UNITED NATIONS

A

General Assembly

Distr.
GENERAL

A/45/539
18 October 1990

ORIGINAL: ENGLISH

Forty-fifth session
Agenda item 34

POLICIES OF APARTHEID OF THE GOVERNMENT OF SOUTH AFRICA

International financial pressure on the apartheid economy of South Africa

Report of the Secretary-General

CONTENTS

90-26717 1905h (E)

/...

CONTENTS (continued)

/...

I. PREFACE

1. The present report has been prepared in response to General Assembly resolution 44/27 E of 22 November 1989, in which the Assembly requested the Secretary-General to submit to its forty-fifth session a report on financial links of Governments and private financial institutions with South Africa. In that resolution, the Assembly, noting South Africa's dependence on external credits and loans, regretted and deplored that international banks had reached agreement with South African authorities to reschedule a substantial proportion of South Africa's external debt for a further period of three and a half years from 1 July 1990; urged Governments and private financial institutions to deny new bank loans to South Africa, and called on Member States to restrict the provision of trade credits by reducing maximum credit terms to 90 days; and called on those States which continue to trade with South Africa to take South Africa "off cover" for insurance purposes at official export credit agencies.

2. The present report surveys the measures that have been adopted by Member States to restrict trade credit for South African trade, as well as action undertaken by the United Nations and intergovernmental organisations concerning financial pressure on South Africa. The report provides a brief review of South Africa's role in the international financial system, explaining the nature and scale of its dependence on external sources of finance. It offers an analysis of its current debt position and the economic and financial measures pursued by the South African authorities to cope with it. The third rescheduling agreement on South African debt, announced on 18 October 1989, is described in some detail, along with an analysis of its actual impact on the economy of South Africa. The report also provides a framework for understanding the operation of trade credits and surveys the measures to restrict trade credits for South Africa that have been adopted by individual Member States, concentrating on those States which have a substantial trading relationship with South Africa. Based on the available data, the international banking sector's involvement in the provision of trade credits to South Africa is also surveyed. Finally, the effectiveness of the measures is discussed, along with a brief account of the impact that a rigorous application of such credit restrictions could have on the South African economy.

II. ACTION BY THE UNITED NATIONS AND INTERGOVERNMENTAL ORGANIZATIONS CONCERNING FINANCIAL PRESSURE ON SOUTH AFRICA

3. In 1962 the General Assembly, in its resolution 1761 (XVII) of 6 November 1962, first called on Member States to adopt economic measures against South Africa in order to assist in the abolition of apartheid. Since then, the Assembly has adopted numerous resolutions calling for the adoption of financial measures against South Africa, that is, the denial of loans and trade credit. In 1966 for the first time the General Assembly, in its resolution 2202 (XXI) of 16 December 1966, called on Member States to discourage the provision of loans by their national banks to the Government of South Africa or to South African companies. In 1985, after the imposition of a state of emergency in South Africa,

/...

the General Assembly, in its resolution 40/64 A of 10 December 1985, requested all States to adopt legislative and/or comparable measures to enforce the prohibition of financial loans to and investments in South Africa and the sale of krugerrands, as well as the withdrawal of investments from that country. In the same year, the Security Council (resolution 569 (1985)) also urged all Member States to prohibit the sale of krugerrands and to suspend the provision of guaranteed export loans to South Africa.

4. In 1989 the General Assembly, in its resolution 44/27 E, again urged Governments and private financial institutions to deny new bank loans to South Africa, whether to the public or private sectors, and to restrict the provision of trade credits and cease loan insurance, in particular, (a) by reducing the maximum credit terms to 90 days and (b) by taking South Africa "off cover" with official government export credit agencies.

5. In summary, the General Assembly has recommended that all Governments adopt specific financial measures against South Africa, including:

(a) The prohibition of new loans and commercial credits;

(b) The cessation of all promotion of and support for trade with South Africa, including the extension of any inducements, credits, guaranties or other incentives with respect to exports to South Africa.

6. In addition, the United Nations has called for a strict monitoring of the implementation of these measures and the imposition of penalties for violations.

7. City and local authorities of Member States have been called upon to withdraw accounts from banks or investments from companies that collaborate with the Government of South Africa and to deny contracts or facilities to financial institutions involved in that country.

8. Similarly, specialised agencies and other intergovernmental organizations have been called upon to withhold facilities or investment of funds from banks, financial institutions or corporations that provide loans to South Africa and to deny contracts or facilities to financial institutions that collaborate with that Government.

9. At the request of the Economic and Social Council, the Secretary-General in 1989 convened a panel of eminent persons to hold public hearings and to consider expert testimony on the situation in South Africa (Geneva, 4-6 September 1989). The primary aim of the hearings was thus to examine the process of change that is under way in South Africa and to investigate actions that the international community could take through sanctions and other means - directly and through transnational corporations - to accelerate the abolition of apartheid and to contribute positively towards the better functioning of a post-apartheid society in South Africa. These hearings, organized by the United Nations Centre on Transnational Corporations, built on an earlier exercise, which was conducted by a panel of eminent persor[illegible] [illegible]aired by the Rt. Hon. Malcolm Fraser, former Prime Minister of Australia. [illegible]e hearings were held in New York in September 1985 and resulted in a comprehen[illegible] sot of recommendations that was submitted to the

/...

Economic and Social Council in 1986 and afterward presented to the General Assembly by the Chairman of the panel. The panel of eminent persons established to conduct the second hearings 1/ urged that, among other things:

(a) Official export credit agencies, such as the United Kingdom Export Credit Guarantee Department, take South Africa risk "off cover" and keep it off covert

(b) National regulatory agencies and the Bank for International Settlements (BIS) review their provisioning requirements for South African exposure with a view to reflecting the country's deteriorating credit worthiness1

(c) National authorities ensure that any trade credits given to South Africa by their banks be of very short duration - no more than 90 days - 80 as both to reflect the country's deteriorating credit worthiness and to maintain continuaus pressure on the South African authorities]

(d) Governments (particularly the Government of Switzerland) forbid South African authorities from raising money either through gold swaps or through sales of gold in the forward market.

10. The United Nations Commission on Transnational Corporations, in its latest resolution, also called upon all multilateral financial and development institutions to cease immediately any kind of support or other forms of collaboration with South Africa. 2/

11. The Committee on Action against Apartheid of the International Labour Conference in 1988, and subsequently in 1989 and 1990, urged Governments to refuse to roll over loans and to deny new loans and trade credits as well as credit guarantees to South Africa. 3/ In 1989 the International Labour Organisation (ILO) established a group of independent experts to monitor the implementation of sanctions and other action against apartheid throughout the world. This group was set up in compliance with the conclusions drawn up by the Committee on Action against Apartheid at the seventy-fifth session (1988) of the International Labour Conference. The group decided to place emphasis on studies concerning an embargo on South African coal, effective financial sanctions and the severance of air links with South Africa. At this time the group has already considered a preliminary study on the subject of financial sanctions.

12. For several years now the International Monetary Fund (IMF) and the World Bank have not made loans to South Africa. Although the country is still a member of both organizations, it has not been represented since 1974 on either board of governors, having therefore no say in their policies. Moreover, the United States Domestic Housing and International Recovery and Stability Act of 1983 includes a clause requiring the United States Director of IMF to vote against requests for drawing rights from the Fund in excess of quota by countries practising apartheid. South Africa drew down funds in 1982, which were repaid by 1987. In the past South Africa has received several project loans from the World Bank, the last of which was fully repaid in 1976. Currently it does no:. qualify as a potential borrower. Both IMF and the World Bank continue to monitor economic and social developments in South Africa.

/...

13, The member States of the Commonwealth, at the meeting of the Heads of Government in Nassau in 1985, recommended a comprehensive package of economic measures against South Africa, including a prohibition on government loans. At the meeting of the Beads of Government at Kuala Lumpur in 1989, they agreed, with the exception of the United Kingdom of Great Britain and Northern Ireland, that these measures should be tightened. To this end, they proposed that member Govarnments should call on all banks and financial institutions to reduce trade credit loans to a maximum of 90 days duration and to have all official export credit agencies take South Africa off cover for trade credit insurance purposes.

14. The Organisation of African Unity (OAU) has consistently called on its members to adopt comprehensive and mandatory sanctions against South Africa. In particular, in 1986 (resolution CM/Res.1019 (XLIII)), its Council of Ministers called on banks that rescheduled South African debt to seize South African assets abroad, while at its fiftieth ordinary session, held at Addis Ababa in 1989, it urged the international banking community not to reschedule Pretoria's foreign debt (resolution CM/Res.1207 (L)).

15. The Movement of Non-Aligned Countries, within the context of its call for comprehensive and mandatory sanctions against South Africa, has called for the adoption of financial sanctions. Specifically, at the Conference of its Foreign Ministers, which was held in Luanda in 1985, it urged all national and international financial institutions to cease their assistance to South Africa (see A/40/854-S/17610 and Corr.1). Furthermore, at the Conference of Heads of States held at Harare in 1986, the Movement requested the cessation of financial loans and of any governmental insurance guarantee of credits to Pretoria (see A/41/697-S/18392).

16. These proposals all have been made in the belief that they will exert pressure on the South African authorities in such a way as to hasten the abolition of apartheid. The grounds for this expectation appear to be in the general dependence of the South African economy on international trade and capital markets. The evidence for this dependence lies in the structure of the South African balance of payments and also in the stabilization and structural adjustment policies that the South African authorities have adopted in recent years. These matters are dealt with in chapter III.

III. SOUTH AFRICA IN INTERNATIONAL FINANCE AND ITS FOREIGN DEBT

A. The structure of the external balance

17. South Africa, like other primary commodity producing countries, has an open economy. In 1989 imports of goods and services accounted for more than 25 per cent of total gross domestic product (GDP), while exports accounted for 33 per cent. The economy is therefore vulnerable to a slowdown in the world economy and to changes in international commodity prices.

18. More specifically, South Africa is heavily dependent on exports of primary commodities to the industrial economies, in particular precious metals and

minerals, with gold providing approximately one third of total export revenue (down from 44.5 per cent in 1980) and manufactured exports representing another third of the total.

19. The manufacturing sector accounted for 23.3 per cent of GDP in 1970, but has largely stagnated since, growing only to 24.1 per cent of GDP by 1988, Expansion of the domestic economy can be achieved only through the import of capital equipment and intermediate goods, which together constitute almost 80 per cent of total imports.

20. As a result, although South Africa has some of the features of a "newly industrialising country", it would perhaps be truer to define it as an unusually highly developed exporter of primary products, which has failed to emerge as a significant producer of manufactured goods. This failure is in turn related to the structural features of the South African economy. One sector is characterised by high incomes, high levels of domestic consumption, advanced welfare and service industries, and substantial ownership of capital. The other sector is characterised by low incomes, low levels of domestic consumption, poorly developed welfare and service industries, and negligible capital ownership. This rector of the economy is also subject to increasingly high levels of structural (long-term) unemployment and widespread poverty.

21. In the past, South Africa's current account position - the balance between imports and exports of goods and services - reflected its business cycle, with alternate surpluses and deficits. Whenever the economy grew faster than about 3 per cent per year, imparts increased rapidly.

22. Furthermore, there has been a marked tendency over the past few decades for the capital intensity of production to increase, implying a growing reliance on imported capital goods. In periods of sluggish growth, however, import volumes declined, allowing the current account to move into surplus - or the deficit. to decline.

23. In the past this pattern was noticeably stable. During an upswing of the business cycle, current account deficits were financed from abroad. High rates of growth and high profits made South Africa an attractive focus for foreign portfolio and loan investment, generating a surplus on the capital account. During a downswing, current account surpluses would allow for deficits on the capital account. Monetary and fiscal policy measures taken by the Government were aimed at producing the appropriate adjustments.

24. However, as a result of South Africa's foreign exchange crisis of 1985, this situation changed sharply. In the absence of any significant new capital inflows, the Government of South Africa has been forced to adopt policies designed to generate a continuing substantial current account surplus in order to meet debt repayment obligations.

25. In the period 1985-1989 (see table 1), annual GDP growth averaged only 1.5 per cent, and the stronger growth experienced in 1988 (3.7 per cent) clearly highlighted the external constraint, with imports growing by 22.5 per cent and a current account surplus diminished by half. Tha fragility of the external balance

/...

Table 1. South Africa: Percentage growth in selected components of gross domestic product, 1985-1989

(at constant 1985 prices)

	1985	1986	1987	1988 First quarter	1988 Second quarter	1988 Third quarter	1988 Fourth quarter	1988 Yearly average	1989 First quarter	1989 Second quarter	1989 Third quarter	1989 Fourth quarter	1989 Yearly average
Private consumption	-3.6	0.8	3.7	4.9	4.6	5.7	6.3	4.9	1.9	1.3	0.2	0.6	2.9
Government consumption	3.4	2.2	3.9	20.6	-14.2	-9.1	3.2	1.6	42.0	-6.3	-7.9	-5.3	4.6
Cross domestic fixed investment	-7.2	-17.9	-2.4	12.6	11.2	6.9	2.0	8.6	5.6	4.6	0.6	-3.2	4.0
Cross domestic expenditure	-7.8	0.1	4.1	25.0	1.5	-6.3	0.4	7.6	6.1	-1.3	-7.5	-7.2	-0.8
+ Exports	10.1	-1.4	-2.6	-5.3	12.0	26.3	19.4	5.7	-14.5	52.3	-12.7	-0.8	9.5
- Imports	-14.8	-2.6	3.9	19.2	8.9	-10.6	11.0	22.5	-5.6	51.1	-38.4	-20.7	0.1
Gross domestic product	-0.8	0.3	2.1	5.5	2.5	3.9	3.4	3.7	2.1	1.3	1.1	-1.5	2.1

Source: South African Reserve Bank Quarterly Bulletin, March 1990.

/...

and the continued weakness of domestic saving and investment led the Government to tighten its domestic policy in order to slow down the economy. The result was a modest 2.1 per cent GDP growth in 1989 and a halt to growth in imports (0.1 par cent).

26. Over the same period (1985-1989), private and public (government) consumption were the substantial factors in the growth of GDP. Fixed investment growth, which declined every year from 1981 to 1987, has made only a modest recovery in the last two years (see table 1).

27. The South African authorities' attempts to employ monetary policy to limit inflation have met with only partial success. Until the first quarter of 1989 this policy was subject to short-term changes for other considerations. Also, up to mid-1988, frequent and sharp adjustments in interest rates (see table 2) resulted in variations in the velocity of circulation of money, which in turn made the attainment of monetary targets more difficult. As a result of repeated overshooting of the targets, the effectiveness of the Government's policy was seriously questioned,

26. Since the first quarter of 1989, however, the Government of South Africa has pursued a different economic strategy consisting of (a) medium-term stabilisation policies, and (b) long-term structural adjustment policies. Stabilisation policies include high interest rates to encourage savings and to restrain consumptioni a stable targeted monetary policy with the aim of reducing inflation; a reduction of the budget deficit to 3 per cent of GDP, making the Government neutral in terms of swings.

29. Structural adjustment policies include an ambitious programme of privatisation, the deregulation of the financial system, a new general export incentive scheme and reform of the tariff structure. The aim is to stimulate growth through the creation of an environment more conducive to market-oriented strategies by the private sector.

30. Both aspects of the strategy reflect the influence of liberal economic theory, though the degree of state interventionism appears to be far greater in South Africa than in developed countries elsewhere that have adopted similar policies in recent years. The primary objective of this strategy is to ensure that the growth created is export-led, particularly in manufacturing, and through the beneficiation of primary commodities, A secondary objective is to devise an "inward industrialisation" that would concentrate development on the promotion of labour-intensive activities with a low import content.

31. With the exception of the first quarter of 1988, the current account of the balance of payments has been in surplus since 1985 (see table 3). Despite the international trade sanctions imposed since 1985, exports have performed positively, partly because mining products seem to be less responsive to sanctions. This may also reflect South Africa's attempts to diversify into new markets, although the extent of its success in this respect has been limited. Except for the temporary acceleration experienced in 1988, imports were kept low primarily by the tight economic policies dictated by the necessity to curb domestic demand to ensure a current account surplus.

/...

Table 2. South Africa: Changes in selected prices and exchange rates, 1985-1989

	1985	1986	1987	1988 First quarter	1988 Second quarter	1988 Third quarter	1988 Fourth quarter	1988 Yearly average	1989 First quarter	1989 Second quarter	1989 Third quarter	1989 Fourth quarter	1989 Yearly average
Consumer prices (percentage)	14.2	18.6	16.1	13.0	13.0	12.3	12.3	12.9	13.6	15.0	15.1	15.1	14.7
Interest rates (prime lending rates) (percentage)	21.5	14.3	12.5	13.3	14.7	16.0	17.3	15.3	18.7	19.1	20.0	21.0	19.6
Real effective exchange rate (1985 = 100)	100.0	02.2	104.1	103.2	97.8	96.3	96.0	98.3	98.4	97.1	97.6	101.7	98.7
$US/rand exchange rate	0.4564	0.4408	0.4914	0.4881	0.4531	0.4111	0.4168	0.4423	0.4068	0.3753	0.3655	0.3811	0.3822

Source: IMF, International Financial Statistics, May 1990, and South African Reserve Bank Quarterly Bulletin, March 1990.

Table 3. South Africa: Current account of the balance of payments, 1985-1989 a/

(Millions of rands)

	1985	1986	1967	1988 First quarter	1988 Second quarter	1988 Third quarter	1988 Fourth quarter	1988 Yearly average	1989 First quarter	1989 Second quarter	1989 Third quarter	1989 Fourth quarter	1989 Yearly average
Merchandise exports fob	20 465	25 048	25 146	26 300	29 282	33 830	36 476	31 472	34 560	44 320	40 610	39 730	39 555
Net gold output	15 460	16 719	17 792	18 530	19 948	20 230	19 780	19 622	18 470	18 150	19 670	20 122	19 228
Merchandise imports fob	23 045	25 514	28 320	36 780	38 310	40 070	41 520	39 170	42 150	49 580	43 930	40 072	44 133
+ Service receipts	5 796	6 222	6 4'3	6 923	6 705	8 OS8	8 330	7 504	8 690	9 230	9 770	9 498	9 297
- Service payments	13 109	15 664	15 350	15 460	16 394	17 701	17 973	16 882	17 690	20 690	20 900	22 244	20 381
Current account balance	5 925	1 196	6 152	-58	1 748	4 620	5 446	2 939	2 710	1 970	5 A40	5 868	4 097

Source: South African Reserve Bank Quarterly Bulletin, March 1990.

a/ Seasonally adjusted annual rates.

32. Invisible transactions in the current account are constantly in deficit, the receipts from services covering less than half of payments. However, dividend and profit remittances as a proportion of export earnings have declined by almost half in the 30 years from 1956 to 1985.

B. Balance of payments and capital flows

33, The capital account of the balance of payments consists of the flows of capital in the form of investment and loans. Investment may be financed through either equity or debt. From the end of the Second World War until the mid-1970s domestic savings replaced foreign capital as the principal source of investment. 4/ As a recent study points out, "nearly 88 per cent of the $11 biliion increase in the value of foreign direct investment between 1956 and 1980 was due to reinvested or retained earnings, and less than 13 per cent was due to new capital inflows from abroad". 5/ Reflecting this fact, the nature of foreign investment in South Africa changed from the mid-1950s. Whereas in 1956 long-term equity investment represented 75 per cent of foreign investment in South Africa, by 1985 foreign investment mostly took the form of debt, and in particular short-term debt, which in 1985 constituted fully 40 per cent of all South Africa's external liabilities 6/ (see table 4). Most of this debt was accumulated in the period 1980-1985, a period that coincided with a sharp decline in the world price of gold, high rates of domestic price inflation and, particularly in the second half of 1984, a sharp depreciation in the value of the rand on foreign exchange markets.

34. Between 1980 and 1984, external debt increased by 53 per cent in dollar terms (up from $US 16.9 billion to $24.3 billion) but by almost 400 per cent in rend terms (from R 12.6 billion to R 48.2 billion) as a result of this depreciation. In the same period, external debt as a proportion of GDP rose from 20.3 to 45.7 per cent.

35. Much of the increase in borrowing was accounted for by the private sector, owing in part to the development of the Eurocurrency market and in part to the search by local business for lover interest rates. By the time of the financial crisis in 1985, approximately 72 per cent of South Africa's loan debt was in short-term instruments of various kinds, much of it inter-bank borrowing. Even so, the quantity of debt, both measured against GNP and compared with other countries, was not large. What South Africa had was a liquidity crisis.

36. As part of the solution to the crisis, in 1985 South African authorities reintroduced a dual exchange rate. 7/ The system involves a commercial rand exchange rate for all transactions included in the current account (imports, exports and invisibles) and for foreign loans. All other capital account transactions, including foreign portfolio investments in South African equities, the repatriation of disinvestment proceeds and the movement of capital by migrants, take place through a lower, floating financial rand exchange rate. The financial rend exchange rate is thus determined by the balance of supply and demand, which acts as an incentive for foreign investments while discouraging the repatriation of foreign aasets. It also insulates the commercial exchange rate used for most

/...

Table 4. South Africa: Changes in external debt, end August 1985-end 1988

(Millions of United States dollars)

	External debt outstanding at			Changes in external debt between end August 1985 and end 1988	
	End August 1985	End 1988	End 1988		
	1	2	3	4	5
	(Valued at current exchange rates)	(Valued at current exchange rates)	(Valued at end August 1985 exchange rate)	(1-2)	(l-3)
Outside the net:					
Banking sector	1 317	517	486	-800	-831
Public sector	5 948 a/	5 600	4 386	-348	-1 561
Private sector	2 828	2 519	2 098	-309	-730
Medium- and long-term loans		3 476	3 436	3 476	3 436
Total	10 093	12 112	10 406	2 019	313
Inside the net:					
Public sector	2 692	2 815	2 377	123	-315
Banking sector	8 814	4 949	4 754	-3 865	4 060
Non-bank private sector	2 122	1 309	1 032	-813	-1 090
Total	13 628	9 073	8 163	4 555	-5 465
Grand total	23 721	21 185	18 569	-2 536	-5 152

Source: South African Reserve Bank Quarterly Bulletin, March 1990.

a/ Approximately 60 per cent of this amount is believed to consist of bearer bonds.

transactions from the pressure deriving from an upsurge of disinvestment; such pressure, born entirely by the financial rand exchange rate, is self-limiting in the sense that depreciation of the rate reaches a point where further disinvestment would no longer be attractive.

37. The level of the discount, that is the ex ante excess of supply of financial rand by those withdrawing from the South African economy over the demand for the currency by new investors and immigrants, represeats a proxy for an index of foreign business sentiment. The discount reached a peak (52 per cent) in 1986 when the financial rand was worth less than half the commercial rate, stabilized at a level of 38 per cent during the following two years, and fell to 29 per cent in 1989.

38. Unlike disinvestment, commercial loans, their servicing and repayment, all take place at the commercial rand exchange rate. They therefore are an important consideration in the overall balance of payments. Recent trends in South Africa's foreign debt and their economic policy implications are examined in the next section. Here it should be noted that the large capital outflows experienced by the country during the 19854989 period reduced the already low level of official gold and foreign reserves, forcing the central baak to costly purchases of foreign exchange through forward dealing (table 5). It is estimated that in the same period total reserves were the equivalent of between a maximum of 13 weeks and a minimum of 6 weeks of import cover.

/...

Table 5. South Africa: Capital account of the balance of payments, 1985-1989

(Millions of rands)

	1985	1986	1987	1988 First quarter	1988 Second quarter	1988 Third quarter	1988 Fourth quarter	1988 Yearly average	1989 First quarter	1989 Second quarter	1989 Third quarter	1989 Fourth quarter	1989 Yearly average
1. Net long-term capital	-445	-3 060	-1 698	-287	-715	-275	175	-1 102	-395	-728	179	-281	-1 225
2. Net short-term capital	-8 786	-3 037	-1 371	-475	-1 494	-2 259	-1 216	-5 444	-1 456	-752	-678	-1 445	-4 331
Public authorities	75	-71	8	-50	-10		1	-59	6	10	26		42
Public corporations	-157	-224	-40	27	-10	90	-72	35	40	185	-100	-28	97
Non-bank private sector	-8 704	-2 742	-1 339	-452	-1 474	-2 349	-1 145	-5 420	-1 502	-947	-604	-1 417	-4 470
3. Net capital movements (1 + 2)	-9 231	-6 097	-3 069	-762	-2 209	-2 534	-1 041	-6 546	-1 851	-1 480	-499	-1 726	-5 556
4. Current account balance	5 925	7 196	6 152	924	-267	1 408	894	2 939	1 432	312	934	1 419	4 097
5. Change in net gold and other foreign reserves (3 + 4)	-3 306	1 099	3 083	162	-2 496	-1 126	-147	-3 607	-419	-1 168	429	-307	-1 465
6. Change in liabilities related to reserves a/	2 071	-2 293	-1 167	-13	1 668	586	-316	1 925	904	1 995	206	-250	2 855

Source: South African Reserve Bank Quarterly Bulletin. March 1990.

a/ Usually short-term purchases of foreign exchange through forward sales of gold, or some other security, to buttress the reserves. A minus sign denotes a decrease in this form of debt.

/...

C. Recent trends in South Africa s foreign debt

39. South Africa is not a major international debtor and its difficulties with its international debt are different in substance from those of other debtor countries. 8/ However, since its financial crisis of August 1985, when the Government found itself compelled to institute a unilateral moratorium on the capital repayment of a substantial proportion of its international commercial debt, its debt has been subject to periodic rescheduling) moreover, South Africa has been almost completely excluded from international capital markets for any *credits* other than those associated with trade. 9/

40. South African policy since 1985 has, therefore, been directed at satisfying its international creditors in the expectation that by doing so it may, in due course, gain readmission to international financial markets, In pursuit *of* this objective the Government has:

(a) Negotiated three successive rescheduling agreements with the international banks that are the principal holders *of* South African debt "inside the net" of the moratorium;

(b) Sought to pursue domestic economic policies which could yield maximum economic growth compatible with meeting its debt obligations.

41. The three debt rescheduling agreements covered the periods: 1 April 1986 to 30 June 1987; 1 July 1987 to 30 June 1990; and 1 July 1990 to 31 December 1993.

42. The size and distribution of South Africa's external debt are set out in table 4.

43. Of the $13.6 billion caught inside the net in 1985, approximately $1.8 billion has been repaid under the terms of the first two rescheduling agreements. It is worth noting that South Africa has not missed a payment under the agreements; it has continued to repay debt that was excluded from the moratorium and it has continued to service all its debt. In the case of the rescheduled debt, interest rates have been about 1 per cent above the level contracted before the moratorium.

44. In addition, approximately $4 billion has been removed from the net by the agreement made by some holders of debt to accept an exit option under which a frozen asset is converted to a lo-year loan, Under the terms of these loans no capital is repaid for the first 5 years, but thereafter it is repaid in full in 16 equal 6-monthly instalments, It is not possible to know exactly when individual creditors decided to take this option, but it seems probable that although some repayments will fall due from 1992, the bulk of them will begin in late 1993.

45. As table 4 shows, exchange rate movements since 1985 had the effect of increasing the dollar value of the outstanding rescheduled debt by about 12.5 per cent from $8 billion to $9 billion at the end of 1988.

/...

46. Under the third rescheduling agreement, which was announced on 18 October 1989, and which came into force on 1 July 1990, South Africa is committed to repaying a further 20.5 per cent of the outstanding capital according to the schedule set out in table 6.

47. Under the agreement, creditors continue to receive the slightly higher interest rate. Terms for the exit option have been changed from those offered under the second interim agreement, however. South Africa now proposes that any creditor opting to convert debt into a lo-year loan will be paid until the end of 1993 (i.e. the end of the third interim agreement) at the same rate as for holders of froaen debt. Thereafter there will be a period of 4 years in which no capital repayments will be made, but after that the outstanding debt would be completely repaid over 30 months in 5 equal 6-monthly instalments.

48. Under the circumstances that currently prevail, approximately $6 billion will still be frozen at 31 December 1993 and require further rescheduling. As table 4 shows, rescheduled debt under the interim agreement does not cover all of South Africa's external debt obligation. There is also the debt outside the net, which is composed largely of bonds and official trade agency debt. One recent estimate of the immediate repayment schedule for this debt is included in table 7.

49. Other types of debt were excluded from the moratorium. As regards trade agency debt, the main reason for its exclusion was that the South African authorities expect to repay froaen and other debt by running a sufficiently large surplus on their current account of the balance of payments. Repudiating trade-related debt, which would have invited exclusion from further trade credit, was incompatible with this strategy. As regards bearer bonds (the majority of which are believed to be held by investors from Germany, Switzerland and the United Kingdom of Great Britain and Northern Ireland), the explanation is more complex, but undoubtedly is connected to the desire not to alienate creditors whose future support will be beneficial to the economy.

50. However, faced with the possibility of difficult rescheduling negotiations in 1989 and with a potentially difficult surge of debt falling due in 1990, South African authorities are believed to have sought the rescheduling of some of the bond debt. Information gathered through informal sources suggests that in 1989 some European banks agreed to assist South African authorities in rolling over bonds valued at approximately $140 million. The new bonds have a life of three years to 1992 and are at significantly higher interest rates. Dond holders have a six-monthly put-option (i.e. each holder can decide twice a year whether to demand immediate repayment in full). Holders of approximately half of the bonds, worth $70 million, are believed to have agreed to the conversion. Whether any of these have since exercised the put-option is not known.

51. This exercise seems to have been a testing of the waters prior to the completion of the third rescheduling agreement. Had this agreement proven more difficult to reach or had other factors made repayment of the 1990 external debt problematic, a more substantial bond conversion exercise might have been attempted. This exercise remaine a policy option for the South African authorities if they should encounter debt repayment difficulties in the immediate future.

/...

Table 6. South Africa: Estimates of capital repayments under the third rescheduling agreement with creditors, October 1989

Payment date		Principal repayment (percentage)	Millions of United States dollars
1990	December	1.5	120
1991	February	2.5	197
	August	3.0	230
1992	February	3.0	224
	August	3.0	217
1993	February	3.0	210
	August	3.0	234
	December	1.5	99
	Total	20.5	1 502

Source: United States General Accounting Office, "South Africa: Debt Rescheduling and Potential for Financial Sanctions, Briefing Report to Congressional Requesters", Washington, D.C., February 1990, (GAO/NSIAD-90-109BR), p. 5.

Table 7. South Africa: Estimates of total debt repayments, 1990-1993

(Millions of United States dollars)

Type of payment	1990	1991	1992	1993
Principal of frozen debt	240 a/	427	441	513
Principal of other debt	1 400	700	700	600
Total	1 640	1 127	1 141	1 113

Source: United States General Accounting Office, "South Africa: Debt Rescheduling and Potential for Financial Sanctions, Briefing Report to Congressional Requesters", Washington, D.C., February 1990, (GAO/NSIAD-90-109BR), p. 5.

a/ Includes final payments due under the second interim agreement, 15 June 1990.

52. The policy objective of the South African authorities in the debt rescheduling negotiations, conversion of bond debt, repayment of trade-related credits and proposals on debt conversion to lo-year terms is to produce a situation of stability in which the country's debt obligations are (a) clearly known by the authorities for some years ahead; and (b) in so far as possible, smooth from one year to the next. As table 7 indicates, these objectives have been more or less achieved. Furthermore, any frozen debt that is converted to lo-year loans from now on will, because of the way principal repayments are spaced, contribute to smooth further debt repayment obligations into the late 1990s. Whether the achievement of this objective has lessened the pressure on the Government for reform, which observers agree was being exerted by South Africa's debt problem, is a matter taken up in chapter V.

IV. SOUTH AFRICA'S ACCESS TO TRADE CREDITS AND RESTRICTIVE MEASURES

A. The role of trade credits and loan insurance in the financing of international trade

53. International trade in the modern world developed on the basis of a system of credit finance and insurance. These servicer helped to minimise risk in the context of uncertainty and to smooth financial transactions associated with trade. Although their importance in the contemporary world varies, partly according to the level of development of a trading country's economy, and partly according to other factors such as its socio-political stability, the need for trade credit finance and related insurance remains strong.

54. Trade credit finance and insurance may be provided by any financial agency that chooses to offer them. In practice, however, the great bulk of the business conducted in the provision of these services is provided by Governments and by commercial banks. Much of the business provided by the private sector (both bank and non-bank) is also underwritten by official government-owned or sponsored trade agencies.

55. There are two principal kinds of trade credit, buyer credits and supplier credits. The credits are made available for periods of from between 30 and 160 days for primary and manufactured goods (known as short-term credits)) 1 to 5 years for agricultural and industrial equipment (medium-term); and 5 to 10 years for capital goods such as power station generating equipment, jet airlines and so on (long-term). Short-term credits are generally made available through an instrument known as a letter of credit, which can be drawn on at a correspondent bank Long-term trade credits often involve more complicated contracts and, because of the large sums involved, as well as other considerations such as the transfer of technology and the importance of the product to the economy of tho supplying country, direct participation by Governments. There is a considerable secondary market in trade finance instruments, which may be purchased (*à forfait*) at a discount if a holder decides to sell.

56. Long-term trade credits are easily documented while short-term trade credits are not. With the increasing speed and efficiency of modern trade many

transactions are rapidly completed and although banks keep detailed records of their activities for all the usual regulatory and legal purposes, the sheer volume of the transactions in international trade makes detailed reporting and documentation at a national or international level extremely difficult.

57. Most of the credit made available to traders with established reputations and strong credit ratings is in the form of revolving credits, where the business is rather more like a stock of debt or simply a credit line on which the customer is entitled to draw, than it is like the traditional form of trade credit finance. This characteristic, which is increasingly true in the developed economies, reflects in some degree a relative decline in importance of trade credit finance as a method for conducting international trade. The main factors contributing to this decline are the emergence of financially secure international corporations and trading companies that are capable of financing their own trading operations; the accumulation of experience and information about the credit worthiness and reliability of traders, which has led to more open-account trading) the general international thrust towards more liberal trade (the lowering or elimination of tariff barriers, faster communication, faster delivery and so on); a general sense in the developed economies that official export credit agencies were really providing domestic industries with disguised subsidies and that this practice (as a part of more liberal trading practices) ought not to be encouraged; and the impact of the world debt crisis, in which a number of official agencies may be compelled to accept considerable losses.

58. These factors have led to a greater interest in the activities of official export credit agencies by intergovernmental organisations. Specifically, member Governments of the Organisation for Economic Co-operation an4 Development (OECD), anxious to avoid the possibility that such agencies were subsidising trade by charging artificially low interest rates for trade credit loans, now require OECD to publish minimal interest rate schedules, which official export credit agencies are required to adhere to. The schedules are different for each of three categories: trade with relatively poor countries, trade with intermediate countries (which category includes South Africa) and trade with developed countries,

59. This classification emphasizes a difference in the trading positions occupied by developed, developing and least developed economies, and that occupied by corporations that trade with them. Whereas established corporations trading within developed economies may have no need of traditional forms of trade credit finance and certainly no underlyiog need to be dependent on official export credit agencies for insurance cover, it is virtually impossible for corporations trading with least developed and other economies to secure any business at all without trade credit arrangements and the support of being "on cover", that is, guaranteed, at an official export credit agency.

B. The provision of trade credits and trade credit insurance to South Africa

60. As a developing economy, South Africa would normally expect to be dependent on trade credit finance for much of its international trade. This is especially true of its imports, approximately 40 per cent of which are capital goods. Moreover,

/...

since trade credits are generally raised in one or other of the participating trading countries and since reasonably accurate (though incomplete) statistics on the aggregates of South Africa's direction of trade are available, it is possible to make educated estimates of both the origins and the quantities of the loans.

61. Direction of trade statistics for various countries and regions of the world that trade with South Africa are set out in table 8.

62. The size of South Africa's trade credit debt can only be estimated. One expert study put outstanding trade credits at the end of 1986 at $US 6.9 billion. 10/ The total fluctuates, however, because traders seek credits on both domestic and international financial markets in response to various factors that include interest and exchange rate movements. A substantial portion of the sharp increase in capital outflow from South Africa in 1988 (R 6.5 billion, more than twice the figure for 1987 (see table 5) appears to have been in response to a change in South African economic policy leading to a sharp reduction in demand for trade credits for imports (see table 10).

63. Although it is not possible to know the full amount of South African trade credit debt, some statistics on export credit agency loans are available. At end September 1.989, the Berne Union reported the following information for South Africa's main trading partners: 11/

(a) The export-import bank Hermes (Germany) has the largest total commitments outstanding to South Africa, namely, short-term $US 2G1.3 million and medium- and long-term $US 2.73 billion;

(b) The United Kingdom's Export Credit guarantee Department has short-term credit commitments for exports to South Africa of $US 197.7 million and medium- and long-term commitmsntn of $US 2 billion)

(c) France's export credit agency, the Compagnie Française d'Assurance du Commerce Extérieur has $US 1.2 billion in medium- and long-term commitments and $US 178.8 million in short-term commitments;

(d) Japan's Ministry of International Trade and Industry has short-term commitments of $US 69.1 million for exports to South Africa and medium- and long-term credit commitments of $US 251.9 million. It appears that the Government of Japan limits credits to South Africa owing to certain political sensitivities. It is thus possible that the bulk of credit to support Japanese trade with South Africa is provided from internal sources by the Japanese trading companies themselves,

64. South Africa's access to international financial markets is largely confined to short- and some medium-term trade-related credits from official trade financing agencies. There is very little incentive, currently, for the private sector to contribute much in this area of business. The reasons for this situation are set out in section E below. Furthermore, most of the countries that permit their official export credit agencies either to make or to guarantee credits for trade with South Africa impose restrictions of various kinds. These are set out in some detail in sections C and D.

/...

Table 8. South Africa: Foreign trade and main trading partners. 1980-1988

(Millions of United States dollars)

	Exports						Imports					
	1980	1982	1984	1986 a/	1987	19%	1980	1982	1984	1986 a/	1987	1988
Total	25 684	17 647	17 377	19 718	21 603	25 847	18 327	17 026	14 963	11 417	14 126	17 333
United States	2 126	1 220	1 458	1 965	1 272	1 445	2 527	2 484	2 375	1 229	1 281	1 691
Japan	1 551	1 533	1 335	1626	2 214	1 777	1 669	1 711	1 934	1 270	1882	2 047
European Community	4 916	3 820	3 264	4 908	5 213	6 720	6 595	6 497	5882	4 657	5 799	7 301
France	524	415	385	343	530	638	703	708	568	412	467	575
Germany	1 029	785	676	1 059	1 135	1 570	2399	2 503	2 339	1 951	2 548	3 332
United Kingdom	1 779	1 300	742	1 0S6	976	1304	2 242	2 029	1669	1 279	1 556	1 911
Switzerland	1 597	947	1 171	324	244	473	308	2 %	265	258	272	320
Asia	680	665	803	1 094	1304	1 900	460	657	763	604	1 009	1 356
Taiwan, Province of China	b/	172	137	2 %	437	827	b/	220	269	216	435	626
Africa	1 412	834	616	808	970	1 164	371	305	284	243	291	349
Western hemisphere	370	234	114	147	175	199	166	193	310	148	175	274
Brazil	171	77	35	55	65	79	100	112	139	49	90	178

Source. IMF. Direction of Trade Statistics Yearbook. 1986 and 1989. The figures are for the South African Common Customs Area, which includes Botswana, Lesotho. Namibia, South Africa and Swaziland.

a/ South Africa stopped reporting its direction of trade statistics to IHF in 1986. From that year onwards the figures are estimates based primarily on other countries' reports of their own trade with South Africa. A detailed description of how the estimates are derived can be found in the introduction to the IMF Direction of Trade Statistics Yearbook.

b/ Not available.

Table 9. South Africa: External bank claims, December 1985-June 1989 (unadjusted for exchange rate movements)

(Milliona of United States dollars)

	December 1985	June 1986	June 1987	December 1987	June 1988	December 1988	June 1989
External bank claims:							
1. Total	17 459	16 725	16 244	16 767	16 052	15 073	14 712
2. Guaranteed	1 996	1 787	1 803	2 224	1 787	1 897	1 373
3. Non-bank trade	1 076	1 113	1 273	1 632	1 475	1 933	1 823
4. Total (1+3)	18 535	17 838	17 517	18 399	17 527	17 006	16 535

Source: OECD and BIS, statistics on *external* indebtedness: bank and trade-related non-bank external claims on individual borrowing countries and territories, new series.. The figures are reported by central banks and official export credit agencies in member countries. The following points should be noted: in some countries, banks whose total external assets and liability are each below a certain minimum cut-off *point* are aot required to report; in some countries, not all of the reporting institutions* external assets are included in the data; and the standard OECD reporting norms may be departed from in two ways: (a) the short-term suppliers' credits data may be incomplete, and (b) data on the timing of shipments, and drawing of export credit lines, may not be available either promptly enough or in sufficient detail for inclusion in the published statistics.

Notes

1. Row 1: These figures are for stocks of debt held by baaks, the majority *of* which is either not trade-related *or*, (surely a very small proportion) though related to trade, is not guaranteed by official export agencies. It therefore includes the debt subject to periodic rescheduling.

2. Row 2: These figures are those parts of all external bank claims which consist of guaranteed financial trade credits (buyers' credits), which are loans extended by banks to importers abroad (i.e. by, say, a British bank to enable a South African importer to import British products). The guarantees are provrded by government agencies in the country of the bank.

3. Row 3: These are guaranteed suppliers* credits, which are credits extended by exporters to importers abroad (i.e. by, say, a company from Germany to a client in South Africa). These are further stocks of debt in addition to external bank claims.

/...

Table 10. Changes in external bank and trade-related non-bank claims, June 1986-June 1989 (adjusted for exchange rate movements)

(Millions of United States dollars)

	June-December 1986	December 1986-June 1987	June-December 1987	December 1987-June 1988	June-December 1988	December 1988-June 1989
External bank claims:						
1. Total	-897	-97	-216	-204	-1 131	-11
2. Guaranteed	-6	-146	239	193	-113	-100
3. Non-bank trrde	165	-149	120	327	104	96
4, Total (1+3)	-732	-246	-96	123	-1 027	85

Source: See table 9.

Notes

1. These figures show half-yearly changes in external stocks of South African trade debt. They have been adjusted for exchange rate movements, which make the reduction in external debt less marked.

2. The increase in guaranteed (i.e. trade-related) and non-bank trade debt after June 1987 is an indicator of quite rapid domestic growth in the South African economy in the second half of 1987 and the first quarter of 1988. This development created such a deterioration in the balance of payments on the current account (imports rose by 22.5 per cent in 1988) that the authorities intervened to impose a range of measures, including import surcharges, a new surcharge on fuel oil, a tighter monetary policy and a reduction of the budget deficit. As a result, GDP growth declined sharply. Falling imports meant a reduced demand for trade credits.

65. None the less, statistics collected by OECD and BIS, indicate that South African entities have been successful in attracting limited amounts of new medium- and long-term credit in the period from 1985 to 1989 (see tables 9 and 10).

66. These credits, applied to the purchase of capital equipment, constitute a partial substitute for alternative capital loans. 12/ Since it is practically certain that these loans have not been made available by any institution that has funds caught in the net of the unilateral moratorium of 1985, the probability is that they come either from capital markets outside Europe and North America or from official trade agencies.

67. The question has arisen of whether South Africa's access to trade credits provides relief to the South African authorities in their efforts to meet the international debt obligations incurred under successive rescheduling agreements since 2 September 1985. Stated another way, do trade credits constitute "new money" that can, even partially, substitute for capital inflows of other kinds? An assessment of this question is set out in chapter V.

C. South Africa's main trading partners: access and restrictions

68. As reported in section B, in 1988, the most recent year for which statistics are reasonably complete, the United States of America, the countries of the European Community, and Japan accounted for approximately 55 per cent of South Africa's non-gold exports and for fully 61 per cent of its imports. In addition, Switaerland, the United Kingdom of Great Britain and Northern Ireland and Italy, by together taking approximately 90 per cent of South Africa's gold production, accounted for another 30 per cent of total South African export earnings. 13/

69. It is widely believed that most, if not all, of South Africa's non-gold trade would be seriously disrupted if trade credits and insurance were not available to finance it. 14/ For this reason, opponents of apartheid have recently focused on the availability of trade credit finance with a view to having it reduced, if not eliminated.

70. Since the South African financial crisis of 1985, and in some cases well before it, all of South Africa's major trading partners have placed some restrictions on capital movements into South Africa. In some cases, these restrictions include trade credit finance, The various arrangements that concern trade credits may be summarized as follows.

United States of America

71. The Comprehensive Anti-Apartheid Act of 1986 prohibits new lending by United States financial institutions and citizens to South Africa, but both loans to firms owned by black South Africans and short-term trade credits (defined as for a duration of less than one year) are exempt from this prohibition.

/...

72. The United States public sector trade credit agency, the Export-Import (EXIM) Bank, is prohibited from financing United States exports to the Government of South Africa or its agencies, and may only provide short-term trade finance for South African imports of United States products to South African companies that are either majority-owned by blacks and non-whites or adhere to specified equal-opportunity principles. 15/ In addition, EXIM Bank has placed South Africa off cover for trade, meaning that United States exporters must either insure their credit arrangements in the private sector or assume the risk themselves by advancing credit without insurance cover.

European Community

73. The 12 member States of the European Community introduced a voluntary ban on new medium- and long-term investment in South Africa in 1986 and, with the exception of the United Kingdom, agreed et their summit meeting at Dublin on 22 June 1990 to continue this arrangement for a further six months. However, this prohibition never applied to short- or medium-term trade credit finance. The Government of South Africa excluded official trade agency debt from the unilateral moratorium on debt repayment that it introduced on 2 September 1985. Since then it has continued to service and to repay all of its obligations in this field. Among the European Community members, by far the largest holders of South African trade credit debt are the official agencies of Germany, the United Kingdom and France.

74. Germany has four export credit agencies, two of which provide guarantees and two the actual credits. One of each is in the public sector. At end September 1989, Hermes, the official guarantee agency, was the world's largest holder of official export credit agency South African trade debt paper, though it has a limit of DM 50 million on each individual transection and agrees to cover sums in excess of DM 20 million only "in exceptional cases". Guarantees may also be provided by the private sector agency, the Treuarbeit. Credits for trade are provided by both the public sector agency, the Kreditanstalt für Wiederaufbau, which is a development bank, and by the AKA-Ausfuhrkredit, which is an organisation jointly owned by banks in Germany. South African trade is supported by all of these agencies, with both credits and insurance cover being available, case by case, for up to five years. It is reported that in 1987 the South African Post and Telecommunications Administration was granted loans of DM 32.8 million by the Kreditanstalt für Wiederaufbau. 16/

75. At end September 1989, the United Kingdom Export Credit Guarantee Department reportedly had outstanding short-term credit commitments for exports to South Africa of $US 197.7 million, and medium- and long-term commitments of $US 2 billion. 17/ The Department has short-term credits open, without restriction. Medium- and long-term credits are also open, but with a limit of £10 million on any individual transaction and subject to a total unspecified commitment ceiling.

76. Credits and guarantees through the official agency, the Compagnie Française d'Assurance du Commerce Extérieur, are open case by case, but without limits. At end September 1989, the stock of debt of South Africa held by the Campagnie was: short-term $US 178.8 million and long-term $US 1.2 billion.

/...

Japan

77. In Japan, one official trade credit agency, the Japanese Ministry of International Trade and Industry, provides guarantees, while another, the Export-Import Bank, provides both credits and guarantees, Both treat applications for rupport of trade with South Africa in the same way as the French agency does: open, case by case, with no publicly stated limit. In the Ministry of International Trade and Industry, the stocks of guaranteed debt were, however, rather lower than those for the European countries referred to above: $US 69.1 million in short-term credits; and $US 251.9 million in medium- and long-term credits at end September 1989. The principal reason for this lower exposure is generally given as Japan's sensitivity to criticisms regarding its trade with South Africa. 18/ However, figures for the Export-Import Bank were not available and the probability is, as Ovenden and Cole point out, that "the volume of insured credits outstanding in Japan in substantial*@. 19/ Japan's trade with South Africa amounted to $US 2,047 millioa in exports and $US 1,955 million in imports in 1988, and it is reasonable to assume that a substantial proportion of this trade was transacted on the basis of credit in the normal way. 20/ It is also likely that, as in the United States, the private non-bank sector takes a rather bigger role in eupplying trade credit than is generally the case in European countries. There matters are discussed in section E.

D. Other trading partners: access and restrictions

76. In Europe, outside the European Community by far the moat important trading partner of South Africa is Switzerland. However, Switzerland's trade with South Africa consists almost exclusively of gold and diamonds, and the provision of banking facilities. Compared with these activities, trade in other commodities is insignificant. However, the official export credit agency, the Export Rieiko Garantie, provides short-term trade credit cover without restriction and medium- and long-term cover on a case-by-case basis. In September 1989 the outstanding debt held by the agency reportedly amounted to $US 38.9 million in short-term instruments and $US 257.1 million in medium- and long-term credit.

79. Elsewhere in Europe outside the European Community, restrictions on trade with South Africa mean that trade credit business is virtually non-existent. Finland, Iceland, Norway and Sweden (with Denmark, which also belongs to the European Community) all adhere to the Nordic Programme of Action against Apartheid, promulgated in 1985, which prohibits almost all trade with South Africa. Each of the Nordic countries has also enacted legislation making loans to South African entities illegal. With almost no trade existing between these countries and South Africa, there would be no demand for trade credits and each of these countries is believed to have official export credit exposure to South Africa of lees than $US 5 million.

80. Austria has South Africa on cover for trade credit, but limits transactions to a ceiling of $US 4.3 million and a maximum term of 24 months. The Österreichische Kontrollbenk, Austria's official trade credit agency, had less than $US 30 million of outstanding credits of all kinds at end September 1989.

81. Outside Europe, Australia, Canada and New Zealand all have South Africa off cover for trade aredit and discourage trading links in other ways. They also urge their private sector banking institutions not to make trade credit available for periods longer than 90 days (see chap. II). The official export aredit agencies in Australia and New Zealand eaah hold less than $US 5 million in South African trade aredit debt and Canada's Export Development Corporation is believed to have none at all.

82. In Asia, official export credit from Bong Kong is believed to be less than $US 5 million, but similar restraint is not thought to be true of Taiwan, Province of China. Although figures are not available, one recent source quotes officials as stating that "the Export-Import Bank of Taiwan, Province of China, has financial programmes for suppliers and buyers of exports to South Africa just as it does for those of other countries". 21/ Since, in 1980 alone, Taiwan, Province of China, is believed to have imported goods from South Africa worth $US 827 million and exported $US 626 million in return, the outstanding trade credit debt is likely to be considerable. 22/ In Asia, Taiwan, Province of China, is South Africa's second most important trading partner after Japan. A recent study and contemporary reports refer to joint venture investment projects from Taiwan, Province of China, in South Africa. 23/ Though figures for recent years are not available, some increase in trade between South Afriaa and the Republic of Korea is suggested in international trade statistics for the years 1982 and 1984.

83, Among the other industrialising end trading countries of Asia, Singapore reports no trading ties with South Africa. India, Malaysia and Thailand specifically prohibit trade with South Africa.

84. South Africa's economic relationship with the other States of southern Africa has been defined by one recent expert study as "asymmetric interdependence", 24/ The overall balance-of-payments benefit of this relationship to the South African economy is estimated to have been between $US 1.25 and $1.6 billion per annum for the years of the mid-19808, the great bulk of this amount coming from a surplus on visibls trade. 25/ This figure represents approximately 40 per cent of South Africa's surplus on its current account balance. Most of this trade will have been financed by credits from within South Africa.

E. The private sector

85. Economic sanctions to restrict the flow of goods and commodities may be imposed by Governments and international organiastions, but are frequently circumvented by private sector firms eager to maintain or to develop profitable trade.

86. The case of the banking sector merits particular attention. In the wake of South Africa's moratorium on the commercial portion of its international debt in 1985, most international financial markets were closed to South Africa. For several months after the announcement on 2 September 1985 the exclusion included credits for trade purposes. However, because South Africa did not renounce repayment of its debt to official trade agencies and because, as it has been shown,

/...

most of these agencies have kept South Africa on cover, private sector financial institutions were in principle able to return to short- and medium-term trade credit financing. In practice, however, it appears that very little of this business is being done through South Africa's main traditional markets.

87. In the United States the General Accounting Office found that United States banks were "reluctant" to provide credits for trade with South Africa. 26/ The Office's report quotes a survey by the United States Treasury's Office of Foreign Assets Control and other evidence in support of this finding, which is attributed mainly to the lack of Export-Import Bank guaranteeat perceived socio-economic risks in South Africa; the increase of United States state and local laws directing investment away from firms doing business with South Africa; increased public awareness of the issue of apartheid; and bankers' sensitivity to debt problems in the context of the world debt crisis.

88. In the European Community the situation is somewhat different. In those countries which undertake most of South Africa's trade with Europe, the private sector is under little pressure from clients to offer trade credit because official export credit agencies are still open to South African business. The private sector is reasonably satisfied with this situation because it can thereby avoid the pressure that their United States counterparts experience from an increasingly aware and srticulats public opinion. They can also avoid the pressure from their clients that would flow from the fact that, in large measure, they share United States bankers' pessimistic views about the current climate for businsss in South Africa, A private survey of major European banking institutions by representatives of one intergovernmental orgsniaation found in late 1989 that very little trade credit business was being carried out by the private sector in any of the main European capital markets. It is likely that some new business is being done in the countries of the European Community, but the probability is that it is small in scale) that it is being undertaken in secondary markets by banks with little or no exposure to the 1985 moratorium; and that it is largely to service domestic exporters.

89. Outside of the United States and Western Europe the situation is less clear, It seems reasonable to assume that substantial trade credit business is being undertaken by banks in Taiwan, Province of China, because the volumes of trade between that country and South Africa have grown rather substantially in the 19808. It has also been reported that Hong Kong banks both provide credit for trade through the crown colony and are active in providing trade finance for business between South-East Asian and South African firms that never itself passes through Hong Kong. 27/ The Japanese authorities are generally believed to restrict the banking sector's contributions to trade finance with South Africa, but the size and competitive ability of the major Japanese corporations end trading companies permit the provision of trade credits from non-bank sources. 28/

90. In sum, however, the quantities of new trade credit being extended to South Africa are probably small. The United States General Accounting Office, relying on data from OECD and BIS, has recently calculated that the total flow of new guaranteed trade-related credits, including government-guaranteed bank credits, from June 1986 up to and including June 1989, was $US 1.066 billion. 29/ The

/...

United Nations has likewise found that, though there has been some increase in leading, with a preference being shown by international banks to lend in United States dollars rather then in their own currencies, the total amounts are small. 30/ The overall stocks of trade debt, though they have increased little, none the less permit South Africa to trade successfully enough to sustain a current account balance-of-payments surplus that permits it to repay debt both outside the moratorium and under the rescheduling agreements. Some reasons for this situation are set out in chapter V.

V. THE EFFECTIVENESS OF THE MEASURES ADOPTED

91. South Africa's ability to engage in international trade has not been seriously inhibited by trade credit restrictions. Four main reasons account for this.

92. Firstly, South Africa's main trading partners in Europe end Japan have continued to keep South Africa on cover at their official trade credit agencies and have kept open the possibility of providing short- and medium-term loans for South African trade and with few restrictions,

93. Secondly, in those developed countries where trade credit restrictions have been imposed (the Nordic countries, Australia, Canada, and New Zealand) the level of trade was rather low, and though there must have been some trading opportunities forgone as a result of the credit impediments, these have not been important enough to affect South Africa's overall trading position.

94. Thirdly, where trade credit restrictions have been applied and the level of trade is significant, trade has been facilitated by other means. For instance, in the United States, in spite of trade credit restrictions, trade has been facilitated by the provision of some small trade credit business that is reportedly granted by at least one bank; by the availability of trade credit facilities elsewhere in the world; and by the ability of the subsidiaries of the United States companies to take advantage of these facilities and the anonymity of international financial marksts. 31/ In addition, firms may choose to trade with established South African companies on an open account basis. The opportunity cost to the supplier can be covered by a higher price for the goods being supplied; but this higher price may still be lower than the combined price of the purchase plus trade credit finance would have been, because intermediate service fees have been eliminated.

95. Fourthly, the structure of the South African economy is such as to make it relatively impervious to trade credit restrictions. The export sector is highly corporatiasd, with a small number of firms operating in an oligopolistic way. As a result of disinvestment by transnational corporations, some of these firms have acquired financial institutions with well-developed correspondent banking connections abroad. They are in a position to supply trade credit finance to their principals and to other domestic clients. Furthermore, many South African firms are the subsidiaries of international corporations or have recently been disinvssted in a way that retains their international access to trading agreements and so are in a position to have access to trade credit facilities. South African

firms are themselves increasingly able to go off-shore for trade credit finance. The main developing markets for other manufactured produats are the countries of southern Africa and the industrializing countries of Asia. In all of these areas of the economy, the state, domestic financial institutions end the trading corporations and banks of the emerging economies of Asia are all in a position to ensure the availability of export credit finance.

96. As far as imports are concerned, South Africa's main trade is in capital and intermediate goods. As long as trade in these items is not banned by international measures, and as long as suppliers remain confident of being paid, trade credit will continue to be made available, either by official export credit agencies, or through open account trading, or on international financial markets. And, as suggested in a recent study, even if sanctions on the trade sector were to be tightened and more rigorously enforced, South Africa's "access to short-term trade credits will probably improve, since financial sanctions-busting activities is likely to be a profitable business". 32/

97. In assessing the impact of restrictions on the availability of loans and trade credits, it is useful to review a number of studies made in this regard and, more generally, on the impact of economic sanctions. Recent analyses of the effects of international sanctions on the economy of South Africa have pointed out the following: 33/

(a) The first impact of sanctions is on prices: they tend to result in a price increase for imports and a price decline for exports. It has been estimated that the cost of sanctions to South Africa amounts to "several billion dollars annually". 34/ This cost places pressure on the external balance of the current account end incresses the rate of inflation;

(b) A second impact is a tendency to distort the domestic alloaation of resources. In the energy sector, for instance, costly and inefficient capital-intensive investments can reduce productivity growth and are likely to be a drain on the economy for years to come. 35/ It should be strsssed though that in South Africa much of this distortion is produced by apartheid itself, irrespective of sanctions, and is most evident in labour market prices, capital markets, transport and communications infrastructure, and training and education;

(c) A third major impact is on economic opportunity forgone. It is estimated that "real South African GDP would be 20 to 35 per cent higher today than it actually is had South Africa not maintained apartheid end pursued a semi-autarkic strategy. This loss is the cost of continuing an apartheid system and taking measures to build a less dependent economy'*. 36/ Other studies differ very little in estimating that South African GNP was 45 per cent smaller in 1987 than it would have been had the economy been able to sustain the growth rates that it achieved between 1945 and 1975 through the years from 1975 to 1987. 37/

98. In this context, an international embargo on trade credits for trade with South Africa, though it would not have the effect of preventing trade, would, nevertheless, add to the economic difficulties already evident in the South African economy. It would do so in the following ways:

/...

(a) The relative saaraity of trade credit finance would make it more expensive, leading to higher (and thus less competitive) export priaes. To counter this problem, exporters would, at least in the short term, reduce prices by autting profits, This mechanism jeopardizes future investment from retained earnings, which in the post-war period has been the main source of direct investment in the South African economy;

(b) With the relative scarcity of trade credit finance, far *more* trade would be conducted on a cash or open aaaount basis. South African authorities would thus have to build up their reserves of foreign exchange in order to meet the demands of cash transactions. To do so, they would need to increase the size of the trade surplus, thereby limiting imports further)

(a) Limiting imports even further will generate greater inflation (higher prices through scarcity)) lead to a shortage of capital end intermediate goods that are sssential to increasing production, all of which will, in turn, lead to lower rates of growth and higher unemployment;

(d) Further limitations on imports will also stimulate the expansion of import substitution industries (whether the authorities encourage them or not), which may result in further misallocation of scarce investment funds, greeter distortion in the allocation of resources generally and thus even lower productivity growth in the medium term.

99. The question has arisen of whether the rescheduling agreements entered into with the South African authorities by international banks have reduced the pressure on the Government of South Africa to *embark* upon a process of meaningful political *reform* (see sect. C of chapter III).

100. Opinions vary on this issue. In achieving their objectives of (a) knowing the scale end duration *of* their debt obligations in the medium term, and (b) smoothing the repayments that are due, year on year, the South African authorities have attempted to bring a measure of stability to the policy-making environment of both the balance of payments end debt management. Certainly the elimination of "bulges" of debt repayment reduces the possibility of one kind of foreign exchange crisis,

101. It is not clear, *however,* that these developments add up to a reduction in the level of pressure being exerted on South Africa by its external account difficulties. One expert study takes the view that the pressure of debt repayment in the absence of new capital inflows is constant and cumulative, becoming progressively more onerous year by year. 38/ According to this view, the rescheduling agreements have had the effect of sustaining pressure on the South African euthorities to pursue political *reform.* The progress of political dialogue in South Africa over the past months and the Government's declared commitment to a negotiated end to apartheid appear to confirm this analysis.

102. If the effectiveness of this pressure is derived from the fact that South Africa must repay foreign debt in the absence of any significant inflows of capital, can new trade credit finance be employed as a substitute for more conventional lending, thereby reducing the financial pressure for reform?

/...

103. The answer to this question has to be assessed in the light of the following: 39/

(a) The quantities of new money involved are too small to be very significant. The United States General Accounting Office assessmsnt (see sect. E of chapter IV and tables 9 and 10) is that between June 1986 and June 1989 the volume of trade credits available to South Africa increased by $US 1.066 billion;

(b) It is not known what proportion of the new trade credit debt is in short-, medium- or long-term instruments. The Government's preference would certainly be for longer-term instruments, while private sector lenders in the international financial markets would favour ehort-term ones. Given that the South African foreign exchange crisis of 1985 occurred because of the high volume of short-term debt felling due, it is reasonable to assume that the South African authorities will seek to avoid a repetition of these circumstances. The result is a stand-off. The government would actively like to expand its stock of trade credit debt, but not by encouraging excessive growth in short-term instruments;

(c) Trade credits are made available for trade purposes and cannot be used as a substitute for other capital requirements. South Africa already had a stock of revolving trade credits adequate for its level of international trade when *the* financial crisis occurred in 1985. Some growth in exports since then justifies limited growth in trade credit finance, but over the same period economic imperatives have led to a curtailment of imports, South Africa may be at the limit of what it can accomplish with trade credits for capital account balance purposes.

104. Though trade credits cannot serve as a satisfactory substitute for other (and much greater) capital inflows, they can provide some assistance to the authorities in the management of the external account in a situation where reserves are thin. Increased inflows of trade credit finance at times when substantial debt and other payments are due in foreign currency can be balanced by repayment at times when export receipts are maximised end there is a surplus over imports. The relief accorded by trade credit finance in these situations does not seem to be substantial, however, and does little to alter the general external account problem, which is basically structural in nature,

Notes

1/ The panel of eminent persons convened for the second hearings was constituted by Canaan Banana (Chairman), Judith Hart (Co-Chairman), Kamal Hossain (Rapporteur), Abdlatif Al-Hamad, Francis Blanchard, Anatoly Gromyko, Flora MacDonald, Mochtar Kusuma-Atmadja, Edward Seaga, Wole Soyinka and Lowell Weicker.

2/ Transnational Corporations in South Africa, Second United Nations Public Hearings, 1989. Report of the Panel of Eminent Persons, Background Documentation, 1989, Vol. 1, United Nations (New York), 1990. During the second public hearings on Transnstional Corporations in South Africa held in 1989, the United Nations Centre on Transnational Corporations published information on Couth Africa's creditors on a country-by-country basis and E/C.10/1990/L.4.

/...

<u>Notes</u> (continued)

<u>3</u>/ ILO Programme of Action against <u>Apartheid</u> 1988, recommendation 4, paragraph II (2), in <u>Special Report of the Director-General on the application of the Declaration concerning Action against Apartheid in South Africa and Namibia</u>, ILO, Geneva, 1989, pp. 143 and 144.

<u>4</u>/ Stephen R. Lewis Jr., <u>The Economics of Apartheid</u>, Council on Foreign Relations, New York, 1990, pp. 62-72, and appendix table F, p. 178.

<u>5</u>/ <u>Ibid</u>., p. 66.

<u>6</u>/ The fact that the growth performance of the South African economy from 1950 to 1978 war achieved with little in the way of new foreign direct investment does not mean that foreign direct investment may not be required for renewed growth in the future. On the contrary, South Africa has experienced a continuous decline in the productivity of investment since the late 19508, and there is widespread agreement in South Africa on the need for (although not the form of) structural reform of the economy. See for example Lewis, <u>op. cit</u>., pp. 127-134; Stephen Gelb, "Economic Crisis and Growth Models for the Future", Economic Trends Group, mimeo, Durban, 1990) Ronald W. Bethlehem, "The Need for Change in the South African Economy", South African Chamber of Business, mimeo, Johannesburg, 1990.

<u>7</u>/ A dual exchange rate had first been introduced after the events at Sharpeville in 1960 and it remained in force until 1983, when it was abolished as part Of the then Government's attempts at liberal reform Of the economy. From 1983 to it8 re-introduction in 1985, and certainly until the depreciation of late 1984, the absence of a dual rate provided a brief opportunity for transnational corporation8 to disinvest without incurring serious losses.

<u>8</u>/ See Keith Ovenden and Tony Cole, <u>Apartheid and International Finance: Programme for Change</u>, Penguin, Melbourne and London, 1989, pp. 75-82.

<u>9</u>/ Lawrence Harris, "South Africa's External Debt Crisis", <u>Third World Quarterly</u>, July 1986, and Ovenden and Cole, <u>op. cit</u>., pp. 75-107.

<u>10</u>/ John E. Lind and David J. Koistinen, <u>Financing South Africa's Foreign Trade</u>, Cannicor Research, San Francisco, March 1988, p. 17.

<u>11</u>/ United states General Accounting Office, <u>South Africa: Relationship with Western Financial Institutions</u>, Washington, D.C., June 1990 (GAO/NSIAD-90-189), pp. 17 and 18.

<u>12</u>/ <u>Ibid</u>., pp. 15 and 16.

<u>13</u>/ The estimate for gold is from <u>Transnational Corporations in South Africa ...</u>, <u>op. cit.</u>, p. 112, and Ovenden end Cole, <u>op.</u> cit., pp. 163-183.

/...

Notes (continued)

14/ Transnational Corporations in South Africa ..., pa. cit., p. 71; Lind and Koistinen, op. cit.; Alan Hirsch, **Sanctions, Loans, and the South African Economy", in Mark Orkin, ed., Sanctions against Apartheid, Community Agency for Social Enquiry, 1990, pp. 282 and 283; Carolyn Jenkins, "Trade Finance and South Africa'8 Foreign Debt: Another Pressure Point?", mimeo, University of Natal, 1989, and United Stat88 General Accounting Office, op. cit.

15/ Defined a8 non-segregation of races in all work facilities; equal and fair employment practices; equal pay for equal work; training programmes to prepare non-whit8 employees for supervisory, administrative, clerical and technical jobs; an increase in the number of non-whit88 in management and supervisory positions; willingness to engage in collective bargaining with labour unions; and improvement in the quality of life for employees in such areas a8 housing, transportation, schooling, recreation and health facilities. See United Stat88 General Accounting Office, op. cit., p. 16.

16/ Transnational Corporations in South Africa ..., op. Cit., p. 71.

17/ United Stat88 General Accounting Office, op. cit., p. 18.

18/ Ibid.

19/ Ovenden and Cole, op. Cit., p. 143.

20/ IMF, Direction of Trade Statistics Yearbook 1989, p. 240.

21/ United State8 General Accounting Office, op. cit., p. 19.

22/ IMF, pa. cit., p. 356. See also table 8.

23/ Ovenden and Cole, op. cit., p. 146, and New York Time& 6 July 1950.

24/ Lewis, QD. Cit., p. 90.

25/ Ibid., pp. 80-90. The figures shown in table 4.5 on p. 89 are for the member countries of the Southern African Development Co-ordinating Conference, namely, Angola, Botswana, Lesotho, Malawi, Mozambique, Swaziland, The United Republic of Tanzania, Zambia and Zimbabwe.

26/ United States General Accounting Office, op. cit., p. 17.

27/ Ibid., pp. 18 and 19, and Commonwealth Secretariat, South Africa and the International Financial System; Report by an Intergovernmental Group, Toronto, 1988, p. 47.

/...

Notes (continued)

28/ Ovenden and Cole, op. cit., p. 143. They suggest that bank8 may make working capital available to Japanese companies selling in the South African market, which thon enables those companies to extend credit to South African importers, They also draw attention *to* the Japanese practice of extending trade credit to Japanese shipping companies, with bill8 falling due on the date the importer is due to settle. In this way, technically, no trade credit ha8 been extended to the importer,

29/ United State8 General Accounting Office, op. cit., p. 15.

30/ Transnational Corporations in South Africa, op. cit., p. 71.

31/ United State8 General Accounting Office, op. cit., p. 17.

32/ Lewis, op. cit., p. 139.

33/ See in particular Lewis, op. cit., pp. 97-143 and Charles M. Becker, Trevor Bell, Haider All Khan and Patricia S. Pollard, The Impact of Sanctions on South Africa, Part 1. The Economy, Investor Responsibility Research Centre, Washington, D.C., March 1990.

34/ Ibid., p. 114.

35/ Becker et al., op. cit., p. 9 et seq. and Lewis, op. cit., pp. 101-108 and 130-131.

36/ Becker et al., op. cit., p. 26.

37/ Lewis, op. cit., p.1271 "The bulk of this difference can be attributed *to* the economic burden8 created by apartheid and the effort to preserve white domination".

38/ Ovenden and Cole, op. cit., pp. 187-192.

39/ United States General Accounting Office, op. cit., pp. 15 and 16; Jenkins, op. cit., p. 20; and Ovenden and Cole, op. cit., pp. 140 and 141.
