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### UNITED STATES BANK POLICY AND APARTHEID'S FINANCIAL CRISIS

by

Diana Bratcher and Timothy Smith

[Note: This paper, which is issued at the request of the United Nations Special Committee against Apartheid, also contains excerpts from a letter by Bishop Desmond Tutu and the Reverend Beyers Naude on the rescheduling of the South African debt.

Miss Diane Bratcher is the Director of Publications and Editor of the newsletter "The Corporate Examiner" of the Interfaith Center on Corporate Responsibility.

Mr. Timothy Smith is Executive Director of the Interfaith Center on Corporate Responsibility.

The views expressed in this paper are those of the authors.]

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I. EXCERPTS FROM A LETTER DATED 20 OCTOBER 1985 FROM BISHOP DESMOND TUTU, NOBEL PEACE PRIZE LAUREATE, AND THE REVEREND BEYERS NAUDE, SECRETARY-GENERAL OF THE SOUTH AFRICAN COUNCIL OF CHURCHES, ADDRESSED TO MR. FRITZ LEUTWILER, CO-ORDINATOR OF SOUTH AFRICAN DEBT RENEGOTIATIONS

The considered judgement of every synod, assembly and conference of the Roman Catholic and mainline Protestant churches in South Africa (with the exception of the Afrikaans Reformed Churches) has been that the present régime stands in contradiction to the Christian gospel to which the churches seek to remain faithful.

In repudiating and opposing the policy of apartheid, the churches have repeatedly, but to no avail, requested the South African Government to convene a national convention representative of all the people of South Africa.

... Political reform is the concern of the total population of the country and not just the enfranchised few. The new constitution has, instead, entrenched apartheid by extending limited political rights on the basis of racial classification and has become a cause of the resentment and violence now endemic throughout the land. The crisis now confronting South Africa is a direct result of financial mismanagement, social corruption and economic incompetence inherent in the Government's political policy.

Rescheduling South Africa's external debt

The church believes that it is called to a ministry of reconciliation in the world. On the basis of our Christian responsibility and our earnest desire for justice, peace and stability in South Africa, we take note of the debt rescheduling negotiations that are to begin in London on 23 October 1985 under the mediation of Mr. Fritz Leutwiler.

... The implications of the debt rescheduling impinge directly upon areas of our concern, including the dignity of all people, freedom of individual conscience and the rule of law.

We have long protested that the economic system of corporate consent existent under apartheid has resulted in grossly uneven distribution of wealth. There is no freedom or virtue in poverty or squalor and we, therefore, affirm that any viable economic system which hopes to meet the challenge of a new South Africa must both maximize production and ensure a just distribution of profit to the benefit of all the people. ...

... Successful rescheduling of South Africa's debt rests upon the Government's title to national and international legitimacy, which is increasingly uncertain. We reject the arguments of South African Government spokesmen that "technical" aspects of rescheduling should be finalized before consideration of "political" reform since the whole issue of rescheduling is fraught with political implications.

... South Africa is a major trading country with an exceptionally "open" economy, and ... the offshore debt will have to be rescheduled irrespective of which Government is in power. Yet, it is also evident that the longer the crisis in South Africa continues, the greater the chance that the debt will be repudiated either by the present Government or its successor.

#### Rescheduling conditional on political change

The emergency in the country is now such that we consider it necessary, as church leaders, to urge that international and domestic financial leverage be applied to minimize further bloodshed and structural damage. Consequently, we request the banks participating in the rescheduling negotiations to make the rescheduling of South Africa's debt conditional upon the resignation of the present régime and its replacement by an interim Government responsive to the needs of all South Africa's people.

... Such a Government must involve the participation of recognized black leaders and necessitate the immediate release of all political prisoners, the return of exiles and the lifting of banning orders on the African National Congress, the Pan African Congress and other political movements. We offer our services as mediators with other church leaders in the transfer of office to an interim Government.

#### Envisaging a new South African Government

We envisage the return to the "Westminster" constitution and a parliament elected by universal suffrage to sit as a national convention to remodel that constitution. Mindful of the abuses experienced from unchecked parliamentary powers, we recommend that emphasis be placed on separation of powers among the branches of Government and that an irrevocable bill of rights be instituted.

Being cognizant that the South African economy has been stagnant for most of the past decade, it is essential that it begin meeting its potential in a manner that assures the black population that its interests are being served, yet also secures the support of the white population. We are conscious that in a siege economy or one struggling to meet the debt schedule, there will be virtual certainty of continuing social unrest.

"Black" and "Colored" education is inferior, one result being that South African productivity levels are appallingly low. Educational opportunities, particularly technical education, must be improved dramatically as part of the rescheduling process to enable the country to meet the debt schedule.

In encouraging South African economic development and the creation of employment, it would be helpful if the creditor banks directly or indirectly "capitalized" their loans as part of the rescheduling process. Repayment

would, therefore, be provided via dividends from profits on investments. We also ask the assistance of the banks in negotiating access to the European and United States markets for labour-intensive merchandise exports and beneficiated raw materials.

Being conscious that the scourge of wars and divisions amongst mankind conflict with Christian ministry, we urge that the future South Africa, while closely aligned with the West economically, should be neutral ideologically between "East" and "West". We address this plea not only in the hope of reconciliation and peace in this, our beloved country, but also in the prayer that South Africa will yet prove a model to the world of racial tolerance and goodwill.

## II. UNITED STATES BANK POLICY AND APARTHEID'S FINANCIAL CRISIS, BY DIANE BRATCHER AND TIMOTHY SMITH

After months in the throes of political and economic crisis, the South African Government is looking to normalize its relations with foreign Governments and creditors. To avoid further isolation and tightened sanctions, the South African Government hopes to create the impression with its traditional allies in Western Europe and the United States that it has controlled political unrest, that political compromise is underway and that the foreign debt will be repaid. In October 1985, South Africa began repayment negotiations with its foreign creditors. In early March 1986, the South African Government suspended the state of emergency in many areas of South Africa. However, Pretoria has not been willing to share power with South Africa's black majority.

Reports from South Africa indicate that black South African opposition to apartheid has grown relentlessly during the state of emergency. Inside and outside South Africa critics of the white Nationalist South African Government predict that the state of emergency will be followed by more draconian apartheid laws and intensified black South African demands for full political and economic rights.

Internationally the anti-apartheid movement, which includes civil rights groups, churches, colleges and universities, state and municipal Governments, unions and pension funds, has gained unprecedented recognition and support. Even previously reluctant Western Governments, such as the Reagan Administration, and banks like Barclays, one of South Africa's staunchest patrons, have pressed the South African Government for political change. According to United States bank officials, the South African Government was told by a number of banks during recent debt-rescheduling negotiations that political reform was a precondition to regaining Western bank confidence.

With the end of United States lending to the South African Government, attention has turned to lending to the South African private sector. This brief paper summarizes United States bank policies on private sector lending as of March 1986.

### The debt-rescheduling negotiations

February press accounts of the meetings reported that Mr. Fritz Leutwiler, the Swiss mediator for South Africa's foreign debt renegotiations, announced "a broad consensus" between South Africa and its foreign creditors on proposals for repayment of its \$24 billion foreign debt. Enthusiastic South African bankers saw Mr. Leutwiler's "broad consensus" as, in effect, a rescheduling agreement that would lead to normalized relations with foreign creditors. United States banking officials, however, argued that the reports were misleading and insisted that it was an agreement on few points beyond creation of a mechanism for ongoing negotiations. The Financial Times (London) reported that 30 creditor banks, accounting for 70 per cent of South Africa's foreign debt, would form a technical committee of 12 United States and European banks, together with South African officials, to continue work on a plan. United States banks represented on the committee are Citicorp, Manufacturers Hanover Trust and J. P. Morgan.

### Political change - a condition for rescheduling and new lending

United States church leaders wrote to the chairmen of major United States banks recommending that they halt all future loans and that political reform be a condition of any rescheduling plan. Nobel laureate Bishop Desmond Tutu, the Rev. Allan Boesak, Head of the World Alliance of Reformed Churches, and the Rev. Beyers Naude, Secretary-General of the South African Council of Churches, proposed several political conditions for an agreement, including the resignation of the current whites-only South African Government. In a letter to the Rev. J. Andy Smith III of the American Baptist Churches, Hans H. Angermueller, Vice-Chairman of Citicorp, described the bank's opinion of the South African political situation, a view shared by numerous United States and British financial institutions:

"On 30 August Citicorp's Chairman John Reed met in New York with Mr. Gerhard de Kock, Governor of the South African Reserve Bank. Mr. Reed made clear that - in his view - the credit problem was political, not financial or economic in nature. He informed Governor de Kock that confidence in South Africa would not return to the global banking community until the Government took forthright action to dismantle apartheid."

### Loans to the South African Government halted

Prior to the civil disturbances of 1985, including the state of emergency declared by the South African Government, most United States banks and financial institutions had already prohibited loans to the South African Government and its agencies. Years of rising pressure from United States anti-apartheid groups including investors, together with the deteriorating political and economic situation in South Africa, forced this change. Belatedly, such lending was legally barred by Reagan Administration sanctions, proclaimed in the summer of 1985 in the face of imminent congressional action.

### United States investment in South Africa has changed

In 1984 South African Finance Minister Horwood revealed that loans to South Africa were becoming of relatively greater importance than equity investments. Moreover, between 1980 and 1984 when United States bank lending to South Africa increased 450 per cent, United States lending to the public sector remained relatively stable. Lending to the private sector accounted for the dramatic increase.

The most dramatic surge came in bank-to-bank lending, which increased 700 per cent between 1980 and 1984. In a spring 1985 meeting with church leaders, Mr. Gerald Muller, chairman of Nedbank, explained two reasons for the surge in United States lending to South African banks. One was the low interest rate charged by United States banks. The second was that South African banks were heavily involved in new lending to South African Government projects and needed United States loans to offset these commitments.

### Back door lending to the South African Government

With so many United States banks refusing to lend to the South African Government and United States Government sanctions prohibiting it, the churches and other anti-apartheid activists have expanded their challenge to include United States lending to South Africa's private sector, particularly bank-to-bank lending. Opponents of bank lending to South Africa have criticized United States banks for failing to anticipate the recent South African banking crisis. The banks are accused of inadequately assessing the instability of the South African political and economic situation and failing to monitor closely the end use of their funds. The Rev. Carol Somplatsky-Jarman, Director of the South Africa programme of Interfaith Center on Corporate Responsibility (ICCR), told the Subcommittee on Domestic Monetary Policy of the United States House of Representatives Committee on Banking, Finance and Urban Affairs, that rising private sector lending by United States banks is "little more than a back door for lending to the South African Government". She explained that "money is fungible" and since the end use of funds lent to South African banks cannot be traced directly, United States lending to South African banks freed funds for South African banks to lend to the Government. The World Council of Churches reported that from mid-1982 until the end of 1984 South African banks had lent \$1,382 million to South African borrowers, up from \$182.2 million. This 658 per cent increase moved South Africa's own banks from number 12 on the list of nations lending to South Africa to number 3.

### Banking crisis

South African banks had grown accustomed to their foreign creditors' practice of automatically rolling over short-term (90 to 180 days), trade-related loans, enabling on-lending to South African customers often at longer maturities. In late July 1985, reportedly citing French economic sanctions and the state of emergency, Chase Manhattan Bank, which had been a major backer of South Africa, decided it would freeze unused credit lines and withdraw its short-term credits as they matured. Other major United States banks immediately decided to follow Chase Manhattan's example and reduce their

short-term South African exposure, estimated to be \$2 billion as of September 1985 primarily to the private sector. South Africa could not meet these obligations and on 1 September 1985 called a moratorium on the repayment of principal on its foreign debt.

Despite efforts to reassure foreign creditors, international confidence in South Africa's political and economic situation continues to erode. In early March 1986, after Mr. Leutwiler's optimistic reports of "a broad consensus" on repayment between South Africa and its foreign creditor banks, Barclays Bank of London publicly announced that it would make no further loans to South Africa until political difficulties were resolved. Barclays Plc., the largest bank-holding company in the United Kingdom, has consistently financed both the public and private sectors of South Africa. Moreover, the London-based bank owns 40.4 per cent of Barclays National Group of South Africa, South Africa's largest bank with about one third of the nation's monetary banking sector assets.

#### Shifting policies on South African loans

One major battle appears to have been won: no United States banks are proposing resumption of lending to the South African Government until apartheid has ended. Also, the United States Government has prohibited all loans to the South African Government. As for lending to the South African private sector, more and more United States banks are linking renewed lending to political change in South Africa. As confrontation continues between the Nationalist South African Government and the black majority and debt-rescheduling negotiations drag on, banks are revising their policies on lending to the South African private sector.

Clearly, for the duration of the moratorium on repayment of principal, foreign lending to South Africa is at a standstill, but a growing number of United States banks, including the Bank of Boston, Bankers Trust Company, the Mellon Bank and Wells Fargo, have decisively announced that they will not renew loans or make new loans until apartheid has ended.

When the moratorium is lifted, however, other banks may extend credit to South African customers. Some banks, such as the NCNB Corporation (previously known as North Carolina National Bank) and Texas Commerce Bank, have said that they limit loans to short-term, trade-related credits.

Others, including BankAmerica, Chase Manhattan, Chemical Bank and Citicorp, have said that they will not lend while the political and economic situation is so unstable, identifying risk and political and economic instability as barriers to renewed lending.

A final group maintains the position that they can best influence political change in South Africa by financing economic growth through loans to the South African private sector, a kind of "constructive engagement" policy, and have not cited political or economic instability as a barrier to lending. This group includes First Chicago, Irving Bank, Manufacturers Hanover Trust and J. P. Morgan.

No loans to South Africa

(a) Bank of Boston

On 25 March 1985, the Bank of Boston, announcing that it was expanding a seven-year-old ban on loans to the South African Government to include loans to the private sector, stated the following:

"The oppressive nature of apartheid has clearly called into question the political and long-term economic stability of [South Africa]. We have publicly declared our abhorrence of apartheid."

"We have no investments, facilities or personnel in South Africa. Our exposure has been confined to trade-related short-term financing under lines of credit for private banks and a few term loans also to private banks."

"The bank has decided to discontinue all remaining lending activity in South Africa. Consequently, no further lines of credit are being extended to private banks in that country and existing loans and lines of credit are being allowed to run off in accordance with this policy."

(b) Bankers Trust Company

In a January 1986 statement to church shareholders Bankers Trust emphasized the destabilizing effects of apartheid on the South African economy and political situation as follows:

"With regard specifically to lending activities to the South African private bank sector, we provide only trade finance and thus are not involved in transactions that may have as their end result a loan to the Government. We have not been involved in bond transactions with South African issuers."

"Bankers Trust Company's exposure in South Africa is entirely to correspondent, private sector banks and is subject to the unilateral standstill announced by the South African Government on 1 September 1985. Since then we have refrained from making any new loans or voluntarily extending our existing exposure. We do not contemplate any new loans or other credit-related activities in South Africa as long as the existence of apartheid continues to impose a destabilizing influence on the social, political and economic environment in South Africa."

(c) Mellon Bank

In a 9 August 1985 letter to ICCR, Mellon Bank (with headquarters in Pittsburgh) stated its policy as follows:

"Mellon Bank is not making any loans to the private sector in South Africa, regardless of whether such entities practice apartheid or not."

(d) Wells Fargo

In a letter dated 11 December 1984 to Mr. John Lind, Executive Director of the California/Nevada Interfaith Committee on Corporate Responsibility, a coalition of Roman Catholic and Protestant religious agencies, Wells Fargo described its South Africa policy as follows:

"Wells Fargo has no loans in South Africa, and we have no offices, investments or facilities in that country. Moreover, our current policy states we are not to make any loans to the Republic of South Africa or to any businesses based in South Africa. Our policy also states we are not to purchase government bonds of the Republic of South Africa."

Short-term lending only

(a) NCNB Corporation

Assistant to the Chairman William A. McGee described the policy of NCNB with regard to South Africa, in a letter dated 22 October 1985 to Dr. Arie Brouwer, as follows:

"In February of this year we announced that no further loans would be made to the Government of South Africa or its parastatals. In September 1985, NCNB announced it is making no further loans to companies in South Africa. For your information, NCNB business in South Africa has been the financing of trade transactions for companies with whom we do business around the world."

(b) Texas Commerce Bank

Mr. N. M. Gaetz, Executive Vice-President and Manager of the International Group, described the Texas Commerce Bank's South Africa policy in a letter dated 13 December 1984 to Mr. Wade Rubick, General Counsel, Christian Church (Disciples of Christ), as follows:

"We do trade financing to support customers' agricultural and manufacturing exports to South Africa. These exports are primarily rice and other agricultural products and mining machinery and equipment. In general, our financing policy is designed to facilitate an existing customer's overseas export business; strategic or military materials are excluded.

"Our criteria on financing to private banks in South Africa is based upon assessment of the sovereign risk, the credit risk of the specific bank and the rate and term of the financing. Such financing is for trade purposes and normally does not have a maturity beyond 180 days. Since this is specific-purpose financing, we are fully aware as to the use of the loan funds. Agricultural products, mining machinery and equipment are the primary items."

Instability a barrier

(a) BankAmerica

BankAmerica (BAC) has long held the view that it is "ethically correct" to lend to the South African private sector. In response to a 1986 church-sponsored shareholder resolution, BankAmerica outlined its South Africa policy in the following terms:

"BAC is not seeking to expand its business in South Africa due to a debt moratorium and other unfavourable economic conditions. We currently have a very modest amount of credit outstanding to a very small number of privately owned banks and companies. ... We have concluded that refusing to lend to the private sector in South Africa would be both impractical and ineffective. Moreover, agreeing to demands that we totally stop lending to private concerns in South Africa would limit our flexibility effectively to manage our global customer relationships.

"Upon a return to improved economic conditions, BAC expects to resume selective lending to the private sector in South Africa. We think it is an ethically correct position to take, because we believe those who would suffer the most from an abrupt withdrawal of capital would be the black majority."

(b) Chase Manhattan

In a letter dated 11 February 1986 to church sponsors of a shareholder resolution, Chase Manhattan stated its South Africa policy as follows:

"The Corporation has established general policies for foreign lending which it believes are in the best interests of the Corporation and its shareholders and does not feel passage of the proposed resolution regarding dealings with particular borrowers would in any way further those interests. Existing policies indicate the Corporation pays strict attention 'to the legal, moral and social implications of all loans and investment decisions on a global basis' and avoids 'business with indistinguishably harmful results'.

"The Corporation's international lending complies with this mandate, and the Corporation monitors the political, social and economic climate in the countries in which it does business so that its exposure in each country will be based on the Corporation's evaluation of the risks.

"With respect to South Africa in particular, the Chase position has been abundantly clear since the late 1970s and is spelled out in a current lending policy that specifically excludes loans that, in management's judgement, tend to support the apartheid policies of the South African Government or reinforce discriminatory business practices."

(c) Chemical Bank

Even before the 1985 banking crisis, Chemical Bank had limited its South African credit to short-term, trade-related loans to the South African private sector. In an officer's report dated 25 February 1986 under an article entitled "Update on South African Debt", Chemical stated its policy on South African lending as follows:

"We do not have offices or investment in South Africa. We have a policy against making loans to private non-banking corporations for their operations in South Africa. Moreover, we do not finance the sale of military or police equipment to South Africa, nor have we engaged in the sale or distribution of krugerrands.

"Chemical Bank has in the past provided short-term finance to private banks in South Africa in support of trade in non-strategic goods. The granting of new trade credit has been suspended during a surveillance period extending to 31 March 1987, in which we intend closely to monitor South African policy and practices.

(d) Citicorp

Citicorp, the only United States banking corporation that has branches in South Africa, has consistently supported "constructive engagement" with South Africa but has halted lending for now due to the repayment moratorium as well as political and economic instability in South Africa. In a letter dated 26 November 1985 to the Rev. J. Andy Smith III, Citicorp Vice-president Hans Angermueller explained the bank's philosophy on South Africa as follows:

"We realize that staying the course in South Africa is unquestionably the more difficult and unpopular policy. But, as John Reed (Chairman of Citicorp) put it recently in discussing the issue, he sees the Christian message as one of "involvement, of interaction and of concern - but not of disinvolvement". Therefore, as long as we can conduct our business and fulfil obligations to our staff, clients and the community according to our performance standards, and while a chance for a peaceful resolution of the conflict remains, we plan to work on the ground to help end the wrongs perpetrated for so long on the black citizens of South Africa."

Citibank Vice-President Wilfred D. Koplowitz described the bank's policy in a letter dated 12 December 1985 to Jennifer Davis, Executive Director of the American Committee on Africa, as follows:

"During the summer we began a programme to reduce gradually our cross-border exposure, i.e., dollar and foreign currency loans outstanding in the private sector. This process reflected our increasingly negative country risk assessment in the face of violence in the townships and related turbulence.

"Despite the underlying strength of its economy and capacity to service its existing external debt, South Africa did not have enough foreign exchange available to handle a concerted request for repayment of principal. The Government declared a temporary standstill on 2 September. Our cross-border exposure was frozen with no repatriation of principal payments possible.

"Citicorp, therefore, is currently not making any incremental dollar or foreign currency loans to private sector borrowers in South Africa. A very small amount of blocked dollars has been relent to existing clients and we continue to lend to private sector clients in rand through our subsidiary."

"Constructive" private sector lending

(a) First Chicago Corporation

First Chicago explained its South African lending policy in a letter dated 17 June 1985 to Mr. Norman Watkins of Chicago Clergy and Laity Concerned as follows:

"The First National Bank of Chicago will extend credit to multinational corporations domiciled in South Africa only if those corporations subscribe to the Sullivan Principles or the European Economic Community Code of Conduct. That is, the corporations must subscribe to equal employment and affirmative action practices that prohibit discrimination against non-whites in South African facilities. Currently the bank's only South African business relationship is a line of credit with another bank to facilitate local transactions with United States-based multinational corporations."

(b) Irving Bank Corporation

In a response to a shareholder resolution sponsored by the Sisters of Charity of St. Elizabeth, Irving Bank explained its policy on South Africa lending as follows:

"The business Irving has done in South Africa has been exclusively with private banks as part of its correspondent banking business. On 31 December 1985, Irving's exposure to banks and other financial institutions in South Africa was \$195 million. In transacting business with such private entities, it has sought to avoid any semblance of supporting apartheid.

"Irving has long held the view that South Africa's credit-worthiness is dependent on its solving the social inequities that divide the country. It is closely monitoring the current situation and any future action in rescheduling or providing new loans will be strongly influenced by resolution of that nation's policy of apartheid, a position Irving has made clear to senior governmental officials and leaders of the business community in that country. Management believes that this posture will better enable it to influence the South African Government than limiting or even cutting off communications which could result from a termination of all future relationships with South African entities."

(c) Manufacturers Hanover Trust Company

In a letter dated 19 November 1985 to Dr. Arie Brouwer, General Secretary of the National Council of Churches of Christ in the United States of America, Manufacturers Hanover stated its South Africa policy as follows:

"Our lending activities have been limited to the private sector where the longstanding policy has been to consider credits only when, in our judgement, they would generate improved circumstances for the population as a whole."

(d) J. P. Morgan

In response to a 1986 church-sponsored shareholder resolution, J. P. Morgan stated its South Africa policy as follows:

"Morgan's directors and management have an obligation to stockholders to conserve and enhance Morgan's assets, including its loans to borrowers in South Africa. While we agree that South Africa must enact fundamental internal reforms, we oppose the proposal to suspend totally banking activity in South Africa. Such a suspension would impair Morgan's ability to manage its existing South African loans in the interests of its stockholders."

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