

CAPE COLONIAL FINANCE*

This paper will attempt to provide a general view of Cape Colonial finance and practice evolved during the period of responsible government from 1873. In so doing it will complement a previous study made of the Cape Bank Act of 1891 which, as was explained, was largely an exercise in capturing a market for Cape Government securities⁽¹⁾. The implications of Cape colonial financial techniques for the balance of payments adjustment mechanism are also considered.

Before any detailed account of Cape finance is provided it is perhaps worth making the following assertions at the outset. Firstly, that a large part of the ordinary business of Cape Government was concerned with the management of the Government owned railway system. Furthermore, the major task of colonial finance was financing the development of the railway system. It may also be noted that a very large proportion of the capital required for railway and other public expenditure was raised in London. Detailed information in support of these statements is summarized in the appendices below.

* This study grew out of an investigation of the Cape Bank Act of 1891. The Bank Act turned out to be mainly an exercise in Cape Public Finance and this much more extensive study followed from it. As in the previous article, access to Mr James A. Henry's notes on the correspondence of the Standard Bank has been most helpful and I must again express my gratitude to Mr Henry. Unfortunately the official records of the Cape Treasury for the period to to have been lost. Heavy reliance has therefore been placed on the superb collection of Merriman papers held by the South African Library in Cape Town. References to the Henry notes are abbreviated as "HSB" followed by the year and page number (e.g. HSB/1891/900). Reference to the Merriman papers are abbreviated as "MP" followed by year and folio number (e.g. MP/1890/118).

Bman Kantar

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The financial orthodoxy of the period demanded that budgets be balanced. While extraordinary expenditure, for example on railways or harbour developments, could be financed by raising loans, ordinary revenues had to be made to meet ordinary expenditures. Reducing government expenditure to match lower revenues seemed no easier then than it is today⁽²⁾. The citizens of the Cape were however very lightly taxed by present day standards. The main source of government revenue, other than railway revenue, was the customs tariff⁽³⁾. The first income tax was only introduced in 1904. It was a slightly progressive tax on individual incomes and the profits of companies⁽⁴⁾. Budgets were balanced in the accounting rather than the economic sense. There was scope therefore for carrying forward deficits incurred in one or more financial years and use could and was made of temporary or permanent borrowing facilities to meet any shortages of cash. Later or better sooner an excess of ordinary expenditure over current revenue had to be made good out of budget surpluses if the all-important credit of the colony was to be maintained.

As Treasurer Walton told the Cape House of Assembly when introducing his tax proposals in 1904:

" . . . The unpopularity of taxation may be increased by times of depression, and I believe the House will agree with the Government that it would not be opportune, and certainly not wise, to pass this deficit in the coming year without making adequate provision for it. States, like men, must pay their way. They must pay twenty shillings in the pound or suffer the result. States which have large responsibilities in the money markets of the world are compelled by common prudence to conduct their business in an honest and straight forward fashion. The government therefore appeals to the confidence of the House to meet this provision by making adequate provision for the expenditure. The expenditure provided for in the estimates is necessary. It may be necessary to economise here and there, but the Government believe it would be impossible without paralysing the machinery of administration to make any great saving in the expenditure . . ." (5)

The colonial borrower could not usefully question the financial orthodoxy though there was some scope for innovation in the methods of borrowing and banking arrangements. The very tangible reward for conforming to the requirements of the financial markets came in the form of cheap loans and high prices for Cape securities on the London Stock Exchange. The terms at which the Cape borrowed even when its economic prospects seemed least promising in the early 1880's were not unfavourable. When its credit stood especially high as it did after 1890, the Cape like other first class financial colonies borrowed at terms that were only slightly more expensive than that available to the British Government itself⁽⁶⁾.

Cape financial practice and policy aspired to, even if it could not always satisfy, Victorian ideals of economy in the use of resources by government. Less government spending was considered in principle to be much better than more and public debt was best avoided.

It is not easy to reconcile these attitudes with Cape Government involvement in the large scale and extremely risky railway business. It was of course no coincidence that the expansion of the railway system by the government closely followed the attainment of responsible government and so financial independence. There was also the example set by some of the Australian governments in assuming responsibility for railway developments. Private efforts at railway building, despite government support,⁽⁷⁾ had ground to an unprofitable halt only 40 miles from Cape Town. The discovery of diamonds promised better rewards but when the decision was taken to extend the line to Kimberley such optimism could not have been justified on commercial grounds. Moreover given the precarious basis of the local economy at the time there was little margin for error. Fortunately for the Cape, promise came to be fulfilled and even more fortunately the later development of the gold fields came to provide a substantial basis for an expanding South African economy

and an economically viable Cape railway system.

On the basis of its financial record, the Cape railway system must be judged a sound investment. The system never failed to cover its direct costs and from approximately 1883 began to cover and more than cover the costs of funds borrowed for railway expansion⁽⁸⁾. If account is also taken of the external benefits provided by the railway system and not reflected in its own accounts, then the railway venture must be counted a substantial economic success.

Railway developments at the Cape were however vulnerable to political rather than economic direction. The North Eastern section of the system emanating from East London was never viable. The Eastern and Western Province sections of the line were more successful. The Cape could not afford much waste and fiscal conservatism was most helpful when it attempted, not always successfully, to determine the expansion of the system on economic criteria⁽⁹⁾ rather than on the basis of parochial pork-barrelling or more grandiose imperial ambitions.

None probably did more to set the tenor of Cape financial politics than John X. Merriman. Merriman was a member of the Cape Legislative Assembly for all but a few months from 1876 to 1910, mostly in opposition but sometime Minister of Public Works and Treasurer and also finally the Prime Minister who took the Cape into Union⁽¹⁰⁾. Merriman's poetical style was eminently Victorian and his model undoubtedly Gladstone. In his budget speeches both as Treasurer and in opposition Merriman took pains to explain and analyse the underlying balance of payments situation of the Cape. With only crude statistics available for gold and specie movements and further complications caused by intra South African trade and with capital plans largely hidden in the accounts of international banks, the calculation of accurate balance of payments accounts was probably impossible⁽¹¹⁾. Merriman's interest in the balance of

payments was out of a mere basic concern for the foreign debt of the colony. The balance of payments deficit after allowance for specie flows represented by definition an increase in the foreign debt of the colony. Merriman held out the increasing size of the official debt as a regular reproach to the Legislative Assembly and to the colony. He did this largely because of a fundamental pessimism about the economic prospects of the region and therefore its ability to ultimately repay debt.

The theory of public finance teaches that the national debt is not a burden one generation passes on to another. The interest receipts of some members of the community at a point in time are the tax liabilities of others. For the community as a whole these transfers net out to zero. The real burden is incurred by the generation sacrificing consumption in order to increase their stock of capital goods.

This analysis however only holds good for a closed economy. There is a burden passed on to future generations if the debt is to be repaid to foreigners. Other things equal, future generations will have to make real savings in order to repay the debt incurred by their grandparents. Other things of course will not be equal and will depend in part on the purposes to which foreign borrowing has been put. Here the careful and useful distinction made by the official Cape statistics between "non-reproductive, partially reproductive and reproductive" works could have been followed through by Merriman and others when analysing the burden of debt. Foreign borrowing by the Cape was perfectly justifiable if the investment proved to be economic in the wider sense of the term, including that is external benefits derived from it. The willingness of foreigners to lend can be taken and was so taken by some Cape politicians⁽¹²⁾ as a sign of their confidence and was a source of pride rather than anxiety.

Financial Procedure

Parliamentary finance procedures at the Cape were based very much on the Westminster model and the techniques applied would not seem to have lagged too far in time behind then, then current Westminster practice. Roseveare has explained in his study of the British Treasury that it was the Exchequer and Audit Department Act of 1866 that then took the Gladstone financial reforms to their "logical conclusion tying together the procedure of estimate, appropriation, expenditure and audit in one coherent system . . ." (13) This Act created the new important office of Comptroller and Auditor General with secure tenure independent of the Commons. Roseveare also indicated that it was only in 1857 that scientific double entry bookkeeping was generally applied in British Government (14).

In the Cape Legislative Assembly a similar system of estimates of revenue and expenditure, votes of expenditure and audit was adopted. Fiscal estimates and proposals were introduced by the Treasurer in a Budget speech before the whole House of Assembly sitting in committee. In his speech and in documents presented to the House, the Treasurer attempted to reconcile differences between actual and estimated revenue and expenditure. Merriman in fact complained that the task of estimating expenditure and revenue was greatly complicated by the unpredictability of railway revenues and expenditure (15). The Cape Railways statistics would seem to bear out the cyclical nature of railway finance (16). The Treasurer, according to his own predilections, would range in his budget speech over the state of the fiscus, the economy generally and the balance of payments.

Ordinary items of expenditure were provided for by votes of parliament while extraordinary items of expenditure, usually of a capital nature, for example, railway, telegraph or harbour developments required acts of the Cape parliament.

The work of the House included a permanent select committee on

public accounts made up of some of the more senior Cape parliamentarians. The committee examined the work of the Auditors General's staff and questioned them on their audit and general considerations of financial policy. The impression the reports of these meetings gives, is as might be expected, one of serious mindedness and earnesty in persuit of Cape Government economy and probity. The 1902 select committee, in paying tribute to the retirement of the first Auditor General at the Cape, Mr C. Abercrombie-Smith, remarked that effective audit at the Cape had dated from his appointment in 1875 and that not very much of an audit had been applied before⁽¹⁷⁾.

The tasks of the Cape Treasurer were greatly assisted by the office of the Cape Agent General in London. The office of the Agent General was created in 1883⁽¹⁸⁾ by the Cape Parliament to take over the tasks performed until then for the Cape by the Crown Agents. Some of the important tasks carried out by the Agent General involved the transmission of the Cape's financial business with the London bankers and the London capital market. Such work would include the arrangements to be made with banks to register and transfer stock and to pay dividends on them. The Agent General also managed the flows of Cape funds between London and Cape Town and took a prominent part in cash budgeting⁽¹⁹⁾. The Agent General kept a very close watch on the capital and money markets and especially of course the prices of Cape securities. He would give advice to the authorities in Cape Town on the timing of new issues and to the size and method of issue. He was responsible for what today would be described as public relations and did what he could to prepare favourable ground with journalists and others for the Cape's financial operations.

Long term borrowing by colonial governments in London could be undertaken, if the colony so preferred, within the terms of the British Colonial Stock Act of 1877. This Act regularised the

procedure for registering and transferring ownership of stock and payments of dividends. Such procedures had to receive the approval of the Commissioners of Inland Revenue. The Act also required that the colonial borrower make perfectly explicit that the British government itself was absolved of all responsibility for the debt. The Act required a statement to this effect on all documents connected with a loan issue⁽²⁰⁾.

The Act offered one major benefit to the colonial borrower complying with its terms. Stamp duties otherwise payable on subsequent transfers of stock from one owner to another could be commuted on the payment by the colonial borrower of 7s6d per cent to the commissioners of the Inland Revenue⁽²¹⁾. This gave colonial stock a similar advantage in the stock exchange to that enjoyed by British consols which also avoided stamp duty.

The Bill was not at all controversial in the Commons or Lords and passed very quickly through all its stages⁽²²⁾. The Bill was introduced by Mr W.H. Smith. Smith's reply to the few questions raised at the Bill's second reading indicates clearly the purpose of the measure

" . . . The Bill would involve no charge on Imperial Revenue. Provision was made that the holders of stock should have the most complete notice that it was to be issued on the security of the colonies only, and that the Imperial Government would be in no way responsible for it . . ." ⁽²³⁾

The Cape Parliament passed the General Loans Act No. 16 of 1881 to enable the Cape to comply with and take advantage of the British legislation. The Cape Loans Act provided, inter alia, for contributions to a sinking fund to be derived from a 1% charge on the general revenues in addition to interest. Act 18, 1883 amended the Loans Act to permit the Cape Treasurer to appoint two or more persons as Sinking Fund Commissioners who were to report on their activities.

The General Loans Act made a distinction between 'Colonial Stock' issued in the Cape and 'Consolidated Stock' issued in London. The market in Colonial Stock was naturally limited. Therefore, the Bank Act of 1891, which required the banks to take up new stock in the Cape in support of note issues, would have disadvantaged the banks should they have wished to sell. The General Loans Act was accordingly amended to allow the transfer of Cape Stock between the Cape and London registers. In moving this amendment, Merriman expressed himself as at a loss to explain why the distinction between colonial and consolidated stock was ever made. (24)

A further institutional development of some importance for colonial stocks took place in 1900. The British Colonial Stocks Acts of 1877 and 1892 and the Trustee Act of 1893 were amended to include Colonial Stocks, so approved by the British Treasury, within the general category of assets eligible for holding by Trust Funds. Other approved assets included British Government stocks and Indian stock issued under the authority of the British parliament and securities issued by the Bank of England, the Metropolitan Water Board, the London County Council and other municipal authorities. Trustees were also permitted to invest in British Railway and coal company stock provided they met certain specified requirements. In the case of railways the company had to have paid a dividend of not less than 3% per annum on its ordinary stock in each of the previous ten years (25).

The first parliamentary attempt to have Colonial Stocks included within the general category of approved securities was made in the Liability of Trustees Bill of 1888. It was proposed that 4% Colonial Stock which stood on the market at a price of £105 or better, or the equivalent of this price for stocks yielding a lower nominal return, should be eligible for purchase by trustees. The relevant clause however was omitted from the Trustee Act and the amended Trustee Act

of 1893 specifically excluded stock issued in terms of the Colonial Stock Act of 1877, together with some other categories.

The Chancellor of the Exchequer in 1891 appointed a departmental committee to consider the 'Question of the investment of trust funds in colonial inscribed stocks'. The committee consisted of members representing the Colonial agents general (Mills was not a member), the Lord Chancellor and representatives of the Treasury, the Bank of England and the Colonial Office. In the instructions to the committee the Chancellor mentioned two points that he thought needed special examination. The first was 'some provision which would enable holders to sue the colonial governments in this country' and secondly 'The maintainance of some standard of credit of the colonial governments as a condition of the admission and inclusion of particular colonial stocks in the trust fund category'⁽²⁶⁾.

The first problem did not apply to colonial securities issued within the terms of the Colonial Stock Act of 1877. However not all colonial securities fell into this category. The Canadian Government had continued to use their own method of registration. Earlier stock issued by the Cape also did not comply and there were some reservations about whether the procedure adopted by South Australia satisfied the requirement.

The departmental committee recommended that all colonial stock be placed in a position similar to that required by the Act of 1877. The committee also attempted to meet the second requirement of them. Their draft bill recommended including within the ranks of approved investments colonial stock for which the colonial governments could be made liable to the judgement of British courts. This would be permissible provided that 'a trustee shall not invest in any inscribed stock yielding to the investor a return on the purchase money exceeding by more than £1 per cent per annum the return yielded by consols'. The relevant price for any such calculation

six months.⁽²⁷⁾

Nothing came of these recommendations until, as has been mentioned, ten years later. The Act of 1900 clarified the issue of the colonial governments' liability in Britain and the British Treasury was given to decide which colonial stocks should qualify for inclusion as Trustee Investments. The Treasury was to advertise such decisions.

Section 19 of the 1877 Act which had required the explicit denunciation of any British financial responsibility relating to a Colonial issue thus became superfluous.

While there was general approval in the Commons for extending the scope of trustee investments to colonial stocks there were reservations about the discretion granted to the Treasury. Mr Haldene remarked

"This Bill proposes to extend the scope of colonial investments in which trustees may invest, and so far this Bill is good, but what I very much demur to is the extent to which the Treasury is made the judge in this matter under this Bill, which I consider is the extension of a bad principle. How can the Treasury usefully supervise the conditions under which colonial stock is deemed to be good or bad. It is all very easy in the case of first class colonies from a trustees point of view, but when you come to deal with other colonial stock what does this hold out? On the one hand there is the Treasury and on the other hand the Trustees, who, I think, would be able to form a much more reliable judgement than the Treasury . . ." (28)

The Sinking Fund and Debt Management

Securities purchased and sold on behalf of the Cape Sinking Fund account and the Post Office Savings Bank proved useful to the Agent General in managing the market for Cape government securities. The Agent General was naturally enough appointed one of the Sinking Fund commissioners. The Agent General, Sir Charles Mills', correspondence with Merriman reveals for example the Agent General in the market buying Cape securities just prior to the £1m. issue of

January 1891⁽²⁹⁾. Mills reported on 5th December 1890 that the Sinking Fund held £75,000 worth of $3\frac{1}{2}$ per cent Cape stock which Mills proposed "without injuring the market price to sell gradually as may be predictable with a slight gain . . ." ⁽³⁰⁾. Mills also told Merriman that ". . . the only danger in this business is insufficient caution in the sale of the stock . . . guarded by careful watch on the market . . . the broker never offers it for sale unless there is strong inquiry for it admitting of the sale of small parcels without depressing the price . . ." ⁽³¹⁾.

Mills' intervention on this occasion, was probably unnecessary for 384 tenders for the $3\frac{1}{2}$ % stock amounting to £4,678,100 were opened. Tenders at £98 received a full allotment and those at £97 19s 6d received about 30% of their application ⁽³²⁾. The Cape in fact floated this particular loan off just in time. It was issued during a lull in the Baring crisis and soon after the long term market became very difficult which complicated Mills' attempts to gradually dispose of surplus stock bought on the Sinking Fund and Post Office accounts. In a letter Mills tells Merriman in May 1891 that "everything from consols to pennywhistle shares is down". The market, Mills thought, was "practically closed to us . . ." ⁽³³⁾

The Cape Auditor General, Abercrombie-Smith expressed reservation about this use of the Sinking Fund. He found it difficult to account for such operations and thought

" . . . that the credit of the colony would be greatly injured if an impression were created that purchases or sales of stock and of trust monies held on behalf of the public creditors are ever made for the purpose of affecting the market and not for the only legitimate reason - the best interests of the trust . . ." ⁽³⁴⁾

Mills queried both the Auditor's philosophy and his book keeping. He claimed that such operations on behalf of the Sinking Fund had yielded a handsome profit. Mills calculated that contributions to the Sinking Fund from the revenues between July 1885 and June

1892 totalled £91,277 and that the assets of the Fund at the end of June 1892 amounted to £108,047⁽³⁵⁾. Even though Mills' operations were essentially risky there is no indication that Abercrombie-Smith's reservations came to be heeded.

The Market for Colonial Securities

Cape securities were considered on the London Stock Exchange as part of an important group of fixed interest redeemable securities described generally as colonial stock. The prices of a large number of colonial securities were quoted daily in the "Times" and weekly in the "Economist" amongst other newspapers. Included in such a grouping in 1890 was stock issued by the Australian and Canadian states, Canada, New Zealand and Natal. Indian government stock, an important part of the market in fixed interest securities, was generally issued under the liability of the British government and so fell into the category of British securities.

The prices and effective yields of the various colonial issues generally moved together with market sentiment though the ranking order of prices and yields could alter as different circumstances affected the credit rating of the different colonies. In an article on colonial stocks in February 1892 "The Economist" found it

" . . . remarkable and altogether unprecedented to find Cape stock standing above the best Australian issues . . ."

The Economist went on to explain what it took to be the reasons for this development

" . . . But it is now reported that the Cape has placed £900,000 of her 3½ per cents internally, and that she will therefore not come here for the time being. Doubtless this issue will filter through to this market in the course of time, but that will be when London is willing to take it up . . ." (36)

These remarks indicate one of the factors that might affect the credit standing of a colonial borrower. That is the supply of

the colonies securities both on and expected to be put on to the London market. Relative independence of the London market and reliance on savings generated within the colony would be taken as a sign of financial strength. The Economist enjoined colonies to look to their own sources of wealth. For example, an article in March 1890 on "The New Colonial Loans", an improved standing of Cape issues was noted and attributed to the fact that the Cape had managed to restrict its calls on the market in the preceding few years ". . . By so doing the Cape had managed to improve their financial position greatly without obtaining the wholesale assistance of the British capitalist, their present appreciation affords a security which those governments that are constantly obtaining money here cannot be said to give . . ." (37)

These sentiments were conveyed by Mills to Merriman who needed no encouragement of this sort. Mills wrote in January 1891 that "When we came into the market to complete railway extensions to the gold fields we ought to be able to say that after the completion of these extensions, we shall want no more loans, no more money than the reveaige brings in for two or three years at least . . ." (38)

In similar vein the Economist discussed with favour Merriman's Budget speech of June 29th 1892. It commented on at length and with obvious approval Merriman's contention that the Cape was "over governed". "Over government" in the Australian states, Merriman saw as the basic reason for their financial problems. Merriman most characteristically wrote to Mills in October 1892 as follows

". . . I quite agree with you in your view of the doings of our Australian friends and the effect of those doings on our credit. The fact is that they are over governed and that consolidation and retrenchment are wanted. Their resources are enormous if properly applied, but if they go on trying to keep up the present inflation a crack must come. What a benefit has the inevitable pressure been to New Zealand. What a

benefit the hard times of 84-87 were to us. It is really in times of inflation and prosperity that a colonial Treasurer must look out. Everyone's hand is against him and people all agree, for the sake of their own interests, to mistake the transient burst of inflation for steady and assured prosperity . . ." (39)

Discussing the significance of large internal loan raised by the Cape Treasury in 1892 the Economist noted that it was "pretty obvious that the floating of the loan at home necessitated an effort that cannot be repeated for some considerable time to come. If more money is to be raised it must be raised in London and Mr Merriman is wise enough to see that the less the colony troubles this market for some time to come the better it will be for its credit"(40)

As is indicated in Merriman's letter, the relationship between the prices of securities issued by the different colonies seemed also to be complementary as well as competitive. What was judged to be the use of unsound financing techniques by some colonies was thought to influence the standing of colonial securities as a whole.

Mills had written to Merriman in January 1891 that "The Australian colonies are deterred from bringing out their loans . . . But of course, the Australian colonies must have loans in the immediate future. Each colony's loan will add to the difficulty of colonial borrowing"(41)

The Economist about this period was extremely critical of some financial methods applied by Australian states and especially Queensland. In particular it disapproved strongly of the practice of issuing short term, two year Treasury Bills, to finance long term projects. These issues the Economist thought had "depressed the market even more than a public issue of inscribed stock . . . (and) . . . shown the impecuniosity of these colonies just the

same." The Economist thought that by these methods colonial borrowing was being reduced to the "low level of South American financial practice".⁽⁴²⁾

Banking Arrangements and the Flow of Funds

The Standard Bank acted as banker to the Cape government both in the Cape and in London. An agreement was reached in 1876 that in return for this custom the bank would deposit £100,000 worth of Cape government securities with the Cape Treasury⁽⁴³⁾. In London the Cape Agent General kept two accounts with the bank, a drawing account and a so-called supply account earning interest.

The Standard Bank was both a borrower from and lender to the Cape through the offices of the Cape Agency General. The Agent General did not feel obliged to use the deposit facilities of the bank in his management of the temporary funds at his disposal. This is indicated in the extract from a letter from Agent General Mills to Merriman reproduced below. This letter may also reflect something of a departure from what had been till then customary practice.

Mills refers to copies of letters

". . . from which it will be observed that the (Standard) Bank expresses its inability to allow a higher rate of interest than $1\frac{1}{2}\%$ below Bank of England rate on the unfixed portion of my supply account balance.

At the present moment it is extremely difficult to obtain profitable employment for short money, but I have succeeded in arranging for a deposit of 50,000 pounds with the Union Discount Company of London for one month from the first proximo, at $1\frac{1}{4}\%$ per cent below . . . Bank rate . . . the company depositing colonial stocks of a like value at the London and Westminster Bank on behalf of the Government as collateral security.

The advantage in interest over that allowed by the Standard Bank is comparatively trifling but I have thought as well that the Bank should understand that the government is not entirely in their hands in matters of this kind . . ." ⁽⁴⁴⁾

A little later Mills gave a statement to Merriman of outstanding Cape short term deposits held in London. It may be seen that

the volume of funds awaiting disbursement could be quite large⁽⁴⁵⁾. The explanation for these sizeable deposits was that the raising of long term funds on the London market was an occasional event which involved amounts of at least one million pounds and often very much more collected over a short period of time. The timing of such issues was highly dependent on the favourable state of the market and the Cape government's place in the issue queue. The spending process was more continuous and ~~one~~ dependent mainly on the pace of railway expansion and deliveries of materials for it. It was however possible for the Agent General to delay payment to contractors if his own cash position was tight⁽⁴⁶⁾.

There is no indication from Merriman's correspondence or elsewhere that the pace of railway development was much influenced by the state of the capital market. There also seems little indication that spending would be delayed to take advantage of temporarily higher short term interest rates in London.

The implication of this observation for the understanding of the balance of payments adjustment mechanism between the Cape and London will be taken up below.

The explanation for this independence of railway and other developments from the state of the long term capital market was the availability to the Cape government of short term borrowing facilities from London banks. The Cape government borrowed against the collateral of Cape stock certificates deposited with the bank. Authority to issue these certificates and to borrow having been previously provided by the Cape parliament. These short term borrowing facilities were more than sufficient for the purpose of tiding the Cape over any temporary difficulties in the long term market. The amounts the Cape did and could borrow in this way were surprisingly large in relation to their ordinary requirements for capital⁽⁴⁷⁾. The Standard Bank itself was not very important

as a source of fund. Mills gave the following explanation of the Cape's relationship with the London banks

"Permit me to point out that there is no arrangement existing with the Standard Bank here, either for overdrafts or for temporary loans. That institution is not available for any such operations. It would have to borrow from the Alliance or other bank any loan or advance we might want, and we should have to pay for a second hand transaction.

The most the Standard was ever able to lend in the hard times of 1883 was £10,000 - when the London and Westminster lent us £800,000; the National and Provincial £540,000 and other banks altogether 3,700,000 pounds on scrip at not more than an aggregate (average) of about 4% interest" (48)

The Crown Agents acted as financial agents for the Cape previously to the establishment of the Agent General's office in London. In May 1882 the Crown Agents reported that the Cape had incurred outstanding short term liabilities to London banks of over 2 million pounds. They therefore recommended going to the long term market for 3 million pounds. They suggested that such a venture would require the services of a leading bank. With the assistance of the Crown Agents an agreement was reached with Baring Brothers and the Cape successfully raised the funds required.

The issue of 4% stock was three times oversubscribed at a price of £95 10s. The Cape Treasurer expressed himself as gratified with the result. The terms of the loan did not however satisfy everyone at the Cape and the arrangements and correspondence with Barings had subsequently to be presented in full detail to the House of Assembly⁽⁴⁹⁾. All in all the critical reaction to the services Barings had provided would seem to have been unjustified. The Cape had done about as well as they should have expected to do and Barings' charges were on balance not more than the going rate. The Crown Agent justified at some length the suitability of the agreement with Barings. The Cape Colonial Treasurer and Prime Minister, W.C. Sargeant, made what he took to be the 'conclusive'

argument

"On the day before the advertisement appeared your four per cents were quoted at 96½% to 97½%, and we were aware that if even so moderate a sum as £50,000 had been forced on the market, purchases could only have been found at a considerable depreciation of that issue." (50)

A £3 million issue was a large one even by the standards of a decade later. Mills for example advised Merriman in 1891 never to go to market for more than £1 million at a time⁽⁵¹⁾.

The Cape transferred its issuing business from Baring Brothers to the London and Westminster Bank in 1883⁽⁵²⁾. The move had probably much more to do with Barings' failure to provide temporary loans for the Cape in 1883 than the argument over the initial issue. Barings is conspicuously absent from the list of banks referred to by Mills as a source of temporary assistance in 1883.

The financial difficulties of 1883 to which Mills refers in his letter were caused largely by the heavy expenditure required to contain tribal rebellions in Pondoland and Basutoland. This expenditure went far beyond the normal range of Cape revenues and consequently the very large volume of short term debt referred to by the Agent General in his letter quoted above was incurred. Notwithstanding this stringency, railway expansion continued uninterrupted. Once again the time soon came for short term debt to be repaid and another long term funding operation had to be undertaken. Consequently loans issues and conversions to the value of approximately £5 million were floated successfully on the London market.

The Market and Imperial Connection

This loan operation according to Mills was made more difficult by the hostility to it of the Baring Brothers, whose banking services the Cape had just previously dispensed with⁽⁵³⁾. The war itself

was damaging to the credit of the colony and the success of the loan seemed to demand extraordinary efforts by the Agent General and the Cape's new banking connections. Andrew Purkiss has suggested that in such inauspicious circumstances any foreign country by contrast could not have borrowed with such facility and that the success of the loan owed much to informal ties and imperial sympathies upon which the Cape was able to call in its hour of need⁽⁵⁴⁾.

This view is debatable and may rely too heavily on Mills' own account of events. Mills' correspondence clearly reveals him to have been a capable servant of the Cape. Nevertheless, the Agent General is probably not the most reliable source of information in such a matter. He shows in his correspondence with his superiors in Cape Town the understandable tendency to exaggerate the extent of the difficulties he faced and therefore the value of his own contributions in solving them.

The Economist in a long article on the Cape's issue of that year while being "startled" by the amount, £4,837,500, of the loan and also noting how regularly the Cape had come to the market was nevertheless surprised at the generous terms the Cape government were offering

"That so large a demand as £4,837,500 would involve some abatement of price was rational enough, but the gap between 4 4s. per cent and 5 2s. is far wider than can well be attributed to this circumstance . . ."

The Economist also thought that the net sum of £17 m. the Cape had borrowed over 10 years was not necessarily alarming or extravagant and that New Zealand had incurred more debt even more rapidly.

". . . as long as the money obtained is usefully and reproductively employed"

By comparison with Australian states the Cape was judged to be lightly burdened but that the weakness of the Cape was political

and not financial. By which the Economist meant "Dutch objections and jealousy and intolerance of English progress . . ." ⁽⁵⁵⁾ For all this the Economist judged the decision to issue at 5% a mistake made by the Cape government and their advisers.

There can be no doubt that the view held generally in the market and elsewhere that the imperial government would itself take major responsibility for the expense of depending or expanding the Empire was an important contributory factor to the credit worthiness of colonial borrowers. It also meant a correspondingly reduced requirement for expenditure of the least reproductive kind. On the other hand, colonial status was neither a necessary nor sufficient condition for a good credit rating on the London market. Colonies, like foreign borrowers, had to be able to prove to the market that they were capable of paying their way. More specifically it would have to be shown that the ordinary revenues of the colony were able to finance ordinary expenditure including of course any interest on debt and gradual repayments of it through a sinking fund. That the Cape would be able to satisfy this requirement was not seriously in question even in the 1880's and the Cape was by no means heavily taxed. The ratio of ordinary revenue to expenditure was quite satisfactory throughout the eighties. This was helped in no small measure by improving returns from the railway system ⁽⁵⁶⁾. In addition the Cape made little further call on the London market until 1889, when finance for further phase in railway development was required ⁽⁵⁷⁾. This abstinence as has been indicated restored the credit rating of the Cape government.

In addition it should be noted that the banking and issuing agency of the colonies was good business for the bankers involved and for which they competed actively. The London and Westminster Bank specialised in this role for the colonies ⁽⁵⁸⁾. In such circumstances one would expect a bank to do as much as it could do to

retain the credit standing of a good or potentially good client, whether colonial or foreign.

Colonial Suspicion

One long standing complaint of the Cape officials was about their London bankers. They did not trust the London banks to serve the colonial as opposed to the banks own possibly conflicting interests. This is clearly illustrated in the Mills - Merriman correspondence. For example, before the Cape select Committee on Public Accounts in 1902 Merriman, after remarking that the London and Westminster were speculators in colonial securities, questioned the Cape assistant treasurer, Mr H. de Smidt as follows

"Is it true that our financial agents have always given us advice to our detriment . . .?"

de Smidt: "I do not know that we have ever wholly accepted the advice of our financial agents. We have fixed a higher rate (price) than we were advised and we have never been unsuccessful . . ." (59)

The Cape officials feared that the market in their securities could be cornered to their detriment by bankers and syndicates. How much justification there was for these attitudes and how much of it reflects the usual ingratitude of the debtor it is difficult to say. It is true as C.A.E. Goodhart confirms that the London commercial banks were very active in the market generally and in issues for which they were responsible (60). There is moreover a clear conflict of interest possible between the bank and the borrower. If the minimum price for an issue by tender is set artificially low as a result of self interested advice by the issuing bank this bank may then enjoy an opportunity to tender successfully at low prices and benefit from the subsequent appreciation of the security. There is also the problem of insider trading. An issuing bank would know before the market of a prospective issue. This would be a factor likely to depress the price of the colonies securities and so encourage the issuing banker to sell ahead of the market. The market for colonial stock in general was a large one and while it would be impossible

for any one bank or group of banks to manipulate the prices of colonial stock in general this would not have been necessarily true of the price of particular colonial issue. The investment portfolios of some of the banks were very much larger than the total debt of the Cape colony for example⁽⁶¹⁾. As has been stated there is no way of knowing if this kind of market power was abused but it is only to note that the Cape officials were very sensitive as to the possibilities.

In his remarkably detailed and perceptive study of the records of the joint stock banks, Goodhart explains that after 1891 the banks turned increasingly to colonial and other fixed interest stocks as an alternative to low yielding consols as a component of their investment portfolios⁽⁶²⁾. Investments generally comprised a large proportion of the banks assets. Holdings of colonial stocks are mentioned in the portfolios of all the banks for which Goodhart provides very full details. Goodhart also points out that it was the banks fixed interest portfolio investment that they considered to be their liquid assets rather than bills. Given the stability of low term interest rates and the well developed market in such securities this is understandable.

One fortunate result of the Cape government's argument with Barings was that the Cape became only remotely involved with Barings during their crisis of 1890-1891. The contract for the domicile of the 1882 £3 million issue was for 10 years. Nevertheless, this did provide the Cape with something of an inside and interesting look at the Baring crisis.

In November 1890 Mills wrote very self satisfiedly to Merriman as follows

"Barings are practically in liquidation - the London and Westminster Bank and Lloyds Bank, which like Barings have gone a long way outside of legitimate banking business by financing brewery and other joint stock companies are spoken on as 'shaky' . . . If ever I did anything for the colony for which I deserve some credit, it was the withdrawal of our financial agency from the house of Baring . . .

Indeed I feel more convinced than ever that all Government financial agencies ought to be in the Bank of England. The sooner this point is considered the better.

We can ~~get~~ our business away from Barings in 1893 or sooner if they don't regain their credit; and from the London and Westminster at twelve months notice . . ." (63)

When the powerful support operation for Barings got underway, Mills became more cautious and told Merriman of the desirability of staying at least temporarily with the new Barings. "Their credit is good and we make them friends rather than enemies."

Merriman did not share Mills' conviction about the advantages of transferring Cape custom to the Bank of England. His own preferences in this matter were revealed to Cecil Rhodes in a long memorandum on Cape financial policy. Merriman compared the advantages and disadvantages for the Cape of different banks. His own view was that the Bank of England would be inclined to be too meticulous and would tend to neglect the special interests of the Cape. Merriman wrote as follows

"The question of a change in the domicile of our loans and our financial agency has been under consideration for some time. The Agent General has more than once recommended that we should as opportunity offered remove our financial business to the Bank of England provided that, that institution was willing to take it over on reasonable terms. Advancing in favour of the step, from a business point of view, that we should gain increased strength, and should be able to get support in times of pressure, which we are not always able to rely on at the hands of our present agents - and he agrees from what I may call the sentimental standpoint, the importance of drawing the financial business of the Empire into one head in an institution which may be said to be becoming more and more an Imperial one.

On the other hand it may be said, and these were some of the considerations that influenced us in selecting the London and Westminster Bank in the first instance, that the Bank of England conducts its financial business on the strictest and that it will not be inclined to show much elasticity in dealing with a colonial customer during one of those periodical fits of colonial depression which the financial public in England indulge in at the most inconvenient times - There will also be some embarrassment in discriminating between various clients of the same description who may want simultaneous accommodation.

It should also be taken into account that in times of severe monetary pressure the Bank of England

has to bear the whole brunt of the strain and may possibly not find itself in a position to afford very generous assistance at the time it would be most needed . . ."

Merriman seemed to favour banking with Rothschilds. He did so with marked reservations about the benevolence of banks in general

"Rothschilds are themselves loan mongers and that they would not forget to squeeze us when we were in their power in much the same way that Baring Brothers acted during 1882-1883.

In this respect they would probably be no better and no worse than the other agencies that we have tried - While on the other hand their commanding financial position and their connection all over the world would give our stocks, if they chose, a currency which they do not, under present circumstances, command when confined to the London market only.

Their well known connection also with other South African enterprizes would seem to give them a kind of personal interest in the credit of the colony which would be wanting in the eminently respectable Bank of England . . ." (64)

Mills took issue with Merriman. He recommended that given the calls the Cape was due to make on the market a change in domicile would be harmful to Cape credit. It would come to be resented by the London and Westminster Bank and so reduce support for future loan operations. Mills argued that such changes of which the Cape had already made two in ten years were ". . . more of less unacceptable and annoying to the Stock Exchange and to the public and therefore to be avoided . . ." Mills repeated his argument for a move to the Bank of England when good opportunity presented itself

". . . Whenever it so happens that the Bank of England is too embarrassed to make advances on any but high terms to its own customers (and it is notoriously more generous to them than to outsiders) all other banking institutions, public and private, will have ceased lending money on any terms . . ." (65)

Despite these arguments the Cape like many other colonies including New South Wales, Victoria, Western Australia, Tasmania and Natal stayed with the London and Westminster. The London and Westminster later merged with the County and Westminster Bank and as the London, County and Westminster

acted as banker for the Union of South Africa.

In his study of the London banks, Goodhart indicates that the London and Westminster often felt obliged to support the market in issued stock it had helped organise. He remarks that the committee book of the London County and Westminster in the 3rd June 1910 included the item ". . . the bank had agreed to take any West Australian stock offered in the market up to £100,000" A later item in the bank records cited by Goodhart refers to the bank covering a tender for Union of South Africa nine months Treasury Bills and that the bank had been obliged to take up £375,000 of the £2,000,000 on offer. There is also a reference to the bank having taken up all of an issue of £600,000 for Mauritius⁽⁶⁶⁾.

These examples do not as Goodhart suggests necessarily reflect the bank assuming the role of a central bank to the colonies but may simply indicate the bank's involvement as underwriter. It does however indicate the large scale on which the bank operated in the market and the market power that Merriman and others were so sensitive about.

Merriman in his memorandum to Rhodes referred to the advantages of a tap issue of colonial stock rather than by way of the tender arrangement

"As a rule a considerable portion if not the bulk of loans so raised (by tender) fall into the hands of speculators . . . who take up large parcels with a view to reselling to the bona fide investors at a profit - of course this is perfectly legitimate and if we are obliged to raise large sums at once, which we have to do if we are under advances to our banker it is probably the only way of getting such relief. But if we anticipate our financial wants, we do not require large sums at once and in fact in a low money market which does not admit of their profitable employment they may be a positive embarrassment. What we really require is a moderate influx sufficient to enable us to meet our monthly requirements. It is worth consideration whether we could not effect this and bring ourselves into contact with the actual investor without the intervention of the middle man by offering a loan for subscription at a minimum either at par or nearly at par . . ." (67)

Mills did not think Merriman's idea very practical or find sympathy for it at the London and Westminster. Nevertheless he soon after reported that British Columbia had successfully floated a loan on this basis. The practice of underwriting loans at a fixed price came to be used on occasion by the Cape⁽⁶⁸⁾.

The Balance of Payments Adjustment Process

The availability and ready use of short term borrowing facilities from the London banks by the Cape and other governments lends further support to the view that the cycles of economic activity in the economies dependent on British capital were led by developments in the borrowing rather than the lending country⁽⁶⁹⁾. Given a satisfactory credit rating the confidence in the future of private, or in the case of railways mostly government, entrepreneurs was the crucial factor determining capital flows, not the temporary state of the long term capital market. The temporary borrowing facilities imply that governments responsible for railway and other developments could ignore the state of the capital market as a factor in the timing of their developments. If the long term capital market became difficult short term borrowing could easily and not very expensively tide them over. There is no indication in the Mills - Merriman correspondence that the state of the long term market actually inhibited the pace of railway development, even when financial circumstances were at their most difficult for the Cape. Some of the Australian states faced much graver financial problems in 1890-1892 and a much sharper fall in the prices of their securities. Nevertheless they seemed to press on with expansion even to the extent of public issues of short term Treasury Bills, a practice which, as has been mentioned, the Economist deplored.

For the capital market the criterion of success and so the credit rating of the borrower would be, as suggested, the rise in revenues and the ability to finance ordinary non capital expenditure. For

the private entrepreneur success would be of course measured by the profitability of the investment earned mostly by way of exports to the developed economies. The role of governments as short term borrowers and lenders in this balance of payments cycle has perhaps been neglected in the literature.

It has been clearly and convincingly explained⁽⁷⁰⁾ that the balance of payments adjustment mechanism for regions attached to the late nineteenth century gold standard was very largely an automatic one equivalent to adjustment process between different regions of a common currency area today. It has been pointed out that the gold standard was essentially a sterling standard. This is clearly true for the Cape colony. The Cape banking system was completely integrated with the British banking system and the London capital market. In most of the countries or colonies dependent on London for capital as the Cape was there was no central bank and no officially held foreign exchange reserves. There was the call money kept by the Cape government in London but these represented funds awaiting disbursement and not held as a precautionary balance.

The precautionary foreign exchange reserves of the region were kept in effect by the region's banks of whom the more important ones usually had their head offices in London. The first line of reserves was gold and silver in the tills of the bank's branches. The more substantial reserve of liquid assets would be earning interest in the London money market. When the balance of payments of the region were in surplus the banks would buy more assets in London in one form or another than they would be selling. The opposite movement would occur when the balance of payments of the region in which they banked were in deficit. The banks would be selling more drafts in London than they were buying. Correspondingly, their portfolio of liquid assets would need to be run down to meet demands made upon them.

The banks might be very happy to meet extra demands for funds from their customers in the colony for the purposes of financing imports by drawing down their balances in London. Usually the rate of return would be more attractive on lending to private borrowers than to other financial intermediaries in London. In effect therefore the banks would be financing a balance of payments deficit by accommodating reductions in their own reserves. The further important point about this process was that the flow of funds was demand led, as were most other capital flows. It was a response to what were considered additional credit worthy demands in the borrowing region. The banks did not and could not easily push funds out to work in the colony even if interest rates in London on their liquid reserves were unattractively low⁽⁷¹⁾.

There was clearly a limit to which the banks would be prepared to reduce their liquid reserves. In the absence of compensating long term capital flows the banks could meet additional demands for funds by rediscounting eligible bills of exchange and by other forms of borrowing in London. There were however also limits to borrowing facilities. Williams has indicated that an abnormal supply of bills from a bank would be noticed in the bill market⁽⁷²⁾. A bank of course could contemplate raising additional equity capital to help finance more profitable business, but this would be very much of an occasional event. If the balance of payments of the region continued in deficit in the final analysis a bank and a group of banks operating within a region would have to cut back their overseas lending in the attempt to increase or maintain cash reserves. If so bank deposits would also contract still further and a painful adjustment to a perhaps sharply allowed money supply would have to be undertaken. It may be interesting to notice in appendix how sharply the supply of bank deposits in the Cape could vary over short periods of time.

The branches of the overseas banks did not always find it easy to adapt their own lending and borrowing in response to the cash reserve preferences of head office. The branches did not find it easy to refuse demands for foreign exchange in the form of drafts on head office. As head office was told if they did so then they would lack bills suitable for rediscounting in the London market⁽⁷³⁾

There were some active steps an individual bank might take to influence its cash reserves position between head office and branches. For example, on at least one occasion the Standard Bank branches, whose cash position was strong at the time, were urged to compete more strongly for sterling bills. The reason for one particular London office request was that 'Randlard' J.B. Robinson had withdrawn a £175,000 deposit with the bank in London and so weakened its position there⁽⁷⁴⁾.

The Cape government's innovation of issuing Treasury Bills by way of tenders called for in the colony proved helpful to the Standard Bank. The General Manager in South Africa asked London Office's authority to tender for Treasury Bills as "opportunity offered and reserves adequate . . ." and that ". . . it was not always practicable to get remittances on England at suitable rates . . . and . . . important to find safe temporary investments of spare funds . . ." ⁽⁷⁵⁾. These remarks indicate the evolution of conditions necessary for the successful development of a short term money market. That is the requirement for a supply as well as demand for short term financial assets. Conditions incidentally that only come to be substantially fulfilled in South Africa after 1949, when the authorities felt the necessity for borrowing short ⁽⁷⁶⁾.

The general manager also made a case for competing for Treasury Bills on the grounds that their issue deprived the bank of interest free deposits ⁽⁷⁷⁾. This is somewhat surprising for as the government bankers it could be expected that the bank would have experienced

a return flow to the accounts of the government with it.

The swings in the flows of funds between London office and local branches could be substantial relative to imports or exports or bank deposits over short periods of time. This is indicated in the item "balances owed to head office" provided by the official banking statistics and is also very clearly revealed in the Standard Bank correspondence. In his report for the first half of 1894 the general manager remarked that the average amount of the capital employed by the bank in South Africa was about £1 million as against less than £100,000 two years previously. This he took as ". . . striking evidence of altered circumstances, of business in this country . . ." ⁽⁷⁸⁾. In 1897 there is a report of a change from a position of £3 million owed by London office to South Africa to one of £673,542 owed by South African branches in London in the space of eighteen months and a change of £900,000 in the final six months of the period ⁽⁷⁹⁾. Similarly in mid 1902 bank funds in London averaged over £5 million while eighteen months later branches were in credit to the extent of £2,840,000 ⁽⁸⁰⁾.

The possibility of being able to rediscount bills was one very good reason why the Standard Bank, amongst other banks preferred bills to bank overdrafts as a form of lending. Bills in general have an advantage for the bank over overdrafts because they represent in principle a more liquid asset than bank overdrafts. Nevertheless, it is no easier for a bank to refuse a line of bill finance without bankrupting its customer than it is to call in an overdraft.

Goodhart has explained that the London joint stock bank did not regard their bills as an especially liquid part of their portfolios and they did not normally require rediscounting facilities ⁽⁸¹⁾.

Nevertheless even in the absence of any need to rediscount, a bill is perhaps better suited from the bank's point of view as a method of financing international trade especially where the purchasing party may not be all that well known. If the bill can be attached

to a specific parcel of goods it clearly provides an additional degree of security for the loan.

Despite the preference expressed on numerous occasions by the London office of the Standard Bank for lending on bills rather than overdrafts the ratio of the Standard and other Cape banks overdrafts to bills increases over the period 1891 - 1909⁽⁸²⁾.

It used to be widely held that the decline of the internal bill in Britain was due mainly to the spread of the branch banking system⁽⁸³⁾. In such a system less reliance needs to be placed on the facilities of a short term money system market and bills to transfer funds between deposit regions short of funds to finance investment and regions with surplus of a savings. With a widely spread network of branches these flows may be transferred within the books of the bank and may not require further financial intermediation. This factor is undoubtedly of importance though from the banks point of view lending covered by bills would still seem to have advantages for the banks. The relative decline of the bill may reveal the preference the banks' customers were able to exercise for overdrafts in a competitive banking system rather than the preference of the banks⁽⁸⁴⁾. This is clearly so for the Standard Bank.

The offices of the Standard Bank in South Africa offered this explanation for the decline in bills, a development about which head office had complained

"Referring to your frequent allusions to position taken up by the Bank's auditors, we think their attention should be drawn to the immense change effected of late years in the character of South African business, owing to the extension of railway and telegraphic communication. Formerly all rates of goods were a six months credit whereas the bulk of such transactions is now a cash basis, and direct importations are the rule rather than the exception. Similarly, produce sent to the coast from up country, and which was at one time drawn against at from 60 to 120 days sight is now also sold for cash and settled for by sight draft or telegraphic transfer. The falling away in the banks purely discount business has thus been unavoidable and

the requirements of the business community are more and more having to be met by granting new secured overdrafts repayable on demand. We allude to the matter because such overdrafts repayable on demand were once rare, and it may possibly be thought that they are now unduly encouraged, whereas their growth is due to causes beyond our control and connected with the changed conditions connected with colonial trade . . ." (85)

The import-export house cum wholesaler was probably the banks' major source of bills good for rediscounting. As indicated in the letter quoted above better communications both reduced the demand for wholesaling services and also led to demand for different kinds of finance. The producer in the interior of wool or ostrich feathers or diamonds et cetera did not need funds to finance the time his output took to get to market. He could instead demand and get cash much sooner. Therefore, as suggested, one source of useful bills dried up. The producer still presumably required funds to finance his costs of goods in production if not in transit. A supplier's credit could serve this need or a bank overdraft to either the supplier or to his customer. In both cases the producer's or the retailer's own bill would unlikely be-eligible for rediscounting and in the circumstances the bank overdraft would naturally replace the bill without great disadvantage to the bank.

A Brief Outline of Fiscal Developments after 1890

As has been argued previously the fortunes of Cape finance were intimately linked to the success of the Cape railways. In 1891 the Cape government came to an agreement with the impoverished Netherlands South Africa Company Railway, who had obtained monopoly rights to railway construction and management in South African Republic. In terms of the agreement the Cape was to finance the construction of a line linking the Cape system with the Reef. The finance required was approximately £900,000 and given the uncertain state of the long term London capital market necessitated the extraordinary efforts to raise the money locally referred to previously. As may be

- 21 -

noticed the De Beers Company under the chairmanship of Prime Minister Cecil Rhodes made an important contribution⁽⁸⁶⁾. This line gave the Cape system first access to the Reef and the absence of active effective competition for the Johannesburg traffic ushered in the halcyon days of the Cape railway system and the Cape Treasury.

Two indications of the relieved state of the Cape Treasury were the Treasury's somewhat off-handed refusals of the banks' requests for more bills in 1895 and the permission granted to the Standard Bank to substitute British Consols for Cape securities in fulfillment of its obligations as government banker⁽⁸⁷⁾.

The Cape Treasurer and Prime Minister, Sir Gordon Sprigg, who was both the immediate successor to and a predecessor of Merriman as Cape Treasurer, took considerable pride in his budget speeches in the achievement of the Cape railways and the high standing of Cape securities on the London market. Sprigg was under no illusions as to the efficiency of the Cape railways. He argued that any private railway company would have been prepared to pay £20 m. for the system, which was roughly equivalent to the debt incurred on the railways behalf. He did not however believe that the railway system should be expected to subsidise the general revenue "He did not think that they should look to their railway any more than they did to their postal and telegraph services as sources of revenue to avoid taxation . . ." ⁽⁸⁸⁾.

Competition from the other railway systems made things more difficult for the Cape after 1898. These developments were responsible for attempts by Merriman, once again Treasurer, to retrench and to attempt to raise an income tax. Merriman's income tax proposals were defeated by one vote in the upper house of the Cape parliament. The war then intervened and by abnormally increasing demands made for the services of the Cape railway served to disguise the fundamentally weaker state of Cape finance. As has been

indicated increased taxation became inevitable and careful economising the general character of Cape fiscal policy in the period leading up to Union.

The income tax of 1904 was accompanied by the reintroduction of an excise tax on locally produced spirits, beer and wine. The excise tax was last applied during the troubles of 1883 and was anethma to the politically influential wine farmers. The mining sector in turn was strongly opposed to an income tax and especially of course to any discriminatory tax on diamond mining. When the budget proposals were made the Treasurer argued that to be fair to both groups it was desirable to spread the burden of extra taxation.

The Treasurer expressed great difficulty in estimating the revenue from the income tax. He estimated a return for the first year of application of some £275,000 including £145,000 from the De Beers Company. His estimate proved remarkably accurate, the actual revenue collected in the first year amounted to some £292,254⁽⁸⁹⁾

In 1908 the rate of income tax was increased⁽⁹⁰⁾.

The study can perhaps best be concluded on a typically Merriman note.

Merriman, as Prime Minister and Treasurer, in 1908 wrote to the Cape Agnet General, Sir Somerset French

"I note what you say about loans but I am not at all anxious to go into the market, the fatal facility of getting money has been our ruin - and people always forget that each million borrowed means an addition of £40,000 to the annual expenditure, with the result that we now have £800,000 more debt expenditure than we had two years ago and most of that money goes overseas . . . imprudent to borrow till we balance"

And finally, a week later, with obvious relish he tells French that

"I have about completed my financial programme £600,000 retrenchment, £1m. taxation and financial expedient. I am looking forward to being the best cursed man in South Africa when the cat gets out of the bag in three weeks time . . ." (91)

The time may be approaching when Victorian fiscal practice becomes fashionable once more and when the main task of government finance is judged to be that of financing government expenditure in a non-inflationary way and not that of attempting to compensate for imbalances originating in other sectors of the economy.

NOTES

1. Brian Kantor, The Cape Bank Act of 1891, unpublished paper.
2. See for example the extracts from a speech by Cape Treasurer Walton quoted below.
3. Customs Revenues as % of total non-railway revenue
4. Details of Income Tax
5. Cape Hansard 1904, p.407
6. Comparison of effective returns from Economist
7. Nature of government support
8. See appendix
9. See Merriman's letter CC Cape Archives
10. P. Lewson, John X. Merriman in Dictionary of South African Biography
11. See John X. Merriman, The Balance of Trade in South Africa, Journal of the Institute of Bankers in South Africa, Vol.II, No.2, May 1905.
12. For example a much less austere attitude was revealed by Sir Gordon Sprigg both a predecessor of and successor of Merriman as Cape Treasurer. See especially Sprigg's budget speeches of 1894 and 1895.
13. Henry Roseveare, The Treasury, The Evolution of a British Institution, Allen Lane, The Penguin Press London 1969. p.139
14. Roseveare (ibid) p.138
15. Memo on Railway Revenues MP/1890/118a
16. See appendix
17. Cape Select Committee on Public Accounts A1 1902 p.vi
18. Relevant Act
19. See Merriman Papers and also the Cape Treasury records, Cape Archives. Also Andrew Purkiss, The Economics of the Imperial Connection, the Case of the Cape 1872 - 1890, unpublished paper.
20. Colonial Stock Act 1877 40 and 41 Victoria Chapter 59 see especially section 19
21. Section 3 of the Colonial Stock Act of 1877
22. The Bill was read for the first time on July 4th and received the royal assent on the 14th August.

23. Hansard 1877
24. Cape Hansard 1892 p.15, see also report of the Assistant Cape Treasurer, Treasury 228 7/12/1891. Cape Archives
25. An act to amend the Colonial Stock Acts 1877 and 1892 and the Trustee Act 1893. Chapter 62, 1900
26. Report of the Departmental Committee appointed to consider the direction of the Investment of Trust Funds in Colonial Inscribed Stocks. C. 6278, 1891, B.P.P. Vol. 56, 1890-91
27. C 6278, 1891
28. Hansard 1900, pp. 969-970
29. Mills to Merriman 5/12/1890 MP/1890/155
30. MP/1890/155
31. MP/1890/155
32. Letter from London and Westminster Bank to Cape Treasury 15/1/1891. T/233/Cape Archives
33. Mills to Merriman, 1/5/91. MP/1891/117
34. Cape Treasury 7/7/1892. MT/2354/Cape Archives
35. T. 235 Cape Archives
36. The Economist, February 13th 1891, p. 213
Mills sent Merriman the following table accompanying the
37. article MP/1891/299a

COLONIAL $3\frac{1}{2}$ % STOCK

	<u>Mean Price</u>			<u>Last Dividend</u>	<u>Redeemable</u>
	<u>1889</u>	<u>1890</u>	<u>1891</u>		
Canada	106	105	103	June	1909 - 1934
Cape	101	98 $\frac{1}{2}$	97 $\frac{1}{2}$	July	1929 - 1949
Natal	100 $\frac{1}{2}$	99	92	June	1914 - 1939
N.S.W.	101	98 $\frac{1}{2}$	94 $\frac{1}{2}$	Sept.	1918
N.Zealand	-	94 $\frac{1}{2}$	93	July	1940
Queensland	101 $\frac{1}{2}$	97 $\frac{1}{2}$	90 $\frac{1}{2}$	July	1924 - 1930
S. Australia	100 $\frac{1}{2}$	97 $\frac{1}{2}$	95	July	1939
Tasmania	100 $\frac{1}{2}$	98	95	July	1920 - 1940
Victoria	103 $\frac{1}{2}$	97 $\frac{1}{2}$	94	July	1921 - 1938

37. The Economist March 22nd 1890, p.363
38. MP/1891/13
39. The Economist August 6th 1892. Also Merriman to Mills, 18/10/92, quoted in Lewson Vol. 2, p.111

40. The Economist August 6th 1892
41. Mills to Merriman 23/5/1891, MP/1891/13
42. The Economist February 13th 1892, p.213
43. Cape Parliamentary Paper, 11th May 1876. SBH/93/965
44. Mills to Merriman 30th July 1889; MP/1889/
45. 26th September 1889. Funds available for disbursement: note from Agent General
46. £100,000 with Standard Bank to 1.10.89 at $\frac{3}{4}\%$ below bank rate
- £ 50,000 " " " to 12.10.89 at $\frac{3}{4}\%$ below bank rate
- £150,000 " " " " " at % below bank rate
- £ 50,000 " " " to 15.10.89 at " " " "
- £ 59,000 " " " at short notice 1% " " "
- £100,000 Union Discount Co. to 1.11.89 at $\frac{3}{4}\%$ " " "
- £ 50,000 " " " to 28.11.89 at " " " "
47. Mills to Merriman 3.10.1890. MP/1890/
48. See below
49. Mills to Merriman 31.10.1890. MP/1890/137
50. Cape Parliamentary Papers; A5 1883
51. Letter to Crown Agents, 7th June, 1882. A5 1883 P.14-17
52. Mills to Merriman 21.11.1890; MP/1890/
53. see also Purkiss (op cit)
54. Purkiss (op cit)
55. The Economist, December 8th 1883, pp. 1429 - 1430
56. See appendix
57. See appendix
58. See C.A.E. Goodhart "The Business of Banking 1891 - 1914", London School of Economics and Political Science, Weidenfeld and London 1972, chap. 8
59. Cape Select Committee on Public Accounts A 1 1902
60. Goodhart (op cit) chap. 8
61. Goodhart (op cit) appendix IV
62. Goodhart (op cit) chap. 8
63. Mills to Merriman MP/1890/

64. John X. Merriman, Memorandum for Hon. C. Rhodes. Financial Agency MP/1891/6
65. Sir Charles Mills 5th February 1891
Report on the Honourable Mr Merriman's Memorandum on Finance MP/1891/209
66. Goodhart (op cit)
67. MP/1891/6
68. See appendix
- 69.
- 70.
71. See the evidence of Mr John Paul Gibson, General Manager of the Standard Bank in South Africa to the Kemmner Vissering Commission of 1925 (U.G. 13, 1925) pp.211 - 212 quoted in quoted in Brian Kantor, The Evolution of Monetary Policy in South Africa, South African Journal of Economics Vol. 39, No.1, March 1971.
72. David Williams, The Evolution of the Sterling System in Essays in Money and Banking in Honour of R.S. Sayers (op cit) p. 276
73. HSB/1891/903
74. HSB/1890/853
75. HSB/1891/887
76. See Brian Kantor, The Evolution of Monetary Policy in South Africa (op cit) pp. 63-65
77. HSB/1891/892
78. HSB/1891/863
79. HSB/1898/1136
80. HSB/1904/1902
81. Goodhart (op cit) p.
82. see appendix. In 1898 the South African General Manager of the Standard Bank gave head office the following analysis of advances

Cape Gov. Debentures and Treasury Bills	980,000
Loan to Cape Government	673,000
Temporary Loan to British S.A. company	111,000
Debentures advances to municipalities and divisional councils	372,000
To collieries	50,000
On Fixed Property	828,000
General advances commercial, agricultural, mining	4,508,000
	<u>£8,155,000</u>