2016-09-26 and 2016-10-03 Compilation from the preparatory notes for Classes 22 and 23 of the introductory course on political economy: 'The evolution of property and how it rules the world'.

These two classes cover the basic features of **companies and shareholding**, as well as **the flow of surplus into the financial economy**.

Pages 1-4 of Robert Charles Clark's *Corporate Law* (1986) on the dominance of the corporate form of organisation was provided to the class beforehand as recommended reading. What we call a 'company' is more commonly referred to as a 'corporation' in the United States.

A detailed history of the 'company' or 'corporation' — in ancient Rome, China, the Islamic world and medieval Europe — is beyond the scope of this course.[1] The term was at first loosely applied to what were really elaborated partnerships, usually of tax-farmers, merchants or tradesmen pooling their resources, and usually dependent on the state. Some towns, universities and religious communities were recognised as 'corporations', able to own property separately from their members. An important stage in the development of the corporate form of enterprise was the rise of royal chartered companies in Europe, such as the English East India Company (1600) and the Dutch East India Company (1602), which were granted monopolies in overseas trade, engaging in warfare and pioneering the imposition of colonial rule.

Clark deals essentially with the United States. At the beginning of the 19th century, the typical business enterprise was a sole proprietorship or a partnership in which a few individuals co-owned the assets of the business, sharing directly in its profits and being directly liable for its losses and debts. As the scale of production for exchange (especially industrial production) expanded, and with it the extent and scale of transportation and trade, a more flexible and potentially much bigger form of enterprise was needed:

> ... the large amounts of money capital needed to launch and sustain large business enterprises must be collected and aggregated into usable pools. Business must solicit investors on a mass scale, not merely by private negotiations with a handful of rich people.[2]

Investors were needed who would play no part in the business itself. They could be geographically scattered, and would leave the running of the company to elected directors. Whereas a partnership has to be dissolved or reconstituted whenever a partner leaves or dies, the life of a company continues indefinitely.

A company, as we encounter it today, is an artificial legal person. Although it commonly has members ('shareholders'), a company is a separate person, with its own assets and liabilities separate from those of its members. In principle, this means that the shareholders cannot treat the assets of the company as their own, and creditors cannot pursue the shareholders for payment of the company's debts.

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[1] See e.g. John Micklethwait and Adrian Wooldrige, *The Company: A Short History of a Revolutionary Idea* (2003), chapter 1.

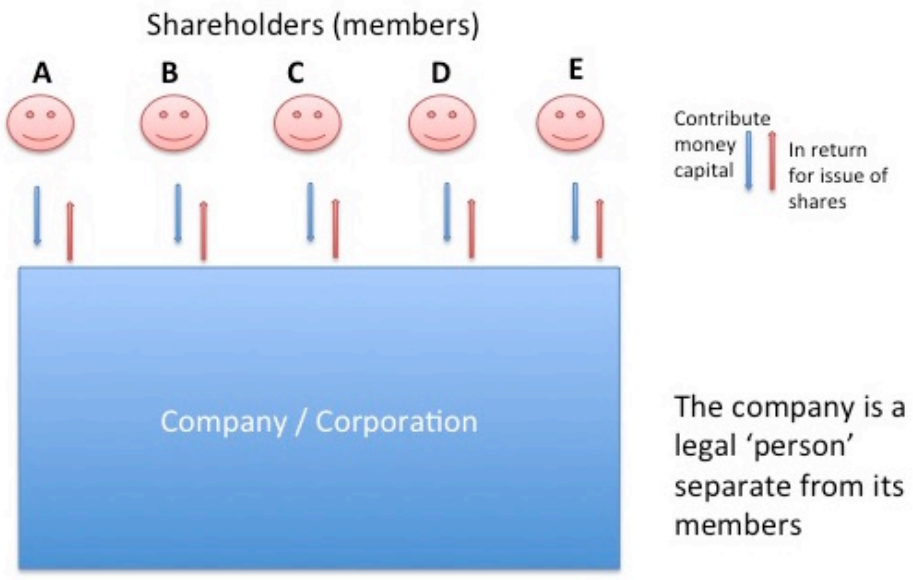
[2] Clark, op cit, p 3.

Shareholders gain from their investment through periodic distributions of profit in the form of dividends, as well as by increases in the market value of their shares if the company succeeds. At the same time they are sheltered from potential losses if the company fails, being limited to the loss of the capital-value that each has invested.

Basic advantages of a company for investors:

1. ***Limited liability for investors.***
2. ***Freedom of shareholders to sell their shares to others (in the case of public companies).***
3. ***Unlimited lifespan.***
4. ***Centralised management by a board of directors, no matter how many investors there are.***

This diagram depicts the basic relationship:



When a company is formed it issues shares to members in return for a capital investment. Later, it may issue more shares to new or existing members in return for more capital. (Sometimes more shares are issued to members in lieu of a dividend, so the company retains the cash — but this is really just a different form of capital investment by the members.)

It is important to note that members (shareholders) may not ordinarily recover their investment from the company itself: they cannot simply decide to return their shares to the company and be paid out. To turn their shares into a cash equivalent, they must find a buyer to take over the shares and pay them out. The share or 'stock' market is the market for the buying and selling of shares. The buyer then takes the place of the seller as member of the company, either directly or through an agent or 'nominee'.

In South Africa, companies are governed by the **Companies Act 71 of 2008.** In terms of section 19(1)(b), a company has 'all of the legal powers and capacity of an individual except

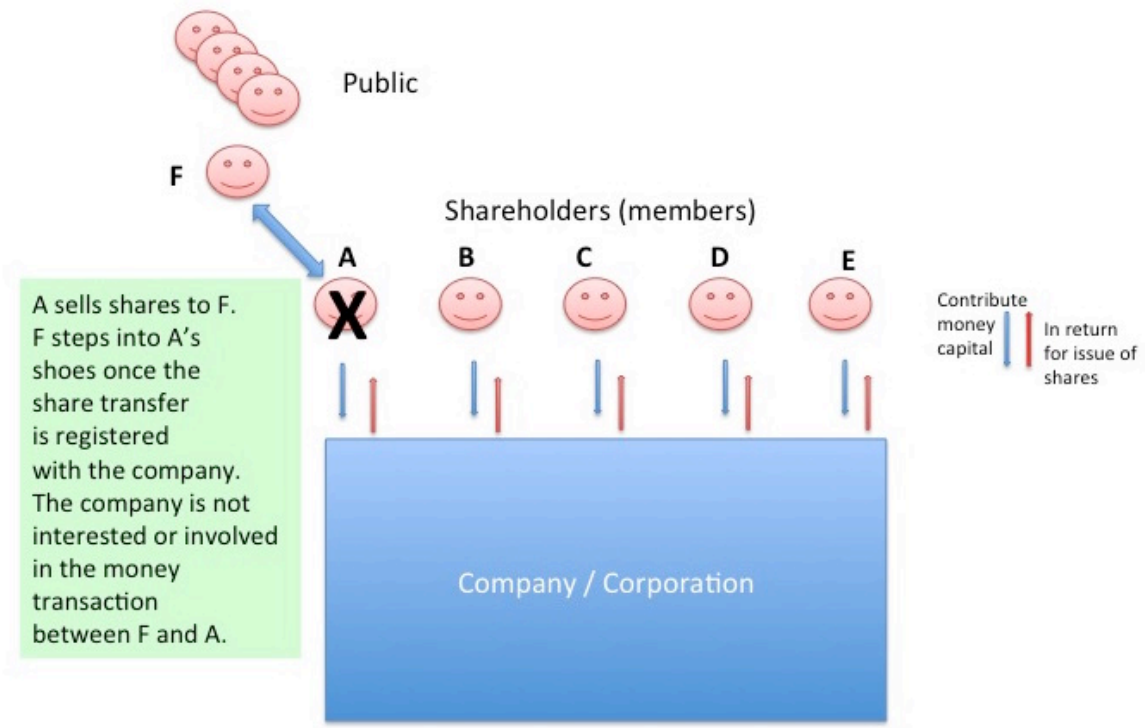
to the extent that a juristic person is incapable of exercising any such power, or having any such capacity', or unless the company's **Memorandum of Incorporation** provides otherwise.[3] (The constitution of a company is called its Memorandum of Incorporation.)

A company (corporation) is thus an artificial legal '**person**', capable of owning its own assets, having its own liabilities, and being able to sue and be sued.

> An '**asset**' is an entitlement, i.e. something owned, or a claim against another.
>
> A '**liability**' is an obligation or debt owed to another.

The Companies Act recognises two types of company incorporated in South Africa: '**profit**' companies and '**non-profit**' companies. We are concerned in this course only with 'profit' companies. The Act also recognises 'external' companies, which are incorporated elsewhere but which operate in South Africa. They are governed to that extent by the Companies Act.

As far as **South African companies** are concerned, there are **four possible types**: (a) a state-owned company; (b) a public company; (c) a private company; and (d) a personal liability company. For present purposes we can leave out state-owned companies and personal liability companies. (The latter are generally incorporated partnerships of professionals, such as doctors or attorneys.)



[3] Section 8(4) of the Constitution of South Africa provides that a juristic person 'is entitled to the rights in the Bill of Rights to the extent required by the nature of the rights and the nature of that juristic person'. The Constitutional Court has held, for example, that the right to property (section 25) applies to juristic persons, as does the right to freedom of expression (section 16) and the right to privacy (section 14, although not to the same extent as natural persons, who are protected not only against unlawful searches and seizures but also in their 'intimate personal sphere'). Juristic persons have long been able to sue for damage to their reputation (as distinct from hurt feelings, which they cannot have) as a result of defamation, whether or not it is proved to have caused actual loss of property, business or prospective gains.

A **private company** is not allowed to offer its shares to the public, and its Memorandum of Incorporation must restrict the transferability of its 'securities' (see below). Thus it is usually suitable for enterprises where the shareholders know each other, and want to keep the business operation to themselves without involving the public other than as customers. Private companies are no longer required to be formally audited. But the potential scale of their business is not restricted.

A **public company** has no such restriction on the offer and sale of its shares. And it must, for example, be regularly audited. To register and get a licence to do business as a bank, or as an insurer, for example, a company must (among other requirements) be a public company.

Under the Companies Act, a 'public company' is simply **a profit company that is not** a state-owned company, a private company nor a personal liability company.

A public company may or may not be listed on the stock exchange. ('Stock' is an old name for shares.) Stock exchanges nowadays are more generally known **securities exchanges**. Thus the JSE changed its name from the 'Johannesburg Stock Exchange' to the 'Johannesburg Securities Exchange'.[4]

The term '**securities**' includes both shares and 'debentures'. When we say that a company is 'listed', this means that securities issued by that company are listed and available for buying and selling on a securities or 'stock' exchange.

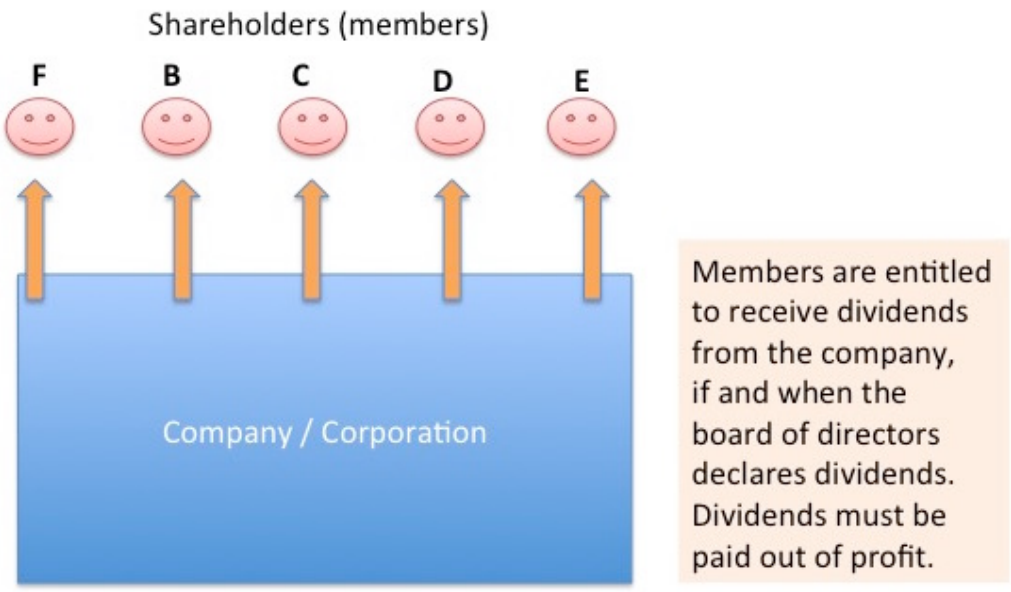
A debenture is a kind of debt instrument which is not precisely defined, but is generally taken to mean an acknowledgement of indebtedness (in other words, an IOU) executed (formally entered into) by the company. A debenture-holder is thus someone who has lent money to the company, irrespective of whether s/he is a shareholder or not. Debentures will vary as to their terms of repayment, interest, and other rights, and may or may not include *security* over the assets of the company. ('Security' means a higher rank or preference in the order of repayment for the particular creditor or class of creditors when the assets have to be sold to pay the company's debts.) Some debentures entitle holders to convert their loan into a subscription for shares. They then cease to be lenders to the company and become shareholders instead. Shareholding in a company means a different kind of risk, and a different kind of possibility for gain, as compared with being a lender to the company.

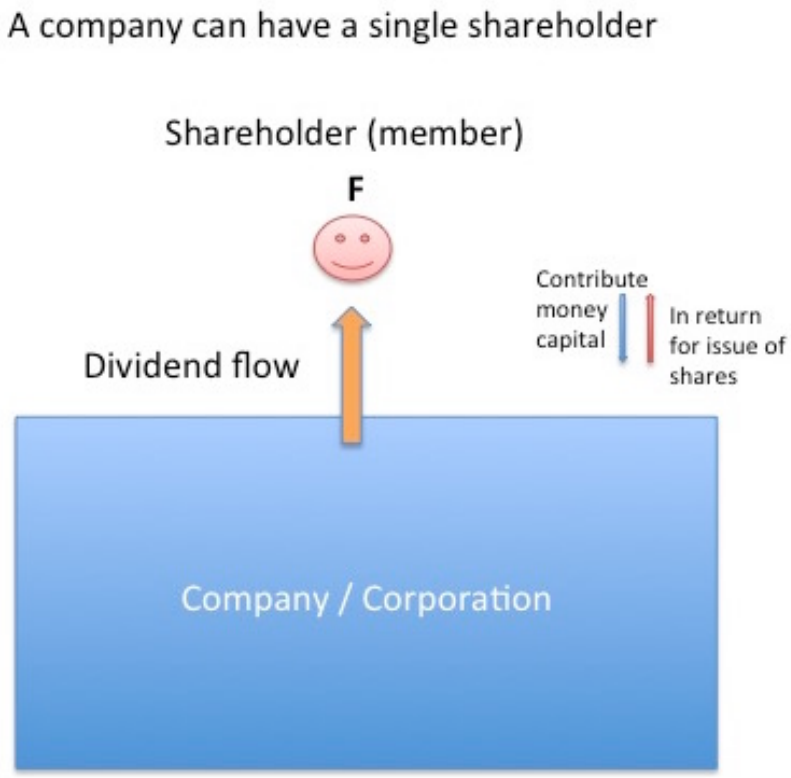
When you read about '**equities**' in textbooks or the financial press, they are generally referring to *shares*. Having 'equity' in a company means having the right to share in profit.

Shares may be of **different 'classes'**, with different rights and obligations attaching to each class. The rights etc within each class must be the same. Typical classes of shares are 'ordinary' and 'preference' shares. A preference shareholder will usually be entitled to receive a dividend before any dividend is paid to ordinary shareholders, and to be repaid first out of any net assets when the company is wound up — i.e. after all liabilities to creditors have been paid. A preference share may be 'redeemable' by the company or non-redeemable, and may be 'convertible' by the shareholder into ordinary shares or not, as the case may be.

[continued on next page]

[4] It is in fact itself a public company, JSE Limited, and the operations of the exchange are regulated by the Securities Services Act, 2004.

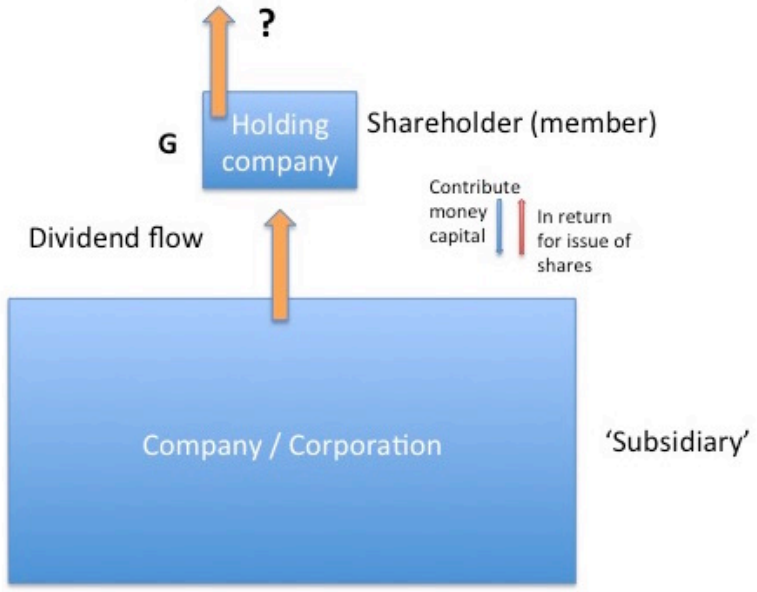


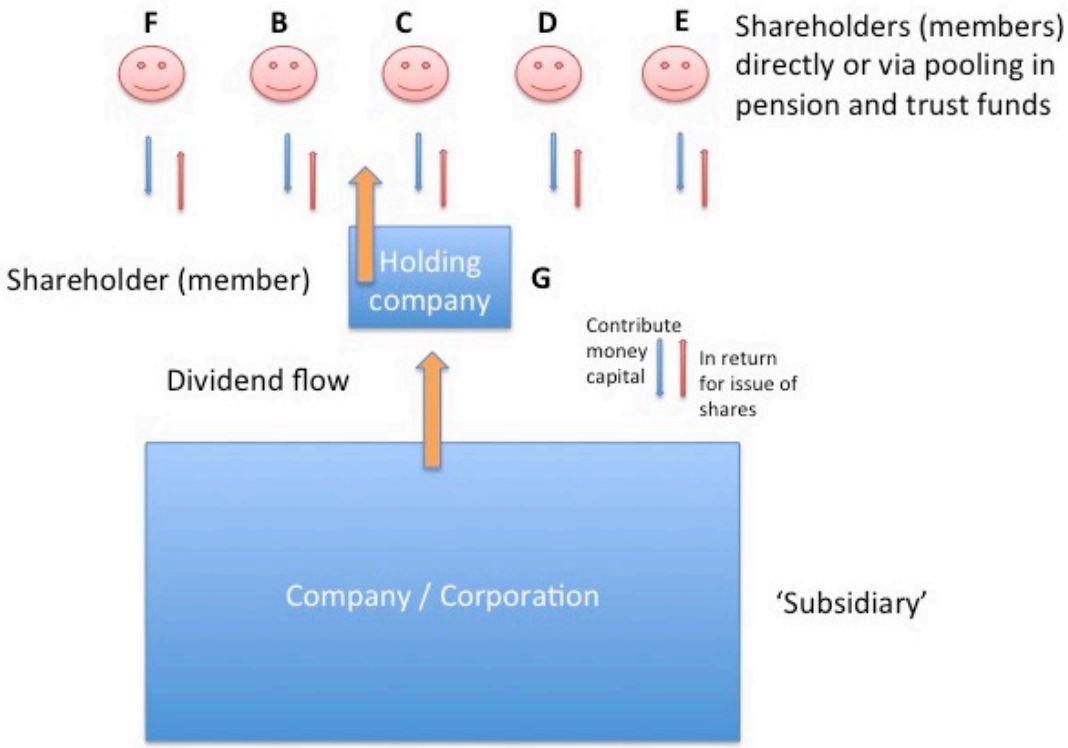


One company can be (and often is) a shareholder in another company — even the sole shareholder. But ultimately there will be human beings entitled to the benefits that are channeled up through hierarchy of companies in a group (either directly as shareholders or via entitlements in pension funds, redeemable units in investment trusts or other forms of financial holdings).

A **company** can own shares (including all the shares) in another company.
This makes it the 'holding company' of the other company

But ultimately human beings hold the interests in the artificial legal 'person' underneath





As an illustration of the global operation of companies, their investments, and their distribution of surplus to their shareholders, let's consider the following report from today's *Cape Times Business Report* (3 October 2016):

A company called **Nepi**[5] is giving its existing investors (shareholders) the choice whether to receive their share of a profit-distribution by way of a cash dividend or by way of additional issued shares.

Nepi readies to hand out new shares to investors

Issue tied to interim dividend

Sandile Mchunu

COMMERCIAL property investor and developer New Europe Property Investments (Nepi) said it was going to issue 2 643 019 new Nepi shares to its shareholders today.

The shares relate to an option the company said shareholders could exercise after realising its half-year results in August.

Shareholder choice

After reporting an increase of 37.61 percent in net operating income to €67.39 million (R1.04 billion) for the six moths to end June at the time, the company declared a dividend of 18.68 euro cents per share. But it said shareholders could either elect to receive the distribution in cash or as an issue of fully paid shares at a ratio between the distribution declared and the reference price.

"The reference price will be determined using a 5 percent discount to the five-day volume weighted average traded price (less distribution) of Nepi shares on the JSE," the group said during the results presentation.

Ian Cruickshanks, the chief economist at the SA Institute of Race Relations, said shareholders had decided to forego the cash dividends and opted instead to reinvest in the company by taking up more shares.

"Shareholders forego short-term dividends sometimes because they want to participate in the future growth of the company. However, they only do that if they believe the company has growth potential. If not they would take the cash and run," Cruickshanks said.

Nepi was founded to acquire, develop and manage regionally dominant retail assets in emerging EU markets with high growth potential.

'Shareholders forego short-term dividends sometimes because they want to participate in future growth.'

The group built an exceptional property portfolio and development pipeline in Romania and Slovakia and is progressing with a retail expansion programme in other target markets.

It said this was consistent with its strategy as it continued to invest in developments that significantly contributed to the growth in distributable earnings a share.

Nepi is pursuing a development pipeline that exceeds €750m (including redevelopments and extensions, estimated at cost), of which €190m was spent by June 30. This is an increase of about €150m compared with last December.

Book build

Before issuing the share option to investors, the company also raised €195m issuing new ordinary shares this year – €156m was raised in the accelerated book build which closed on July 13. As at June 30, the group had €54m in cash, €20m in listed property securities and an additional undrawn revolving facility of €80m.

Cruickshanks said shareholders who decided to take up shares had made a good investment as the property sector was a good place to invest in currently. "Nepi is attractive because of its exposure to foreign currency," he said.

Nepi shares fell 1.11 percent to close at R155.50 on the JSE on Friday.

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[5] According to the Bloomberg website, 'New Europe Property Investment Plc is a commercial property company incorporated in the Isle of Man. The Company focuses on investments in dominant retail assets and offices in Romania with a strategy bias towards long-term leases.' According to the Nepi website, it is listed on the JSE as well as on stock exchanges in Bucharest and London. The shares are interchangeable between these registers. [The information on Nepi and other companies provided in these notes is for illustrative purposes only, and is not intended as an investment assessment or recommendation of any kind.]

What does Nepi do? The information below appears in the August 2016 Nepi company profile:[6]

Profile

INTEGRATED COMMERCIAL PROPERTY DEVELOPER, INVESTOR AND OPERATOR

NEPI is a leading property investment and development group in the CEE, with a highly effective and skilled internal management team which combines asset management, investment, development, leasing and financial expertise.

BUSINESS STRATEGY

Continued above industry growth in recurring distribution per share by:
- Expanding the investment property portfolio via developing, extending, re-developing and acquiring dominant or potentially dominant retail assets in emerging European markets with high consumption growth potential;
- Generating additional revenue from retail assets via active asset management;
- Active re-positioning of portfolio by disposing of non-core and lower growth assets when opportune, and
- Optimising funding costs, given increase in scale.

PROPERTY PORTFOLIO

Exceptional property portfolio and development pipeline in Romania, Slovakia, Serbia and the Czech Republic, progressing with a retail expansion program in other emerging European retail markets, that generates earnings from long-term, triple net leases in Euro with strong corporate covenants.

LISTINGS

— the Main Board of the Johannesburg Stock Exchange (JSE)
— the regulated market of the Bucharest Stock Exchange (BVB)
— the Alternative Investment Market (AIM) of the London Stock Exchange (LSE)
The shares are transferable among the three registers.
The JSE is the most liquid in terms of share trading of the three stock exchanges where NEPI is listed.

INVESTMENT GRADE RATINGS

Moody's — Baa3 (stable outlook)
Standard & Poors — BBB- (stable outlook)

DISTRIBUTIONS

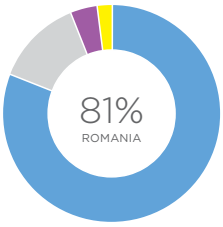
NEPI generally distributes at least 90% of its net rental profits on a semi-annual basis, with a scrip dividend election option.

INVESTMENT PROPERTY OVERVIEW AS AT 30 JUNE 2016

	Number	Weighted GLA '000m²	Weighted Valuation €m	Weighted Passing rent/ERV €m	Occupancy %
TOTAL PROPERTIES	**56**	**1 213**	**2 152**	**161**	
INCOME-PRODUCING	**33**	**902**	**1 928**	**147**	**98.1**
Retail	26	732	1 595	120	98.2
Office	5	142	317	25	97.5
Industrial	2	28	16	2	98.0
DEVELOPMENTS	**5**	**275**	**203**	**13**	
Under construction	2*	73	91	13	
Under permitting and pre-leasing	3**	202	89	–	
Land bank	–	–	23	–	
NON-CORE	**18**	**36**	**21**	**1**	

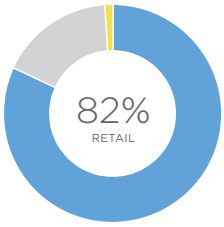
* out of seven properties under construction, five are extensions to existing properties.
** out of the seven properties under permitting and pre-leasing, four are extensions to existing properties.

GEOGRAPHICAL PROFILE
by rental income

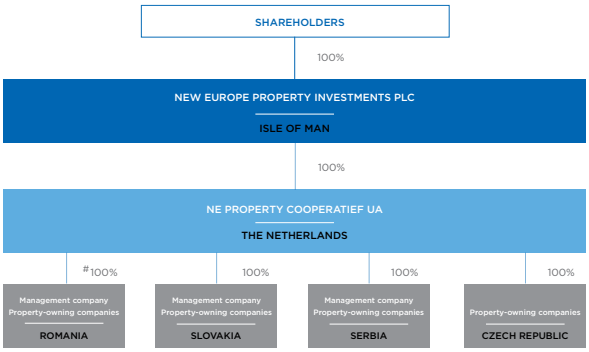


Romania	81%	€119.3 million
Slovakia	13%	€18.7 million
Czech Republic	4%	€5.5 million
Serbia	2%	€3.5 million
	100%	€147.0 million

SECTORAL PROFILE
by rental income



Retail	82%	€119.9 million
Office	17%	€25.3 million
Industrial	1%	€1.8 million
	100%	€147.0 million



#except for 50% interest held in Ploiesti Shopping City and The Office.

Top 5 Shareholders (as at 29 July 2016)	% of issued shares
Fortress Income Fund*	17.64%
Public Investment Corporation**	11.23%
Resilient Property Income Fund***	8.90%
Investec Asset Management Holdings (PTY)	3.28%
Standard Bank Group LTD	3.22%
Total	**44.37%**

*JSE listed fund focused on retail, directly or by investing in listed securities.
** One of the largest investment managers in Africa, managing assets of over €100 billion; it invests funds on behalf of public sector entities.
*** JSE listed REIT focused on retail, directly or by investing in listing securities; it is the founding shareholder of NEPI.

In other words Nepi is applying the capital invested by shareholders, from various parts of the world including South Africa, to the development and management in particular of 'retail assets' (shopping malls and offices) in Eastern Europe.

This is just one illustration of the global interconnections and flows of finance capital, where those living in one part of the world are invested in and receive profits from business activities in another, distant part. In particular where the local scope for profitable investment of surpluses is limited, there is an inbuilt compulsion for those surpluses, turned

[6] Pp 3 and 11.

into money capital, to seek investment opportunities further afield.

Here is a graph showing the recent performance of the Nepi share price.

How would you decide whether to buy, sell or hold on to Nepi shares? You would need to make a forecast of the likely future fall or rise of the share price (a potential capital loss or capital gain), and also take into account the history and prospects of the company's dividend payments to its shareholders. You would have to compare this forecast with forecasts for other potential investments. Investment managers and advisers are doing this constantly across the whole range of potential investments, nationally and globally.

As another illustration of companies and shareholding, let's consider the South Africa-based **Aspen Pharmacare Holdings Limited**. Consider the information provided on the next page, and discuss how you might go about making an evaluation of the company's prospects as a possible destination for the investment of your money-capital — assuming you had any.

[continued on next page]

Business Report 30 September 2016

Aspen to bide its time post-GSK

Confirms disposal of stake

Siseko Njobeni

BRANDED and generic pharmaceutical products group Aspen Pharmacare Holdings was unlikely to look for an investor in the mould of global pharmaceutical group GlaxoSmithKline (GSK), which had disposed of its remaining stake in Aspen, a South African analyst said yesterday.

Aspen, the largest pharmaceutical company listed on the JSE, confirmed yesterday that GSK on Wednesday had offloaded the remaining 6.2 percent interest in the company.

The disposal translates to 28.2 million ordinary shares after GSK sold the shares to institutional investors for R300 a share or R8.47 billion.

Aspen has a market capitalisation of about $10bn (R14bn).

R140 bn

Divesting

GSK started divesting its stake in Aspen in November 2013 when it sold 28.2 million shares for about R7bn.

Last year it sold the same number of shares through institutional investors for R372 a share, raising R10.5bn.

GSK, which had a stake in Aspen since 2009, felt it was the right time to move on but said the decision should not cast Aspen in a negative light.

Shmuel Simpson, a 36ONE Asset Management investment analyst, said yesterday that the move was expected.

Simpson said GSK's decision to dispose of the interest should not reflect badly on Aspen.

"It is more about GSK wanting to redeploy capital elsewhere," he said.

GSK's so-called strategy of simplification entails focusing on core therapeutic areas.

Simpson said the sale should be somewhat of a relief to Aspen shareholders. "It was an overhang for a while."

"The market assumed a placement was coming, it was only a question of when," Simpson said.

He said Aspen was unlikely to look for an investor similar to GSK.

"They have a strong and diverse investor base and do not require a core investor of the likes of GSK," Simpson said.

Aspen said the disposal would not affect the ongoing collaboration and trading relationships between the two companies in South Africa.

David Redfern, GSK's chief strategy officer, would remain a member of the Aspen board of directors, Aspen said.

Aspen Pharmacare

Relationship

Group chief executive Stephen Saad said the two companies would maintain their relationship.

"We are pleased that Aspen shareholders are relieved of the uncertainty caused by GSK's stated intention to dispose of its interests, which eliminates the overhang caused by this uncertainty," Saad said.

GSK spokeswoman Aoife Pauley said the decision to sell the company's remaining shares in Aspen was part of a desire to focus on core franchises and efficiently manage its balance sheet.

"We have been gradually reducing our holding since 2013 and now was the appropriate time to conclude that process and realise what has been a very successful investment for GSK," Pauley said.

Aspen shares on the JSE were down 1.85 percent at R311 yesterday.

Below is a graph of Aspen Pharmacare's share price over 5 years

[continued on next page]

Discovery Limited is an example of a South African holding company with many subsidiaries. This page and the next are taken from Discovery's published financial statements for 2015 (highlighting added):

Directors' report

for the year ended 30 June 2015

The directors present their 16th annual report, which forms part of the consolidated and separate financial statements of Discovery Limited for the year ended 30 June 2015.

Nature of business

Discovery Limited (the Company) is listed on the Johannesburg Stock Exchange and is an integrated financial services organisation specialising in health insurance, life assurance, wellness, investments and savings products, short-term insurance and credit card products. The Company is directly and indirectly the holding company of:

- Discovery Health Proprietary Limited (Discovery Health).
- Discovery Life Limited (Discovery Life).
- Discovery Life Collective Investments Proprietary Limited (Discovery Life Collective Investments).
- Discovery Life Investment Services Proprietary Limited (Discovery Life Investment Services).
- Discovery Life Nominees Proprietary Limited.
- Discovery Third Party Recovery Services Proprietary Limited (DTPRS).
- Discovery Vitality Proprietary Limited (Discovery Vitality).
- Discovery Investment Management Proprietary Limited (dormant).
- Discovery Insure Limited (Discovery Insure).
- Destiny Health Inc. - this company holds Discovery's interests in Destiny Health Management Company LLC, Destiny Health Insurance Company and Destiny Health Administration Company (dormant) (Destiny Health); The Vitality Group Inc. and The Vitality Group LLC (The Vitality Group), which are incorporated in the United States of America.
- Discovery Group Europe Limited, which is incorporated in England and Wales.
- Discovery Offshore Holdings No 2 Limited (dormant), which is incorporated in England and Wales.
- Discovery Holdings Europe Limited - this company holds Discovery's interests in Vitality Life Limited (dormant), Vitality Corporate Services Limited, Vitality Health Insurance Limited and Vitality Health Limited, which are incorporated in England and Wales (VitalityHealth).
- Discovery Partner Markets Asia Private Limited – this company holds Discovery's interests in Discovery Partner Markets Services Private Limited, which are incorporated in Singapore.
- Southern RX Distributors Proprietary Limited.

The subsidiaries are wholly-owned with the exception of Destiny Health Inc. in which the Company has a 99.98% interest and Discovery Holdings Europe Limited in which the Company has a 98.57% interest. The balance of the interest being held by senior management for both subsidiaries.

"Discovery Limited and its subsidiaries" are referred to herein as Discovery or the Group.

In addition to the above subsidiaries, Discovery consolidates unit trusts in which the Group has control in terms of IFRS 10. The consolidated unit trusts include:

- Discovery Balanced Fund
- Discovery Cautious Balanced Fund
- Discovery Diversified Income Fund
- Discovery Dynamic Equity Fund
- Discovery Equity Fund
- Discovery Flexible Property Fund
- Discovery Global Balanced Fund of Funds
- Discovery Global Value Equity Feeder Fund, previously Discovery Global Contrarian Equity Feeder Fund
- Discovery Global Equity Feeder Fund
- Discovery Moderate Balanced Fund
- Discovery Money Market Fund
- Discovery Target Retirement 2010 Fund
- Discovery Target Retirement 2015 Fund
- Discovery Target Retirement 2020 Fund
- Discovery Target Retirement 2025 Fund
- Discovery Target Retirement 2030 Fund
- Discovery Target Retirement 2035 Fund
- Discovery Target Retirement 2040 Fund
- Discovery Target Retirement 2045 Fund
- Discovery Target Retirement 2050 Fund
- Discovery Worldwide Best Ideas Fund

Directors' report

for the year ended 30 June 2015

Review of Results

Profit attributable to ordinary shareholders is R5 480 million, a 69% increase from profits of R3 246 million reported in the prior financial year. The profit for the year ended 30 June 2015 includes a once-off gain for the fair value adjustment on puttable non-controlling interest of R1 661 million. Normalised headline earnings, which excludes this gain and other once-off items, increased by 16.5% to R4 027 million.

Share capital

The share capital of the Company at 30 June 2015 was as follows:

Class of shares	Authorised number of shares	Issued number of shares
Ordinary shares of 0.1 cent per share	1 000 000 000	647 427 946
A preference shares	40 000 000	-
B preference shares	20 000 000	8 000 000
C preference shares	20 000 000	-

Dividends

The following interim dividends were paid during the current financial year:

- Preference share dividend of 465.0 cents per share, paid on 16 March 2015.
- Ordinary share dividend of 85.5 cents per share, paid on 23 March 2015.

The directors are of the view that the Discovery Group is adequately capitalised at this time. On the statutory basis the capital adequacy requirement of Discovery Life was R557 million (2014: R522 million) and was covered 3.9 times (2014: 3.8 times).

B preference share cash dividend declaration:

On 27 August 2015, the directors declared a gross cash dividend of 458.699 cents (389.89415 cents net of dividend withholding tax) per B preference share for period 1 January 2015 to 30 June 2015. The dividend has been declared from income reserves and no secondary tax on companies' credits have been used. A dividend withholding tax of 15% will be applicable to all shareholders who are not exempt.

The issued preference share capital at the declaration date is 8 million B preference shares.

The salient dates for the dividend will be as follows:

Last day of trade to receive a dividend	Friday, 11 September 2015
Shares commence trading "ex" dividend	Monday, 14 September 2015
Record date	Friday, 18 September 2015
Payment date	Monday, 21 September 2015

B preference share certificates may not be dematerialised or rematerialised between Monday, 14 September 2015 and Friday, 18 September 2015, both days inclusive.

Ordinary share cash dividend declaration:

Notice is hereby given that the directors have declared a final gross cash dividend of 89.0 cents (75.65 cents net of dividend withholding tax) per ordinary share, out of income reserves for the year ended 30 June 2015. A dividend withholding tax of 15% will be applicable to all shareholders who are not exempt.

The issued ordinary share capital at the declaration date is 647 427 946 ordinary shares.

The next page is taken from Discovery's Audited Results booklet for 2016:

Statement of financial position
at 30 June 2016

R million	Group 2016 Audited	Group 2015 Audited and restated	Group 2014 Audited and restated
ASSETS			
Assets arising from insurance contracts	**33 815**	28 144	23 044
Property and equipment	**1 052**	727	666
Intangible assets including deferred acquisition costs	**4 584**	2 526	2 344
Goodwill	**2 447**	2 375	2 239
Investment in equity-accounted investees	**491**	505	551
Financial assets			
– Available-for-sale investments	**9 794**	9 454	7 578
– Investments at fair value through profit or loss	**50 948**	40 132	32 753
– Derivatives	**590**	825	588
– Loans and receivables including insurance receivables	**4 891**	3 884	3 110
Deferred income tax	**824**	690	406
Current income tax asset	**97**	5	46
Reinsurance contracts	**410**	362	266
Cash and cash equivalents	**8 634**	6 251	3 650
Total assets	**118 577**	95 880	77 241
EQUITY			
Capital and reserves			
Ordinary share capital and share premium	**8 300**	7 488	2 582
Perpetual preference share capital	**779**	779	779
Other reserves	**1 934**	2 024	1 501
Retained earnings	**19 594**	17 065	12 549
	30 607	27 356	17 411
Non-controlling interest	**–**	–	–
Total equity	**30 607**	27 356	17 411
LIABILITIES			
Liabilities arising from insurance contracts	**44 673**	37 236	30 842
Liabilities arising from reinsurance contracts	**4 894**	3 827	2 247
Financial liabilities			
– Puttable non-controlling interests	**–**	–	4 494
– Negative reserve funding	**4 248**	5 437	4 684
– Borrowings at amortised cost	**5 400**	954	572
– Investment contracts at fair value through profit or loss	**13 514**	10 059	8 264
– Derivatives	**49**	7	10
– Trade and other payables	**8 563**	5 506	3 752
Deferred income tax	**6 035**	5 077	4 647
Deferred revenue	**291**	192	157
Employee benefits	**169**	152	154
Current income tax liability	**134**	77	7
Total liabilities	**87 970**	68 524	59 830
Total equity and liabilities	**118 577**	95 880	77 241

4

The financial sector of the capitalist system has developed substantially over the years so as to draw in the savings of the middle class and working class to add to the funds of the wealthier investors.

Unit trust funds ('collective investment schemes'):

Small investors can nowadays invest in large companies globally without directly holding shares and having to worry about whether and when to buy or sell them. They can do this by buying units in various 'unit trust' or 'collective investment' funds. (In the USA these are called 'mutual' funds). In South Africa these are regulated under the **Collective**

Investment Schemes Control Act 45 of 2002.

Different funds may specialise in different asset classes (equities, bonds, property, etc), or simply track the general performance of the companies listed on various exchanges.

The investor buys the units directly from the fund, and can also redeem the investment at its current market value directly from the fund. This means not having to find a buyer in the market place. It also means that the fund managers (in return for a fee, usually linked to performance) constantly evaluate the underlying holdings of the fund, buying and selling securities according to their own estimation of likely results. Complexity for the small investor is thus reduced to evaluating the likely performance of the fund itself, taking into account its choice of asset class (if relevant) and the track record of the particular fund managers. Investment advisors constantly watch the funds, their managers and their investment choices and performance as if studying race horses, so as to advise their clients how best to gamble — i.e. invest.

Pension funds are another vitally important focus of ownership in the financial system. Increasingly pension funds are the ultimate owners of the shares in major corporations globally. Anyone with a pension entitlement, however small, is an investor in a pension fund, and thus an investor in global capitalism. In South Africa, pension funds are regulated under the **Pension Funds Act 24 of 1956.**

Another important investment vehicle is the 'life' insurance policy — more accurately called a **long-term insurance policy** — issued by an insurance company. The 'policy-holders funds' through which investments are made are kept separate from the insurance company's own funds that render profits to its own shareholders. In part, the premiums paid by people purchasing insurance provide the source of profit to those shareholders, but the premiums are mainly applied to purchasing underlying investments in securities etc, in the policy-holders funds. The returns on these pooled investments provide the eventual payouts to the insured, or to the surviving beneficiaries of the insured. In the case of short-term insurance there may be no payout, because the risk insured against (such as theft or a fire) may never occur. Insurance is both a means of purchasing protection against risk and a matter of individual betting against the pool. It is regulated in South Africa under the **Long-term Insurance Act 52 of 1998** and the **Short-term Insurance Act 53 of 1998**.

Finally let's consider **bank deposits**. For present purposes, to keep matters simple, we'll assume that interest rates are positive (+ rather than -%). To support the payment of interest to depositors, a bank must be able to lend out the deposited funds to borrowers in return for interest paid by them. To make a profit from taking deposits and remain in business, the bank must be able to lend out the funds at a higher rate of interest than the rate it is paying to its depositors. In fact the banks multiply their earnings by lending out funds they do not have. How they are able to do this, and how it is regulated by the Reserve Bank under the 'fractional reserve system' is a fascinating subject which, unfortunately, we do not have time to cover in this course.

We also cannot go into how a depositors' 'run on the bank' in a time of uncertainty can lead to a general financial crisis when the bank cannot recover from its borrowers, or cannot recover immediately, the funds needed to repay the depositors on demand.

Lack of time prevents us more generally from discussing other causes of crisis in the

financial system, and how financial crisis may precipitate a wider crisis in the global system of production for exchange.

Quiz question: who owns the money in your bank account?

Answer: the bank owns it. You have *lent* the money to the bank to do with it what the bank pleases. Assuming you are in credit, the bank is your *debtor* to that extent. (The bank may have other duties, such as making and receiving payments on your behalf, which do not alter the basic debtor-creditor relationship where bank deposits are concerned.)

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Multinational (or 'transnational') corporations

[Lack of time prevented an examination of this topic, which was referred to only in general terms during class. The following illustrative material is included in these notes for future reference.]

To illustrate the scale and global reach of multinational corporations, let's look briefly at the BHP Billiton group. A few extracts from its 2016 annual report will suffice for this purpose:

1.5.1 About us

BHP Billiton is among the world's top producers of major commodities including iron ore, metallurgical coal, copper and uranium. We also have substantial interests in oil, gas and energy coal.

We extract and process minerals, oil and gas from our production operations located primarily in Australia and the Americas.

Our products are sold worldwide, with sales and marketing led through Singapore and Houston, United States. Our global headquarters are in Melbourne, Australia.

We operate under a Dual Listed Company structure with two parent companies (BHP Billiton Ltd and BHP Billiton Plc) operated as a single economic entity. We are run by a unified Board and management.

With a team of more than 65,000 employees and contractors, we prioritise our people's health and safety and strive to create an environment free from fatalities, injuries and occupational illnesses.

Our size and scope allow us to make meaningful contributions to communities and the long-term nature of our operations means we are able to build collaborative community relationships.

We aim to maximise the social and economic benefits of our operations, contribute to economic development and minimise our environmental footprint through innovation, productivity and technology.

Workforce of approximately

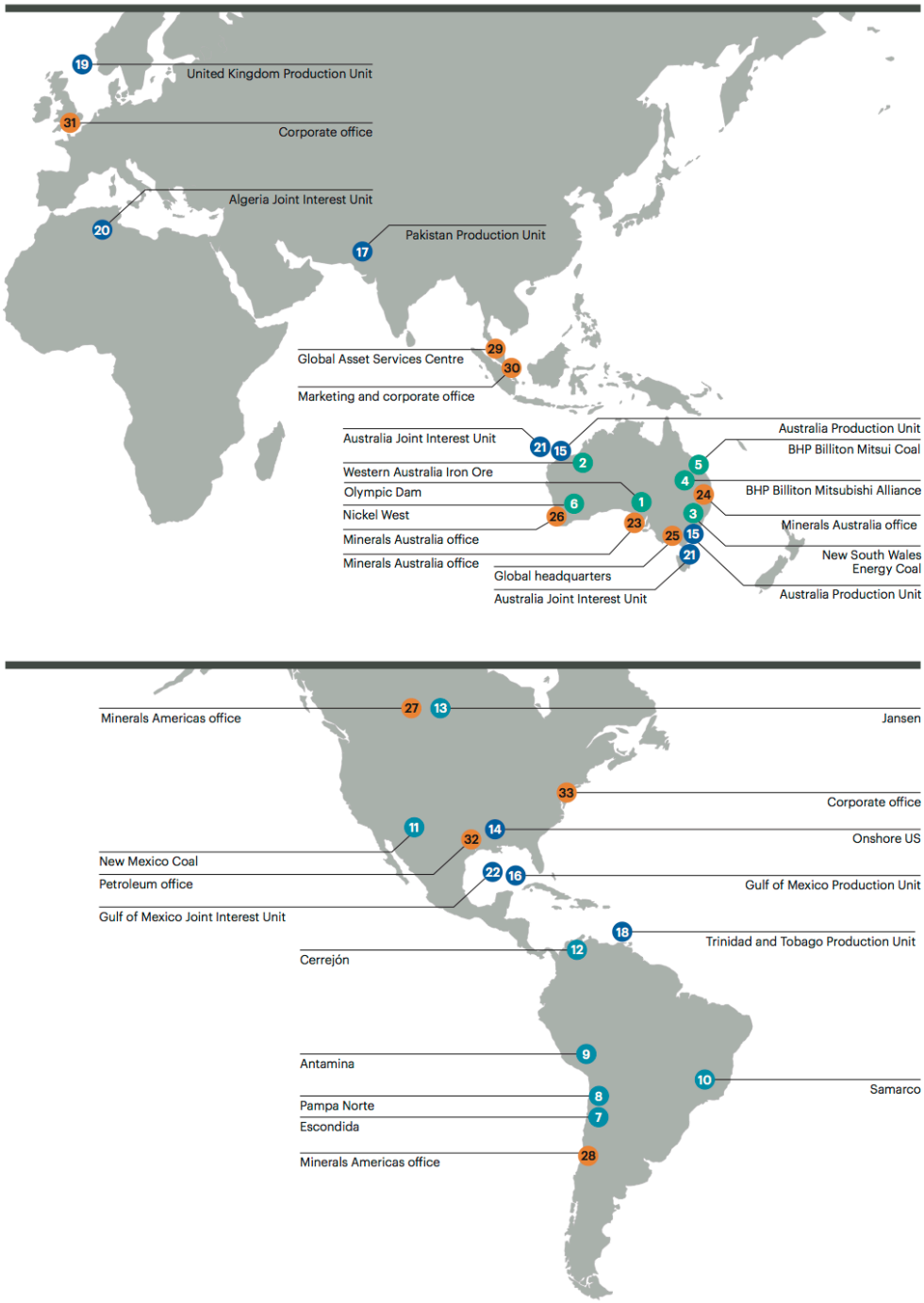
65,000

employees and contractors as of 30 June 2016

This is from page 11 of the report (highlighting added).

On pages 14-15 of the report, we are shown the locations of BHP Billiton's operations [see next page]. BHP Billiton sold its mining interests in South Africa to Gencor Ltd and then divested from Gencor in the 1990s. In 2016, in the context of the global commodities slump, a bad bet on shale oil and a costly dam collapse in Brazil that killed 19 people, the previously profitable BHP Billiton reported a loss of US$6.2 billion.

1.5.4 BHP Billiton locations (includes non-operated)



Minerals Australia

Ref	Country	Asset	Description	Ownership
1	Australia	Olympic Dam	Underground copper mine, also producing uranium, gold and silver	100%
2	Australia	Western Australia Iron Ore	Integrated iron ore mines, rail and port operations in the Pilbara region of Western Australia	51–85%
3	Australia	New South Wales Energy Coal	Open-cut energy coal mine and coal preparation plant in New South Wales	100%
4	Australia	BHP Billiton Mitsubishi Alliance	Open-cut and underground metallurgical coal mines in the Queensland Bowen Basin and Hay Point Coal Terminal	50%
5	Australia	BHP Billiton Mitsui Coal	Two open-cut metallurgical coal mines in the Bowen Basin, Central Queensland	80%
6	Australia	Nickel West	Integrated sulphide mining, concentrating, smelting and refining operation in Western Australia	100%

Minerals Americas

Ref	Country	Asset	Description	Ownership
7	Chile	Escondida	Copper producing mine, located in northern Chile	57.5%
8	Chile	Pampa Norte	Consists of the Cerro Colorado and Spence open-cut mines, producing copper cathode in northern Chile	100%
9	Peru	Antamina (1)	Open-cut copper and zinc mine in northern Peru	33.8%
10	Brazil	Samarco (1)	Open-cut iron ore mines, concentrators, pipelines, pelletising facilities and dedicated port	50%
11	US	New Mexico Coal (2)	One energy coal mine in New Mexico	100%
12	Colombia	Cerrejón (1)	Open-cut energy coal mine with integrated rail and port operations	33.3%
13	Canada	Jansen	Our interest in potash is via development projects in the Canadian province of Saskatchewan, where the Jansen Project is our most advanced	100%

Petroleum

Ref	Country	Asset	Description	Ownership
14	US	Onshore US	Onshore shale liquids and gas fields in Arkansas, Louisiana and Texas	<1–100%
15	Australia	Australia Production Unit	Offshore oil fields and gas processing facilities in Western Australia and Victoria	39.99–90%
16	US	Gulf of Mexico Production Unit	Offshore oil and gas fields in the Gulf of Mexico	35–44%
17	Pakistan	Pakistan Production Unit (3)	Onshore oil and gas fields	38.5%
18	Trinidad and Tobago	Trinidad and Tobago Production Unit	Offshore oil and gas fields	45%
19	UK	UK Production Unit (1)	Offshore oil and gas fields	16–31.83%
20	Algeria	Algeria Joint Interest Unit (1)	Onshore oil and gas unit	38%
21	Australia	Australia Joint Interest Unit (1)	Offshore oil and gas fields in Bass Strait and North West Shelf	8.33–50%
22	US	Gulf of Mexico Joint Interest Unit (1)	Offshore oil and gas fields in the Gulf of Mexico	4.95–44%

BHP Billiton principal office locations

Ref	Country	Location	Office
23	Australia	Adelaide	Minerals Australia office
24	Australia	Brisbane	Minerals Australia office
25	Australia	Melbourne	Global headquarters
26	Australia	Perth	Minerals Australia office
27	Canada	Saskatoon	Minerals Americas office
28	Chile	Santiago	Minerals Americas office
29	Malaysia	Kuala Lumpur	Global Asset Services Centre
30	Singapore	Singapore	Marketing and corporate office
31	UK	London	Corporate office
32	US	Houston	Petroleum office
33	US	New York	Corporate office

(1) Non-operated joint venture.
(2) Sale of Navajo Mine completed, however BHP Billiton will continue to manage and operate the mine until the Mine Management Agreement ends on 31 December 2016.
(3) Pakistan Production Unit was divested in FY2016.

Page 282 from the same report (highlighting added) indicates who were the most significant shareholders in BHP Billiton as at 12 August 2016. [See next page.]

Note the footnotes referring to nominee holdings.

7.6 Share ownership

Share capital

The details of the share capital for both BHP Billiton Limited and BHP Billiton Plc are presented in note 15 'Share capital' to the Financial Statements and remain current as at 12 August 2016.

Major shareholders

The tables in section 3.4.23 and the information set out in section 4.18 present information pertaining to the shares in BHP Billiton Limited and BHP Billiton Plc held by Directors and members of the Operations Management Committee (OMC).

Neither BHP Billiton Limited nor BHP Billiton Plc is directly or indirectly controlled by another corporation or by any government. Other than as described in section 7.3.2, no major shareholder possesses voting rights that differ from those attaching to all of BHP Billiton Limited and BHP Billiton Plc's voting securities.

Substantial shareholders in BHP Billiton Limited

As at 12 August 2016, there were no substantial shareholders in BHP Billiton Limited. A substantial shareholder is a person who (together with associates) has a relevant interest in five per cent or more of voting rights conferred by ordinary shares in BHP Billiton Limited. Notifications to BHP Billiton Limited under section 671B of the Corporations Act 2001 indicate that no person (together with their associates) beneficially owned more than five per cent of BHP Billiton Limited's voting securities.

Substantial shareholders in BHP Billiton Plc

The following table shows holdings of three per cent or more of voting rights conferred by BHP Billiton Plc's ordinary shares as notified to BHP Billiton Plc under the UK Disclosure and Transparency Rule 5 as at 30 June 2016.[1]

Title of class	Identity of person or group	Date of last notice			Percentage of total voting rights[2]		
		Date received	Date of change	Number owned	2016	2015	2014
Ordinary shares	Aberdeen Asset Managers Limited	8 October 2015	7 October 2015	103,108,283	4.88%	6.06%	6.34%
Ordinary shares	BlackRock, Inc.	3 December 2009	1 December 2009	213,014,043	10.08%	10.08%	10.08%

(1) No changes in the holdings of three per cent or more of the voting rights in BHP Billiton Plc's shares have been notified to BHP Billiton Plc between 1 July 2016 and 12 August 2016.
(2) The percentages quoted are based on the total voting rights conferred by ordinary shares in BHP Billiton Plc as at 12 August 2016 of 2,112,071,796.

Twenty largest shareholders as at 12 August 2016 (as named on the Register of Shareholders)[1]

BHP Billiton Limited	Number of fully paid shares	% of issued capital
1. HSBC Australia Nominees P/L	639,750,740	19.92
2. JP Morgan Nominees Australia Limited	454,398,834	14.15
3. National Nominees Ltd	206,630,417	6.43
4. Citicorp Nominees Pty Ltd	181,277,380	5.64
5. Citicorp Nominees Pty Limited <Citibank NY ADR DEP A/C>	169,453,030	5.28
6. BNP Paribas NOMS Pty Ltd	66,041,956	2.06
7. Citicorp Nominees Pty Limited <Colonial First State Inv A/C>	30,939,540	0.96
8. BNP Paribas Nominees Pty Ltd <Agency Lending DRP A/C>	23,964,819	0.75
9. Aust Mutual Prov Society	16,542,870	0.52
10. HSBC Custody Nominees (Australia) Limited <NT- Comnwlth Super Corp A/C>	15,084,727	0.47
11. Australian Foundation Invest	13,990,941	0.44
12. Computershare Nominees Cl Ltd <ASX Shareplus Control A/C>	12,262,311	0.38
13. Argo Investments Limited	8,428,904	0.26
14. HSBC Custody Nominees (Australia) Limited <Euroclear Bank SA NV A/C>	7,168,329	0.22
15. RBC Investor Services Australia Nominees Pty Limited <BKCUST A/C>	5,881,948	0.18
16. Navigator Australia Ltd <MLC Investment Sett A/C>	5,166,136	0.16
17. Computershare Trustees Jey Ltd <RE 3000101 A/C>	4,380,484	0.14
18. RBC Investor Services Australia Nominees Pty Limited <BKCUST A/C>	4,353,968	0.14
19. IOOF Investment Management Limited <IPS Super A/C>	3,975,063	0.12
20. Bond Street Custodians Limited	3,846,360	0.12
	1,873,538,757	58.33

BHP Billiton Plc	Number of fully paid shares	% of issued capital
1. PLC Nominees (Proprietary) Limited[2]	331,280,556	15.69
2. Chase Nominees Limited	140,840,217	6.67
3. National City Nominees Limited	106,698,037	5.05
4. State Street Nominees Limited <OM02>	101,159,454	4.79
5. Nortrust Nominees Limited	51,486,322	2.44
6. State Street Nominees Limited <OM04>	50,832,288	2.41
7. Lynchwood Nominees Limited <2006420>	49,136,235	2.33
8. The Bank of New York (Nominees) Limited	47,994,299	2.27
9. State Street Nominees Limited <OD64>	45,798,401	2.17
10. Government Employees Pension Fund – PIC	40,961,160	1.94
11. Vidacos Nominees Limited <13559>	39,864,705	1.89
12. Vidacos Nominees Limited <CLRLUX2>	34,543,044	1.64
13. Industrial Development Corporation of South Africa	33,804,582	1.60
14. HSBC Global Custody Nominee (UK) Limited <357206>	32,425,250	1.54
15. BNY Mellon Nominees Limited <BSDTGUSD>	25,860,615	1.22
16. Nutraco Nominees Limited <492762>	25,165,035	1.19
17. Nutraco Nominees Limited <781221>	24,200,000	1.15
18. Chase Nominees Limited <BBHLEND>	23,374,720	1.11
19. Vidacos Nominees Limited <CLRLUX>	23,369,058	1.11
20. Vidacos Nominees Limited <FGN>	22,289,497	1.06
	1,251,083,475	59.27

(1) Many of the 20 largest shareholders shown for BHP Billiton Limited and BHP Billiton Plc hold shares as a nominee or custodian. In accordance with the reporting requirements, the tables reflect the legal ownership of shares and not the details of the underlying beneficial holders.
(2) The largest holder on the South African register of BHP Billiton Plc is the Strate nominee in which the majority of shares in South Africa (including some of the shareholders included in this list) are held in dematerialised form.

On page 284, BHP Billiton states its group policy on the payment of dividends to shareholders. It provides for 'a minimum 50 per cent payout of Underlying attributable profit at every reporting period'.

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Consider next the extensive and complex **supply chains providing inputs** via the market to major companies. A few years ago, the *Financial Times* reported on a rationalisation being carried out by the diversified manufacturer Siemens with the aim of reducing the number of its suppliers from 113,000 to about 90,000.[7] One of the aims of the exercise was to reduce potential supply disruptions.

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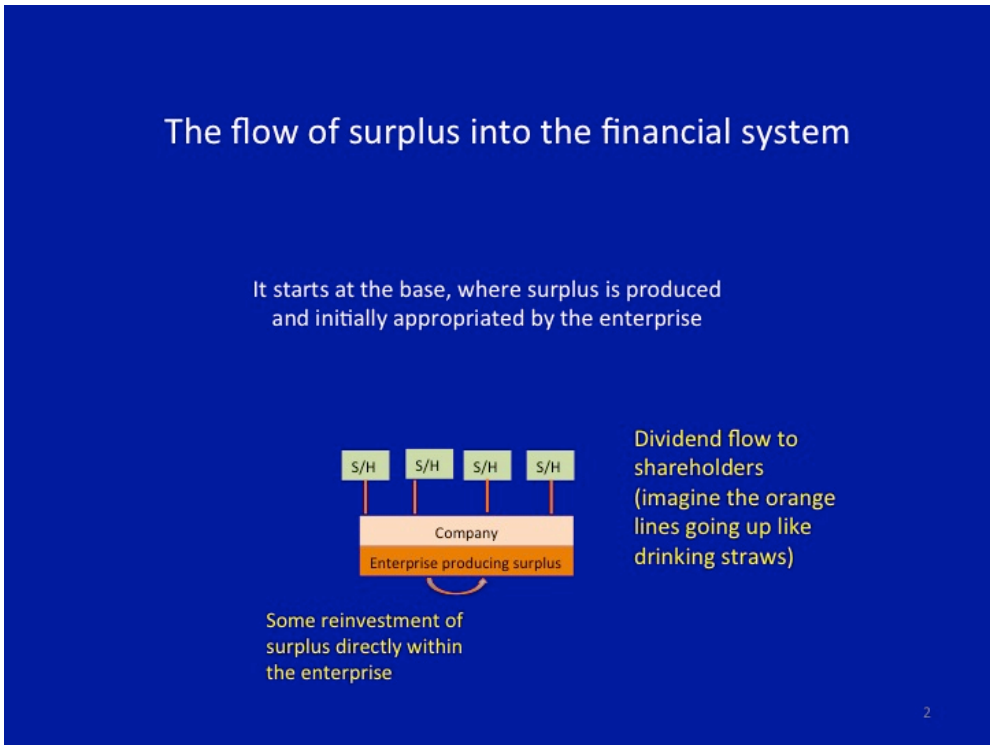
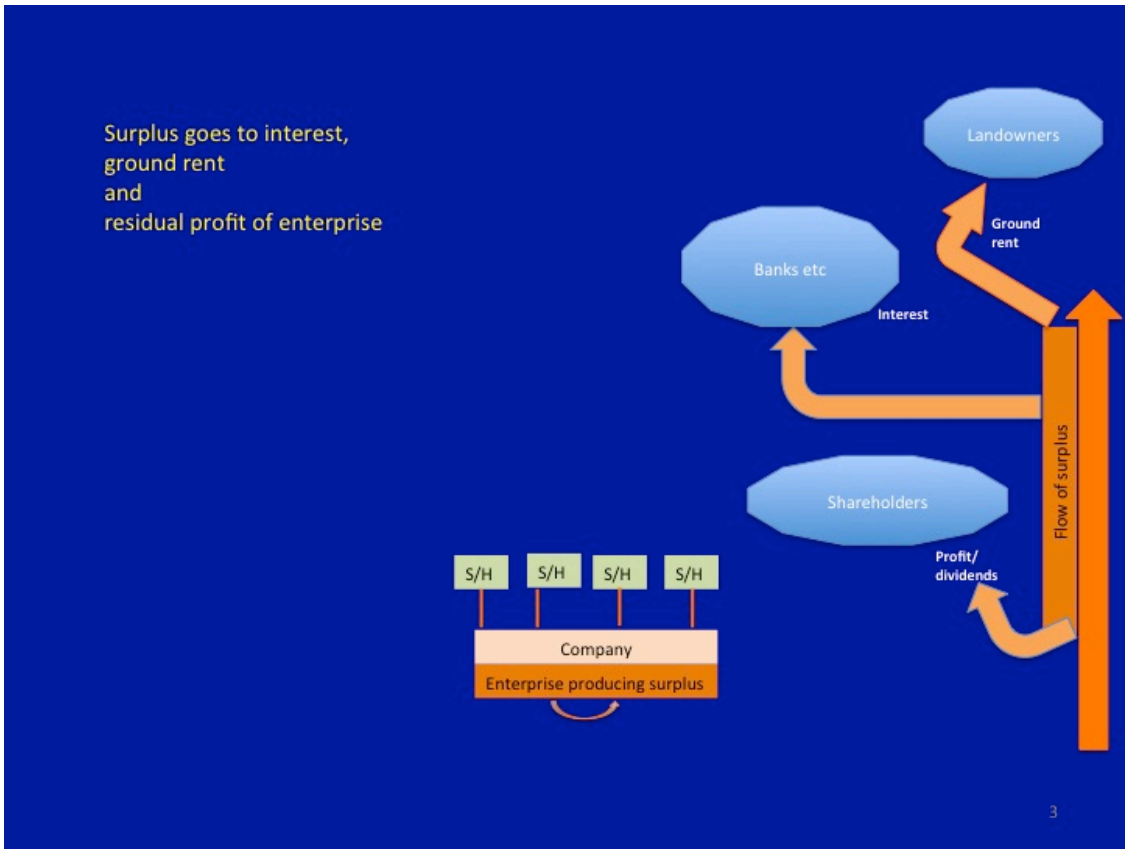
The crucial point to bear in mind — to repeat the analysis made earlier in the course — is that **the material surplus of society is a *produced* surplus**, resulting essentially from the division of labour and combination of the outputs of enterprises engaged in production for exchange. In broad principle, each enterprise receives its allocation of portion of the total social surplus in the price paid to it in the market when it succeeds in selling its goods or services — i.e., in its revenue. Its profit before tax is the difference between its own costs of production (including here ground rent and interest paid) and the revenue it has earned — assuming the revenue is higher. If it persistently makes a loss or no profit it will have to exit the business. Capital invests in production for profit, not production for its own sake.

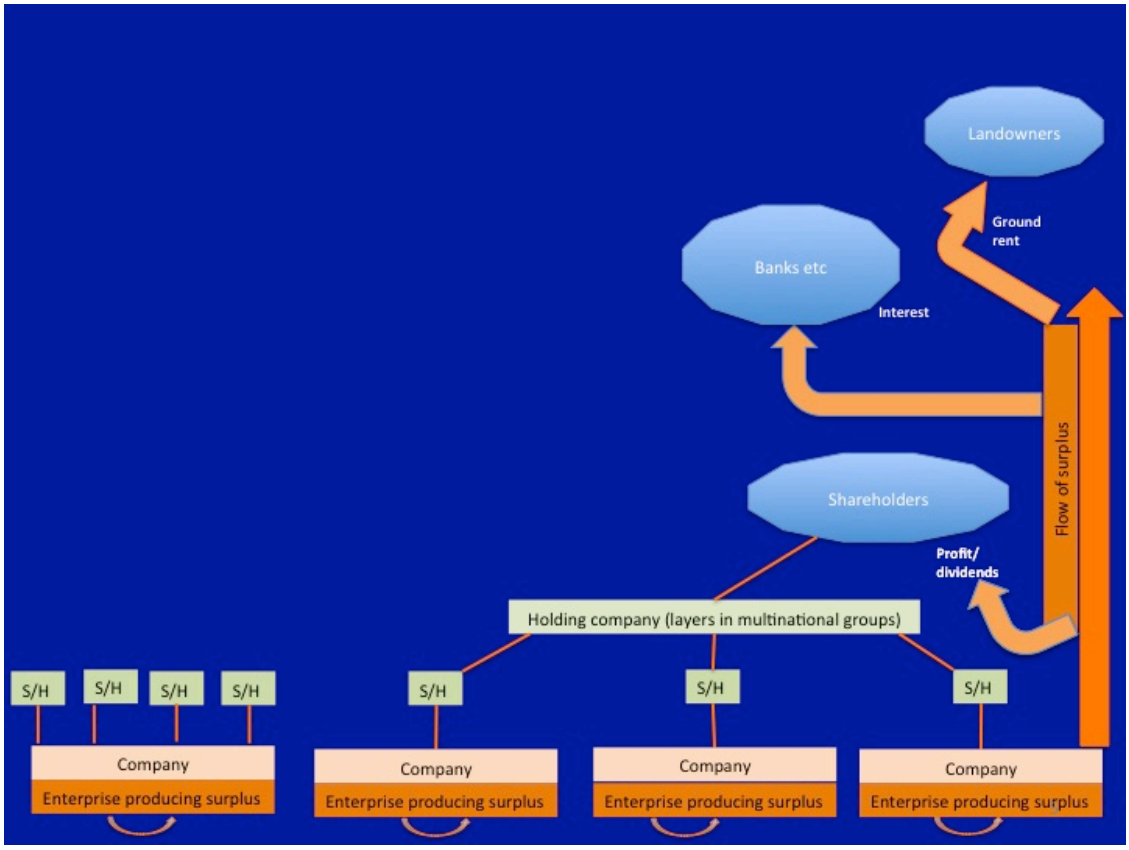
We are now in a position to present by way of a series of **diagrams**, in simplified terms, **the flow of surplus in financial form in the capitalist economy**. To the extent that a money-surplus accruing to an enterprise is not reinvested there, it makes its way into the financial economy before finding a way to come down again as reinvestment in material surplus-production at the base. In the following sequence of diagrams, the orange lines represent the flow of financial surpluses and can be compared with drinking straws drawing those surpluses up to those whose entitlement to them is socially recognised in the prevailing property system. **The predominant form of *property* today is abstract financial entitlements**.

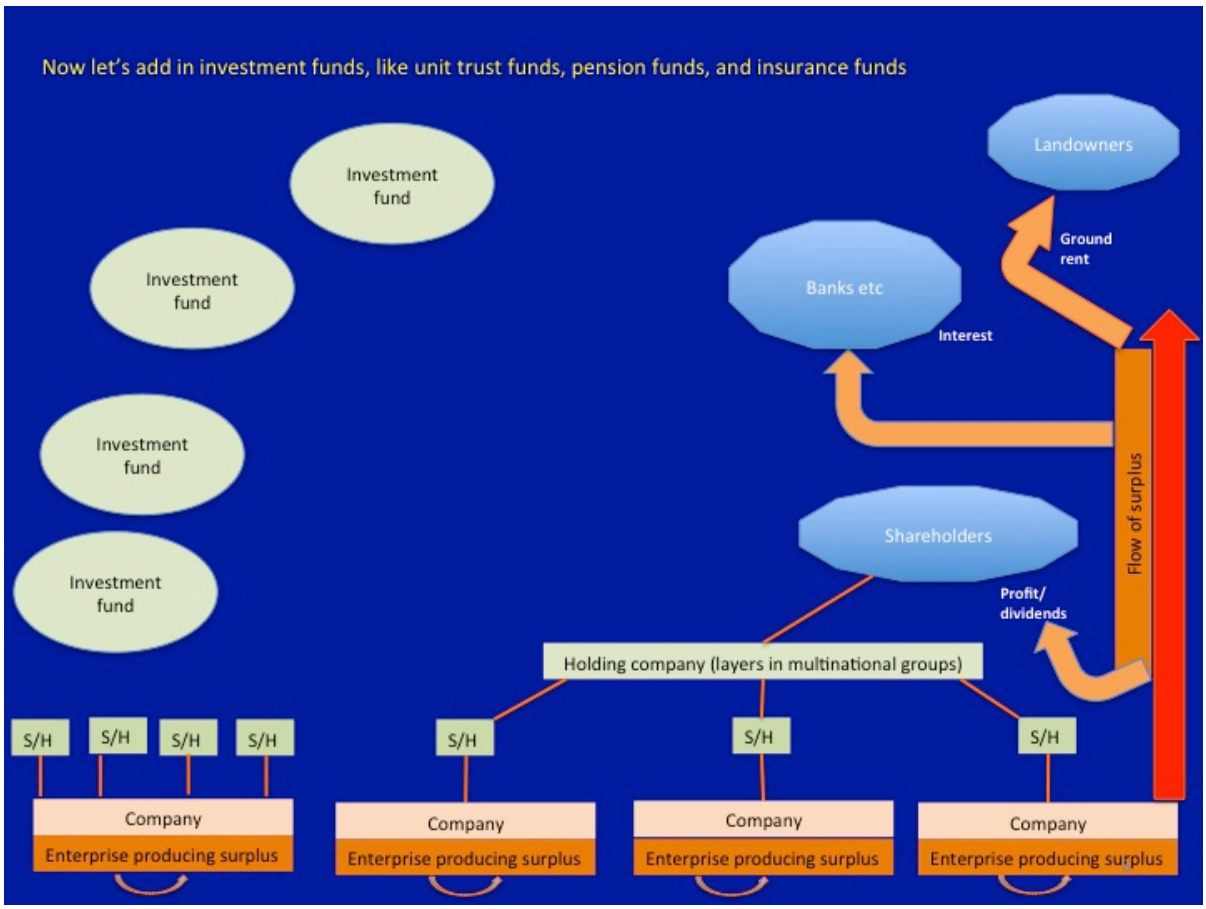


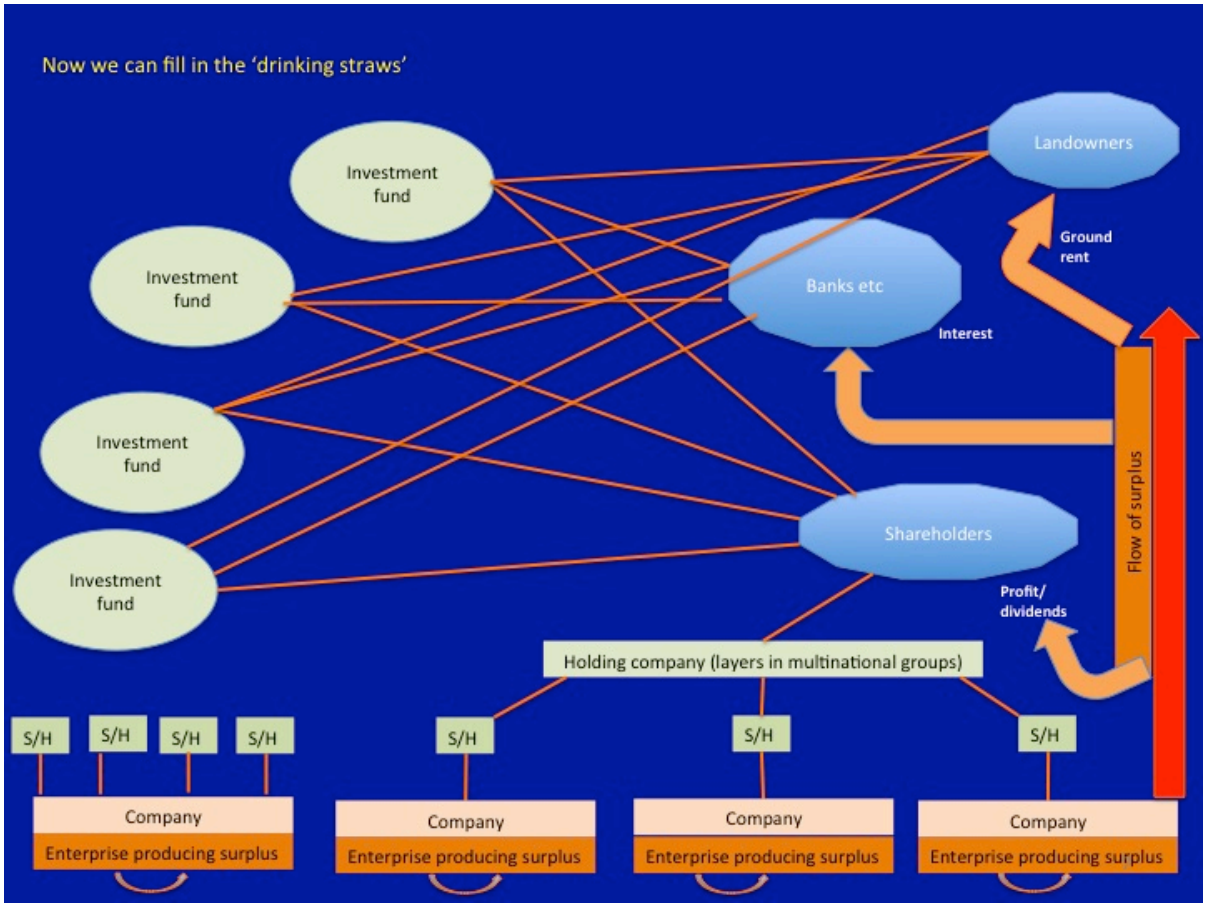
[7] 'A stronger chain of command' by Daniel Schäfer, *Financial Times*, 11 October 2010.

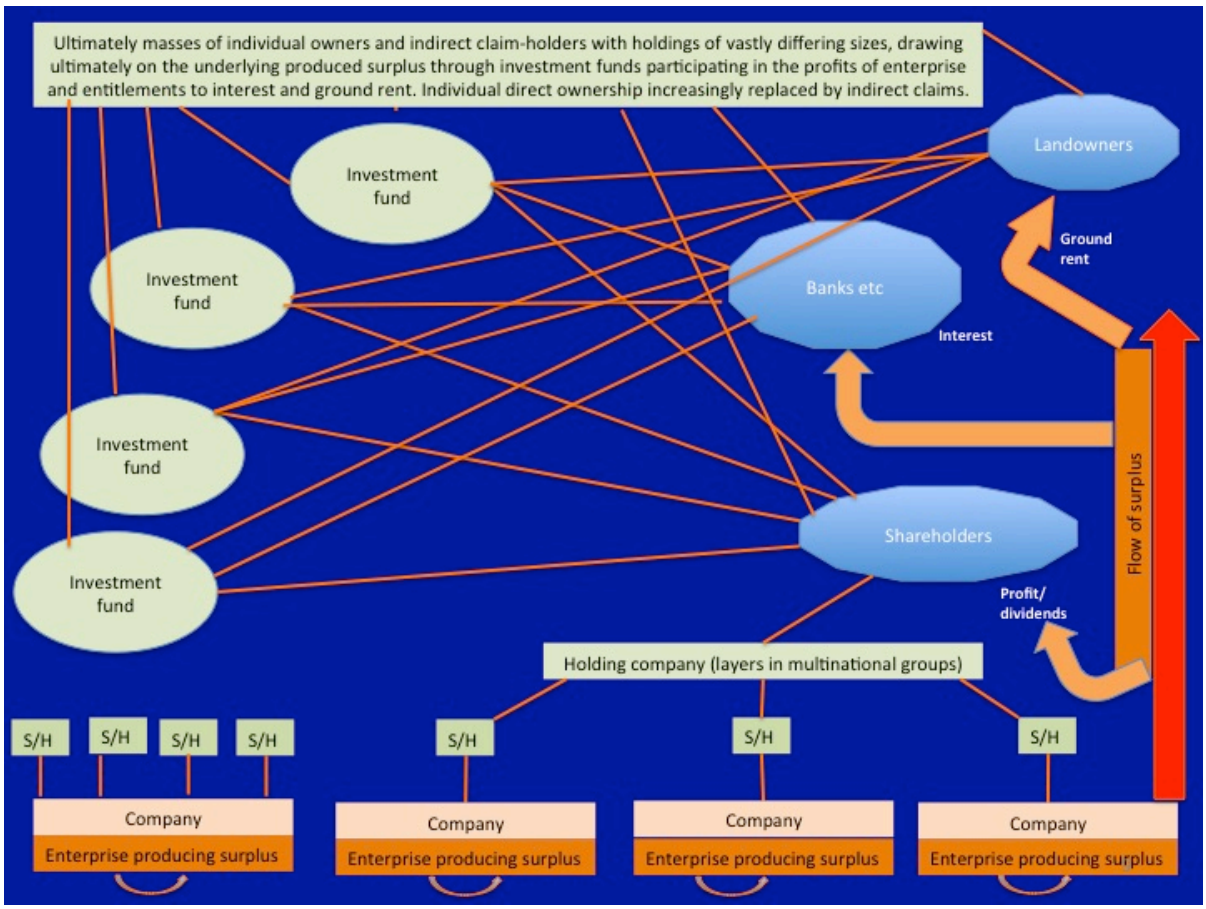
Bear in mind that tax is also paid out of surplus; in these diagrams, however, we shall leave tax aside. Note also that, as we have discussed previously, while each enterprise treats interest and ground rent as part of its own costs of production, from a social point of view they are a charge on the aggregate surplus — a pure return to property.






Now let's add in investment funds, like unit trust funds, pension funds, and insurance funds
Investment fund
Investment fund
Investment fund
Investment fund
Landowners
Ground rent
Banks etc
Interest
Flow of surplus
Shareholders
Profit/ dividends
Holding company (layers in multinational groups)
S/H
S/H
S/H
S/H
S/H
S/H
S/H
Company
Enterprise producing surplus
Company
Enterprise producing surplus
Company
Enterprise producing surplus
Company
Enterprise producing surplus


Now we can fill in the 'drinking straws'
Investment fund
Investment fund
Investment fund
Investment fund
Landowners
Ground rent
Banks etc
Interest
Flow of surplus
Shareholders
Profit/ dividends
Holding company (layers in multinational groups)
S/H
S/H
S/H
S/H
S/H
S/H
S/H
Company
Enterprise producing surplus
Company
Enterprise producing surplus
Company
Enterprise producing surplus
Company
Enterprise producing surplus



Remember that the surplus, to the extent that it is not consumed by those who receive it, must find its way back down again into profitable investments in enterprises at the base. Otherwise it will evaporate. The flow back down is not depicted in these slides.

Next time, we'll consider in more detail the nature of abstract proprietary entitlements, and some of their implications in the financial economy.