Kingston University London

Economics Discussion Papers 2016-5

FINANCIAL AND CORPORATE STRUCTURE IN SOUTH AFRICA

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25 February 2016

Abstract

Concentration in the South African financial sector has its origins in three main influences that are all historical (i) the legacy of domination by a small number of large imperial banks, (ii) the struggle between English and Afrikaner capital and (iii) the statutory legislation that framed the operation of banks. In this paper we describe the part played by these three historical influences in the formation and development of the corporate sector in South Africa. One recurrent theme throughout the history is the relative position of the foreign bank and domestic bank in the local market place. We take up this theme and argue that the scale and extent of foreign bank operations in South Africa is far greater than estimates provided by the local authorities. We have found that the main vehicle in deepening the concentration of the sector has been the merger. In later sections of the paper we lay out how the amalgamation by absorption approach to expansion that has been a constant feature of the country's business life comes together with a merger frenzy in the late 1980's and 1990s that succeeds in further deepening concentration within banking, finance and industry. Last, we end with an analysis of industry structure by Johannesburg Stock Exchange (JSE) capitalisation between 1994 and 2011.

Keywords: Banks; Concentration; Corporate Structure

JEL codes: B15; L19; N27; P16

Acknowledgements: I gratefully acknowledge helpful comments by Paul Auerbach. All remaining mistakes are the author's.

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1. Introduction

The most obvious feature of South Africa’s corporate and financial life is its large size and concentration. The entire corporate structure of South Africa is characterised by this concentration and in what follows we explain this tendency as a product of South Africa’s historical development.

The pattern was established towards the end of the 19th century when in 1888 Cecil Rhodes’ DeBeers completed what Chabane et al (2006) call the “amalgamation” of the diamond industry in the region. In 1917, Anglo-American Corporation (AAC) was founded by Ernest Oppenheimer. Capital for its formation came from Britain, the US, and South Africa. The company aimed to exploit the gold mining potential of the East Rand. In 1924, Oppenheimer made AAC the largest single shareholder in De Beers and established a cross-holding linking the two companies in 1929. This type of cross listing that connects companies in an intricate web of shareholdings was the *sine qua non* of corporate South Africa up until the corporate unbundling and re-bundling of the 1990s. The huge banking conglomerates are part of a larger conglomerate structure that has emerged from the unique circumstances of South Africa’s past.

2. Measuring Concentration

According to Okeahalam (2001), the number of firms that supply products in a market and the proportion of the market that each firm supplies determines concentration. Concentration in turn is said to indicate the degree of competition to be found in an industry.

The Herfindahl–Hirschman Index (H-index) measures the market concentration in a banking system. An H-index from 0.1 up to 0.18 indicates no concentration to moderate concentration. An H-index above 0.18 speaks to heavier and higher levels of concentration. The H-Indices for the South African banking sector for the years 2006-2011 are presented in Table 1.

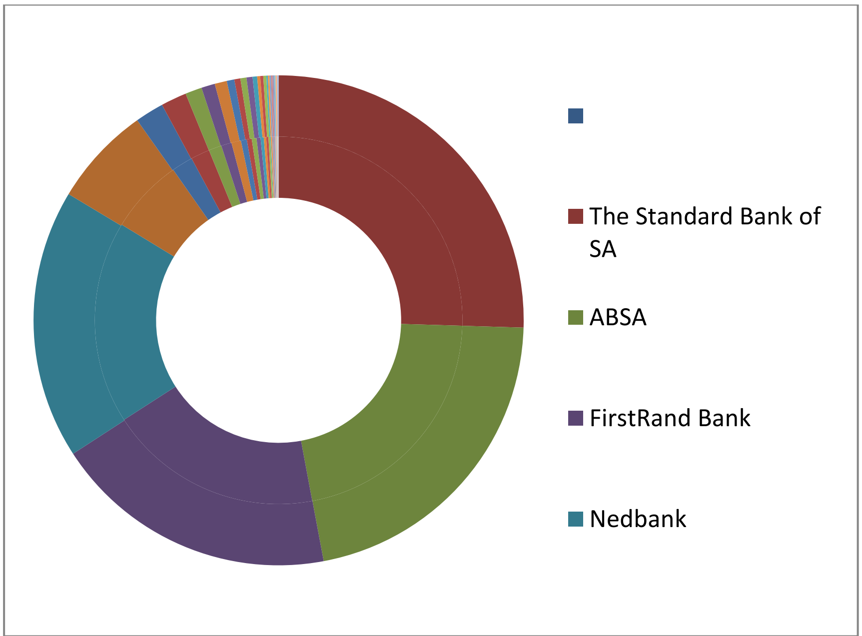
Table 1: South Africa Bank Sector H-Index, 2006-2011

2006	2007	2008	2009	2010	2011
0.184	0.190	0.189	0.189	0.188	0.187

Source: SARB Overview 2011

According to the Falkena Report of 2004; "*the concentration levels of the South African banking industry are high, but not out of line with other emerging markets.*" This we believe is half the story, in that it is not just the high levels of concentration in banking and finance. It is the concentration in finance alongside very high levels of concentration across the economy, in mining, energy and other sectors tied to the fact that South Africa is one of the more financialised countries in the world that makes South Africa a fairly unique case. The South Africa Reserve Bank (SARB) attributes the high level of concentration within its system to the high concentration of banking assets among South Africa's big four banks[1]. The big four – Standard Bank, ABSA, First Rand Bank and Nedbank account for just over 84 per cent of aggregate banking assets in the system[2].

Fig 1: Banks by Total Assets



Source: SARB, 2011, Overview

Concentration in the South African financial sector has its origins in three main influences that are all historical:

1. The historical legacy of domination by a small number of large imperial banks
2. The struggle between English and Afrikaner capital
3. Statutory legislation that framed the operation of banks

[1] See Bank Supervision Department Annual Report 2011, Pg 55

[2] If we include Investec as many writers are increasingly doing we in effect a "big five" that hold over 90% share of total assets in the bank sector.

In the rest of this paper we describe the part played by these three historical influences in the formation and development of the corporate sector in South Africa. One recurrent theme throughout the history is the relative position of the foreign bank and domestic bank in the local market place. We take up this theme and argue that the scale and extent of foreign bank operations in South Africa is far greater than estimates provided by the local authorities. We have found that the main vehicle in deepening the concentration of the sector has been the merger. In later sections of the paper we lay out how the amalgamation by absorption approach to expansion that has been a constant feature of the country's business life comes together with a merger frenzy in the late 1980's and 1990s that succeeds in further deepening concentration within banking, finance and industry. Last, we end with an analysis of industry structure by Johannesburg Stock Exchange (JSE) capitalisation between 1994 and 2011.

We find that a fair degree of continuity remains between the two periods. By JSE capitalisation the largest industrials (including mining), still account for six of the top 20 firms (including services). Continuity is also reflected in continued high levels of concentration within sectors. A large proportion of mergers have been vertical, increasing control of dominant firms through production chains. While this avoids the direct competition concerns of horizontal mergers, it realizes greater consolidation within industries.

3. Imperial Domination:

One of the main influences in determining the structure of South African finance is the imperial legacy; British banks were an integral part of British imperialism and as such they occupied dominant positions in the local economy since the 1860's. When Barclays Bank acquired National Bank in 1926, Verhoef (2009) contends that the final domination of the British banks was complete. And notwithstanding the formation of Volksas in 1934 and the expansion of the Netherlands Bank for South Africa, by 1970 South Africa's banking sector was still dominated by Standard Bank and by Barclays with Head Offices in the United Kingdom. Both banks were headquartered in the United Kingdom and both represented British interests. Starting in the Cape Colony, the banks followed the gold mining industry. By 1910 the two owned and controlled over 90% of the total capital of banks in South Africa (Verhoef 2009).

By the early 1930s AAC's 1929 cross listing of companies with DeBeers secured dominance within the mining industry. Starting with Rhodes' amalgamation mining too had evolved as a highly concentrated sector. Oppenheimer's AAC competed with five other mining companies. According to Chabane et al (2006), "the (limited) backward linkages created by the mining industry and the demand for consumer goods generated by white wage earners provided a stimulus for industrial development." According to the authors, it was at this point the mining houses saw the opportunity for diversification into related activities. The mining houses diversified into explosives and mining equipment, banking, industrial commodities (steel, paper, and chemicals), engineering, and consumer goods (including beer and furniture). By the end of this process the each mining house had its own financial arm and it is here that Innes (1984) argues that productive capital and financial capital were in effect married. O'Meara (1983), reports that this model was to define Afrikaner capital for some considerable time thereafter.

4. English and Afrikaner Capital

The 20th century began with Afrikaner nationalism in retreat. For the first two decades of the 20th century saw a huge increase in the number of poor whites, and in addition English capital enjoyed an unchallenged position in industry. There were many significant responses. One such was the creation of Santam (the South African Trust and Insurance Company). Santam was founded in 1918, and Sanlam the South African National Life Assurance Company) was formed in the same year as its life assurance subsidiary.

According to Verhoef (2009: 124-5), Sanlam's was established with three objectives;

1. to contribute to the growth of the South African economy;
2. to encourage and facilitate Afrikaner saving; and
3. to strengthen Afrikaner (participation in the South African economy.

Another significant response was the formation a people's savings bank by the Afrikaner Broederbond in 1934. The savings bank later became Volkskas Bank, (up until 1991, South Africa's largest Afrikaner bank) [3]. In due course these institutions became crucial vehicles of Afrikaner capitalism and nationalism.

The economy wide tendency to conglomeration was reinforced at the Economic People's Congress in Bloemfontein in 1939, when Sanlam advanced the formation of an investment company that would provide capital for Afrikaner business. *'If we want to be successful, we need to use the capitalist system in a similar fashion as displayed by the gold mining industry.'*(Verhoef 2009a: 128)

The FVB (Federale Volksbeleggings or Federal People's Investments) was established with Sanlam having a controlling shareholding and overlapping members of the board of directors. Through FVB, Sanlam was critical in channelling Afrikaner savings and agricultural surplus into the development of an 'Afrikaner' industrial base (O'Meara 1983 in Ashman and Fine, forthcoming).

The state established the Industrial Development Corporation (IDC) in 1940, and in 1949 the state established the National Finance Corporation (NFC). The NFC used its deposits to purchase the state's Treasury Bills and the debentures of the mining houses. Here were the early beginnings of the long term capital market and the one of the earliest beneficiaries was the Orange Free State Goldfields (Fine and Rustomjee, 1996). The scale and scope of the development could not be undertaken without the involvement of the NFC.

As the NFC matured it established a mechanism for moving funds from AAC'c diamond operations to the company's mining interests. As this practice takes root, the finance role, moves from private sources to institutional ones. In addition Ashman and Fine (ibid) point out this change ultimately helps to erode differences between English and Afrikaner capital.

Further support from the state for Afrikaner finance capital during the 1940s and 1950s, meant that Afrikaner capital was able to break the stranglehold that English capital had imposed on the economy. "*Minerals and energy then were the*

[3] In 1991, Volkskas merged with United Bank, Allied Bank and Trust Bank to form Amalgamated Banks of South Africa.

vehicles through which Afrikaner capital integrated into the industrial core of the economy" (ibid). A critically important strategy was the creation of state owned sectors in electricity, steel, chemicals and fuels. Fine and Rustomjee, 1996, point out that these state owned sectors complemented the mining conglomerate needs and provided a growing link between the state and the private sector.

Bonuskur was founded by Sanlam in 1946. "Bonuskor took the bonuses of policy holders and invested them in shares in listed companies on the Johannesburg Stock Exchange."(ibid).Bonuskur along with FVB established their own mine holding company Federale Mynbou Beperk or FM (Federal Mining Limited) in 1953 and it was FM that broke the English hegemony in coal, gold and asbestos and became *".... increasingly interested in diamonds, eventually co-operating with Anglo-American, through Genmin, though AAC wanted to ensure FM's operation in diamonds came under the De Beers Central Selling Organisation.*[i] *FM eventually controlled Genmin and in 1974 Genmin took over the Union Corporation Company, a British owned gold mining company, creating Afrikaner control of the second largest gold mining house, renamed Gencor in 1975 (Jones 1995; O'Meara 1983). "*

Verhoef (2009, 133) chronicles FVB development into an industrial holding company that by the 1970s managed nearly 30 industrial enterprises. The capital market remained small relative to European standards, and foreign capital and internal financing by mining houses remained important (Ashman and Fine, ibid).

The last important development in the story of Afrikaner capital in South Africa is the growth of the investment/merchant banking sector. In 1955, AAC established its own investment bank-Union Acceptances Limited. By 1968 Union owned assets approaching R145 million which made it the largest investment bank in the country. Another major entity established during this period was Volkskas Trustbank. Volkskas in particular grew as a result of close links with the National Party who transferred the accounts of state corporations and municipalities to the bank.

Ashman and Fine (forthcoming) describe the growth in some detail:

The very rapid growth of merchant banking from the late 1950s onwards, under conglomerate control, reinforced the close connection between finance and industry. A major series of mergers increased concentration in the economy, including financial ones, most importantly those led by Anglo's Union Acceptance Limited which merged with Syfrets Trust Co. owned by insurance firm the South African Mutual Life Association Society (later to become Old Mutual) and which was backer of Anglo's Rand Mines which merged with manufacturing conglomerate Tomas Barlow to form Barlow Rand in 1971. The combined group then merged with the originally Dutch owned Nedbank Group (then the third largest commercial bank) to form in 1974 Nedsual (Nedbank and Syfrets-UAL Holdings). Three groups, Standard, Barclays and Nedsual thus dominated banking with Volksas in fourth place and both Anglo and Old Mutual had expanded significantly into finance, especially given Anglo retained a minority stake in both Barclays and Standard. Anglo then took over the Schlesinger financial group so gaining controlling stakes in Eagle Life Assurance and Western Bank (7th largest) and Sorec Ltd (second largest property company) (Innes 1984). All the major finance groups had significant industrial and property holdings with the exception of Standard/Liberty Life which remained purely financial.

5. Key Pieces of Legislation:

Legislation has helped to define the structure and the form of competition which prevails in South African finance. The 1965 Banks Act No. 26, classified banks in functional form, commercial banks, merchant banks, hire purchase banks, etc. Commercial banks were viewed by the SARB as the only ones with money creating capabilities and therefore in the face of an ongoing money supply expansion were subject to liquid assets and capital reserve requirements. In addition, the commercial banks were required to keep interest free deposits to cover their liabilities with the SARB. Thus, legislation itself framed competitive conditions in which commercial banks were severely disadvantaged.

The SARB too has played a pivotal role in the development of the South African banking sector. The SARB in defining ownership and setting the limits to competition induced a response from the commercial banks which saw them diversifying their traditional bank functions into new areas such as hire purchase, leasing and other short term credit facilitates. More importantly, the commercial banks sought to circumvent central bank's onerous restrictions by;

a. Acquiring majority ownership of other financial intermediaries that specialised in the exempted areas.
b. Establishing their own subsidiaries to carry out such functions.

In so doing: "*Commercial banks succeeded in expanding their traditional bank operations through subsidiaries and gaining a grip on the competition by other financial intermediaries.*" Thus as Verhoef (ibid) points out by the first half of the 1980's South Africa's bank sector was dominated by five large consolidated banking groups; First National Bank Group, Standard Bank, Nedcor, Bankorp and Volkskas. Each group had at least one entity specialising in commercial, general, merchant, industrial and/or hire purchase banking. "*The sheer size of the bank groups and the number of subsidiaries within groups reduced competition effectively" (ibid).*

6. Franszen – the importance of nationally owned banks

Another aspect of the recent past material to the structure of the industry today is the Franszen Commission Report finding in 1970. The Commission found that that the foreign domination of the bank sector contained an inherent threat to the security of the country. The Report proposed that "foreign shareholding in South African banks in excess of 50 per cent should be gradually reduced to a minority position" (ibid).

Legislation would follow in 1976 restricting foreign share ownership in South African banks. Commenting on these developments Itzikowitz was to observe: "*Since the Franszen Report in 1970 monetary and fiscal policy attempts have been made to control the size of single shareholding in banks. These have been motivated by economic xenophobia and its historical corollary – fear of concentration of power in a few large organisations*[4]"

To understand these developments properly one has to recall that South Africa operated its peculiar apartheid system in an increasingly hostile world. As Verhoef (2009, 172) observes,

2. A. Itzikowitz, "The Deposit-taking Institutions Act, 94 of 1990: Its history and overview of its main provisions", *South African Mercantile Law Journal*, 4, 1992, p 181 in Verhoef, 2009.

"This was not only a fear of concentration per se, but also a fear of foreign control of a strategic sector of the economy of a country in a hostile international environment." In terms of the wider global tendency towards financialisation, as direct non market controls over banks were replaced by indirect market mechanisms, the South African monetary authorities moved in unison with the rest of the world; however in placing restrictions on the foreign ownership of bank capital, the authorities restrictions were in effect, placing restrictions on the free flow mobile capital in the industry. This is sharply at odds with what was taking place in the rest of the world and is a peculiarly South African feature of the past.

7. De Kock Commission Deregulation and Liberalisation

The De Kock Commission was established in 1978 and it produced three reports. The first in 1979 sought an end to exchange controls. The second assessed the relative positions of the building societies and financial markets in general. The third produced in 1985 signalled a sea change in South African monetary affairs by replacing direct regulatory controls with "market determined mechanisms" which were to serve as controls. In effect this 1985 Report aligns South Africa with the then new global tendency towards marketisation and financialisation.

De Kock's recommendations were embodied in the Financial Institutions Amendment Act, N° 106 of 1985. In addition and in keeping with the Banque for International Settlements (BIS) directives, more stringent capital adequacy rules were applied, and tellingly the Act removed the distinctions between the different types of banking institutions. What resulted was increased competition right across the spectrum of banking services. The new post De Kock competitive environment squeezed interest margins and induced rapid product innovation (DT Merett in Verhoef, 2009, 176).

In terms of ownership, banks could only be owned by bank holding companies or by other banks, and changes in ownership were placed under the sole purview of the Registrar of Banks. According to Verhoef (2006, 165), "*The rationale behind these restrictions was to prevent "undesirable concentration of economic power, credit privileges, bank captivity and a* *conflict of interests that result from banks and bank holding companies' control over non-bank enterprises".* For the most part this was the thinking that informed the SARB's opposition to mergers of banks and insurance companies. Of course such opposition was to be drowned out in the deluge of global deregulation which was to follow in the middle of the 1980s.

In an effort to cut unit costs in the more competitive post De Kock environment the banks were motivated to embark on a programme of rapid computerisation that required increased capital investment. Further diversification of banking services as well as a marginal decline in concentration are the chief features of this period.

The Deposit-Taking Institutions Act, N° 94 of 1990, brought South Africa further into line with BIS thinking. New prudential requirements were introduced in conformity with Basle requirements for risk management and all deposit-taking institutions were subject to uniform capital adequacy, minimum reserve balances and liquid asset requirements.

According to Verhoef (2009), the 1990 legislation aimed, *"to create a framework for the regulation, including the supervision, of the business of accepting and employing deposits of the general public."*[5]

In summary, the 1985 and 1990 legislation stipulated:

- All banks were to have sufficient capital
- All banks were to be owned by registered banks or by registered bank holding companies
- No shareholder was allowed to own more than 10 per cent of the shares issued by any one bank without the permission of the Registrar of Deposit Taking Institutions[6]

Although foreign banks were not allowed to conduct any business in the Republic, the South African banking sector

[5] A. Pienaar, "The prudential requirements of the Deposit Taking Institutions, Act 94 of 1990", *Tydskrif vir Suid-Afrikaanse Reg*, 3, 1992, pp 475

[6] If the total shareholding was to exceed 30 per cent, permission from the Minister of Finance was required. According to Verhoef (ibid), "These ratios were raised in 1992 to 15 per cent for registrar's permission and 49 per cent for ministerial permission,44 thereby perpetuating a high degree of concentration in the bank sector."

became linked the rest of the world through the contingent liabilities on its balance sheet. It was the Banks Act, N° 94 of 1990 that gave the statutory approval for the return of foreign banking interests in the form of Representative Office(s). The Representative Office (RO) of a foreign bank was not permitted to carry out the business of a fully fledged bank; however the a RO gave foreign finance a toe hold towards re-entry. While the 1985 Bank Act sought to eliminate the differences between banking institutions and building societies the 1990 legislation extended the process by doing away with the distinction between the local or foreign domicile of shareholders. The only restriction that remained was that on the maximum holdings of shareholders.

8. Mergers

Verhoef (2009) argues that the *concentration through absorption* of subsidiaries in bank holding companies was encouraged by two developments in the mid 1980's. First, there was Standard Bank's decision to disinvest in 1986, and then the 1987 Bank Act removal of the statutory differentiation between banks and building societies.

A train of mergers and acquisitions followed. Standard Bank (by equity the largest of the banks with a market capitalisation of R29.7 billion) was wholly acquired by South African interests in 1987[7].

It was then Barclays turn: Barclays PLC sold its remaining 40.4 per cent shareholding in Barclays of South Africa. The bank was renamed First National Bank and constituted the largest of the bank groups with assets of R30.3 billion in 1989. Anglo American Corporation, Southern Life Association and De Beers Consolidated Mines all featured as buyers. The large consolidated bank group had begun to emerge. The process continued, in 1988 Nedbank merged with the permanent building society and Finansbank. Old Mutual owned 52 per cent of the shareholding of the Nedcor Group. Trust Bank, established in 1956, was the commercial bank in the Bankorp Group, of which Sanlam held 66 per cent of the shareholding.

Volkskas group was the fourth largest of the bank at the end of the 1980s with assets of R3,595 million. When the

[7] Among the new owners were Liberty Life, Old Mutual, Rembrandt and Gold Fields of South Africa

distinction between bank institutions was removed Volkskas and the largest and oldest building society in South Africa, the United Building Society, exchanged shareholdings. Volkskas obtained 30 per cent shares in the building society and United 10 per cent of shares in the bank in 1987.

In January 1991 the largest single bank group was formed in South Africa, Amalgamated Banks of South Africa (ABSA). ABSA was the result of a merger of the Volkskas group, the former United Building Society, the Allied Bank and the Sage Group. The rationalisation deal was worth R1.7 billion. Finally in February 1992 ABSA acquired the Bankorp group from Sanlam and ABSA group controlled assets in excess of R80 million.

Building societies were the natural targets for banks once the demutualisation process of the mid-1980s got underway. By the end of the 1990s they were all absorbed into one or other of the large bank groups. The demutualisation of the large insurance companies started with Southern Life in 1985 and was followed by Old Mutual and Sanlam in 1998. After 1998, Sanlam consciously realigned its business to financial services and sold its controlling shareholding in ABSA.

In 1997 First Rand Group was established as a joint holding company for Rand Merchant Bank, Rand Merchant Bank, First National Bank, Southern Life Assurance Company and Momentum Life.

9. Mergers across Corporate South Africa

Complex cross-holdings and pyramid type ownership structures served big business well from Harry Openheimer’s diversification of AAC in 1927 until the 1980s and 1990s. These mechanisms reinforced the control of the families and bolstered Chandler’s (2004) notion of *personal capitalism*. Starting in the 1980’s with the ascendancy of the maximisation of shareholder value approach, new imperatives emerged that prioritised the need for effective management that would maximise the return to the shareholder[8]. According to Chabane et al (2006), “*Conglomerate unbundling and restructuring to ensure stronger focus and better strategic direction*

[8] As Chabane et al, point out, “In general, conglomerates were trading significantly below their net asset value—22% in 1995 in the case of AAC.”

represented a fundamental shift in the managerial mindset of South Africa's richest individuals and the corporations they controlled." Thus, while the South African Merger and Acquisition (M&A) frenzy that was to follow coincided with the same event in the rest of the world, its motivations arise from peculiarly South African origins.

The M&A activity in South Africa, was started by Gencor in 1993 when it disposed of a range of non-mining assets and created Billiton. According to Chabane et al; *"Barlow Rand, now called Barlow, followed suit by focusing on "brand management"—among its main businesses are Caterpillar and Hyster fork-lift truck dealerships—and greatly reducing its exposure to the domestic market. The majority of unbundling (and related "rebundling" or consolidation within sectors) deals took place in 1999, when there were 60 of such deals (accounting for R80 billion) compared with 40 deals in 1998 and 17 deals in 1997."*

When this process began in the early 1990s, ownership and control of large South African companies rested with the big conglomerates. But by 2005 this unity had been split, control now resides with an new class of managers who actually run the company on a day to day basis. Today, institutional fund managers comprise the largest group of shareholders on the JSE.

10. Internationalisation of the South Africa Finance

Conglomerate South Africa has always argued for exchange control liberalization and overseas listings. The rationale has always been that this would allow South African firms to raise capital more cheaply in international capital markets, and this in turn would increase investment in South Africa. Most fundamentally, liberalization would encourage inward foreign direct investment (FDI). Gelb (2001), notes that both private investment and inward FDI have remained low and Rashid (2011) points out that, *"South Africa is the only large emerging economy (and the only BRICS country) where net inflow of portfolio investment is higher than FDI inflows. In 2010, the ratio of portfolio investment to FDI was nearly 10 (SARB sources)."*

Starting in the late 1990s, big conglomerates moved their primary listings overseas. New valuations in hard currency eradicated the foreign exchange risk of a Rand holding thereby reducing risk premia and improving expansion capabilities. According to Chabane et al (ibid), the first important issue was by Billiton, (currently the world's largest mining company). Billiton was listed by Gencor on the London Stock Exchange (LSE) in 1997. SAB followed in early 1999 and since then has taken advantage of its larger liquidity by acquiring breweries in Asia, Europe, and Latin America.

When SAB merged with Miller to create the world's second largest brewery, Altria (previously Philip Morris) has become SABMiller's single largest shareholder with 23.5%. "*... by far largest and most evocative, listing was Anglo's. In October 1998, AAC absorbed Minorco and simplified its highly complex ownership structure. Following the London listing in May 1999, AAC joined Billiton and SAB in the FTSE 100 index. Old Mutual and Liberty International have also obtained primary London listings, as have two infotech companies, PQ Holdings and Datatec. In 1999, Sappi, though still with a primary JSE listing, had secondary listings in four foreign stock exchanges; 52% of its shareholders and ¾ of its assets were abroad and 85% of earnings in hard currency." (ibid)*

International listings have been used to access liquidity that has funded a pattern of aggressive outward foreign investment and acquisitions by corporate South Africa. Firms like SAB, Sasol, and Sappi have also been involved in acquisitions, joint ventures, and greenfield investment in Organization for Economic Cooperation and Development (OECD) countries and other emerging markets; outward FDI has grown from $8.7 billion in 1995 to $28.8 billion in 2004 (Goldstein, 2006). In addition the number of South African companies doing business in Africa, has more than doubled since 1994.

The pace and scale of the international listings process ignited concerns about conglomerates' motivations and the benefits and costs to South Africa led the Government to reconsider its approach, In February 2000, the Government published new criteria for future cases. Since then overseas listings have been few and far between[9].

It is quite clear that South Africa's conglomerates enhanced their ability to raise new capital more cheaply through the overseas listing. It also seems clear that they ... "have generally found relationships with investors, analysts, and financial and accounting regulators more demanding than in their home country, where companies such as AAC or SAB were used to dictating the terms of engagement." If as Rashid (2011) speculates, *"One should expect considerable political influence of the financial sector given the sector's share of national income in South Africa. It is almost universally true that larger the share of a particular sector in the economy, the more deferential the economy is likely to be to the demands of that sector."*And if as Chabane et al advance, *"the increased autonomy of firms with overseas listings and the increased proportions of conglomerates' revenues coming from overseas activities,"* weakens the leverage of the South African authorities, the state would be considerably less influential in its ability to regulate the conglomerates.

The internationalisation of the South African bank sector proceeded in its own specific manner contrary to what has been observed in many other developing countries. Rather than the foreign banks deploying in South Africa the overarching tendency was for South African Banks to extend their operations overseas in an effort to serve South Africa's conglomerates that were deploying resources overseas.

Almost as soon as permission was granted in 1997 ABSA, Investec Bank, First National Bank, Nedbank, Standard Bank and Rand Merchant Bank followed their customers and sought to acquire overseas interests. One of the first moves by all the banks was to establish offices in off shore tax centres like Mauritius, Guernsey, Jersey, the British Virgin Islands and the Grand Cayman.

By 2011, South African banks had migrated to many far flung parts of the world including Canada, the USA, Ireland, Hong

[9] One notable exception is Investec. In November 2001 the Government granted Investec permission to list overseas. The financial services group, which was then earning 60% of its revenues outside South Africa, was given the go-ahead on condition it kept its headquarters in Johannesburg (see Chabane et al, 2006).

Kong, Malta UK, Hong Kong, Liberia, the United Arab Emirates and Russia. Australia Argentina, Brazil, Peru, Colombia, as well as in the People's Republic of China, Singapore, Germany, Switzerland Italy, Iran, India and Turkey. One notable trend in the expansion of operations has been an expansion into other countries in Africa that started around the turn of the century and has continued unabated. Today South African banks operate in Kenya, Zimbabwe, Botswana, Uganda, Nigeria, the DRC, Angola and other African countries.

As Verhoef (2009, 192) puts it; "*The ability of South African banks to extend operations on such a scale, was testimony to the sophistication of their management, the strength of their capital base and the confidence of both the domestic clients they followed into global markets, and the international clients doing business in South Africa. Globalisation of bank operations was as much a function of the size and level of experience and expertise of the banks as of the soundness of domestic central bank regulation.*"

11. Foreign Banks

Today, by comparison with other BRIC and emerging market countries, the South African economy has a very large presence of foreign banks (Rashid, 2011). According to the World Bank financial sector database [10], banks that are 50% or more foreign-owned controlled nearly 30% of the banking sector assets. This is contrary to the data report in the 2011 Annual Report of the South African Reserve Bank, which claims that foreign banks and their branches control only 6.1% of the banking sector assets.

The Banks Act, N° 94 of 1990, allowed foreign banks to re-enter the local market. In the period 1992-2005 the number of foreign banks authorised to establish representative offices (RO's) in South Africa rose from 31 (at the start of the period) to 61 (in 2000), but then declined to 43 in 2011 (See Table 1). The representative offices were not fully fledged banks, they did not engage in in the full range of bank operations, rather they were specialist institutions providing a presence for foreign banks seeking to enter the market or

[10] Barth, James R. Gerard Caprio, Jr. and Ross Levine (2001, updated 2008). "The regulation and supervision of banks around the world - a new database". The World Bank Policy Research Working Paper Series, 2588

they specialised in providing economic and trade information to select clients.

In 1992 the nationality of the representative offices operating in South Africa was largely European. By 2011 American, Canadian, Chinese, Japanese as well as European and other banking interests from a total of 22 countries were all represented.

It was the Banks Amendment Act, N° 26 of 1994 that finally opened South Africa to the entry of foreign banking institutions as banks, licensed to conduct banking business. As South Africa entered the 1990's we find that all the banks were subjected to a single set of regulations and crucially foreign banking competitors were allowed to enter the market. The imperial legacy remained in the form of the domination of the big four commercial banks (the two former imperial banks along with Nedbank and Volkskas).

The number of fully fledged branches of international banks registered in South Africa rose from 4 in 1995 to 15 in 2005 declining to 12 in 2011. Making up this number are ABN Amro Bank NV, Bank of Baroda, Citibank, Commerzbank Aktiengesellschaft, Credit Agricole Indosuez, ING Bank NV, Morgan Guaranty Trust Company and Société Généralé.

Table 2: South Africa's Registered Bank Sector

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Banks*	30	22	20	19	19	19	19	18	17	17
Mutual Banks	2	2	2	2	2	2	2	2	2	2
Branches of international banks in the Republic of South Africa	14	15	15	15	14	14	14	13	13	12
Representative offices	52	44	43	47	43	46	43	42	41	43
Controlling companies	27	19	16	15	15	15	15	15	15	15
Banks under curatorship	1	1	0	0	0	0	0	0	0	0
Banks in receivership	2	2	0	0	0	0	0	0	0	0
Banks in final liquidation.......	1	1	2	2	2	2	2	2	2	2

Includes active banks and banks exempted by the Registrar of Banks (with effect from 1 July 1996) in terms of the Supervision of Financial Institutions Rationalisation Act, 1996 (Act No. 32 of 1996) and section 1(cc) of the Banks Act, 1990. Source: SARB 2011 Overview

Two significant developments took place in the middle 2000's; first in 2005 Barclays Bank PLC obtained controlling share ownership in ABSA. Thus ABSA became a subsidiary of Barclays. This was the first acquisition by a foreign bank of a large South African bank in terms of section 37 of the Banks Act, N° 94 of 1990, and it required the approval of the Minister of Finance himself. Then in 2006 the Chinese entered the South African market with two banks, China Construction Bank Corporation and Bank of China Ltd[11].

Foreign banks in South Africa are principally involved in specific areas like investment banking or trade finance. They generally service the corporate sector. According to the Task Group Report for the National Treasury and the South African Reserve Bank (in Verhoef, 2009, 186) *"they did not succeed in penetrating the retail sector. The main reason for this development was the regulatory environment: foreign banks are required to be separately capitalised with South Africa and be structured as subsidiaries of foreign holding companies rather than as branches[12]. This is not the case in many industrialised countries where 'home-country' regulation applies."*

Between 2004 and 2007 (expressed as a percentage of GDP), the claims of foreign banks vis-à-vis the South African private sector increased from 14% to 42%. This entailed huge credit expansion that Rashid (2011), estimates was in excess of USD 90.0 billion. Looked at over the period foreign lending would appear to be strongly pro-cyclical. With the onset of the Great Recession of 2008, foreign banks reduced their exposures in South Africa by approximately USD 20.0 billion in the year between December 2007 and December 2008. *"As a percentage of GDP, the contraction in credit from foreign banks was as large as 7% of GDP, compared to 2.5% and 0.87%, 0.89% contraction in foreign bank lending in Brazil, China and India respectively."*

The foreign banks in South Africa appear to be more risk averse compared to their domestic counterparts. We have also established that foreign bank lending to the domestic economy

[11] Both moves taken together confirm the relative attractiveness of South Africa as a destination for international banking capital.

[12] There is no restriction on foreign bank entry into South Africa through acquisition, subsidiary or branch operation.

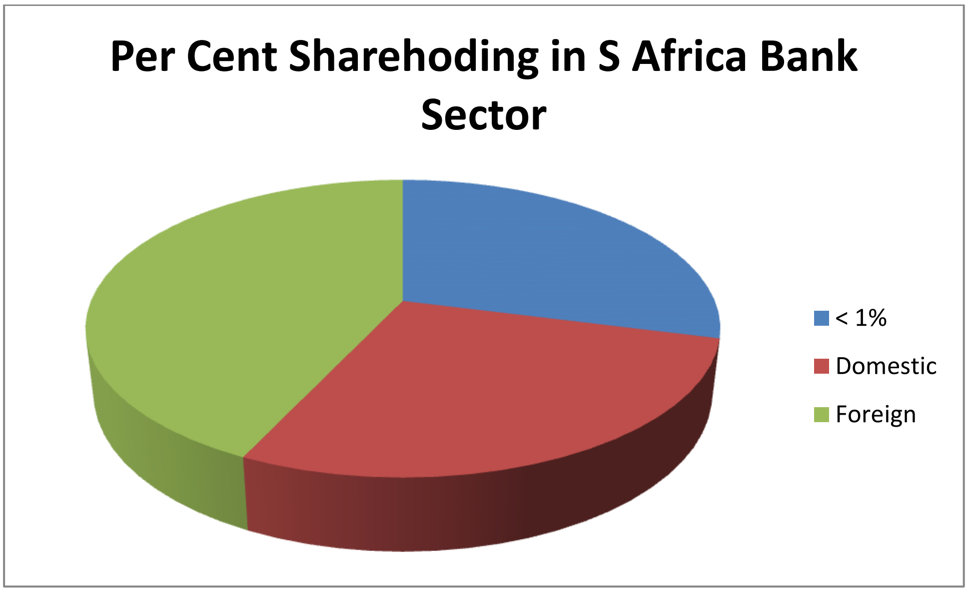
can be strongly pro-cyclical. And from experience around the world we know that foreign banks in general tend to avoid lending to small and medium sized enterprises in the developing countries because of the problems of information asymmetry (Stiglitz, Rashid). Given that foreign banks specialise in consumer and trade credits,(especially credit for imports of consumer goods), and given too that the banks in South Africa do not face any restriction in capital market activities, it suggests that these banks engage in equity trading activities, where they earn a higher return from non-lending activities.

12. Domestic Banks

In keeping with the historical legacy, in the contemporary period from 1990 to 2011, the domestic banking landscape has been dominated by the big four. Their assets as proportion of assets of all bank assets rose from 70 per cent in 1995 to 82.2 per cent in 2007 to 89 percent at the end of 2011[13].

With respect to ownership, 43 per cent of issued banking shares are held by foreigners with 28 per cent being held by domestic shareholders. The remaining 29 per cent of shares are held by the "small" shareholder who owns less than 1 per cent of the total issue.

Figure 2



Source: SARB, 2011, Overview

[13] Verhoef (2009) and SARB, 2011, Banking Sector Overview

13. Structure by JSE Capitalisation

In order to determine changes in the structure of corporate South Africa, Chabane et al, (ibid), undertook a comparison of the rankings of the top 100 listed companies in 1994 with those of 2004. The significant conclusions are as follows:

1. Confirmation that a radical restructuring has occurred. Only 41 of the top 100 listed companies in 1994 were still ranked ten years later.
2. In 1994, 83 of the top 100 companies were owned or controlled by the top six conglomerates. By 2004, the number of companies controlled by these conglomerates had fallen to 47.
3. The importance of the top conglomerates remained significant. Albeit listed separately, three of the top 20 (Anglo American, Amplats, and AngloGold) were still effectively part of the Anglo group in 2004. Of the top 20 companies in 2004, 13 were part of a major conglomerate grouping.
4. Foreign-controlled firms in the top 100 increased from five in 1994 to 11 in 2004. The authors attribute this to both internationalization in the ownership structure of South African firms now listed abroad and acquisitions of local firms by international companies.
5. Although black ownership increased over the period, it did so unevenly and marginally as only five companies under black control were in the top 100 in 2004.
6. With regard to the change in sectoral composition of the top 100 over the period, there is a mixed picture. The authors find that the number of firms engaged in financial, retail, and other services increased significantly. These firms include MTNSA, Netcare, Pick n Pay, and Edcon. Banking and insurance companies emerge as particularly important and account for seven of the top 20 in 2004, including the demutualized Old Mutual and Sanlam.
7. A fair degree of continuity remains between the two periods as the largest industrials (including mining), still accounts for six of the top 20 firms, even including services.
8. Continuity is also reflected in continued high levels of concentration within sectors. A large proportion of mergers have been vertical, increasing control of

dominant firms through production chains. While this avoids the direct competition concerns of horizontal mergers, it realizes greater consolidation within industries. Vertical integration can yield efficiency gains such as from the internalization of transactions costs but can also increase barriers to entry, make collusion easier to maintain, and lead to foreclosure of competitors (Riordan and Salop, 1995).

Table three (below) extends the Chabane et al (ibid) measure of control by adding data on the market capitalisation shares by group for selected years from 2004 onwards.

Foreigners (corporations and other), dominate the JSE by market capitalisation. Foreign controlled interests now account for 30% of JSE capitalisation, far more than any other group on the exchange.

Table 3: Summary of control of JSE market capitalisation (% of total)[14]

Group	1985	1990	1994	1998	2002	2004	2006	2011	2012
Foreign	5.9	2.1	2.2	3.9	10.1	18.5	20.8	29.8	30.0
Institutions			0.9	4.2	9.1	10.3	9.1	17.0	19.4
Directors	8.1	6.7	7.0	14.4	7.4	5.8	6.7	8.9	9.2
SABMiller					4.0	5.1	5.7	7.5	9.2
Anglo American Corp	53.6	44.2	43.3	17.4	20.2	18.7	21.0	11.8	8.9
Rembrandt/Remgro	3.8	13.6	13.0	9.0	10.0	7.9	7.8	5.2	7.2
Black Groups[15]				9.6	3.5	6.3	5.1	4.6	3.9
RMB/FirstRand			0.5	4.8	4.7	4.9	3.9	3.1	3.9
SA Mutual/Old Mutual	10.6	10.2	9.7	8.8	12.0	4.5	5.5	2.9	3.3
Sanlam	12.2	13.2	10.5	11.1	6.3	2.7	2.3	1.2	1.4
Liberty Life/Standard Bank	2.0	2.6	7.2	9.5	6.0	4.7	3.5	2.4	1.1
Bidvest Group				1.0	1.0	1.2	1.0	0.8	0.9
Investec			0.4	3.3	1.9	0.8	1.2	0.6	0.7
PSG									0.6
State						2.2	2.0	0.2	0.1
Altech								0.1	0.1
ABSA						2.2			
Sasol			1.7	2.2	3.8	4.2	4.6	3.9	
Anglovaal[16]	2.1	2.5	3.6	0.8					
TOTAL	**100**	**100**	**100**	**100**	**100**	**100**	**100**	**100**	**100**

Source: McGregor's (1999, 2000, 2003, 2007, 2011) Who Owns Whom

Foreign control and dominance has proceeded through capital inflows, (especially portfolio flows) and South Africa with

[14] Control is assessed by *McGregor's* taking into account the various cross-holdings of shares that exist and may be associated with a relatively small direct shareholding in any given company.

[15] The Black owned groups are identified as such by *McGregor's* on the basis of all those companies which have significant black influence in their ownership.

[16] In 1998 the Anglovaal shareholding was split equally, giving the Hersov and Menell families each control over 0.4% of the JSE capitalisation.

its sophisticated stock exchange is something of a magnet for hot money flows (particularly during periods of uncertainty. Foreign direct investment has also played its part, most notably the R30-billion deal by Barclays to become the biggest shareholder in ABSA[17].

Unbundling by the big conglomerates has served as a vehicle by which foreign and institutional investor's have extended control. The Competition Commission (2008) reports; *"Conglomerate groupings still dominate the JSE. The market share of the 6 big conglomerates has continued to shrink ... This however does not take into account other companies owned or controlled by these conglomerates. Despite unbundling by the major conglomerates they are still 'remarkably significant, with their overall size being increased by international acquisitions and mergers, such as to create BHP-Billiton and SAB-Miller."*The number of merger notifications to the Commission increased substantially between 2001 and 2007. Most mergers during this period occurred in the manufacturing sector and in financial services and real estate sector. According to the Commission, the number of mergers in the agriculture and mining sector has grown dramatically ... broadly in line with the commodity price boom. The number of conglomerate mergers[18], where the products produced by the merging parties do not compete directly with one another, has increased significantly over the period (Competition Commission, 2008). High concentration, coupled with low levels of competitive rivalry, results in supra-competitive prices. Associated with this is that existing dominant firms are able to create barriers to entry and enjoy abnormal profits.

Table 3 records that in 2012 SAB-Miller replaced AAC as the largest listed company by market capitalisation. This is a notable development because it would be the first time in the history of the exchange that market capitalisation would be dominated by any other company but AAC. Whether it signifies a deeper more meaningful change remains to be seen.

[17] According to Competition Commission (2008), this has been critical in the increase of foreign ownership on the JSE.

[18] Conglomerate mergers are neither horizontal nor vertical. These are mergers between firms with complementary products, neighbouring products, and unrelated products (Competition Commission, 2008).

Conclusion

The structure of banking in South Africa has been shaped by the history, competition and legislation. Although the circumstances have changed conglomerate concentration reproduces itself from period to period and despite unbundling, cross-holdings linking company with company remain essential features of the arena just as they were in 1929.

By far the most important change has been in the internationalisation of local banking. When taken together with the dominance in the corporate market makes it clear that South African finance is in large part propelled by foreign interests.

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[i] A confidential letter (cited in Verhoef 2009a:141) from Anglo's Harry Oppenheimer to the chairman of the FM board stated that should FM 'or any other company over which it exercised effective control (including General Mining) make any new diamond discoveries or were invited to hand any new diamond venture, such discovery or venture would be offered in the first place to a new company to be formed for that purpose, and the capital of the new company would be owned 51 per cent by De Beers and 49 per cent by Federale Mynbou.'