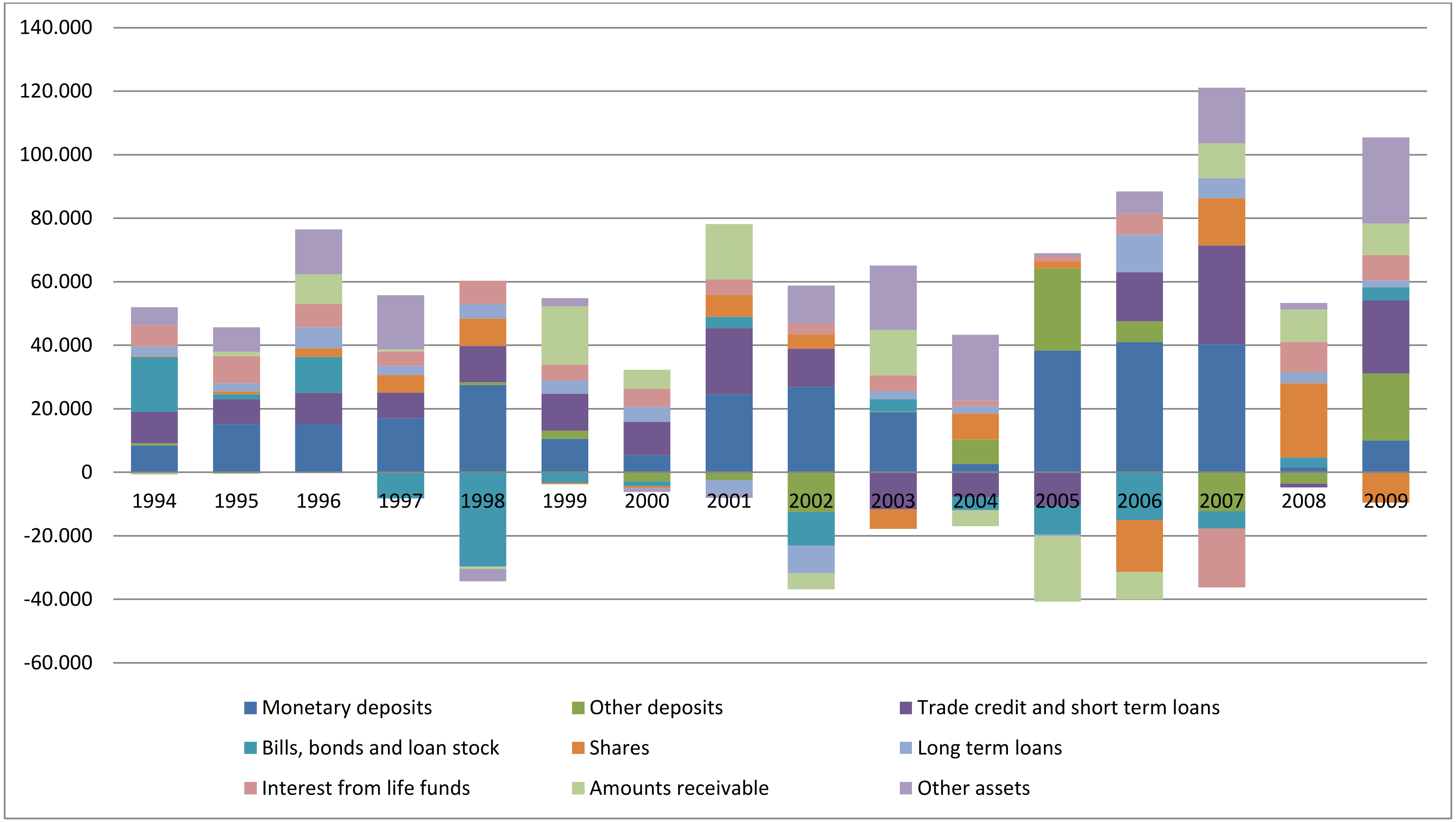


Figure 4.4. FoF Gross Assets (Selected items, Mn rand, 1994 prices).

Source: Computed from SARB, National Financial Account

Corporations still rely heavily on bank deposits for their excess funds[39]. The ratio of banking deposits to total uses reaches a record high in 2005 (41%) and abruptly drops in 2008 (1.1%) and 2009 (5.4%) with the beginning of the international financial crisis. Equity in other corporations and debt securities both have little weight relative to the total uses made. Debt securities exhibit a negative impact in most of these years, which seems to be mainly related to the selling of public debt securities. Securities are thus mainly used as funding instrument and not as a financial investment.

Table 4.4. Ratios of selected items to total assets flows.

	1994	1995	1996	1997	1998	1999	2000	2001
Financial Assets	0.565	0.437	0.560	0.430	0.579	0.491	0.304	0.553
Banking deposits	0.085	0.152	0.112	0.163	0.370	0.108	0.067	0.189
Securities	0.174	0.016	0.084	-0.077	-0.400	-0.034	-0.017	0.028
Shares	0.003	0.009	0.020	0.053	0.117	-0.005	-0.007	0.053

	2002	2003	2004	2005	2006	2007	2008	2009
Financial Assets	0.301	0.417	0.239	0.247	0.317	0.420	0.301	0.544
Banking deposits	0.289	0.183	0.026	0.406	0.449	0.272	0.011	0.054
Securities	-0.114	0.037	-0.040	-0.096	-0.164	-0.036	0.022	0.022
Shares	0.048	-0.059	0.081	0.023	-0.180	0.101	0.164	-0.052

4.3.3. Discussion

Drawing on these two complementary approaches to the FoF of the South African non-financial private sector, we are now in a position to assess whether this sector complies with our initial assumptions. Hypothesis 1), of an increasing involvement with the financial markets, is confirmed. Debt securities play an increasing role as both a net and gross source of finance for corporations, while equity consistently plays an important role in the dealings of corporations both as a funding source and a financial use. The net finance role of the latter has nevertheless been declining throughout the last fifteen years, meaning that the access to capital markets has not increased funding capacity of corporations. Hypothesis 2), which refers to the turn away from banking finance, is not confirmed. The role of banks as both a net finance source and as recipient has not declined. On the

[39]According to the SARB (2008), 42.5 % of all bank deposits came from non-financial corporations in 2007.

contrary, there is an increasing dependence on banking finance. It thus seems that, for South African companies, the access to direct capital and debt markets has not produced any kind of “crowding-out” of banking finance. Hypothesis 3), of increasing accumulation of financial assets, is of difficult assessment. The analysis of the gross flow of funds shows an increasing ability of corporations to manage their financial assets, measured by the growing of their financial assets absolute value, but there is no growth of financial assets accumulation for the whole period. Yet, a strong increase during the second half of the last decade may be indicative of an emerging trend within the non-financial sector.

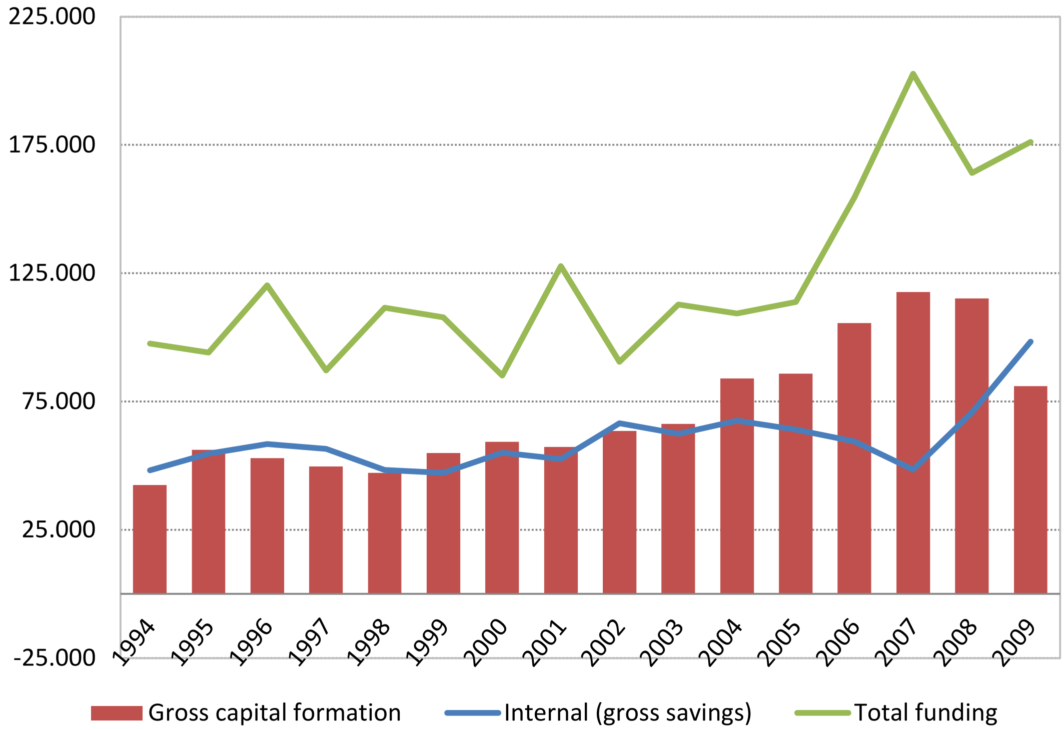
The analysis of flow of funds into the financialisation of the South African corporate sector, as previously defined, shows thus mixed results. It seems clear that financial markets play a new and increasing role in the daily life of this sector, albeit the aggregation of Small and Medium Enterprises and large corporations that this approach implies. Nonetheless, the hybridization of originally non-financial corporations to a more financial outlook, where financial assets play a pivotal role of investment, was not found. The relation between the involvement of the non-financial corporate sector with financial markets and the real investment sheds some more light on these mixed results.

Again using the flow of funds data, figure 4.5 shows the investment behavior of corporations compared with the gross sources (internal and external) of funding. There is investment growth during the past decade until 2009, when the effects of the international financial crisis become clear. Moreover, it is discernible that this investment surge was mainly funded by external sources of finance.

Investment growth in the economy is clear during the past ten years, growing from 15% of GDP to 23% in 2008. Such growth was generally uniform across different sectors of activity with the biggest increases in FIRE (Financial, insurance and real estate) and mining and quarrying (see Chapter 3).Traditional capital-intensive sectors - refineries, chemicals, basic iron and steel, basic non-ferrous metals and motor vehicle industry - continue to be the major recipients of such investment boost (Roberts, 2007). Still, one should not overestimate this surge. The weight of investment in South African GDP is small, particularly for a middle-income country rich in commodities[40]. Relative to GDP, investment

[40]According to World Bank (2011) South Africa’s real returns to capital have risen to an average rate of 15 % between 1994 and 2008, owing to falling inflation and interest rates.

is under the OECD average and it is strikingly low when compared to other high investment middle-income countries (China, India, Russia) (World Bank, 2011)[41].



Source: SARB, National Financial Account

Figure 4.5. Investment, Internal resources and Total net funding (Mn rand, current prices).

If the corporate sector has been accumulating both physical and financial assets, benefiting from the access to financial liabilities reported above, the conventional notion of financialisation, as inducing the stagnation of real investment, should be taken with reservation in the case of South Africa. Since the financialised profile is not here completely confirmed, the relation between finance and investment has to be dealt with prudence. The growth of both financial liabilities and assets during the 2005-2007 period comes mostly from the banking sector. Given that such growth coincides with the investment surge, it may indicate the importance of the latter to fund real investment.

[41] The mediocre level of investment can be traced decades back as a consequence of the abrupt decrease of investment as a share of GDP during the eighties, when public intervention was pulled back from its post-war activist behavior. A public decline not matched by the private sector, whose investment has remained poor since the sixties (Roberts, 2004).

Finally, given the domestic focus of the flow of funds, the role of the foreign sector in financing the corporate sector is not completely discernible from the data. The flow of funds SARB notes have nonetheless compiled the net inter-sectoral flows from 2004 to 2009, providing data on the net flows from the foreign sector to the private non-financial sector.

Table 4.5. Foreign sector flows to non-financial sector Bn rand.

2004	2005	2006	2007	2008	2009
87	78	191	120	68	63

Source: (Zhello and Meyerl, various years)

The foreign sector is a net and continuous provider of funding to the corporate sector, particularly as an equity buyer, as it was shown on table 4.6. This is compatible with the data showing that most international capital inflows to the South African economy are portfolio inflows rather than foreign direct investment absorbed by (see Chapter 3). These foreign flows indicate a changing property structure of large corporations, with foreign holders gaining an increasing share. If the involvement of foreign agents is clear, the role of the foreign sector as a net provider of funds to the South African economy should nevertheless be taken with caution. Fine, Ashman and Newman (2011) understand the financialisation of the major South African corporations as the mechanism whereby they managed - through their listing on international stock exchanges and extensive use of financial instruments - to legally export resources and overcome existing exchange controls[42]. Further examination is thus needed on the interactions between the international sphere in and the large South African corporations entail with finance in South Africa.

4.4. Finance as the restructuring force of big conglomerates

From the flow of funds analysis presented above, it can be argued that the South African corporate sector has embraced financial markets in a similar way to what has been

[42]Such instrumentality is demonstrated by the strengthening of one of the major South African financial and economic problems: capital flight. Capital flight has plagued the economy throughout the last decades (Fine and Rustomjee, 1996) and by definition it is not accountable in the FoF. Recent estimates (Fine et al, 2011b) found that capital flight between 2001 and 2007 was on average 12 % of GDP each year, peaking at 20% of GDP in 2007.

the case in developed countries. Two major differences are nonetheless apparent: the importance of bank funding and the relative absence of financial assets accumulation. Previous analysis of financialisation in the corporate sector has demonstrated the variegated nature of this process across different national and institutional settings. Lapavitsas and Powell (2013) show how the historical background and institutional idiosyncrasies explain different patterns of corporate behavior among developed countries – with Japanese and German corporations still influenced by the coordinated market mechanisms that shaped their post-war development, for example.

It is my assertion that the originality of the South African corporate sector should be dealt with the same framework. The South African corporate sector, particularly its large corporations, needs to be further scrutinized in order to better understand its particular historical path and insertion in international markets and contextualize the empirical results presented above, namely the close relation with the banking system and the relative absence of financial assets accumulation throughout most of the period starting in 1994.

Focus on the historical dynamics of the limited set of major South African conglomerates can be of help in the mapping of the path of the South African corporate sector. These large corporations were originally born from Anglo-Saxon capital, originally either in mining interests (Anglo-American Corporation, Anglovaal) or insurance and financial services (Liberty Life, SA Mutual). After the Second World War, the initial group of conglomerates was joined by new ones created to accommodate the historically marginalized Afrikaner interests. Sanlam Group and the Rembrandt Group were the biggest to be built with the decisive support of the state.

The economic importance of these conglomerates was later reinforced by the economic isolation imposed on South Africa during the apartheid years. The conglomerates were forced to diversify and expand to new sectors, thus gaining additional weight in the economy as a whole. The diversification of activities extended to manufacturing, finance and other services. However, the primary location of capital accumulation still revolved around the mining and energy sectors. Fine and Rustomjee (1996) showed how the economy was organised, since the nineteenth century until the mid-nineties, around what they identify as the Mineral-Energy Complex (MEC). According to the authors, the declining share of mining in GDP and the increase of manufacturing and, during the last two decades, finance should not disguise either the importance of the MEC as the prime accumulation site of South African capitalism or the power it exercised over the country. In manufacturing industries such as iron and basic steel, non-metallic products or chemicals, the dependence of inputs and output demand from the MEC was paramount.

Six major axes of capital are identified by Fine and Rustomjee (1996) as constituting the MEC, with interests in various sectors of the economy, but all present in the oligopolistic mining market: Anglo American Corporation (AAC), Sanlam, Rembrandt, Anglovaal, Liberty and SA Mutual (now Old Mutual). The origins of these groups, in terms of the sectors in which they began their operations, were quite diverse: tobacco for Rembrandt; insurance for Sanlam, Liberty Life and Old Mutual; and mining for AAC and Anglovaal (Chabane et al, 2006). These major groups have undergone major transformations in their managerial structure and position within the domestic and international markets since the end of the apartheid. Nonetheless, the relevance of studying the recent developments of these large South African conglomerates is present in more recent research (e.g. Carmody, 2002 and Chabane et al, 2006).

It is true that new corporations, listed domestically, have arisen, going beyond what was the traditional MEC focus and expanding to new services such as retail, finance, healthcare and telecommunications. Examples of such companies include MTN, Netcare and Pick-n-Pay, which, at least initially, were boosted by new international capital (Chabane et al, 2006). These corporations have expanded successfully beyond the South African borders focusing both in developed countries (i.e. Netcare in the health care sector) and regionally across Africa (i.e. MTN and Pick N'Pay) (Goldstein, 2006).This apparent diversification of the larger Stock Exchange listed companies has not, however, implied a significant diversification of the South African economy.

It is our contention that the recent trajectory of the MEC conglomerates is of great relevance to understanding the contemporary trajectory of the South African corporate sector, encapsulating the transition of this economy from an isolated semi-peripheral position to a new transnational and financialised landscape.

Different forces of change have affected the corporate structure of the South African economy: unbundling and restructuring, transnationalisation, privatisation, BEE (Black Economic Empowerment), the emergence of new service corporations, etc. It is difficult to analyze each of these trends in isolation given that they are closely interconnected. However, these transformation forces, with both domestic and international origins, are dealt separately in order to provide a more comprehensive analysis, focusing on the crucial role of financial markets.

4.4.1. Unbundling and restructuring

With the opening and liberalisation of the South African economy, the large conglomerates, being characterized by their large, typically family-controlled, structure, underwent a deep restructuring. The complex and diversified nature of these conglomerates, born from their relative economic isolation, had placed them in an unfavorable position within international and financial markets. With opaque cross-sharing holdings and wide ranges of activities it was difficult to comply with international corporate governance standards and, as a consequence of that, they were trading below the net value of their underlying assets (Chabane et al, 2006) and quasi-isolated from the international financial markets funding.

These conglomerates, motivated by potential access to cheap capital and money markets, started a profound process of activity unbundling. This process typically involved the separation of mining, manufacturing and finance sectors into new companies. Each of prior conglomerates is now centered in core sectors, usually the ones from which these conglomerates were born, with straightforward and transparent property structures, complying with international financial accounting standards, and thus excelling shareholder value.

This trend started even before the end of apartheid, when Gencor (Sanlam Group) created Billiton, now one of the biggest commodities companies in the world and the biggest South African company listed in the domestic stock exchange. It concentrated all of its mining activities in this single company (Chabane et al, 2006). Anglo-American Corporation, the largest South African conglomerate, unbundled JCI (Johannesburg Consolidated Investment), separating its mining activities from its investment and property firms (concentrated in Johnsic), and later further unbundled both its gold and platinum operations into Anglogold (from which it has now completely exited) and Amplats. It concentrated its financial interests in a financial services group (First Rand) and spun off its paper and packages industry, Mondi (AAC website[43], 2011). The Rembrandt Group

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[43] http://www.angloamerican.com/about/history

unbundled its operations into three separate groups: Remgro (tobacco, mining and financial services), Venfin (telecommunication and technology); Richemont (overseas activities in luxury goods, tobacco and retailing). Smaller conglomerates followed the same path with Liberty Life unbundling Libsil and the First International Trust in 1998 (Liberty Life website[44]) and Anglovaal unbundling its industrial interests (AVI and AVENG) and mining interests (AVMIN), with the latter being controlled by Anglo American in 1999, thus determining the dissolution of the conglomerate.

The unbundling of the large MEC conglomerates enabled the entry of foreign investment, which took over many of the newly created corporations, and allowed a corporate governance structure suitable to access both foreign capital and debt markets and to attract foreign flows to domestic financial markets. Moreover, this new configuration and the access to new capital provided the opportunity to expand internationally in the core sectors where they were now focused.

4.4.1.1. Transnationalisation

The end of the economic sanctions against apartheid enabled the participation in the on-going liberalisation of international trade. South Africa is a member of the World Trade Organisation since its creation, in 1995. The importance of exports and imports in the overall economy has since increased. However, with a few exceptions (furniture, leather products, plastic products and motor vehicle industry[45]), natural resources still account for the majority of exports as they are the "best performing manufacturing sectors, while overall industrial performance has been relatively poor" (Roberts, 2010: 225). According to Roberts:

> "In broad terms, liberalisation and increased trade appear to have reinforced the existing patterns of comparative advantage based on natural resources, cheap energy and previous government support (Machaka and Roberts2003). It has not altered the overall capital-intensity of South Africa's exports." (2007: 14)

Trade liberalisation enabled the reinvented major corporations to reinforce their position within the South African economy, as they could better explore existing capabilities, benefitted from public intervention – mainly through the Industrial Development Corporation lending focused in mega infra-structure projects, tax breaks and

[44] http://www.libertyholdings.co.za/ABOUT-LIBERTY/Pages/about-liberty.aspx

[45] The success of the motor vehicle industry can be largely traced back to the importance of the state-supported "Motor Industry Development Programme". See Roberts (2010) for an overview.

incentive programs – and were the few corporations able to finance investments in order to take advantage of their economies of scale and scope (Roberts, 2010). Despite the unbundling of activities, the concentration at the level of sector and industry has remained quite strong. New services, such as telecommunications and healthcare, are themselves highly concentrated (Hodge et al, 2007). The outcome of that concentration is the capacity of "extracting rents through supra-competitive pricing and anti-competitive behavior" (Roberts, 2010: 233).

South African corporations took advantage of financial and trade liberalization to expand internationally. This was not a new path for most of the major conglomerates, but it gained a new boost following the lifting of the economic sanctions against apartheid, which provided access to markets at the regional and global level. Some of the major South African companies are today among the biggest multinational corporations.

Theory on the transnationalisation of companies has been dominated by the eclectic OLI approach (Buckley and Casson, 1976; Dunning, 1977): Ownership advantages, Location specific advantages and Internalisation of value chain. Recent developments (Goldstein (2006)) point to a typology taking the from a resource-based perspective - where companies dependent on resources (oil, gas, mining) expand internationally in order to access fresh capital, guarantee stable supply sources at predictable prices and gain market control -or one taking the form of a market based perspective -where companies expand in order to get access to new markets, raise new technology and profit from a more skilled workforce. The transnationalisation of the South African corporate sector does not follow a homogenous pattern that fits into any of the two aforementioned categories. Corporations have expanded in different markets according to their needs and capabilities thus fitting in different categories.

A number of companies have expanded regionally in Africa, taking advantage of geographical proximity and profiting from close cultural, geographical and political links in markets such as telecommunications or retail super-markets. New pools of resources – benefitting from privatizations that swept the continent - for traditional sectors such as mining (AAC) or energy (ESKOM) are also part of the reason for regional expansion. Despite South Africa being the major source of FDI for Sub-Saharan countries, most foreign investment is directed to European markets (Goldstein, 2006). The motivations behind such decisions are again diverse, from diversification of revenue sources, access to new markets, and search for cheap funding.

Having been one of the biggest promoters of the liberalization of capital controls, the conglomerates were major winners from the new access to international capital markets through their primary listing in major stock exchanges (the London Stock Exchange being the most important) (Chabane et al, 2006). Even though the internationalization of big conglomerates listings preceded the end of apartheid (Liberty International was listed in 1981 in London, Rembrandt created Richemont in 1988 in Switzerland), the liberalization of domestic markets and international transactions in the 1990s accelerated the transnationalisation of South African capital. Three, simultaneous, strategies were employed: 1) Access to international capital and money markets through international listings; 2) mergers and acquisitions in the international arena; 3) Increasing sales of South African equity in non-core sectors.

Major primary international listings in the post-apartheid era started with Billiton in the London Stock Exchange in 1997, followed by South African Breweries (SAB), in 1999. Today, primary international listing is a common feature of the former big conglomerates (AAC, Old Mutual, Liberty Life, Remgro are all listed). Benefiting from the new access to international markets, the abundance of hard currency capital and the international mergers and acquisitions frenzy, these groups succeeded in internationalizing their operations at the cost of now having foreign investors as shareholders. There were a number of advantages for these companies, indicated by Walters and Prinsloo as consisting of:

"(…)easier access to capital at lower costs; opportunities to raise efficiencies by competing head-on with global competitors; opportunity to escape from the volatility of financing costs in an emerging market economy; the opportunity to expand their core business into other countries and regions; the possibility of benefiting from divergent business cycle movements in different markets; the benefit of a diversified business approach which limits the impact of a severe contraction in the economic activity of a single market." (Walters and Prinsloo, 2002: 61).

These reasons point to the overcome of the disadvantage of being from a middle-income country with a particular focus on financial issues as in the new access to the lower cost abundant capital of the core, the avoidance of the peripheral volatility or the opportunity to have arbitrage gains from operations in different countries. These moves were supported by the South African state, which loosened exchange controls and granted approval for these moves to companies wishing to obtain approval for an offshore primary listing.

With the move of their headquarters to core countries, listing in the London FTSE 100 index, and by financially delinking with South Africa, these companies profited from having hard currency denominated assets, thus increasing their asset value and share price, and overcoming a market capitalization that was under net asset value. While AAC was valued 22 % below asset value in 1995, it was being traded at 37 % above that value in 2001 (Carmody, 2002). The move of primary listings to London by five major companies - Billiton, SAB, AAC, Old Mutual and Dimension Data (an IT company founded in 1983) –entailed a dramatic increase in the share of non-resident shareholders in these companies (Table 4.7).

Table 4.6. Non-resident shareholding in companies listed on the London Stock Exchange (% at end of year).

Companies	1998	1999	2000	2001
Billiton	48.6	62.9	67	77.4
South African Breweries	19.7	45.1	43.8	59.8
Anglo American	16.9	44.1	46.5	77.5
Old Mutual	-	38.7	38.1	43.9
Dimension Data	10.9	31.2	55	59.2

Source: (Walters and Prinsloo, 2002)

Many of the large South African corporations became foreign companies. The traditional family management was replaced by large fund managers focused on the new financial demands of high share prices and dividends (Carmody, 2002). This outward shift of South African capital may explain the lack of domestic financial asset accumulation during the post-apartheid period reported in the previous flow of funds analysis. With the access to international financial markets and hard currency denominated assets sheltered from the volatility of middle-income countries, a preference for foreign financial assets is to be expected. Looking at the foreign mergers and acquisitions frenzy of these companies, that seems to be the case.

Anglo-American, still the second largest company in the Johannesburg stock exchange, sold its gold mining interests in South Africa[46] to an American investment fund and consolidated its interests both in the most profitable sectors of mining and in the paper and pulp industries, buying companies in Argentina, Namibia, Chile, Australia, Colombia, Brazil, Russia and France. Rembrandt's tobacco company Rothmanths merged with British

[46]http://www.angloamerican.com/about/history

American tobacco, and is currently under the control of Philip Morris. SAB acquired breweries in Asia, Europe and Latin America and later merged with Miller, granting Philip Morris its largest stake (Chabane et. al., 2006). Liberty Life International was taken over by Standard Bank, with which it had established a joint venture (STanlib[47]), thus creating a major international wealth manager. Old Mutual bought the Norwegian insurer Skandia in 2005. New international industrial groups were therefore formed, focusing in particular areas of activity and expanding around the world, some of them even transferring their headquarters to other countries (e.g. Billiton, AAC). The lack of domestic financial asset accumulation thus seems to be have been compensated by the accumulation of foreign assets.

Yet, the success of individual companies in the international sphere seems to have come at a cost to South Africa. Transnationalisation and displacement of headquarters enables escape from any kind of political control, putting corporate wealth beyond the influence of the South African state. Moreover, the shift of the corporate sector to foreign markets has come at the cost of an increasing negative net outflow of financial dividends from the country, reaching a negative impact of -3% of GDP in 2008 (Figure 4.6).

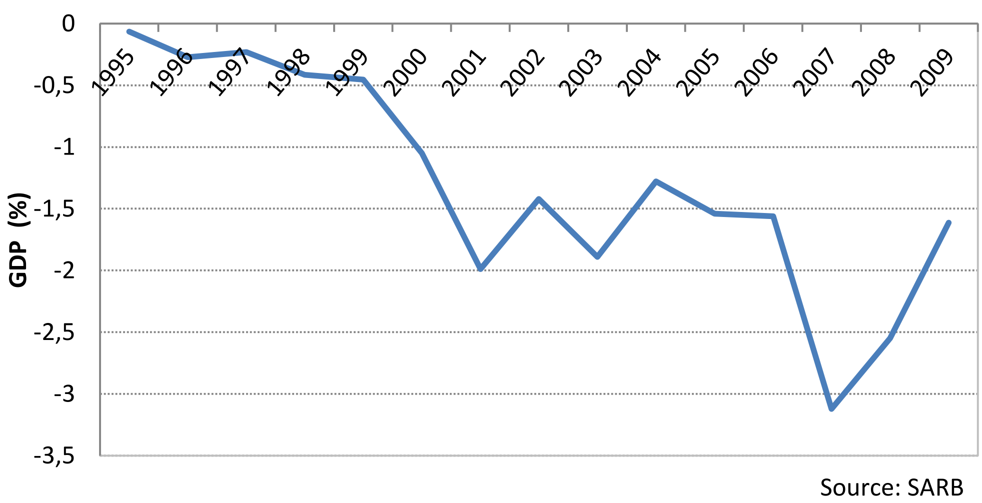

Figure 4.6. Net flows of dividends from the Rest of the World (% of GDP).

[47]http://www.libertyholdings.co.za/ABOUT-LIBERTY/Pages/about-liberty.aspx

The transnationalisation of South African capital, by making it less dependent on domestic financial markets, additionally provides a further explanation for the continued reliance on the banking system at the domestic level. If, on the one hand, the big industrial conglomerates disposed of their assets in the financial sector as part of their unbundling, on the other hand their international operations enabled them to take advantage of the semi-peripheral position of South Africa in the international financial sphere. Forced to keep interest rates high in order to tame inflation and promote foreign capital inflows, and benefiting from the increase in the value of the rand from 2002 onwards, South Africa is one of the major destinations of international currency carry trade (Gallati et al, 2007). This financial strategy, if usually pursued by banks with leveraged assets, can also be profitable for corporations with assets in different currencies. Additionally, from the analysis of the uses and sources of flows presented in the previous section, bank credit is particularly used during periods of international volatility. The robust South African banking sector may thus serve as a funding alternative in periods of stress, such as in the 2001 and 2008 crisis years, when net foreign capital flows became negative and banking loans surged.

4.4.1.2. Black economic empowerment

Black Economic Empowering goes back to the foundational principles of the African National Congress (ANC) in its Freedom Charter. The strategy of increasing black participation in the economic arena was therefore to be one of the central elements of the post-apartheid period when the ANC came to office. Restrained by the liberalizing agenda agreed in the GEAR (Growth, Employment and Redistribution) document, BEE was, until the late 1990s, limited to a number of financial transactions (Tangri and Southall, 2008). Black-owned leveraged Special Purpose Vehicles were to acquire shares in some of the major South African companies, particularly in sectors no longer perceived as core businesses by the conglomerates. For instance, Sanlam sold its insurance company METLifeto NAIL - New Africa Investment Ltd (a holding investment company) and Anglo American industrial arm, Johnnic, was partially sold (39.5%) to black-owned The National Empowerment Consortium (Freund, 2007).

With the absence of an activist state, the new South African government tried to emulate the promotion of Afrikaner interests during the post-war decades through financial markets in a racialised version of “popular capitalism”. However, because it was dependent on stock performance and financial returns, this strategy – limited from the start to a minority of the black population, from whom redistribution would supposedly trickle down – failed to succeed given the high interest rates and falling financial markets of the end of the 1990s[48] (Ponte et al, 2007). A second phase of BEE was then started after the presentation of the National BEE strategy in 2001, paving the way for a broader approach, envisioned to tackle a range of social "imbalances" (skills development, labor rights, corporate social investment, etc.). Within the corporate sector, this report led to BEE charters in a number of sectors, with several criteria to be followed. Compliance had again been conducted with the help of the financial sphere, either in the form of private equity intervention or of funding by the state-owned Industrial Development Corporation. In terms of ownership, the number of financial M&As identified as connected to BEE grew from 10–15 % of the total in the period 1998–2002 to 24–32 % in 2003–5 (Ernst and Young, 2007). However, this remained limited to a few large deals, with little room for new small and medium black businesses, since, as pointed by Ponte et al:

"Concentration at the sector level also means that it is difficult for new firms to enter and grow except through acquisition of one of the existing dominant players although there have been some exceptions to this, notably in rapidly growing services such as mobile telecommunications, media, information technology and healthcare."(Ponte et al, 2007: 947)

As minor (although growing) as BEE might be in the South African economic structure, the role played by the financial sphere in the implementation of this policy should be stressed here. Political power used the financial markets to, through the extensive use of credit and financial innovation, acquire participations in the corporate sector with newly acquired shares to be used as collateral. The accommodation of elite black interests served the unbundling of non-core assets that the corporate sector was then pursuing and the expansion of domestic financial markets.

4.4.1.3. Privatisation

Large public companies were established during the apartheid era (SASOL chemical, ESKOM electricity, ISCOR in steel and coal). These companies proved important to compensate the economic isolation of apartheid and to provide infrastructure for big private capital conglomerates (Fine, 1997). The political motivations for the privatization of public assets have changed overtime. The privatisation of SASOL and ISCOR (now controlled by Arcelor/Mittal since 2001) in the end of the 1980s was driven by the need for short-term funding because of the economic isolation of the apartheid regime (Roberts, 2010). The ANC post-Apartheid governments established privatization as a way to restructure the state

[48] NAIL was eventually affected by a number of internal scandals and ended up under the control of white-owned groups.

sector, increase efficiency and reduce national debt (Chabane et al, 2006). A National Empowerment Fund was established which sought to take residual stakes in the newly privatized firms and transfer them to black owned groups. Privatization during the Mandela presidency years was however modest. The later Mbeki government that followed gave it an extra boost through the promotion joint ventures with the private sector and establishing a new legal corporate governance framework for these firms and modeled public corporations to behave as private corporations.

4.5. Conclusion

In this chapter the meaning of financialisation for non-financial corporations was to be better captured. Given the inability of neoclassical theory to recognize the systemic and historical nature of this process in their abstract and microeconomic approach to corporate finance and, more generally, to the firm, an alternative theoretical framework was provided, building on Marxist political accounts on financialisation in this sector. An account of non-financial corporations in South Africa, reflecting their particular international position, was provided in order to better grasp the meaning of financialisation in this sector.

It is undeniable that the South African corporate sector has undergone profound transformations in its structure during the post-Apartheid era, with financial markets playing a pivotal role. Financialisation within the South African non-financial corporate sector was assessed through flow of funds data. These data showed that there is increasing involvement of South African corporations with domestic financial markets, thus converging with the transformations that their core-country counterparts went through in the last decades. Yet, the convergence with the Anglo-Saxon model of funding through the markets is not completely repeated here. Stock and bond issuance played an increasing role, but the persisting relevance of banking credit (and deposits) shows the close relation between banks and industry. In this aspect, South African corporations seem to behave in a closer way to continental European companies (Artus, 2011).

Nonetheless, one should not conclude that South African corporations (or, for that matter, continental European) are not financialised. Through their international listings, adoption of corporate governance, involvement in international M&A and the use of new, sophisticated financial products, it is clear that these companies have a close relation with international financial markets, from which they have benefitted by gaining access to capital and financial instruments. Corporations in South Africa transformed themselves from big domestic conglomerates with interests across the economy to transnational companies focused in particular core operations. That focus was mainly driven towards the most dynamic sectors, namely the traditional mineral-energy complex and the rising financial sphere. The importance of the international arena and the possibilities it provided (access to cheap funding and hard currency financial assets) explain the domestic parsimony of South African corporations in regards to one of the criteria for financialisation presented in the beginning of this chapter: the accumulation of financial assets.

Given the growing involvement of non-financial corporations with the different sources and uses of finance at the domestic level, the domestic financial sphere has taken on an increasing role but with a different configuration from what is the case in the Anglo-Saxon countries. Corporations still rely on banking finance as an important source of funds to invest domestically and as a destination of its flows, profiting from fluctuations in the domestic exchange and interest rates relative to foreign, core, countries.

The financialisation of the South African corporate sector should thus be taken as an example of the heterogeneity of this process across the globe. The “structural power” of global finance is evident here. The opportunities created by the liberalisation of the economy and the subsequent liberalisation of capital flows imposed a profound restructuring of South African capital. The conglomerates had to reinvent themselves either as financial holdings or transnational corporations focused on specific sectors in order to fully participate and compete in the international arena. This process has favored the pinnacle of the international financial sphere’s hierarchy. It has provided flexible and profitable outlets for international short-term capital flows, which can now be placed in compliance with the international standards of financial investment. It has facilitated capital flight from the periphery to the financial core and promoted the transfer of the headquarters of the South African conglomerates to core countries, evading any kind of domestic political control that might have pursued policies favoring the much-needed structural change towards an employment-creating economy.

Nonetheless, the specificities of the South African corporate sector financialisation should not lead us to consider that these corporations and the fractions of capital they represent are consequently in a subordinated position. Financialisation was not the effect of an external imposition, but of compliance with the interests of South African capital to expand internationally and profit from the recent financial boom and with the need to accommodate the new political landscape in the country with the introduction of BEE. The new international power relations have benefited particular fractions of domestic capital whose interests converge with their counterparts in core countries without changing the overall dual economic structure of the country. This reorganisation of the corporate sector has not induced significant transformation of the South African economic structure, which continues to revolve around the production and processing of minerals and energy. In fact, the pattern seems to have been reinforced. The uneven and combined character of South African capitalism has gained a stronger, financialised appearance within the corporate sector.

5. Financialisation and banks: from theory to the South African case

5.1. Introduction

Research on the transformation of the banking sector during the last decades of liberalisation, deregulation and privatization is still scarce in political economy. However, nascent research on financialisation from a Marxist political economy perspective, which breaks theoretically with the abstract and atomistic dominant neoclassical approach, has been recently presented by Lapavitsas and Dos Santos (2008), Dos Santos (2009) and Lapavitsas (2009). Building on contributions from other political economy accounts and other social sciences, this approach has provided a new theoretical framework for analyzing contemporary bank transformation.

The new role and position of banks are understood in this context as part of a broader process of financialisation - i.e. the rise of financial markets, agents and motives (Epstein, 2005; Krippner, 2004) relative to the rest of the economy - which constitutes a structural transformation that has swept all of the most developed capitalist economies. Put briefly, financialised banks, having partially lost their traditional role as financial intermediaries for major corporations given that the latter have become able to access financial markets directly in order to fund themselves, have turned to financial market mediation operations and lending to households as new markets and sources of income. This reinvention was only made possible by the role of public policy – liberalising and deregulating markets and rolling back the provision of public services, thus forcing households to enter into debt –, alongside the availability of new technologies that provide new credit assessment instruments and faster access to data, thus enabling the extension of credit. As a result of this reinvention, financialised banks did not simply survive as financial intermediaries – rather, they reinforced their position, with growing assets and increasing profits relative to the overall economy.

This chapter is driven by two main objectives. The first one is to establish the theoretical bases for analyzing the banking sector in a way that confronts the dominant mainstream theoretical approaches to banks and the new political economy literature on financialisation. It is to be shown that mainstream neoclassical theoretical accounts, being primarily concerned with the theoretical challenges of the existence of financial intermediation in a market economy, are unable to free themselves from a highly abstract, perfect-competition standpoint, which proves inadequate for tackling the contemporary transformation of banking and its specificities in different settings. The second task of this chapter is to provide an historical account of the evolution of the banking sector in South Africa, the impacts of liberalisation and deregulation, and the recent transformations of the sector in terms of structure, ownership and internationalization during the post-apartheid years. This initial work will also serve to ascertain the soundness of the theoretical approaches adopted here, by assessing both the mainstream and political accounts against the South African reality.

This sector's close historical and institutional ties to the most developed Anglo-Saxon banking systems, the political transformations it underwent with the end of apartheid, and the constraints and opportunities created by rising international capital flows demonstrate a common path with the financialised banks of developed countries. Post-apartheid South Africa has been the recipient of increasing international capital flows, particularly during the 2004-2008 period, and has exhibited some of the highest real interest rates in the world – two of the features that are normally associated with financialisation in developing countries. Nonetheless, South Africa, having endured neoliberal public policies, which promoted the integration of the domestic financial system in the international arena, still has non-financial corporations relying on bank loans, reflecting the much less developed than those of developed countries. Moreover, the opposition between a booming financial sector and a declining "productive" sector assumed in the literature on South Africa should be taken with caution, given that the rise of capital inflows has in fact been accompanied by a surge of investment and economic growth in this country. Finally, the typical public services of the Welfare State were always incipient in this setting and, therefore, the impact of the neoliberal rolling back of the state would be not so important in pushing households to the arms of finance. Additionally, a large share of the population still lacks access to sophisticated financial services. Research on the financialisation of the banking sector of middle income countries, and of South Africa in particular, is thus justified not only as a further geographical inquiry into the transformation of the international contemporary banking sector in Lapavitsas' and Dos Santos' sense, but also as a specific case-study of the historical path of the asymmetric impacts of waves of neoliberalism[49] and international insertion of increasing and volatile international capital flows.

Only by taking into account the specificity of the historical and political trajectory of South Africa can the differences and convergences be better grasped against the theoretical framework on financialisation adopted here. A path of concentration and of domestic and international expansion, which followed efforts at liberalisation and deregulation and the growth of capital inflows, will become evident for the South African banks, illustrating their convergence with their developed country counterparts. The interest of undertaking an empirical scrutinity into these financialisation dynamics, like the one presented in the next chapter, is justified by the historical and institutional account of the trajectory of South African banks which is presented in the present chapter.

This chapter is organised as follows. I start with a brief literature review on banking, which covers the mainstream neoclassical approaches arising from the asymmetric information paradigm as well as the political economy theoretical contributions on banks. Special attention is given to the recent Marxist political economy literature, which frames our approach to the South African banking sector. I then address the historical evolution of the South African banking sector, by focusing on the processes of liberalisation and deregulation that this sector went through over the last few decades. This includes an assessment of the changes in terms of the ownership and internationalisation of this sector. I conclude by putting forth the reasons for adopting a political economy perspective when studying South African banks and with a call for further empirical research as a means to validate the financialisation framework in the case of such middle-income countries as South Africa.

5.2. The nature and role of banks: an appraisal of the literature

5.2.1. Neoclassical theory - why do banks exist?

In the neoclassical economics “Arrow-Debreu” equilibrium theory of complete markets, there is perfect information and agents behave rationally with homogeneous expectations. Within this approach, there is no reason why banks, and financial

[49]See the previous discussion about the contributions of International Political Economy and Economic Geography to the study of financialisation (Chapter 1).

intermediaries more generally, should exist. Financial instruments to exchange savings would be "constructed and traded costlessly and they (would) fully and simultaneously meet the needs of both savers and investors" (Scholtens and Van Wensveen, 2003: 9).

It was only the imperfect information and transaction costs theoretical paradigms, born in the 1970s, that a theoretical *raison d'être* was provided within neoclassical economics for the existence of banks and financial intermediation. These approaches, which are based on microeconomics, are analogous to the various neoclassical theories of the firm. Banks and financial intermediaries, as hierarchical non-market institutions, arise as a more efficient institutional arrangement for reducing transaction and/or information costs when compared to market arrangements.

Building on the imperfect information paradigm, Leland and Pyle (1977) put forth one of the seminal contributions in this area. For these authors, financial institutions, given their economies of scale, would provide individual investors with better information at a lower cost through their own monitoring[50]. Diamond (1984) develops this theoretical approach by focusing on the advantage that financial intermediaries have in the asset diversification they can build in order to achieve lower costs of bankruptcy for lenders (depositors). Financial intermediaries, by behaving as "delegated monitors", thus function as an institution that reduces risk for lenders.

Boyd and Prescott (1986) add a more elaborate reasoning. In order to avoid problems of adverse selection between "good" and "bad" investment projects, agents with their endowments join forces to evaluate investment projects. In this approach, financial intermediaries are regarded less as delegates than as coalitions of agents that gather information on investment projects, invest in the best and issue claims with different "contingent payoffs" to the ones of the ultimate borrowers (Gorton and Winton, 2003).

Being primarily concerned with bank runs, Diamond and Dybvig present a different rationale for the existence of banks. The authors define banks as those institutions that are "able to transform illiquid assets by offering liabilities with a different, smoother pattern of returns over time than the illiquid assets offer" (1983: 300). Without banks, only savers who postpone their consumption decisions to a distant future would enjoy high returns

[50]The same goal could be theoretically achieved by markets for information, but the "public good" character of knowledge and the consequent problems of information pricing impede such arrangements and create the incentives for the emergence of financial intermediaries which buy and hold assets on the basis of their own (better) gathered information

from lending. For the bank run risk caused by shifts in expectations, banks would provide risk sharing arrangements for depositors, such as deposit insurance schemes. Holmstron and Tirole's (1998) model of financial intermediation focuses more on the borrowers' investment projects than on the lenders (depositors). Access to credit is regarded as constrained by both the capital of borrowers and financial intermediaries[51]. In their model, Holmstron and Tirole highlight the fact that small capitalised firms are most vulnerable to credit squeezes and that the capital growth of the intermediary, by being invested in the projects that it funds, promotes the investment of the latter in the monitoring of its investments.

More recently, Diamond and Rajan (2003) elaborate this liquidity and illiquid asset matching agenda by stressing how the risk of a bank run commits banks to use their human capital to monitor and collect loans, thereby preventing the extraction of rents from lenders (depositors) and increasing the overall efficiency in the allocation of resources. For Diamond and Rajan (2001), banks, given their capital fragility, are forced to extend liquidity to the overall economy as they continue to issue deposits when initial depositors have liquidity needs. Banks thus constitute an arrangement that utilizes "economy's collateral better but also enhances it" (2001: 321).

All these different streams of the neoclassical literature, with their atomistic and formalized models, while able to justify the existence of banks as efficient arrangements between savers and borrowers that ultimately enhance the aggregate level and quality of investments (Bhathacharya and Takhor, 1993), are at pains to take into account the transformations that contemporary banking has gone through over the last few decades, as well as their macroeconomic consequences. The increasing growth of the sector relative to GDP and the increasing number of agents and products are scarcely accounted for. Allen and Santoremo (2001) try to tackle some of these issues by focusing on the rise of financial intermediaries in bond and stock markets, on the dynamics of financial innovation and on the growth of the banks' off-balance sheet activities. These authors start their analysis from the apparently paradoxical consequences of the recent decrease in transaction and information-seeking costs - fostered, for example, by new information technologies -, which should have implied the progressive withering away of financial intermediaries -when in

[51]This approach has the advantage of being a better approximation to the modern behavior of banks, whose expansion is more constrained by capital adequacy ratios than by the traditional notion of reserves.

fact these agents have been multiplied in number and size. An alternative rationale for financial intermediation is presented based on the participation and risk costs in financial markets incurred by agents, which compel them to resort to financial intermediaries.

This theoretical framework rests on the imperfect information and transaction cost paradigms. Although it accommodates the increase in the number of financial agents and in the size of the markets, and indeed provides a rationale for the continuing existence of financial intermediation, this approach fails to account for the importance of the financial sphere in contemporary economies. Moreover, as argued by Lapavitsas and Santos (2008), this framework proves particularly inadequate in light of the risk assessment failure patent at the core of the 2007-2008 financial crisis. Ultimately, the growing number of financial intermediaries seems to have led to an increase in systemic risk, rather than to a decrease. Neoclassical banking theory, insofar as it is limited by its microeconomic underpinnings, has therefore done little more than provide ex-post explanations for the existence of banks and their recent evolution. It has neglected the role of public policy in the transformation of the sector and failed to take into account the increasingly powerful role of banks in contemporary economies, plagued by financial volatility.

5.2.2. Financialisation on banking: the transformation of contemporary banking

The profound transformation of the banking sector across all of the most developed countries over the past thirty years has nonetheless been the subject of an emergent literature, from political economy perspectives, on the changing role of banks. Ertuk and Solari (2007) provide a critical overview of that literature. They refuse both the mainstream idea of banks as mere intermediaries between lenders and borrowers, arising from asymmetric information and transaction costs in financial markets (translated into risk management in the Allen and Santomero world of intermediation), and the literature on “varieties of capitalism” (Hall and Soskice, 2001), with its concepts of market-based and coordinated economies which supposedly mould the trajectory of the banking sector in each national context. According to Ertuk and Solari, the former falls short of explaining the increasing number of mergers and acquisitions in the sector, which has produced mixed results in terms of efficiency gains and profits, while the latter, with its interest in providing a more historical and institutional perspective, fails to provide a comprehensive understanding of the multiple and contradictory national indicators, and adopts a static perspective that makes it impossible to account for the changes in the banks’ behavior patterns across the most developed countries. By drawing on a number of empirical indicators, the authors show the constant reinvention of banks that has characterized this sector over the last few decades. Despite not necessarily abandoning their traditional intermediation role between lenders and borrowers, banks have increasingly turned to new activities and new sources of income: an increasing emphasis on retail banking and on the collection of fees from providing financial services to customers, with households as new targets, alongside a rise in proprietary trading in investment banking, thus "resulting in a considerable expansion of banking as relatively profitable sector in capitalist economies" (2007: 383).

Dos Santos (2009) follows this lead and, from a Marxist political economy perspective, seeks to show empirically the new sources of income for banks in the most developed countries. For Dos Santos: "contemporary banking is very different from the traditional business of taking deposits from corporations and the general public, making loans to enterprises, and making profits from the difference in interest rates between them." (2009: 4). The changing pattern of funding of corporations, now involved in financial engineering schemes, and households is also considered. Corporations, particularly in the US, have become less and less dependent of banking finance as they increasingly seek to access money and capital markets directly. This has caused a symbiotic arms-length relation with banks, which profit from the fees that the organisation of these financial operations involves. At the same time, banks have increasingly turned their lending operations towards households. This took place in a context where the latter find themselves in an increasingly vulnerable position due to the privatisation of public services, which pushed households into the arms of banks both as assets holders (as in pension funds) and as debtors (in order to finance housing, education and health, now taken over by the private sector).

This perspective takes the traditional Marxist notion of financial income as coming exclusively from interest-bearing, loanable capital a step further, by adding a new role for banks in the extraction of revenue from the circulation sphere. Powell and Lapavitsas (2011) develop this stream of research and identify financialisation in banks as relying on "an increase in the relative weight of their lending to finance, insurance and real estate as well as to households. This would relate to the ability of financial institutions to extract profits in the sphere of circulation, even by deploying expropriating and predatory methods, including from the revenue of workers and households." (2011: 13).

The financial system, and more specifically banks, plays a pivotal role in this context, as they are the primary financial institution where different financial relations are intersected between different agents. The way in which the financial system is organized as an institutional setting depends on different historically-determined national trajectories. Powell and Lapavitsas (2013) scrutinize the evolution of banks, corporations and households in a number of developed countries, and confront the distinction, which originates in the "varieties of capitalism" literature, between bank-based and market-based financial systems. They conclude, despite recognizing that this analytical distinction still holds for different countries, that for banks, financialisation is visible as lending has turned toward other financial corporations, real estate and households.

However, as was already seen, financialisation differs from developed and developing countries. Research on the financialisation and transformation of the banking sector should thus take into account the specificities of the historical and geographical settings in which these processes take place. The specificity of middle-income countries in the present international financial architecture was shown, among others, by Becker et al (2011). Middle-income countries feature their own variety of financialisation, which is characterised by the expansion of interest-bearing capital thus implying the expansion of the banking sector. In the absence of mature financial securities markets, financialisation in the latter context is brought about because of the growing dependence upon international capital inflows. Now, as these authors themselves admit based on the four cases that they analyze (Chile, Brazil, Slovakia and Serbia), there is far from being a linear transition from "interest-bearing capital financialisation" to the "fictitious capital financialisation"[52] that would characterize developed countries. The possibility of variation should be taken into account. The role of banks in furthering financialisation based on the expansion of interest-bearing capital is here highlighted, in contrast to financialisation in developed countries where it is the securities markets that play the leading role. Another feature commonly identified as being at the core of financialisation in these countries is foreign bank entry (Lapavitsas, 2010). Having gained access to these markets as a result of international liberalisation, these banks structure the financial markets of these countries by exporting their contemporary practices to new geographical settings. One therefore needs to examine carefully their historical trajectory, the role played by public regulation and the

[52]The straightforward identification of Marx's notion of fictitious capital as corresponding to financial securities may be problematic, insofar as this conceptualisation calls for an understanding of the financial sphere as being virtual, with its inner mechanisms totally detached from the "real" economy. For a discussion of the concept, see Lapavitsas and Levina (2011).

type of international insertion, which structured the transformation of their operations in the post-apartheid era. This assessment is crucial in order to identify the motives that have driven and molded their specificities, and to understand the particular form taken by financialisation in this country.

5.3. The specific path of the South African banking sector

5.3.1. From imperial banks to neoliberalism

In order to understand the evolution of the South African banking system since 1994, one must take into account its origins and the regulatory environment in which it evolved until the early 1990s. In this section, a brief history of the trajectory of this sector is presented which emphasises the role of public policy in structuring the sector and pays special attention to the neoliberal turn that began in the late 1970s and continued after the post-apartheid democratisation of the country. This new regulatory framework has enabled South African banks to grow and reinvent themselves domestically and internationally to converge with the banks of developed countries.

The history of the South African banking system dates back to establishment, in the late eighteenth century, of banks in different colonies (Cape, Natal, Orange Free State) with the aim of meeting the needs of the farming communities (Gidlow, 2008). From the mid-nineteenth century onwards, imperial banks from Britain –the Standard Bank and the London & South Africa Bank –gradually took on a dominant position. These banks profited from the various cycles brought about by price fluctuations or by the new discoveries of minerals (copper, diamonds, gold), and functioned as a conduit for the flow of local surpluses to the capitalist center in Britain (Bond, 1998). These “booms and busts” eventually led to the centralization of capital around a small number of banks held by foreign shareholders. This concentration process was further enhanced by the formation of the Union of South Africa in 1910, and went hand in hand with the latter’s promotion of, and accommodation to, Afrikaner capital (creation of the Volksas Bank and support of the Netherlands Bank for South Africa). In 1921, in the wake of a period of turmoil in the international gold market, which had a serious impact on South African banks, the South

African Reserve Bank[53] was established with the aim of protecting banks from financial instability through its monopoly on gold-converted banknote issuance. After the National bank was acquired by Barclays in 1926, the former, along with the Standard Bank, Volksas bank and the Netherlands Bank became the four dominant banks in the country – a hegemonic situation which would remain unchanged throughout the post-war period and which was not only tolerated but actually promoted by the South African state (Verhoef, 2009).

Industrialisation in the post-war period turned the domestic banking system into a pivot of the funding required by the new emergent industries, by allocating the surpluses that originated in the dynamic mining and energy sectors. This was accompanied by the banks' expansion into new markets, such as consumer credit. The banks thus ensured both the supply of capital and the increase in aggregate demand that was required by the state in its industrialisation and regulation efforts, to reorganize both "English" and Afrikaner interests (Bond, 1998). This process resulted in the overall modernisation of the banking system, with the emergence of new markets, such as money markets, and new agents, such as building societies, in a process that, nonetheless, was heavily regulated by the state. The first comprehensive Banks Act, of 1942, regulated and segmented the bank according to their functions, and imposed strict capital reserves and liquid assets requirements (Verhoef, 2009). Later on, with the 1965 Banks Act, this regulation was to be further restricted, through the establishment of limits to credit creation through public controls over both price (interest) and quantities (Gilbert et al, 2009). The age of financial regulation that characterized the Bretton Woods international financial architecture until the 1970s had its own South African declination.

However, the South African system stood out at the international level due to the continuing hegemony of the old imperial banks: by 1970, 55.8% of all deposits were held by banks controlled by foreign shareholders – a reality that was increasingly perceived as problematic, particularly by the "Franzen commission" of enquiry established in the same year. In 1976, a cap of 50% on foreign-held shares was imposed, with a view to promoting the gradual departure of the major foreign shareholders from Barclays Bank, Standard Bank and the smaller American Citibank. This process gained its final thrust with the domestic

[53]From its inception until the present day, the South African Reserve Bank has had private shareholders, following the model of the American Federal Reserve (SARB website).

debt crisis of the mid-1980s. The South African government was eventually forced to declare a partial default on its debt after foreign banks, led by Chase Manhattan bank, withdrew their credit lines. Fleeing from the economic and political turmoil, foreign capital was then replaced by the South African conglomerates: Anglo American Corporation, De Beers and Southern Life Association in the case of Barclays (later renamed First National Bank), in 1986; Old Mutual, the Rembrandt group and Liberty life in the case of the Standard bank, in 1987 (Verhoef, 2009).“Loose” monetary policies set by the government accompanied this turn, encouraging banks to extend their operations to new markets, such as the market for housing in the black townships or the stock market[54] (Bond, 1999).

The national encroachment upon the banking sector was short-lived. In the late 1970s, with the creation of the “De Kock” Commission, a new period of financial liberalisation and deregulation ensued, which favoured the lifting of exchange rate controls - allowing the variable pegging of the rand with the dollar and ending the previous dual exchange rate system (Singleton and Verhoef, 2010) - and a more market-oriented public regulation of the financial system. Even though the debt crisis of the mid 1980s brought a halt to these efforts at financial liberalisation, this financial turmoil seems to have given a new impetus to the market-oriented De Kock recommendations. The 1990 Banks Act ended the previous bank segmentation (with only mutual banks considered as a separate category) and introduced prudential requirements (capital adequacy, liquidity, minimum reserves), aligning domestic regulation with the international standards of the 1998 Basle agreements for risk management (Gilbert et al, 2008). These transformations brought about changes in the financial sector, with a rising share of GDP coming from the financial system despite the overall economic stagnation. The result was the integration of the merchant banks into the major South African banks, and the gradual demutualization of banks, perceived as a necessary step to find cheaper capital in the markets, a process later followed by insurance companies like Sanlam and Old Mutual. New financial agents emerged which benefited from the booming domestic capital market, such as unit trust

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[54] The subsequent tightening of monetary policy in 1989, with interest rates hikes, led to another economic crisis with massive defaults (40% rate) in the new bonds issued for black lenders. A halt to the expansion to black lenders was the practical result of a crisis that did not affect the major banks structurally (Bond, 1998).

funds – which grew from 31 in 1990 to 260 in 2000 - and foreign banks like HSBC, Sociéte Générale or Deutsche Bank, which bought local brokerage houses (Jones, 2003).

The final push for liberalisation and deregulation came with the end of apartheid and the later implementation of the pro-market GEAR (Growth, Employment and Redistribution) public strategy. The short-lived financial rand[55] was terminated in 1995. Exchange controls were gradually liberalized, namely with the introduction in 1995 of assets swaps - between a part of existing portfolios and foreign assets held by foreign investors -, in order to allow institutional investors such as pension funds, insurers and unit trusts (mutual funds) to diversify their portfolios internationally (later scrapped in 2001) and with the gradual allowance of growing amounts of investments abroad for companies and individuals (Farrel and Todani, 2004). In its turn, capital account liberalisation enabled the promotion of foreign capital inflows, particularly as portfolio investment.

The independence of the monetary policy was to be constitutionally guaranteed by the independence of the Reserve Bank. The domestic banking market was opened finally to foreign banks with the 1994 Banks Act amendment (Hawkings, 2004). If South Africa might have been a laggard when compared to developed countries in adopting neoliberal reform, it quickly sought to follow the financial deregulation and liberalisation trends that opened the way to financialisation in the most developed countries.

To the public policy efforts aimed at liberalising and deregulating the financial sector, one should add the role played by macroeconomic policies, overviewed in Chapter 3, which adopted an orthodox approach on both the fiscal and monetary sides. Public budget surpluses were attained in 2007 and 2008, even if deficits of 3.9% in 2009 and 7.3% of GDP in 2010 were registered, there were mainly due to the international crisis. After rising during most of the 1990s, public debt has been decreasing for most of the last decade, having reached 27.1% of GDP in 2010 (see Chapter 3).On the other hand, monetary policy has been strongly supportive of the financial sector, in general, and the banking sector, in particular, following the general consensus on the priority to be given to price stability, central bank independence, internationally standardized supervision and an hands-off approach to the high concentration in the insurance and bank markets. The

[55] The rand for capital operations by non-residents reintroduced in 1985 during the debt crisis

inflation target, between 3% and 6%, is set by the South African Reserve Bank, which follows a policy of high interest rates[56] in order to comply with its target.

5.3.2. Competition or concentration?

The neoliberal political turn concerning public policy in the banking sector was to be justified on the basis of the need for competition to enhance efficiency within the highly concentrated banking sector, particularly thanks to foreign bank entry. However, the liberalisation of the banking sector had little effect in terms of enhancing domestic competition – in fact, concentration has grown in the last two decades. The total number of registered banks dropped from 41 in 2000 to 18 in 2009, and the number of controlling companies exhibited a similar trend– from 37 to 15 (Table 5.1).

Table 5.1. South African registered banks and controlling companies.

	2001	2002	2003	2004	2005	2006	2007	2008	2009
Banks	41	30	22	20	19	19	19	19	18
Mutual Banks	2	2	2	2	2	2	2	2	2
Controlling companies	37	27	19	16	15	15	15	15	15
Branches of foreign banks	15	14	15	15	15	14	14	14	14

Source: SARB Annual Bank Reports.

The smaller local banks that had emerged with the deregulation of the early 1990s struggled to survive in the new liberalised but stagnated economic environment and began to be assimilated by larger ones. The Asian financial crisis of the late 1990s and the outflow of portfolio capital that ensued – greatly increased in the previous years as a result of the liberalisation of capital controls – caused liquidity problems to smaller banks, which were worsened by the depreciation of the rand in 2001. Fuelled by the outward escape of capital flows during this period (see chapter 3), a number of smaller banks collapsed due to public mistrust, with deposits fleeing away. These were either taken over, notably the BOE bank by the Nedbank (former Netherlands bank), or placed under curatorship, notably the Islamic Bank and Sambou (which was the seventh largest bank at the time) (SARB, 2002). This consolidation ensured that the high concentration of the banking system remained stable around the four major banks.

[56] 5.5% for repo and 9.5 % in prime overdraft rates in 2012 (SARB web-site).

The South African banking system is now composed of eighteen commercial banks and two mutual banks (SARB Annual Report, 2010). The sector is mainly concentrated around four major banks - Standard Bank, ABSA (former Volksas bank, merged with UBS Holdings and Allied Groups), Nedbank and FirstRand - which in 2009 accounted for 84.6% of total assets (SARB, 2010). Concentration in the banking sector is a common feature of the new liberalised landscape across the world. Nonetheless, the level of concentration found in South Africa stands out when compared to other middle income countries, such as Mexico or Turkey, where the level of concentration is high – in Mexico, the same level of concentration of assets has to be enlarged to the six major financial groups and in Turkey to the top 10 banks (Marois, 2011). This level of concentration has brought about few gains in terms of reduced interest rates yields for banks, as might be expected to have occurred as a consequence of enhanced liberalisation. Indeed, according to Gilbert et al (2009), despite reduced yields in commercial (investment) banking, retail yields actually rose after the banking reforms of the 1990s.

A more convincing rationale for the liberalisation of the financial system than the fostering of competition and efficiency is to be found in the domestic pressure for international economic integration. After the general foreign disinvestment of the 1980s, external account deficits caused by economic isolation and the fall in the price of gold and other commodities, along with the devaluation of the rand by 50% between 1983 and 1990 (Singleton and Verhoef, 2010), pushed the South African state to try to revitalize the economy by promoting foreign capital inflows and allowing domestic corporations to operate abroad. Liberalisation and the parallel democratization, in compliance with the standards of developed countries, were mandatory in order to achieve these aims. Banks, now subjected to the same supervision standards (determined by the Basle agreements) as international banks and operating in a competitive environment with foreign players, played a pivotal role in this process: they helped South African capital into its new international placements and provided the financial sophistication required to compete successfully in the international arena. Moreover, they benefitted from the large liquidity of international capital markets, which enabled the very substantial increase in capital flows into the South African economy during the period 2004-2008.

From the early 1990s, the regulatory environment and history of banks in South Africa seemed to be favourable to the financialisation of the banking sector. This was facilitated by the adoption of the new rules for international banking on the part of South

African banks, and of the South African economy more generally, which favoured the convergence of bank practices and norms vis-à-vis their financialised counterparts. However, liberalisation and deregulation should not be understood as an exclusive consequence of external demands. The particular history and position of the South Africa economy prior to end of the apartheid regime, namely its economic isolation, low levels of investment and low growth rates, alongside the uneven and combined character of an economy based on capital-intensive sectors in which a large share of the population was excluded from the formal economy, posed endemic problems of surplus absorption and capital over-accumulation (Bond, 2006; Andrews, 2005). The emergence of a liberalised financial sector, with banks at its center, enabled the legal inflows and outflows of capital which reorganized the big industrial conglomerates and promoted their international expansion. Additionally, the booming financial sector accommodated the new black economic elite and paved the way for the acceleration of the circulation of capital through the expansion of credit markets, e.g. across the household sector.

5.4. Property transformations and the transnationalisation

As the historical trajectory of the South African banking sector shows, the transformations that this sector has undergone cannot be understood by referring only to their domestic operations. In addition to the changing nature of banks, one also has to take into account their ownership structures and their transnationalisation strategies, in order to better understand their place and role in the international financialised realm.

The four larger banks, which were a part of the big conglomerates of the Mineral-Energy Complex during the 1980s (Fine and Rustimjee, 1996), underwent significant changes in their ownership structure. With the unbundling of the big conglomerates during the 1990s, those which reinvented themselves as financial sector companies (see previous chapter)remained as significant shareholders in the banking sector, mainly through their life insurance companies (Jones, 2003). Old Mutual still holds the majority of the shares in Nedbank (over 50%), in addition to minority participations in ABSA (3%) and in the Standard Bank (3.3%).The Sanlam financial group has minority participations in the Standard Bank (1.7%) and ABSA (1.3%). Remgro holds 25% of FirstRand – the holding company of First

National Bank[57]. The close relation between banks and South African capital seems to have outlived the liberalisation of the sector and may explain the on-going close domestic relation between banks and the non-financial corporate sector, with the latter as both lenders and borrowers. This relation is matched by public involvement in banks through the Public Investment Corporation (PIC) – a public agency, now mainly funded by the Government Employee Pensions Fund, which manages public stakes in various private companies. The PIC holds around 10% of the shares in ABSA, 12% of FirstRand bank, 13% of Standard Bank and 7% in NedBank (recently holding 20% of its international venture Ecobank). Despite the private management model of the PIC, the state's influence upon the major banks is still apparent.

The second major transformation in the ownership of South African banks came with Black Economic Empowerment (BEE), and was materialised in the Financial Services Charter. Due to enter into effect between 2004 and 2014, this Charter has a long list of goals among which the promotion of black people as equity owners in the banking sector is one of the most important. It established that, by 2010, 25% of the shares of the entire financial sector should be owned by black people (Moyo and Rohan, 2006). Over the past ten years – i.e., sometime later than the original BEE deals within the non-financial sector –, a number of deals aimed at accommodating these demands were signed across the banking sector. In 2004, ABSA sold 10% of its equity to black-owned investment fund Botho Bonke, led by Tokyo Sexwale, a former ANC activist. Standard Bank and its subsidiary, Liberty Group, also sold 10% to staff and to an investment consortium led by Cyril Ramaphosa, former Secretary-general of the ANC, in an initiative named Tutuwa (Southall, 2008). Tutuwa shareholders now own 5.6% of the bank[58]. 7.6% of Nedbank is held by its BEE "Eyethu" scheme, while 10% of the FirstRand group is by BEE trusts. BEE has thus followed a similar model in the banking sector as in the case of non-financial corporations, with black-owned financial holdings acquiring minority stakes in banks, without there being any substantial changes to the governance of those banks.

The third major, and probably most relevant, change in the ownership of the South African banking sector was related to the entry of foreign banks, and more generally,

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[57]Information retrieved from the banks' websites.

foreign capital. Foreign banks in South Africa have a somewhat turbulent history. As already depicted, foreign capital played a central role in the South African banking system throughout its history, but the economic crisis of the 1980s and the international pressure against the apartheid regime led the major foreign banks present in the South African market to go away, leaving the banking system in the hands of domestic shareholders. However, with the banks act of 1990, the South African state tried to reverse this reality, by giving permission to foreign banks to establish themselves and allowing foreigners to acquire a maximum of 10% of the capital of domestic banks (a restriction that was subsequently relaxed) (Singleton and Verhoef, 2010). In 1995, there were 46 foreign representative offices and 4 foreign banks with local branches (SARB, 1996). By 2009, there were as many as 13 foreign branches, down from a peak of 15 in the first half of the 2000s (SARB, 2010). Despite their growing number, foreign bank branches did not succeed in challenging the four major South African banks that still dominate the retail market, not in profiting from the extraordinary bank expansion during the period 2004-2008. By the end of 2009, the local branches of foreign banks held just 5.5% of all banking assets, down from a peak of 8.4% in 2004[59]. This declining trend may be accounted for by their concentration in the corporate and investment banking sectors (Gidlow, 2008), which did not undergo as large an expansion as the retail banking did in the course of the 2000s.

The entry of foreign capital in the banking system seems to have been more effective through the takeover of shares in the big four banks. Indeed, the level of foreign ownership of South African banks has increased, having reached 47.5% of the nominal value of bank shares in December 2009 (SARB, 2010). Dispersed in small stakes over all listed South African banks, two of them are now controlled by foreign capital. The Standard bank's single largest shareholder is the Industrial and Commercial Bank of China (20.1%, bought in 2008) while ABSA was taken over by Barclays Bank in 2005 (55.5% share). The two largest South African banks are now back in foreign hands. These international capital inflows have enabled banks to expand their balance sheets and their operations to new domestic credit markets. Nonetheless, the motivations behind these international acquisitions consist not only of the ability to access the South African market, but also of the will to take advantage of the growing networks that South African banks have been

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[59]Computed from the reported assets of foreign banks in SARB Annual reports and the total assets from the DA 900 converted (2004) and BA 900 (2009) returns.

developing across the continent (Gidlow, 2008). The refocusing of Standard Bank in the sub-Saharan African market (for example, it recently sold its assets in Argentina to the ICBC[60]), shows the intermediary role that these banks play in the expansion of the major international banks to less developed markets.

5.5. South African banks in foreign countries

In spite of the economic isolation that apartheid and the debt crisis entailed in the 1980s, South African banks were well placed to expand internationally. With the "1994 Banks Act", banks were authorized to establish offshore interests (Singleton and Verhoef, 2010), and this enabled a wave of acquisitions that lasted until the present day. During the 1990s, this expansion took place mostly either to core financial centers (Hong Kong, USA, London, Jersey Islands) or to such neighboring countries as Botswana, Mozambique and Zimbabwe, spurred on by the creation of the Southern Africa Development Community in 1995. In another cases, it seems that this expansion has followed the outward orientation of the non-financial private sector. Nonetheless, this expansion reached places as different and far away as India, Latin America, Turkey or Australia.

The international expansion was pursued by all the major four South African banks (ABSA, Standard Bank, Nedbank, First National Bank). During the course of the last decade, their focus was on the sub-Saharan African markets. This was very actively encouraged by the South African government, which was motivated by the banks' domestic dynamism. In 2002, Lesetja Kganyago, director-general in the Ministry of Finance, announced the intention of turning South Africa into a financial "hub especially focused on the needs and circumstances of the region, much in the same way that Singapore and Hong Kong cater for the capital needs of the Asian continent(…)" (in Bond, 2004: 146). This political goal has been embodied in the broader New Partnership for Africa's Development (NEPAD) in 2001, a South African initiative that aims at improving the integration of the continent's economies.

This process has been championed by the Standard Bank, which operates in 16 other African countries besides South Africa. Such expansion started within southern

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[60]http://www.businessweek.com/news/2011-08-05/icbc-pays-600-million-for-standard-bank-s-argentina-stakes.html

African neighbor countries as Namibia, Zimbabwe, Botswana, and recently progressed towards the rest of the continent. Assets sold in Argentina and Russia were compensated by recent acquisitions in Nigeria and Kenya. Nedbank either with direct operations or with its Ecobank partner has now commercial branches in 35 countries now holding being the largest banking network in Africa. ABSCA and the First National Bank are laggards in this process, being still concentrated Southern Africa region (Mozambique, Namibia, Botswana, Zambia, and Tanzania)[61].

As pointed by Singleton and Verhoef (2010) the pulling force for the internationalization was domestic and international deregulation and liberalization of the financial markets. Roberts and Mukonoweshuro (2005) point how the entry in the African markets was achieved mainly through the acquisition of either majority or minority stakes in existing banks, benefiting often from the privatizations that many of these countries started (e.g. the acquisition of Banco Austral in Mozambique and Tanzanian National Bank of commerce in Tanzania by ABSCA). The authors point other different motives that drove the expansion to these new markets: the existence of large reserves to invest externally; profitable market opportunities in these countries where ROE are on average higher than in well-developed ones; relationship with South African transnational corporations now present in these markets (following the client); and search for efficiency and scale economies. All these reasons for expansion focus on the locational advantages of South African banks in Africa and ownership advantages, thanks to its robustness and the domestic thrive they have enjoyed.

The authors also add the role of digital technologies in the regional expansion of the South African Banks. The rise of information technologies within the banking sector is here important to stress as it has enabled banks to increase their economies of scale. Initial large investments in these technologies are compensated by the large consumer base it now can reach (through new credit scoring techniques) and "hard" information database it can compile in order to statically assess credit risk (Lapavitsas and Dos Santos, 2008). Concentration and internationalization are therefore favored. South Africa has the most developed market in IT infrastructure[62] in Africa (Roberts and Mukonoweshuro, 2005). The

[61] Information retrieved from banks' websites.

[62] It is the country with more cell phone and internet users in the continent.

scale of the internal market coupled with the sophistication of the South African banking system enabled these banks to gain competitive advantage in the use of IT when compared with other African banks. Nonetheless, contrary to what some accounts of financial internationalization argue where technological variable are understood as the main “independent” driving force (Cerny, 1994), the regional bias of South African banks show that if IT is an important factor in bank foreign entry, the historical, social and institutional framework within these banks operate is still important. The geographical embeddedness of South African banks shows therefore the salience on how these processes vary across the globe and are dependent on the international power relations present in each geographical and institutional setting.

5.6. Conclusion: banks as pivotal institutions of the South African economy

This chapter has shown that the mainstream theoretical approaches are ill-equipped to analyze the evolution and role of the contemporary banking sector. In the case of South African banks, the problems with the adequacy of mainstream economic theory are in fact intensified. As is the case for developed countries, mainstream neoclassical theory is at pains to explain the growth in size of this sector in newly liberalized and deregulated environment where markets should progressively replace financial intermediaries. Declining transaction costs and information asymmetries from liberalisation and deregulation, in addition to the information technologies boom, instead of producing a more competitive environment with more market players and a more relevant role of markets at the expense of firms, have led, in the South African case, to a growing and more concentrated financial sector. The rise of equity and debt markets took place alongside to the increase in the scale of banks, with the latter arguably driving the former. The “enhanced efficiency in the allocation of investment” argument, which constitutes neoclassical theory’s rationale for the existence of banks, is also very hard to identify in this context. Despite the overall increase in investment in the late 2000s, in which banking credit played an important role, the growth of the banking sector has by far outpaced the rest of the economy, thus constituting one of the main drivers of economic growth. Hence, despite the fact that the banking sector has played an important role in boosting investment, it can hardly be argued that capital allocation efficiency has increased, given that more resources seem to be needed to allocate proportionally lower amounts of investment in the rest of the economy.

By contrast, political economy approaches to the banking sector prove much more suitable for analyzing the trajectory of South African banks. They provide a more institutional and historical account of the evolution of contemporary banking, which allows for a better understanding both of the banking sector in the context of financialisation in general and of the variations and specificities that characterise different geographical and socio-economic settings, such as South Africa. In the case of many developing countries, these specificities include the role played by foreign capital inflows in newly liberalized environments (Painceira, 2010) as well as the impact of high interest rates (Becker et al, 2011), which lead to the process of financialisation being centered in the banking sector – features which are clearly visible in the South African case. However, the South African case is also characterized by a number of peculiar features, including in terms of the effects of capital inflows upon investment and economic growth, as previously discussed in chapter 3, or as regards the continuing reliance of South African corporations on banking finance, as discussed in chapter 4.

The neoliberal financial liberalisation and deregulation reforms present from the early 1980s in the most developed countries were started in South Africa during the final years of the apartheid regime. Their pinnacle was nonetheless reached already in the democratic period, with the adoption of the "Growth, Employment and Redistribution" (GEAR) program by the ANC-led government to replace their previous "Reconstruction and Development" developmental program. However, the role of public policy should not be overstressed[63] in this context, nor regarded as independent of the international political economy of capitalism during the course of the last few decades. The unbundling of the South African conglomerates made it possible for new shareholders to come in, thus accommodating the interests of the new "black" domestic elite. South African banks took advantage of capital inflows to expand domestically and, by maintaining their close ties to the South African elite – both the private and public sector (through the PIC) -, repositioned themselves internationally, primarily by expanding across the African continent (where it enjoys cultural and political advantages and benefits from its maturity compared to the recently liberalized new environment where it operates). The robustness of the sector and its strategic place at the international level eventually led to the entry of foreign capital –

[63] The determinant role of public policy has also been highlighted in the context of financialisation in developed countries (see Helleiner, 1994).

both returning British capital and new Chinese capital. The increasing integration of the world economy provided the opportunities and incentives for South Africa to comply with international liberalisation norms and practices, thereby escaping the economic isolation and stagnation that characterized its economy during the 1980s. Although banks have remained highly concentrated around the big four institutions that have dominated this sector for decades, they have become independent from the big conglomerates and affirmed themselves as the most dynamic institutions in the economy.

The specific effects of liberalisation and deregulation upon the South African banks and the latter's extraverted strategy are features that are shared with the global banks of advanced countries. However, such preliminary historical analysis, being of paramount importance to understand the emergence of financialisation, should not point to straightforward identification of it in this sector. Research on financialisation needs to go beyond its institutional framing and look at the content of what financialised banks do. The question of whether these banks have followed their developed country counterparts' financialised behavior in their domestic funding and lending relations with the other sectors of the economy, still remains largely open and unanswered. The empirical examination of those domestic trends constitutes the object of the next chapter.

6. Financialisation in South African banks: an empirical assement

6.1. Introduction

Having presented the theoretical framework which shall be mobilised to address the issue of the financialisation of the banking sector, and provided an institutional and historical overview of this sector in the South African case, in this chapter I aim to empirically test the extent to which South Africa's banking sector has been undergoing the aforementioned process of financialisation.

As was referred in the previous chapter, South African banks went through profound transformations through the liberalisation and transnationalisation of the sector. As in other emerging countries, banks remained at the center of the South African financial sector, contrary to more market-based financial sectors in countries such as the UK or the US. The modernisation described during the past twenty years, reflected itself in their transnationalisation and their increasing relevance in the South African economy, goes against neoclassical theoretical formulations where the liberalization of markets should result in more efficient, thus smaller and leaner, banks. In this chapter, I build upon the notion of financialised banks that goes beyond their growing scale relative to the rest of the economy and scrutinizes the recent changes on bank's business model and sources of income. By empirically analysing this sector, the aim is to identify the common and divergent features of the transformation of this particular banking sector, in its domestic environment, when compared to the abstract theoretical depiction of the financialised banks process as put forward by Lapavitsas (2009) and Dos Santos (2009). Undertaking this sort of assessment in contexts like South Africa is crucial in order to provide a more comprehensive theoretical framework for dealing with financialisation as a phenomenon that transcends the developed world.

I start this empirical scrutinity with a broad assessment of banks, by drawing upon the popular definitions of financialisation which assert the rising relevance of the financial sphere (Epstein, 2006) or which, as in Krippner (2011), "refer to the growing importance of financial activities as a source of profits in the economy" (2011: 27). By contrast to this latter author, in this chapter I do not seek to assess the share of financial profits relative to non-financial profits[64], or of financial assets relative to non-financial assets across the economy. Instead, I seek to circumvent the ontological discussions around financial profits and assets, as well as the methodological problems that their empirical measurement gives rise to, by focusing on assessing the banks' increasing size, income and profitability relative to the financial sector and to the economy as a whole. This approach suffices to demonstrate the validity, in this particular context,of the general concepts of financialisation concepts, while highlighting the pivotal role that banks have played in the South African financial system (thus vindicating the sectoral choice of banking undertaken in this chapter).

This assessment shall have a complementary character with regard to the subsequent test, to be undertaken further on in this chapter, of financialisation in more subtantive sense. In the present instace, I shall draw on general aggregated statistical data on the banking sector, including its weight relative to GDP, its income relative to GDP, its ROE and its ROA, retrieved from various "Bank Annual Reports" published by the South African Reserve Bank (SARB), as well as from the aggregated monthly balance sheet and the income statements returns of South African banks made available by the SARB.

These standard comparative indicators are complemented by the flow of funds data for "Other monetary Institutions" – which comprises banks - provided by the SARB national financial account. Flow of funds data provides a year-to-year flows of bank liabilities and assets. By aggregating and consolidating these flows, it is possible to analyse the sector's lending/borrowing position in relation to the rest of the economy throughout the post-apartheid period, as well as its relative importance in total and financial flows. The rising importance of banks in the South African economy in the allocation of capital will thus become apparent. In addition, the gross analysis of the FoF data will allow for a

[64]See Lapavitsas and Levina (2011) for a thorough discussion on the analytical difficulties such distinction poses.

preliminary assessment of the scale and category composition of the instruments employed both as a source and use of funds._This preliminary assessment of the uses and sources of flow of flows in the banking sector will allow an evaluation of the changes in the South African banks business model, identifying similarities and differences from the concept of financialised banks presented in the previous chapter. For example, bank's turn to households can be identified in the form of rising mortgage lending and the importance of finance-to-finance funding can be partially pin pointed by the relative relevance of debt securities as a funding source.

I will test four different assertions concerning the composition of assets and liabilities and the various income sources for the post-apartheid period: 1) the rising importance of finance-to-finance funding; 2) the increasing turn of banking lending towards households; 3) increasing income from households; 4) the increase in income from financial market mediation activities for banks. All of these four assertions were originally put forth by the aforementioned authors with reference to the case of developed countries.

Our empirical scrutiny offers three original contributions. First, I provide an assessment of whether financialised banks are limited to a small number of (developed) countries, or whether it is a global phenomenon that also concerns middle-income countries with sophisticated banking sectors such as South Africa. Secondly, in light of the specific trajectory of the South African banking sector, I provide a set of analytical insights that contribute to more robust and comprehensive understanding of the phenomenon of the financialisation of the banking sector, by taking into account the semi-peripheral nature of middle-income countries. Finally, a third contribution consists of furthering the knowledge and understanding of the South African economy. By drawing on some of the most recent contributions made in the domain of financialisation, the analysis that follows contributes to a better understanding of the political economy of post-apartheid South Africa and, in particular, of one of the main sectors driving its recent growth dynamism.

In order to test the financialised bank hypothesis, I draw on descriptive statistics of flow of funds and the banks'balance sheets, namely in terms of thecomposition of their assets and liabilities to the various sectors[65]. Encompassing liabilities makes it possible to

[65]Previous analysis of bank financialisation as in Lapavitsas and Powell (2013) do not provide an analysis of the bank's balance sheet liabilities as they find difficult to have comparable data on its

undertake a more comprehensive analysis of the sources of funding, and thereby to test the rising finance-to-finance hypothesis. Additionally, this has the advantage of providing complementary data on sources of funding other than finance - including, in particular, the foreign sector, given that capital inflows have played a major role in the South African economy in recent years. In its turn, our second hypothesis (that households have been taking on an increasingly important role in terms of the allocation of lending) will be assessed not only through an assessment of the agreggate weight of household debt in the assets of banks, but also through a complementary decomposition of the various kinds of household debt incurred, so as to provide a more detailed analysis of the relationship between banks and households.

Aggregate balance sheets for the banking sector are provided by the South African Reserve Bank (SARB) on a monthly basis, and until 2007 these were based onthe DI 100 forms submitted by thebanks, which provided a detailed breakdown of the banks' assets and liabilities. From 2008 onwards, in order to comply with Basle II standards, the new BA 100 forms were adopted instead. Given that these new forms organise the banks' variousbalance sheet items in different ways, it becomes impossible to undertake a meaningful comparison of a number of items throughout these two periods.The DI 100 returns will therefore constitute our default option for analysing balance sheets, given that it is based on these forms that the SARB presents the official banking data for its Bank Annual Reports, in addition to the fact that the period until 2007 coincides with our focus on the evolution of the South African banking sector between the end of apartheid and the international financial crisis. Whenever coherent, however, the time span of the analysis will also encompass the crisis years of 2008 and 2009.

The SARB also provides data that allows for the institutional and maturity breakdown of balance sheet items (liabilities and assets) based on the BA 900 forms that banks have been required to report since 2008. The SARB has presented the conversion of previous returns for the 1994-2007 period (DI 900 forms), thus making it possible to undertake consistent and meaningful comparisons between the two periods. These data

composition by instrument and sector. The availability of data concerning not only instruments but sectors as the source of these liabilities in South Africa enables here a more comprehensive empirical approach, for instance, on the role of finance-to-finance funding for banks.

are very important in order to test our initial hypothesis, given the interest in assessing the patterns of borrowing and lending by the banking sector to and from the various sectors (which is far from clear based on a simple asset/liability item analysis). Nevertheless, this data source is beset by two problems: 1) small discrepancies - particularly for 1990s data - exist between the DI 100 and BA 900 for equivalent items[66]; 2) data are not available for several financial categories and sectoral breakdowns, particularly between 1994 and 2000. This latter problem is particularly salient in the case of the private (non-bank) financial sector, for which the available data for 1994-2007 makes it impossible to undertake any meaningful overall analysis of the sector.

The two final hypotheses regarding bank financialisation, namely concerning the increasing importance of income originating in households and infinancial market mediation, are tested following the Dos Santos' (2008) approach to banking in developed countries, by looking at the evolution of banks' non-interest income – particularly in the categories related to investment banking, such as"knowledge based fees" and "trading and own investment income" – and at interest income coming from those debt categories in which households account for an overwhelming share of the debts incurred: mortgage debt and credit card debt. Income data is taken from the SARB monthly DI 200 returns until 2007 given that, once again, there are problems of comparability with later years. The figures presented here consist of the sum total of the monthly agreggate bank reports for each year, in order to obtain comparable annual data.

Both our balance sheet and income statement analyses differ from those traditionally presented in the SARB Annual Bank reports and most the remaining literature on South African banks. By drawing on both the DI 900 and the converted BA 900 forms for the period starting in 1994, it is possible to analyse the evolution of borrowing and lending by sector, thus making it possible to test our hypothesis. A similar sectoral breakdown analysis is also provided herefore income statements, making it possible to distinguish between different household debt categories and income from securities investment and

[66]Nonetheless, in this section I shall draw upon both of these sources, given that they provide data on differentliabilities and assets that are complementary wih regard to our analysis. Since the BA 900 and DI 900 converted returns provide a useful breakdown of items, we shall often draw on them as well.A ll the annual data provided here correspond to the agreggate bank holdings in December of each year, and were last revised in February 2012[66].

trading, thereby overcoming the traditional aproach which only distinguishes between interest margins and income from fees as analytical categories.

6.2. The increasing relevance of the banking sector

6.2.1. Banks within the financial system

In this empirical analysis of the South African banking sector, I shall begin by highlighting the significant and increasing centrality of bankswithin the financial sector –by showing the rising share of the total net flow of funds that is channeled through banks.This is followed by a display of the increasing weight and income of this sector relative to the overall economy, as well asof its increasing profitability. Additionally, I also draw on gross flow of funds data in order to show the gross annual expansion of both the liabilities and assets of banks in abolute terms, and to put forth a preliminary analysis of flow composition.

By drawing on flow of funds financial national account[67] data, it is possible to assess the rising importance of the South African banking sector as a source of funds for the economy as a whole, as well as its centrality within the financial sector. Equation (1) indicates how the amount of net funding provided by the banking sector to the rest of the economy may be computed:

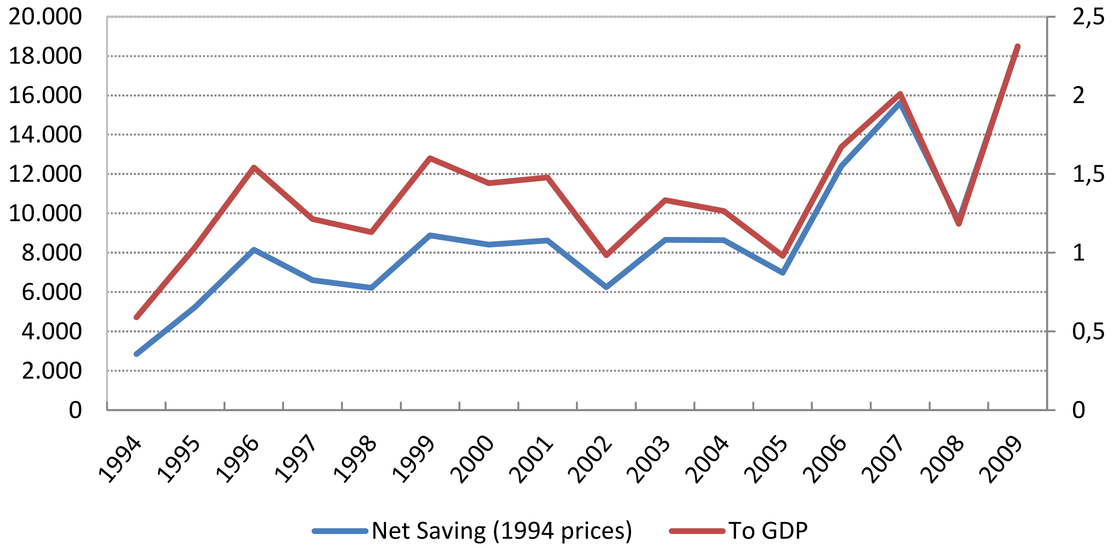
(1) Net Funding (Net saving of the sector) = Total Net incurrence of Assets (Uses of Funds) – Total Net Incurrence of Liabilities (Sources of Funds) – Consumption of Fixed Capital Formation + Gross Capital formation

Figure 6.1 shows the net funding of banks (Monetary Financial Institutions) at 1994 constant prices[68]. Two different periods of increase can be identified: a rise between 1994 and 1996, from 2846 million rand to 8156 million, and 6989 in 2005 to 18448 million rand in 2009. Its weight relative to GDP exhibits a similar trend, from 0.3% in 1994 to 2%in

[67]National Financial accounts, flow of funds, provide consolidated data on the flow of funds for Other Monetary Institutions, including all private banks, mutual banks, the Land Bank and Postbank. Flow of funds data is taken from the Tables published in 2010 by the SARB.

[68]Deflated using the GDP deflator for South Africa provided in the World Bank database. This is defined as the ratio of GDP in current local currency to GDP in constant local currency.

2007[69].The increasing importance of the banking sector is clearly illustrated by its increasing share of total financial intermediary asset flows – from less than a third in 1999 to around half of all flows in the late 2000s (Table 6.1). The expansion of the banking sector thus seems to have outpaced the growth of the rest of financial sector, indicating a smaller role for other non-monetary financial institutions, and thus vindicating the choice of this sector as the central object of the analysis in this empirical assessment.



Source: SARB, National Financial Account

Figure 6.1. Net financing extension (Mn rand, 1994 prices).

Table 6.1. Banking Flows in the economy.

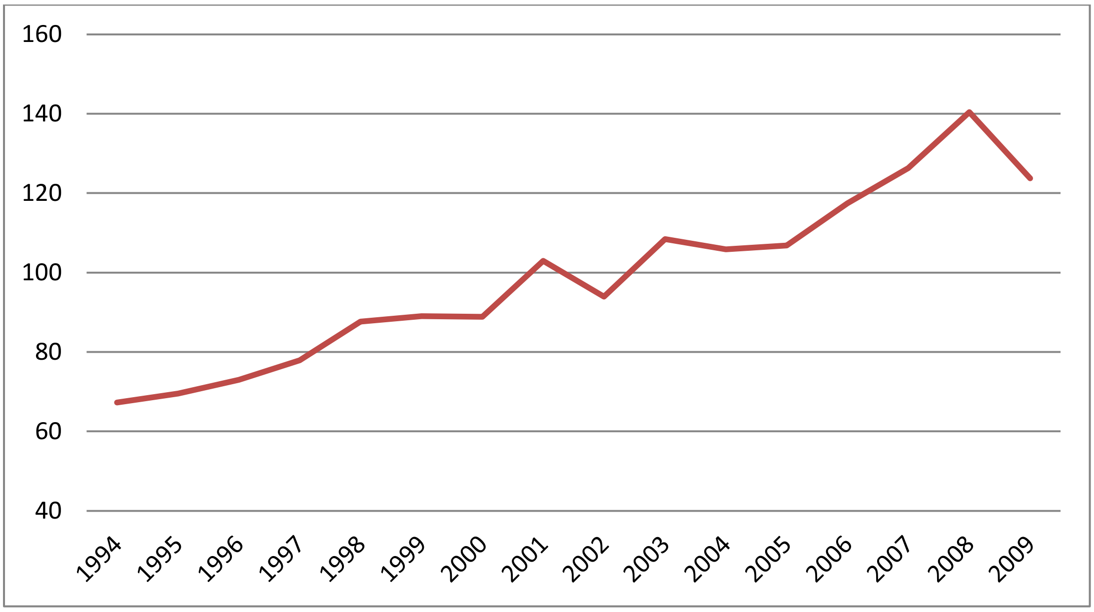
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Percentage of total asset flows	12.8	18	22.2	18.6	21.6	15	22	22	22	25	-2
Percentage of total financial intermediary asset flows	32.7	39.1	48	46.6	59.9	37	48	49	52	60	-9

Source: Notes to Flow of Funds (Zhello and Meyer, various years)

[69]The period of the international financial crisis should be treated with special caution. Contrary to what happened in 2008, 2009 saw a severe contraction of both gross liabilities and assets, with the former shrinking at a faster pace, thus resulting in what appears to be a strong recovery of bank sector net funding. See below for gross sources and uses.

6.2.2. Increasing weight and income relative to the overall economy

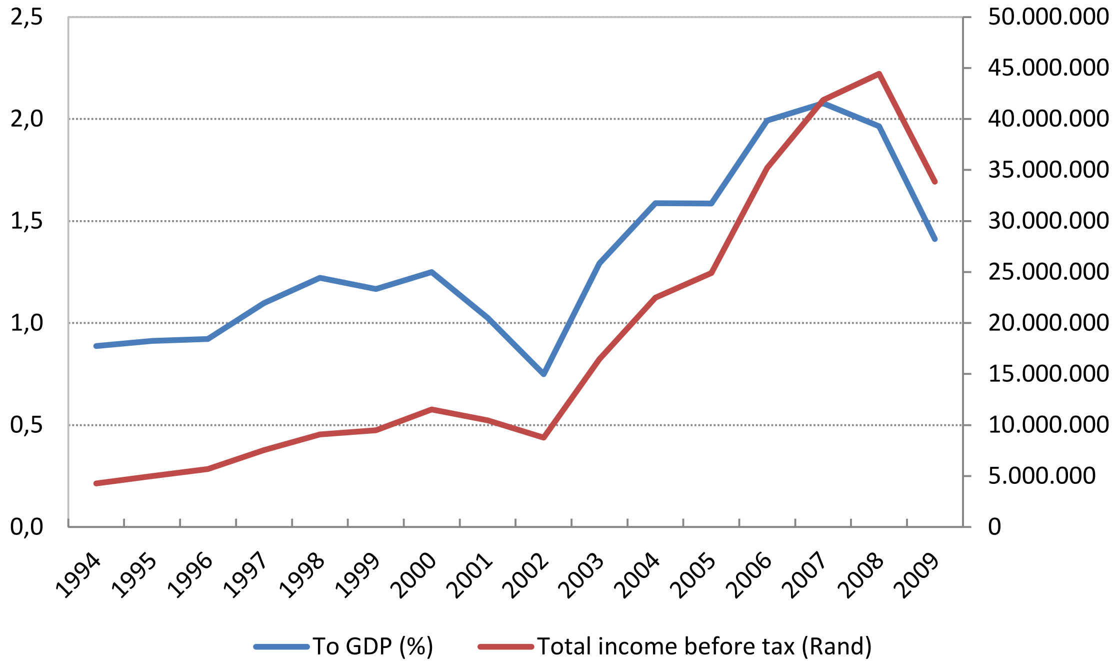
By the end of December 2009, South African banks held assets that amounted to a total of 2967 billion rand, or 123% of GDP. The total assets in their aggregate balance sheets, as a percentage of GDP, increased from 67.3% in 1994 to 140% in 2008 (Figure 6.2) – more than doubling their weight and thereby turning the banking sector into one of the most dynamic sectors in the South African economy as a whole. There were only three interruptions to this constant annual growth: 2002 (due to the domestic banking crisis), 2004 (when two banks were deregistered: SARB, 2004) and 2009 (international financial crisis).



Source: SARB DI 100 and BI 100 returns

Figure 6.2. Total Assets as % of GDP.

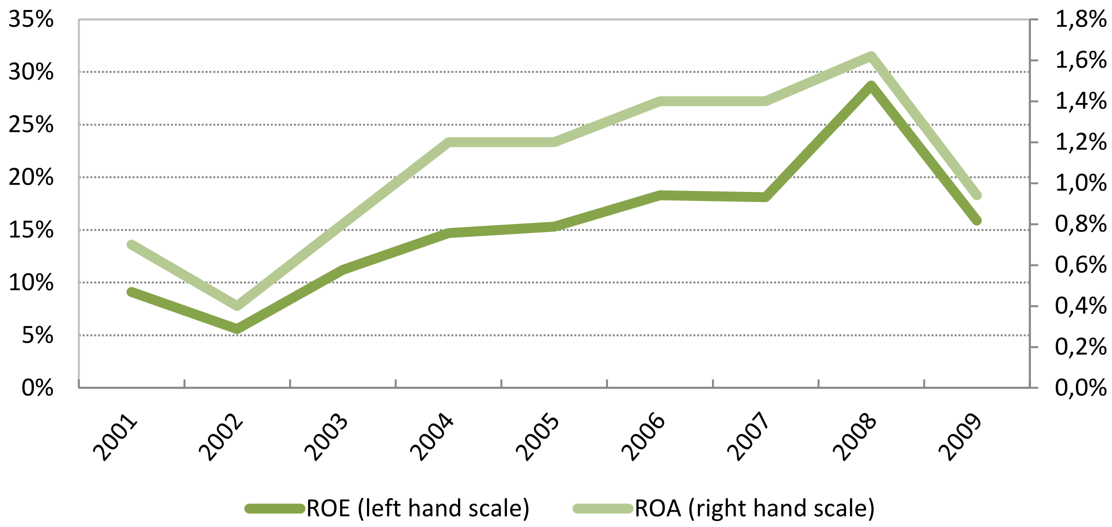
The banks' net income before taxes has also increased at a fast pace since 1994 – from 4 billion to 44 billion rand, once again outpacing GDP growth. Income before tax relative to GDP grew from 0.9% in 1994 to 2% in 2007 (1.4% in 2009) (Figure 6.2). South African banks have low Return-on-Equity (ROE) and Return-on-Assets (ROA) when compared with banks in developed countries, which can be explained by their relative high capital ratios[70]. However, these standard indicators of bank profitability have been rising throughout the last decade (Figure 6.3), showing that the banks' revenues have not only risen relative to the economy as a whole, but have in fact grown relative to the banks' own assets and equity. Despite increasing credit losses in 2009, the main ratios have remained positive, with ROE and ROA reaching 15.9% and 0.94%, respectively, which compares with ROE and ROA around 20% and 1.1% for the mid-2000s. In historical terms, credit losses are currently at considerably high levels, exceeding 40% of the net interest. However, these losses are compensated by the high margins charged on interest rates: between 3% and 4% for the period between 1994 and 2009 (SARB, various years).



Source: SARB.

Figure 6.3. Bank Net Income before tax.

[70] Capital ratios have stayed well above the Basel (I and II) requirements due to domestic regulation, reaching 14% for the capital adequacy ratio in 2009 (11% for the Tier 1 Capital adequacy ratio) (SARB 2009). In its turn, the level of financial leverage of South African banks has been declining, from 17.9 times in 2008 to 15.7 times in 2009 – well under the ratios of banks in more developed countries. However, as indicated above, this apparently low risk profile must be understood as reflecting the necessary cautions that banks must take in an uncertain environment characterized by high credit losses, as seem to be endemic in South Africa.



Source: SARB Annual Bank Reports

Figure 6.4. Return-on Equity (ROE) and Return on Assets (ROA).

6.2.3. Gross FoF

The gross Sources and Uses components of South Africa's Flow of funds tables - which are annual snapshots of the evolution of the banks' balance sheets - provide a clearer picture of the growth of the banking sector and a preliminary overview of their balance sheet composition. In the present analysis, FoF categories have been reorganised in order to allow for a clearer understanding of the main sources and uses[71]. Total net flows to bank liabilities grew from 47,285 million rand in 1994 to close to 150,000 million rand in 2008 (at 1994 prices), thus undergoing a295% increase. The expansion of the bank's balance sheets was made, on the liabilities side, mainly through the growth of monetary deposits for every year since 1994. This growth is particularly striking in two periods: between 1994 and 1997; and between 2004 and 2007, when the flow to monetary deposits increased from 56,000 million to 117,000 million rand at 1994 prices (Figure 6.5). The category "Amounts receivable", where derivatives are included, take second place amongst liabilities, particularly in 2003 (20 000 million rand) – even though accounting changes overstate their importance in that year (see SARB Annual Report 2004) - and 2008 (19 000 million rand).

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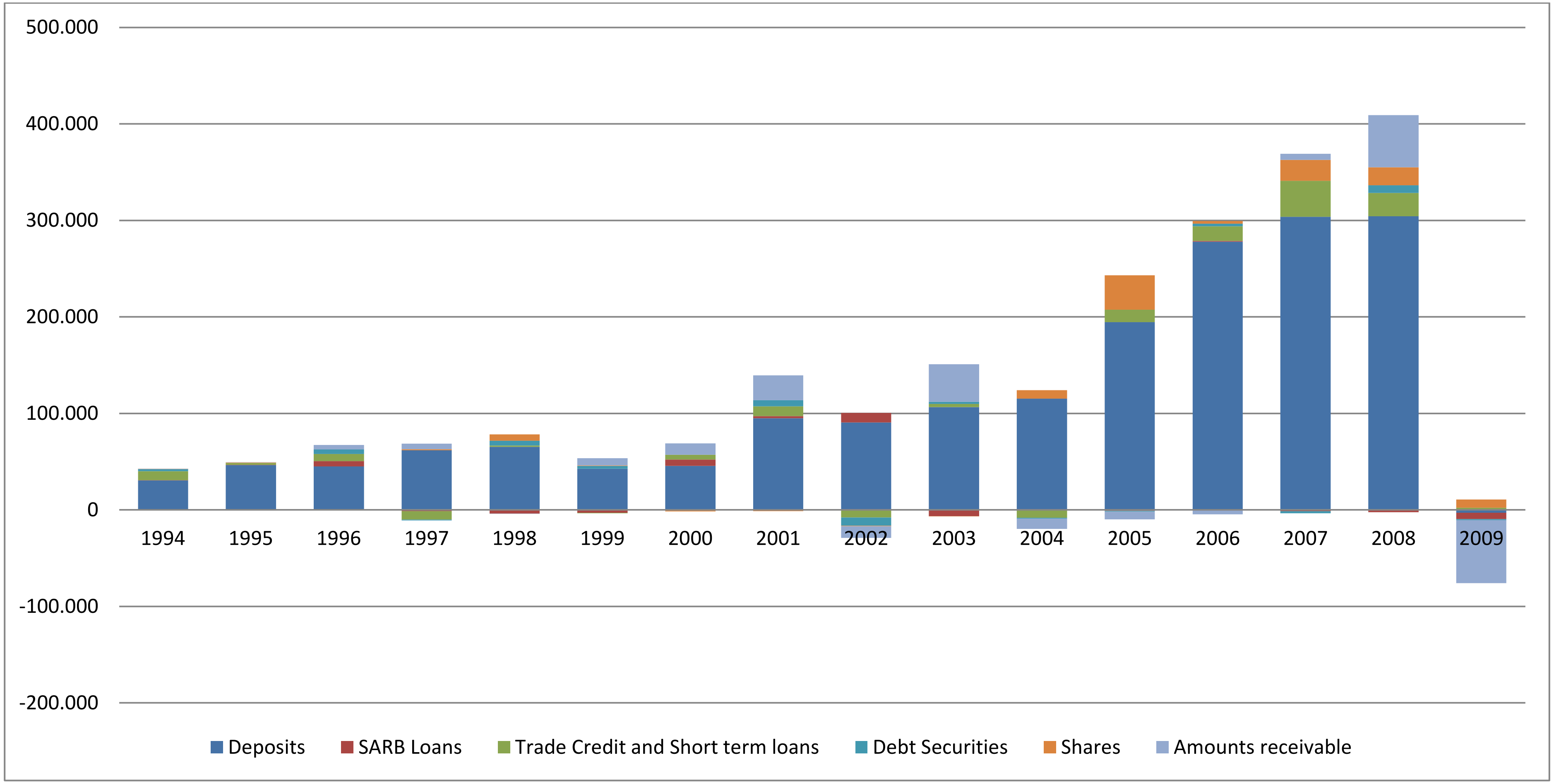
[71] Deposits are the aggregation of: Cash and demand monetary deposits; Short/medium term Monetary Deposits; Long-term monetary deposits). Private debt securities are the aggregation of: Other bills; Other loan stock and preference shares. Other deposits are the aggregation of: Deposits with other financial institutions; Deposits with other institutions.

The flow of funds gross data also illustrates the decline of the banks' balance sheets in 2009, as well as the role that derivatives seemingly played in this decline during the financial crisis (-65 000 million rand in the "Amounts receivable" item). The only two other items of significance for banks are the issuance of equity (shares) – 19,000 million in 2005, 8,000 million in 2007 and 18,000 million rand in 2008, which can be partially accounted for by capital inflows induced by the foreign take-over of domestic banks – and the resort to foreign short-term loans observed in that period as a consequence of the international turmoil that started in 2007.

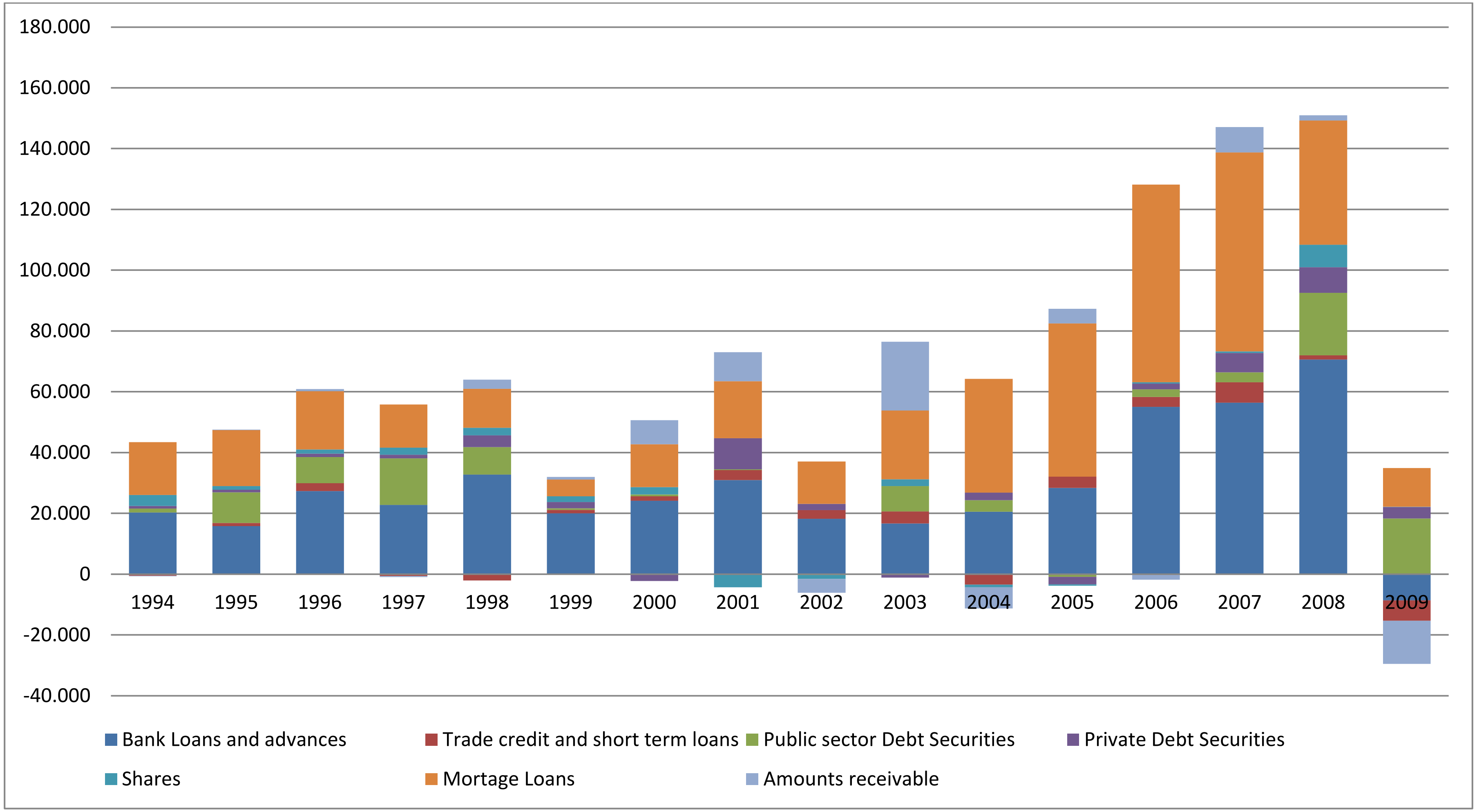


Source: SARB, National Financial Account

Figure 6.5. Flow of funds – Gross liabilities, selected items - (Mn rand) at 1994 prices.

On the assets side, flow of funds data provides an explicit picture of how bank assets increased during the 1994-2009 period (Figure 6.5). Again, the growth between 1994 and 2003 is dwarfed by the increase in assets during the 2004-2008 period, when the flow to assets rose from a total of 60,000 million rand to 148,000 million (at 1994 prices). The only year in which this flow was negative was 2009, when the international financial crisis exerted its greatest impact upon the South African economy. The two items that most contributed to this growth were “Mortgage Loans” and (other) “Bank loans and Advances”. The latter category was the single largest flow of funds category between 1994 and 2003 – between 11 and 51 % of all flows -, but it was overtaken by Mortgage in the period between 2004 and 2007 (which peaked at 172,000 million rand, compared to 148,000 million for other Bank Loans). There is thus preliminary evidence of a change in the lending pattern of banks which is indicative of changes in lending at the level of this sector as a whole, given that Mortgages typically concern households rather than any other sectors.

The holdings of private debt securities (a measure of the relevance of financial market mediation) was negligible during the 1990s and exhibited an erratic behaviour during the 2000s (negative flows for 2000, 2003, 2005), despite its rising importance in years of financial turmoil (2001, 2008-2009), which is indicative of relatively small, albeit rising, debt market. Public securities as a flow to assets exhibited the opposite behaviour. Their weight in total flows was significant during the 1990s, but it decreased in the 2000s until it once again became significant in 2008-2009. This behaviour is accounted for by the strict public fiscal policy aimed at reducing public debt after the latter’s fast increase in the period that preceded the end of apartheid. A reversal of this policy was only undertaken due to the recession caused by the international crisis in 2008-2009.



Source: SARB, National Financial Account

Figure 6.6. Flow of funds – Gross assets, selected items - (Mn rand) at 1994 prices.

6.2.4. Discussion

Our analysis clearly confirms the growth of the banking sector's balance sheets and income relative to the rest of economy: South African banks have grown in relative terms throughout the post-apartheid period. This expansion was especially significant during the second half of the 2000s and up until the onset of the international financial crisis – a period of rising inward capital flows. Income from banking activities has followed a similar path, thus reflecting the growth of financial profits relative to the rest of the economy. Moreover, the flow of funds data also demonstrate the quasi-exponential rise of bank assets and liabilities in the 1994-2009 period, revealing the main sources (deposits) and uses (mortgage and other bank loans, with the former rising in relative importance in the most recent years) of the funds, as well the pivotal role played in financial intermediation by this sector when compared with other financial institutions (insurance companies, retirement funds, unit trusts, public financial institutions, etc.).

Based on these data alone, the role of secondary financial markets is far from clear. Derivatives and private debt securities seem to play an increasingly important role for South African banks, but the role of wholesale funding and other money market instruments, as well as the importance of financial market mediation for South African banks are not easily discernible. Hence, even though it is clear that South African banks have profited significantly from the processes of liberalisation and deregulation that were mentioned in the previous chapter (thus corroborating the broader notions concerning the rising importance of the banking sector as part of the emergence of the South African financial sphere), these data prove insufficient for assessing the hypothesis of a process of financialisation in the sense in which was defined (which requires an examination of funding and lending trends as well as income sources during the post-apartheid period). Thus, it is necessary to draw on some additional data in order to test the adherence of this notion to the case of South African banks – specifically, data regarding the banks' balance sheets (in terms of their composition by sector and type of instruments) and sources of income.

6.3. Bank financialisation hypotheses: banks balance sheets – liabilities

In order to test our first bank financialisation hypotheses (concerning the rise of finance-to-finance funding (1) and the turn to household lending (2) in the South African case), I begin by analysing the evolution of the banks' balance sheets throughout the post-apartheid era and then discuss that evolution in light of the aforementioned hypothesis.

6.3.1. Item composition

The BI 900 and converted DI 900 returns confirm that deposits[72]constitute the overwhelming source of funding to banks, accounting for 79% of all liabilities at the end of December 2009 (Table 6.2). This high proportion of deposits has been a constant feature since the 1990s, at which time it reached between 80 and 90 % of all liabilities. During the 2000s, this item dropped to between 71% and 81%, but there is no clear declining trend given that the years of strong liability growth saw a 4% increase in deposits relative to total liabilities (from 74 to 78 % between 2004-2007). The extraordinary increase in liabilities during the 2004-2008 period was thus matched and even outpaced by the increase in deposits.

Table 6.2. Ratio of total deposits to total liabilities.

1994	1995	1996	1997	1998	1999	2000	2001
0.87	0.88	0.87	0.90	0.83	0.83	0.80	0.75

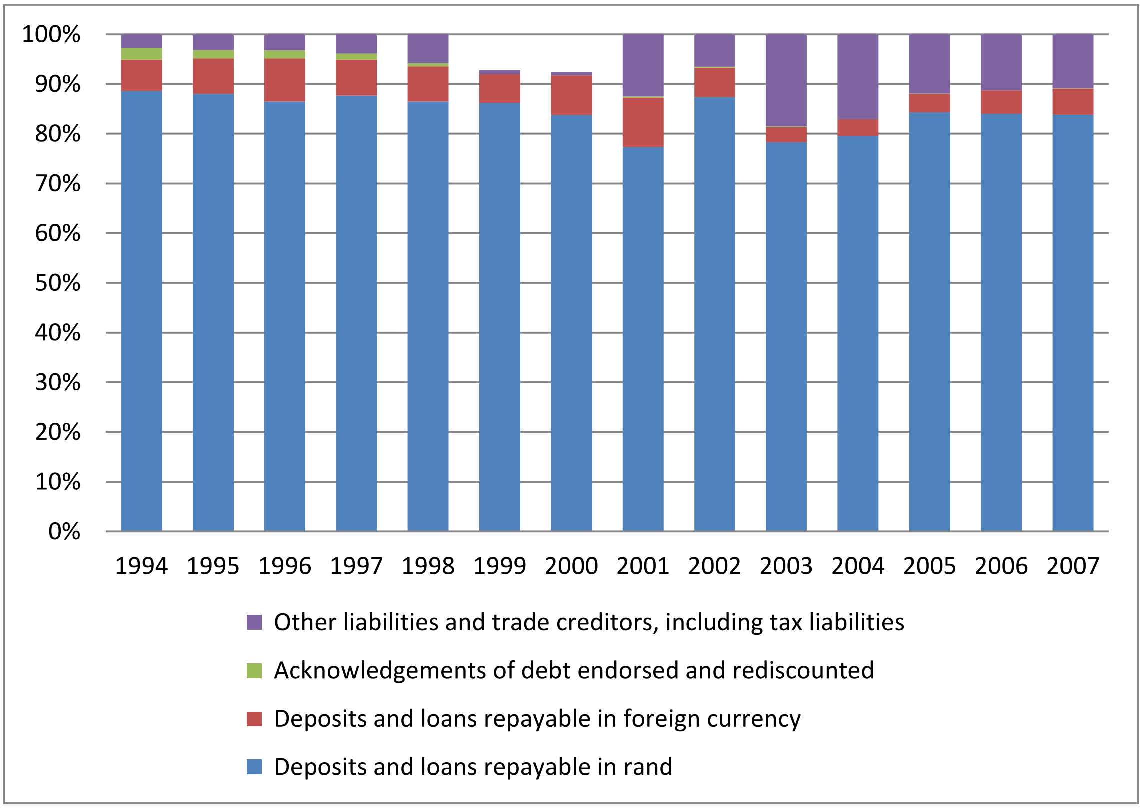
2002	2003	2004	2005	2006	2007	2008*	2009*
0.81	0.71	0.74	0.79	0.79	0.78	0.73	0.79

Source: SARB, computed from the BI 900 and converted DI 900

The DI 100 balance sheet returns for the 1994-2007 period make it possible to distinguish liabilities (not including equity) by instrument (Figure 6.7). This exercise generally confirms the importance of deposits (in this case, including repurchase agreements) as the overwhelming funding category. The DI 100 returns also provide data on the use of such debt securities as commercial paper, bills and promissory notes, and similar acknowledgements of debt included in the "Acknowledgements of debt" category.

[72]Total Deposits are only considered in the DI 900 converted to BI 900 forms where the category "Deposits" contrary to DI100 returns where we have "Deposits and loans repayable" in the same category. The values of the former are thus slightly lower than the latter, as they do not include repurchase agreements.

All of these seem to have marginal weight as funding liabilities. On the other hand, “Other liabilities and trade creditors” (including tax liabilities and derivatives), despite their small relative weight, show a growing presence in the banks’ balance sheets[73].Hence, the declining trend of the deposit to liability ratio for banks in the most developed countries (with the exception of Japan) identified by Lapavitsas and Powell (2013) does not seem to hold in the South African case.



Source: SARB DI 100 returns

Figure 6.7. Liabilities breakdown by instrument to total liabilities.

The “deposits” category can nonetheless be an elusive one, given that it includes both wholesale (through money market instruments) and retail deposits, which play different roles: the former constitute a vital element of the finance-to-finance funding as

[73]The growth of these funding instruments should be read with caution, however, given that an amendment in bank regulation in 2003 forced banks to report the gross figures in their trading books instead of the net figures (SARB, 2004), thus conferring greater weight in the balance sheets to these securities.

money markets are today a major source of bank funding in more developed countries. A more exhaustive analysis of deposit composition is thus required in order to test our first financialisation hypothesis, concerning the rising importance of finance-to-finance funding in the case of South African Banks.

Compared to wholesale deposits, retail deposits decreased in importance in two different periods (Table 6.3): during the banking turmoil of 2000-2002 – from 73.7% of all deposits in 2000 to 69.6%– and, most importantly, during the 2003-2007 period – from 73.7% to 69.4% in 2007 –, when South African banks experienced the largest spell of balance sheet growth in the post-apartheid era. In turn, there is evidence of the rising importance of money market instruments, not only during the period of domestic bank turmoil and declining capital inflows in 2000-02, but also during the swift recovery of bank growth in 2003-2007 (which led to a record high of 30.6 % of all rand deposits in 2007).

Table 6.3. Ratios to total Deposits.

	1994	1995	1996	1997	1998	1999	2000
Money Market Instruments[74]	0.260	0.248	0.242	0.256	0.269	0.252	0.263
Deposits[75]	0.740	0.752	0.758	0.744	0.731	0.748	0.737

	2001	2002	2003	2004	2005	2006	2007
Money Market Instruments[76]	0.289	0.304	0.263	0.268	0.270	0.284	0.306
Deposits[77]	0.711	0.696	0.737	0.732	0.730	0.716	0.694

Source: SARB DI 100 returns

The evolution of the various uses of wholesale deposit instruments, as reflected in the DI 100 returns, is far from clear, however, due to the financial turmoil and the changes in accounting and tax regulations in the early 2000s[78]. Moreover, the aggregated category "inter-bank funding"[79] does not provide any additional information on what the specific

[75] Includes: Interbank funding; Negotiable certificates of deposit (NCD's) issued; Repurchase Agreements and Other Funding liabilities (including balances due to the SARB).
[75]"Demand", "Notice and Fixed" and "Savings" deposits.
[75] Includes: Interbank funding; Negotiable certificates of deposit (NCD's) issued; Repurchase Agreements and Other Funding liabilities (including balances due to the SARB).
[77]"Demand", "Notice and Fixed" and "Savings" deposits.
[78]In 2004, negotiable certificates of deposit were exempted of tax duties (SARB, 2004), turning them into a more attractive financial instrument.
[79]Inter-bank repos are not included here.

financial instruments consist of (Figure 6.8). The almost symmetrical behaviour of inter-bank funding and NCDs issued to non-bank agents should thus be understood as reflecting a rising demand for NCDs on the part of non-bank institutions, rather than an overall decline in the use of these instruments. Nonetheless, if the focus is on the period of exponential liability rise in 2004-2007, a sustained increase in the use of repos, NCDs and inter-bank funding is clearly discernible. In addition to the aforementioned increasing relevance of derivatives and other liabilities, this proves the increase dependence of South African banks upon instruments other than the traditional retail sources of deposits.

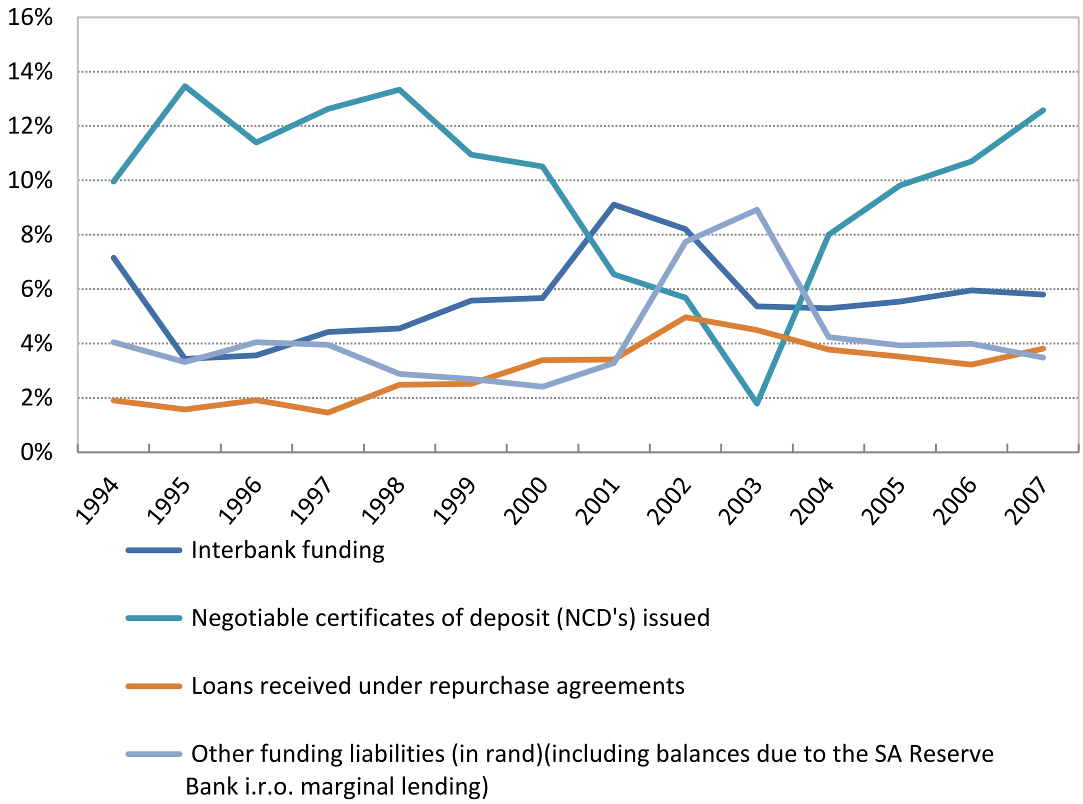


Figure 6.8. Money market instruments to total liabilities. Source: SARB DI 100 returns

6.3.2. Sector decomposition for deposits

Further evidence of the increase in finance-to-finance funding, as well as of the funding role of the other sectors of the economy, is provided by the breakdown of deposits by sector, which can be computed based on the BA 900 and converted DI 900 returns. With regard to deposits made by households, the available data for the sources of rand deposits[80] (from 2001 to 2009) shows a slight decrease in this sector's weight in total rand deposits over the 2001-2009 period- from 22% to 18% (Table 6.4). Even though households remain an important source of funding, the extraordinary growth of deposits during the second half of 2000s was clearly not due to this sector as much it was to other sectors. Another category whose relative weight exhibited a declining trend in this period consisted of "Other sources of deposits" (which includes various different sub-sectors, from public entities to the foreign sector): its share of total deposits dropped from 38% in 2001 to 24% in 2009. In their turn, non-financial corporations have proven a stable source of bank deposits, their weight in total deposits fluctuating between 17% and 22% throughout the period, which corroborates the conclusion, previously reached based on flow of funds data for 2005-2008, concerning the growth of deposits originating in this sector.

Table 6.4. Ratio of rand deposits to total assets by sector (2001-2009).

	2001	2002	2003	2004	2005	2006	2007	2008	2009
Households	0.22	0.21	0.20	0.19	0.18	0.17	0.16	0.17	0.18
Non-financial corporate sector	0.17	0.22	0.18	0.16	0.19	0.18	0.18	0.16	0.17
Monetary Institutions	0.04	0.11	0.08	0.07	0.06	0.07	0.06	0.07	0.07
Non-Bank Financial sector	0.20	0.19	0.22	0.26	0.26	0.28	0.31	0.31	0.33
Other sources	0.38	0.27	0.31	0.31	0.30	0.30	0.28	0.29	0.24

Source: Computed from the SARB BA 900 and converted DI 900 returns.

The only sector that exhibited a clear increasing trend, in relative terms, as a source of deposits was the non-bank financial sector, particularly in the period 2003- 2007 – from 20% in 2001 to 33% in 2009. This sector is the result of the aggregation of insurers, pension funds and the private financial corporate sector[81] (which includes Money-market unit trusts, Non-money market unit trusts, Fund-managers and "Other sources"). Table 4 shows the relative contribution of each of these sub-categories in the period 2001- 2009. It is clear that, despite the importance of insurance companies in the South African economy, it is within the private financial corporate sector that the main explanation for the relative

[80]Rand Deposits are used in this context because this category accounts for the overwhelming majority of deposits and because it is the only category for which a breakdown of the various institutional sources of funding provided. The 2001-2009 period refers to the years for which there is available data for all sectors.

[81]The disaggregated data for this sector is not presented since it is only available for the 2008-09 years. In those exceptional years "Fund managers" were the most relevant category.

increase in deposits originating in this sector is to be found –especially in the rising industry of unit (mutual) funds. Indeed, the BA 900 and converted DI 900 returns also make it possible to break down this sector's deposits into monetary deposits, Negotiable Certificates of Deposits (NCD) and Promissory notes (PN): what it shows is that the observed growth of deposits originating in the private financial corporate sector, from 12% to 28%, is accounted for by the growth of wholesale funding instruments held by these financial agents, from a negligible 3.5% (as a share of total deposits) to 13.6% (Table 6.5). Given the nature of these financial instruments, this confirms the increasing relevance of money markets.

Table 6.5. Rand deposits to total deposits for non-bank financial institutions.

	2001	2002	2003	2004	2005	2006	2007	2008	2009
Insurers	0.05	0.04	0.04	0.04	0.04	0.03	0.04	0.03	0.03
Pension funds	0.02	0.02	0.01	0.02	0.02	0.02	0.02	0.02	0.02
Private financial corporate sector	0.12	0.13	0.17	0.20	0.19	0.23	0.25	0.26	0.28

Source: Computed from the SARB BA 900 and converted DI 900 returns.

Table 6.6. Share of private financial corporate sector NCDs and PNs in total rand deposits.

2001	2002	2003	2004	2005	2006	2007	2008	2009
0.035	0.041	0.049	0.074	0.077	0.079	0.109	0.127	0.136

Source: Computed from the SARB BA 900 and converted DI 900 returns.

6.3.3. Foreign sector funding

Given that the international opening-up of the South African economy and banking sector has been one of the most relevant transformations to have affected this economy in recent times and that the behaviour of the banks seems to have been influenced by the inflow of foreign capital, it is important to dedicate special attention to the role of the foreign sector as a provider of direct funding to South African banks. Table 6.7 shows the ratio of aggregated foreign funding items to total liabilities[82]. Some clear breaks were found in this series: throughout the 1990s and until 2001, total foreign funding amounted to between 7.8% (1999) and 10.4% (1996) of total liabilities; in the early2000s, by contrast,

[82]Foreign funding is taken from the DI 900 returns until 2007 (the data is not comparable for subsequent years) as the sum of the following categories: Total Deposits of the foreign sector (rand and foreign); Foreign sector loans received under repurchase transactions; Foreign sector "Collaterised borrowing"; Other foreign sector funding.

funding originating externally dropped significantly, reaching a low of 3.2% during the domestic financial turmoil of the time. Since 2004 and until 2007, foreign funding increased once again, particularly in the form of short-term loans (see Chapter 3), and reached 6% of total liabilities in 2007.Despite its increasing relative weight in the bank's balance sheets in the last few years, the importance of direct funding by the foreign sector (equity is not considered here) has declined if the period 1994-2009 is considered as a whole. This rather surprising result (when the intense economic integration in the international sphere is taken into account) is probably accounted for a preference on the part of foreign capital inflows entering the country for taking the form of portfolio and foreign direct investments. In this case, the influence of the foreign sector upon South African banks thus made itself manifest, on the one hand, through the rising bank equity held by this sector (as was asserted in the previous chapter) and, on the other hand, through the rising availability of capital for domestic non-bank financial and non-financial agents which supported the expansion of the banks' balance sheets.

Table 6.7. Foreign sector funding (liabilities), Mn rand.

	1994	1995	1996	1997	1998	1999	2000
Total Foreign Funding	27033	32980	44210	46832	59755	53681	67153
Ratio to Total liabilities	0.087	0.091	0.104	0.096	0.097	0.079	0.087

	2001	2002	2003	2004	2005	2006	2007
Total Foreign Funding	88661	49948	42501	458969	64843	92613	144016
Ratio to Total liabilities	0.090	0.048	0.033	0.033	0.041	0.047	0.060

Source: Computed from the SARB converted DI 900 returns.

6.3.4. Banks balance sheets – assets

6.3.4.1. Instrument composition

The aggregated balance sheets of the South African banking sector show that "Total loans and advances to customers"[83]constitute the single largest asset category for these banks. This item exhibited a relatively stable trend throughout the 1994-2009 period,

[83]"Total loans and advances to customers" in DI 100 returns is reached from "Loans and Advances less "Specific provisions", in the BA 100 returns for 2008-09 it is the same category less "credit impairments". No institutional breakdown, based on the BA 900, is here provided as it is not possible to distinguish all the sectors presented as deposit sources (households, financial corporate sector, non-financial corporate sector and banks) as there is no complete data between 2001 and 2007.

accounting for between 71% and 83% of total assets (Table 6.8). In its turn, the relative importance of the banks' investment and trading positions[84] exhibited two different trends: between 1994 and 2003, its relative weight in total assets increased from a mere 7%in 1994 to 24% in 2003 (a figure which should be put into perspective by taking into account the accounting changes that entered into effect in that year). However, from between 2003 and 2009, the relative share of investment and trading positions declined once again to just 6%, reflecting both the effects of the international financial crisis and the declining weight of these positions relative the intense increase in total assets in 2004-2007.

Table 6.8. "Total Loans and Advances" and "Investment and trading positions" ratios to total assets.

	1994	1995	1996	1997	1998	1999	2000	2001
Total loans and advances	0.83	0.83	0.84	0.85	0.83	0.81	0.80	0.77
Investment and trading positions	0.07	0.08	0.07	0.07	0.09	0.10	0.13	0.16

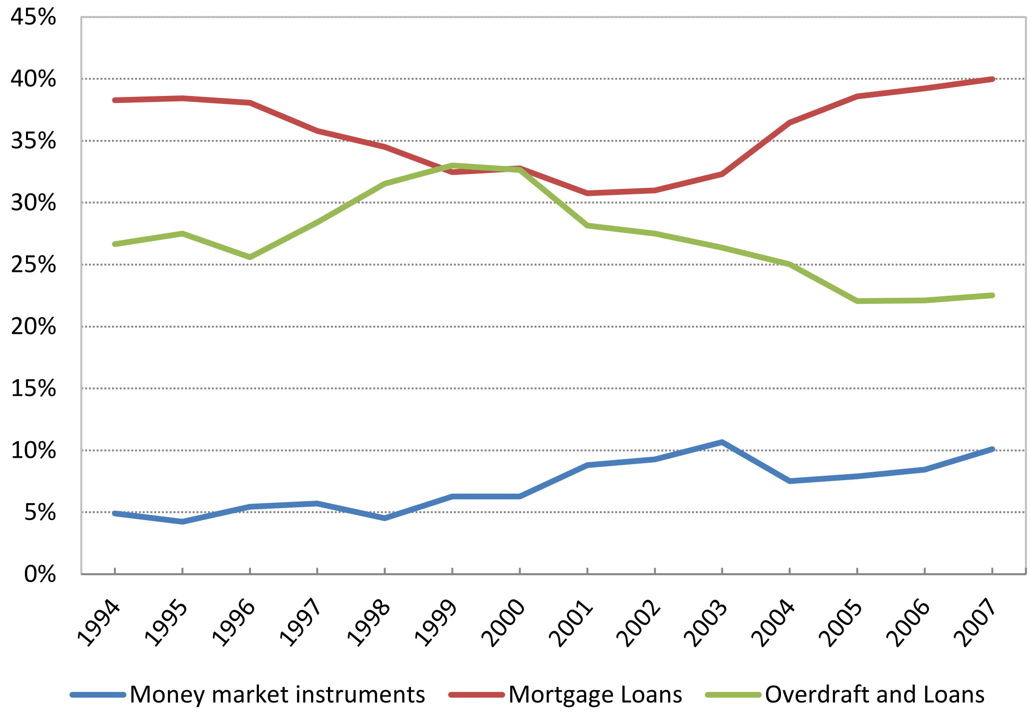
	2002	2003	2004	2005	2006	2007	2008*	2009*
Total loans and advances	0.80	0.71	0.73	0.80	0.83	0.83	0.72	0.74
Investment and trading positions	0.12	0.24	0.22	0.15	0.13	0.12	0.05	0.06

Source: SARB DI 100 and BA 100 returns for 2008-09

The breakdown of "Loans and advances" by instruments makes it possible to distinguish between three major items: Mortgage loans, other loans and overdrafts, and money market instruments (resulting of the aggregation of instruments made above). Mortgage loans and other loans and overdrafts exhibit a roughly symmetrical behaviour with regard to each other, with the relative weight of the former (latter) dropping (increasing) between the mid-1990s and the early 2000s, and then recovering (decreasing) during the period 2004-2007. However, what might be simplistically interpreted as mortgage loans resuming their previous importance (in terms of their share in total loans) must be analysed in the context of the quasi-exponential rise in total assets experienced in 2004-2007. When this is taken into account, it becomes clear that mortgage loans have risen significantly in the overall context of the South African economy and have been a major driver of the total growth in the banks' balance sheets that took place during the

[84] In the DI 100 it refers to" Investment and trading positions after mark to market adjustments where applicable" where "Specific provisions" are subtracted in the BA 100 it refers to "Investment and trading securities" where "Impairments" are subtracted.

2000s. In their turn, money market instruments have experienced a steady increase in their share of assets throughout the 1994-2007 period, doubling their share from around 5% to 10% over the period. This confirms the increasing importance of wholesale funding in the context of the South African economy (which was already highlighted in our analysis of liabilities).Comparing the South African case with those of more developed countries, it is found that the pattern of increasing lending to non-productive accumulation (usually associated with the FIRE – Finance, Insurance, Real Estate –sectors) observed in those countries also applies in South Africa – at least in the 2000s, when both mortgage (real-estate) and finance-to-finance lending increased.



Source: SARB, DI 100 returns.

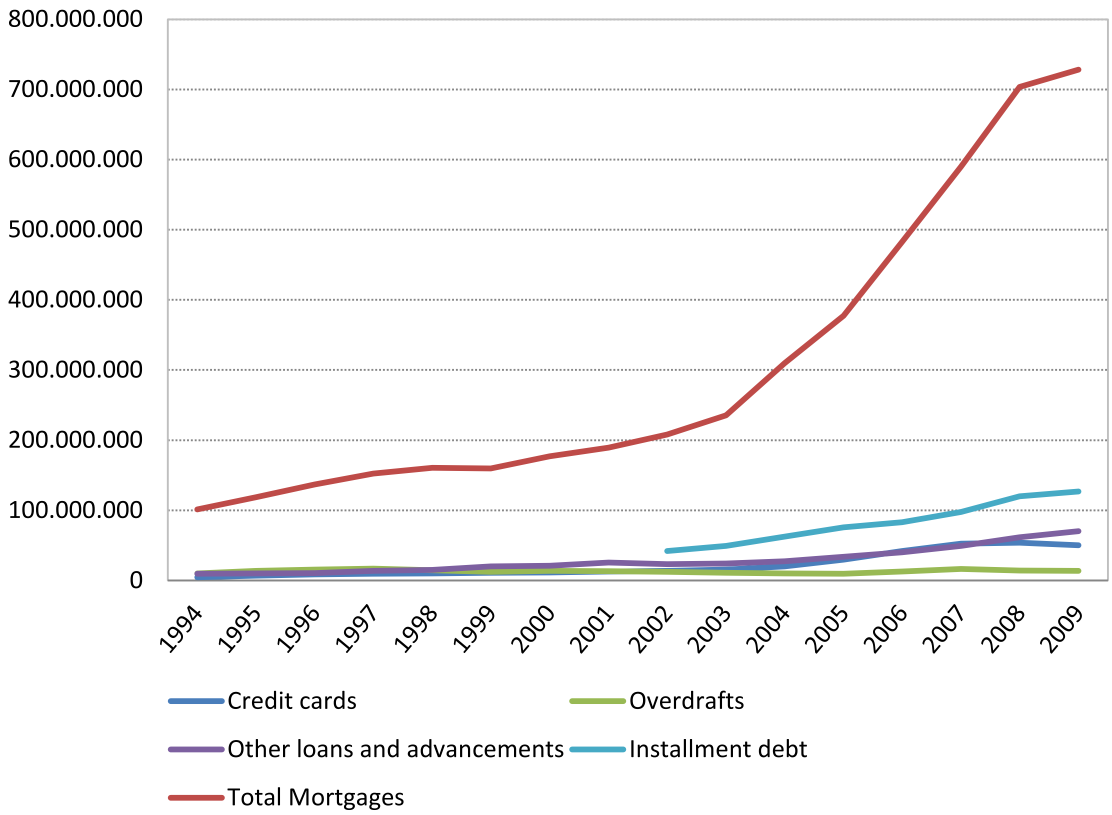
Figure 6.9 Breakdown of total loans and advances to total assets - selected items

6.3.5. Asset sector decomposition

Based on the DI 900 converted returns, it is difficult to undertake a clear decomposition of assets for all sectors in order to assess the relative weight of each sector. This is because there is no available data for specific breakdown assets for financial and non-financial private corporations. Still, from the available data provided in these returns makes it possible to undertake an assessment of one of the most important assertions made in the context of testing the notion of financialised banks in the South African context: increasing lending to households.

Four different categories of household debt are discernible[85]: Mortgage debt (sum total of Residential, Farm and Commercial mortgages held by households), Credit Card Debt, Overdrafts and Other loans and advancements. Figure 6.10 shows the total amount of debt held by the South African banking system for each of these household debt categories. There has been an increase in all categories of household debt, reaching a total of 989,000 million rand in 2009 compared to 125,000 million in 1994. This increase was particularly pronounced in the years 2004-08, when total household debt grew from 429,000 to 952,000 million rand. Household Mortgage debt is the single largest contributor to this increase: the value of household mortgage debt grew from 101,000 million rand in 1994 to 728,000 million in 2009, and experienced an especially steep increase between 2003 and 2008. Mortgage debt accounts for between 40 and 45% of total household debt throughout this period.

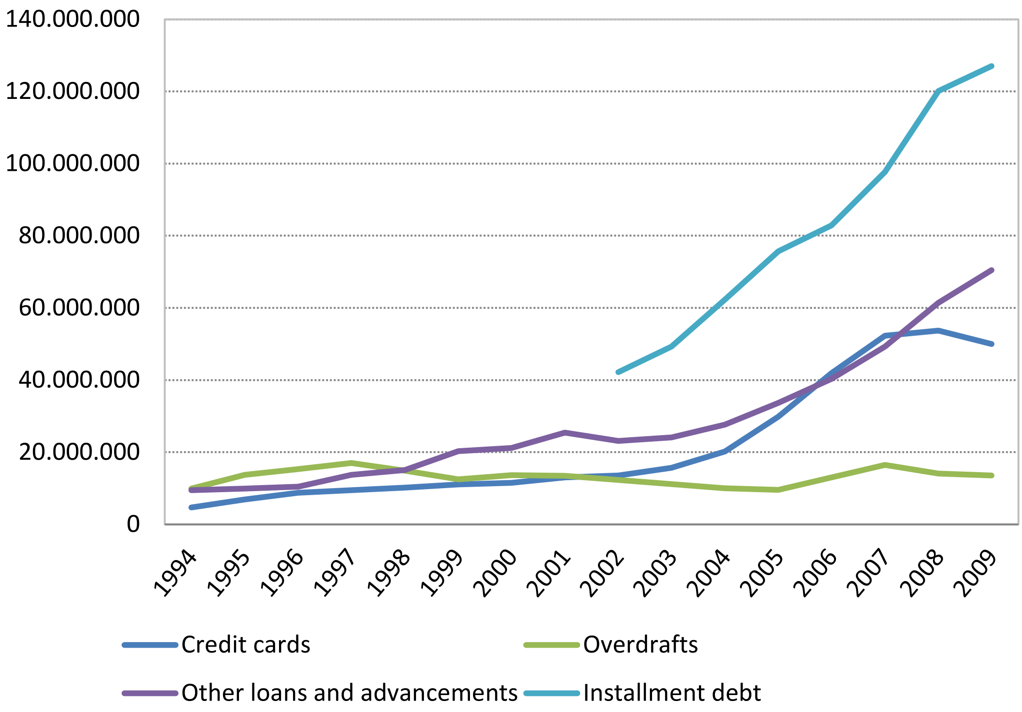
[85] From 1994 to 2001 there is no data available in DI 900 converted to BA 900 returns concerning households in the category of “Installment debtors, suspensive sales and leases”.



Source: SARB, DI 100 returns and BA 100 returns for 2008-09

Figure 6.10. Household debt by category (K rand)

All other debt categories with the exception of overdrafts (which, as expected, have relatively minor importance) exhibit a similar pattern of increase throughout this period, with especially pronounced growth occurring in the period 2004- 2008. “Installment debt” grew from 41,000 million in 2001 to 127,000 million rand in 2009; “Credit card” debt increased from a negligible 4,000 to 49,000 million rand in 2009; and “Other loans and Advancements” grew from 9,000 to 70,000 million rand. The exponential rise of household indebtedness (vis-à-vis the banking sector) is unambiguous in absolute terms, which confirms our initial hypothesis concerning an increasing lending to households.



Source: SARB, DI 900 converted and BA 900 returns.

Figure 6.11. Household debt (excluding mortgages, K rand)

Still, some caution needs to be exercised before interpreting the data presented above as confirming the hypothesis that banks have been increasingly turning away from corporations and other agents as recipients of their lending. From the analysis of the evolution of the ratio of household debt to total assets between 1994 and 2007 (Table 6.9), two distinct periods emerge. Between 1994 and 2001, this ratio dropped from 36.5% to 23%; from that year onwards, household debt as a whole regained its previous weight in the banks' liabilities, reaching 33.4% of the total. Given the weight of mortgage debt in total household debt, this evolution was largely determined by the evolution of this particular type of lending as a percentage of total assets (29.5% in 1994, 18% in 2001 and 23.1% in 2007). Other household debt categories, particularly credit card debt and other loans and advances, seem to have followed a similar U-shaped pattern, with only a small time gap: credit card debt dropped from 1.4% of total assets in 1994 to 1.1% in 2003 before recovering to 2.1% in 2007; while "Other loans and advancements" declined from 2.8%to 1.7%, in 2003, before increasing to 1.9% in 2007.

It is therefore found that the relationship between South Africa's banking and household sector, regardless of the extent to which it may have been influenced by the dynamics of any particular market (such as real estate) is characterised by a common pattern that applies to all debt categories. The recent increase in total household debt, which has taken place in the context of the period of fastest growth in the banks' assets, shows the extent to which the household sector has become the main driver of the banks' expansion. However, given the banks' continuing reliance on the corporate private sector (as shown in the previous chapter), one should not interpret this ongoing shift as a turning away from corporations on the part of banks, but rather as a consequence of the fact that the increase in the importance of the household sector as a recipient of banking credit has outpaced that of all the other sectors.

Table 6.9. Ratio of household debt to total assets.

	1994	1995	1996	1997	1998	1999	2000
Total Household debt	0.365	0.374	0.363	0.350	0.306	0.280	0.272
Mortgages	0.295	0.297	0.290	0.277	0.245	0.220	0.215
Credit cards	0.014	0.017	0.018	0.017	0.016	0.015	0.014
Overdrafts	0.029	0.034	0.032	0.031	0.023	0.017	0.017
Instalment debt[86]							
Other loans	0.028	0.025	0.022	0.025	0.023	0.028	0.026

	2001	2002	2003	2004	2005	2006	2007
Total Household debt	0.230	0.271	0.243	0.287	0.313	0.318	0.316
Mortgages	0.180	0.188	0.170	0.207	0.225	0.232	0.231
Credit cards	0.012	0.012	0.011	0.013	0.018	0.020	0.021
Overdrafts	0.013	0.011	0.008	0.007	0.006	0.006	0.006
Instalment debt[87]		0.038	0.036	0.042	0.045	0.040	0.038
Other loans	0.024	0.021	0.017	0.018	0.020	0.019	0.019

Source: SARB, DI 900 converted returns.

6.3.6. Bank financialisation hypothesis (1) and (2) discussion

The data presented thus far in this chapter shows that South African banks have followed their developed countries' counterparts when it comes to the latter's general tendency to grow relative to the economy as a whole. In the case of South Africa, this growth, in terms of both size and income, demonstrates the extent to which the banking sector has become one of the most dynamic sectors in the economy.

However, decisively assessing the two initial hypothesis entailed by the narrower concept of financialisation – rising finance-to-finance lending and an increasing turn

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[86] No available data from 1994 to 2000.
[87] No available data from 1994 to 2001.

towards households as credit recipients – proves more problematic. Our first hypothesis is confirmed by the analysis of both the liabilities and asset sides of the banks' balance sheets for the use of money markets (where mutual funds play a growing role). Nonetheless, the reliance on some other financial instruments, such as credit derivates or bonds, does not exhibit the same rising importance on both sides of the balance sheet. Moreover, "traditional" deposits from domestic non-financial corporations (profiting from the boom in international commodity prices and the consequent overall economic growth of the South African economy), as well as, to a lesser extent, deposits by households have continued to be resilient sources of funding.

Thus, the increase in finance-to-finance lending is indeed present in the South African case, but seems to be biased towards money markets instead of other financial instruments – and its growth has been modest when compared to that of other sources of funding. Its rising importance may be attributed to the dominance of banks in financial intermediation, the small scale of other financial markets and the volatility experienced in emerging countries, which pushes financial agents towards shorter term, safer securities that nevertheless benefit from relatively high interest rates (Eichengreen and Luengnaruemitchai, 2006).

Finally, the increase in finance-to-finance lending should not interpreted in isolation from the general rise in net foreign capital flows. As it was seen, the role of the banking sector as a direct recipient of these funds, albeit significant and increasing, is far from being the most significant in the SARB typology (banking sector, private non-banking sector, public authorities), the concomitant increase in the banks' balance sheets(particularly through wholesale funding during the 2000s), on the one hand, and in the short-term portfolio capital inflows, on the other, points to the other private sectors as an important indirect conduit of these inflows.

As regards to our second hypothesis (concerning an increasing turn by banks towards lending to households), our findings seem clearer. Real estate-related lending through mortgage loans (of which households constitute the overwhelming majority of recipients) did indeed increase very significantly, while total household debt has been rising in both absolute and relative terms throughout the 2000s. Even though the share of total household debt in 2007 was still below its level of 1994, there are increasing signs of a new relationship being established between banks and households, given that new categories of debt have experienced sustained increases throughout the 1994-2007 period and that mortgage debt has been the main driver of the recent exponential rise of bank assets. In any case, the hypothesis put forth by Dos Santos (2009), according to which contemporary financialised banking has moved away from its “traditional” role of taking deposits and lending to firms, does not seem to be fully corroborated in the case of South Africa.

The South African banking sector has undergone some significant changes in recent years) in the expansion of the banks’ balance sheets. These changes do not seem to have been motivated by corporations turning away from bank lending, but mostly by the fact that new significant sources of funding have become available to the banking sector. The changes in the banks’ lending patterns, most apparent in their increasing reliance upon households as credit recipients, reflects the search for new profitable credit outlets as a major ‘pull’ factor driving these changes. Whether or not banks derive an increasing share of their income from households, on the one hand, and from their investments and trading operations, as put forward in our two remaining hypothesis on the financialisation of the banking sector, thus takes on an added importance when it comes to assessing the overarching financialisation hypothesis.

6.4. Banks income analysis

6.4.1. Households Income

One of the foundational features of the adopted financialisation hypothesis consists of increasing lending to households. As it was concluded from our analysis of the balance sheets of South African banks, that has been the case in the South African context, too. However, that analysis did not enable us to undertake a detailed assessment of the importance of households as a source of income for the banking sector, given that the latter depends on the interest rate margins charged on the various categories of debt and on non-interest income –such as fees charged for banking transactions (withdrawals, foreign exchange fees, etc.). Thus, in the following pages I seek to assess the income aspect of the banks-households relationship by testing our financialisation hypothesis (3), namely that South African banks has been deriving an increasing share of its income from its operations with households. This hypothesis takes on special importance in the South African context given that, as was seen, non-financial corporations continue to be quite relevant loan recipients. Therefore, it is important to assess not only the hypothesis of rising income from operations with households in absolute terms, but also its growth relative to the total amount of debt held by the household sector – insofar as that would provide an alternative rationale for increasing lending to households (not so much as a consequence of a “turning away” from “traditional” creditors as reflecting the relative higher profitability of this market). The period considered in this analysis consists of 1994-2007, i.e. finishing prior to the onset of the global financial crisis of 2008-2009.

6.4.1.1. Interest income from households

Even though it is impossible to determine with absolute precision what the exact share of the banks’ revenue is that originates in households, an approximate picture can be provided by focusing on those debt categories in which households constitute the overwhelming majority of the debtors, such as mortgage debt and credit card debt. Throughout the period 1994-2007, households consistently held more than 85% of all mortgage debt and more than 90% of all credit card debt. These two categories provide complementary information on different aspects of the relationship between banks and households: while the former relates to a more traditional form of debt, involving the provision of collateral by households, the latter helps to shed light on an unsecured type of credit to households, which banks have been feeling increasingly confident to provide.

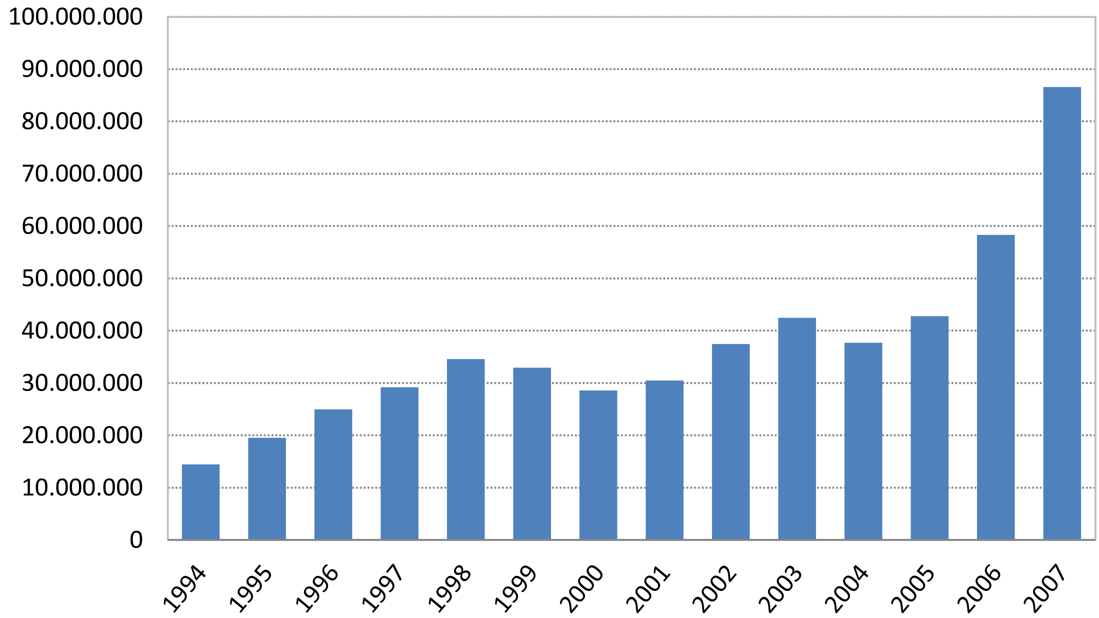


Figure 6.12. Mortgage loans interest revenue (K rand). Source: SARB, DI 200 returns.

Gross interest revenue from mortgages rose consistently between 1994 and 2007, from 14,400 million to 86,500 million rand. The greatest increases took place in 2006 and 2007, involving an increase from 47,000 million in 2005 to 86,500 million in 2007 (Figure

6.12). While interest income from mortgages followed a parallel path vis-à-vis the evolution of the real interest rate throughout most of the period under analysis, it decoupled from that other variable in 2005-07, reflecting a qualitative change in the role played by mortgages, insofar as the total income earned from this source became more dependent on the quantity of debt extended than on its price. This new development is confirmed by the share of mortgage interest income relative to total income: despite the declining interest rates of the 2000s, its share of total income increased in the years that preceded the international financial crisis (Table 6.10), from a record low of 25% in 2001 to 32% in 2007. Given this recent evolution, it is difficult not to conclude that households have taken on an increasingly important role as a source of income.

Table 6.10. Share of mortgage interest revenue to total income.

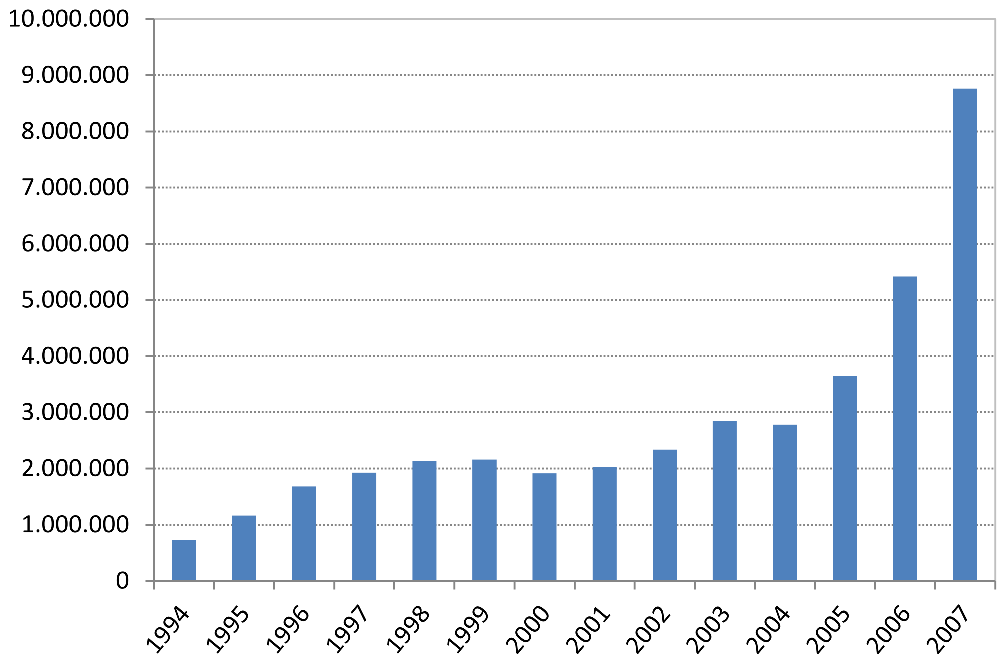
1994	1995	1996	1997	1998	1999	2000
0.366	0.368	0.363	0.352	0.322	0.297	0.274

2001	2002	2003	2004	2005	2006	2007
0.250	0.266	0.268	0.263	0.270	0.299	0.324

Source: SARB, Computed from DI 200 returns.

6.4.1.2. Credit card debt

Interest income from credit card debt exhibited a slightly different pattern. Even though it followed a pattern similar to mortgage debt as far as its absolute growth is concerned - from 731 million rand in 1994 to 8 billion in 2007 (Figure 6.13), the growth of its share in total income - from 1.8% in 1994 to 3.2% in 2007 (Table 6.11) – outpaced that of mortgage interest income over the same period. The relative income extracted from this market has also grown at a faster and more sustained rate (77 %) than the relative weight of this type of debt in the banks' balance sheets, as seen in the previous section (20% for the same period). This income evolution shows that, at least for this unsecured consumer loan market (in which interest rates are normally higher), profitability has risen as a consequence not only of an increase in the quantity of credit extended, but also of an increase in the income extracted from it. There is thus significant evidence of what is a qualitatively change, over the 1994-2007 period, in terms of how banks increasingly profit from household debt.



Source: SARB, DI 200 returns.

Figure 6.13. Credit-card interest revenue (K rand).

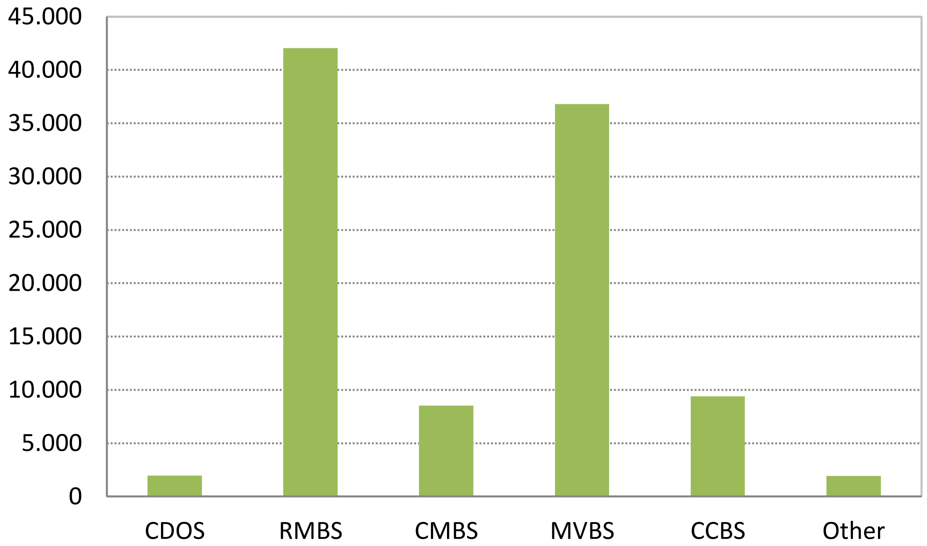
Table 6.11. Share of credit card income to total income.

1994	1995	1996	1997	1998	1999	2000
0.018	0.021	0.022	0.019	0.021	0.021	0.020

2001	2002	2003	2004	2005	2006	2007
0.018	0.016	0.017	0.018	0.022	0.027	0.032

Source: SARB, Computed from the DI 200 returns.

This qualitative turn in household finance becomes even more salient with the evolution of the debt derivatives market (despite its small size). Debt securitisation in South Africa was slow to take off in the 1990s, but grew throughout the 2000s and up until the world financial crisis, from 482 million rand in 2000 to a total of 25,2 billion 2007 (Moyo and Firer, 2008).Fostered by the Basel II standards, these new products were concentrated within the five major banks - Rand Merchant Bank (First Rand Bank), Investec Bank, Standard Bank, ABSA and Ned Bank -, and their growth considerably outpace that of the debt market. These issuances have covered all types of debt securities present in mature markets: Collaterised Debt Obligations (CDO), Residential Mortgage Backed Securities (RMBS), Commercial Mortgage Backed Securities (CMBS), Motor Vehicle Backed Securities (MVBS), etc. Despite the inexistence of sub-prime mortgage securities (Deloitte, 2007), most of these debt securities issuances have been concentrated in household debt, particularly Mortgage and Motor Vehicle debt (Figure 6.14), reflecting the adoption of the financial innovation instruments that were pioneered by developed country banks and which allowed for the expansion of credit through off-balance sheets vehicles for both domestic and off-shore investors. It should however be noted that this new trend, despite being further evidence of the importance of household debt, has still scarce relevance in banks' balance sheets.

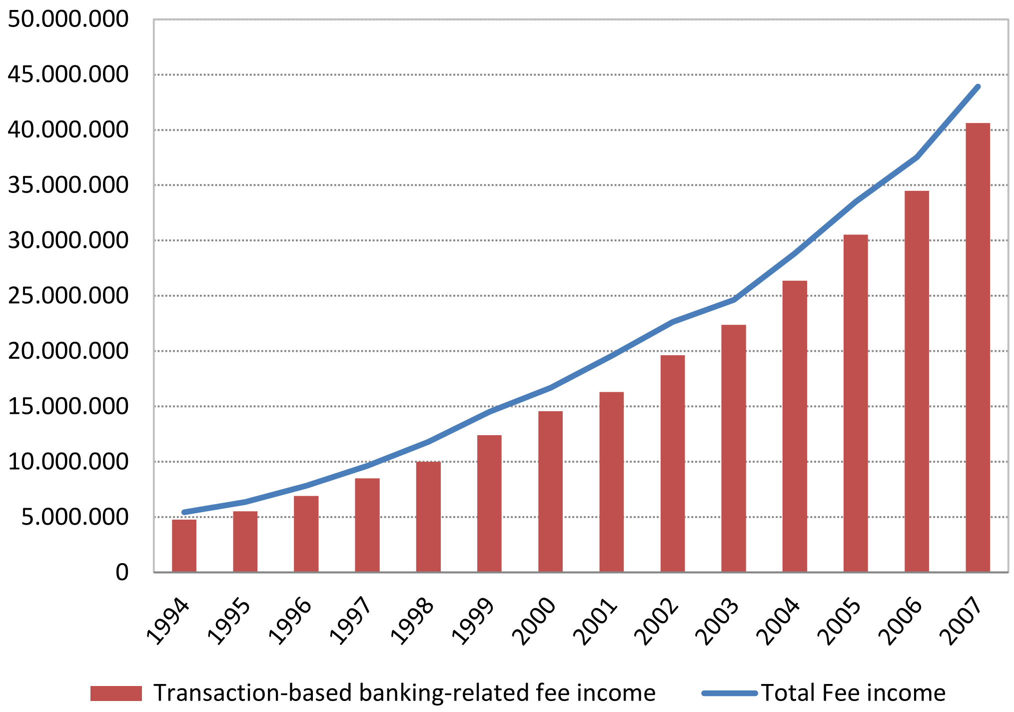


Source: Moyo and Firer (2008) from Johannesburg Stock Exchange data.

Figure 6.14. Total security issuance by classification 2000-07 (Mn rand).

6.4.1.3. Transaction fee income

As noted by Dos Santos (2009), the growing importance of household revenue for banks is far from being limited to interest revenue. In fact, one of the ways in which Dos Santos assesses banking revenue originating in households consists of examining the increase in non-interest income from fees charged for such bank operations as withdrawals, statements, foreign exchange, credit penalties, etc. Much of this fee income is charged to households as fees for money dealing activities and should be taken into account in this context.



Source: SARB, DI 200 returns.

Figure 6.15. Fee income (K rand).

Figure 6.15 shows the total amount of fees charged. Transaction fees account for an overwhelming share of this income, having grown exponentially from 4,000 million rand in 1994 to 40,000 billion in 2007. More significantly, the weight of these fees relative to total income has also been growing (Table 6.12), from between 8% and 10% in the late 1990s to 14.6% in 2007, after peaking at 18.6% in 2005.

Table 6.12. Ratio transaction fees to total income

1994	1995	1996	1997	1998	1999	2000
0.100	0.088	0.087	0.089	0.085	0.105	0.132

2001	2002	2003	2004	2005	2006	2007
0.139	0.135	0.138	0.178	0.186	0.168	0.146

Source: SARB, Computed from DI 200 returns.

This empirical assessment has been confirmed by the Competition Commission established in 2006 the fact that the four major banks control 96 % of all personal transaction account products enabled South African banks to charge for all transactions, contrary to what is the usual practice in more developed countries (Finmark, 2009). Research by Beck et al (2006) on the fee costs of banking services show that South Africa, despite having low requirements in terms of the amounts required to open and maintain current and savings accounts, has high relative costs when it comes to annual fees. The annual fee for holding a checking account was calculated as amounting to 2.13% of the annual GDP per capita (compared an average of 2.43% amongst all countries surveyed), while that for a savings account amounts to 0.91% of GDP per capita (which compares to a median of 0% and an average of 0.38% among the countries in the sample).

6.4.1.4. Discussion

Financialisation hypothesis (3), concerning increasing income coming from households, is corroborated by the data, insofar as the banks' revenue originating in the household sector has increased in its various forms. The importance of households as a source of income has even been increasing at a faster pace than their share of total debt. Interest income from mortgages has already reached the level of the mid-1990s, while credit card interest – a new market characterized by higher interest rate margins - has steadily grown since 1994. The growth of household debt in the banks' balance sheets throughout the 2000s cannot be simply interpreted as a mere recovery to the levels and importance of the mid-1990s. Financial innovation in the form of debt securitisation seems to be especially aimed at this particular sector, thus confirming, if not a quantitative change in lending behavior, then a more sophisticated interest in dealing with households on the part of banks. This new relationship between the banks and the households, with the latter taking on increasing importance as a source of income, is confirmed by the rise of bank transaction fees income (a relatively less regulated way for banks to charge their customers).

The only caveat in our analysis – the relatively short time span in which this new behaviour is apparent (limited to the second half of the 2000s) – should not lead us to underestimate this new relationship between the banks and the households. South African banks have followed their own path at their own pace, particularly related to the net capital inflows from abroad, but households have certainly become a new target for accruing income in various forms. This is indicative of a qualitative leap in their relationship with households, which parallels the practices of the banks of more developed countries, as indeed some recent news have additionally confirmed[88].

6.4.2. Financial market mediation income in South African banks

Albeit to a lesser degree than the increase in income from households, the increase in financial market mediation is often presented as one of the most salient features of financialisation. According to Dos Santos (2009) and Lapavitsas and Dos Santos (2008), banks arguably turned to this profitable market in order to compensate for a decrease in traditional lending to corporations (which have become increasingly able to access financial markets directly). Dos Santos (2009:195) identifies these new sources of income as coming "from a range of activities, from conventional investment banking functions of underwriting, brokerage and corporate advisory services to investment and insurance fund management and the issuance and dealing in derivate assets. Associated with all these activities are the increasingly significant capital gains made by banks on their trading and own accounts". At the end of the 1990s, it seemed that the South African banking system was indeed following such a path. The consulting firm KPMG stated in 1998 that:

> "Most banks diversified their operations away from their original businesses. New products were constantly originated, especially for those operating in the capital markets, such as options, swaps and futures. Active research for new market opportunities and products stimulated the growth of earnings from sources other than from the pure lending activity through intermediation. Value added services such as advisory, structured transactions, mergers and acquisitions, project finance, derivative trading and off-balance sheet activities developed at a rapid pace." (1998:3)

However, as was already seen, the relative weight of trading and investments positions in the banks' balance sheets has decreased throughout the 2000s**.** A more careful analysis is thus required in order to overcome the limitations of the relative weight of these assets in the banks' balance sheet as an indicator, which ignores the turnover of these assets and its trading revenue over the year. More importantly, the fees accrued from investment banking activities need to be taken into account, given that they play a more relevant role in this sort of banking activities than they do in retail. Testing our financialisation hypothesis concerning an increase in income from financial market mediation (encompassing revenues from financial instruments and attached fees), is thus a necessary step in order to assess the importance of these activities for banks.

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[88]ABSA bought a 50 % stake in Woolworth's in 2008 and recently bought Edcon's store-card credit business for 1.2 billion dollars in June 2012 (Wall Street Journal, 2012).

From the aggregate income statements of South African banks, it is possible to calculate the evolution of the ratio of non-interest income to total revenue (an indicator, used by Dos Santos, which shows the relative importance of revenue from non-traditional lending activities) throughout the post-apartheid period and up until 2007, in comparable terms[89]. Table 6.13 shows the ratio of non-interest income to total revenue: there has been an increase in the relative importance of non-interest income between the mid-1990s (when it averaged 17 to 20%) and the 2000s (when it peaked at 28.5% in 2005 before dropping to 22% in 2007). Compared to developed countries, where non-interest income accounts for more than 30% of all revenue (Dos Santos, 2008), the weight of non-interest income can still be considered relatively limited in the South African context.

Table 6.13. Ratio non-interest income to total revenue.

1994	1995	1996	1997	1998	1999	2000
0.199	0.183	0.173	0.181	0.186	0.217	0.259

2001	2002	2003	2004	2005	2006	2007
0.216	0.197	0.218	0.281	0.282	0.265	0.223

Source: SARB, Computed from the DI 200 returns.

The weight of non-interest income is not exclusively accounted for by revenue from financial market mediation. Non-interest income also includes transaction fees charged on such traditional banking services as withdrawals or foreign exchange operations. Of all the non-interest income sources of revenue, two main categories from the DI 200 income returns have been calculated in the context of this analysis in order to encapsulate investment and trading revenue: trading and investment revenue (encompassing both proprietary trading and trading on behalf of others) and knowledge-based fees such as that relate to investment banking fees from trading and advisory activities.

[89]Two sources of data are drawn upon in this analysis. For the period 1994-2000, the data comes from the SARB Bank Annual Reports (Appendix Tables for "Composition of Income Statement"), due to the fact that the monthly D 200 income statements do not provide data on investment and trading income . For the 2001-2007 period, selected items from the D200 income statements were used. Small differences exist between these two sources, given that the data from the SARB Bank Annual reports is usually revised at a later stage. The D 200 refers to the latest revision of these returns, published in February 2012. "Total income" is calculated as the sum of Interest Income, Non-Interest Income and Associated Income.

6.4.2.1. Investments and trading income

The ratio of the banking sector's investment and trading income to total income rose in the 1990s –a rise which took place alongside the increase in the relative weight of these activities in the bank's balance sheets, as shown in the previous section –, but then decreased abruptly in 2001 to just 0.6% of all revenue, before recovering to around 5% in 2007 (Table 6.14). These relatively low figures may be compared to data provided by Dos Santos (2009) for some major international banks for which "trading and own account" revenue in 2007 accounted for between 12% for Santander and 33% for BNP Paribas. The hypothesis of an increase in the relative importance of the banks' operations in financial markets, which either relate to trading on behalf of clients or consists of own investments, is thus not confirmed by the data.

Table 6.14. Ratio of investment and trading revenue to total income[90].

1994	1995	1996	1997	1998	1999	2000
0.081	0.078	0.072	0.078	0.085	0.095	0.108

2001	2002	2003	2004	2005	2006	2007
0.085	0.006	0.035	0.086	0.056	0.074	0.055

Source: Computed from SARB DI 200 returns

However, one should examine in detail the banks' holdings in absolute terms as well as their composition, by taking into account the role of public debt securities within those holdings. Despite the lack of data on income earned from public securities and their relative weight within the banks' overall income from investments and trading, the flow of funds data for the banking sector, previously discussed, showed the declining flow to these instruments. The declining relevance of public debt securities should not come as a surprise as public debt relative to GDP, after a steep rise before the end of apartheid, has been dropping particularly during the 2000s.

[90]Trading and Investment income" is calculated as the sum of items "trading income" and "investment income" of the SARB Annual Bank reports for the 1994-00 period. For the 2001-2007 period the item "Trading and Investment" is directly taken from the monthly DI 200 returns calculated on an annual basis.

The income earned from investment and trading positions has thus undergone a qualitative change, which reflects a shift from public assets onto other, generally private, securities. That shift can be traced by drawing on income DI200 returns data for 2001-2007[91](Table 6.15). An increase in the income from such new securities as derivatives and non-specified assets (which include new financial products) is found. However, the relative stagnation of income from "interest bearing securities" – which include public debt securities –, alongside the increasing importance of derivatives and other assets (including income earned from such activities as foreign exchange and trading in commodities) illustrate the changing nature of these operations. South African banks have increasingly turned to new private securities, thereby providing evidence of their willingness and ability to engage with new financial instruments. Nonetheless, these still account for a relatively small share of their total revenues[92] when compared to their developed country counterparts.

Table 6.15. Income from investment and trading positions – % of total income.

	2001	2002	2003	2004	2005	2006	2007
Interest bearing	0.26%	-0.27%	0.31%	0.03%	0.41%	0.33%	0.46%
Equities	0.55%	0.57%	0.44%	0.62%	0.43%	1.09%	0.55%
Bank-related investments	0.90%	0.27%	0.46%	0.79%	0.90%	1.40%	1.00%
Derivative instruments, including hedging	3.71%	0.56%	-0.27%	2.62%	1.64%	2.00%	-0.67%
Other (including unlisted equities)	3.56%	-0.41%	2.97%	3.86%	2.77%	4.44%	6.14%

Source: SARB, Computed from the DI 200 returns.

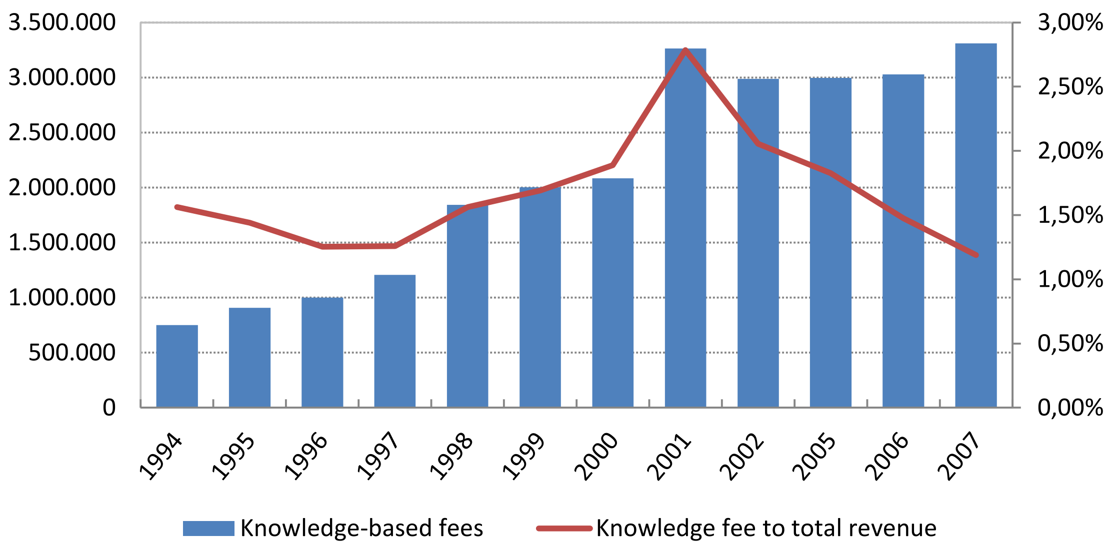
6.4.2.2. Knowledge-based fees

South African income statements provide data on the item of knowledge-based fees for the 1994-2007 period. This income is defined as including income from buy outs, listing fees, mergers and acquisitions, etc., and is therefore directly related to financial market mediation. Knowledge-based fees grew intensely during the second half of the 1990s, from 750 million rand in 1994 – 1.6% of total income - to 3,200 million in 2001 – or

[91]There is no publicly available data for the years 1994-01. Income from securities does not include mark-to-market adjustments that may be accounted as either profits or losses.

[92] The small importance of these items as source of revenue is confirmed by the small relevance of off-balance sheet assets (overwhelmingly composed by unwithdrawls facilities and guarantees on behalf of clients).

2.6% of total income –, but then stagnated during the 2000s, their weight in total revenue dropping to 1.1% in 2007.This relative stagnation may be attributed to the frenzy of conglomerate unbundling during the 1990s, when foreign capital inflows started to gain momentum. New corporations emerged, while others became publicly listed both domestically and internationally, thereby enabling the financial sector to benefit strongly from its investment banking activities. During the 2000s, the significance of financial market mediation as a source of fee income has decreased in the total bank revenue. Moreover, looking at data provided by the Ernst and Young report (2005) on corporate finance in South Africa ranking the investment advisers and sponsors a number of foreign investment banks (i.e. Merrill Lynch, Goldman Sachs) and consultants appear in the top places (i.e. PricewaterhouseCoopers; Ernst and Young). Such reality points to how investment banking income is distributed among non-banking agents (thus eluding our figures) and the relevance of major international investment banking local branches of which income may be shared with their headquarters and thus not accounted in South Africa.



Source: SARB, Computed from the DI 200 returns.

Figure 6.16. Knowledge-based fees (K rand).

6.4.2.3. Discussion

Despite the increasing importance, in absolute terms, of the revenue from trading and investment operations and from knowledge-based fees, as well as the banks' increasing willingness to engage with new financial instruments, the low and stagnant weight of these sources of revenue relative to the banks' total revenue does not support the hypothesis of increasing income coming from financial market mediation operations – i.e., our bank financialisation hypothesis (4). Despite the banks' increasing ability to undertake and engage with the processes of financial innovation that lie at the core of the current evolution of international finance, the hypothesis of the financialisation of banking in this specific sense (of an increasing importance of income from financial market mediation) thus fails to be corroborated by the data in the South African case. Moreover, the importance of public debt securities for banks, which is present in many middle-income countries, seem to be rather small in the South African case, which can be easily explained by the relatively small size of the South African public debt stock. In its turn, this can be accounted for by South Africa's semi-peripheral position in the world economy. Investment bank activities tend to be concentrated in the main international financial centers where major transactions are brokered, in order to benefit from the abundant liquidity, the dynamics of innovation and the ability to undertake dealings in "hard" currency. In the South African case, this is facilitated by the fact that, as was seen in the previous chapter, the major South African corporations have gained access to more dynamic financial markets located in developed countries.

6.5. Conclusion

The processes of liberalisation and deregulation that characterised the post-apartheid period had a profound impact upon the South African banking sector. The convergent path of these banks vis-à-vis their developed country counterparts therefore called for an empirical assessment of financialisation in this sector. Even though South Africa's financial system is largely bank-based (and despite the fact that the role of banks as intermediaries of financial flows has, if anything, been reinforced as a consequence of the aforementioned processes), it was possible to clearly demonstrate the existence of a clear process of financialisation in this context, in the sense of a relative growth of this sector's balance sheet and income compared to the rest of the economy.

However, this generic notion of financialisation can be a source of some theoretical ambiguity within the Marxist political economy debates. Although the issue of financialisation is rooted in the historical debates among Marxists as a problem of surplus absorption which originates in the sphere of production (see chapter 2), the ascendancy of financialisation is often regarded as the rise of an independent sphere of the economy which generates higher profits solely due to its speculative dimension, thereby constituting a haven or outlet for over-accumulated capital fleeing from low-profit production. This interpretation has proven popular within the context of the political economy analysis of

South Africa, given both the stagnation and low investment rates that have plagued this economy and the concomitant ascendancy of finance over the past decades (Bond, 2006; Fine et al, 2011). However, the second half of the 2000s has seen a parallel growth surge by both by the financial sector (centered around banks) and in investment. This seemingly lasting and complementary relationship between banks and the non-financial sector apparently challenges the aforementioned theoretical interpretation.

The concept of financialisation adopted in the context of this thesis has a more precise meaning, which seeks to avoid the debates around the measurement of profit rates and favors a more systemic approach, whereby financialisation is regarded as a consequence of an overall transformation of the economy which does not imply the rise of the “virtual” financial sphere at the expense of “real” production. Lapavitsas (2009) argues that financialisation should be understood as the rapid growth of capital circulation when compared to production, arising from financialised interactions among agents of the capitalist economy. This notion of financialisation refuses the simplistic opposition between production and finance, as well as the class implications that obtain as a result (i.e., opposing “monied” or rentier capitalists to industrial capitalists). Without denying that relatively higher returns have accrued to finance in recent times, this sector is not understood as a “virtual” booming sphere necessarily arising at the expense of a stagnated “real” sphere – but rather as a product of a systemic transformation arising from interactions between the various agents in the economy (corporations, financial institutions, households).

Building on this framework, I have sought to assess empirically the process of financialisation in the case of the South African banking sector, while keeping the specificities of this context. With that aim, I have tested four initial hypotheses, concerning the balance sheet and income composition of banks, which are directly derived from this theoretical approach.

I found confirmation for our hypothesis (1) on the increase in finance-to-finance funding in the banks’ balance sheets. However, this increase has been skewed within money markets towards wholesale deposits; other instruments, like debt securities or derivatives, have played a small, albeit increasing, role. These wholesale funding markets are essential for banks to support their own expansion and fine-tune their balance sheet liquidity management. They provide the required homogenisation to funds available for lending, which plays a crucial role in the rise of bank-centered financial intermediation in countries like South Africa. Nonetheless, it should be stressed that retail deposits have continued to account for an overwhelming share of the banks' liabilities, particularly in the case of non-financial corporations, which proves that banks continue to play a central role in the collection of idle funds, thereby partially contradicting the argument put forth by Lapavitsas (2009) and Dos Santos (2009), according to whom there is a general tendency towards the "bank disintermediation" of the relation between non-financial corporations and finance.

Given this specific South African pattern, it comes as no surprise that investments and trading positions have played a relatively minor role as an income source for banks. If we add to this the fact that "knowledge-based" fees have taken on decreasing weight in the banks' total income, we are led to the conclusion that our hypothesis (4) on the increasing role of financial market mediation does not hold in the South African case. The biased finance-to-finance structure may be explained by South Africa's semi-peripheral position in the international financial system: on the one hand, these are markets that are more prone to general financial volatility of both its exchange and interest rates, due to the unstable short-term foreign capital inflows, and this uncertainty may hamper the development of a more robust debt and derivative markets; on the other hand, as we have seen in previous chapters, the major South African corporations are nowadays able to access the financial markets of developed countries, providing them with cheaper funding and the ability to profit from arbitrage revenues. This reduces the need to access domestic debt markets.

In their turn, the political economy accounts of Dos Santos and Lapavitsas concerning the rising importance of households as a source of bank income seem to hold in the South African context to a much greater extent. Private households have become increasingly important not only as borrowers but also as a source of income with different origins (both through interest rates charged on different debt categories and through transaction fees). Our financialisation hypotheses of (2) increasing lending to households and (3) increasing income accrued from the household sector were indeed corroborated by the data. This transformative tendency therefore seems to be present across very different national settings and to lie at the core of contemporary financialised banking. Still, the seemingly robust relationship between South African banks and households, which is based on the relevant role that the latter continue to perform as providers of funds and increasingly as recipients of credit, calls for more detailed research on the household sector and the sustainability of its current role in the South African economy. The predatory nature of contemporary banking was confirmed in this case by the rise of various kinds of household debt – which shows a structural change in the interaction between the two sectors – as well as by the multiple ways in which banks extract income from households, with fees playing a major role in the process.

Nonetheless, it is not entirely clear whether this increasing extraction of income from households is a result of the extension of credit to new layers of the population or a consequence of the retreat of public services. The strong reliance on mortgage debt and the inexistence of a subprime market indicate that this increasing reliance on households by the banking sector was largely limited to the South African middle-class, which profited from the extraordinary rise of house prices during the last decade. It remains to be seen whether the mild impact of the international financial crisis upon South African banks, cushioned by a steep drop in the interest rates and by the swift recovery of its export sector, reflected a more sustainable debt relation between banks and households, or merely a postponement of the problems that have afflicted the more mature economies.

7. Financialisation and households in South Africa

7.1. Introduction

Household finance has been at the centre of the current financial turmoil. The international financial crisis that began in 2007 was triggered by record-breaking levels of default among American real-estate subprime borrowers, which rapidly spread across the financial system by means of complex mortgage-based derivative products. After almost a decade of low interest rates, increasing household debt and booming housing markets in many developed countries, most notably the US, this international crisis exposed how the economic dynamism of developed countries such as the US and the UK had been fuelled by consumer spending enabled by households' increasing involvement with finance. The increase in interest rates of the mid-2000s and the related increase in the burden for households proved to be unsustainable, particularly for the most vulnerable layers of the population (subprime borrowers), eventually leading to the worst economic crisis since the Great Depression of the 1930s.

The rising involvement of households with the booming financial sector has normally been attributed in political economy to liberalisation, deregulation and privatisation (e.g. Dumenil and Levy, 2011; Lapavitsas (2009); Lapavitsas and Dos Santos, 2008**)**.The liberalised financial sector, benefiting from the new information technologies that provided huge amounts of data on individual credit profiles and credit scoring techniques, on this analysis, acquired the social trust needed to extend unprecedented amounts of credit to new layers of the population without affecting the Value-at-Risk models on the basis of which the banks assessed their risk exposure. This expansion is also seen, on the other hand, as having been fostered by the neoliberal movement of privatisation, labour market reform and retreat of welfare state public services of the 1980s and 1990s. Households are said to have been pushed into the arms of finance in order to access goods with respect to which the public sphere had previously been, if not the exclusive provider, at least a strong disciplining force on the market. Retreat from public provision of housing, education and social security are the recurrent sectors that illustrate this trend in the most developed countries. This wave of neoliberal policies, allied with stagnant real wages and rising inequality, is then said to have left workers' households in a vulnerable position with respect to the financial sector, enabling increasing extraction of income (Lapavitsas, 2009). The later, resorting to predatory methods, extract rising individual income. This financialisation of households has been encapsulated in the concept of financial expropriation (Lapavitsas, 2009). The increasing involvement of households with the financial sphere as holders of financial assets, such as in pension and mutual funds for which they pay high fees and commissions, has also been noted as being part of this new stream of financial revenue (Dos Santos, 2009). In Marxist political economy terms, the nature of this income is different from income derived from financial sector lending to investment, where a share of the profits from the ensuing expansion of value is captured by the financial sector. Financial profit from households does not originate in the sphere of production, but in the sphere of circulation, as it relates to “existing flows of money and value, rather than new flows of surplus value” (Lapavitsas, 2009: 16).

Previous chapters have established the financialised profile of non-financial corporations and banks in South Africa. Households have gained a rising importance for banks as sources of income and recipients of growing debt, particularly in the form of mortgage debt. Benefiting from declining interest rates, household debt rose during the later years of the 2000s: this sector was the main driver of bank expansion during this period. Here I examine the implications of this trend for South African households. Given the similar pattern previously seen in more developed countries, I aim to observe whether households in South Africa have the same financialised profile as those in the most developed countries, in the terms proposed by Lapavitsas (2009) and Dos Santos (2009). On the other hand, the features of households in post-apartheid South Africa, as a middle-income country, are very distinct from those in high-income countries. The country presents extremely high levels of inequality, high unemployment, informality in labour relations, and poor provision of public services at a scale not known in developed countries. Moreover, as seen in the previous chapter, in South Africa the development of new forms of bank lending expansion such as securitisation is still limited, hinting a different pattern of lending expansion among households.

Having established one of the assumptions required to apply the concept of financial expropriation—banks’ growing extraction of profits from households, as described in the previous chapter—here we examine the content of this new relationship for households. In this chapter we aim to assess the validity of the financial expropriation analysis by means of the financial position of South African households—and the depiction of debt relations in this specific country. Empirical scrutiny of South African households in aggregate is thus need for the presence of financial expropriation, testing the similarity of their situation to the pattern seen in the most developed countries before the financial crisis—rising burden of household debt, mainly in the form of mortgage debt, and rising debt-service costs as a proportion of income. It should be noted that, as in developed countries, this rise in indebtedness coincides with a huge influx of foreign capital for which high real interest rates were of paramount importance. The subaltern position of South Africa in the international financial sphere is thus reflected in the debt costs of South African households.

We start this chapter with a literature review on household finance, from the shortcomings of mainstream neoclassical contributions—household portfolio theory, the life-cycle hypothesis, and behavioural economics—to the contributions from political economy outlined above. We then look at financialisation of South African households, using aggregate South African Reserve Bank data on household balance sheets and flow of funds in order to measure the extent to which households' financial position has been transformed and to establish the debt and asset composition of their financial dealings. These will provide a general overview of the impact of the rising indebtedness of South African households, highlighting the extreme form that this trend has taken in the country. I end this chapter with the overall assessment of financialisation among South African households: the specificities of the case and the theoretical insights that it offers.

7.2. Household finance: an overview of approaches from mainstream and political economy

7.2.1. Mainstream economic theory

There have been significant efforts to include the fact of the increasing involvement of households with the financial sphere in the neoclassical mainstream of economic theory. Motivated by the growing relevance of this sector in financial markets as both debtors and asset holders, this research builds on seminal contributions from the 1950s and 1960s as well as more recent developments (e.g. informational asymmetries, adverse selection, behavioural theories) to present a prolific, albeit fragmented, theoretical framework that tries to explain household financial behaviour. These theoretical efforts have remained, however, within the realm of the efficient markets hypothesis (Fama, 1965): according to this approach, "in an efficient market at any point in time the actual price of a security will be a good estimate of its intrinsic value" (Fama, 1965: 76). Theoretical work is thusexclusively focused on the rational microeconomic behaviour of agents in the context of competitive markets, with recent contributions attempting to explain apparently irrational behaviour and suboptimal outcomes within the same neoclassical market framework. Two major branches of household financial behaviour are examined here: modern portfolio theory and consumer choice theory.

7.2.1.1. Households as financial asset holders: portfolio theory

The study of how households invest in financial assets is a recent domain even within mainstream economics. Initial theoretical efforts to account for financial engagement were intended to be applied to financial market analysts and fund managers, not households. Guiso et al (2001) argue that this negligence is explained by the relative novelty of the emergence of equity culture (households' willingness to participate in financial markets). Bertaut and Starr-McCluer (2001) present some reasons for this new involvement of households in financial markets in the US: the steadily rising price of stocks during the 1980s and 1990s; the promotion of a wider supply of financial products following extensive financial liberalisation and innovation; and the creation of tax-deferred retirement accounts during the 1980s which promoted a migration from defined-benefit pension arrangements to defined-contribution arrangements based on investment in financial markets.

However, it is still the works of Markowitz (1952) and Tobin (1958) which, being the seminal contributions to portfolio theory, are used to research household financial behaviour. These contributions were developed on the belief that the demand for financial assets is dependent on expected rates of return (compared to a benchmark risk-free) and the opportunity costs of holding them. In a competitive market, if the expected returns on an asset increase relative to the non-risk benchmark then demand for that asset should rise. When relative prices fall demand should decrease. Finally, any proportional price change should have no effect in the market. Following this reasoning, but integrating different risk preferences in the demand of financial assets, the capital asset pricing model (CAPM) was developed, taking into account the covariance of returns on a risky asset with the returns on a market portfolio. Robert Merton (1973) later expanded this model, adding the possibility of inter-temporal hedging against shocks on the rate of return at which wealth can be reinvested. In his inter-temporal CAPM, assuming continuous trading, investment opportunities vary over time for utility-maximising consumers.

All of these theoretical contributions tend to emphasise the risk choice of different assets. Such theories aim to eliminate non-systemic (individual asset) risks from portfolios. However, conventional asset pricing models offer a very partial account of how households behave. They were developed in order to explain the behaviour of financial market agents in general, and not specifically that of households as financial asset holders. The motivations and behavior of the latter, who face particular informational and borrowing constraints, are not same as those of fund managers (particularly in pension funds).

7.2.1.2. Integrating household behaviour

Since the 1990s, portfolio theory has undertaken a long and complex series of efforts to integrate household behaviour into its original models. A number of particular household realities that hamper a clear adaptation of the old models to these realities have been pointed out. Surveys on American household portfolios have shown that the developing engagement of households with financial markets in the US still leaves out large sections of the population (Bertuat and Starr McCluer, 2001). This would amount to a non-rational choice not to participate in the investment opportunities offered by financial markets. Moreover, household portfolios are normally characterised by a small number of safe assets, which seems to go against the suggestion by CAPM theories that financial actors will hold a range of assets with an optimally diversified risk profile. As pointed out by Gollier (2001), there are risks which cannot be hedged against. The author argues for the abandonment of the static models wherein consumers have the same income and preferences at all times in favour of a dynamic one where risk preferences change over time and can be adapted to specific conditions. What would be a non-optimal situation in a static model is reconceptualised as a “second-best” result. On this new analysis, the revealed preferences of rational agents would still stand for sub-optimal results, allowing thus for the Portfolio theoretical core to stand.

Much of literature on integrating household behavior into portfolio theory has also focused on the possible role of human capital risk—the risk that individuals face of having their incomes diminished or terminated (unemployment)—to explain risk-adverse preferences. Since human capital is not tradeable and unemployment is only partially insured by social benefits, this restriction is considered to lead to risk aversion in portfolio choices (Heaton and Lucas, 2000) leading to non-optimal choices in household financial portfolios. Such risk, on this account, is fostered by rigidity in the labour market, and greater labour market flexibility would allow households to adjust their supply of labour time to the evolution of their asset returns, thus increasing their willingness to take on financial risks (Bodie, Merton and Samuelson, 1992).Other examples of limits to an optimal household investment strategy come from the transaction costs literature. These costs are said to affect household behaviour on a significant scale, acting as a barrier to entry in financial markets and to further diversification (Collier, 2001).

Another significant problem that households face when investing in financial markets pointed out by economists in these currents rests in liquidity and borrowing constraints, which are said to produce more conservative non-optimal behaviour. On this account, households that are unable to borrow as they wish hold more conservative portfolios since they cannot diversify their risk when facing an adverse shock. As pointed by Campbell (2006):

"Households must consider the fact that their future consumption may be determined not just by their wealth and investment opportunities, but also by their net future income if they are borrowing constrained. Financial investments that do poorly when income is temporarily low may be unattractive for this reason." (Campbell, 2006: 1560)

Housing as an asset has been gaining importance among middle-income households as ownership has been rising. The importance of this class of assets has posed new challenges to portfolio theory, since this collateral could facilitate risk-taking and produce closer-to-optimal behavior. Sinai and Souless (2005) argue that the alternative (to rent) is risky and that homeownership should be taken here as an investment hedge. They argue that for households which devote large shares of their income to housing and live in places where rent prices are more volatile, homeownership is a hedge against fluctuations in future rent payments. Housing is thus here taken just as one portfolio choice out of a range of possible investments. Its importance as basic need and the arrangements behind its provision are completely neglected. Households are here taken as optimal agents, investing in assets solely on the basis of the expected returns and risks of each asset, ignoring the different social roles of different types of goods.

Finally, the attention of modern portfolio theory has also been directed to empirical differences in investor behaviour among different income percentiles. Although theory predicts that all households should invest at least some of their income in assets with a positive expected return, financial asset holders are concentrated in the top percentiles. With the integration of borrowing constraints, risk-averse behaviour, and human capital risks, new dynamic models that allow for heterogeneous household income positions have been tested against new sets of empirical data, and some general results on risk-taking behavior have been presented: under the decreasing relative risk aversion assumption, wealthier people should invest a larger share of their wealth in risky assets and people burdened with riskier human capital should invest less in risky assets (Collier, 2001). Wealthier households are thus the ones whose behaviour is closer to the original predictions of the models (diversified portfolios and risk-taking behaviours: Carrol, 2002). Bertuat and Starr-McCluer (2001) point to fixed costs of participation, which overwhelm potential gains, as the reason for this asymmetry. Nonetheless even among wealthier households, participation is far from universal. Heaton and Lucas (2000) argue, for example, that only business owners hold more stocks. This would amount to what the authors call "entrepreneurial risk," only held by a particular profile of households.

Household portfolio theory is interested in researching how households should behave as asset holders, particularly their risk strategies, neglecting their social position in terms of income, savings and goods provision. Differences in behaviour are explained by different risk preferences and by market rigidities. However, even in the countries where households are most engaged in financial markets, such as the US, their behaviour is far from what would be expected of rational investors. As this leads to the abandonment of the standard revealed preferences framework, the alternative found in much of the literature (Campbell, 2006), is to qualify some of the choices of most households (e. g. non participation in risky asset markets, under-diversification of portfolios) as "mistakes," and stress the importance of financial literacy and the need for long-term educational programs to improve the ability of households to manage and diversify their portfolios. Given the growing complexity of financial products and the formal sophistication of financial investment theories, this seems to be a far-fetched proposition. Moreover, given the abstract approach that these theories entail, there is no particular focus on the distributive implications of the types of financial assets held by households (mainly concentrated in pension and mutual funds), the historical dynamics behind the emergence of such products, or the sustainability of household indebtedness. Finally, given that, as in the original contributions, they focus on the minimisation of non-systemic risk, they fail to account for the increase in the volatility of financial markets in recent decades, culminating in the present crisis. Events like this crisis are taken as adverse, unpredictable, exogenous shocks, which theory cannot explain and which are thus ignored in this exclusively micro-economic approach, where economic structures do not seem to exist.

7.2.2. Household debt and the life cycle and permanent income hypotheses

Theoretical work in mainstream economics on the other dimension of the relation between households and finance—increasing indebtedness—normally stresses the seminal life cycle consumption hypothesis (LCH) of Modigliani (1954). According to this hypothesis, rational young consumers smooth their consumption levels over their life time by taking on debt in the earlier stages of their working lives. Although it is focused on consumer behaviour, this theory can explain individual debt, since discounted marginal utilities of consumption are to be followed by credit demand at times when current income does not fulfil consumption needs. Such debt will be paid against expected higher income later in life. It is assumed that individuals will reduce their levels of debt and start to save when reaching middle-age in order to prepare for retirement. These savings are then assumed to be channelled to the young through the financial system. Indebtedness, on this view, is the natural outcome of transfers of resources among rational individuals. These individuals are supposed to maximise their inter-temporal utility through credit, anticipating how much they are going to earn indifferent life periods. Here, current assets are irrelevant to each individual's capacity to incur debts. The implausible assumptions of rational indebtedness, its restriction to brief periods in the life cycle, and the irrelevance of collateral seem however unlikely to lead to a robust theoretical account of modern individual debt even within the mainstream framework.

Another, theoretically close, example of an influential theory of consumer debt is Milton Friedman's permanent income hypothesis (PIH). Friedman argues that consumption is not determined by current income but by individuals' expected wealth over their entire lifespan. Individuals may indebt themselves during certain periods in order to smooth their consumption spending over the course of their lifetime. This theory may be more likely to explain recent trends in household indebtedness, since it does not depend on the notion of a particular life-period for debt (as in Modigliani's hypothesis) and may be consistent with the determinant influence of home wealth's on consumer spending in recent years. The rising value of housing wealth, then, may be treated as an upward shift in the household's inter-temporal budget constraints, thus increasing consumption. But here again, this theory has little explanatory power, for three main reasons. First, it cannot describe the stagnating consumption that came along with rising debt and soaring house prices (a wealth increase) in the US in recent years (Lapavitsas, 2009). Secondly, since debt is conceptualised here as the rational result of income anticipation, consumer debt should always be sustainable.

Something the current crisis has shown to be, at the least, unlikely. Finally, because increasing debt is attributed to rising house prices, it cannot explain the concomitant overuse of forms of credit other than mortgages, such as credit cards, pay-day loans, etc.

The introduction of liquidity constraints and adverse selection create problems of internal consistency for the LCH/PIH hypothesis, as it is assumed here that people borrow as much they feel they need to smooth their consumption. With the introduction of liquidity constraints, people cannot borrow as much as they would like, and may not borrow at all if their future income is uncertain (Kehoe and Levine, 2001). The equilibrium quantity of borrowing depends on the terms on which agents can obtain credit and particularly on their wealth, when lenders demand collateral. These market imperfections show, therefore, that while consumers can in fact save in order to smooth future consumption, they cannot borrow as much as they want unless they already have assets to serve as collateral. This puts at risk the separation between income and consumption postulated by the LCH/PIH hypothesis. Still, Deaton (2005) argues that life cycle theory has managed to circumvent such problems by reducing the periods to a few years at a time. According to models of this type, people only save to smooth out their consumption over short periods, when assets are available and income can be predicted, leading to a "high-frequency" smoothing of income. With the introduction of shorter time periods, the problems created by liquidity constraints thus should not run to the point of rupture with both the Life cycle hypothesis and Permanent Income Hypothesis. The role of debt as an individual consumption smoother, a product of inter-temporal utility maximisation, remains untouched. However, this account neglects the overwhelming role that (long-term) mortgage debt normally plays in total household debt. Furthermore, over-indebtedness problems are still understood as marginal, against a background of broadly efficient markets and rational individuals. Household defaults are to be attributed only to non-anticipated personal misfortunes (e.g. disease or unemployment).

The various mainstream theoretical approaches would thus welcome the exponential rise in mortgage loans and their expansion to new sectors such as the subprime market, as they should offer all households the possibility of more efficient financial planning. Thanks to decades of financial liberalisation, such changes should allow finance to efficiently extend to everyone. However, as the present crisis as shown, these record levels of borrowing and indebtedness were actually unsustainable. Granted on the basis of a speculative bubble in the real estate sector and of variable interest rates, such loans were subject to a massive wave of defaults with increased interest rates along with the slowdown in housing demand and the consequent collapse of housing prices. With the depreciation of many households' main asset and rising monthly payments, over-indebtedness problems became systemic, primarily among the most vulnerable, the situation that triggered the current financial crisis.

Nonetheless, there is some concern in the mainstream literature on household debt and the housing market. Barnes and Young (2003) integrated debt as a financial device to be used to finance durable goods, particularly housing, and not just for consumption smoothing. Bridges et al (2006) argued that house prices affect the value of lifetime wealth. They suggest that increasing house prices work as a "signal" of creditworthiness, even on unsecured credit such as access to credit cards, thus promoting further household indebtedness. However, at least for the UK, the country upon which this research is focused, there was no evidence for a relation between debt and home ownership: in fact, households' levels of unsecured debt and debt arrears were negatively associated with home ownership. Another observation that was surprising for mainstream economists is the post-crisis perception that adjustable rate mortgages (prevalent in the subprime market) were more risky than fixed rate mortgages. The first should be safer since "it has a stable value that is almost unaffected by movements in interest rates, while the value of a long-term bond is highly sensitive to interest rates" (Campbell, 2006: 1561). However, housing is a long-term investment; variations in interest rates can affect real borrowing costs, particularly in the presence of borrowing constraints. Fixed rate mortgages may thus be a proxy form of hedging against this risk. Adjustable rate mortgages would then be attractive to households with low risk aversion, such as subprime borrowers (Campbell and Cocco, 2003).

7.2.2.1. Behavioural economics as a fix to the LCH/PIH hypothesis

As Deaton (2005) pointed out, the emergence of behavioural economics has posed profound theoretical challenges to the core of PIH/LCH theory. Building on contributions from psychology, behavioural economics dismisses the neoclassical assumption of the individual as solely self-interested and able to fully compute the costs and benefits of his actions. The assumption of maximisation of expected lifetime utility subject to budget constraints is abandoned. Individual views are understood to depend on the present context, where (for example) procrastination and lack of self-control influence household economic behaviour (Thaler and Banertzi, 2004).

Since Kahneman and Tversky's (1979) paper on prospect theory, demonstrating a variety of ways in which individuals' behaviour violates "rationality", a number of concepts have been advanced to characterise heuristics used as alternatives to total rational behaviour: "hindsight bias", "representativeness", "framing effects", "context effects", "contingent valuation" (Camerer and Loewenstein, 2003). These heuristics account for two major behavioural challenges to the LCH/PIH: 1) Individuals show time-inconsistent behaviour, giving more weight to current and near-term consumption than to long-term future consumption, resulting in "farsighted planners and myopic doers" (Thaler and Shefrin, 1981: 394); 2) Individuals' revealed preferences are characterised by loss aversion: losses are more heavily weighted than gains, making preferences inconsistent. The resulting behaviours are then said to explain the recurrent postponing of plans to save and immediate, non-calculated, recourse to consumption credit.

In order to model the first inconsistency, David Laibson (1997) introduces the concept of "hyperbolic discounters" to describe "irrational" consumer behaviour:

> "Hyperbolic discount functions are characterised by a relatively high discount rate over short horizons and a relatively low discount rate over long horizons. This discount structure sets up a conflict between today's preferences and the preferences that will be held in the future" (Laibson, 1997: 445).

According to this theoretical framework, consumption will follow income through time. Laibson's model is thus able to offer an explanation for the drop in savings in the US during the 80s and 90s; in this context he also introduces some institutional and historical features such financial liberalisation and subsequent financial innovation. He points at the increase in "instantaneous" access to consumer credit as reducing the role of illiquid savings as commitment devices for individuals ("golden eggs") "(...) by enabling the consumer to instantaneously borrow against illiquid assets, financial innovation eliminates the possibility for partial commitment" (1997: 461). Over-indebtedness is thus seen as the result of myopic behaviour on the part of households, who could not anticipate the future implications of their actions. This theoretical insight gains robustness with Kanheman and Tversky's notion of individual loss aversion. On this account, individual utility functions are concave for gains, convex for losses, and steeper for losses than for gains. This would influence saving plans, since the "loss" of available income to be spent, especially for "hyperbolic consumers," will discourage saving plans and promote consumption. The LCH becomes inconsistent: income is directly influenced by current income and there is no consumption smoothing over time.

While impatience and loss aversion may impede truly optimal choices, there have been some efforts to characterise a new, second-best "behavioural" LCH. Following Shefrin and Thaler's (1998) suggestion of dividing wealth into three different accounts—current income, current assets, and future income—where the impatience to spend current income is greater than for future income -- this account suggests that individuals use some behavioural rules, such as postponing the receipt of income, in order to control spending. At the same time, the behavioural life cycle hypothesis also integrates the use of mental accounts to restrict the allocation of certain types of income to certain types of consumption. Individuals would then recognise their own limitations and act accordingly. This fits with proposals like Thaler and Benartzi's "Save more tomorrow,"™ (trade mark) where people commit themselves to allocating a portion of their future salary increases toward retirement savings in advance. This can at least partially resolve temporal behavioural inconsistencies.

Nonetheless, while discarding the full set of classical assumptions about *homo economicus* overcomes many of the limitations of LCH/PIH, this contribution remains inscribed within the reductionist neoclassical framework. The "reformed" behavioural LCH tries to preserve the logic of the original theory. As noted by Camerer and Loewenstein (2003) behavioural economics: "does not imply a wholesale rejection of the neoclassical approach to economics based on utility maximization, equilibrium, and efficiency. (…) It is more like a school of thought or style of modelling, which should lose special semantic status when it is widely taught and used" (2003: 48). It opportunistically adopts more realistic assumptions for individual behaviour, and even hints at some institutional and historical insights—as in the case of Laibson (1997)—but these are not integrated into an analytical framework, and remain exogenous to economic theory per se.

While behavioural economics is a clear breakthrough for neoclassical theory, its efforts to stay within the boundaries of the economic mainstream result in serious theoretical pitfalls when trying to understand contemporary household indebtedness. The approach allows household behaviour to be more robustly modelled, but it offers no account of the role of the financial system in current trends in household debt, as it remains constrained by its positioning within microeconomics. As in canonical neoclassical theory, here the role of finance is just to allocate resources efficiently to firms and households. Its hegemony in the world economy, the expansion to new household markets, and its new role in the provision of essential goods and services is ignored. Moreover, an account that restricts itself to the reductionist methodological stance cannot explain the class implications of increases in the holding of financial assets and debt. As noted by Nelson (2006), the choice to enter into a loan contract is not the expression of a preferred future but the outcome of constrained options in terms of the *current* state of affairs. The social position of each economic agent must thus be acknowledged in order to understand the heterogeneous roles of household finance in the economy.

The reductionist position needs to be abandoned when studying the relationship between households and finance, adopting a more comprehensive and systemic approach, profiting from historical and institutional insights, which not only identifies the structural transformations that the world economy has endured during the past decades but that also allows for variation within different social and geographic settings. Individual households must, at the same time, be integrated into more general concepts, such as social class, and contextualised within the specific socio-economic reality in which they live. Only such an approach, based in political economy and enriched by other political economy traditions within economic theory, can present a differentiated analysis of the causes and effects of household debt and financial assets during the last decades, but also offer a general account of the relationship between finance and households as embedded in a systemic contemporary transformation of capitalism.

7.2.3. The political economy of household finance

Some new avenues for research on household political economy that allow for a more comprehensive approach to household finance have been recently opened up by approaches from research in sociology and cultural economy. Erturk et al (2007) draw attention to the ways in which the financial system has encouraged households in all developed countries to engage increasingly with both financial assets (pension funds) and liabilities (mortgages, credit cards).Assuming that households should behave as financial managers, a paradox emerges. Since they lack the necessary financial literacy, new social actors (such as financial agents), with their own idiosyncratic interests, replace them as managers of their own assets. Household finance thus becomes the product of a mediated relation wherein households play a limited role in decision-making processes with regard to their liabilities and assets.

The securitisation of liabilities and assets is understood to have been pivotal in this new financialised environment, where households only play a small part in the transactions enabled by the new stream of securities. This is thought to lead to households' integration into rising financial capitalism, which, as Thrift and Leyshon (2007) showed, "is dependent on the constant searching out, or the construction of, new asset streams, usually through a process of aggregation, which then—and only then—allows speculation to take place" (2007: 98). These authors present three main categories of new financialised streams of revenue now possible through securitisation: aggregation of existing obligations (as in securities based on ground rents); public-private partnerships in infrastructure investment and management (highways, roads, airports, water supply, etc.); and finally mortgages, pioneered by the American agencies the Federal National Mortgage Association (known as Fannie Mae) and Federal Home Loan Mortgage Corporation (known as Freddie Mac), which led to the expansion of subprime lending that triggered the current financial crisis.

However, it is work within political economy, particularly that of Lapavitsas (2009) and Paulo dos Santos (2009, 2010), that offers a new and better understanding of the relation between individuals and finance. This work integrates together fragmented findings on the financialisation of individuals through the extensive study of class analysis and power asymmetries, not restricting itself to understanding households' rising financial involvement as the product of financial innovation alone (such as, for example, the rise of financial securitisation). Presented against a background of decades of triumphant neoliberalism which deregulated financial markets and imposed a general retreat of the welfare state, this new approach focuses on the reorientation of banking in this financialised period away from loans to corporations (which now have increasing direct access to capital markets) and toward loans to individuals, particularly through unsecured and mortgage credit. As shown by Dos Santos (2009), usurious money dealing fees and the higher interest rates paid by individuals, which come mainly from wages, have come to represent an increasing share of profits in the major American banks, accounting for between one third and half of total profits. This new asymmetric relationship has entailed regressive distributional outcomes and, in the end, revealed itself in the form of unsustainable household over-indebtedness. Lapavitsas (2008) conceptualises this new relation as "financial expropriation":

"Financial expropriation has exploitative aspects deriving from systematic differences between financial institutions and workers in terms of information availability, economic and social power, and alternatives in undertaking transactions. On the one hand, workers have been increasingly forced into the arms of private finance as public provision of key wage goods has retreated. (…)On the other hand, financial profits have also been generated out of wage income through predatory lending and other forms of over-charging through fees and commissions." (Lapavitsas, 2008: 19)

It is important to stress the power dimension—almost absent in conventional economic theory—presented here by Lapavitsas, as workers are forced to use the financial system as an intermediary to access essential goods once exclusively or partially provided by the state(housing, education, health and social security). This new approach is deeply grounded in Marxist political economy, incorporating original approaches to Marx's own work on finance and acknowledging the roots of financialisation in transformations of the real economy over the last decades. However, as Dos Santos argues, there is still the "need for robust conceptualizations of credit relations in the process of accumulation, including the distinctive social content of credit to wage earning households" (2009: 28).

Financial expropriation can be understood as a new power relation with capital that workers stand in today. Nonetheless, this concept must be analysed against the background of the classical exploitation of labour in order to understand its full implications. The best way to understand the exploitative dimension of the relationship between capital and labour within the framework of Marxist political economy is through the circuit of capital, first captured in a diagram by Fine (1975).

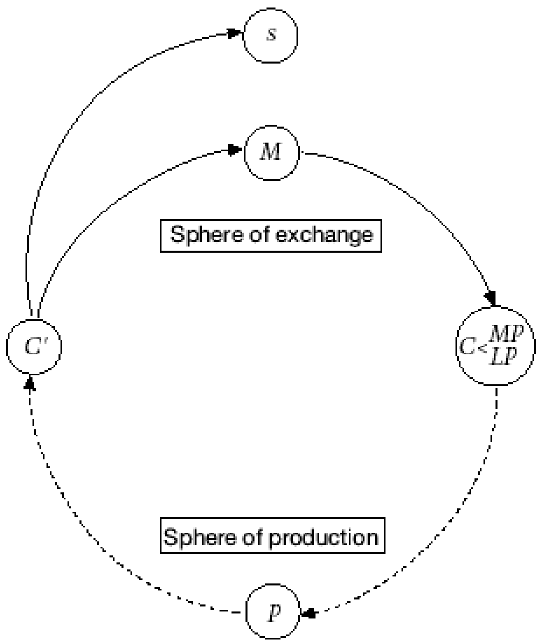


Figure 7.1. Circuit of Capital, in Fine (1975).

In this diagram, money capital(M) is used to purchase inputs (C) labour power (LP) and means of production (MP) which will enter into production (P), thus producing finished output (C'), which incorporates the surplus-value (s) created by workers. The surplus value is then sold and the original money capital plus the profit (C’) of the transaction is gained by the capitalist. The analytical stance represented by this circuit enables us to distinguish two different spheres in the circuit of capital: the production sphere (P) and the circulation of money and commodities (C’-M-C). In the first sphere, use values are transformed and value and surplus value are created. The second contains the exchange of C and C’ and the realisation of surplus value, S (Fine and Saad-Filho, 2004).

Financial expropriation should be situated in the sphere of exchange, since such profits come directly from workers’ wages. Here we are in a partially different realm from the classical stance of exploitation in production, what Marx in *Das Kapital* (1867 [1982]) calls secondary exploitation, derived by profit from alienation with its roots in pre-capitalist modes of production as presented in the Marx’s *Grundrisse*:

> “What takes place is the exploitation by capital without the mode of production of capital. The rate of interest appears very high because it includes profit and even a part of wages. This form of usury, in which capital does not seize possession of production, hence is capital only formally, presupposes the pre-dominance of pre-bourgeois modes of production.” (Marx, 1939 [1973]: 853)

Financial expropriation, although not arising directly from the exploitation of labour in production, is nevertheless the result of the deprivation of the working class and the power asymmetry that it suffers, not as wage labourers per se, but in the sphere of circulation, at the hands of a “class of usurers.” Financial expropriation, being a form of exploitation, albeit with roots in pre-capitalist modes of production, acquires a new relevance in the context of financialisation, as its two defining features gain importance, namely: the rising share of financial profit coming from households and the rising vulnerability and labour exploitation of the working class, expressed in growing inequality and the privatisation of social provision. It thus has a particular social content in capitalist economies that overcomes the mere transfer of income, and which should be kept in mind when researching this phenomenon.

Financialised” workers not only provide the profits to be transformed into money capital, but also serve as an important source of sustained demand for consumer goods, which is essential for the circuit of capital to work, thus sustaining the process of capital accumulation. Financial expropriation should thus be understood as a crucial part of what “regulationists” would call the new “wage-nexus” relation at the core of the contemporary financialised capitalism.

7.2.4. From core to periphery?

One of the shortcomings of this new literature is the exclusive focus of research on the rising financialisation of households in the most developed countries, with particular attention devoted to "market-based" countries such as the US, the UK, which have endured a boom and bust cycle within their credit-fuelled housing markets. Admitting geographical variation, Lapavitsas and Powell (2013) divided the five major economies studied (the US, the UK, France, Germany and Japan) into two groups with regard to household debt. The first, described as "eager financialisers," are the US and the UK, which have seen high levels of household debt relative to disposable income (over 100%) during the past decades, a trend that gained pace during the years 2001-2007. Germany, France and Japan have considerably lower levels of household debt relative to total income, thus being classified as "reluctant financialisers." All have nevertheless endured periods of strong household debt ratios: Japan during the 1980s, Germany during the 1990s and France during the 2000s, all coinciding with major rises in housing prices. Lapavitsas and Powell recognise the overwhelming role of mortgage debt in these trends. In fact, the social content of household debt seems to have been clearly related to the evolution of housing markets, normally the good that consumes the largest part of households' expenses. With changes in public regulation and the availability of capital to play an important role in the structuring of this market, most developed countries have endured strong boom and bust cycles in their real estate markets. Japan had its real estate bubble during the 1980s, whose bursting in 1989 condemned the economy to a prolonged period of stagnation. Germany saw the same trend during the 1990s after the reunification. The burst of this bubble condemned the German housing market to a long period of stagnation. Finally, increasing French household debt can be traced to the 60%rise in the ratio of the housing price index to disposable income during the 2000s, after thirty years of stability. As Thrift and Leyshon (2007) pointed out, these observations show that growth in household debt is not necessarily correlated with the new securitisation and the related propulsion of financial speculation, but mainly reflects the evolution of housing prices, which, on the one hand, force households to incur increasing amounts of mortgage debt and, on the other hand, provide the collateral needed for banks to lend and reinforce price booms.

Analysis of the financialisation of households should not, however, be restricted to its more salient feature: debt. Households have also increasingly been holders of financial assets: pensions, mutual funds and shares. Again here, Lapavitsas and Powell (2013) signalled the geographical variation in the prevalence of household financial assets, between the US and the UK on one hand and France, Germany and Japan on the other. In France, however, households' involvement in the market for shares and pension and insurance funds has been rising. Yet the type of financial assets held by households seems to be heavily related to the incentives provided by public policies, such as the privatisation of public companies and the erosion of public pension schemes and the accompanying migration toward more private arrangements. Dos Santos (2009) points to the high cost of these new dealings for households in the form of commissions and fees which may lead to a situation where "the return realised by the average equity mutual fund investor is not much higher than rates available for long-term savings deposits" (2009: 198). Financial expropriation from households is not therefore limited to debt, but encompasses the assets held by this sector, as they further prove both the increasing income coming from households and their new social vulnerability with the privatisation of public social security provision.

The comparison of the reality in developed countries with that of a middle-income country such as South Africa should be helpful in assessing the financialisation of households and financial expropriation in geographical settings whose role in the international economy and whose financial and non-financial sectors are different from their developed country counterparts, as explored in the previous chapters. We have seen that bank household debt and bank income from South African households has been increasing, despite the still-small market for debt securities. The impact of these trends on South African households in the relative weight of debt in their balance sheets, their debt servicing costs relative to income and the distribution of debt among different income levels, as well as their holdings of financial assets and the related costs, remain to be examined.

7.3. Financial expropriation of South African households

In order to assess the evolution of the financial position of South African households, we start with their balance sheet position. However, some caveats apply to the use of this instrument; this analysis is thus followed by a more detailed dynamic examination of households' financial engagement using flow of funds data, in both net and gross forms. Through this data the expected higher indebtedness is shown to be present not only in absolute terms, but also relative to disposable income. The rising share of household income going to banks becomes evident. This empirical assessment proves crucial in the identification of financial expropriation in the country, as households are increasing captured by the financial sector. This power asymmetry is particularly evident within the mortgage debt market. Faced with a boom in housing prices, households incur rising levels of banking debt in order to access this good, since the price of the collateral seems to be growing non-stop at a rate that far outpaces inflation. And while debt is the main relation that characterises financial expropriation, it is important to scrutinise household financial assets, as they provide further evidence of the power relation between households and the financial sector, especially in the case where pension systems are mostly private and thus force households to resort to the financial sector in order to secure their retirement. The associated costs are integrated into the analysis as further evidence of rising financial sector income coming from households.

These data, although accounting for change in the financial interactions between households and the financial sector at the macroeconomic level, should be taken with caution. Flow of Funds and Household Balance sheet data are the result of an accounting aggregation of all households present in the formal economy. Households belong to different social classes. The analysis present is this chapter does not allow for an assessment of the financial expropriation hypotheses in the stricter sense that it mainly affects workers and not the most privileged. The power relations relations present between the banking sector and different classes cannot be thus identified in their asymmetry. Nonetheless, the analysis of aggregate evolution of household financial flows and wealth will allow the pinpoint of common trends between South Africa and core-developed countries where financial expropriation was identified. Further cross examination of the household financial dealings and their disaggregate social position (income and race) is provided in the next chapter.

7.3.1. Household balance sheets

Our starting point relies on the South African Reserve Bank's estimates of household sector balance sheets, running from 1975 to the present, and which have been published in the SARB Quarterly Bulletin since 2006. This work has been carried out by Janine Aron, John Muellbauer and Johan Prinsloo, building on the work of the Office of National Statistics of the United Kingdom (Aron et al, 2006, Aron and Muellbauer, 2006). These balance sheets are built using data from different sources, namely the DI 900 returns of South African banks, flow of funds accounts, and the Johannesburg Bond Exchange.

The evolution of the ratio of total household assets to disposable income shows that the period between 1994 and 2009 can be broken down into two different periods. From 1994 to 2002 this ratio was decreasing, going from 3.73 to 3.31, but from 2002 to 2009 the ratio picked up again, reaching 4.13 (Table 7.1). Financial assets are the most relevant category to explaining this trend, particularly within the non-banking assets sector (interest on pension funds and long-term insurance). However, the evolution of the role of "residential buildings" as a household asset should be stressed. Its growth relative to disposable income has been constant, with the ratio starting at just 0.64 in 1994 and attaining 1.1 in 2009. The scale of household liabilities relative to disposable income has also been growing, but apparently at a slower rate. The mortgage debt ratio increased from 0.33 1994 to 0.52 in 2009, decreasing during the 1994-2002 to 0.29 and rising again for the rest of the 2000s. The ratio of "other debt" to all disposable income rose at a slower rate in relative terms, from 0.27 in 1994 to 0.30 in 2009. Finally, the total net wealth of South African households seems to have progressed, its ratio increasing from 3.12 to 3.31 for the whole considered period —again, with a decreasing trend from 1994 to 2002. Household balance sheet data thus shows growing wealth, with assets growing more than liabilities.

These figures should, however, be interpreted with caution as they involve a number of assumptions that limit their implications on how household net wealth is linked to the evolution of asset prices (both financial and residential). In the context of rising debt and asset prices, as during the mid-2000s, balance sheet expansion seems well-balanced, but in the context of declining and stagnating housing prices and financial turmoil, as was the case during the 2008-2009 period, asset wealth naturally declines more steeply than liabilities (Table 7.1), although the burden of the latter was nonetheless cushioned by a decline in interest rates.

Table 7.1. Household balance sheets relative to annual disposable income.

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Non-financial assets	**0.96**	**0.90**	**0.86**	**0.87**	**0.87**	**0.85**	**0.86**	**0.89**	**0.91**	**1.00**	**1.17**	**1.27**	**1.34**	**1.38**	**1.30**	**1.31**
Residential buildings	*0.64*	*0.60*	*0.56*	*0.58*	*0.59*	*0.58*	*0.62*	*0.64*	*0.67*	*0.76*	*0.94*	*1.04*	*1.12*	*1.16*	*1.09*	*1.10*
Other non-financial assets	*0.32*	*0.30*	*0.30*	*0.29*	*0.28*	*0.27*	*0.25*	*0.24*	*0.24*	*0.24*	*0.23*	*0.23*	*0.22*	*0.22*	*0.21*	*0.21*
Financial Assets	**2.76**	**2.70**	**2.64**	**2.49**	**2.35**	**2.66**	**2.51**	**2.64**	**2.40**	**2.42**	**2.53**	**2.76**	**3.07**	**3.09**	**2.63**	**2.82**
Assets with Monetary Institutions	*0.48*	*0.41*	*0.40*	*0.41*	*0.41*	*0.36*	*0.34*	*0.34*	*0.35*	*0.36*	*0.35*	*0.35*	*0.36*	*0.37*	*0.40*	*0.39*
Interest in pension funds and long-term insurers	*1.47*	*1.55*	*1.52*	*1.45*	*1.36*	*1.41*	*1.37*	*1.41*	*1.31*	*1.27*	*1.36*	*1.42*	*1.59*	*1.58*	*1.40*	*1.46*
Total household assets	**3.73**	**3.61**	**3.50**	**3.36**	**3.22**	**3.51**	**3.37**	**3.53**	**3.31**	**3.42**	**3.70**	**4.03**	**4.41**	**4.47**	**3.93**	**4.13**
Total household liabilities	**0.60**	**0.64**	**0.65**	**0.65**	**0.62**	**0.59**	**0.57**	**0.57**	**0.54**	**0.57**	**0.62**	**0.70**	**0.79**	**0.86**	**0.84**	**0.82**
Mortgage debt	*0.33*	*0.34*	*0.35*	*0.34*	*0.34*	*0.31*	*0.30*	*0.29*	*0.29*	*0.30*	*0.34*	*0.40*	*0.47*	*0.53*	*0.53*	*0.52*
Other debt	*0.27*	*0.30*	*0.31*	*0.30*	*0.29*	*0.28*	*0.27*	*0.28*	*0.26*	*0.27*	*0.28*	*0.30*	*0.32*	*0.33*	*0.31*	*0.30*
Net wealth	3.12	2.97	2.85	2.71	2.59	2.92	2.80	2.96	2.77	2.85	3.08	3.33	3.62	3.61	3.09	3.31

Source: Computed from SARB data

This data are, however, still valuable for assessing the recent rise in aggregate household debt and its link with housing assets. Data shows that South African households have had what seems to be a surprisingly similar pattern with those of households in developed countries, which endured a parallel rise of debt and housing prices. The evolution of housing prices in South Africa during the 2000s was staggering, with nominal prices increasing 348% between 2000 and 2009 (it should, however, be noted that real prices dropped by 6.2% and 6.8% in 2008 and 2009). It was during the expansion of mortgage debt between2003 and 2007 that prices saw their biggest increase, with real average prices growing 108% between 2003 and 2007, according to ABSA data[93] (Figure 7.2). The growth of household balance sheets throughout the 2000s should thus be set against a background of record housing price increases and booming financial markets, which halted during the international economic crisis. A more detailed analysis using the household flow of funds analysis is thus needed in order to examine households' financial position throughout the post-apartheid period.

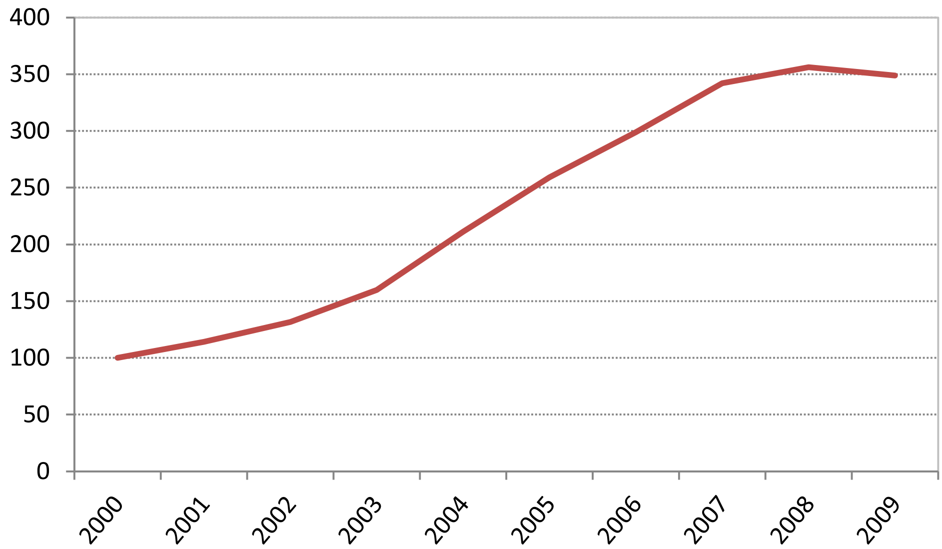


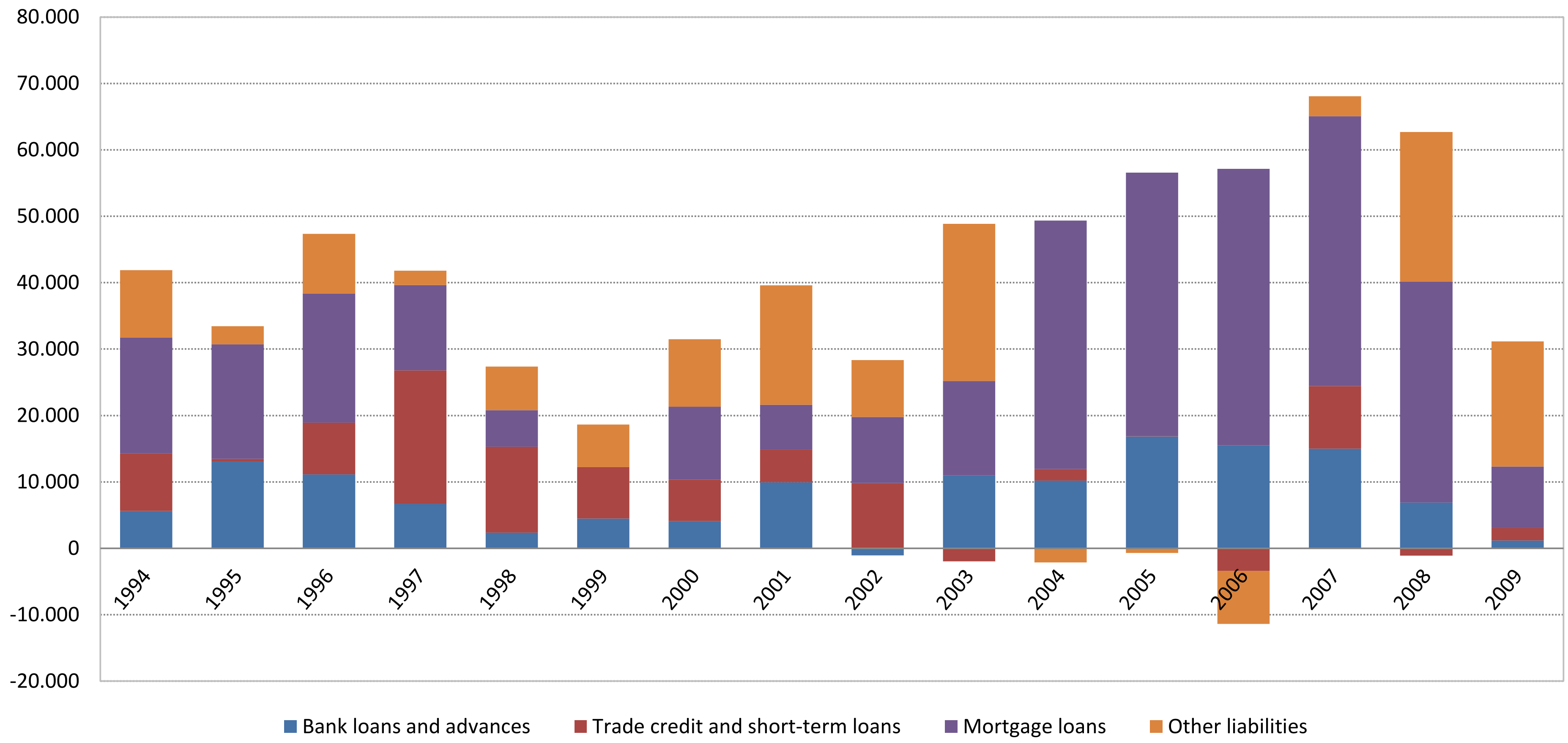
Figure 7.2. ABSA House Price Index (2000=100, nominal prices).

[93] Absa housing prices data are the most-used source data on the evolution of this market in South Africa.

7.4. Flow of funds analysis

7.4.1. Liabilities

Flow of funds data provide a more accurate perspective on the trends among households and in the South African financial sector, since they capture the financial flows from households to other sectors of South African economy for each year, thus overcoming the problems identified above with asset financial — and non-financial — valuation in the balance sheets. Figure 7.3 shows the flow for liabilities of households, unincorporated companies and non-profit organisations. Sources of funding for households are concentrated in three main categories: mortgage debt, other bank loans, and trade credit and short-term loans. Mortgage loans have been the main category of liability growth, more than doubling in real value from 17,247million rand in 1994 to a record high 41,652 million rand in 2006 at 1994 prices, and from 5.6 to 8.9% of disposable income for the same period. This increase is particularly clear during the 2003-2007 period, growing from 3.5% of disposable income in 2003 and thus becoming the main category of household debt (Table 7.2). Other bank loans, after a strong rise in 1995 to 13,063 million rand (4% of disposable income), declined in subsequent years, actually dipping to -1,072(-0,027%of disposable income in 2002), recovering afterwards to 16,030 million rand in 2005 (3.7% of disposable income) and almost vanishing during the 2008-2009 crisis. This pattern is coherent with the stagnation of the value of household debt other than mortgages held by banks during the 1990s and their subsequent rise after 2003 to 2007, as pointed out in the analysis of banks' balance sheets in the previous chapter. Finally, the behaviour of the liability category "Trade credit and short-term loans" was exactly opposite that of other bank loans, increasing in percentage of relative disposable income in years of lower consumer credit engagement with banks. This category thus seems to be related to consumer credit extended by the corporate non-financial sector. This category of debt, after playing an important role during the second half of the 1990s—between 2.81% in 1994 and the record 5.7% of disposable income in 1997—almost disappeared in the bank credit boom between 2003 and 2007.



Source: Computed from SARB National Financial Account

Figure 7.3. Flow of funds, selected liabilities (Mn rand, 1994 prices).

Table 7.2. Flow of funds relative to disposable income.

LIABILITIES																
	1994	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**
Bank loans and advances	0.0182	0.0402	0.0329	0.0190	0.0066	0.0126	0.0110	0.0269	-0.0027	0.0270	0.0236	0.0374	0.0333	0.0311	0.0139	0.0025
Trade credit and short-term loans	0.0281	0.0012	0.0230	0.0570	0.0363	0.0216	0.0167	0.0132	0.0248	-0.0048	0.0041	0.0001	-0.0073	0.0196	-0.0022	0.0039
Long-term loans	0.0102	0.0171	0.0122	0.0009	0.0016	0.0054	-0.0056	0.0025	0.0123	-0.0005	-0.0037	-0.0004	0.0000	-0.0004	-0.0001	-0.0010
Mortgage loans	0.0564	0.0532	0.0574	0.0364	0.0155	-0.0003	0.0293	0.0183	0.0252	0.0352	0.0865	0.0882	0.0896	0.0844	0.0671	0.0192
Amounts payable	-0.0002	0.0021	-0.0015	0.0006	0.0045	0.0011	0.0015	-0.0012	-0.0003	0.0007	0.0001	-0.0046	0.0166	0.0382	0.0268	-0.0001
Other liabilities	0.0329	0.0083	0.0265	0.0061	0.0184	0.0179	0.0272	0.0486	0.0217	0.0584	-0.0049	-0.0015	-0.0172	0.0062	0.0455	0.0390
ASSETS																
Bank Deposits	0.0461	0.0360	0.0417	0.0450	0.0113	-0.0181	0.0221	0.0297	0.0401	0.0330	0.0293	0.0293	0.0396	0.0495	0.0569	0.0100
Deposits with other institutions	0.0000	0.0130	0.0179	0.0366	0.0321	0.0515	0.0315	0.0173	0.0313	0.0442	0.0119	0.0136	-0.0071	0.0140	0.0150	0.0108
Trade Credit and Short-term loans	0.0074	0.0062	0.0022	0.0052	0.0056	0.0028	0.0005	0.0049	-0.0054	0.0040	0.0049	-0.0032	0.0045	-0.0044	0.0016	-0.0005
Public securities	-0.0063	-0.0077	-0.0011	-0.0011	-0.0015	0.0035	-0.0025	-0.0005	-0.0024	-0.0001	0.0011	0.0005	0.0011	-0.0016	0.0000	0.0018
Other loan and stock and preference shares	-0.0002	0.0000	0.0001	-0.0005	-0.0001	0.0009	0.0025	-0.0012	-0.0004	-0.0001	0.0000	0.0000	0.0000	0.0001	0.0000	0.0000
Ordinary shares	0.0231	-0.0047	-0.0023	0.0117	-0.0025	0.0106	-0.0179	-0.0073	-0.0080	0.0118	0.0003	-0.0002	0.0001	0.0000	0.0001	0.0000
Long-term loans	-0.0018	-0.0018	0.0015	0.0001	0.0001	0.0014	0.0014	0.0011	-0.0070	0.0023	0.0017	-0.0001	0.0000	-0.0001	0.0002	0.0001
Interest in retirement and Life funds	0.1312	0.0987	0.1107	0.0802	0.0778	0.0537	0.0757	0.0690	0.0716	0.0802	0.0544	0.0493	0.0479	0.0975	0.0614	0.0434
Other Assets (amounts receivable + other assets)	-0.0120	-0.0023	-0.0036	-0.0405	-0.0247	-0.0306	-0.0211	0.0048	-0.0295	-0.0392	-0.0017	0.0156	0.0021	-0.0004	0.0001	-0.0003

Source: Computed from SARB National Financial Account

7.4.2. Assets

Three categories of assets stand out from the flow of funds data: interest in pension funds and life insurers; bank deposits; and other deposits. Interest in retirement and life insurers—which includes investment in official and private self-administered pension and provident funds—have played the most important role as recipients of household savings. With between 20,000 and 40,000 million rand at 1994 prices for the whole period (Figure7.3) - and 13%of all disposable income being directed to these assets (Table 7.2).Their role has nevertheless decreased from its levels during 1994-2000, when it averaged almost 9%of all disposable income, versus 6.4% during the 2000s.

Bank deposits are the second largest class of household assets, with households bank savings to be aligned with the general economic growth of the economy, being particularly low or negative in years of low growth such as 1998-1999 – 4,000 million rand in 1998 and - 6,000 million rand in 1990at 1994 prices (Figure 7.3), corresponding to 1,1% and -1.8%of disposable income (Table 7.2) - and particularly high in the years of stronger economic growth 2004-2007 – between 12,246 million and 28,178 million rand at 1994 prices (2.9-5.7%of disposable income).

Other deposits, which mainly consist of deposits with other financial institutions such as (mutual) unit trusts, participation in mortgage bond schemes, trust companies, finance companies and public financial companies, are also important recipients of household savings (Figure 7.3). The role of this class of assets relative to disposable income declined a little between the 1990s (2% average) and the 2000s (1.8% average), but nonetheless, coupled with pension funds and life insurance policies, shows the significance of the South African shadow banking system for households. Finally, there is little evidence of households investing significantly in public or private securities ("Other loan stock and preference shares" and "ordinary shares") (Table 7.2), showing low desire for the direct holding of debt securities.

More importantly, the evolution of financial flows in households' asset financial flows did not match the one of liabilities. It has remained stable in real terms (Figure 7.4), with just the years of 2007 and 2008 standing apart, showing the increasing relevance of debt relative to the one of financial assets and thus the degrading of the household financial position in opposition to what seemed a balanced outlook from the households' balance sheets.

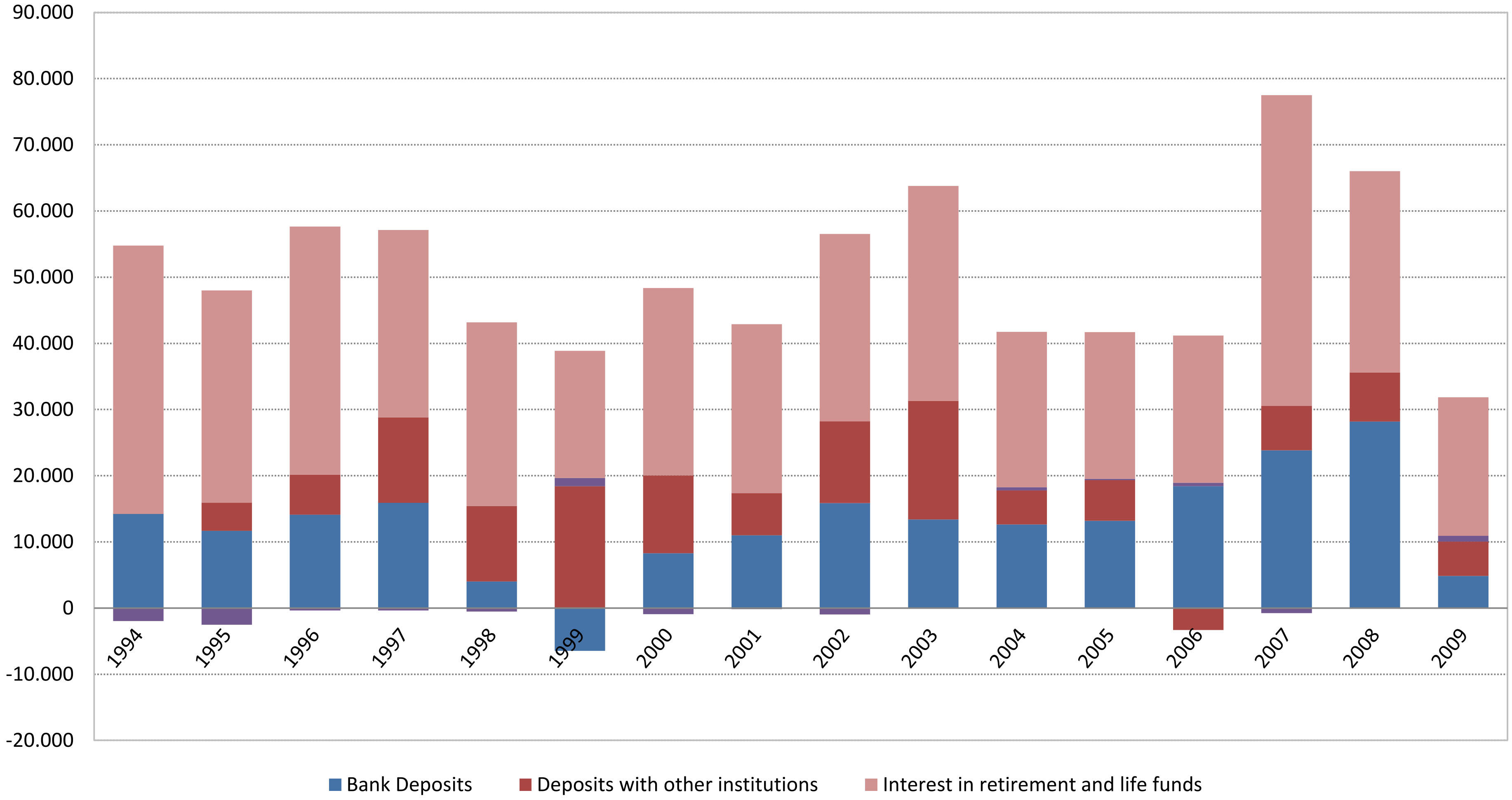
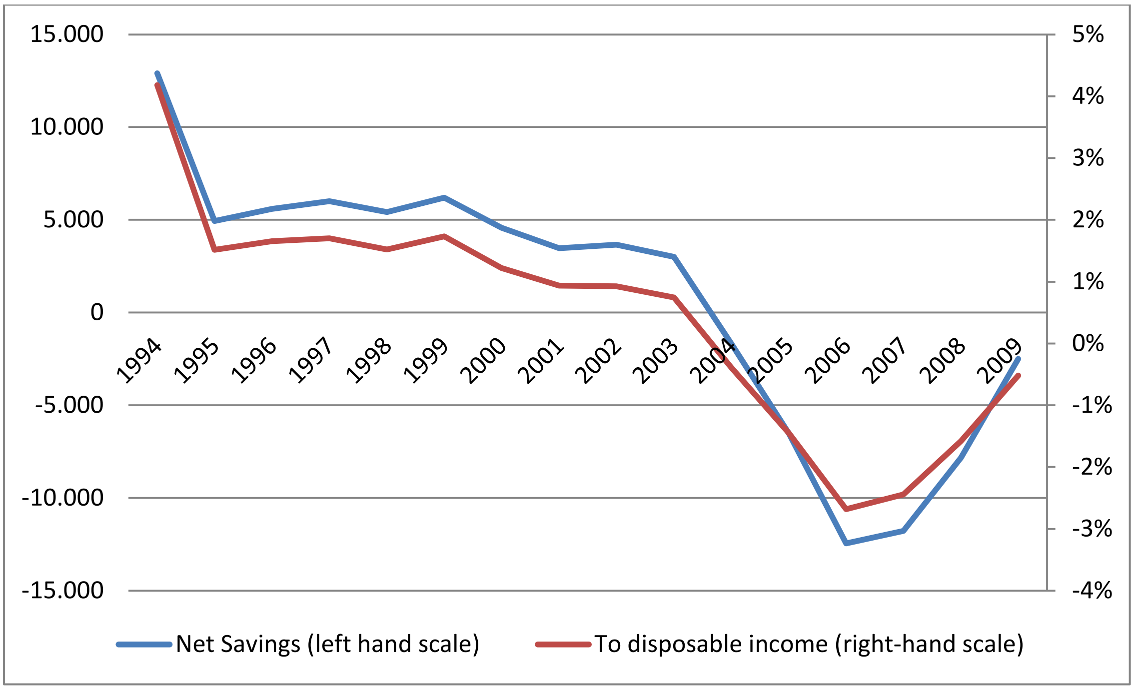


Figure 7.4. Flow of funds, selected assets (Mn rand, 1994 prices).

Source: Computed from SARB National Financial Account

7.4.3. Household financial position

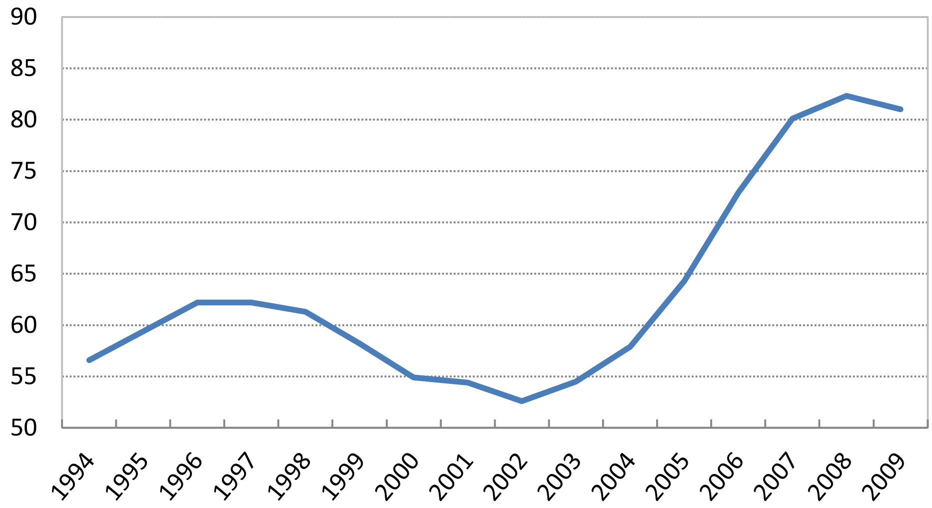
This difference between the stability of asset use and changing sources of funds seen in the gross flow of funds figures (7.3 and 7.4) explains the negative evolution of the household sector, from a net lender of funds to a net borrower, between 2004 and 2009 (Figure 7.5). Household sector savings as a percentage of disposable income, which were already low during the 1990s (below 2%), collapsed to negative levels (-3% in 2006) from 2003 to 2009. These data thus show an evolution similar to that seen in the most developed countries, such as the US, where household savings have been low (Lapavitsas, 2009) but a much faster pace (American households had a record low savings rate as a proportion of disposable income of 0.4% in 2007).



Source: Computed from SARB National Financial Account

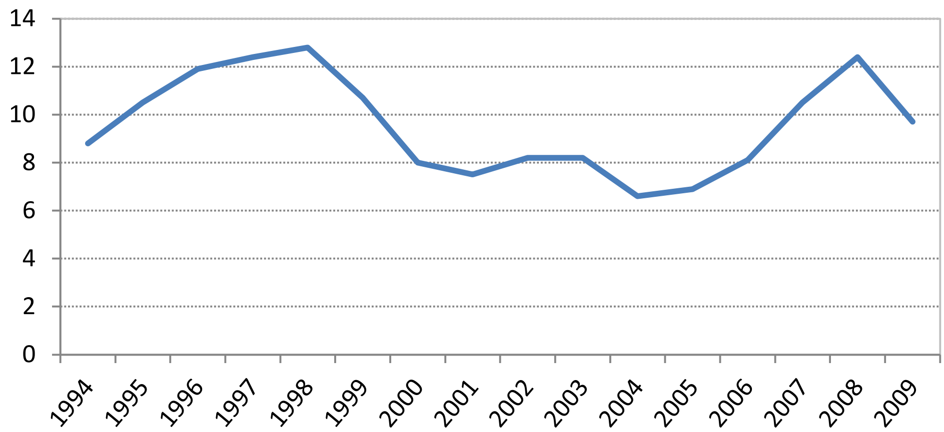
Figure 7.5. Net Savings, (Mn rand, 1994 prices).

Further evidence of the degradation of households' financial position can be seen in the growth of total household debt relative to disposable income (Figure 7.6). After decreasing to minimum of 52.6% in 2001, it rose to a record high 82.3%in 2008, a rise that was concentrated intheyears2004-08. Despite this steep progression, these levels are still lower than those observed for some of the developed countries. The debt service cost—the percentage of disposable income spent on interest payments—has risen accordingly, almost doubling, from 6.4% in 2004 to 12.3% in 2008. This debt service cost still falls behind the high levels observed during the second half of the 1990s, but its origins are different in the two periods. The second half of the nineties witnessed historic highs in real prime interest rates (13.2% in 1998) whereas levels of real prime interest rates during 2004-2008 were relatively lower (between 4.6 and 5.7%: World Bank Development Indicators). The recent rise of debt service costs is therefore related more to the household debt stock than to interest rates. Recent estimates of debt service costs that include these rising payments on principal show a substantial increase in the estimated household debt service ratio when compared to just the interest rate debt service ratio (Mokoena, 2008).



Source: SARB

Figure 7.4. Ratio of household debt to disposable income (%).



Source: SARB

Figure 7.5. Debt service to disposable income (%).

7.4.4. Discussion

South African households as an aggregate have gone through the same trends as those in other countries where booming housing prices have been coupled with even faster growth in mortgage debt. Those in South Africa saw their net financial position deteriorate rapidly, attaining negative savings rates, unseen in the most developed countries. Due to the steep fall in real interest rates during the international financial crisis—from 5.7% in 2008 to 1.5% in 2010 (World Bank Development Indicators), the costs of debt service have dropped, thus allowing for a softer landing from the boom than in the most developed countries. However, growth in the amount of debt coupled with the volatility of interest rates in South Africa raise new doubts as to the sustainability of this new debt burden in the case of a new interest rate hike.

The social content of financial expropriation, not only as a rising stream of revenue from households to the financial sector but as a new power relation between the two sectors, is confirmed by these data. Rising indebtedness is reflected in the transfer of a larger share of income to the financial sector as measured by debt service costs (with banks as the main recipient) and a rise in the stock of debt to record levels, putting households in a greater vulnerability vis-à-vis the banking sector and the overall evolution of the economy, particularly given the historical volatility of interest rates in South Africa.

Furthermore, this increasing vulnerability is stressed by the major category of debt incurred by households, mortgages and, relatedly, booming housing prices. Once again, South Africa seems to have followed the pattern seen in the most developed countries. It should be noted, however, that the character of the debt relation between households and banks on South Africa has distinct aspects, given the much higher real interest rates charged in this country. The result of a strict monetarist policy by the SARB in order to attract the foreign capital flows that pushed domestic credit extension, these higher interest rates may explain the more extreme evolution of the financial position of households in the country—expressed through both their negative net financial position during the second half of the 2000s and the extraordinary housing price growth of the same years.

The formidable scope of household debt must not divert our attention from the second type of relation that households stand in with the financial system: as asset holders, particularly in private accounts in pension and mutual funds. As seen in flow of funds data, despite a stagnating level of purchasing of financial assets in real terms during the post-apartheid period, South African households have concentrated their financial holdings in three categories of assets: deposits with banks, deposits with other financial institutions (mainly mutual funds), and retirement and insurance products.

The most exhaustive work on the costs of insurance, pension and mutual funds is that of Rob Rusconi (2005), who measured explicit[94] administrative charges of different savings instruments for South African households. Given the opacity of the sector and the complexity of fee structures, this is a difficult exercise. Not only is access to information difficult, but a number of ambitious assumptions must be made concerning inflation, wage and return growth per year (5%, 7%, and 10%, respectively). Nonetheless, for South African pension fund costs, the reduction in yield (RiY) could go from 0.86% to 2.36% per year, resulting in charge ratios of between 13.4% and 38.4% for a 40-year period. Pension fund charges in South Africa seem to be amongst the highest in the world, with Rusconi cautiously concluding that:

> (…) it appears that, in comparison with most countries, South African retirement funds are expensive to run. The exceptions include the UK occupational-scheme environment, one or two of the newly established national systems and the sophisticated sectors of the Australian environment." (Rusconi, 2005: 113)

This finding of high retirement fund costs in South Africa has been confirmed by more recent research. Gluckman and Estheruysen (2011) researched the Sanlam Umbrella Fund, a commercial umbrella retirement fund (with occupational sub-funds for a number of employers) sponsored by Sanlam. Under slightly different assumptions, the authors calculate a mean 1.9% RiY and a charge ratio of 18.7% for this particular fund, with a clear regressive distribution. The corresponding figures for wages under 3,000 rand (25% of the sample) were 2.5% RiY and 24.5% charge ratio.

Our initial analysis of flows of funds also drew attention to the importance of deposits in financial institutions other than banks, such as mutual funds (normally known in South Africa as unit trusts), particularly at the end of the 1990s and the beginning of the 2000s. Unit trusts are collective financial investment mutual funds that normally specialize in particular classes of financial assets (money market, bonds, equities, international assets, etc.). Rusconi (2005) also analysed the costs of these savings products, concluding that for a

[94]The study only looks at explicit charges, and not implicit one such as trading charges, which are reflected in the reduction of portfolio value or/and the prices of unit trusts.

40-year saving period[95], RiY could range from 0.74% a year for “cash” funds (14.14% charge ratio) to 1.87% RiY (31.65% charge ratio) for international investment funds, with the overall average of RiY at 1.58%. According to Rusconi, these costs compare reasonably well with those in the US, despite being considerably higher due to the economies of scale and competitive environment in the latter. However, the high costs of these products to investors, the high volume of income transfers through these savings instruments—in which households play a considerable role—thus provide proof that financial expropriation encompasses not only the most salient form of relation between households and banks (debt), but also household assets.

7.5. Conclusion

This chapter began with a theoretical overview of household finance. Having established the ahistorical and abstract character of neoclassical approaches, both in strong rational-choice and more flexible behavioural approaches, we turned to political accounts of financialisation. Not only are these accounts able to provide a theoretical framework that integrates the historic and social content of the last decade’s transformations in household finance in developed countries, but they are more robust in their approach to the international financial crisis of 2007-08, which had household finance at its center. The concept of financial expropriation is of paramount importance here, but the limitation of existing research was its exclusive deployment in the context of the developed countries, which lay at the center of the crisis.

The financial expropriation concept of Lapavitsas (2009) was scrutinised in the context of a middle-income country, South Africa. Findings on this country confirmed the applicability of this concept, as South African households have endured increasing levels of debt and costly financial savings arrangements, which result in a growing stream of income transfer to the financial sector. This has overwhelmingly taken the form of mortgage debt, which rose steeply during the years 2004-08. Despite the declining interest rates that bolstered the rise in debt, South African interest rates are still very high when compared to other economies.

[95] Rusconi uses the same macro-economic assumptions outlined above, assuming an ambitious 10% annual return on investments 10% and annual growth in contributions of 7%. It should be noted that smaller saving time spans involve considerable higher RiYs and charge ratios.

This debt expansion was accompanied by a parallel extraordinary rise in housing prices, at a rate not seen in the most-developed countries. The sustainability of this debt expansion depends thus on the maintenance of an equivalent increases in household wealth through rising housing prices, to compensate increasing debt service costs. Still, the acceleration of the capital circuit in the country through rising household debt allowed increased consumption levels and rising financial profits from households. The growth of this new debt market made possible the exponential growth of the financial sector during the mid-2000s.It also explains the increase in investment in sectors such as retail trade and construction.

The same asymmetric portrait emerges from an examination of households' involvement with financial assets. In the absence of a public system, only a small part of the population, normally those who benefit from formal labour relations and saving capacity, has access to private retirement arrangements. In South Africa there are no mandatory pension schemes. Still, under apartheid, civil servants feared that the transition to democracy would entail failure to honor previous pension arrangements. Public pensions were migrated to a fully funded scheme (Hendricks, 2008). Although they are concentrated among the most affluent, pension and retirement funds are the overwhelmingly dominant forms of household investment in financial assets. New forms of savings, such as mutual funds which profit from the booming capital and money markets, also receive a significant amount of the savings of the most affluent households. But the literature on the costs of these arrangements shows that South African households pay higher costs for these instruments in the form of commissions and fees than those in most countries.

In light of the empirical data presented here, it seems clear that South Africa's subordinate position in the international financial sphere has led to higher costs for households through debt relations than are seen in developed countries. The requirement of high real interest rates in order to sustain capital flows, and the almost complete non-existence of public provision arrangements that mimetise market dynamics, means that the expansion of household debt and its consequences are replicated here at a higher and more concentrated level. Additionally, the power asymmetry faced by households vis-à-vis of the financial sector is further enhanced by financial institutions' particular position within the South African economy. Contrary to what was pointed out for the big South African corporate conglomerates, households lack the same access to international financial markets, and are thus bound to resort to the domestic banking sector. They are burdened not only by the replication of household indebtedness relations within South Africa, but also by the asymmetric domestic impacts of the country's subaltern position in the international sphere.

Nonetheless, while on the one hand some of the trends observed in developed countries are present here in a more salient form, on the other hand, with household debt reaching more than 80% of disposable income and debt service to disposable income ratios reaching a record level of 12%, these figures still lag behind what has been seen in more developed countries. A contradictory picture of the South African households' financial position therefore begins to emerge. These apparently contradictory results are the result of specificities of South African population, with its high unemployment and poverty rates and acute inequality, which are hidden from our aggregate analysis. Further analysis in the next chapter is thus needed to better grasp the specific content of the concept of financial expropriation that, as shown above, specifically requires that inequality and the role of social provision be examined.

8. Debt and inequality in South Africa

8.1. Introduction

In the previous chapter of this thesis the assessment of the financialised aggregate profile of South African households was presented. It was shown that a rising share of South African households' income is devoted to paying mortgage debts and that their financial position has worsened, particularly over the course of the post-2003 financial boom years. The balance between liabilities and assets seemed to rest on the fragile foundation of steeply increasing housing prices. A pattern of financial expropriation (Lapavitsas, 2009), understood as the systematic extraction of income from households by banks, with the latter benefiting from the power leverage of standing between households and essential assets (such as housing and pensions), was shown for the South African case.

However, having apparently followed a similar financial path to their developed countries' counterparts, South African households' aggregate financial position is somewhat contradictory. Burdened by extraordinary increases in house prices, eventually leading to a negative savings position, the ratio of aggregate debt and debt-service to disposable income during the 2000s was nevertheless below the levels observed in the most-developed countries.

In this chapter we examine another aspect of the concept of financial expropriation, namely its relation with income inequality. Accounts of this issue in developed countries have stressed how changes in banks—such as the introduction of debt securitisation—coupled with the vulnerability created by rising inequality among households have led to increasing and unsustainable household indebtedness among the poorer segments of the population, which, in turn, has deepened the dynamic of inequality in these economies. Given the middle-income character, huge inequality, and recent political transformations in South Africa, a possible unequal expansion of household debt needs to be scrutinised in order to shed further light on the apparently contradictory portrait of household indebtedness set out in the previous chapter.

Thanks to public policy efforts to expand access to formal financial services coupled with the power of an oligopolistic banking market structure, formal (but unsecured) debt is present among almost all household income categories in South Africa. However, I argue that the expansion of household debt has been asymmetric and with regressive impacts, taking on a particular configuration in South Africa, wherein the greatest share of household debt (in the form of mortgages) is concentrated in the most affluent layers of society. I argue that a regressive distributional outcome emerges from this peculiar distribution of debt among households, with the most affluent households benefiting from lower debt costs compared with the usurious prices paid for consumer debt by poorer people. I argue that the asymmetric and regressive impact of the expansion of household finance has taken on a particular configuration in South Africa, wherein the greatest share of household debt (in the form of mortgages) is concentrated in the most affluent layers of society. Yet, thanks to public policy efforts to expand access to formal financial services coupled with the power of an oligopolistic banking market structure, formal (but unsecured) debt is present among almost all household income categories. I argue that a regressive distributional outcome emerges from this peculiar distribution of debt among households, with the most affluent households benefiting from lower debt costs compared with the usurious prices paid for consumer debt by poorer people.

This chapter is organised as follows. I start with a brief discussion of inequality in the context of rising household indebtedness in developed countries and its regressive impacts. I then provide an overview of the social conditions of South African society in terms of employment, inequality and housing provision during the last decades, in order to explain the different pattern of unequal access to debt markets in comparison with what has been seen in the US and UK. In the third section, I present public policy efforts in favour of financial inclusion and regulation of the consumer credit market. I then analyse households' different levels of engagement with the financial sector. Household debt distribution and prices across different layers of the population are analysed, in connection to the efforts towards public financial inclusion. Through recent official surveys conducted both among formal credit providers (such as the Feasibility survey (NCR, 2011)) and households (Finscope survey (Finmark, 2009) I show that the income regressive impact of the extension of household debt and related problems of over-indebtedness were already present in South Africa before the 2008 international financial crisis and its impact on the domestic financial sector and housing market.

8.2. Debt and inequality

Inequality has been a recurring theme in analysis of the subprime crisis and more generally in the context of the rising engagement of households with finance. The financial expropriation argument of Lapavitsas (2009) rests on a supply and demand analysis of household debt where inequality is central.

On the supply of credit side, as argued and empirically documented by Dos Santos (2009) and Lapavitsas (2009) for developed countries, increasing lending to households was only possible because of financial institutions' expansion of credit to previously excluded poorer households, the most notable case of this phenomenon being the rise of the subprime market in the US. Progresses in information technologies enabled improved assessment of individual risk, but also—and this is of paramount importance here—to disperse risk more efficiently (Lapavitsas and Dos Santos, 2008).

Securitisation was seen as a major breakthrough in this apparent technological progress toward extending credit to new layers of the population. Thanks to the growing liberalisation of financial markets, allowing commercial banks direct access to investment banking activities in securities markets, bank credits were transformed into securities—most notably into mortgage-backed securities—which could then be passed on to financial markets, disappearing from commercial banks' balance sheets. Divided into different "tranches" of risk, these securities were presented as allowing a more efficient allocation of risk and capital. With the standardisation of credit and growing demand for these securities, banks were able to separate loan making from risk-bearing activities (Dymski, 2009). The result was greater liquidity in the consumer credit market and increasing confidence to expand credit to less credit-reliable (poorer) households.

If the new standing of financial institutions gave them leverage in their relation to households, that fact alone does not suffice to explain the explosion of consumer credit. In fact, it can only explain the availability (supply) of consumer credit, not its engagement (demand). Only by considering the growing vulnerability of workers in relation to finance can that growth be explained. This vulnerability has many dimensions closely related to the emergence of neoliberalism, but thirty years of wage stagnation and rising inequality have been presented as central reasons for households' increased engagement with finance. At least in the US, the median wage has stagnated since the 1970s—with a brief increase during the second half of the 1990s —after 3-5% growth rates during the 1960s. Wage differentials have been growing, especially in Anglo-Saxon economies such as the US and the UK, increasing social inequality (Glyn, 2006). This trend has been combined with the erosion of social benefits and the retreat of public provision from an important set of goods (housing, health, education) (Lapavitsas, 2008), therefore pushing individuals into the arms of the financial system.

But why should stagnant income and rising inequality lead to growing debt? In this context, institutional economics may be of help, being one of the few heterodox currents which provide a theoretical framework that relates consumer behaviour with the credit system. This can be credited to one of its founders, Thornstein Veblen. This author's analysis of "emulative consumption" offers important insights on the current behaviour of the American working class. He defines it as "a wish to conform to established usage, to avoid unfavourable notice and comment, to live up to the accepted canons of decency in the kind, amount, and grade of goods consumed" (quoted in Adkisson and McFerrin, 2005: 115). While emulative consumption follows the neoclassical stance that "more is better," it also grants social meaning to consumption. Levels of consumption reflect not individual, idiosyncratic, optimizing preferences, but a relationship to the social context, wherein comparison with others provides a heuristic for the evolution of consumption behaviour. This social understanding of consumption may explain why consumers do not easily adapt their levels of consumption to their wealth and income, since "any retrogression from the standard of living which we are accustomed to regard as worthy (…) is felt to be a grievous violation of our human dignity" (Veblen [1899] 1994: 156 in Scott 2007). This feeling of violation of human dignity may then explain why consumers will indebt themselves in order to maintain consumption levels, even though the choice to do so may be myopic and unsustainable or, at the least, more expensive in the long run. Nonetheless it should be noted that much of this consumption—on education, health and even conspicuous consumption—should be seen as necessary for social reproduction.

Weller (2007) provides a clearer view of the relation between inequality and debt over the last few years in the US. He shows that debt payments relative to income rose faster for the third and fourth income quintiles between 2000 and 2004 than for the rest of population. A reality that can easily be seen to have expanded into the fifth quintile, the emergence of subprime borrowing is considered for the subsequent years. "The fact that payments relative to income rose and in some cases reached their highest level ever, despite the lowest interest rates in decades, shows that factors, other than the costs of credit, were at work in determining how much families borrowed" (2007: 23). Adding to this account of stagnant income and rising inequality the fact that prices for essential goods (food, health and education costs, housing) have risen above the rate of inflation, explanatory factors other than cheaper access to credit to explain households' increasing engagement with finance are provided. Since most of the debt was used to buy necessity goods, it is clear that middle-and low-income groups had be enforced into debt in order to preserve their consumption levels. This trend was clearly regressive, disproportionately affecting poorest households, and has proved unsustainable. The personal bankruptcy rate in the US more than quadrupled between 1980 and 2004 (Boushey and Weller, 2008) and has reached record levels with the financial crisis, triggered by subprime credit defaults.

Growing inequality is not only at the root of rising household debt and the resulting international financial crisis, but it is itself also an outcome of this new asymmetric engagement between households and the financial sector. The different positions of households, depending on their social class, and distributional outcomes of their debt commitments must thus be looked at carefully, given the discriminatory access to credit, and in some cases usurious practices. Research on household debt should not be limited to the content of the relation per se, but also discuss under what conditions this relation between households and banks may arise, as well as its consequences.

The comparison of the reality in developed economies with the situation in South Africa, which presents some significant differences, may be helpful in order to shed further light on the relation between households and banks. On the supply side, as shown in previous chapters, the securitisation of household debt was still in its initial stages during the 2000s in South Africa, and had had a marginal impact on the overall trend of rising household indebtedness. One should thus be careful in straightforwardly identifying these new "credit techniques" with the rising financial engagement of households. On the other hand, given the extreme inequality of this country, the impacts of the rising involvement of households with finance need to be better grasped in light of both the asymmetric power relations that it unleashes and its regressive impacts on the most vulnerable layers of the population.

8.3. From inequality to unequal debt in South Africa

8.3.1. A weak and precarious labour market

Despite a strong reliance on wages as the main source of income – 62.4%[96] of the population rely on wages (SSA General Household survey, 2010), South African households have endured extremely high unemployment rates. Around a quarter of the work force was unemployed throughout the 2000s (Table 8.1). Were discouraged workers to be included, that number would jump to around a third of the workforce (Marais, 2011).

The growth spurt of 2005-2008 caused a small decline in the unemployment rate. This decline was concentrated in the male population (23% to 19.3%) during the period 2001-2007, whereas women's unemployment rose over the same period (26.4% to 28.4%), a trend that was particularly marked among black women. Furthermore, this slight downward trend seems minor when set against the background of the 4-5% growth rates of this period, thus highlighting the limited scope of job-creation over this time.

The economic crisis of 2008-2009,however, led to a rapid rise in unemployment—with the unemployment rate going up by 2.5% in a year, and 870,000 jobs lost during 2009 (Statistics South Africa, 2009). The impacts of this crisis were unevenly distributed, with the depressive effects to be concentrated on the informal economy and domestic work whereas formal sector workers had their incomes cut, thus reducing the demand for goods and services provided by the informal sector (Makgetla, 2010). The recession and rise in unemployment came to a halt in late 2009, thanks to the recovery of exports (4.5 percent growth rate in 2010, driven by the recovery in commodity prices) and to the counter-cyclical fiscal behavior of public spending that preceded the international crisis[97] and the investment engaged by the large South African parastatals.

Marais (2011) attributes these persistently high levels of unemployment to the mix of previous low economic growth rates, restructuring of the economy, and reliance on the capital-intensive mining and energy sectors, which failed to absorb the country's growing active population. Further to the bleak employment picture in South Africa, the precarious

[96]Recent programs for the expansion of social grants to the most deprived households make 44.9% of the population to benefit for these transfers.
[97] In the preparation for the 2010 Football World Cup, the state committed more than 400 billion rand (10 percent of GDP) to investment in infra-structure upgrade between 2006 and 2010 (Cornelissen, 2010).

conditions of many South African workers are also worthy of note. Despite a decline in recent years, around a quarter of the workforce still works in the informal sector.[98]

The increasing levels of household debt in South Africa and its weight relative to disposable income, mainly in the form of mortgage debt, are thus surprising as the country's labour force continued to endure high levels of unemployment and informality that should seemingly have impeded any further engagement with credit markets. As Lapavitsas put it, "the party that advances credit must have trust in the counter-party making the requisite transfer of value in due time" (2003: 68). It is therefore apparently contradictory that a population whose main source of future income is dependent on precarious informal conditions should have been the recipient of high aggregate levels of banking debt.

Table 8.1. Official unemployment rate (%).

2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
23.3	26.2	26.6	24.8	23	23.5	22.1	21	21.9	24.3	23.9

Source: revised Labour Force Survey (LFS) 2000-2007 and Quarterly Labour Force Survey 2008-10

Table 8.2. Informal labour relations (%).

2000	2001	2002	2003	2004	2005	2006	2007	2008*	2009*	2010*
34.9	30.6	29.7	28.7	29.1	30.1	30.4	27	25.6	25	25.4

Source: revised LFS 2000-2007 and QLFS 2008-10, calculations by the author

8.3.2. Inequality

The answer to the apparent contradiction between rising levels of household debt and the persistence of unemployment is to be found in the South Africa's enduring high levels of inequality. Post-apartheid South Africa inherited a deeply unequal society, divided along racial and economic lines. According to the Income and Expenditure Survey of 2005/06[99], the Gini coefficient—0.72 of household disposable income— was one of the

[98]Statistics South Africa defines informal employment as having "the following two components: i) Employees working in establishments that employ less than five employees, who do not deduct income tax from their salaries/wages; and ii) Employers, own-account workers and persons helping unpaid in their household business who are not registered for either income tax or value-added tax." (SSA, QLFS2012).

[99]Data on income and expenditures by household in South Africa is limited here to the 2005-06 survey, as the data from the most recent survey (2010-11) is not yet available.

highest in the world with a dismal progression since 1995 when the coefficient was 0.62 (Bhorat and Jacobs, 2009). The richest decile of the income distribution (with a median income of 290,253 rand per year, which does not include capital gains)[100] holds 51% of all income, versus just 0.2% for the poorest decile (median income of 4,509 rand) (Figure 8.1). This inequality also splits the population along strong racial lines. Only 8.9% of the whole black African population—76.2% of all households—was part of the highest quintile (Table 8.3), versus 78.8% of white population — 12.8% of all households (Statistics South Africa, 2008).

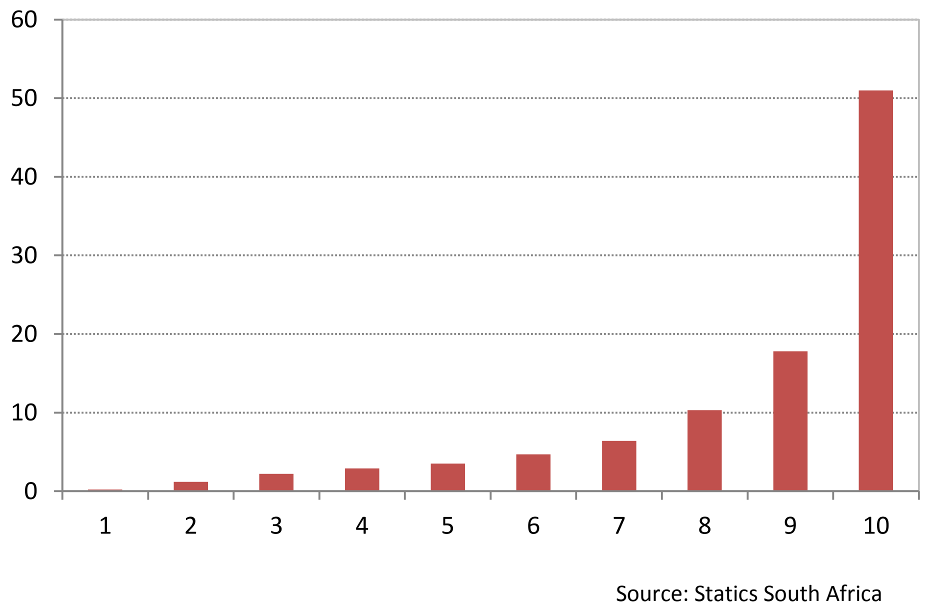


Figure 8.1. Share of income by population decile (%)

The racial divide has been increasing since the end of apartheid. According to Bhorat and Jacobs (2009), black South Africans experienced a decrease in real *per capita* income of 1.78% between 1995 and 2005, which compares to a 35% rise for "coloured" people and 40.5% for whites. The authors point to wages as the main driver of inequality growth in South Africa:

"Wage inequality in the latter part of post-apartheid South Africa is therefore explained by increasing wages for skilled workers and particularly the gap between the wages of those at the top (90th percentile) and middle (50th percentile) of the distribution" (2009: 22).

[100]Household income includes only income from work (salaries, wages, self-employment and business income) and social security grants.

This rising wage inequality is apparently explained by structural transformations in the economy, with a rising service sector that depends on scarce (white) skilled labour, which consequently has higher wages. Dividends from the country's economic growth during the post-apartheid period have thus been unevenly shared, offering the most affluent households a stronger financial standing that may have allowed them to go increasingly into debt and thereby to participate in the housing price boom of the 2000s.

Table 8.3. Percentage of individuals included in each income quintile by racial group.

	Black African	Coloured	Indian/Asian	White
Upper quintile (90,467R +)	8.6	27.5	46	78.8
4th quintile (36,043R–90,466R)	19.5	29.3	28.2	15.4
3th quintile (20,203R–36,042R)	23	20.2	13.6	3.6
2nd quintile (11,378R- 20202R)	24.2	13.8	8.1	1
1st quintile (less than 11378R)	24.8	9.2	4.2	1.2

Source: Statistics South Africa

8.3.3. Uneven housing

South Africa's extreme inequality is reflected in the housing market, which - as it was shown in chapter 7 - is the main cause of household debt. According to recent statistics, the percentage of households living in formal dwellings that were fully owned was only 58.8% in 2010, a modest rise from 53.1%in 2002 (SSA Household survey, 2010). On the other hand, the percentage of shack dwellers increased from 12.2% to 18.8% over the same period. This reflects the pressures of urbanisation—a product of South Africa growing population, continuing migration from rural areas, and household fragmentation (Todes et al, 2010) in an uneven market where public provision is residual.

Housing conditions changed little with the end of apartheid. Social movements that struggled for better housing conditions for the whole population—notably the bond boycotts organised by the South African Civic Organisation on credit previously extended for black-owned houses in townships—were quite strong in the overall anti-apartheid movement but failed to sustain their mobilisation after the inception of democracy (Bond, 2006). The National Housing Forum (where the ANC, trade unions and non-governmental organisations were already represented) tried to respond to the housing crisis created by the rapid urbanisation through a market-oriented policy, using a revised version of the small one-off capital subsidies for low-income housing that had been put in place at the beginning of the 1990s following the De Loor report (Gusler, 2000). This approach changed little after the new ANC government's 1994 *Housing White Paper*[101]which claimed that "the State has insufficient resources to meet the needs of the homeless on its own and recognises that sustained, substantial investment in housing from sources outside the national fiscus will be required." A market-oriented approach was adopted, granting financial incentives to banks (loan guarantees offered through the Mortgage Indemnity Fund) and developers in order to promote private provision. The results were dismal. The million new state subsidised houses promised in 1994 for a five year period to compensate a backlog of 1.6 million houses was not delivered, and banks failed to extend credit to low-income households (Bond, 2006). The financial sector, which had suffered from the mortgage boycott movement, did not show any further appetite for the low-income housing market in the post-apartheid period.

The last decade saw state subsidies for low income housing increase—covering twice as many people in 2008 (11.2%) as in 2002 (5.6%) (Marais, 2011)—but the efforts engaged to extend formal finance to low-income housing through the provision of microloans by second-tier banks (such as Sambou and Unifer) were badly affected by the banking crisis of the beginning of the 2000s, which struck these banks. In 2008, the United Nations Human Settlement Program (UN-HABITAT, 2008) concluded that the majority of South Africans could not access banking mortgage debt, as banks still perceived the low- and middle-income layers of the population as too risky for long-term credit:

> "In South Africa, the upper end of the mortgage market has experienced exceptional growth and returns on investments. (…) New home buyers took out bigger loans, while existing home owners increased their mortgage loans to turn capital appreciation into cash for consumption purposes. But this did not translate in to a trickle down effect on the lower end of the market." (2008: 51)

South Africa thus has a two-tiered housing market, with expanding mortgage credit concentrated within the most affluent layers of the population. This concentration, which differs from the extension of mortgages throughout the population of the most developed countries, partially explains the extraordinary rise in prices observed in the housing market, which outpaced the price boom seen in other parts of the world. These are the households who can more easily accommodate such price hikes. On the other hand, the majority of

[101]http://www.info.gov.za/whitepapers/1994/housing.htmwhy

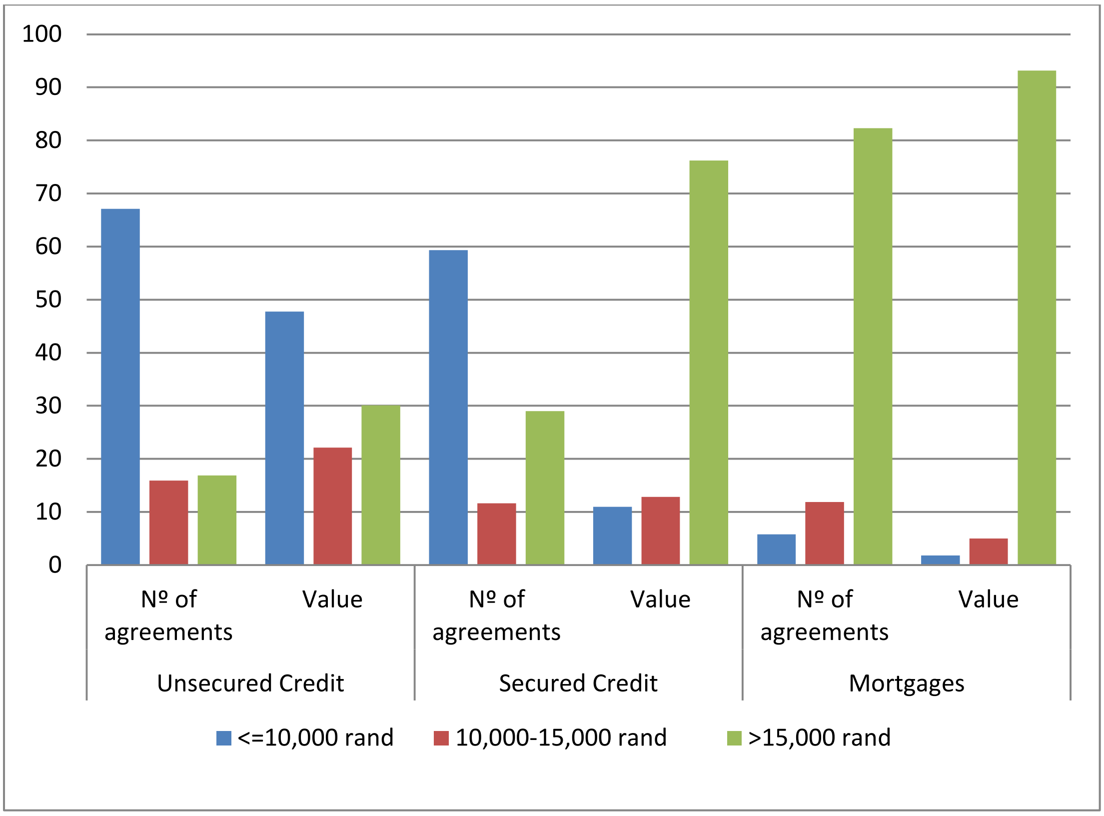
South African households still live in precarious housing conditions, dependent on small public subsidies to build low-quality housing, and without access to the booming mortgage credit market.

8.3.4. Unequal debt

From this set of facts about the socioeconomic structure of the South African population, a coherent explanation for the apparent contradictory household debt situation emerges. Given the almost-total absence of securitisation of household debt by South African banks, coupled with the country's extreme inequality and social deprivation, the overall picture of household debt is thus distinct from what is found in the most-developed countries. While the scale of this debt and its close relationship to the housing market are similar, its development seems to be limited to a small part of the population. In light of the precarious labour conditions and extremely high inequality, which has impacts on the position of households in relation to banks, it is unsurprising that the distribution of the banking credit has been highly unbalanced. In 2008, there were 32 million active consumer credit accounts in South Africa, with store cards accounting for 36% of the total and with credit cards as the second most common credit account (18.9%). However, mortgages accounted in 2008 for only 6% of all accounts, but 68.9%of all household debt, according to the Feasibility Survey (2011) commissioned by the National Credit Regulator.

This high level of inequality is reflected in the distribution of credit among different income categories. Figure 8.2 provides a snapshot of the unequal distribution of household credit contracts from the 3rd quarter of 2010 according to data from the National Credit Regulator of South Africa.[102] Mortgages are the overwhelmingly dominant category of debt for the top bracket (>15,000 rand), with a share of 82% in number of agreements (93% in value) while the number of agreements granted to the lower income bracket amounted to just 5.8% of all agreements (1.82% of value). Moreover, the estimated percentage of households living in mortgaged dwellings was only 14% for 2008 (Feasibility, 2011) thus confirming the skewed distribution of mortgage debt.

[102] The shares of both the number of agreements and the value of credit have remained stable since, when the NCR started to publish the Consumer Credit Reports after its creation with the National Credit Act in 2004.



Source: National Credit Regulator

Figure 8.2. Credit distribution by income category in 2010 (%).

This unequal portrait of household access to debt is further illustrated by the Finscope surveys. These surveys on financial access are conducted directly with South African households, thus providing data on informal credit arrangements, access to financial services, and the racial distribution of the surveyed population. Given the high degree of racial inequality, it is unsurprising that the level of debt varies considerably according to race. Only 11% of black respondents had contracted formal financial debts, compared with 50% of white respondents. Fifteen percent of black households incurred informal debt against 6% of white ones (Table 8.4). However, as access to banking increases, it is not surprising that the number of low-income individuals with debt is increasing, albeit at a lower rate. 28% of South Africans were borrowers (informally and formally) in 2008, compared to an estimated 12% in 2006 (Finscope, 2009).

Table 8.4. Sources of Credit (% of population).

	Black	White	Coloured	Indian/Asian	Total
Informal debt	15	6	10	4	13
Formal debt	11	50	17	37	16

Source: Finscope (2009)

It should be noted that high levels of informal debt, particularly within the black population, do not imply a lack of involvement in complex financial arrangements. The Financial Diaries surveys provide a detailed evolution of the cash flow of the poorest South African households during a year (Collins, 2008; Collins et al, 2009). This study presents the major motivations for poor households (many of whom are below the two-dollar-a-day poverty line): managing the basics (such as buying food and clothing); managing the high-risk economic environment (credit as a temporary solution for unexpected expenses such as health problems, funerals, unemployment, etc.); and lump sums raised to profit from specific business opportunities (such credit may be regarded as funding investment and not consumption). These motivations show that informal finance is not always an abusive, usurious, financial arrangement for poor people lacking access to banks. It may emerge as a complementary scheme that responds to the very short-term financial needs of precarious households from non-interest loans by family and friends to savings and credit associations. However local loan sharks (known as mashonisas) are also identified, which demand interest rates as high as 30% per month (Collins et al, 2009).

Finally, the unequal distribution of debt depicted above explains the lower levels of aggregate indebtedness and debt-service costs relative to disposable income seen in the previous chapter. The debt market that has seen the most impressive growth is concentrated, along with the largest amounts of debt, in a small part of the population. Contrary to the pattern in the most-developed countries, growth in household debt in South Africa did not result from the expansion of credit to new populations. It was supported by extraordinary rises in housing prices during the 2000s, which offered banks the confidence needed to extend credit (particularly mortgages) to the housing market, in the form of collateral.

8.4. From unequal debt to further inequality

8.4.1. Consumer credit regulation

Despite unequal distribution of debt in terms of value, the data presented above makes it clear the rising level of engagement of the South African households' with debt markets, particularly, unsecured consumer credit. The rise in household debt and its income-distributional impacts must be set in the context of the overall effort to expand financial services to the South African population. These efforts have been promoted by international organisations, such as the UN[103], because of the perception that formal access to finance represents a necessary condition to escape from poverty, by enabling access to capital as well as basic services such as health care and education. In South Africa the effort towards financial inclusion preceded the international enthusiasm about microfinance of the 2000s, and can be situated at the beginning of the 1990s, with financial access being one of the motives for the liberalisation and deregulation of the financial sector, on the view that this would enhance competition and thus lead to the provision of financial services to previously unbanked populations.

The initial steps of liberalisation started even before the end of apartheid, in 1992, with the exemption of micro-loans of less than 6,000 rand, later extended to 10,000 rand in 1999, from the Usury Act interest rate ceilings (Schoombee, 2009), understood as a hurdle to extension of credit to poorer (mostly black) households. This move gave a decisive boost to the emerging micro-loan industry, contributing to increasing levels of formalised debt among the poorest layers of the South African society. It was hoped that this new market coupled with the entry of foreign banks would promote further competition within the financial sector and broader access to credit (Kirsten, 2006). However, rising problems of over-indebtedness and the financial turmoil that the country endured at the beginning of the 2000s led to the failure of important micro-loans providers in 2002-03, notably the Sambou bank and UniFer. Moreover, access to financial services was evaluated as costly to depositors in terms of fees and penalties. According to the "leaked" Competition Commission's 2008 report[104] on South African banking practices:

"In the case of retail banking it appears that banks capture their costumers to price them. Such Capture is a consequence of the market power of the banks. (...) This market power allows the banks to segment the market through the application of differentiated price and product options. The

[103] It should be noted that during the 2000s, financial inclusion of low-income households was at the center of the development policies of international organisations. In the words of the former UN Secretary-General Kofi Annan: "Building inclusive financial sectors improves people's lives, in particular those of the poor. Asmall loan, a savings account or an insurance policy can make a great difference to a low-income family" (p. iii, UN, 2006).

[103] The confidential report was leaked onto the Internet. The whole report is available at: ftp://ftp.uwc.ac.za/FOSS/myadsl/Uncensored%20Competition%20Commision%20report%20on%20Banking.pdf

application of complicated fee structures, the addition of new fee categories, and general increases in the level of fees are all manifestations of this power."(2008: 119)

Given its conclusion that limited financial inclusion in South Africa resulted from a low level of competition and opacity towards clients, the commission's recommendations were aimed to promote competition, encouraging new entrants into the payment system (e.g. dedicated banks and cooperative banks) and encouraging transparency in the pricing of financial products, with recommendation for a 5 rand pricing capon penalties on dishonoured debit orders (Finmark, 2009).

The most significant public effort towards financial inclusion, given the lack of consumer protection, reckless lending practices, and rising problems of over-indebtedness, was a new law, the National Credit Act (NCA), created in 2004 in order to regulate consumer credit practices with the aim of both promoting access to credit and regulating credit providers—microlenders, banks and retailers (Kirsten, 2006).This new legal framework created the National Credit Regulator, which replaced the Micro-finance Regulatory Council, and a National Consumer Tribunal. Although its applications were varied, from financial education to debt counseling, the core provisions of the National Credit Act focused on three main axes of intervention in the consumer credit market: preventing reckless lending and over-indebtedness; promoting transparency; and defining cost caps.

The aim of the first two axis of the NCA was to promote competition and disclosure by credit providers on debt costs and repayment schedules, in order to align consumer credit protection with international standards (Goodwin-Groen, 2006), avoid reckless lending practices, and prevent household over-indebtedness. However, the definitions of reckless lending and over-indebtedness in the Act are very broad. The former is said to be caused by the failure to provide adequate information on the risks and costs of credit to the borrower and by non-assessment of the borrower's ability to repay his debt, and the latter is said to occur "if the preponderance of available information at the time a determination is made indicates that the consumer is or will be unable to satisfy in a timely manner all the obligations under all the credit agreements (…)" (Government Gazzete, 2006: 113), being thus identified with default on payments. In any of these cases, the credit agreement can only be suspended after a court ruling: the power to evaluate such situations thus rests with the court. The third axis, embodied in the introduction of interest rates and fee caps, had the greatest potential to discipline lender practices in this market. However, the ceilings on total credit costs (of both interest rates and fees) were so high—between 55.2%

and 481% annually, depending on the maturity and amount of credit—that, as the work of Goodwin-Groen on the impacts of NCA stated: “these rates are so high that under normal economic conditions they are likely to be academic” (2006: 24). It can be concluded that, despite efforts to prevent extreme forms of predatory lending, consumer credit regulation in South Africa rests on a market-friendly approach, fostering disclosure and competition that are supposed to allow an efficient allocation of household credit without attempting to effectively cap credit providers’ income from lending to households.

8.4.2. Financial services expansion

Such a market-oriented approach, focused on collaborating with the banking sector, was indeed the one that directed the more activist public stance during the 2000sto foster financial inclusion. This approach, based on the principles of broad-based BEE, resulted in the Financial Sector Charter of 2004, which aimed to promote the participation of the black population in the financial sector (in terms of ownership and employment)and the broadening of access to low-cost financing. One of the landmarks of this commitment was the establishment of the low-cost Mzansi current accounts (accounts with free debit cards, no monthly administration fees, ceiling balances, etc.) by the four major South African banks and the publicly owned Postbank (which dominated this new market). By December 2008 over 6 million Mzansi accounts had been opened (90% by previously unbanked people), although only 3.5 million had active movements, constituting 18% of the banked population (Finscope, 2009a).

The results in terms of expanding access to finance have been successful, as shown by the IMF Financial Access survey. The number of branches of banks and other deposit corporations (ODC) and Automatic Teller Machines (ATMs) increased consistently over the years 2004-2009, reflecting an overall expansion of the financial sector during this period (Table 8.5). The combination of a growing supply of financial services with the public promotion of low-cost current accounts is reflected in the increase in the number of banked individuals (depositors) from 386 per 1000 adults in 2004 to 839 in 2009. According to the same data source the number of borrowers also rose during the same period, albeit at a smaller rate: from 343 to 421 per 1000 adults for the same period, which suggests financial institutions’ continuing hesitancy to extend credit, particularly in the form of mortgage debt, to new layers of the South African population (Table 8.5).

Table 8.5. IMF Financial Access indicators

	2004	2005	2006	2007	2008	2009
Number of commercial bank branches per 1000 km2	1.25	1.9	2.00	1.7	2.2	2.3
Number of ODC branches per 1000 km2	4.08	4.6	4.87	4.4	4.9	4.7
Number of commercial bank branches per 100,000 adults			4.83	7.2	7.5	6.1
Number of ODC branches per 100,000 adults	15.7	17.4	18.19	16.2	17.6	16.8
Number of ATMs per 1000 km2	7.8	6.7	7.23	8.5	12.4	14.6
Number of ATMs per 100,000 adults	30.1	25.4	27.0	31.1	44.7	52.4
Depositors with commercial banks per 1000 adults	386.1	525.2	671.6	743.7	782.9	839.1
Depositors with ODCs per 1000 adults	400.4	551.7	700.1	772.5	814.5	878.4
Borrowers from commercial banks per 1000 adults	343.1	398.2	491	552	429.1	421.6

Source*: IMF*

Nonetheless, according to the Finscope survey (2009) only 38% of South Africans claimed to be saving. Formal bank financial products (taken by 8.5% of the whole population) and financial products in other financial institutions (16.8%) have to compete with plain home savings (12.7%) and informal products (9.7%). Informal products are prevalent amongst the poorest populations and take different forms, from informal savings clubs (known as Stokvels) to "Rotating saving and credit associations" where members "save the same amount as each other every period—a month, say—and the total amount saved each period is given in whole to one of the members." (Collins et al, 2008: 116). Again, the racial divide reflects itself in the access to different savings products, with 51% of the white population using some sort of formal savings product, versus only 15% of the black population (Finscope, 2009).

8.4.3. Debt deepens inequality

The newly created National Credit Regulator commissioned two major Feasibility surveys on the composition and prices of household debt, which surveyed the 45 top providers of consumer credit in 2008 and the top 40 in 2011. These surveys provide extensive data on the distribution and pricing of household debt: using this data it is possible to assess its evolution during the years of the 2008-2009 economic crisis. The income distribution is characterised according to the divisions of the population in the Living Standards Measure (LSM) of the South African Audience Research Foundation.[105] This is an analytical tool, primarily used for marketing purposes, which divides the South African

[105] http://www.saarf.co.za/LSM/lsms.asp

population into ten groups according to a number of criteria based on living conditions (from access to running water to owning a car or cellular phone);an average income is established for each group. The Feasibility survey consolidated the population into four different groups according to income:

i) LSMs 1 to 3 with incomes ranging from 0 to 2,441 rand per month;

ii) LSMs 4 to 6 with income ranging from 2,442 to 8,232 rand per month;

iii) LSMs 7 to 9 with incomes ranging from 8,233 to 22,779 rand per month; and

iv) LSM 10 with income above 22,779 rand per month.

The survey established a distribution of the credit to households by type of credit, calculating the share of each of the income groups and the Weighted Average Annual Percentage Rate (WAAPR). This average provides the annual cost of different household debt categories, including not only the interest rate charged but also the fees involved, thus providing an accurate measurement of borrowing costs.[106]

As discussed above, the distribution of credit along the income scale reflects the high inequality and racial divisions of South Africa, with very low-income households being unable to access the formal consumer credit market. As reported by Hawkins (2009):

> "Estimates of access to credit suggest that low income individuals earning less than R1 825 per month (an estimated 8.6 million people) have limited access to credit (around 1.4% of the total credit disbursed). Their credit is limited to unsecured home loans, furniture loans, store cards and short-term loans, and collectively represents close to one per cent of the total credit extended to households. These forms of credit tend to be unsecured and are substantially more expensive than other forms of credit available to higher income groups." (2009: 6)

As can be seen from the new data in the Feasibility (2011) survey, this analysis has not changed. Household credit remains highly concentrated in the top LSM bracket (Table 8.6).The lower-income LSMs (1 to 3), comprising 17% of the population, continue to have marginal access to the formal credit market (2% of all Personal Loans; 6% for Store cards

[106]Monthly Annual Percentage rate (APR) is the result of the number of periods, Payment per period, and Present value of loan. Feasibility provides the following illustrative example: "a person takes a short-term loan of R10,000, over 12 months. The consumer is required to pay back R1,000 per month to cover the interest and the capital sum. Compounded monthly, the interest rate will be 35.1% p.a. But if the provider charges an initiation fee of R1,140 (R1,000 plus VAT) which is capitalised, and a monthly service fee of R57 (R50 plus VAT), over and above the interest rate, the consumer will have to pay R1,171 per month, and the effective cost of the loan will be 45.2% p.a." (Feasibility, 2011: 49)

credit). The middle-income layers LSM 4-6, comprising 50% of the population, receive only 17% of all mortgage credit, but a larger share of unsecured forms of credit such as credit cards and personal loans. The bulk of household debt is thus concentrated in the top layers of the population. LSM 7-9, comprising 27% of the population, have 49% of all mortgage debt and 71% of asset debt, mainly composed of motor vehicle credit. And the small layer of the population that falls in the top LSM group, comprising only 6% of the population, concentrates 35% of all mortgage debt, 82% of overdrafts, 54% of credit cards and 61% of credit cards.

Table 8.6. Estimated allocation of credit by credit type in each LSM group, 2010.

	LSM 1-3	LSM 4-6	LSM 7-9	LSM 10
Mortgages (%)	0.0	47.1	61.5	77.1
Asset finance (%)	0.0	3.1	27.4	7.6
Pension/Equity-Backed (%)	0.0	3.7	0.3	0.2
Furniture (%)	45.2	2.5	0.7	0.9
Overdrafts (%)	0.0	1.7	0.8	5.7
Credit Cards (%)	0.0	5.8	5.0	4.9
Store Cards (%)	38.1	8.0	0.8	1.5
Unsecured Personal Loans (%)	17.9	28.1	3.6	2.2
Total (Bn rand)	8.4	149.3	592.7	321.4
% Share of Total Credit	0.8	13	55	3

Source: Computed from Feasibility (2011).

More importantly, these surveys illustrate how the unequal distribution of credit is replicated in debt costs, showing how household debt results in a regressive distributional outcome. This regressive impact comes about in two different ways: the different cost of the same category of debt for different LSM groups, and the different relative weight of the individual debt categories for each LSM. In the categories of debt to which almost the whole population has access to, the Weighted Average Annual Percentage Rate for 2010 was significantly higher for the lowest LSMs—61% for LSMs 1-3 against 31% in LSM 10 for furniture loans; 34% against 12%for store cards; 35% against 19% for personal Loans (Table 8.7). The second form in which the unequal distribution of debt is found is in the predominance of the cheapest kinds of debt, namely mortgages and asset-backed debt, in LSM groups 7-9 and 10 (61.5 and 77.1% respectively) with the most expensive kinds of household debt, such as unsecured loans (furniture, store cards, personal loans), making up the highest proportion of debts in the lower LSM groups (Table 8.7). The cost of household debt is thus higher for poorer households not only for identical categories of debt, but also in the relative proportion of their debt commitments that fall into the most expensive categories. The result is a deepening of inequality among different LSM groups. Furthermore, the forms of debt incurred by the poorest groups are typically incurred to sustain minimum living standards, and are most frequently resorted to in case of emergencies (Hurwitz and Luiz, 2007).

Table 8.7. LSM group shares and APR for selected kinds of debt.

		LSM 1-3	LSM 4-6	LSM 7-9	LSM 10
Mortgages (R683 billion)	LSM group's share of total in 2008	0%	17%	49%	35%
	LSM group's share of total in 2010	0%	10%	53%	36%
	Weighted average APR in 2008		16%	16%	15%
	Weighted average APR in 2010		10%	9%	9%
Asset Finance (R191 billion)	LSM group's share of total in 2008	0%	8%	72%	20%
	LSM group's share of total in 2010	0%	2%	85%	13%
	Weighted average APR in 2008		20%	19%	18%
	Weighted average APR in 2010		11%	11%	9%
Overdrafts (R25 billion)	LSM group's share of total in 2008	0%	5%	14%	82%
	LSM group's share of total in 2010	0%	10%	18%	72%
	Weighted average APR in 2008		27%	22%	18%
	Weighted average APR in 2010		22%	20%	19%
Credit Cards (R54billion)	LSM group's share of total in 2008	0%	23%	23%	54%
	LSM group's share of total in 2010	0%	16%	55%	29%
	Weighted average APR in 2008		48%	33%	29%
	Weighted average APR in 2010		29%	25%	19%
Furniture Loans (R14 billion)	LSM group's share of total in 2008	39%	5%	23%	33%
	LSM group's share of total in 2010	27%	27%	26%	20%
	Weighted average APR in 2008	70%	70%	63%	54%
	Weighted average APR in 2010	61%	61%	43%	31%
Store Cards (R26billion)	LSM group's share of total in 2008	6%	14%	19%	61%
	LSM group's share of total in 2010	13%	49%	19%	19%
	Weighted average APR in 2008	48%	33%	31%	28%
	Weighted average APR in 2010	34%	16%	10%	12%
Personal Loans (R72 billion)	LSM group's share of total in 2008	0%	35%	25%	40%
	LSM group's share of total in 2010	2%	58%	30%	10%
	Weighted average APR in 2008	81%	48%	42%	32%
	Weighted average APR in 2010	35%	32%	26%	19%
All Credit Types	LSM group's share of total in 2008	0.90%	15.40%	48.80%	34.90%
	LSM group's share of total in 2010	0.80%	13.90%	55.30%	30%

Source: Feasibility Surveys (2008, 2010) in Feasibility Report 2011.

The extraordinarily high borrowing costs have resulted in endemic problems of over-indebtedness, mainly affecting a middle-income population of individuals who live in urban areas, hold formal jobs and has access to formal debt (Collins, 2008).[107] A relevant survey by Hurwitz and Luiz (2007) focused on urban middle-income working class consumers earning between 2,000 rand and 5,000 rand with access to formal finance, both from micro-lenders and banks. They found that 60% of their sample had debt servicing costs exceeding 30% of their gross monthly income, if retail debt was included. The prevalence of the type of high-cost unsecured credit for which most of this population qualify was evident, leading to concerns about the particularly vulnerability of this population to over-indebtedness. The burden of debt and problems of over-indebtedness seemed to have been unaffected by the public regulation of consumer credit put forward during the 2000s. The alleviation of the debt burden in 2008-2009 was here mostly the result of a drop in domestic interest rates resulting from the international financial crisis.

Finally, despite the deepening of socio-economic differences within the South African population produced by unequal costs for debt, the high cost of debt seen in all debt categories (reaching usurious levels at some of them) should be highlighted here, as it reflects high interest rates and rising fees and penalties within the context of rapidly expanding consumer credit. The rising indebtedness of South African households was thus achieved at a much higher cost than similar expansions of consumer credit in developed countries, confirming the internationally unequal position of South Africa pointed to in the previous chapter.

8.5. Conclusion

This chapter examined the particular case of rising household indebtedness in South Africa, relating this issue to the extreme inequality and precarious social conditions that affect most of the country's population.

South African household debt replicates the extreme inequality of South African society, reflected in what can be approximated as a three-tier market. The most affluent layers, where banking credit is concentrated, benefit from access to asset-backed and mortgage debt, determining the overall aggregate behavior described in the previous chapter for households. Middle-income layers of the population where, despite low earnings, formal

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[107] It should be noted, however, that it is among rural households (collectively, South Africa's most deprived population) that debt, being mainly informal, seems to be most persistent, according to the *Financial diaries* survey (Collins, 2008).

jobs are more common, still lack full access to secured credit. Unsecured credit, in the form of furniture loans, credit cards or store cards, which households engage to sustain their minimum dignity, have staggering high costs. At the lower end of the income scale (particularly for rural households), access to formal finance is still scarce and households are forced to resort to informal arrangements that may trap them in spirals of debt (Mashigo, 2006).

Two major findings emerge here on the relations between inequality and debt, which can deepen our understanding of financial expropriation in a middle-income country such as South Africa. The first relates to how inequality is reflected in access to different kinds of debt in this particular setting. In the absence of new banking practices such as securitisation, which would enable banks to extend mortgage credit to new layers of the population, this form of credit remains concentrated among the most affluent (predominantly white) households.

However, as noted in the previous chapter, this did not stop banks from increasing the volume of mortgage credits accorded to households to new record highs. This seems mainly to have been the product of an unequal housing market, to which only the most affluent—and credit-worthy—have access, and the parallel evolution of housing prices in South Africa. From this particular case, it seems that the relation between financial expropriation (mainly in the form of household debt) and the housing market is of crucial importance in this new relation. Houses, being a durable good, are secure collateral in case of default. Banks, having gained a new role as exclusive intermediaries in access to housing and facing an atomistic and opaque market where individuals have little negotiating power, have profited from an increasingly asymmetrical relation with households. However, given the importance of booming housing prices in this new reality, it may be argued that the trust necessary for these credit relations arose not only due to new information sources that allowed the screening of households' financial situation or, in the case of South Africa, from the more favourable social standing of the targeted households, but mainly from the myopic perception that rising house prices would indefinitely ensure the future stream of revenue needed to cover household "promises to pay". In the terms of the French convention school, this is a new "convention" (Orlean, 1999) that drove the financial sector to extend credit to households. The expansion of mortgage credit and the consequently increasing housing prices, along with their effects on the general rate of economic growth served, on this view, as a self-referential, mimetised heuristic for banks across the world.

The second major finding of this chapter is on the failure of attempts to promote financial inclusion in distributional terms. Despite the overall progress in access to credit, the most vulnerable layers of the population, lacking access to the most relevant collateral (housing) to benefit from lower debt costs in their relationship with the banking sector, enter into usurious formal debt relations in order to access consumer goods. Consumer credit regulation appears to have had at best a marginal impact, limited to the most extreme forms of predatory lending, given its market-friendly approach. The result in South Africa was thus a regressive redistribution of income through debt, with the proportion of income extracted from poorer households being higher than among the most affluent. Given the clearly discriminatory practices present in South Africa, the concept of financial expropriation acquires a correspondingly clearer meaning: here as elsewhere, it is the result of an asymmetric power relationship between the financial sector and households as a whole, but in the South African case its predatory and expropriatory elements are exacerbated by extreme inequality. The South African case shows clearly that, more than competition, only social progress in the population (particularly the provision of basic goods such as housing) coupled with more "activist" intervention by the State in the financial sector can result in a balanced relationship between banks and households.

9. Conclusion

9.1. The Significance of financialisation

Finance has gained a rising importance in the contemporary capitalist economies during the last three decades. The associated multiplication of financial crisis, rising economic volatility, and bleak economic growth and persistent high unemployment in developed countries, in contrast with the previous post-wear period, have been the object of prolific research from political economy. From the end of the nineties, the new financial hegemony has been captured in the concept of financialisation. Pointed as a systemic transformation of capitalism, grounded in the historical and social realities of the most developed countries, financialisation has proved to be a popular concept within political economy. Nonetheless, or perhaps due to its popularity, the concept has been treated either in vague terms or with different understandings according to various currents of political economic thought.

In this thesis, these diverse currents of thought were reviewed in their understanding of financialisation or equivalent concepts (such as finance-led accumulation regime). Pointing to the limits of many of these approaches – from the stress put by post-Keynesians in the public policy turn of neoliberalism as the sole root of this process to the negligence of Marxist political economy of the mechanisms at place within the financial sphere -, an emerging new literature on financialisation grounded on the Marxist political economy was here highlighted, building on the work of Lapavitsas and Dos Santos, among others. In light of the current international financial crisis started in 2007, triggered by a wave of subprime defaults among the most deprived American population, this literature provided new insights, looking in detail at how credit relations have been reorganized during the last decades between different sectors of the economy and how that enhances the hegemony of finance. Particular attention is devoted to the relationship between households and the financial sector and the extraction of income derived from the former.

Such theoretical framework offers a more systemic analysis of the financialisation phenomenon, covering how different sectors of the economy have interacted, resulting in a change in their financial conduct and financial position in the economy. This new theoretical approach starts to point to the increased ability of large corporations to directly access financial markets, by-passing the intermediation of banks, becoming thus new financial agents. Having lost this credit market, banks engaged in investment banking activities from which rising fees can be earned and, most importantly, targeted workers as their new lending market, extracting rising income from them. Workers, and more generally households, are understood as being in a vulnerable position in this relationship since the retreat of public provision during the last decades forced them to resort to credit in order to maintain their consumption. This process of income extraction is encapsulated in the concept of financial expropriation. Capital expropriates workers, not in the classical sphere of exploitative production, but in the sphere of circulation through finance. Hence, the rise of the financial sphere is the result of this pattern of interactions that promotes a redistribution of income that benefits finance. Such theoretical approach, although recognizing variations in different countries of these financial interactions, has been nonetheless circumscribed to the most developed countries - a gap shared by the general literature on financialisation.

In this thesis this new theoretical framework was adopted against the South African economic evolution since the end of apartheid in order to test its general validity. This thesis, anchored in a Marxist political economy approach, but enriched by contributions from different schools of economic thought and other social sciences, such as economic geography, provided an account of the content of financialisation in this middle-income country, filling the aforementioned gap. This particular methodological stance implied the confrontation with the dominant neoclassical theoretical paradigm, whose shortcomings in analyzing social and historical processes for the different sectors here scrutinised were shown across this thesis.

Through the analysis of financial flows and financial positions of different sectors of the South African economy – non-financial corporations, banks and households -, different financialisation hypotheses were tested in order to assess the adherence of the aforementioned theoretical framework to each of the chosen South African economic sectors. This empirical work was contextualized with the economic and political evolution of South Africa during the post-apartheid era – a period characterised by the international opening of the economy and the domestic neoliberal Washington consensus-like processes of liberalisation and deregulation of the economy - thus providing the specificities of this country that explain its variations against the adopted theory. The evolution of the international economic insertion of South Africa shown here are of paramount importance to frame the domestic financial evolution of the analysed sectors.

This thesis answered positively to the question of whether South Africa has a financialised economy, pointing to the theoretical need for variation in specific geographical settings. A more robust political economy approach on the transformations of contemporary capitalism in the last decades was thus provided, overcoming the elusive considerations of financialisation in middle-income countries, such as South Africa, present in the literature.

9.2. The content of financialisation in South Africa

9.2.1. Non-financial corporations

Through the analysis of funding sources and uses of non-financial corporations, the financialisation hypothesis of increasing access to debt and equity markets was empirically confirmed. However, it was found that non-financial South African corporations, despite being financialised in the sense of an increasing access to equity and debt markets, did not show a declining reliance on the domestic banking sector, both as a source of funding and a recipient for deposits. The close relation between non-financial corporations and banks shown in this thesis is the contrary of what was to be expected by the Lapavitsas hypothesis. Such result was further highlighted by the analysis of the banks' balance sheets, where non-financial corporations remained strongly linked with the banking sector both as depositors and borrowers. The "crowding-out" effect of banking credit by the rising financial markets did not hold. Depending of the international and domestic conditions, South African banks were still considered an important funding source and recipient of deposits, particularly in the years of rising net capital inflows and overall economic growth. Research on financialisation in the non-financial corporations sector should thus be attentive to the specificities of countries where debt and equity markets do not have the same importance as in countries like the US or the UK, which benefit from their financial international centers.

Nonetheless, this thesis showed how the rising interaction between the newly liberalised financial sphere and non-financial corporations promoted a profound restructuring of the organization and operations of the South African economy. With the opening of the economy to the international financial sphere, the largest conglomerates unbundled their operations, expanded internationally and integrated the small black elite born from the end of apartheid. They transformed themselves into transnational corporations with direct access to the core international markets, thus favouring the most outward oriented fractions of capital. Research on financialisation in middle income countries should thus be conscious, not only of the semi-peripheral position of these countries in the international financial sphere pointed above, but also of the asymmetric effects of financialisation in the diverse standing of domestic corporations. Depending on their size and transnationalisation, major corporations may overcome their initial disadvantaged geographical origin.

9.2.2. Banking Sector

Through the analysis of banks flow of funds, aggregate balance sheets and income statements, it was found that banks have exponentially expanded their balance sheets, having now households as their primary target for lending operations (particularly in the mortgage market). The rising income extracted from households in its various forms - interest and fee income – showed the profitability of this market for banks, which explain the targeting of that sector. Furthermore, the financialisation hypothesis of rising finance-to-finance funding -although lacking the same sophistication that the arousal of debt securitisation enabled in the most developed countries - was also confirmed, particularly in the form of short term money market instruments, which supported the overall expansion of banks' balance sheets. The arousal of these markets pointed to the increasing relevance of non-monetary financial institutions, such as mutual funds, in the overall growth of the financial sphere. Moreover, this reality pointed again to the semi-peripheral position of the South African economy, vulnerable to volatile capital flows and forced to sustain high interest rates, which explain the importance of these highly liquid instruments in this country.

Another significant result brought by this thesis was the scarce evidence found for the rising importance of investment banking income in South Africa, through the banks' income statement analysis. The oligopolistic South African banking sector was bypassed in favour of international investment banks and consulting firms in the mergers and acquisitions frenzy that characterised the domestic unbundling and restruturing of the industrial conglomerates, thus focusing its operations in the retail market. The significant share of investment banking income identified for the biggest banks in the world should be thus taken with parsimony when researching financialisation outside the capitalist center, as national and regional banks that do not have the same global outreach cannot compete with the major international investment banks. Nonetheless, the semi-peripheral position of South African banks has enabled their international expansion, with the sub-Saharan

African continent to play an increasingly important role in their operations. The domestic buoyancy and international expansion of South African banks has, in turn, proved attractive for foreign banks to acquire stakes in some of the oligopolistic South African banks, namely ABSA and Standard Bank, after their ineffective entry with their own branches during the 1990s.

9.2.3. Households

The rising engagement of households with the financial sector, particularly in the form of debt, was shown through the flow of funds and balance sheet analysis of this sector. It was found that this new scale of engagement resulted in an increasing share of household disposable income dedicated to debt payment, to which it should be added the high-cost fees charged for financial transactions and households' financial assets. The whole profitability of the banking sector, and more generally of the whole financial sector, is increasingly related to this kind of income. The financial expropriation hypothesis in this setting was thus confirmed. Moreover, it was shown that South African households endure higher interest rates and transaction fees than their developed country counter-parts, reflecting their vulnerability vis-à-vis the oligopolistic retail banking sector whose concentration has been reinforced during the past two decades.

The pattern of debt distribution in South Africa is, nonetheless, peculiar. Household debt and, particularly, mortgage debt was found to be concentrated in top income layers of the population and not across all the population, as it was the case, for example, in the US in the subprime market. Despite the increasing levels of defaults in the awake of the international financial crisis, such banking behavior seen in South Africa, coupled with the still incipient securitization of debt, explains the recent apparent robustness of South African banks when compared to developed country counter-parts[108]. This thesis found thus that, contrary to the perspectives that place the arousal of new credit techniques as securitization and credit-scoring at heart of the expansion of household debt, more

[108]Nonetheless, the recovery of the South African economy should not be mistaken as a specific resilience or even autonomy in relation to the international economy. On the contrary, this small recovery seems directly related to the resume of the same international trends that benefitted South Africa in the second half of the 2000s, namely the recovery of commodities prices, thus fostering the export growth seen in 2010 and the role of capital inflows.

attention should be dedicated to the role of mortgage debt – and the associated evolution of housing prices - as the kind of debt that structures the relation between households and the banking sector, particularly in South Africa.

Even though household debt was found mainly concentrated in top layers of the population, another finding of this thesis rested on the public efforts in expanding financial services to new (middle-income) layers of the population, trying to shrink the role of informal finance, through a market friendly approach. After the failed liberalisation aimed to promote micro-lending in the nineties, standard formal finance expansion has been progressing during the last decade. However, its distribution is not balanced, with poorer layers of the population to only have access to the most costly kinds of consumer debt and with the costs for the same kind of debt varying widely for different income layers, in favour of the better off. In a country with one of the highest real interest rates in the world, debt costs for households reach usurious levels, resulting in emerging problems of over-indebtedness in the middle income layers of the population and an overall deepening of inequality.

9.3. Final remarks

The financialisation hypothesis, from which this research was conducted, was confirmed for the South African economy during the past years, proving the relevance of this theoretical framework in the study of financialisation. The results presented in this thesis contribute to a more robust approach to financialisation, pointing to the relevance of this concept in the analysis of contemporary capitalism, particularly in light of the current financial turmoil that afflicts the international economy. The diverse nature of the financialisation process was highlighted in South Africa, reflecting the international economic hierarchical position where this country is integrated. It is my understanding that further research on the content of financialisation should thus follow the path chosen in this thesis, taking into account its findings. Financialisation should be understood as being anchored in processes of international integration and domestic reorganization of production and redistribution of income, which favours the financial sector and the outward fractions of domestic capital, punishing, with asymmetric impacts, workers and, more generally, households. This depiction of financialisation is of the utmost importance for any developmental effort that aims for social progress. The detailed understanding of the different mechanisms that were here scrutinized is conditional for any successful simultaneous break with the international and the domestic interests that have been nourished by this new capitalist configuration.

10. References

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