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The impact of financialisation on the IDC in South Africa since 1994

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The impact of financialisation on the IDC in South Africa since 1994

by

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Abstract

This study examined the impact of financialisation on the IDC's mandate to support industrial development in South Africa. While there is a vast literature on financialisation, a review of the literature in this study showed little understanding of how financialisation affects development banks. Thus, using a case study of the IDC and relying on a quantitative research design, the study sought to fill this above-mentioned gap. The findings indicate that the IDC shows signs of being a financialised development bank. Given its self-funding model, the development bank has prioritised financial maximisation over industrial development projects and goals. Results show that the IDC offers minimal concessionary finance, and through its equity, IDC forms part of shareholders that expect shareholder value maximisation. The implication is that South Africa is unlikely to achieve its industrial policy goals of diversifying away from primary commodities and capital-intensive industries.

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List of Acronyms

BEE	Black Economic Empowerment
BRICS	Brazil, Russia, India, China, and South Africa
DCCS	Duty Credit Certificate Scheme
FDI	Foreign Direct Investment
GEEF	Green Energy Efficiency Fund
IDC	Industrial Development Corporation
IPAP	Industrial Policy Action Plan
JSE	Johannesburg Stock Exchange
KfW	Kreditanstalt für Wiederaufbau
MEC	Mineral Energy Complex
MIDP	Motor Industry Development Programme
NDB	New Development Bank
NDP	National Development Plan
NIPF	National Industrial Policy Framework
ODI	Overseas Development Institute
RSA	Republic of South Africa
SARB	South African Reserve Bank
SDG	Sustainable Development Goals
SMMEs	Small Medium and Micro Enterprises

Chapter 1: Introduction

Background to the Problem

The unprecedented expansion and interconnectedness of the global financial markets has mushroomed with contemporary financial architecture that is not responsive to industrial development needs (Newton, 2021). Historically, the financial system and the real sector had a symbiotic relationship whereby finance was deployed into productive activities in the real economy. In turn, profits were accrued primarily from production activities. This relationship, which served as an engine for industrial development, was severed during the wave of financial deregulations at the back of the Reagan and Thatcher revolutions in the 1980s. That is, finance was decoupled from its primary role of serving the needs of the real economy and acquired the ability to profit from itself (Ashman et al., 2011). Consequently, the growth of the financial economy over the past three decades has been disproportionate to that of the real economy, causing structural imbalances. This phenomenon is referred to as financialisation and has fundamentally transformed economic systems at the macro and micro levels. In addition to raising the size and importance of the financial sector relative to real sectors[1], financialisation has shifted income from the real sector to the financial sector, exacerbating income inequality (Palley, 2007).

The concept of financialisation is fiercely debated in the literature. Generally, it refers to the unprecedented expansion and dominance of financial markets and their practices in the national and global economy (Epstein, 2005). Some scholars, however, contend that financialisation is more than a proliferation of financial markets but represents a more profound systematic transformation of the operations of economies, states, firms and households through a shift in capitalist accumulation patterns, from a Fordist accumulation regime to a finance-led regime (Krippner, 2005; Ashman et al., 2011; Lapavitsas, 2011; Aalbers, 2016). At its core, financialisation represents a new frontier of capital accumulation in which money accrues more money without being deployed

[1] In this study, real sectors refer to agriculture, manufacturing, construction and mining.

into production, leading to greater social instability and inequality (Krippner, 2005; Ashman et al., 2011; Lapavitsas, 2011; Marois, 2021).

The literature on financialisation has grown enormously over the past three decades and can be categorised into three research strands. The first research strand focuses on the changes in capital accumulation patterns, whereby profits are increasingly made from the financial market instead of production activities. Here, analysts focus on the macroeconomic level impact of financialisation, characterised by a shift in dominance away from the manufacturing sector to the financial sector (Krippner, 2005; Ashman et al., 2011; Sokol, 2017). The second strand of research focuses on changes in non-financial firms as they have become increasingly dependent on the financial markets to boost their earnings (Andreoni et al., 2021; King, 2021). This dependence results from non-financial firms prioritising shareholder value maximisation at the expense of engaging in productive investment. That is, non-financial firms, in the face of financialisation, have focused on distributing a large part of their profits to shareholders as opposed to reinvesting them into productive capabilities (Lazonick & O'Sullivan, 2000). The third strand of research focuses on the financialisation of households and workers, highlighting that these entities have become part of financial markets through holding financial assets and debt (Sokol, 2017).

Problem Statement

As noted above and later in more detail in the literature review section, financialisation has been widely investigated. However, its analysis concerning public institutions, particularly development banks, is conspicuously missing from the debate. This is despite the state being a key factor in enabling financialisation (Sokol, 2017). For instance, a shift to finance-led capital accumulation is not possible without the facilitation of the state in the form of active deregulation of finance (Karwowski & Centurion-Vincencio, 2018). It should be noted that there have been attempts to fill in this gap, with Karwowski (2018 & 2019) providing an overview of the financialisation of the state by looking at fiscal and monetary policy. While these efforts are noteworthy, the research on the financialisation of public or semi-public entities remains nascent, with little

knowledge of the financialisation of development banks. This is despite development banks being a central part of the financial system that is highly financialised and disengaged from the real economy.

Development banks are financial institutions with a minimum of 30% state ownership and a mandate to deliver specific developmental goals within a particular geographic region or sector (Luna-Martinez & Vicente, 2012). By their initial design, the development banks were formed to fill a financing gap left by commercial banks. This financing gap is related to economic transformation and involves large-scale projects with concessional interest rates and a long-term maturity period (Gottschalk et al., 2016). As part of state institutions, development banks play a key role in ensuring the success of the industrial policy. In addition to addressing market failures such as capital market imperfections and coordination failures, development banks also provide funding and technical assistance, which ensure that industrial and infrastructure development projects are viable. Indeed, evidence shows that development banks have been instrumental in the industrial development success of nearly all late industrialisers (Amsden, 2001). For example, development banks in Brazil, Mexico and South Korea directed most of their funds towards infrastructure projects from the early 1950s. More specifically, between 1953 and 1959, 74% of the lending from development banks in Brazil was directed towards infrastructure projects (Amsden, 2001). Development banks also invested heavily in the manufacturing sector of all late industrialisers. In 1970, the Korean Development Bank accounted for 45% of total manufacturing sector investments. Similarly, from 1990, development banks in Thailand accounted for 46% of total investment in the manufacturing sector (Amsden, 2001). Thus, it is evident that the development banks are meant to catalyse industrial development.

Yet, little is known about the financialisation of development banks and how this phenomenon impacts their mandate to deliver industrial development. This is an important neglected area of research in financialisation for two reasons. Firstly, through long-term finance, grant funding and concession rates, development banks are instrumental in directing finance towards productive activities in the economy and ensuring industrial development. Financialisation can thwart this role of development banks, turning them into private-like financial institutions that prioritise financial gain over industrial development goals. If this phenomenon is not adequately understood in the

literature, the concerted effort to industrialise, especially for developing countries, will stall if not move backwards. Secondly, the financialisation of development banks needs to be sufficiently understood so that they can, in turn, be used as a buffer against rampant financialisation. Given the public nature of development banks, they can be used to protect real economic activities from financialised market imperatives (Marois, 2021).

This research aimed to fill the abovementioned gap using a case study of the Industrial Development Corporation (IDC) from 1994. The IDC is a South African state-owned development bank established in 1940 through the Industrial Development Corporation Act (22 of 1940) (IDC, 2021). Its mandate is to "maximise development impact through job-rich industrialisation while contributing to an inclusive economy" (IDC, 2021:11). The IDC is an appropriate case study for three reasons. Firstly, the IDC is part of South Africa's highly financialised economy with well-developed financial markets. That is, the IDC operates within a highly financialised economy (Ashman et al, 2013). Secondly, the IDC does not get funded by the government but rather sources funding from some of its debt capital markets (Goga at el, 2019). As a result, the IDC has strong interaction and a relationship with the financial system that is largely unsupportive of the real economy. Thirdly and more importantly, the IDC is meant to serve as a catalyst for industrial development in South Africa through its funding and technical assistance. Thus, the in-depth examination of the IDC will advance the limited understanding in the literature on the nature of the financialisation of development banks.

Research Question

With that background, this research sought to answer the following question.

a. To what extent has financialisation impacted IDC's ability to fulfil its mandate of supporting industrial development in South Africa since 1994?

Research Objectives

With such a glaring knowledge gap in the literature about the financialisation of the development banks, the overarching objective of this study was to critically analyse the impact of financialisation on the IDC's mandate to deliver industrial development, to build a solid theoretical foundation and empirical evidence on the financialisation of development banks. More specifically, the study aimed to:

1. Critically explore the relationship between financialisation and development banks.
2. Identify and develop indicators for analysing financialisation in development banks.
3. Measure the financialisation of the IDC using the measurements developed and identified in the literature.
4. Examine the implications of a financialised IDC on industrial development in South Africa since 1994.

Significance and Contribution of the Study

The state and its institutions are not just passive players but are active in driving and enabling financialisation. The analysis of the IDC brings to the fore the extent to which financialisation has penetrated productive sectors by highlighting the bank's role in driving or halting the financialised behaviour of key economic agents in South Africa. More importantly, by building a theoretical foundation and empirical evidence, the study advances the limited understanding of the implications of financialised development banks on industrial development. This, in turn, enables new policies and institutional paradigms to emerge, which will realign and repurpose the development banks to their original mandate of advancing industrial development.

Research Design and Methods

This study used a quantitative approach with a case study method. The research gap and contribution to the financialisation literature informed the choice of this approach. Given that the financialisation of development banks has not been thoroughly investigated in the literature, it was crucial to understand its extent and implication. To effectively do this, there was a need for a quantitative approach that could measure the depth of financialisation and its impact. The main advantage of relying on quantitative as opposed to qualitative research methods is the element of objectivity and generalisability. That is, studies conducted using quantitative methods are seen to be objective and the findings can be used to make broad generalisations (Mertler, 2021).

Notably, previous studies also relied primarily on the quantitative approach to measure the level of financialisation and understand its impact on various segments of the economy. Mainstream economists relied on econometric models to understand the extent of financialisation and its impact. Heterodox economists, on the other hand, used a composite of economic and financial indicators to understand a shift to finance-led accumulation (King, 2021). Moreover, to illuminate the extent and impact of financialisation, most heterodox literature on the phenomenon is context specific. That is, most scholars used case studies to understand the prevalence of financialisation. According to Yin (2018), a case study is a formal research method that can be used both in quantitative and qualitative approaches, which investigates a contemporary phenomenon within its real-world context, particularly when the boundaries between the phenomenon and context are not clearly defined. Generally, case studies are useful because they allow in-depth focus and provide holistic and real-world perspectives (Yin, 2018).

This study did not deviate from the heterodox methodological approach as it used the case of the IDC. The case study method made it possible to understand the depth and complexity of financialisation in development banks in a specific context. Without an in-depth and context-specific analysis, the study would fall short of making a meaningful contribution to the literature because it is extremely complex to understand financialisation only at the level of abstraction. Similar to most heterodox literature, the

study relied on key indicators, such as the drive of shareholder maximisation, financial deepening and profit maximisation to measure the financialisation of the IDC. These indicators were used to demonstrate the extent of financialisation in the IDC and, more broadly, outline the logic of financialisation in development banks.

In terms of data collection, the study triangulated multiple sources of data that are publicly available, including inter alia IDC annual reports, national statistics provided by the South African Reserve Bank (SARB) and Statistics South Africa, and secondary data from other scholars.

Limitations of the Study

This research would have benefitted immensely from interviews with key personnel from the IDC and recipients of IDC funding. However, interviews were excluded from this research due to time and resource constraints and the confidentially of these issues. Although there are multiple dimensions of financialisation, this study was limited to measuring financialisation in the IDC using indicators mentioned in the research design and method section. Finally, the timeline for the analysis began in 1994, which marks the transition into democracy. The reason for starting the analysis from 1994 is that South Africa financially liberalised its economy, effectively triggering financialisation (Ashman et al, 2013). Relatedly, the analysis had no end period, given that the data collected was relatively non-standardised. In this regard, efforts were made to get the latest data.

Structure of the Study

The rest of the study is structured as follows. The second chapter is a literature review. Here, key debates on financialisation are discussed and the review locates the literature on the financialisation of development banks. The third chapter is an analytical framework, which consists of newly developed indicators for measuring the financialisation of development banks. Notably, these indicators are drawn and adapted from existing literature. The fourth chapter uses indicators developed in

chapter three to analyse the case study of the IDC. The fifth and final chapter provides a conclusion and policy recommendations. Furthermore, the final chapter also discusses further areas of research that can be conducted on this issue.

Chapter 2: Literature Review

Introduction

As noted above, financialisation has been the centre of attention for many scholars, with its research agenda burgeoning over the past three decades. The most observable fact from the literature on financialisation is that it is heavily skewed towards advanced economies. However, in recent years, the research on the phenomenon has expanded to include variegated developing world experiences. Notably, financialisation research in the developing world is relatively nascent, with the literature mostly documenting the experience of East Asian and Latin American countries (Bonizzi, 2013; Karwowski et al, 2020). In Africa, South Africa remains the most widely studied country in the financialisation literature, with scholars looking at the macroeconomic impacts (Ashman et al., 2013; Isaacs, 2018; Mohamed, 2019) and others looking at the changing behaviour of non-financial corporations (Karwowski, 2012; Andreoni et al., 2021; King, 2021).

Generally, the literature on financialisation uncovers a vast range of phenomena, including the change in capital accumulation patterns (Krippner, 2005; Ashman et al., 2011; Lapavitsas, 2013), the rise of shareholder value as a model of corporate governance (Lazonick & O'Sullivan, 2000), financialised behaviours of non-financial firms and banks and financialisation of households (Andreoni et al., 2021; King, 2021). These remain dominant approaches and metrics to the study of financialisation. However, the literature review also indicates that the financialisation process is non-linear and differs in each country. More specifically, financialisation in developing countries has been observed to have peculiar features compared to developed countries (Bonizzi, 2013). Consequently, different theoretical perspectives, mainly from the heterodox tradition, have emerged to explain the financialisation process in developing countries. Moreover, there is a plethora of empirical research concerning developing countries that do not necessarily follow theoretical approaches but rely on the abovementioned dominant approaches to measure financialisation.

It should be noted that even though the literature on financialisation is variegated and based predominantly on advanced economies, the financialisation of development banks is missing in the literature covering both the experiences of developed and developing countries. Karwowski & Centurion-Vincencio (2018) contend that the role of the state in the literature is an afterthought, including its institutions such as development banks. Neoclassical economists focus on the role of finance in development and typically conduct their analysis using econometrics models. On the other hand, many heterodox economists focus on a sectoral analysis of financialisation, and those that investigate the phenomenon at the macro level also omit the role of the state (Karwowski & Centurion-Vincencio, 2018). Overall, there is a general acknowledgement in the literature that the public sector is missing from the financialisation debate (Sokol, 2017; Karwowski & Centurion-Vincencio, 2018). Despite this acknowledgement, there are very few attempts to fill this gap.

This review analyses the financialisation literature focusing primarily on developing countries, outlining different interpretations of the phenomenon within the developing context. More importantly, this review highlights research strands of financialisation that have been explored in developing countries, including the recent insights on the financialisation of the state. This narrow focus is crucial as it provides an appropriate context for the study. Analysing the literature of developed countries is unhelpful in this regard, as financialisation assumes a different form in developing countries shaped mainly by imperialist relations.

Theoretical Approaches to Financialisation in Developing Countries

As a starting point, many scholars use Epstein’s definition of financialisation as "the increasing role of financial motive, financial markets, financial actors and financial institutions in the operations of the domestic and international economies" (Epstein, 2005:3). Although this definition has been criticised for its broadness, it has allowed many different interpretations and approaches based on scholars' ideological inclinations and schools of thought (Bonizzi, 2013; Marois, 2021). Notably, financialisation as a concept emanates from the heterodox tradition, and many

different theoretical approaches to the issue come from this tradition. Most of the existing theoretical perspectives on financialisation come from either the regulationist school of thought, post-Keynesian economics or the Marxist political economy – all of which belong to the umbrella term of the heterodox tradition. Often, these perspectives borrow from each other, and thus distinction among them can be hard to detect (Karwowski & Stockhammer, 2017). These perspectives also explain financialisation in developing countries.

Bonizzi (2013) points out that the regulationist school of thought is the first to highlight that financialisation plays out differently in developing countries vis-à-vis developed countries. The theory of regulation emerged in the 1970s in France as a different stream of Marxist political economy (Becker et al., 2010). At its core, the regulationist theory attempts to explain how the regime of accumulation in the capitalist economy, which is inherently unstable and crisis-prone, is stabilised to ensure continued economic and social reproduction. According to the regulationist theory, a regime of accumulation, which is an organisation of production and distribution of surplus value, needs a mode of regulation for long-term reproducibility (Becker et al., 2010). In this regard, the mode of regulation, which is a set of institutions, practices and policies, provides stability to the regime of accumulation (Becker et al., 2010; Bonizzi, 2013; Eckhard et al., 2015).

Regulationist theory is useful in the analysis of financialisation because it places a greater emphasis on policy changes. This, in turn, allows for the examination of policies that have enabled the process of financialisation and the agents involved in that process (Becker et al., 2010). As noted above, developing countries underwent massive financial liberalisation from the 1980s based on policy prescripts from international organisations such as the International Monetary Fund and World Bank. At the same time, there was a consensus commonly known as the Washington Consensus within the global economy that market-friendly policies are deus ex machina for development, especially for developing countries (Bonizzi, 2013). However, as pointed out above, these policy changes were the back door for financialisation in developing countries. Without financial deregulations, financialisation would not have taken place in developing countries. In addition, Becker

et al. (2010) distinguish between financialisation based on the inflation of financial asset prices and interest rates. The former is much more prevalent in developed economies, while the latter manifests in the developing world. In other words, due to low domestic savings, many developing countries rely heavily on foreign capital flows and thus set exorbitantly high-interest rates to attract these flows (Becker et al., 2010).

On the other hand, the post-Keynesian approach postulates that non-financial firms' increasing role in the financial market as asset holders and their enforced preference to distribute earnings to shareholders comes at the expense of real investment (Hein & Till, 2010; Stockhammer, 2010). In addition, Stockhammer (2010) argues that in an era of financialisation, consumption expenditure rather than capital investment has become the main driver for growth because households have increased access to credit. The findings from post-Keynesian literature on the financialisation process have been corroborated by empirical research in developing countries. For example, King's (2021) research points out that Shoprite Holdings Limited, a South African multinational retail corporation, has accumulated financial assets that crowded out investment in productive capabilities within the company. Similarly, Ashman et al. (2013:32) argue that "financialisation [in South Africa] has directed capital away from the long-term investment necessary to diversify the industrial base. Instead, capital has flowed to finance and consumption and the sectors with strong linkages to these activities". Indeed, non-financial corporations, the backbone of industrial development in any country, have become financial rentiers (Demir, 2007).

Marxist political economy has the most comprehensive literature on the theoretical approaches to financialisation in both developed and developing countries. Within the developing context, two components characterise the Marxist approach to financialisation. Firstly, financialisation in the developing context is conceptualised as subordinate (Powell, 2013; Lapavitsas & Soydan, 2022). To be more specific, "financialisation in developing countries retains some of the fundamental tendencies observed in developed countries but assumes a distinctive subordinate form shaped by imperial relations" (Lapavitsas & Soydan, 2022:6). In this case, subordinate financialisation allows the extraction of surplus generated domestically because domestic firms in developing countries rely heavily on foreign capital (Bonizzi, 2013;

Powell, 2013). In addition, developing countries with weak currencies have to pay higher interest on debt borrowed on foreign currency and pay higher dividends to compensate for high-risk perceptions associated with developing countries (Lapavitsas & Soydan, 2022). Santos (2022:9) puts it succinctly that "financialisation in emerging capitalist countries is subordinated because accumulation models are based on the reliance on (short-term) financial capital, high-interest rates, and overvalued exchange rates". In turn, this subordinate form of financialisation causes massive current account deficits and external debt, slowing productivity in real sectors (Santos, 2022). It should be noted that the is new theoretical approach to the financialisation literature.

Secondly, the Marxist political economy usefully deploys the concept of the core versus periphery developed by the dependency theorists in the 1960s to explain the process of financialisation in developing countries. Notably, dependency theory is not a principal component of Marxist political economy but has been used in various heterodox scholarship to explain financialisation in the developing world. Generally, dependency theorists argue that the underdevelopment of countries in the Global South is due to their peripheral position within the global economy (Hryniewicz, 2014). These peripheral countries in the Global South export raw materials cheaply to countries in the core (industrialised nations). Core countries, in turn, transform these raw materials and sell them back to peripheral countries at higher prices (Hryniewicz, 2014). Drawing from this theory, the Marxist political economy indicates that as the capital accumulation regime in the core shifts to the financial sphere, peripheral countries also become attractive destinations for capital (Lapavitsas & Soydan, 2022). Therefore, financialisation in peripheral economies is sparked by financialisation in core countries. Foreign capital flows become the main transmitter for financialisation in peripheral economies. In sum, the Marxist political economy argues that financialisation emanates from developed nations, and thus spread to the developing countries. Additionally, in developing countries, financialisation is argued to have a different form compared developed countries.

Stylised Facts of Financialisation in Developing Countries

The research on the financialisation of developing countries mainly comprises empirical work. In this case, the literature does not neatly follow the theoretical frameworks mentioned above but relies on various indicators to measure the extent and impact of financialisation in developing countries. Notably, these empirical studies use the characteristics of financialisation in the developed world to measure financialisation in developing countries. Nonetheless, these studies offer important insights into the impact of financialisation on various segments of the economies, including macro-level impact on non-financial firms' behaviour and banks.

At the macro level, the literature looks at the changing patterns of capital accumulation and its implications on development. In this case, scholars mainly look at short-term capital flows and capital flight (Ashman et al., 2011; Ashman et al., 2013; Mohamed, 2019). It is argued in the case of South Africa that the liberalisation of capital flows has been destructive, as the country has attracted mainly short-term speculative flows instead of foreign direct investment (Mohammed, 2019). Mohammed (2019) shows that the disproportionately high inflow of short-term capital compared to foreign direct investment has partly driven the structural composition of South Africa's economy by favouring the service sector linked to debt-driven consumption. This, in turn, has led to the growth of the financial sector outpacing real sectors. Moreover, Isaacs and Kaltenbrunner (2018) posit that the economic prices such as exchange rate in South Africa are primarily determined by capital flows, more specifical portfolio investment rather than economic fundamentals.

In addition, financialisation in the developing world is associated with capital flight. Ashman et al. (2011) and Mohammed (2019) highlight that South Africa has experienced massive capital flight since 1994 due to financial liberalisation that took place as the country transitioned into democracy. South African multinational corporations drove this capital flight. Ashman et al. (2011) argue that this capital outflow could have been reinvested in the domestic economy to improve its productive capabilities. In sum, at the macro-level, excessive inflow of short-term capital combined with capital flight has reduced productive investment in developing countries (Bonizzi, 2013).

At the sectoral level, the impact of non-financial firms is the most studied theme in the literature that covers developed and developing countries. In this regard, scholars argue that similar to developed countries, non-financial firms located in developing countries acquired technical abilities in financial markets and are increasingly holding financial assets at the expense of productive investment (Lapavitsas, 2013; Lapavitsas & Soydan, 2022). Using the case of Argentina, Mexico and Turkey, Demir (2007) highlighted that non-financial firms have held non-financial assets in these countries mainly due to uncertainty in the macroeconomic environment. However, in most of the literature, the financialisation of non-financial firms is associated with the rise of shareholder value maximisation as a corporate governance model (Lazonick & O'Sullivan, 2000; Kalinowski & Cho, 2009; Bowman, 2018; King, 2021; Andreoni et al., 2021).

Finally, there is ample literature that looks at the financialisation of banks. In this regard, it is argued that commercial banks have changed in two respects in the face of financialisation. Firstly, they have increased their role as lenders to households and individuals to increase and sustain their profits (Lapavitsas, 2011). Secondly, commercial banks have increased their intermediation role in the financial markets to earn fees and commissions and amass more money through trading by establishing business functions such as investment banking (Lapavitsas, 2011). In addition, Santos (2011) argues that foreign banks have encouraged financialisation by driving debt-driven consumption and starving Small Medium and Micro Enterprises (SMMEs), the economic backbone of many developing countries, of much-needed funding. Echoing the point raised by Santos, Lapavitsas and Soydan (2022) argue that foreign banks, through their activities and practices, have transformed domestic banks towards financialisation. In this regard, domestic firms become part of the international financial architecture by providing foreign funding to domestic non-financial firms.

Financialisation of the State and its Institutions

The financialisation of state and public institutions is a newly emerging research agenda in the literature. As previously noted, the research is not adequately investigated in developed and developing countries, so this review section focuses on

the general interpretation of the phenomenon. So far, Karwowski & Centurion-Vincencio (2018) and Santos (2022) are the only scholars who have endeavoured to conceptualise the financialisation of the state. According to Karwowski & Centurion-Vincencio (2018:3), the financialisation of the state refers to "a changed relationship between the states, understood as sovereign with duties and accountable towards its citizens, and financial markets and practices, in ways that can diminish those duties and reduce accountability". There are generally four ways financialisation in the state plays out, namely: (a) it is through the adoption of financial motives in public institutions; (b) embracing and accepting of the finance-led accumulation regime; (c) active involvement in the creation of new financial instruments; (d) directly contributing to the financialisation of households (Karwowski & Centurion-Vincencio, 2018; Karwowski, 2019). Furthermore, financialisation assumes form in fiscal and monetary policy. In the case of fiscal policy, Karwowski (2019) postulates that financialisation turns public services into traded financial assets; it also develops a secondary market for public debt, which in turn transforms the state into an active financial market player that extracts rents from the financial market. In the case of monetary policy, financialisation encourages central banks to prioritise inflation targeting and pursue market-based short-term liquidity (Karwowski & Centurion-Vincencio, 2018; Karwowski, 2019).

The conceptualisation of state financialisation consolidates different aspects of the phenomenon in the public sphere. However, similar to Epstein's widely used definition of financialisation, Karwowski's definition of the state's financialisation is too broad to have any meaningful analytical contribution. It merely explains the state as a key enabler and player within the process but does not highlight the structural relationship between finance and the state. Santos (2022), on the other hand, proposes a slightly narrower definition of state financialisation. According to Santos (2022:148), state financialisation refers to "a mode of governance whereby the state engineers and repurposes financial tools and markets as instruments of statecraft in such a way that they bestow increased financial sector infrastructural power". By infrastructural power, Santos (2022) refers to the financial sector's influence on the state's capacity to implement policy decisions. In this context, the government is not only a key enabler

of financialisation but allows greater involvement of financial agents in policy decisions, thus effectively serving the interests of financial agents.

Development Banks and Financialisation

As highlighted earlier in the problem statement, there is little to no literature that meaningfully explores the relationship between financialisation and development banks. There is, however, a fair amount of literature that investigates the operational efficiency of development banks. Worryingly, the bulk of literature on development banks is rather superficial as very little focuses on structural issues within development finance and its relationship with the economy. Most of the literature clarifies the role of development banks (Luna-Martinez & Vincente, 2012; Lazzarini et al., 2015). Other aspects of the literature focuses on the effectiveness of development banks (Gutierrez et al., 2011). Another strand of research on development banks, located primarily within the discipline of global politics, focuses on development banks as the locus of power that shapes the economic policy of developing countries. In this debate, the recently established New Development Bank (NDB) by the Brazil, Russia, India, China and South Africa (BRICS) group is seen as a bulwark against the ever-increasing influence of Western-dominated development banks (Qobo & Mills, 2015).

More importantly, there is sporadic literature that is tinkering covertly with the connection between financialisation and development banks, particularly in South Africa. For instance, Goga et al. (2019)'s assessment of the developing financing landscape in South Africa reveals that the IDC self-funding model imposes real constraints on the institution's ability to fund industrialisation. Goga et al. (2019:39) explain that the "IDC is self-sustainable means that it is governed by a financial logic which makes it much less likely to take on the role of providing a significant amount of risky funding in the economy". Although Goga et al. (2019) do not explore the relationship between financialisation and development banks in South Africa, the explanation of the IDC's funding constraint does indicate the broader logic of financialisation. In addition, Karwowski (2022) identifies blended finance, among others, as a conduit for financialisation. Blended finance refers to the use of public resources to de-risk investment to crowd in more private sector investment, and often,

development banks are used to carry out this approach (Karwowski, 2022). Unfortunately, Karwowski's analysis remains superficial as it does not unpack how this financialisation process through blended finance plays out in South Africa and, more broadly, in the developing context.

Against this context, this study sought to move the debate forward on the nature of the financialisation of public institutions such as development banks using the case of the IDC. It sought to collate the sporadic efforts made by Goga et al. (2019) and Karwowski (2022) and provide a comprehensive overview of the relationship between financialisation and development banks. Different theoretical perspectives analysed in this review have provided appropriate context and analytical tools that can be used to conceptualise the issue of financialisation and development banks meaningfully. More importantly, empirical studies also provided direction and appropriate indicators to measure financialisation in a developing context.

Conclusion: Summary of the Literature

Financialisation in developing countries assumes a different form compared to developed countries. Heterodox approaches reveal that financialisation in developing nations is not an endemic process but is transmitted from developed countries. The regulationist school of thought highlights that policy shifts, such as financial liberalisation in developing countries based on the advice from the International Monetary Fund and the World Bank, have resulted in financialisation in these countries. More so, the financialisation in developing countries comes in the form of interest rates, whereby capital flows play an essential role. Post-Keynesians point out that the financialisation of non-financial firms comes at the expense of productive investment, even in developing countries. Marxist political economy highlights that financialisation in developing countries is shaped by its imperial relations with developed countries, and in this context, it is considered “subordinate financialisation”. Furthermore, different authors tested the extent of financialisation on various segments of emerging economies, broadly illustrating the negative consequences of financialisation. The research on the financialisation of the state is relatively nascent.

Nonetheless, the scholarly contributions so far reveal that the state is not only a facilitator of financialisation but has also bestowed power to financial markets through policy decisions. Finally, no literature makes meaningful connections between the development banks and financialisation, although scholars such as Goga et al. (2019) and Karwowski (2022) have come close. Therefore, this study's task was to make that connection and move the debate forward.

Chapter 3: Developing the Analytical Framework

Introduction

As noted in the introductory chapter, the literature on the financialisation of development banks is limited and a practical analytical framework is yet to emerge. However, given the permeation of financialisation in every aspect of society, scholars (Carrol & Javis, 2014; Rowden, 2019; Gabor, 2021; Marois, 2021) have begun to contemplate the implications of financialised development finance. This nascent but emerging literature is on the financialisation of development. Here, Gabor's (2021) Wall Street Consensus is the first comprehensive attempt to theorise the financialisation of development finance. Gabor (2021) argues that the Wall Street Consensus precedes the Washington Consensus. This new development paradigm aims to reorient the investment decisions of global investors towards development projects in health, education, infrastructure and energy. In the Wall Street Consensus paradigm, state and multilateral development banks play a crucial role in attracting private capital into development projects by socialising and minimising risk associated with development projects and maximising returns for private investors (Gabor, 2021; Marios, 2021). This process, called de-risking, is a key tenet of the Wall Street Consensus.

The Wall Street paradigm is a useful theoretical framework of financialised development finance at the macro level. However, it is limited in providing a micro-account of financialisation in development banks. As noted earlier, development banks operate in a highly financialised environment, and thus, it is important to have a comprehensive understanding of how financialisation manifests in this context. Goga et al. (2019) argues that development banks like the IDC operate like commercial banks because of institutional constraints that involve no government funding. This institutional arrangement is likely to be key contour of financialisation in development banks. Thus, this section aims to provide a micro-level account of the financialisation of development banks relying on different accounts from the literature, including the macro-level accounts of Gabor (2021).

The remainder of the chapter is structured as follows: the first section discusses the Wall Street Consensus. Here, the aim is to account for the paradigm shift in development finance over the last decade. The second section discusses the theoretical framework of development banks. There are many different types of development banks and the section aims to provide definitional parameters. Equally important, this chapter discusses the theoretical underpinning of these banks, including their mandates and function in society. The third section discusses the financialisation of development banks. In this case, the discourse is led by the following question: what would the financialisation of development look like? This section also indicates key indicators for measuring financialisation in development banks. The final section discusses the implications of a financialised development bank on industrial development.

Financialisation of Development Finance: The Wall Street Consensus

Finance for development has undergone a paradigm shift in recent years. Previously, development projects in the Global South were funded through Official Development Assistance, which was government aid that targeted economic development. However, this development financing paradigm changed in 2015 with the introduction of the Sustainable Development Goals (SDGs). The international development community led by multilateral development finance institutions forged a consensus that a global partnership with private capital is crucial to achieving these goals by 2030 (Rowden, 2019). At the time, it was estimated that $US4.5 trillion a year in government spending would be needed to meet SDGs (World Bank, 2015). Hence, a case was made by the multilateral development banks led by the World Bank (2015) that public resources alone are insufficient to meet these goals, and private capital would need to be courted. The view that public resources are inadequate in meeting development needs is based on the pro-market principle. This economic principle posits that market-based mechanisms, including private capital, are the best respondents to the climate crisis (Marois, 2021). In the context of development finance, the principle is premised on attracting private capital using public resources to socialise investment risks and maximise returns (Marois, 2021). It is a new development finance mantra which Gabor (2021) calls a Wall Street Consensus.

In the Wall Street Consensus, the role of the state and its institutions is reduced to de-risking development projects to attract private capital. That is, the state's role is to assume the investment risks associated with development projects, thus maximising profit for private capital. Hence, de-risking is central to this new development mantra. The state undertakes two forms of de-risking: regulatory and financial. The former refers to the removal of regulatory barriers to improve the risk-return nexus for development projects. (Gabor, 2021). On the other hand, financial de-risking refers to any form of financial support from the government, including but not limited to subsidies and credit guarantees to reduce investment costs and ensure a steady cash flow for investors (Sweerts et al., 2019; Gabor, 2021). In addition, the process of de-risking involves assuming several risks, including the demand risks associated with commodification and securitisation of development assets, political risks emanating from national policies that pose a threat to profit maximisation and currency risks that would prevent free capital outflow from global investors (Gabor, 2021). In sum, in the new development paradigm, financialisation has extended beyond the balance sheets of non-financial corporations and banks and has become a state-mediated process. Development has become profit-driven, and the state's institutional mechanisms have been reoriented towards protecting private finance interests (Carroll & Jarvis, 2014; Mawdsley, 2018; Gabor, 2021).

Development banks lead the efforts in designing the de-risking measures to entice global private investors into developing countries and mobilise private finance towards development projects. Several measures are used by development banks, including inter alia concessional finance, blended finance, grants, credit guarantees, and first loss structures in pooled vehicles to reduce risk for private investors (Ingram, 2022). Concessional finance consists of capital priced below market rates and targeted at high-risk projects (Ingram, 2022). Concessional finance is used in the early stages of the project cycle, whereby the project is too risky for private investors. Conversely, blended finance combines non-concessional public finance and non-concessional finance (OECD, 2020). The primary aim of blended finance is to provide a subsidy to bring the risk-adjusted rate of return on investment in line with the market, thus increasing the attractiveness of the investment to private investors (OECD, 2020).

The overall implication of the Wall Street Consensus is that it is likely to undermine the role of the state in structural transformation. Previously, the state autonomously decided which sector to support to transform the economy from an agrarian to a manufacturing-based economy. History is replete with early and late industrialisers intentionally using the state and its resources to support sectors considered important in transforming their economy. This will be a challenge moving forward, given that the state will be subordinated to the interests of private capital, whose main concern is only profit maximisation. Furthermore, de-risking policy reforms under the Wall Street Consensus would prevent developing states from using many financial regulations, including capital controls, to support and retain investments in the productive sectors that ignite long-term economic development (Rowden, 2019).

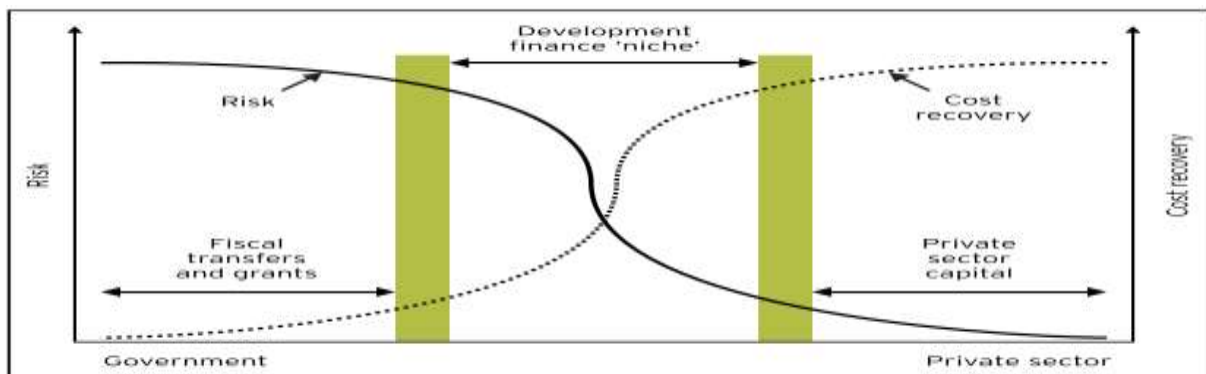
The Theory and Function of Development Banks

Development banks are wholly or partially state-owned financial institutions that provide long-term capital to projects that have the potential to advance industrial development or other socio-economic goals (Luna-Martinez & Vincente, 2012). As the name suggests, development banks are mainly concerned with financing development and often are equated to economic development (Marois, 2021). Some literature defines development banks by their theoretical rationale, which is to intervene in the financial markets to address market failure related to the provision of long-term, socially beneficial capital (Thorne & Du Toit, 2009; Xu et al., 2021). In this case, market failure relates to the under-provision of capital by private investors to projects with higher socio-economic value than costs. In general, Xu et al. (2021) indicate that the primary role of development banks is to provide financial support for productive investments, which incorporate social and environmental value, and this kind of capital is typically underprovided by the market. Moreover, development banks play a role in mitigating market failures arising from costly information asymmetries that hamper access to long-term finance capital (Gutierrez et al., 2011). Relatedly, development banks play a key role in providing counter-cyclical finance during financial crises which are seemingly endemic to the financial markets (Griffith-Jones, 2022).

In addition, it is important to note that development banks are called various names, including inter alia policy banks or development finance institutions. Bruck (2001) notes that development finance institution is a more precise term. This is because it includes all development finance institutions with different legal forms, including those with mixed, private or public ownership structures. However, for the sake of simplicity, this study uses the term ‘development banks’ as it is closely synonymous with development financial institutions and is commonly used in the literature.

Regarding the design, development banks are different from commercial and investment banks in two respects. Firstly, in addition to providing long-term capital, development banks conduct an economic appraisal of the projects they seek to fund (Bruck, 2001). In this case, socio-economic returns are an integral part of the criterion for judging the development contribution of the projects requiring development banks' funding. Unlike most commercial banks, which only consider the return on investment, development banks conduct a cost-benefit analysis to examine the developmental contribution for projects considered for funding. Secondly, development banks function as lenders of last resort. In this case, the development banks provide funding to projects that cannot receive funding from other private or public entities (Bruck, 2001).

Graph 1: The role and position of development banks



Source: Thorne & Du Toit (2009).

Development banks operate at the intersection between government and markets, relying on market mechanisms to achieve developmental goals (Xu et al., 2021). On one side of the spectrum sits the state, which provides funding to projects with high risk where cost recovery is impossible. On the other end of the spectrum lies private finance comprising investment banks, commercial banks and venture capital firms that seek to maximise return on investment. In this regard, private finance finances low-

risk projects with high-cost recovery; see Graph 1 above (Thorne & Du Toit, 2009; Xu et al., 2021). As noted earlier, development banks lie in the middle, operating at the frontier between state and private finance, funding projects with high risk and limited revenue (Thorne & Du Toit, 2009).

The Structure and Functions of Development Banks

As noted earlier, development banks are typically government-owned institutions with varying levels of government ownership. Luna-Martinez and Vincente's (2012) development bank survey indicated that 74% of 90 development banks indicated that the government wholly owned them. Meanwhile, 21% had government ownership of between 50% and 99%, and 5% had less than 50% government ownership. Xu et al. (2021) indicate that of 527 public development banks and development finance institutions, 75% were fully owned by the government. In instances where the development bank is privately owned or government has less 50% of ownership, the banks still retain its development focus (Luna-Martinez & Vincente, 2012).

Similarly, in terms of funding, development banks use various methods to fund their operations, including receiving savings from depositors, raising money in both the international and domestic capital markets, borrowing from other financial institutions, using their equity, and receiving a budget allocation from the government. Of 90 development banks surveyed in 2012, 41% indicated receiving deposits from the public, 89% indicated raising money by borrowing from other financial institutions, and 40% indicated receiving direct government transfers (Luna-Martinez & Vincente, 2012). In addition, development banks can either have a broad or specific mandate. With the former, there is no reference to any specific sector. At the same time, the latter would typically have a specific mandate to state the sector and/or type of customers to be supported by the development bank (Luna-Martinez & Vincente, 2012).

Furthermore, development banks perform various functions in society. In addition to long-term financing and a counter-cyclical role, development banks assist with the promotion of development projects and capital markets in developing countries. They

provide technical support to critical infrastructure projects and connect borrowers to the international financial market. The function of the development banks is aptly summarised in Table 1 below.

Table 1: Additional Functions of Development Banks

Function	Description
Promotion of development projects	Development banks act as entrepreneurs who invest in new productive activities which are often innovative and technically challenging.
Long-term financing and capital market development	Development banks contribute to the development of domestic capital markets in developing countries. Countries with infant domestic capital do not have sufficient savings to provide long-term investment. Thus, through the provision of long-term finance, development banks ignite a rapid development of infant domestic capital markets.
Financial agents and catalyst	In certain instances, development banks perform the functions of financial agents, blending public and private finance into one financial package. This function is often done to augment developing funding. In addition, development banks act as catalytic agents by helping potential borrowers find capital in international and domestic capital markets.
Technical assistance	In developing countries, development banks assist with technical assistance required in modern production processes that are often lacking.

Source: Adapted from Bruck (2001)

History and Evolution of Development Banks

Development banks have played a key role in building new local industries and boosting existing ones for early and late industrialisers. The rapid industrialisation of Europe in the 19th century was largely due to the development banks. Industrial development in the Netherlands and France was boosted by the creation of development banks in the 1800s (Aghion, 1999). In particular, Comptoir d'Escompte and the Credit Mobilier played a significant developmental role in France by providing long-term finance (Aghion, 1999).

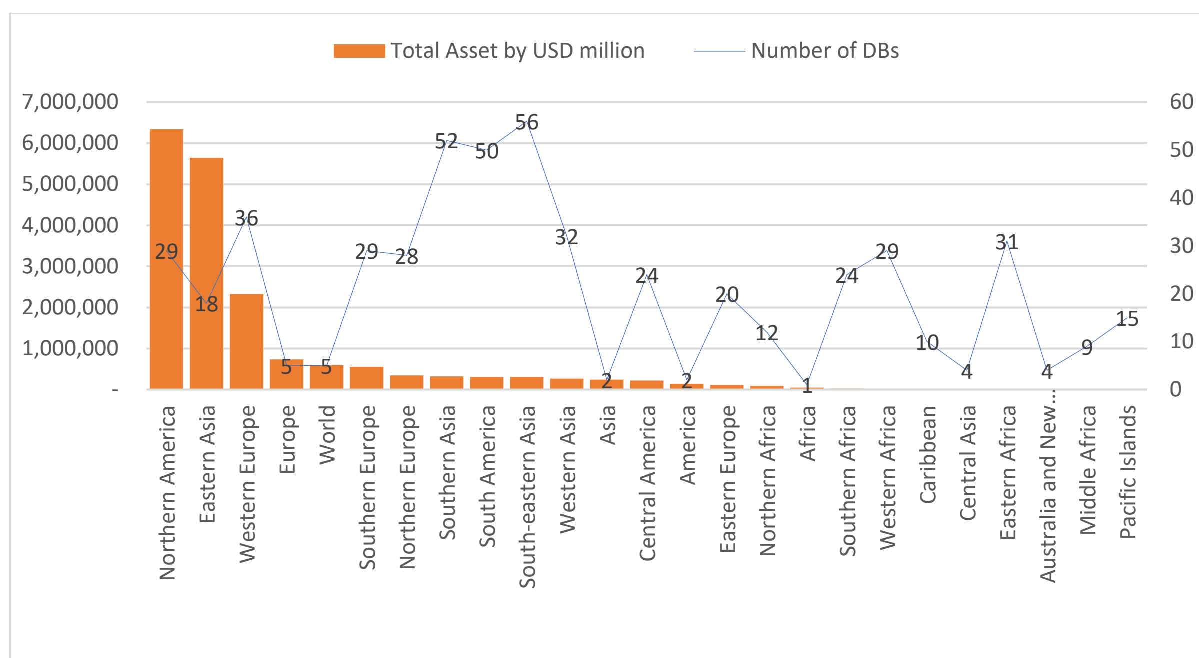
Table 2: Share of development banks in total manufacturing investment between 1970 and 1990

Country	1970	1980	1990
Thailand (Board of Investment)	na	na	45.9
Brazil (BNDES)	11.0	18.7	18.1
Turkey (TSKB. Ind. Dev. Bank of Turkey)	6.7	na	na
India (All Development Banks)	7.6	16.8	26.0
Korea (Korea Development Bank)	44.7	10.1	15.3
Mexico (NAFINSA)	35.5	11.4	na

Source: Amsden (2001)

Similarly, late industrialisers have used development banks to spur their industrial growth. Chandrasekhar (2016:30) investigated the role of development banks in developing countries such as Brazil, India, South Korea, and China and found that "[development banks] have played a role independent of the kind of industrialisation strategies pursued and irrespective of the extent of industrial and financial regulation". Table 2 above shows that development banks have played a substantial role in the industrialisation of some developing countries, including Thailand, where share manufacturing investment made up 46% in 1990. In sum, development banks are key state institutions that have played a fundamental role in the structural transformation of economies in developed and developing countries alike.

Graph 2: Development banks by assets and number



Source: Author's calculation using a database developed by Xu et al. (2021)

Today, the number and total assets of development banks differ depending on what the authors and data classify as development banks. Graph 2 shows that there are 527 development banks in the world with a total asset value of USD 18.7 trillion. It should be noted that this might not be an entirely accurate figure, as the authors of these databases only surveyed approximately 527 development banks. Marois (2021), on the other hand, indicates that as of 2020, there were about 32 000 active public and private banks with USD 281 trillion in assets. Once again, the size and value of these banks depend on what the author counts as development banks. Graph 2 also shows that the largest development banks by total assets are in Northern America, Eastern Asia, and Western Europe. In the Southern African region, South Africa has the largest number of banks, with eight banks with combined assets of USD 50 billion, and the IDC being the largest bank in South Africa by total assets (Xu et al, 2021).

Financialisation of Development Banks

As noted earlier, the micro-account of the financialisation of development banks is missing in the literature. Thus, the discussion in this chapter was prompted by an analytical question of what would the financialisation of development banks look like.

The question is answered using a collation of different strands of financialisation literature. To start, given that most development banks are state-owned institutions, the definition of a financialised development bank relies on Karwowski's (2019) definition of financialisation of the state and its public institutions. Here, a financialised development bank would be one that (a) adopts financial maximisation motives, (b) embraces and accepts the finance-led accumulation regime, (c) drives and entrenches the financialised logic within society, and (d) actively creates new financial instruments that entrench financialised logic in society (Karwowski, 2019).

The first part of the above definition indicates that a financialised development bank seeks profit maximisation. Generally, as discussed in the section, development banks are expected to make limited revenue. Their raison d'etre is to provide funding to risky developmental projects that would typically be underfunded by the financial markets (Xu et al., 2021). Thus, a financialised development bank would go against this logic, seeking to fund projects with limited risk and high return. It would operate towards the end of the spectrum provided in Figure 1, competing with commercial and investment banks. The key indicator, in this case, is the funding and investment strategy of the development bank. It would reveal the investment patterns of a development bank and indicate the extent to which it chooses financial maximisation over its original mandate. Furthermore, the extent to which development banks provide long-term patient capital, as per their original design, is assessed.

The second and third parts of the definition are related and speak to development banks entrenching financialisation in society. Here, a development bank entrenches a financialisation logic if it takes equity in locally listed firms and forms part of investors that demand shareholder value generation. Shareholder value maximisation is a key part of the financialisation literature and refers to a corporate governance model where shareholders are paid high dividends regularly while keeping share prices high (Karwowski, 2022). Shareholder maximisation comes at the expense of productive investment and to the detriment of industrial development (Andreoni et al., 2021; King, 2021). Moreover, shareholder value maximisation pressure has resulted in unsustainable, and short-sighted investment strategies by non-financial corporation. This is exemplified in the South African platinum mining sector (Bowman, 2018). The key indicator, in this case, is the investment and funding strategy whereby a development bank has taken equity in firms that regularly pay dividends.

The fourth aspect of the definition discusses the aspect where development banks actively engage in financial engineering to develop new financial instruments that involve a partnership with private finance. Here, the role of development banks is to de-risk development projects to attract private investors. This forms part of the Wall Street Consensus discussed earlier in this chapter.

Conclusion: Implication for a Financialised Development Bank

Financialised development banks imply the pace of industrialisation and the level of structural transformation that can be achieved. Suppose development banks deviate from the original mandate of providing long-term capital to risky and innovative projects that can result in the creation of new industries as well as boost the existing ones. In that case, policy efforts to industrialise an economy are likely to stall. In addition, the entrenchment of financialisation deeper in the economy by the development banks will indeed produce profound structural transformation but not the kind that is desired by the state. Finance is likely to become a dominant sector within the economy, with manufacturing growth declining in the long term. Thus, it is imperative to investigate the impact of financialisation on development banks. The case study of the IDC is

instrumental in this case, given that it is a development bank that is mandated to support industrial development in South Africa.

Chapter 4: The Case Study of the IDC

Introduction

The purpose of this chapter is to discuss the evidence related to the financialisation of the IDC. As noted earlier in the methodological section, the case study approach is advantageous because it makes it possible to understand financialisation in-depth within a specific context rather than in abstraction. To facilitate this understanding, the chapter is structured as follows: the first section discusses the history of the IDC, its mandate, and its funding model. Here, the aim is to provide an in-depth context and precursor to the discussion of the evidence related to the financialisation of the IDC. The second section delves deeper into three indicators developed in the third chapter to measure the financialisation of development banks. The first indicator analysed is the funding strategy of the IDC. As noted earlier, this indicator is principally designed to measure the extent to which development banks deviate from their mandate of providing long-term concessional finance in favour of short-term financial maximisation. The second indicator discusses the extent to which the IDC is a conduit of financialised behaviour in the economy by assessing shareholder value generation demand. The third indicator looks at the financial innovations from the IDC and seeks to ascertain the extent to which they are linked to financialised imperatives. The third and final section discusses the implications of a financialised IDC on industrial development in South Africa.

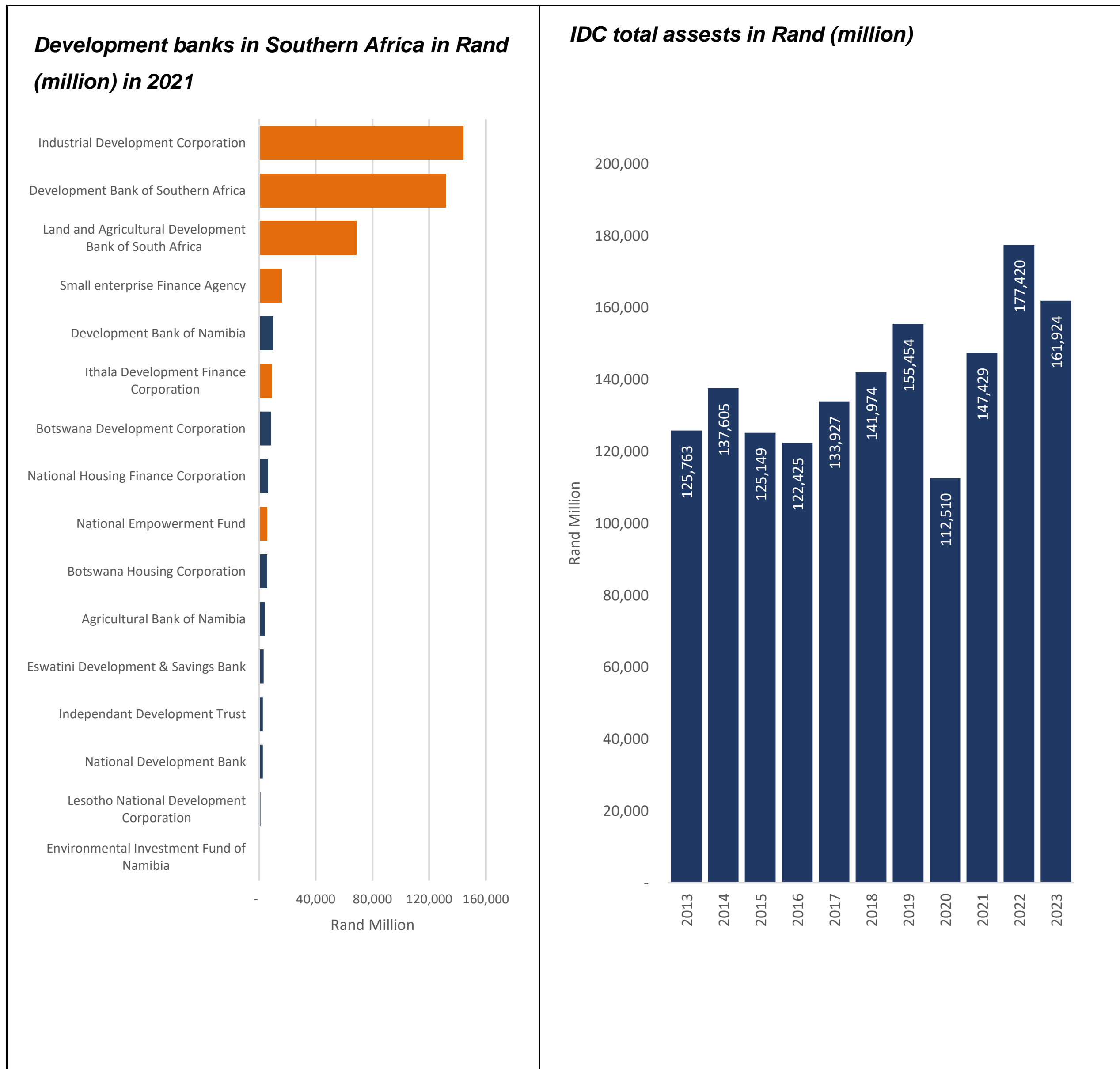
The History and Evolution of the IDC

The IDC is a fully state-owned development bank established in 1940 under the Industrial Development Corporations Act, 22 of 1940. At that time, the mining houses took care of the mining sector, the farming community looked after the agricultural sector, and no institution was solely dedicated to financing the manufacturing sector (De Waal, 1982). The IDC, championed by Dr van Eck and Dr Van De Bijl, was born out of that necessity (Gihwala, 2011). Thus, its raison d'etre has been to provide funding support to South African industrial activities centred on the manufacturing

sector. This purpose is firmly rooted within the Industrial Development Corporations Act 22 of 1940, which indicates that the primary objective of the IDC is “to promote the establishment of new industries and industrial undertakings and the development of existing industries and industrial undertakings” (SA Government, 1940: xi).

In terms of the mandate, the IDC has a narrow mandate in line with the theory of development banks noted in the preceding chapter. That is, it has a range of specific sectors it is mandated to support in the economy. These sectors include manufacturing, mining, agriculture, and tourism (IDC, 2023). Furthermore, the IDC’s mandate has been amended several times in 83 years. The most notable amendment was the expansion of IDC investment activities into the rest of the African continent in 2001 as well as the prioritisation of inclusive industrial development (Qobo & Soko, 2015). Accordingly, between 2001 and 2010, the IDC committed USD 2 billion of funding to 41 projects across 17 African countries (Qobo & Soko, 2015). To improve inclusive industrial development, the IDC has directed a proportion of its funding to black industrialists, women, and youth-owned enterprises (IDC, 2023). In addition, the IDC proclaims that its funding priorities are aligned with South Africa's national policies, including inter alia the National Development Plan (NDP), Industrial Policy Action Plan (IPAP), and the Industry Master Plans (IDC, 2023).

Graph 3: Comparison of Southern African Development Banks with Total Assets of IDC(a)



Source: Author's compilation using IDC annual reports and Xu et al.'s (2021) database. Note (a): Development Banks highlighted in green are from South Africa.

In terms of size, the IDC dominates South Africa and the Southern African development finance landscape. It is the largest development bank in terms of assets. Graph 3 shows that in 2022, the IDC's total assets amounted to R177 billion, accounting for approximately 33% of South African manufacturing Gross Value Added.[2] As noted, the IDC is also the largest development bank in the Southern African region. In the region, it is closely followed by the Development Bank of

[2] Calculation done by the author, with data from Statistics South Africa (2022).

Southern Africa – a South African development bank focusing on infrastructure investment, with total assets of R100 billion (DBSA, 2022). The third largest development bank in the Southern African region is the Land Bank of South Africa, dedicated to funding agricultural activities in South Africa. Combined, these three development banks make up 95% of the total assets of South Africa's national development banks (IDC, 2015). It is important to note that of approximately eight development banks in South Africa, the IDC is the only bank that is dedicated to financing the industrial sector in South Africa.

IDC Funding Model

Although fully owned by the government, the IDC does not receive financial support from the state. Rather, the IDC funds itself in three ways. Firstly, the IDC raises capital from divesting established assets (IDC, 2023). In this case, the IDC would sell off well-established and profitable assets. The proceeds from asset divestment are typically used for equity funding (Goga et al., 2019). Secondly, the IDC raises capital from the domestic and international capital markets. The capital raised in capital markets is used for loan funding. Thirdly, the IDC uses internal profits from its investment activities to raise capital (IDC, 2023). By pooling these resources, the IDC provides business funding through equity or loans. The choice of equity funding is a strategic decision for the IDC, with the bank providing equity funding to established businesses with a record of profitability. The equity funding is informed by the IDC's need for a healthy balance (Goga et al., 2019). The IDC equity funding will be discussed in detail in the next sections of this chapter. In addition, the split between loan and equity funding is not clearly stated by the IDC in its reports; however, Goga et al. (2019) suggests that it is an equal split between the funding types, with slight variations now and then.

The IDC and South Africa's Industrial Development

At its inception in 1940, the IDC prioritised the expansion of South Africa's industrial capacity ensuring that the country could meet its basic supply needs (Jafta, 2017). In the 1950s and 1960s, the IDC was instrumental in funding capital-intensive industries such as Sasol and Foskor, among others.[3] Its focus on capital-intensive industries was largely due to the political climate of that time. The Afrikaner National Party, which took power in 1948, prioritised the development of large-scale strategic projects that were unlikely to be funded by the private sector because of scale (Goga et al., 2019). As South Africa became increasingly isolated from the global economy due to its apartheid policies in the 1960s and 1970s, the IDC prioritised funding import replacement activities in addition to promoting resource-intensive industries to increase export earnings (Jafta, 2017). However, from the 1990s onwards, import substitution proved unviable for growth; thus, national policy shifted towards export-oriented policies (Fumbata, 2016; Jafta, 2017). Industrial policy tools such as General Export Incentive Schemes were introduced to promote exports (Fumbata, 2016). The IDC reoriented its priorities as the policy landscape changed and focused on export promotion. Overall, the IDC played a crucial role in developing and entrenching the Mineral Energy Complex (MEC) under the apartheid regime (Fine & Rustomjee, 1996). The bank funded capital-intensive industries such as basic chemicals, metals, and fuels (Mondi & Roberts, 2005). In addition to supporting major projects in these areas, it had significant shareholdings in South African blue-chip companies, most notably Sasol and Iscor (now ArcelorMittal South Africa) (Mondi & Roberts, 2005).

The post-apartheid era was characterised by two periods. First, it was the early transition from 1994 to 2007, whereby the national economy was dominated by orthodox laissez-faire economic reforms (Zalk, 2014; Fumbata, 2015). At that time, there was no coherent industrial policy besides piecemeal initiatives such as the Motor Industry Development Programme (MIDP) for the automotive industry and the Duty Credit Certificate Scheme (DCCS) for the textile industry (Fumbata, 2015). In this era, the IDC's mandate expanded to include the African continent, SMMEs' development and transformation imperatives, including Black Economic Empowerment (BEE) funding (Jafta, 2017). In 2007, the government developed the National Industrial Policy

[3] Sasol and Foskor are chemical manufacturing companies. Sasol produces fuel components and chemical products, which the company further uses to deliver diesel, petrol, liquid petroleum gas (LPG), and polymers, among other products. Foskor, on the other hand, mines and processes phosphate rock.

Framework (NIPF) – the first national industrial policy, and its implementation plan – the IPAP. The NIPF had the following five objectives: (i) reduce reliance on commodity dependence and diversify the economy; (ii) intensification of South African industrial development and a move towards a knowledge economy; (iii) promotion of labour-intensive industries; (iv) inclusive industrialisation by ensuring greater participation of historically disadvantaged South Africans; (v), contributing to Africa's industrial development (Department of Trade and Industry, 2007). In this regard, the IDC realigned its funding priorities to IPAP, consolidating its support for SMMEs and supporting black industrialists, among others (Jafta, 2017).

Financialisation and the IDC

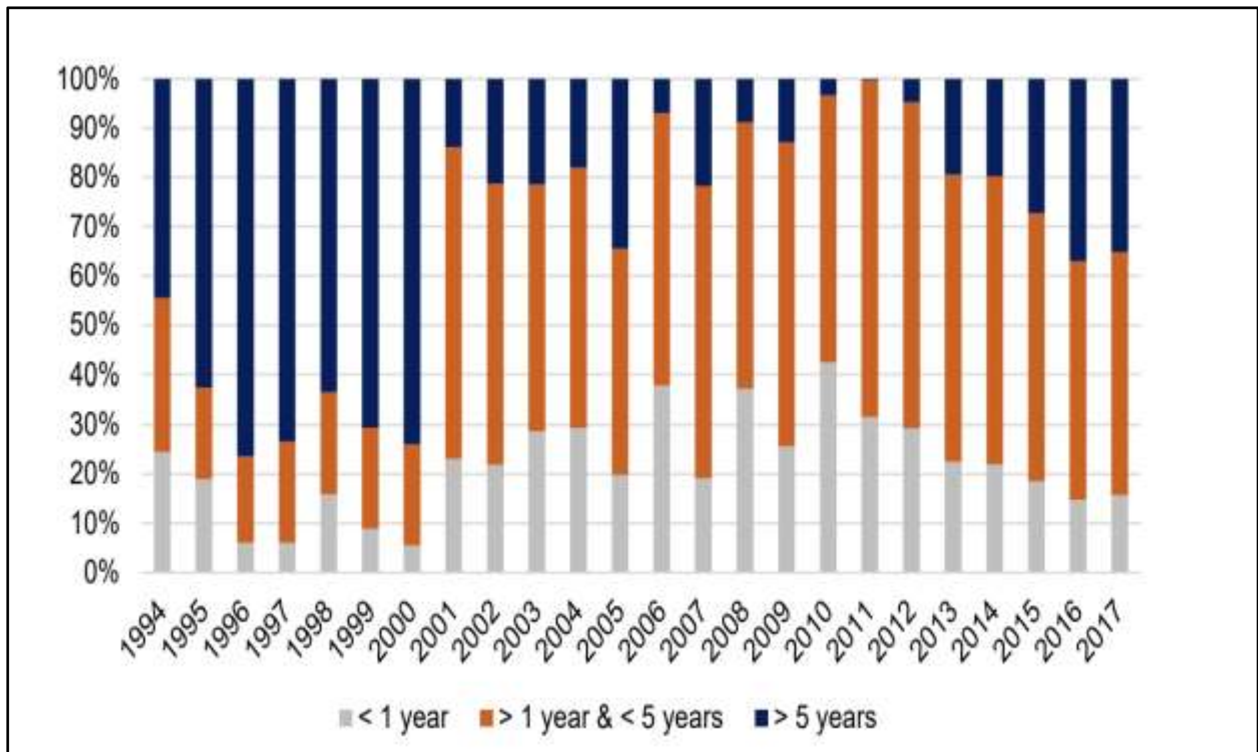
The IDC's funding strategy

As indicated in the preceding chapters, the primary role of development banks is to fill the financing gap left by commercial banks in the market through the provision of concessional interest rates and funding with a long-term maturity period (Gottschalk et al., 2016). More succinctly, concessional finance is key to a successful industrial policy. It allows for the emergence of new industries that are unlikely to be profitable in their infant years. Private sectors would typically not fund these industries because of high risk and low return. However, given the development benefits of having these industries, concessional finance provided by development banks becomes key.

With that said an analysis of the IDC's funding strategy suggests that the IDC does not play this role effectively. Firstly, the IDC does not provide loans with long-term maturity. Graph 4 below shows that most loans offered by the IDC have a maturity of less than five years. The trend of providing short-term loans seems to have intensified from the early 2000s. The reasons behind the provision of short-term loans are related to the IDC's funding model. In this regard, the IDC uses its borrowings from the domestic and international markets to provide loans, while equity funding is mostly pooled from the divestment of mature assets, as noted earlier (Goga et al., 2019). Capital markets are highly financialised and prioritise short-termism and profit

maximisation. Thus, their investment horizons are typically short, forcing the IDC to provide short-term loans to repay the debt in line with capital markets expectations.

Graph 4: IDC loan book by maturity, 1994 to 2017



Source: Data and visualisation adapted from Goga et al. (2019)

Secondly, scholars argue that the IDC's interest rates are not competitive (see Bosiu et al., 2019; Goga et al., 2019; Bosiu et al, 2023). That is, in most instances, the IDC's lending rates are higher than commercial banks, as indicated by some black industrialists (Bosiu et al, 2023). This effectively makes the IDC the lender of last resort, with firms only approaching the development bank when they fail to secure funding with commercial entities. Similarly, the IDC's high lending rates can be partly explained by its funding model. Given that the IDC uses funds borrowed from capital markets for loan funding, the interest rates of loans are associated with interest rates charged to the IDC for borrowing (Bosiu et al, 2023).

It should be noted that the IDC's lending rates are not publicly available, thus it is challenging to ascertain the exact premium that IDC clients pay. However, there is some evidence from research (Goga et al, 2019; Bosiu et al, 2019; Bosiu et al, 2023) which indicates that the IDC's lending rates in certain instances are higher than

commercial banks. For instance, as far back as 2002, the textile federation argue that the "IDC's lending rates are not much different to the commercial lending institutions" in the Parliamentary portfolio committee (Parliamentary Monitoring Group, 2002).

Notably, the IDC does offer low interest rates and longer-term repayment periods on some of its funding schemes. These schemes are called on-balance sheet schemes and are designed to ensure that specific and targeted economic interventions receive subsidised funding (Goga et al., 2019). The IDC funds these schemes through a cross-subsidisation of portfolio assets, using proceeds from equity investment to cross-subsidise its loan books to provide loan funding on concessional rates (Goga et al., 2019). Notably, these on-balance schemes comprised 6% of total IDC funding approval between 2011 and 2017. Therefore, their development impact is minimal (Goga et al., 2019).

Shareholder generation demand and the role of the IDC

Before discussing the evidence related to the IDC, it is important to reiterate the meaning of shareholder value maximisation and more broadly its implications. As indicated in the previous chapter, shareholder value maximisation is a key contour of financialisation. It refers to a shift away from managerial capitalism, whereby firm earnings are retained and reinvested in productive capabilities for further growth, to a shareholder-oriented model, where shareholder value is prioritised (King, 2021). Here, profits are distributed to shareholders in the form of dividends and a rise in share prices. This financialised behaviour is rampant among non-financial firms as they have increased their role in the financial markets as asset holders (Hein & Van Treeck, 2010; Stockhammer, 2010). The key indicators to measure financialisation in non-financial firms from the shareholder value approach include dividend payments, share buybacks, interest payments, and return on equity (King, 2021). Shareholder maximisation comes at the expense of productive investment, thus becoming an antithesis to industrial development.

The evidence presented below suggests that IDC entrenches financialisation to a certain degree in the South African economy. The entrenchment of financialisation in this case is indirect because the bank forms part of shareholders that expect shareholder value maximisation. The IDC has taken equity in some of the largest

companies on the Johannesburg Stock Exchange (JSE). Table 3 shows some listed companies the IDC has an equity share in, including Sasol, Khumba Iron Ore, and Arcelor Mittal South Africa, among others. Notably, this is not an exhaustive list of companies, but it presents an adequate picture of the IDC's investment activities. These are strategic investments for the IDC because they assist the bank in maintaining a healthy balance sheet that attracts lenders and investors.

Moreover, these investments make up a significant proportion of IDC income. According to IDC (2023), top three contributors in terms of dividend income were BHP Billiton with R2.5 billion, followed by Kumba Iron Ore with R1.9 billion and Sasol with 1.2 billion (IDC, 2023). Together, these top three contributors accounted for 22% of the total revenue generated by IDC in 2023.[4] Graph 5 further underscores the importance of dividends income in the IDC's overall revenue. Notably, dividend income as a share of total revenue has been increasing over the years compared to interest income. In 2017, dividend income accounted for 25% of IDC's total revenue, and in 2022, this share has increased to 70%, see Graph 5. In addition, capital growth from the rise of share prices of these non-financial corporations' results in an overall increase of the IDC's total assets. Here, if the share prices of the IDC-listed equities rise due to shareholder maximisation activities such as share buybacks, the value of the IDC's equities also increases, ultimately resulting in an increase in total assets for the bank. In fact, the IDC's asset base increased by 21%, from R144 billion in 2021 to R174 billion in 2022 due to an increase in share prices of both listed and unlisted firms (IDC, 2022)

Table 3: IDC shareholding in major listed firms in South Africa

Company	IDC shareholding (%)	Market cap (Rand)	Sector	Regular dividend payment
Sasol Limited	8.3%	151,33 billion	Basic Materials	Yes
Kumba Iron Ore	12.8%	157,12 billion	Basic Materials	Yes
ArcelorMittal	8.1%	473,2 billion	Basic Materials	Yes

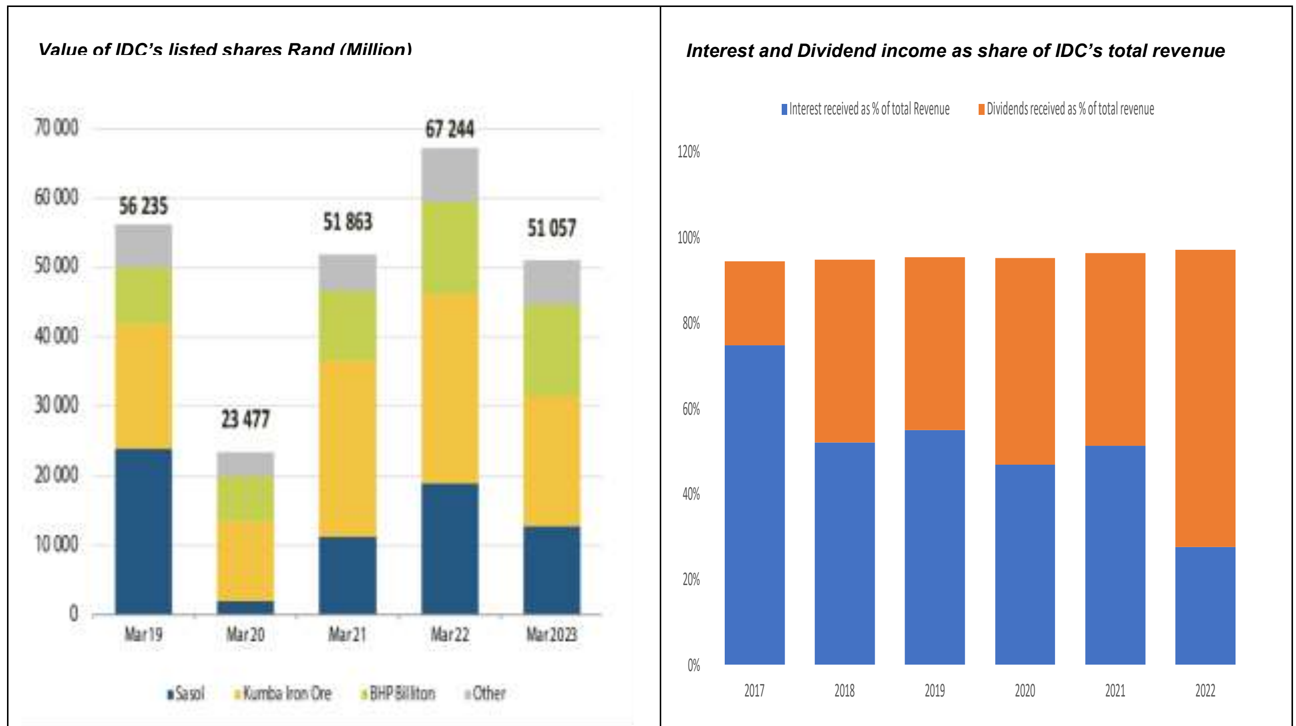
[4] It should be noted that these are just top three companies, and not an exhaustive list of all listed invested in which IDC has an equity share.

Merafe Resources Limited	21.7%	3,1 billion	Basic Materials	Yes
Hulamin Limited	29.1%	1,09 billion	Basic Materials	Yes, last dividend was paid in 2019
York Timber Holdings Limited	28.7%	995,61 million	Basic Materials	Yes
Basil Read Holdings Limited	5.9%	59 million	Industrials	No
WG Wearne Limited	15%	8,29 million	Industrials	No

Source: Author’s compilation using Who Owns Whom data and various reports. Note: this is not an exhaustive list, and the data was collected in February 2022.

The IDC can receive large dividends because it has strategically invested in non-financial corporations that are highly financialised and regularly pay dividends to maximise shareholder value at the expense of productive investment. For example, Sasol is the most cited case of a financialised non-financial corporation in South Africa (Andreoni et al., 2021, 2023). Recently, Andreoni et al. (2023) argued that Sasol faces significant shareholder demand pressure, with the firm continuously distributing dividends and interest income independent of its actual profitability level. In order words, Sasol has maintained dividends payouts to shareholders regardless of whether the firm has been profitable. According to Andreoni et al. (2023), Sasol's profit distributions to its shareholders have risen markedly over the past two decades. Between 2000 and 2009, Sasol distributed 66% of its net income to the financial markets. Furthermore, between 2010 and 2022, the petrochemical giant distributed 106% of its net income to the financial markets, with dividends (53.9%) accounting for the lion's share of distribution (Andreoni et al., 2023).

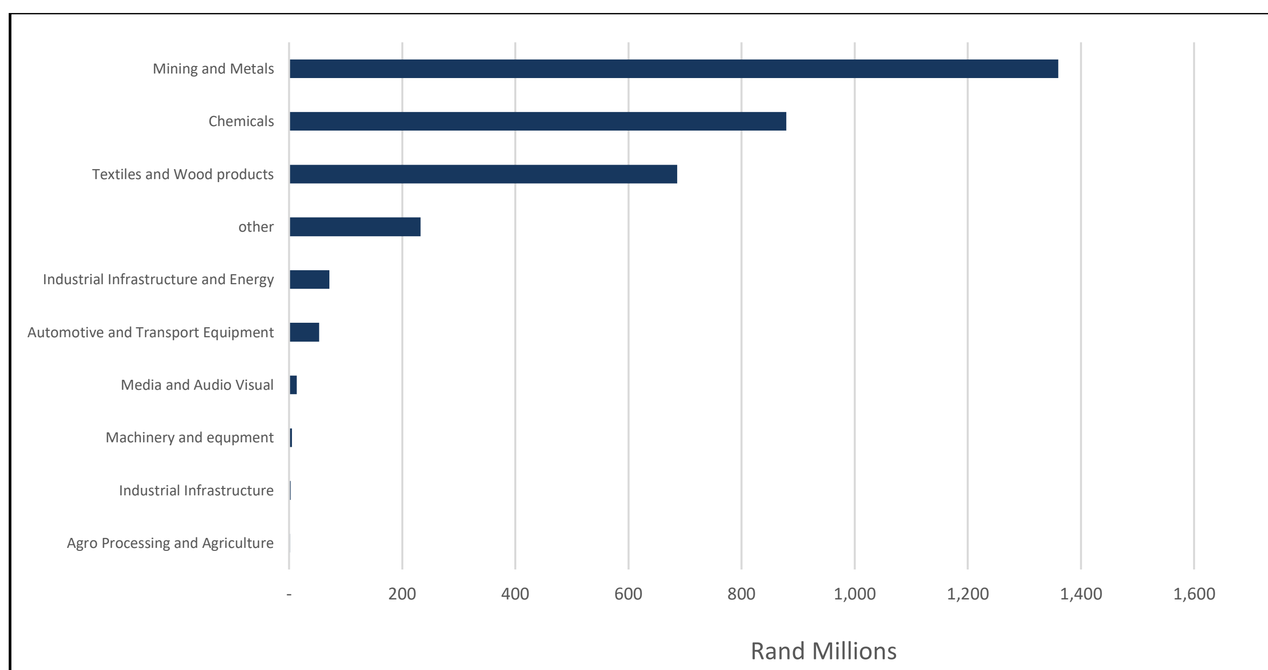
Graph 5: Value of IDC's listed shares in Million Rand and interest and dividend income as share of IDC's total revenue.



Source: The first graph was adopted from the IDC annual report, and the second graph is the author's compilation using IDC annual reports.

It is important to be clear that dividend income and capital appreciation from the listed equities noted above play an important role in enabling the IDC to meet its development mandate. This is especially important in an environment where the IDC must be self-sustainable. However, the IDC can contribute to industrial development while also entrenching financialisation through shareholder maximisation. The two propositions can be true at the same time. This is seemingly the paradoxical nature of the relationship between financialisation and development banks. The active participation and entrenchment of financialisation do not negate the development contribution of the bank. Moreover, there is no plausible industrial development case that can be made as to why the IDC has equity participation in all companies listed in Table 3 except for financial gain. These are large companies with access to a wide range of funding options.

Graph 6: IDC equity participation (in unlisted firms) by sector from 2018 to 2022



Source: Author's calculation using IDC data published on the IDC website. Note: This is not an exhaustive list and not the valuation of IDC unlisted equities.

The financialisation of IDC is further underscored by the fact that the bank continues to make equity investments in primarily well-established upstream sectors in unlisted companies. Instead of using dividends from listed firms noted in Table 3 to invest in diversifying South Africa's industrial structure, it has continued investing in capital-intensive sectors in unlisted firms, see Graph 6. In 2022, the IDC's equities in unlisted shares amounted to R6.5 billion (IDC, 2022). Graph 6 above shows the IDC's funding in unlisted firms in which it has shareholding between 2018 and 2022.[5] The graph shows that mining, followed closely by the chemical sector, accounted for the lion's share of equity funding in unlisted firms for the IDC. Although the IDC does not publicly disclose this information, it is possible that it only provides equity funding to large established businesses that have a long record of profitability.

Financial innovation

[5] The data for this graph was obtained from the IDC website. In terms of the calculation, the IDC does not specifically whether the funding is a loan or equity but does indicate its shareholding value in each funded company. Thus, the value shows firms funded by the IDC in which it has an equity, aggregated by sector.

In terms of innovation of new financial instruments, the IDC has mainly come up with funding schemes related to funding the transition to a low carbon and climate resilient economy (see Table 4 below). In addition, the IDC was the first South African development bank or institution to issue a green bond of R5 billion in 2012 for clean energy infrastructure (National Treasury, 2020). The bond was issued in private placement with the Public Investment Corporation. Since then, the IDC has partnered with the African Development Fund and the German Development Bank to create funding schemes related to climate resilient economy (see Table 4 below for more details on these funds). However, these funds are very small compared to the overall disbursement of the IDC.

As noted in the analytic framework, financial innovations and engineering relate to financial deepening in the financialisation literature. In this regard, a development bank would develop new financial instruments to extract rents for private capital. The bank's role would be to de-risk development projects to attract private capital into development projects. In the case of IDC, the details on the financial innovations are too thin for adequate analysis.

Table 4: IDC financial instruments

Instrument	Description	Amount	Prominent partnership
Green Bond	IDC issued a R5.2 billion green bond to finance clean energy projects, with an expected return of 9%.	R5.2 billion	Public Investment Corporation
ADF Green Fund	With R1 billion allocations, this fund is designed to provide finance to renewable energy and energy-efficient projects in South Africa. Notably, these would be smaller-scale projects.	R 1 billion	

Green Energy Efficiency Fund (GEEF)	This fund is a partnership between the IDC and the German Development Bank (KfW), dedicated to funding self-use renewable energy and energy-efficient projects. According to the IDC, the GEEF provides loan funding from R1 million to R50 million, with an interest rate of prime less than 2% and a repayment period of 15 years.	R500 million	German Development Bank (KfW),

Source: Author's compilation of IDC annual reports

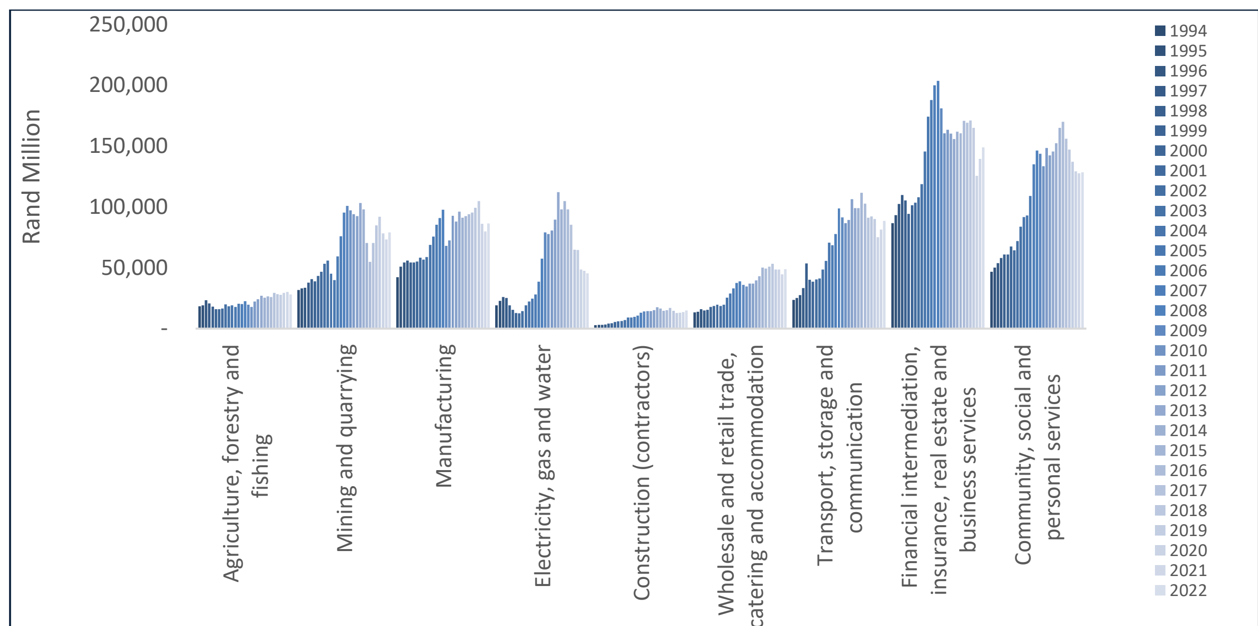
Implications of South Africa's Industrial Development

This chapter has demonstrated that the IDC's investment patterns and funding activities exhibit signs of a financialised development bank. The financialised behaviour of the IDC has adverse implications for South Africa's industrial development. Firstly, as noted earlier, concessional and patient capital is critical to industrial development. Sommer (2021) shows that patient capital increases the probability of firms making productive investments, including investment in innovation and fixed assets, by 5.5%. This is because loans with longer maturity periods and equity are normally used in projects that require long-term capital commitment and thus contribute to productivity growth (Sommer, 2021). With that said, given that the IDC is the only development bank in the country with the mandate to support industrialisation, its inability to largely provide patient capital means that the pace and structure of South Africa's industrial landscape are unlikely to change. Further, without patient capital, the South African economy will remain untransformed. Without low-interest rates and longer maturity of loans, high barriers of entry related to funding will remain in place for most sectors.

Secondly, evidence suggests that the IDC has driven financialisation further by forming part of shareholders that demand shareholder value generation. Instead of being a bulwark against financialised behaviour, the IDC has embraced non-financial corporations that are financialised. As noted earlier, the financialisation of non-financial corporations adversely affects the industrial development and growth prospects of the

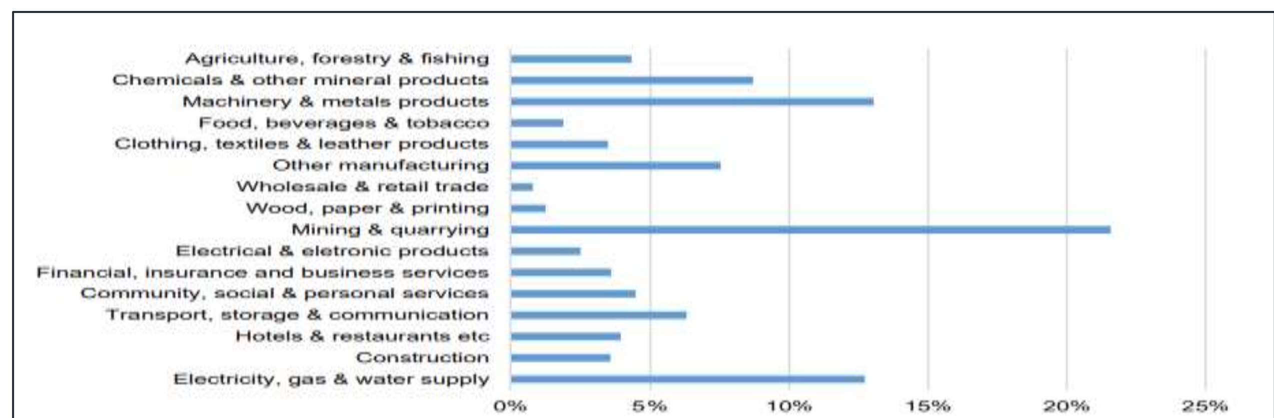
country. The financialisation of non-financial corporations' results in changes in savings and investment behaviour from the long term towards the short term (Ashman et al. 2011). Ultimately, the shifting landscape of accumulation from productive assets towards financial assets is regarded as one of the key drivers of stagnant economic growth in South Africa (King, 2021).

Graph 7: South Africa's gross fixed capital formation from 1994 to 2022



Source: Authors calculation using data from SARB data downloaded from Quantec.

Graph 8: IDC sectoral funding composition (percentage) from 2008 to 2017



Source: Adapted from Goga et al. (2019)

Thirdly, the IDC's funding in listed and unlisted firms remains mostly in the capital-intensive sectors, such as mining, chemicals and metals. While these are important sectors of the economy, the South African government has sought to diversify the

economy away from commodity-dependence and capital-intensive sectors towards more labour-absorptive sectors (Republic of South Africa Government, 2007). These objectives are unlikely to be achieved without adequate funding from key institutions such as the IDC. A comparison between overall gross fixed capital formation and the IDC's funding by sector in graphs 7 and 8 above indicates that there is not sufficient investment going into the manufacturing sector. Graph 7 shows that the overall gross fixed investment is mostly concentrated in the tertiary sector, with the financial sector accounting for the largest share of 22% of total fixed investment, amounting to R148 billion in 2022. Meanwhile, the IDC's funding, as shown in graph 8, has remained in the upstream sectors, with mining, metals, and chemicals accounting for the largest share of the funding. Thus, the objective of diversifying towards labour-absorptive industries is unlikely to be achieved given that there is no adequate funding flowing firstly to the manufacturing sector as a whole, and more specifically to labour-absorptive industries.

Conclusion

This chapter examined the financialisation of the IDC using indicators developed in chapter three. The evidence above suggests that the IDC is financialised. That is, given its self-funding model, the development bank has prioritised financial maximisation. The section above has shown that the IDC does not provide patient capital, and its interest rates are not competitive relative to commercial banks. In short, the IDC, in most of its loans, does not provide concessionary finance. Moreover, it has been shown that the IDC pursues shareholder value maximisation with its equity funding. In this regard, the bank has taken equity in non-financial firms, mostly in the upstream sectors, that are financialised and have prioritised shareholder value maximisation in the form of regular dividends payments and share buybacks. Similarly, in unlisted firms, the IDC has invested in well-established upstream sectors of the economy, such as mining and chemicals.

Chapter 5: Conclusion, Policy Recommendations and Further Research

The purpose of this study was to investigate the impact of financialisation on the IDC's mandate to support industrial development in South Africa. There is a vast amount of literature on financialisation, with scholars focusing on the impact of the phenomenon on various segments of the economy. However, a review of the literature in this study showed that there is little understanding of how financialisation affects development banks. Thus, using a quantitative approach, with the case study of the IDC, the study sought to fill in the abovementioned gap.

To provide an adequate understanding of financialisation in development banks, this study developed a functional definition of financialisation of development banks based on Karwowski's (2019) definition of financialisation of the state. Here, a financialised development bank refers to a bank that has adopted and embedded the financialised logic of profit maximisation in its operations. It is a development bank that has embraced the finance-led regime and actively drives financialisation within society. Moreover, this study has developed three indicators to measure the financialisation of development banks. These include (a) the funding strategy, (b) the demand for shareholder value generation, (c) financial innovation. All these three measures are developed to measure the extent to which a development bank uses its funds to generate more profit at the expense of other development goals. They also measure the extent to which development banks, through their funding model, drive financialised logic in the economy.

The case of the IDC exhibits signs of financialisation. The assessment of the IDC's funding strategy shows that the bank does not provide patient capital, and their interest rates are not very competitive with those of commercial banks. This is mostly because the IDC is self-funded, and uses capital borrowed from the capital markets to provide loan funding. Furthermore, as noted earlier, the IDC indirectly drives financialisation in the South African economy by forming part of investors that demand shareholder value maximisation. Its equity investment has largely remained in the MEC core (Fine and Rustomjee, 1996), thus reproducing the historical structure instead of diversifying the economy as envisioned by the incumbent government. In terms of financial instruments designed specifically for financial deepening, the IDC has mostly come up

with instruments related to green transitioning. The IDC was the first financial institution in South Africa to come up with a green bond in private placement with the Public Investment Corporation. However, the secrecy related to these instruments currently limits the analysis of their potential impact.

The study has shown that a financialised IDC has enormous implications for the pace and direction of South Africa's industrialisation. Thus, it is recommended that the government, as the sole shareholder of the institution, review the self-sustainability model of the IDC. It is recommended that the government provides the IDC with capital that it can use for structural transformation activities. Currently, the Department of Trade, Industry and Competition (DTIC) has different funding activities aimed at supporting industrialisation. These funds could be redirected to the IDC annually so that the bank can ringfence more patient capital and equity funding for labour-absorptive sectors.

Notably, while this study has attempted to address the gap in the literature on the financialisation of development banks, it does not claim to provide an exhaustive account of the phenomenon. Given that this is a new area of the financialisation literature, many questions remain unanswered. Thus, a comparative study between different development banks in different regions needs to be conducted to deepen the understanding of the financialisation of development banks. Moreover, development banks increasingly play a crucial role in climate and Just Transition finance. An extensive inquiry is needed to understand how development banks advance or hinder climate goals in the financialised world.

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