

**Financial sector change in
the context of oil-abundance:
Angola, 1991-2014**



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Abstract

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This thesis contributes to our understanding of the drivers of financial sector change in the particular case of resource-rich authoritarian countries. Existing studies assume that political leaders in countries characterized as resource-rich and authoritarian are disinterested in advancing financial markets. These studies moreover assume that the resource wealth that these leaders have at their disposal makes them act to the detriment of the financial sector without bearing any consequences. This thesis challenges these existing interpretations.

Building on a detailed qualitative case study of financial sector change in Angola, covering the period from 1991 to 2014, the thesis argues that contrary to what prevailing theories might expect, the financial sector has been useful for maintaining Angola's resource rich ruling coalition in a position of power. Financial sector change in the country is explained by political leaders' need to appease supporters coupled with the latter's ability to balance the pressure of domestic excluded factions and external actors. When political leaders are not able to satisfy their supporters, they are inclined to introduce financial sector change. Their ability to do so, however, depended on political leaders' ability to balance the pressures exerted on them by domestic and external actors.

The study contributes to the political economy of finance literature by offering a new take on how the financial sector can benefit regime survival and using this logic to explain the process of financial sector change in the setting of a resource-rich and authoritarian country. This study of Angola moreover adds to the growing scholarship seeking to nuance the assumption that leaders of resource rich authoritarian countries are autonomous from societal demands. Drawing on data collected over five months of fieldwork in Angola, the thesis also contribute empirically by being amongst the first studies to critically examine the political economy of postcolonial finance in one of Africa's largest economies.

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Selected Acronyms, Abbreviations, and Units

ABANC	Angolan Association of Banks, <i>Associação Angolana de Bancos</i>
AML/CFT	Anti-Money Laundering/Combating the Financing of Terrorism
BCA	Banco Comercial Angolano
BAI	Banco Angolano de Investimentos
BCI	Banco de Comércio e Indústria
BESA	Banco Espírito Santo Angola
BNA	National Bank of Angola, <i>Banco Nacional de Angola</i>
BPC	Banco de Poupança e Crédito
CAP	Agro-Livestock and Fisheries Credit Bank, <i>Caixa de Crédito Agro-Pecuário e Pescas</i>
ENDIAMA	National Diamond Company of Angola, <i>Empresa Nacional de Prospecção, Exploração, Lapidação e Comercialização de Diamantes de Angola</i>
EIU	Economist Intelligence Unit
FAPLA	People's Armed Forces of Liberation of Angola, <i>Forças Armadas Populares de Libertação de Angola</i>
FDI	Foreign direct investment
FNLA	National Front for the Liberation of Angola, <i>Frente Nacional de Libertação de Angola</i>
FSDEA	Sovereign Fund of Angola, <i>Fundo Soberano de Angola</i>
GDP	Gross domestic product
IFI	International financial institution
IMF	International Monetary Fund
IOC	International oil company
MPLA	People's Movement for the Liberation of Angola, <i>Movimento Popular de Libertação de Angola</i>
NPL	Non-performing loans
OPEC	Organization of the Petroleum Exporting Countries
SOE	State-owned enterprise
Sonangol	National Society of Fuels of Angola, <i>Sociedade Nacional de Combustíveis de Angola</i> ,
SWF	Sovereign Wealth Fund
UNITA	National Union for the Total Independence of Angola, <i>União Nacional para a Independência Total de Angola</i>
Monetary units:	In this thesis I state values in terms of US dollar (denoted as \$) unless otherwise stated.

Figure 0.1: Map of Angola



Source: Map Library (2013).

Chapter 1

Introduction

1. Introduction

What drives financial sector change in the particular case of resource-rich authoritarian countries? Existing studies assume that political leaders in countries characterized as resource-rich and authoritarian will act indifferently when it comes to financial sector advancement.¹ This thesis provides a novel explanation as to why it can be in the interest of authoritarian resource-rich leaders to advance their financial sectors. The thesis employs Angola and the notable financial sector change that the country has experienced since early 1990 as a case study to advance this theory.

At the beginning of the 2000s, Angola's financial sector was amongst the smaller ones in sub-Saharan Africa with merely \$3 billion in assets (Boone, 2005; George, 2015).² Yet, in under two decades, the sector had grown to become one of the main sectors in the region's third largest economy (Wallace, 2014).³ Previously dismissed on the basis of their simplicity, Angolan banks are growing increasingly well-versed in the sphere of global finance, a transformation fuelled by the commodity boom of the last decade (Wallace, 2014). In a country where less than 30 years ago people relied on packs of beer cans as a

¹ See for instance Bhattacharyya and Hodler (2014) and Barth et al. (2008).

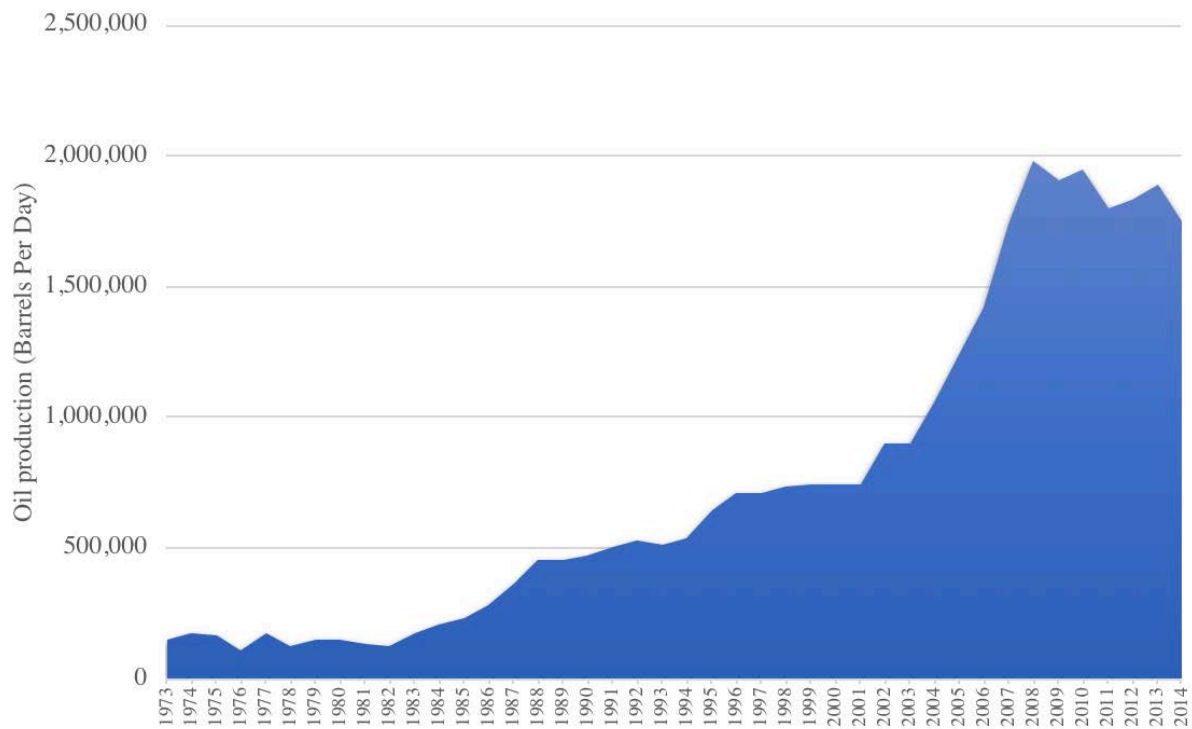
² According to a comparison of 19 sub-Saharan African countries for which adequate data was available, Angola's financial sector was the third smallest by assets in 1998 (Boone, 2005, p.405). From the sample of countries, only the financial sectors of Zambia and Sierra Leone were smaller than that of Angola.

³ By 2013, the Angolan financial sector held an estimated \$60 billion in assets (George, 2015).

medium of exchange (Birmingham, 2015, p.96), debit cards are today widely accepted across Angola's capital city of Luanda.

Angola's financial sector advancements have come about in a particular context. Angola is the second biggest oil-exporter in Africa (OPEC, 2017), and oil production has increased greatly since the country's independence in 1975 (see Graph 1). The impressive growth of the oil sector has been a major driver of growth in the rest of the economy (OPEC, 2017).

Graph 1.1: Angola crude oil production, 1973-2014



Source: U.S. Energy Information Administration (2015) Directorate of Intelligence (1987).

Whilst the oil sector has progressed significantly since independence, political power has remained in the grip of the ruling party, the Movimento Popular de Libertação de Angola (MPLA) since 1975 and the president, José Eduardo dos Santos, from 1979 to

2017. The Angolan regime is best described as authoritarian one where popular demand does not readily translate into policy (Roque, 2009; Soares de Oliveira, 2015). Rather than tending to the needs of the population, abundant resources revenues are assumed to have allowed the Angolan regime to act in a largely autonomous manner.

Central to this research endeavour is addressing the question of why political leaders⁴ with access to abundant resource wealth, as is the case in Angola, are motivated to promote financial sector change in the absence of pressures shown to have stimulated such change elsewhere, be it through popular demands routed through formal political institutions (Barth et al., 2008; Bhattacharyya and Hodler, 2014) or in the form of pressure coming from domestic business entrepreneurs (Calomiris and Haber, 2014). The thesis argues that even in the absence of effective political institutions, it is too simplistic to assume that political leaders act unconstrained. Rather this thesis assumes that even in the case of resource-rich countries, political leaders rely on the support of critical constituencies to maintain power (Bueno de Mesquita et al., 2003). To maintain social order, what is here referred to as a political settlement,⁵ political leaders moreover need to ensure that critical constituents are getting a share of economic resources to match their power and expectations. If not, political leaders risk the social order becoming undone (Khan, 2010, p.4).

Based on the above assumptions, the thesis argues that political leaders introduce financial sector change when economic performance becomes too poor or falls below the

⁴ Discussed further in section 5 of this introductory chapter, political leaders are defined as “those who have the authority to raise revenue and allocate resources to pursue chosen policies” (Bueno de Mesquita et al., 2003, p.38-39).

⁵ “A political settlement is a combination of power and institutions that is mutually compatible and also sustainable in terms of economic and political viability” (Khan, 2000, p.4). The concept will be presented and discussed in chapter 2.

expectations of critical constituencies. Financial sector change is thus part of political leaders' efforts to maintain the existing settlement. The direction of institutional change and political leaders ability to carry out the prescribed changes are in turn contingent on the policy space that they enjoy vis-à-vis domestic and international actors. In the case of resource-rich Angola, I argue that the leverage that political leaders enjoyed vis-a-vis domestic actors and international actors was closely tied to their access to oil revenues. When oil prices were high, political leaders were able to take a long term view when it came to policies that would form the financial sector with little external interference. When prices were low, short-term policies prevailed and international actors enjoyed greater sway over the policy process.

After this brief presentation of the thesis argument, the introductory chapter will proceed by outlining the research puzzle that motivates this study and the consequent research questions. After stating my research question, I will delve into the arguments of the thesis in greater depth. Subsequently, I turn to the justification of Angola as the case for this study and ask what the country is a case of. This justification exercise helps me situate the Angolan story in a larger comparative context and leads me to the last section of the introductory chapter where I discuss and rationalize the methodological choices that guide the thesis. I emphasize issues related to conducting field research in an authoritarian country. Finally, I give an overview of the forthcoming chapters, discussing their unique contribution but also how they help support the overall argument of this thesis.

2. Research puzzle

The existence of a negative relationship between the presence of abundant non-renewable natural resources⁶ and financial sector development has been demonstrated by a growing body of cross-country studies.⁷ That there appears to be a *resource curse*⁸ in financial development is worrying, given that the preponderance of existing research suggests that countries with better functioning financial institutions grow faster (Levin, 2005).⁹ The negative correlation between resource abundance and financial sector development is also paradoxical. Whilst many developing countries struggle to attract international investors or have limited access to international financial capital markets due to collateral constraints, this is less of a problem for resource-rich countries (Asiedu, 2006; Arezki et al., 2015). Windfall gains from resources, higher incomes and the resultant expansion of the non-traded goods sector should in theory lead to a higher private demand for financial services in these countries, consequently deepening their financial systems (Beck and Poelhekke, 2017). Yet the opposite is more often the case. On average, countries rich in resources exhibit lower levels of financial development, normally measured as the ratio of private

⁶ From now on referred to as simply resources. By non-renewable natural resources I am referring to oil, gas and minerals.

⁷ See for instance Beck, 2010; Beck and Poelhekke, 2017; Bhattacharyya and Hodler, 2014; Barajas et al., 2013. The negative relationship between resource-abundance and financial sector development is also confirmed by van der Ploeg and Poelhekke (2009), who also show that countries with better developed financial sectors are able to cope better with the adverse effects of resource dependence in the form of high commodity price volatility.

⁸ The idea of a resource curse refers to the recurring paradox that countries rich in natural resources are found to perform worse across a number of development indicators, including lower economic growth (Sachs and Warner, 1995), conflict proneness (Collier and Hoeffler, 2004) and political development (Ross, 2001).

⁹ Historically, a heated debate among economists has concerned the role of the financial sector in economic growth. More specifically, scholars disagreed on whether financial sector development has a positive effect on economic growth, whether financial sector development follows from economic growth or whether financial sector development does not have any effect. Central work in this regard includes McKinnon (1973); Shaw (1973); Robinson (1952); Lucas (1988). More recent, comprehensive reviews of existing literature on the topic conclude that financial sector development tends to assert a positive effect on long-run economic growth (Levin 2005; Beck, 2008). The effect of financial sector development on other dimensions of economic development, including poverty alleviation, is more mixed (Levin, 2005).

sector lending to gross domestic product (GDP)¹⁰ (Beck, 2010). Beck (2010) finds that financial institutions in oil-rich countries do a worse job at intermediating domestic savings into domestic investment and allocate scarce resources less effectively.

Different explanations have been adopted in an effort to explain the adverse relationship between resource-abundance and finance. One influential strand of the literature maintains that low financial sector development is due to the structural conditions of these countries that either limit demand or hinder their ability to meet rising demand. Starting on the demand side, the overall demand for external finance is expected to be less in resource-rich countries because non-resource sectors are crowded out by the extractive sector, which typically receives financing from abroad.¹¹ Because the non-extractive sector tends to be smaller in resource-rich countries, the demand for external finance suffers (Gylfason, 2004; Beck and Poelhekke, 2017). Others argue that firms in resource-based economies demand the same level of external finance as firms in other countries and that the problem is rather one of supply. Beck (2010) argues that financial development in resource-rich countries suffers because the financial sector is not prioritized but falls in the shadow of the extractive sector. Lack of supply of financial services can also be due to weak legal protections for investors, as demonstrated by La Porta et al. (1997; 1998; 1999; 2000). In what has since become an influential strand of literature, it is argued that a country's legal tradition significantly determines the extent to which the current legal system protects minority

¹⁰ Private sector lending to GDP measures the ability of banks to channel resources to borrowers. Another measure of the size or depth of a financial system is the ratio of liquid to GDP, which captures the monetary resources mobilized by banks (Upadhyaya, 2017).

¹¹ What is known as the 'Dutch disease' effect. The Dutch disease, introduced in the work of Corden and Neary (1982) and Neary (1988), refers to the structural changes that occur in an economy when a boom in the export of resources reduces the competitiveness of non-resource exports. The concept will be further explored in chapter 2.

shareholder and creditor rights, thus conditioning the development of financial markets (La Porta et al., 1997; 1998; 1999; 2000).

Whilst compelling, these large-N studies fall short when it comes to accounting for the heterogeneity in financial outcomes across countries, even within the subset of countries with similar legal origins or economic structures. Additionally, as Rajan and Zingales (2003) underscore, the history of financial sectors is one of advances and reversals, something that is hard to reconcile with the idea of structural determinants of financial development. Especially at the early stages of economic development, access to financial services may be limited to the wealthy and connected (Lamoreaux, 1986; Haber, 1991). In the words of Rajan and Zingales (2003), “this is not to suggest that structural theories are incorrect, but that they are incomplete. A theory with a more variable factor is needed to explain both the time series variation in financial development as well as the cross-sectional differences” (2003, p.7).

A more recent strand of literature seeks to address this shortcoming in the finance and growth literature by introducing a political economy dimension. Influenced by the work of Acemoglu and Robinson (2012) and Acemoglu et al. (2001; 2005), the political economy of finance literature contends that political institutions are an important determinant of the quality of financial institutions as it impacts on the financial sector policies chosen by countries’ political leaders (Calomiris and Haber, 2014; Barth et al., 2008; Bhattacharyya and Hodler, 2014). The concept of political institutions is here used to signify the competitiveness and regulation of political participation, the openness and competitiveness of recruitment, and constraints on the executive (Bhattacharyya and Hodler, 2014). By introducing basic aggregate measures of the quality of political institutions, the political

economy literature suggests that the relationship between resources and finance is mediated by institutional quality (Bhattacharyya and Hodler, 2014). Specifically, as argued by Bhattacharyya and Hodler (2014), resource rents negatively affect financial development in countries with weak political institutions, but that the negative effect decreases in absolute value and eventually vanishes as the quality of political institutions improves. The findings of Bhattacharyya and Hodler (2014) corresponds with that of the broader literature interested in the impact of resource abundance on economic development, which finds that countries are less likely to be ‘cursed’ by their resource abundance when the institutions that hold politicians in check are stronger (Mehlum et al., 2006; Boschini et al., 2007).

Whilst the latter strand of literature is less deterministic than the authors who argue that resources have an unconditional effect on financial sector outcomes (Herb, 2017), the former still leaves much unexplained. Notably, the aggregate measures of political institutions utilized by amongst others Bhattacharyya and Hodler (2014) does not provide us with a satisfactory picture of how politics works in different country contexts. Amongst other reasons, which will be further discussed in the next chapter, this is because these studies assume political bargaining to only take place through formal political channels, such as elections. The rigid understanding of how politics works and influences institutional outcomes in the financial sector is problematic and risks missing important nuances that can help us make sense of financial sector change. For instance, in his study of the banking sector in the Philippines, Hutchcroft (1998) shows how even in the face of weak political institutions, power politics was integral to key financial policies such as those involving banking supervision and credit allocation. Similarly, in their 1997 study of financial liberalization in then authoritarian Nigeria, Lewis and Stein found that political and institutional factors were fundamental to explaining the disappointing outcomes of

financial sector reforms in the country. Boone (2005) likewise emphasizes the domestic political economy as a key variable explaining divergent success in banking sector reform across sub-Saharan Africa. And as Johnson (2000) clearly demonstrates in the case of post-Soviet Russia, banking and politics cannot easily be disentangled because controlling the banking system habitually means controlling the economic lifeblood of a country.

Whereas differences in financial sector performance amongst democracies have been the subject of some scholarly attention,¹² we still know fairly little about what causes variation in financial sector performance between non-democratic countries — a category into which resource-rich countries frequently fall.¹³ Variation between autocracies is often disregarded based on the assumption that these countries' financial sectors are small and repressed (Ferreira and Soares de Oliveira, forthcoming). The implication of such an assumption in the literature is that authoritarian countries are typically grouped together, even when financial sector performance in these countries vary significantly.¹⁴ The degree of variance amongst resource-rich authoritarian countries is exemplified in a 2006 IMF study on financial sector development in the Middle East and North Africa region, where resource rich countries were amongst the highest scorers in the region¹⁵ but also amongst the worst¹⁶ (Creane et al., 2006). Similarly, on the African continent, Gabon, the Republic of Congo and Angola all fall into the same group of resource-rich and authoritarian states yet the countries' financial sectors differ notably in their performance and setup. All countries have undergone considerable financial sector liberalization, but whilst most

¹² See for instance Menaldo and Yoo (2015), Bordo and Rousseau (2006), Keefer (2008).

¹³ The link between resource-abundance and authoritarianism will be discussed in more detail in section 5 of this chapter. The view that oil and mineral abundance is linked to authoritarianism is widely held in the literature. See for instance Mahdavy (1970); Beblawi (1987); Karl (1997); Wantchekon (2002); Ross, 2001. Ross (2001) shows how a higher ratio of oil and mineral exports to GDP is correlated with lower levels of democratization.

¹⁴ As in the case of Bhattacharyya and Hodler (2014).

¹⁵ Bahrain, Kuwait, Oman, Saudi Arabia, UAE, Qatar.

¹⁶ Iran, Sudan and Libya.

banking operations in the Republic of Congo are foreign banks or branches of foreign banks, the financial sectors in Angola and Gabon continue to be state dominated (State Department's Office of Investment Affairs, 2017; Making Finance Work for Africa, 2017b). And whereas private sector credit as a percentage of GDP — a common measure of financial sector depth – constituted only 14% in Gabon for 2015, in Angola's case the same share was almost 30% (World Bank, 2017a). Consequently, the differences observed between countries assumed to be equivalent based on their political institutions, suggests that there is a need to disaggregate the picture further.

The limited attention devoted to understanding the political economy dimension of the resource and finance story has led researchers to make oversimplified assumptions about the incentives faced by political leaders in resource-rich countries when it comes to the financial sector. Existing studies assume that where formal political institutions are weak, non-democratic leaders need not concern themselves with popular support for their policies and the risk increases that political leaders will engage in rent seeking behaviour to the detriment of the financial sector (Bhattacharyya and Hodler, 2014; Barth et al., 2008). Leaders of democracies, on the contrary, risk being removed at the next election if they fail to act in a manner conducive to growth and are therefore incentivized to promote financial sector development even if access to abundant resource wealth means that they do not have to do so (Bhattacharyya and Hodler, 2014). Yet, it is known that developmental outcomes can arrive in the absence of quality political institutions.¹⁷ This is also the case for the financial sector. Bahrain and Chile (between 1973 and 1988) are cases in point where financial sectors advanced in spite of sizable resource revenues and weak political

¹⁷ See for instance Whitfield et al. (2015), Lewis (2007), Ang (2016), and Haber et al. (2003). The authors all demonstrate instances where weak political institutions and developmental policies have coexisted.

institutions.¹⁸ These examples underscore that whilst political leaders of resource-rich authoritarian countries might choose to act in a way that damages the financial sector, leaders might also choose to act in a manner conducive to financial sector advancement. An abstract understanding of a country's political institutions based only on a reading of formal institutions is of limited help to explain why some resource-rich authoritarian countries chose to institute financial sector change and others not. Rather, one needs to delve deeper into the political economy of these countries to uncover the causal processes underpinning the observed change. Existing large-N studies are not very useful in this regard and do not offer a ready explanation for how institutions conducive to financial development emerge. Overall, there has been little effort to explain the process of financial sector change as existing large-N studies remain fixated on outcomes. The fixation on financial sector outcomes over performance is problematical, because in the majority of developing countries, resource rich and authoritarian included, considerable change to the structure and role of financial sectors has taken place over the last 40 years. These processes remain largely unexplained.¹⁹

3. Defining the dependent variable

The objective of this thesis is to understand the drivers of financial sector change. As was stressed in the proceeding section, in the existing finance and resource literature, financial development is understood as an outcome whilst the process of financial sector change is

¹⁸ Both countries are amongst the top 70 percentile private credit to GDP levels according to the World Bank (2017) indicator "Domestic credit provided by financial sector (% of GDP) 2016". Bahrain is categorized as "Not Free" according to Freedom House (2017). Chile was a military dictatorship under Augusto Pinochet when it undertook extensive economic reforms paving the way for financial development (Haggard and Kaufman, 1992).

¹⁹ There are notable exceptions in this regard of studies that focus on the process of financial sector change over outcome. These studies are referred to multiple times throughout this study and include Hutchcroft (1998); Lewis and Stein (1997); Boone (2005); Johnson (2000) and Haber et al. (2003).

often ignored. Financial sector performance is moreover commonly measured as private credit to GDP (Beck, 2010), which means that a functioning financial sector is understood to take a particular form; one that provides information so as to enhance resource allocation, monitor investments and exert corporate governance after providing finance thus helping to boost the efficient use of scarce resources. Additionally, a functioning financial sector is expected to provide diversification services to alleviate risk, mobilize and pool savings and facilitate the exchange of goods and services (Demirgüç-Kunt and Levin, 2008). It follows that financial development takes place when “financial instruments, markets, and intermediaries ameliorate—though do not necessarily eliminate—the effects of information, enforcement, and transactions costs and therefore do a correspondingly better job at providing the five financial functions” (Demirgüç-Kunt and Levin, 2008, p.4).

The definition of financial development that dominates current literature does not leave the direction of institutional change open. It assumes that countries naturally progress towards a particular type of financial sector, characterized by free markets and arms-length transactions. The problem is that such aggregated measure of financial sector change do not capture financial sector change more broadly (Creane et al., 2003). A financial sector characterized by arms-length transactions might not be the type of scenario to which countries aspire²⁰ and even if it is, financial sector change might not produce the outcomes that political leaders intended. Demirgüç-Kunt and Levin (2008, p.4) acknowledges such scenarios when they remark that because “laws, regulations, and policies differ markedly across economies and over time”, improvements along any one of these dimensions should

²⁰ The case of Ethiopia comes to mind where political leaders preference for strong political control over the financial industry shapes the development of the sector. Seeking to emulate the development model of the first East Asian newly industrialized countries, financial repression represents a key tool in the pursuit of rapid industrialization for the Ethiopian government (Weis, 2016).

be expected to have “different implications for resource allocation and welfare depending on the other frictions at play in the economy”.

Additionally, one can imagine a situation in which it would be in the interest of some political leaders to endorse certain features of what is understood to be a developed financial sector whilst holding back in other respects. For instance, in the study by Haber et al. (2003) of Mexico under Porfirio Díaz (1830-1915), the authors show how property rights can be enforced selectively so as to facilitate a rent generating partnership between bankers and rulers. As existing studies are interested only in capturing outcomes for the sector as a whole, the conventional way of defining financial development misses such important details.

Consequently, in this thesis I will widen the focus from financial sector development to institutional change in the financial sector. Focusing on financial sector change opens up the possibility of explaining it also in cases where financial sectors are doing a poorer job at channelling resources to borrowers, which is what the much used private sector credit to GDP measure captures. The understanding of financial sector change that I adopt in this thesis is in line with how the Cambridge English Dictionary (2017) defines development, namely as a “process in which someone or something grows or changes and becomes more advanced”. Whilst the definition assumes that financial institutions and markets become more advanced as they develop, the definition does not assume that markets become more inclusive.

In order to further clarify the dependent variable, let us now turn to the case study of the thesis, Angola. Advancement from one banking order to another has been a key aspect of

Angola's financial sector experience in the decades since the country's independence in 1975 (IMF, 2015; Bureau of Economic and Business Affairs, 2017).²¹

After independence in 1975 the Angolan government nationalized all financial institutions in response to new economic realities and in line with the socialist leanings of the ruling party, the MPLA. The country became a de facto mono-banking system; with a central bank, Banco Nacional de Angola (BNA), which also acted as the only commercial bank (Law no. 4/78; Ferreira, 2002b). The degree to which the BNA carried out the task of ordinary commercial banks was limited, however, and predominantly the BNA lent to the government (World Bank, 1991). Political leaders controlled access to financial sector resources by retaining everything under state control and setting financial sector policies according to state priorities. The activities of the financial sector were limited at the time because domestic economic activity overall was limited. The major exception in this regard was the oil sector. Quickly after independence, oil became the country's main revenue earner and source of foreign exchange (Soares de Oliveira, 2007). The BNA was the sole legal holder of this foreign exchange but had little influence over how the currency was used, acting rather as a dispenser of foreign currency to the wider economy (Hodges 2001; World Bank, 2001).²²

With the opening up of the Angolan economy from 1987, the structure of the financial sector changed. Importantly, the state's grip on the economy loosened in a number of

²¹ The financial sector will refer to the banking sector specifically when not specified otherwise (such as in chapter 6). This is not due to a lack of interest in non-banking institutions. Rather, as will become clear in subsequent chapters, for most of Angola's history banks have dominated the financial sector whilst the emergence of non-banking financial institutions has lagged significantly behind. Equating the financial sector with the banking sector is not unfounded in other developing countries either where non-banking financial institutions often lag behind (Calomiris and Haber, 2014)

²² The Ministry of Planning set annual exchange budgets according to government priorities.

important areas, including bank entry. A two-tier banking system was established in 1991 (Law no. 5/91), with two commercial state-owned banks inaugurated followed by the entry of foreign banks in 1992 (World bank, 1992). A large number of enterprises were privatized (Decree no. 32/89), which meant that the demand for banking services and foreign exchange was no longer limited to the state but also opened to private individuals and firms. Nonetheless, the state maintained its dominant role in the financial sector as in other parts of the economy after the initial liberalization of 1991. The state kept interest and foreign exchange rates artificially low (IMF, 1995; 1997). Such administrative measures permitted those Angolans who had access to subsidised loans and foreign exchange to become exceedingly rich to the detriment of the nascent commercial banks (Hodges, 2001; Ferreira, 1995).²³ Also emerging at this stage were the locally-domiciled foreign banks, who were able to, largely unconstrained, carve out a space in the mounting interactions between the local economy and the global markets.²⁴

The state monopoly in crucial domains such as foreign exchange did not subside until 1999 when further liberation of Angola's financial sector was introduced,²⁵ opening up the lucrative foreign exchange market to commercial and foreign banks. 1999 also saw the end to other administrative measures that had marked the financial sector during the first decade of the country's transition from socialism, including the liberalization of interest rates

²³ The administrative practices on behalf of the state meant that the bank businesses were loss making.

²⁴ The oil sector remained an economic (and physical) enclave throughout the 1990s, its interaction with the domestic economy wholly intermediated through the state. Interview, banker previously Angolan public bank, Luanda 20.09.2015.

²⁵ From 1999, banks and exchange houses were permitted to buy and sell foreign currency at freely negotiated exchange rates (Notice no. 1/99). Banks domiciled in the country could open current and foreign currency deposit accounts in the name of residents and non-residents (Notice no. 4/99), they could carry out credit operations with exporters (Notice no. 5/99) and capital restrictions were significantly eased (Notice no. 10/99; Notice no. 11/99). The requirement of prior BNA approval of foreign exchange purchases for imports was abolished; limits on purchases of foreign currency for travel and transfer abroad were substantially relaxed; some capital account transactions were pre-authorized up to maximum amounts specified in United States dollars; and external tariffs on imports and exports were drastically reduced (IMF, 2000).

between banks and clients (Notice no. 7/99). The liberalisation measures meant that commercial banks were able to take advantage of the financial sector business previously reserved for the state (Hodges, 2001), as a result growing their balance sheets, from 4.2 billion Kwanza in assets in 1999 to 139 billion Kwanza three years later in 2002 (BNA, 2007; IMF, 2000; IMF, 2005; IMF, 2007).

The growth on Angolan banks' balance sheet was particularly noticeable following the end of the country's civil war in 2002. The arrival of peace triggered an increase in government spending and growing economic activity in the oil sector. Money that previously was directed to finance the war effort could now be channelled elsewhere, including towards physical reconstruction of the country (Soares de Oliveira, 2015). An increasing amount of capital flowed overseas.²⁶ Bank credit to the economy grew markedly during the first post-war years, albeit from a low base (BNA, 2007). The post-2002 era moreover marked a different connection between the oil and the financial sector, as banks were no longer solely redistributing money that came through the state – even though it remained a main undertaking (Hodges, 2008). Banks were increasingly intermediating business opportunities that sprang up around the oil sector (BNA, 2007). By this stage, private Angolan banks had emerged with state-owned enterprises and current and former government employees amongst their shareholders. The Angolan private banks together with well-connected Portuguese banks became the main counterparts of foreign banks entering into business in the country at an increasing pace (Ferreira, 2005; Reuters, 2010). The growing activity in the banking sector did not readily translate into the development of the non-banking financial sector, however. Following several false starts, the non-

²⁶ Based on authors own calculations of net capital outflows as reported by the IMF 1995-2014. This finding is in line with that of Andersen et al. (2014) who show that, in the case of oil-rich authoritarian states, a rise in the international price for oil translates into greater amounts of wealth being hidden in secrecy jurisdictions overseas.

banking financial market, including capital markets but also insurance companies, pension fund management companies, and microcredit institutions remained largely absent in the post-2002 era (IMF, 2015; KPMG Angola, 2012; World Report International, 2005; *afrol News*, 2005).

The expansion of banking institutions and services in the early 2000s were not matched by the state apparatus readiness to regulate the sector (Wallace, 2014; IMF, 2012b). The weaknesses of the sector became apparent in the immediate aftermath of the 2008 global financial crisis when oil prices collapsed with devastating effects on Angola's state finances and on domestic banks' earnings (IMF, 2009b, p.28).²⁷ The stability of the banking sector was shaken when the state defaulted on payments to government contractors, who in turn were no longer able to service their loans (IMF, 2009b). It was clear that banks had not taken the necessary provisions to protect themselves from adverse economic conditions (Wallace, 2014; IMF, 2012b). Even if the banks had started to diversify their business into real estate and construction in the years prior to the crisis, their business model remained highly dependent on the state.²⁸ The signing of a Stand By Agreement by Angola with the IMF in 2009 marked the start of regulatory reform to the financial sector (IMF, 2009a; Engebretsen and Soares de Oliveira, forthcoming). With a greater emphasis on regulation post-2009, Angola was able to ensure that capital could continue to be moved outside with ease (Reuters, 2011). Additionally, the country sought to expand its access to international financing (EIU, 2011a). The post-2009 period therefore signified an important role change

²⁷ The global price for crude fell from an average of \$97 a barrel in 2008 to \$44 in the first quarter of 2009, shifting Angola's fiscal and external surpluses to substantial deficits (IMF, 2009b).

²⁸ Interview, representative IFI Financial Markets specialist, Washington DC 8.12.2016.

for the Angolan financial sector, as a number of larger banks went from being fixated on redistributing state revenue to increasingly wanting to retain and attract capital as well.²⁹

From this brief overview of Angola's financial sector trajectory, it is clear that the country's financial sector has witnessed considerable change and advancements over recent decades. Yet, a theoretical framework to explain political leaders' motivation for introducing the changes that have succinctly been presented here, is lacking. The resolve to address this gap in the literature leads me to the research questions presented in the next section.

4. Research questions

The discussion so far highlights a gap in our knowledge concerning the drivers of financial sector change in what I have so far referred to as resource-rich authoritarian countries (to be defined in section 5). Existing theories suggests that a weak financial sector will persist in resource-rich authoritarian countries but as was highlighted earlier, the picture is not uniform. Moreover, the nature and performance of these countries' financial sectors changes over time, as the example of Angola so vividly illustrates. The puzzle motivates the central question of the thesis, which is *why do political leaders of authoritarian resource-rich countries choose to introduce financial sector change?* By asking the latter question, the thesis will also shed light on the highly interconnected question, which is *what underpins the direction of financial sector change in authoritarian resource-rich countries?*

²⁹ In 2014, Angola's leading private bank BAI became the first Angolan bank to gain an international credit rating. Theodore Giletti, Director of BAI, speaking at Chatham House (2015); BAI (2014). The implementation of a foreign exchange law for the oil sector (Law no. 2/12) in 2012 helped channel more business to the Angolan domiciled banks.

5. Central arguments

In the thesis, I argue that to understand financial sector outcomes in non-democratic resource-rich countries one needs to take seriously the role that politics plays in shaping institutional outcomes. The thesis shows how political leaders chose to instigate institutional change in the financial sector, at times advancing it, as a way to maintain their hold on political power. Drawing on the definition of Bueno de Mesquita et al. (2003, p.38-39), I use the concept of political leaders in this thesis to signify “those who have the authority to raise revenue and allocate resources to pursue chosen policies”. As becomes clear from studying Angola’s immediate post-independence period (the focus of chapter 3) the composition of the country’s political leadership is not static over time. However, within a short time of independence, decision-making power become concentrated in the executive and his immediate advisors, civil and military (Soares de Oliveira, 2015; Jones et al., 2013). Whereas in Angola, political authority is exceedingly concentrated and exercised by a small number of individuals, in other cases, which fall under the same description of resource-rich and authoritarian, power is more dispersed.³⁰ I consequently use the term political leadership so as to enhance the generalizability of the study. That being said, I endeavour to specify the actors involved whenever possible.

Building on the political settlements approach as first developed by Mushtaq Khan (1995; 2010; 2017), I assume that for political stability to prevail and political leaders to sustain power, the distribution of resources from a society’s prevailing institutional structure needs to be aligned with the division of political power. Equally important, the institutions, both formal and informal, have to achieve minimum levels of economic performance and

³⁰ Nigeria pre-1999 comes to mind as a case where concentrating authority has been difficult due to the multiple cleavages between political elites (Lewis, 2007). Additionally, the fragmented Saudi Arabian state as described by Hertog (2011).

political stability to endure (Khan, 2010). Ruling coalition is the factions that support political leaders in an incumbent regime (Kjær, 2015; Goodfellow, 2017), and whose support translates into victory (Bueno de Mesquita et al., 2003).³¹

The kind of institutions that a ruling coalition and the political leaders it supports will be able to form and sustain is understood to depend on its internal structure (that is, the strength of lower-level elite factions also called the vertical distribution of power) and the ruling coalition's position within society (that is, the strength of excluded factions also called the horizontal distribution of power) (Khan, 2010).

Drawing on evidence from the Angolan case, I argue that financial sector change can be a reactive strategy by political leaders in times of weakness. Findings presented in this thesis suggest that responding to external pressures by political leaders to reform Angola's financial sector was necessary in order to improve the country's economic performance. The nature of the pressure also determined the direction of institutional change, towards greater market liberalization in the 1990s and tougher banking compliance in the late 2000s. Yet acting on such international pressure did not mean that political leaders had to discontinue the use of the financial sector to serve their political purposes. An important reason for why political leaders have been able to shape reform outcomes to their advantage was that external conditions became more favourable and external pressures therefore did not endure (Aguilar, 1999). Political leaders were equally skilled at appeasing external actors whilst not giving up too much policy space (Shaxson, 2009; Ferreira and Soares de Oliveira, forthcoming). Therefore, even in the face of sector liberalization throughout the 1990s, the commercial state-owned-banks maintained their role as de facto extensions of

³¹ Bueno de Mesquita et al. (2003) coins this the "winning coalition".

the state and of state-largesse to critical constituencies. Unlike many other developing countries that transitioned from a centrally planned economy, Angola never privatized its state-owned banks but maintained them as a key part of the financial sector. Likewise, the regulatory advancements introduced post-2009 helped strengthen the economic clout of the Angolan banks to the benefit of political leaders and not to the detriment of the latter's discretion over the sector.

Financial sector change does not need to come from a position of weakness, however. It has also been a way for a country's political leaders to consolidate their power from a position of strength, allowing economic performance to be enhanced and leaders' power to be fortified. Financial sector change can open up new avenues for accumulation and added roles for the banks, as was evident in Angola from the late 1990s, at the end of the war in 2002 and after the global financial crisis of 2008. In the late 1990s, the liberalization of the financial sector allowed state and state-connected private businesses to take advantage of market opportunities that so far had been unavailable, to the benefit of the wealthy and connected (Hodges, 2001). Correspondingly, financial sector change in the early 2000s also materialized as the MPLA and its leaders, found themselves in a position of strength. Political leaders in the post-war era realized the usefulness of the banking sector, not only to contribute to the physical outreach of the state through the expansion of bank branches and to accommodate political allies but, perhaps more importantly, to ensure the connection to global financial markets so as to ease the outflow of capital. More recently, post-2009, Angola's financial sector has transformed beyond the role of distributor of financial resources to increasingly attracting resources as well. Greater alignment between Angola's financial regulation and international best practice meant that local financial institutions

could tap into international financial markets to a degree that had hitherto not been possible, thus expanding the financial means available to the country's ruling coalition.

My thesis argument thus builds on the assertion that financial sector change is closely linked to political leaders bid to maintain and even strengthen political power. I use the Angolan case to substantiate my argument for reasons stated in the next section.

6. Why Angola and what is it a case of?

In an effort to widen our knowledge of financial sector change in the resource-rich authoritarian context, the thesis will rely on an in-depth case study of Angola. The thesis will cover the period from the country's independence from Portugal in 1975 to 2014, with an emphasis on the period after the official transition to a market economy in 1991. The period of study ends in 2014 because that year marks the end to the commodities super cycle of the 2000s and the beginning of a new period in Angola's post-war history. A case study of Angola was chosen as the preferred research strategy for the project for two main reasons.

First, Angola is a typical case of a resource-rich authoritarian country, meaning that it exemplifies what is considered to be a typical set of values for the broader group of countries to which the country belongs (Gerring, 2007). Resource-rich authoritarian countries, which I will define below, have often been ignored in the large-N literature on the grounds of their overall poor financial sector performance. Yet as was established earlier, remarkable change has taken place in the country's financial system over the last three decades. This makes sector change in the country difficult to dismiss outright. Change from one banking order to another is a key aspect of Angola's financial experience and it

is a trajectory that it shares with other resource-rich authoritarian countries. Shedding light on the Angolan trajectory therefore represents a first step in gaining a better understanding of financial sector change in the resource-rich and authoritarian context.

The second reason why Angola was chosen for the study is that the case allows us to reconsider the role of the state in the story of financial sector change. An assumption in the political economy of finance literature is that financial sector change will be driven by bargaining between private holders of wealth on the one hand, and the demands of a political leader, on the other.³² Yet, in the Angolan case, financial sector change has historically been driven by the state and even in the face of financial liberalization, the state has remained firmly in control of the sector. Angola is not unique in this regard. The distinction between private capitalists and the state has proven problematic in other post-communist countries, including Russia (Johnson, 2000), across Central Asia (Cooley and Heathershaw, 2017) and China (Shih, 2007).³³ The situation is not limited to former communist countries, however. As Arriola (2013) displays, in much of post-independence Africa, the state acted as a *de facto* gatekeeper for capital to the detriment of private sector entrepreneurs. Yet, due to historical circumstances, it could be argued that Angola's experience is particularly extreme. A combination of historical and more contemporary circumstances, made it so that no significant counterweights to the state in the economy developed in Angola's modern history. Prior to independence, in Angola like in Portugal's other colonies, private capital was dominated by European settlers (Gonzalves, 2011; Pitcher, 2002). When independence came in 1975 and Portuguese settlers fled, the majority

³² As argued by Calomiris and Haber (2014), financial sector outcomes reflect a deal struck between political leaders in need of financing and financiers seeking government guarantees (p. 38-41). Similar reasoning is presented by Haber et al. (2003); Rajan and Zingales (2003); Girma and Shorthand (2008).

³³ China is still a unitary one-party socialist republic but since 1978 the country has been in the process of replacing its socialist economic system with state capitalism.

of the economy was nationalized, excluding the oil and diamond sectors (Ferreira, 2006). A private informal commercial sector flourished in the 1980s, led by Northern Angolans of largely Bakongo origin who had returned to Angola after seeking refuge in the Democratic Republic of Congo (Zaire). Yet the Bakongo never came to constitute a consequential group of private capitalist in Angola and the private sector activities of the returnees was increasingly repressed by the MPLA throughout the 1990s and people of Bakongo origin were victims of anti-MPLA purges in the cities (Birmingham, 2002; 2015). The MPLA's repression of any economic activity outside the purview of the state has ensured that the party has consistently controlled the distribution of economic resources in the country, ensuring that no counterbalance emerged that could jeopardize its hold on power.

This thesis further limits itself to the group of countries labelled as resource-rich. I follow the IMF classification of resource-rich countries as those that derive at least 20% of exports or 20% of fiscal revenue from non-renewable natural resources (IMF, 2012a).³⁴ Although it has been pointed out that resource abundance as a measure might better reflect export intensity or dependence than abundance (Brunnschweiler and Bulte, 2008), the definition is nonetheless appropriate for the purpose of this thesis seeing that I am interested in studying the impact of natural resource wealth on country outcomes rather than the natural resources per se (Kolstad and Wiig, 2009). Another useful concept to add in this regard is that of the rentier state, defined as countries that derive a large fraction of their revenues from external rents (Beblawi and Luciani, 1987).³⁵ Hussein Mahdavy is widely credited with giving the term its current meaning: a state that receives substantial rents from “foreign

³⁴ See Appendix 1 for an overview of the countries.

³⁵ In classic economic theory, rent is a surplus paid to the owner of the land after all the costs of production have been met (Yates, 1996).

individuals, concerns or governments” (1970, p.428). Hazem Beblawi later refined the definition, suggesting that a rentier state is one where the rents are paid by foreign actors, where they accrue directly to the state, and where “only a few are engaged in the generation of this rent (wealth), the majority being only involved in the distribution or utilization of it” (1987, p.51). Although the rentier state theory and revised versions of it, have most often been used to describe the experience of Middle Eastern oil exporters,³⁶ the concept helps explain the experience of other resource-rich countries included in the list above, where governments control a large portion of the resource revenues because laws allocate the ownership of finite resources to the state and the extractive sector is state-owned.³⁷

When studying the list of resource-rich countries as referenced above, the number of countries with authoritarian regime types stand out. Out of 50 countries defined as resource-rich according to the above definition, 28 are defined as *Not Free* by independent watchdog organization Freedom House, judging on countries’ political rights and civil liberties.³⁸ Despite the prevalence of resource-rich countries with authoritarian regimes, the group is poorly explained by existing literature as discussed earlier. This adds to the importance of selecting this group of countries as the focus of this study.

One challenge that quickly emerges when studying authoritarian regimes is the significant variance that exists within the group of countries categorized as authoritarian (Brooker, 2014). Rather than say what is meant by an authoritarian regime, it might be simpler to follow Linz’s (2000) lead in saying what it is not. Authoritarian regimes are non-democratic. Whereas democratic regimes are expected to meet certain minimum criteria,

³⁶ Including Beblawi (1987); Hertog (2010a; 2010b); Herb (2009); Gray (2011).

³⁷ Rentier state theory has also been applied to Sub-Saharan Africa e.g., Yates (1996) and Omeje (2008).

³⁸ For more information on Freedom House methodology see Freedom House (2017)

including free and fair elections, universal suffrage, political rights and civil liberties, authoritarian regimes, by contrast, violate these criteria frequently enough and seriously enough to create an uneven playing field between government and opposition (Linz, 2000; Levitsky and Way, 2010). At the one end of the spectrum, there are the ‘classic’ authoritarian regimes in which electoral institutions exist but yield no meaningful contestation for power (Levitsky and Way, 2010). Oil-rich Equatorial Guinea, Turkmenistan, and Qatar come to mind. However, a more common position in the post-Cold War era has been that of hybrid political regimes.³⁹ In its most basic form, hybrid regimes combine democratic and authoritarian elements (Diamond, 2002). Scholars have proceeded to give hybrid regimes many different names in an effort to capture the diverse experiences of these countries (Collier and Levitsky, 1997), including competitive authoritarianism (Levitsky and Way, 2010) and electoral authoritarianism (Schelder, 2002: 2006). Common to the above-mentioned subtypes is their emphasis on the use of formal democratic institutions, including elections, in obtaining and exercising political authority (Levitsky and Way, 2010; Schelder, 2002).⁴⁰ Angola, particularly since 2002, is habitually categorized in the latter group of hybrid regimes.⁴¹ Since the end of the civil war in 2002, the country has held three elections, yet each has been firmly controlled by the MPLA.⁴² Without going further into the debate of regime types, the point here is to acknowledge the considerable variation that exist between authoritarian regimes, and the prevalence of hybrid regimes like Angola, which challenge a strict dichotomy between democracy and authoritarianism.

³⁹ See for instance Diamond (2002); Collier and Levitsky (1997); McFaul (2002); Schelder (2002).

⁴⁰ As argued by Schelder (2006,p.36-37), “By organizing periodic elections they [political leaders] try to obtain at least a semblance of democratic legitimacy, hoping to satisfy external as well as internal actors. At the same time, by placing those elections under tight authoritarian controls they try to cement their continued hold on power.”

⁴¹ The categorization of Angola’s political regime as a hybrid one is used by Roque (2009) and Soares de Oliveira (2015). Croese and Pitcher (2017) use the concept of electoral authoritarian to refer to the regime.

⁴² As argued by Roque (2009) holding multi-party elections have helped the MPLA to gain long-elusive national and international legitimacy, thus cementing the ruling party’s hegemony further.

7. Methodology

An in-depth case study of Angola was deemed appropriate given the current state of knowledge in the field. As has already been established, existing models are not equipped to deal with the case of resource-rich and authoritarian regimes pursuing financial sector change, as the models remain too general. In order to establish the causal mechanisms driving the outcome of interest, it is necessary to take into account the different role that politics plays in countries often grouped together based on their regime type.

A heuristic case study of Angola allows us to inductively identify new variables and causal mechanisms that can be subsequently applied when studying other cases (George and Bennett, 2005). Case studies are moreover ideal for the purpose of theory development. With a case study design, existing theories can be brought up against complex realities. Moving beyond large-N studies through a case study design was deemed appropriate given the scant attention to the politics of finance in authoritarian and resource-rich contexts. Yet, as the thesis also demonstrates, the findings in the Angolan case have wider relevance and heuristic value, to the larger group of countries that I argue Angola is part of – resource-rich and authoritarian. Additionally, findings from the Angola case can shed light on financial sector drivers in a wider set of African countries where the relationship between the state and private sector has historically been skewed in favour of the former (Arriola, 2013).

It is also necessary to consider the limitations that come from proceeding with a single case study design. A common critique of case study methods is that they are particularly prone to selection bias.⁴³ Selection bias is the predisposition introduced by the selection of

⁴³ As argued by for instance Geddes (1990); King et al., (1994); Hug (2003).

individuals, groups or data for analysis in such a way that proper randomization is not achieved. In such cases, the sample is deemed unrepresentative of the larger population (see King et al., 1994, p.138-139). In case study research, cases are often chosen based on an observed outcome that one is interested in explaining and for which existing theories cannot offer a satisfactory explanation (Flyvbjerg, 2013). George and Bennett (2005, p.23) point out, in the early stages of research programmes, selection of the dependent variable can serve a heuristic purpose of identifying the potential causal paths and variables leading to the dependent variable of interest. Subsequently, the causal model identified in a case study can be tested against cases in which there is variation of the dependent variable (George and Bennett, 2005; Collier and Mahoney, 1996).

Related to the argument of selection bias is another criticism often lodged against case study analysis, which is their lack of representativeness. Because the sample is small and idiosyncratic, and because data is predominantly non-numerical, it is difficult if not impossible to establish the probability that findings are representative of a larger population (Gerring and Cojocaru, 2016). The latter is not the objective of most case studies, however. Rather, case study analysis typically emphasizes greater explanatory richness within a type of case at the cost of explanatory power across cases (Flyvbjerg, 2013). Case studies are consequently more helpful in identifying conditions under which specified outcomes occur, and the mechanisms through which they arise, rather than uncovering any frequency with which those conditions and their outcomes appear (George and Bennett, 2005, p.31). Furthermore, cases are often chosen exactly because of their unrepresentativeness of wider populations, seeing that such cases are often excluded from other forms of investigations that concentrate upon common patterns and themes in the data (Gerring, 2007; George and Bennett, 2005). The latter has often been the case with resource-rich countries, where the

economic structures are deemed too different to include these countries in a cross-case comparison (Beck, 2010). Theories developed through case study research are not expected to have wide-ranging applicability and any generalization is necessarily conditional and likely to be applicable only to the subclass of cases similar to the one under study (George and Bennett, 2005). That being said, the anticipation is that the causal mechanisms within the Angolan case will illustrate causal factors applicable in other case studies that share the country's characteristics (Seawright and Gerring, 2008).

7.1 Empirical justification and a note on sources

Beyond its theoretical value, the study of Angola has empirical significance. The study will be amongst the first that examines the political economy of finance in one of Africa's largest economies.⁴⁴ It will be the most comprehensive study of the financial sector in Angola to date and will thus provide researchers, policy makers and other stakeholders with novel insights into the inner workings of the sector, from the country's independence until today, with emphasis on the post-1991 period. Moreover, the thesis will contribute to the literature by making a first effort to situate the Angolan financial sector trajectory in a comparative perspective. In order to accomplish this task, the thesis builds on substantial empirical research and original data collected between 2015-2017. Five months of fieldwork were conducted in Luanda, Angola, supplemented by trips in the United Kingdom and to the United States.

Extensive fieldwork is especially important when studying post-conflict and authoritarian countries like Angola where data is often limited and when it exists, can be of dubious

⁴⁴ A notable exception is Ferreira and Soares de Oliveira (forthcoming) and Engebretsen and Soares de Oliveira (forthcoming).

quality (Art, 2016).⁴⁵ Because of Angola's prolonged conflict, global development data covering the country is incomplete.⁴⁶ The IMF has flagged the "lack of timely, accurate, and comprehensive data for all economic sectors" in Angola as a serious problem throughout the 2000s.⁴⁷ Relying only on the use of secondary data in the case of Angola is therefore problematic and would risk producing an analysis that is not only incomplete but also prone to inaccuracies. Similarly important, as highlighted by Araham and Goode (2016), in using publicly produced data in an authoritarian country like Angola one runs the risk of replicating the regime's claims to legitimacy. Whereas replicating the regime's claims to legitimacy to some extent is unavoidable, "scholars must be wary of relying on regime-produced interpretations of those data" (Araham and Goode, 2016, p.842). The latter does not mean that secondary sources should be avoided. Secondary sources, including detailed reports published by the IMF and World Bank as well as NGO reports and international news coverage, represent an extremely valuable source of information, allowing the drawing of ready comparisons between Angola and other countries. To ease cross-country comparison, throughout the thesis I state values in terms of US dollar (denoted as \$) whenever possible. Using the US dollar as the unit of measurement is moreover appropriate given that the value of Angola's national currency, the kwanza, has been subject to great changeability during the period of study. Four different currencies using the name kwanza have circulated since 1977, three of them in the 1990s (Hodges, 2001).⁴⁸

⁴⁵ Art (2016) provides a strong case for the importance of fieldwork for theory development in political science.

⁴⁶ For instance, the World Bank Development Indicators only covers Angola from 1995.

⁴⁷ See for instance IMF (2000), IMF (2003), and IMF (2005).

⁴⁸ During the 1990s, the kwanza moreover experienced prolonged periods of hyperinflation, further undermining the currency's function as an unit of account (Aguilar, 2001).

To ensure the soundness of the data used in this thesis, I make use of multiple data collection methods to substantiate my claims. The use of several data collection methods and sources in the study so as to verify my findings, what is known in the social sciences as triangulation, is also compatible with the use of process tracing in the study. The process tracing method necessitates the collection of large amounts of data from a wide range of sources in order to link causes with outcomes (Tansey, 2007; Beach and Pedersen, 2013).

In the course of fieldwork, I collected primary written sources dating back to the early 1970s. These included MPLA party documents, company reports, and newspaper articles. Additionally, important sources of official legislation, including laws and resolutions enacted by the National Assembly, Presidential Decrees and Decree-Laws, Decrees and Resolutions of the Council of Ministers were consulted. I also visited newspaper archives in Luanda and in the United Kingdom. Since 2002 the availability of data in Angola has improved,⁴⁹ and consultancy reports, research papers, records and communications published by government entities, as well as official meeting protocols, are more frequent, although they are not always easily obtainable.

During my data collection efforts, it was quickly confirmed to me that “information is power” in Angola.⁵⁰ Evidence is vested with the individual as opposed to the organisation. While my original plan was to conduct archival work in Luanda to obtain primary documents I learnt that official collections might be of less use as one's best hope of obtaining a certain document is often through personal acquaintance. To make things more complicated, archives were often closed or when open, less useful. The deficiency of

⁴⁹ My informants often described the 1990s to me as a “black hole” when it came to official data records. Interview, civil servant Ministry of Finance, Luanda 26.10.2015; Interview, civil society leader, Luanda 2.10.2015.

⁵⁰ Interview, state secretary, Luanda 23.10.2015.

written sources made data collection through elite interviews critical to the research project. I make use of interview data throughout the thesis to substantiate and further elucidate findings from a variety of sources. By using elite interviews, I was able to access information that was not available elsewhere (Richards, 1996). Qualitative interviews form a critical part of academic study in a place like Angola where the “lack of authoritative data and credible statistics” makes research particularly challenging (Soares de Oliveira, 2015, p.21).

I adopted a semi-structured approach to interviewing as it is commonly believed to be an interview method that allows interviewees to express themselves in a more unrestrained manner (Tansey, 2007). By adopting a more flexible approach, I increased my chances of capturing people’s beliefs and attitudes (Hammer and Wildavsky, 1989; Art, 2016). I did not choose my informants through random sampling but rather, I identified and selected people for interviews based on their position and assumed ability to offer me insights into particular episodes or situations. As emphasized by Mosely (2013), non-random sampling is appropriate when one seeks to understand specific cases for the purpose of theory development rather than generating representative samples to test theory. Additionally, using random sampling in an authoritarian context like Angola, where informants may be sensitive to scrutiny by foreign researchers, can be particularly challenging,⁵¹ although recent studies have made important strides in this area.⁵²

⁵¹ Both Soares de Oliveira (2015) and Schubert (2010) testify to the difficulties of conducting research in Angola as researchers are not only met by mistrust by authorities but can also have a hard time gathering interview data because people are reluctant to voice their opinion freely. Similar challenges have been documented by researchers studying other authoritarian countries, including Goode (2016) writing about Post-Soviet Eurasia.

⁵² I am here referring to the household survey conducted by Allan Cain, Sylvia Croese and Anne Pitcher in 2014, in which the authors randomly identified 300 households within purposefully sampled neighbourhoods in Luanda. See Croese and Pitcher (2017).

To access informants, I relied heavily on my personal network built over several months. Yet even when I came recommended I was not always granted an interview. Generally, however, my ‘snowballing’ technique generated positive results.⁵³ Interviewees were often interviewed on two or more occasions, allowing me to resolve any doubts that might have arisen in the course of the first interview or to address any new and unexpected information that needed additional sources for verification and elaboration (Davis, 2001).

In the course of the fieldwork I conducted 78 in-depth interviews. Interviews in Luanda during the fall of 2015 and 2016 were supplemented by interviews conducted in London, Washington DC, and via Skype.⁵⁴ Interviewees included representatives from the Angolan Government, key ministries including the Ministry of Finance, Ministry of Foreign Affairs and Ministry of Justice, in addition to regulatory bodies such as the BNA and the Capital Market Commission. I also met with politicians from the opposition parties. From the financial industry, I interviewed representatives of eight different banks, public, private and foreign as well as management consultants. From the oil industry, I interviewed national oil company Sonangol officials as well as representatives from the international oil companies, international and local service companies. Academics, journalists and civil society representatives were also consulted. The foreign presence in Luanda is not confined to the business sector and interviews were also conducted with representatives of the international financial institutions, diplomatic missions and international organisations.

I have chosen to conceal the identity of my informants but make reference to their affiliation and rank whenever possible. I anonymize in order to protect the interests and safety of the

⁵³ A snowballing technique refers to a method, often applied in interview-based research, “when one relies on each respondent to suggest other possible respondents – creating a snowball effect (the ball of respondents gets larger as each new snowflake joins the ball)” (Gerring and Christenson, 2017, p.57).

⁵⁴ See Appendix 2 for list of interviews by affiliation, location and date.

people that participated in the research. Unfortunately, in Angola, like in other authoritarian countries, asking politically sensitive questions or revealing politically sensitive opinions can put both the interviewees and interviewer in danger. For scholars studying authoritarian regimes, it is necessary to balance the need for knowledge with the security of informants (Araham and Goode, 2016). Sometimes just being seen to associate oneself with a foreign researcher can put respondents in danger, and as researchers we should seek to limit the exposure if needed (Reny, 2016). Notwithstanding, I do not believe that anonymization of sources reduces the strength of the data. Moreover, the findings from interviews were always triangulated using other forms of evidence so as to check and establish validity.

8. Outline of the thesis

To help fill the gaps in our knowledge of what drives financial sector change in resource-rich authoritarian countries, the thesis contributes by providing an in-depth study of the Angolan financial sector and the changes that have taken place therein since 1975, with a particular weight on the period from 1975. The thesis represents a first attempt to elucidate the role of politics in financial sector change in resource-rich countries.

Following the introduction, chapter 2 will critically review existing literature and outline the theoretical framework of the thesis in more detail. Then in chapter 3, I will outline the political economy of post-independence Angola, from the country's independence until late 1980s when liberalisation of the economy began in fits and starts. These two chapters are considered essential because they place the evolution of Angola's financial sector in the broader theoretical but also historical and political context. Whilst the empirical chapters will focus on the more immediate political economy factors relevant to explaining financial

sector change, chapter 2 and 3 allows us to delve deeper into the fundamental assumptions underlying this thesis.

In the four subsequent chapters I tease out the causal processes underpinning the financial sector changes in Angola, as described earlier in the chapter. Whilst recent scholarly attention to Angola's financial sector has tended to focus on the country's post-war reconstruction period, this thesis starts a decade earlier, incorporating the transition from a centrally planned to a market based economy in the 1980s-1990s. I include the early post-independence period because it was during this time that the foundation for what is Angola's modern financial sector was laid. Furthermore, many of the arrangements prevalent during these early years, including state-owned banking, arbitrage and subsidized credit, endured in later periods.

Chapter 4 focus on developments in the 1990s and offers a clear example of how the unviability of the economic model forced Angola's political leaders to give in to external pressure to change the country's financial sector in a more market friendly direction. Full liberalization did not take place at this stage, however. I argue that lack of liberalization has to do with the financial sector becoming an important tool for ensuring the redistribution of resources to politically important constituencies when the state could no longer do so directly. The chapter offers a first example of how advancing the financial sector may be useful also to an authoritarian regime mainly as it seeks to please a certain constituency.

Following partial-liberalization in the early 1990s further financial sector changes were not initiated before the late 1990s. The reasons behind these liberalization measures – which

were seen as fundamental to the financial sector's development in the subsequent decade — are the focus of chapter 5 which offers an alternative explanation to the existing literature which emphasizes the recurrence of war and the persistent economic crisis of the 1990s to explain why political leaders initiated additional financial sector changes. Whilst these factors were important, they are not sufficient. Rather, I suggest that the late 1990s reforms reflected the changed mind-set of the political leadership and elites who at the time were becoming increasingly confident and thus started to question the viability of the prevailing economic model. The introduction of a number of important economic reforms during the late 1990s, including the new Financial Institutions Law in 1999, laid the foundations for more sophisticated forms of accumulation that would soon overtake the arrangements characteristic of the “partial-reform equilibrium” of the early 1990s (Hellman, 1998, p.204).⁵⁵ Chapter 5 thus contributes to the theory of this thesis by demonstrating how financial sector change not only arises as a response to external pressure but also from an internal willingness to update the status quo, thus strengthening the position of political leaders in power.

Chapter 6 covers a particularly interesting period in Angola's post-independence, the end of the civil war and the extraordinary post-war reconstruction period that followed. In this chapter, I show how the advancement of the financial sector in the post-war period was compatible with the ruling coalition's strategy of ensuring political support. Specifically, in the light of the institutional changes described in the last chapter, holders of power needed to be accommodated within the new post-war economic order. The need to maintain but also expand the party's political base led the country's financial sector down a particular

⁵⁵ Hellman (1998) uses the term partial reform equilibrium to describe the reform experience of post-communist and post-Soviet states, where winners from initial economic reforms used their new found power to prevent further reform initiatives.

development path, heavily skewed towards short-term banking and away from more long-term and inclusive financial instruments. In line with the overall objective of the thesis, chapter 6 demonstrates how a particular form of financial sector advancement was useful for the regime. Their political objective furthermore leads political leaders to favour certain institutions and disfavour others, producing the kind of financial sector outcomes that one has learned to expect from resource-rich authoritarian regimes.

The final empirical chapter, chapter 7, will focus on the other advancements in Angola's financial sector, namely the post-2009 regulatory reform. As in chapter 5, I argue that the increasingly difficult economic situation and the external pressure for reform were important in explaining why change happened, but it is not the only reason why political leaders decided to go ahead with them. Similarly, to the situation in the late 1990s, in the late 2000s President dos Santos and his associates understood that change had to be introduced for the financial sector to be able to continue performing its important role in the economy. What was different in the late 2000s was that using the financial sector for political purposes was becoming increasingly difficult for the ruling elite. External actors were becoming less willing to overlook major weaknesses in the sector. Chapter 7 hence points to an interesting yet overlooked issue when it comes to financial sector development in resource-rich countries, which is that due to the inherent interconnectedness of the financial sector, resource-rich countries do not stand free to do as they please. If they want to remain part of the club of international finance, Angola like everyone else, has to play by international rules.

In the final chapter, the findings from the thesis will be synthesized so as to provide an overview of the main theoretical and empirical implications of this study for the literature

and for other cases which share Angola's characteristics. Crucially, by employing a case study design, this thesis contributes towards filling a gap in the political economy of finance literature, which typically has relied on large-N designs with a fixation on outcomes to the detriment of understanding the processes that underlie financial sector change. Far-reaching financial sector change over the last decade is not a feature unique to the case chosen for this thesis, and thus the findings of the study will help to shed light on similar processes beyond Angola.

Chapter 2

Theorizing financial sector change

1. Introduction

If finance is important for economic development, why do some countries promote development enhancing financial institutions while others fail to do so? Particularly, why do countries abundant in resources have less developed financial sectors relative to their resource-poor peers? Acknowledging the positive properties of financial development, a growing body of literature is probing the determinants of financial sector change. The aim of this chapter is to elaborate the theoretical grounding that will help frame the forthcoming empirical analysis of Angola, which seeks to shed light on the question of what drives political leaders of resource-rich and authoritarian countries to institute financial sector change. Two bodies of literature receive particular attention here: that dealing with financial sector development generally and that concerned with resource-rich countries in particular.

The chapter will first discuss the general literature that deals with financial sector change and development. The literature emphasizes the historical determinants of financial sector change including the legal traditions and other colonial legacies of a country. There is also a smaller and more specialized literature speaking directly to the case of resource-rich countries, highlighting the structural drivers of financial sector outcomes including the

negative effects of large foreign currency inflows or macroeconomic volatility.¹ Whilst offering important insights, the latter studies downplay the effect of politics, which is why I introduce another body of literature that approaches the question of interest from a political economy perspective. At the heart of the political economy of finance literature is the idea that financial development is an outcome of particular institutions and that these institutions in turn reflect a country's particular political context. This thesis builds on the political economy literature understanding of financial sector change but it also extends it in two important regards.

First, I show that the nature of politics is different in resource-rich countries and therefore one must reconsider the underlying assumptions of existing political economy studies that places the demands of the private sector at the centre of the financial development story. Resource-rich states have access to ample external rents so that political leaders of these countries are less dependent on the private sector for generating revenues. Consequently, the state rather than the (usually state-dependent) private sector tends to be the driving force in financial sector development in the resource-rich context, as discussed in the introductory chapter.

Another prevailing assumption that this study seeks to part with is that in the absence of well-developed formal political institutions, political leaders of resource-rich countries rule unrestrained and often to the detriment of financial sector development. As a number of recent studies presented in this chapter demonstrate, this is not necessarily the case. Rather,

¹ These studies tend to take little or no account of conditionality, meaning that resource-abundance has an unconditioned effect on the dependent variable, in this case financial sector development (Herb, 2017). This is the case for the influential paper by Beck (2010).

I contend that political leaders, regardless of regime type and resource endowments, still answer to some groups that helps them preserve their position in power.

To address the gaps in existing literature and to better account for the particular experience of resource-rich countries, I propose a new explanation. To do so I build upon the political settlement framework as developed by Khan (1995; 2010; 2017). The work of Khan is instructive in explaining the importance of a country's balance of power in shaping institutions and policy. Still, particular changes in policies or institutions do not mechanically reflect the distribution of power in a society (Khan, 2017). It also necessary to also take into account the agency of governments and other organizations in shaping policy. In resource-rich countries like Angola, international factors play a crucial role in structuring the state's policy space.

My argument is that it was the poor economic performance of prevailing institutional structures that initially triggered Angolan political leaders to institute institutional change, bringing about financial sector advancement in the country in the early 1990s. Changing external circumstances meant that existing forms of accumulation, on which the distribution of power rested, had become financially unviable. Yet, financial sector change does not only happen in times of weakness. Financial sector change progressed also when pressure on the MPLA from excluded factions declined. Financial sector change in both the late 1990s and the late 2000s was less due to external pressure for reform. Rather, political leaders understood that with a more advanced financial sector their ability to survive in power was enhanced.

Contrary to what existing literature expects, the Angolan case shows that having a modern financial sector is useful also for resource-rich countries even when the state does not rely on this sector to provide it with the revenues necessary for survival. Put together, the empirical evidence demonstrates how the Angolan financial sector has become important to the MPLA regime's hold on power by supporting new forms of accumulation as well as becoming a centre for accumulation itself. The argument will be elaborated upon at the end of this chapter before forming the basis of the subsequent empirical analysis. Let us start by examining what established theories have to say on the topic.

2. Determinants of financial sector development

The following section will review the literature concerned with understanding the determinants of financial sector development generally and on resource-rich countries in particular. An influential body of scholarship in the finance and growth literature focuses on the historical and institutional factors of financial sector outcomes, arguing that how a financial sector develops is largely a result of the origin of a country's institutions, many which were shaped during colonial times (Acemoglu et al., 2001; 2002). The studies that will be reviewed in the following section identify strong correlations between certain institutional legacies and present-day development of financial sectors.

According to the first body of literature, differences in legal origin help explain the cross-country differences in financial development observed today. A country's legal origin is argued to influence economic growth through its role in shaping national financial systems (Levin 1998;1999). The basic premise of the 'law and finance literature' is that the finance sector consists of a set of contracts. These contracts are defined and made more or less effective by legal rights and enforcement mechanisms. From this perspective, a well-

functioning legal system facilitates the operation of both financial markets and intermediaries (Levin, 2005). The law and finance scholarship originated in a series of influential papers co-authored by La Porta, Lopez-de-Silanes, Shleifer, and Vishny (1997; 1998; 1999; 2000). The authors argued that much of contemporary variation in financial institutions can be traced back to the prevailing influences of countries' different legal traditions. Specifically, the authors argued that the degree to which a country's legal tradition offers protection for investors was as a condition for more external finance, i.e. financial sector development. La Porta et al. (1997; 1998) show how countries that were colonized by Great Britain and whose laws are based on British Common Law provide better protection to minority shareholders and therefore have larger financial systems. This is contrasted with the experience of former French colonies whose laws are based on the French Civil Code. In contrast to Common Law, it is argued that Civil code countries offer only weak legal protection for investors as well as weaker property rights (La Porta et al., 1998, p. 1126).² Other authors attribute the superiority of common law to more fundamental and even philosophical differences between common law countries and others. Mahoney (2001) argued that the divergence between countries with different legal traditions comes down to the greater orientation toward private economic activity in common law countries and the civil law's greater orientation toward government intervention. This latter view is echoed by La Porta et al. (2008).

Extending on the early law and finance literature, Demirgüç-Kunt and Levine (2001) and Beck et al. (2002a; 2000b; 2005) argue that the adaptability of a country's legal system is the crucial factor for explaining financial sector development. According to the authors,

² British Common Law and the French Civil Law were the two most influential legal traditions. The French Civil code tradition was transplanted to other colonies, including the Portuguese colonies (LaPorta et al., 1998).

legal traditions differ in terms of their responsiveness to changing socioeconomic conditions. As the economy's need for financing is continuously changing, more flexible legal systems, defined as "Legal systems that adapt quickly to minimize the gap between the contracting needs of the economy and the legal system's capabilities" (Beck et al., 2002, p.2), are argued to foster financial development more effectively than do more rigid systems (Demirgüç-Kunt and Levine, 2001). British legal origin countries have the most adaptable legal systems in this regard whilst French legal origin countries have the least adaptable legal systems, making the authors conclude that Civil Code countries are less able to meet the continuously changing financial needs of the economy (Beck et al., 2002). According to the most influential works in the financial and law scholarship, politics and political institutions do not matter (La Porta et al., 1998; 1997) or they matter less than legal traditions (Beck et al., 2002).

Moving beyond countries' legal foundations, other historical legacies have also been proposed to explain the differences in financial outcomes observed across countries, including strategies pursued by the colonial powers. The endowment view,³ as advanced in the work of Engerman and Sokoloff (1997), Sokoloff and Engerman (2000), Easterly and Levine (2003) and Acemoglu et al. (2001), claims that countries' environment and endowment of resources are key to explaining economic outcomes through the impact that the former have on institutions.⁴ Specifically, as argued by Sokoloff and Engerman (2000), the strategies that colonizers pursued were reliant on the conditions in the colonized lands, the factor endowments. The different strategies that colonizers adopted based on the factor endowments that they encountered in the different colonies in turn impacted on the

³ The label used by Beck et al. (2002).

⁴ As opposed to those who argue that the environment shapes economic development directly by influencing the inputs into the production function and the production function itself. See for instance Sachs and Warner (1995; 1997) and Diamond (1997).

institutions that evolved (Sokoloff and Engerman, 2000). The environment of the colonies also impacted on the ability of the colonial powers to settle there (Acemoglu et al., 2001). Where Europeans were not able to settle due to factors such as the disease environment, colonial powers focused on extracting resources, whilst little attention was paid to foster institutions that supported private property rights. In other places, where Europeans found hospitable conditions, colonial powers established settler institutions that supported private property and checked the power of the State (Acemoglu et al., 2001). Overall, the body of scholarship here referred to as the endowment view emphasises how initial endowments of land, climate, and the disease environment profoundly influenced colonization strategies and the types of institutions that colonialists established in the colonies. These institutional structures endured even with the end of colonialism (Sokoloff and Engerman, 2000; Acemoglu et al., 2001). “Settler colonies tended to produce post-colonial governments that were more democratic and more devoted to defending private property rights than extractive colonies” (Beck et al., 2002, p.140).

Building on the work of Acemoglu et al. (2001), Beck et al. (2002b) apply the endowment theory to the study of financial development. The authors find that countries with poor geographical endowments, which made them less likely to become settler colonies, generally have less developed financial intermediaries, less developed stock markets, and weaker property rights protection (Beck et al., 2002b). The authors suggest that lower financial development in the colonies characterised by inhospitable conditions, is due to the fact that colonizers were here more concerned with “maintaining power and control, rather than on creating an open and competitive financial system” (Beck et al., 2002b, p.151). In settler colonies, on the other hand, colonizers were much more likely to construct institutions that protect private property rights, in turn fostering financial development.

Referring to these established theories on historical determinants of financial development to shine light on the Angolan case we are left with two conflicting sets of expectations. On the one hand, the legal origins view leads us to expect lower financial development in Angola based on the fact that the country's legal system is most closely related to the French Civil code. As explained by La Porta et al. (1998) the French Civil code tradition was transplanted to other colonies, including the Portuguese colonies. Angola's current legal system is based upon the Portuguese civil law and its Civil Code resembles the original version implemented by the Portuguese pre-independence.⁵ A period of Marxism-Leninism in Angola did not dramatically alter the legal tradition and like other transitional countries, the Angolan government reverted to their pre-socialist systems following the abandonment of socialism (La Porta et al., 2008). Consequently, we would expect protection of investors to be weaker and property rights equally so, exerting a negative influence on the development of the financial sector.

On the other hand, the endowment view leaves us with a different expectation. By the end of colonial rule, in 1974-1975, Portuguese settlers represented more than 5% of the total population in Angola and they were the second largest settler community in Africa, only exceeded by South Africa (Morier-Genoud, 2012). Angola fits Acemoglu et al. (2001, p.1374) description of a settler colony as a place where "Europeans settled in large numbers, and life was modelled after the home country". The country's popularity amongst white settlers would have one believe that institutions to promote long-run prosperity would

⁵ Angolan law firm Vítor Carvalho & Associados estimate that 40-50 per cent of the law is based on the Portuguese legal code, pre-independence (Vítor Carvalho & Associados. 2010).

be favoured amongst the colonizers establishing themselves in the country, resulting in financial development.

Whilst insightful, neither the explanations focusing on legal traditions or geographical endowments offer satisfactory explanations. Property rights protection and contract enforcement is indeed weak in Angola, reflecting a feeble and fragmented legal system that impacts negatively on the country's financial development (African Development Bank, 2012). This is in line with the expectations of the legal origins view of countries that share Angola's legal traditions. Yet it is unclear whether this is the result of Angola's legal system being more closely related to the Civil Code rather than Common Law or the fact that laws are not always enforced and the justice system is, as one business publication described it, "slow, arduous and not always impartial" (USA International Business Publications, 2015). Additionally, as emphasised by Volpin and Pagano (2001) legal systems are not exogenous variables but are subject to alteration in line with the political process. The primacy of politics, also when it comes to country's legal systems, helps explain why one sees advances and reverses in legal systems over time, as has been the case in Angola. Whilst the country generally performs poorly on the World Bank's Ease of Doing Business ranking, the country has made considerable progress in recent years when it comes to protecting investors, scoring above the sub-Saharan African average (World Bank, 2016).

The endowment view does a poorer job of predicting Angola's financial sector outcomes. Early institutions have certainly influenced institutional trajectories in Angola but not in the way Acemoglu et al. (2001) would expect. According to Acemoglu et al. (2002, p.1370), in settler colonies "settlers tried to replicate European institutions, with strong emphasis on private property and checks against government power." Yet, in Angola,

defence of private property for the white settler population did not translate into similar conditions for the majority African population. Most Africans, living under customary law (as opposed to Portuguese civil law) until 1974, did not enjoy the equal protections of their property (Clarence-Smith, 1985; Cain, 2013). The settler colony was not able to place checks on the power of the metropole. Portugal was first a military regime and then a civilian dictatorship from 1926 to 1974. The settlers had no political power nor administrative control of the state apparatus.⁶ What developed in Angola was thus less akin to what Acemoglu et al. (2001) would expect in a settler colony. Rather, what developed in Angola was a highly unequal society, where the rights of settlers were largely protected whilst those of the African population were often ignored (Clarence-Smith, 1985).⁷ This divide was also visible in the financial sector. In pre-1975 Angola, there was a reluctance to expand the financial system beyond serving the white minority population (Bender, 1978). As emphasized by Wickins (1986, p.63) banking “services were directed primarily at expatriate interests and the investment of surplus funds in Europe.” Branches tended to be opened only in towns where expatriate enterprises had already established themselves. The native population had little to do with them either as savers, because the banks were uninterested in small deposits, or as borrowers, because they were not thought to be very credit worthy.” Whilst the endowment view offers important insights on Angola’s trajectory and the determinants of financial sector development, like other established theories it is unable to satisfactorily explain Angola’s trajectory, in part because it does not take into account the settler colonies across Africa.⁸

⁶ This was different in Rhodesia, where the Rhodesian whites enjoyed more power due to administrative decentralization (Clarence-Smith, 1985).

⁷ Whilst a 1961 law reform meant that all inhabitants in Angola enjoyed equal status and could be subject to Portuguese civil law if they wanted to (by becoming full Portuguese citizens) far from everyone made this transition (Clarence-Smith, 1985).

⁸ For a discussion on the different European settler colonies, see Marx (2017).

An explanatory variable that has so far received less attention in the finance and growth literature is that of natural resource abundance. As noted by Beck (2010, p.1) “many papers in the finance and growth literature omit oil countries or natural-resource- based economies in general, arguing that economic development is driven by different factors in these countries and that the financial sector has a different role and structure in these economies”.

The few studies that explore the association between financial sector development and resource development point to a particular effect of resources on finance (Beck, 2010; Barajas et al., 2013; Beck et al., 2008). Intuitively, windfall gains from resources – and the resulting expansion in non-traded goods – should lead to a rise in demand for financial services as revenues rise. Yet this is not always the case, due in part to what has become known as the Dutch Disease effect (Gylfason, 2004). The “Dutch disease” refers to the structural changes that occur in an economy when a boom in the export of resources reduces the competitiveness of non-resource exports (Corden and Neary, 1982, p.825). This happens through a “spending effect” and a “resource movement effect” (Corden and Neary, 1982, p.827). Whereas the former effect relates to the increased use of revenues leading to higher prices, the latter centres on the relocation of capital and labour into the oil sector, causing the alternative tradeable sector to shrink. It is the resource movement effect that Gylfason (2004) argues is likely to have a negative effect on financial sector development, as the crowding out of the non-oil tradeable sector by natural resource exports leads to a decrease in a demand for financial services.

An emergent extractive sector is moreover less likely to make up for falling domestic demand since foreign extractive companies are unlikely to seek financing domestically given that their financial needs often outstrips the capacity of local banking sectors

(Kurronen, 2012; Lin et al., 2009). Findings such as these have led researchers to predict lower demand for banking services in resource-based economies with the consequence that financial sectors in these countries remain less developed (Kurronen, 2012). In his study of a broad cross-section of countries over the period 1960 to 2008, Beck (2010) questions the finding that demand for financial services is apparently lower in resource-rich countries. The author shows how the lesser use of financial services in resource-rich countries is not the outcome of lower demand. Rather, the need for credit is no less for firms in resource abundant countries, leading him to argue that the issue must rather be one of supply (Beck, 2010). Beck (2010) suggests that higher investment in the natural resource sector can lead to lower investment in the financial sector and draw away skills from the financial system, in line with the Dutch Disease resource movement effect as discussed earlier. In addition, the heavy dependence of the financial system on a sound institutional framework, including an effective contractual framework, can hamper financial deepening in countries where resource abundance undermines institutional development (Beck, 2010).⁹

What are the implications of the abovementioned studies for the Angolan case? On the one hand, we would expect lower demand for financial services as Angola's non-oil tradeable sector has historically been crowded out by oil exports. On the other hand, low financial development in the country would be expected due to low supply of financial services stemming from Angola's weak institutions, including poor contract enforcement. Both accounts apply to the Angolan case although timing seems to matter. Before 2002, lack of demand arising from low economic activity can help explain the low demand for external finance in Angola's non-oil sector (IMF, 2007).¹⁰ As emphasized by Ferreira (2006), new

⁹ A number of studies find a negative impact of resource abundance on institutional development. See for instance Leite and Weidmann (1999); Isham et al. (2003); Sala-i-Martin and Subramanian (2003).

¹⁰ Interview, representative Angolan private bank, Luanda 20.11.2015.

economic activity at that time was hampered by the workings of the Dutch Disease and thus the demand for financing likely suffered. Yet by the 2000s an increased demand for credit was evident. Growth in the construction and transport sector accelerated the demand for external financing (IMF, 2007), as did the growth in small and medium sized enterprises (USAID, 2008). Supply of credit did rise (BNA, 2007), but only to a limited extent. The latter points in the direction of supply side constraints, which fits with the reports that have covered Angola's financial sector over recent years. For instance, the 2014-2015 Global Competitiveness Report showed "access to financing" to be the most problematic factor for doing business in Angola (IMF, 2015). The most frequently cited reason why banks do not extend credit is due to lack of financial infrastructure. As the IMF 2012 Financial System Stability Assessment noted, in Angola "credit extension is limited by institutional deficiencies, including inadequate property and collateral registries, and a weak judiciary."

Macroeconomic volatility generated by highly cyclical commodity prices is another central factor that authors argue impact performance outcomes in resource-rich countries (Van der Ploeg and Poelhekke, 2009). The financial sector is shown to be particularly sensitive to macroeconomic volatility (Boyd et al., 2001). As Kurronen (2012) argues, volatility in GDP growth, terms-of-trade and in the real exchange rate is prevalent in economies dependent on resources and is likely to produce suboptimal conditions for financial sector development. The causality is not clear, however, as authors also argue that having a developed financial sector helps dampen the negative consequences of volatility, through alleviating the liquidity constraints on firms and facilitating long-term investment (Aghion et al., 2010). As explained by Van der Ploeg and Poelhekke (2009, p.735), "with complete financial markets, long-term investment is counter-cyclical and mitigates volatility." The latter does not hold if firms face tight credit constraints, however, as investment becomes

pro-cyclical and amplifies volatility (Van der Ploeg and Poelhekke, 2009). Consequently, financial sectors serve both as an amplifier and reducer of volatility, although in resource-rich countries like Angola, where credit provision is recurrently limited, the former would be expected. Indeed, as the last decade has shown, investments in Angola have been largely pro-cyclical whilst long-term investments have been limited (IMF, 2015). Rather than a check on volatility, the financial sector has acted as an amplifier.

There is moreover no consensus as to how volatility impacts on financial sector development. Boyd et al. (2001) suggest that the macroeconomic uncertainty associated with volatility discourages banks from lending and allocating resources effectively. Another possibility, as explained by Berglof and Lehmann (2009), is that resource-dependent economies tend to suffer from large and sporadic investments and thus lack more sustainable demand for financial services. Both explanations speak to the Angolan case. As in the studies discussed earlier, Boyd et al. (2001) and Berglof and Lehmann (2009) also suggest that lower financial sector development results from a lack of demand and supply, although these authors suggest that the conditions emerge as a result of volatility.

As in the case of the previously reviewed literature, the explanations focusing on the effect of volatility on financial sector outcomes shed light on the Angolan case. Yet, the above-mentioned theories share a deterministic view of the impact of resource abundance on countries, which scholars studying resource-rich countries in recent times have come to question (Herb, 2017). One important reason that scholars have come to debate these types of studies is the observation that similar countries with comparable resource endowments manage their endowments very differently. As was emphasised in the introductory chapter,

outcomes are therefore found to differ between otherwise similar countries when it comes to financial sector development.

The theories presented so far in this section emphasize exogenous rather than internal determinants of financial sector development, be they legal origin, resource endowments or macroeconomic volatility. The studies devote little attention to understanding the “underlying political and institutional processes that set off economic laws and market forces in the first place” (Karl, 1997, p.6),¹¹ despite the commonplace observation in social sciences that institutions and politics matter. This is problematic, for as Pagano and Volpin (2001) note, legal systems and institutions are not exogenous variables but are recurrently altered via the political process. Rather, as I will argue in the next section, political differences are why we observe changes in financial systems taking place over time, even in countries that appear initially doomed by their structural features, such as Angola. Bringing the underlying political processes to the fore when studying financial sector outcomes therefore appears highly relevant.

3. The case for a political economy approach

In the following section I will introduce the political economy literature to the study of financial sector change. This thesis shares the broader political economy scholarship’s concern not just for the outcome itself — financial sector development — but also for the politics and political institutions that produced the specific laws and regulations which shaped financial sector outcomes in the first place (Haber et al., 2008).

¹¹ As Mahoney and Thelen (2009) emphasise, in the literature on institutional change, most scholars point to exogenous shocks that bring about radical institutional reconfigurations, overlooking shifts based on endogenous developments that often unfold incrementally.

A growing body of political economy literature emphasizes what previous studies on the drivers of financial sector outcomes have so far discounted, namely politics.¹² The political economy literature stresses the need to understand the distribution of power and the institutional framework that emerges from this power constellation if we are to account for different financial sector outcomes. When a group gains power it is often assumed that this group will shape policies and institutions to its advantage (North 1990; Olson 1993). This also holds true in the financial sector. Consequently, “a country does not *choose* its banking system: rather it gets a banking system that is consistent with the institutions that governs its distribution of political power” (Calomiris and Haber 2014, p.4).

Pagano and Volpin (2001) show how the pressure of interest groups and the career concerns of politicians combine to produce specific political interventions in financial markets, in turn shaping and entrenching political constituencies via its economic effects. Relatedly, Rajan and Zingales (2003) emphasize the influence of powerful constituencies, in their case industry incumbents, to explain why domestic political leaders would be opposed to something as beneficial as financial sector development. The authors show that incumbents will have an interest in undermining financial sector development when the latter fosters competition and arms-length lending, from which incumbents benefit less (Rajan and Zingales, 1998).

The analyses of Barth et al. (2008) and Calomiris and Haber (2014) go one step further and ask under what circumstances self-interested actors, including political leaders, are able to further their own interest when it comes to the financial sector. In their study of bank

¹² Prominent works include Haber et al. (2008); Calomiris and Haber (2014); Pagano and Volpin (2001); Rajan and Zingales (2003); Barth et al. (2008).

regulation globally, Barth et al. (2008) argue that political leaders and bank regulators will abuse their powers in order to steer regulation and supervision to their own private benefit if not held accountable through formal representative institutions. Similarly, Calomiris and Haber (2014) show how political institutions are crucial in accounting for differences in banking sector vulnerability and scarcity of bank credit across countries. In these studies, political leaders are assumed to act in line with their own self-interest with the aim of maximizing private over public welfare, what is frequently referred to as the 'private interest view' (Beck, 2016). This means that political leaders will use their influence over policy to "enrich and protect special interests in society" over serving broader societal interest (Barth et al. 2008, p.258). Their ability to do so depends on the strength of "open, competitive, democratic political institutions" (Barth et al. 2008, p.314; Calomiris and Haber, 2014). Political institutions thus play a crucial role in these models, as they represent the principal check on the self-maximizing behaviour of policy makers. Political leaders of authoritarian countries enjoy freedom of action, seeing that they do not need to be concerned with popular support for their policies. Leaders of democracies, on the contrary, stand the risk of being removed at the next election if they fail to play by the rules (Calomiris and Haber, 2014). As a consequence, political institutions define "what is feasible within each country's banking system" (Calomiris and Haber, 2014, p.477).

Financial sector outcomes according to these authors are the result of arrangements between political and economic elites. Financial sector outcomes are in turn either inclusive or exclusive depending on the strength of political institutions. In the model that the abovementioned authors propose, political leaders are expected to rely on banks and markets to provide them with finance and bankers in turn rely on governments to establish and sustain the institutions that make the functioning of a financial system possible. The

latter happens at the cost of limiting the government's own authority and discretion. The interdependence between state and financiers is thus central to how laws and regulation governing the financial system are defined (Calomiris and Haber 2014; Barth et al. 2008).

The above-mentioned studies understand outcomes to follow from political deals, a sort of negotiated equilibrium, between holders of power and the holders of wealth. They assume this to be a deal struck between political leaders in need of financing and economic actors in need of government guarantees (Calomiris and Haber 2014, p. 38-41). This is not too different from the broader state-building literature, which holds that state building has historically taken place and been maintained through a series of exchanges of resources for institutions (Tilly 1975). Over time these institutions were supplemented by economic institutions like private property rights and markets, which stimulate economic growth (see Rodrik, 2000; 2005). As Haber et al. (2003) elaborate in the case of Mexico, "These governments understood that they needed a source of credit in order to restore political order" (p.80). "Armies had to be paid, a bureaucracy had to be created, and regional transport barriers had to be overcome" (p.84). The only option of Porfirio Díaz, president of Mexico for 30 years, was to "use domestic sources of credit to finance the establishment of political order and then gamble that political order would produce economic progress that could be taxed" (p.84).

With the above model in mind, the case of financial sector development in resource-rich countries presents us with a particular conundrum. In resource-rich countries, the division of roles between the state and bankers – decision makers and financiers – does not follow the logic of aforementioned studies. Prevailing studies assume that the government acts as an enforcer of financial contracts whilst the banks and markets act as a source of finance.

In the case of resource-rich countries, however, sizeable revenues accrue to the state from external sources rendering the state less dependent on the domestic economy to satisfy their financial needs (Karl, 1997). The dominance of external financing is one of the central features of resource-rich countries as defined in this thesis (Beblawi, 1987). The situation is not confined to resource-rich countries, however. Over much of post-independence Africa, nationalist movements inherited state machineries endowing their rulers with tremendous economic power vis-à-vis society (Arriola, 2013). Rather than domestic financing, ruling elites relied on “import and export taxes, royalties and corporate taxes from extractive natural resources (such as minerals and oil), from state marketing of agricultural primary commodity exports, or from official foreign aid channelled through the government” (Gray and Withfield, 2014, p.20). Fostering an autonomous productive private sector was thus less important; in fact, political leaders frequently viewed the development of one as a threat to their own hold on power (Boone, 1992). As a result, “African governments, regardless of avowed ideology, became the principal financiers of their economies after independence” (Arriola, 2013, p.103).

There are exceptions in this regard: in resource-rich Nigeria (Saylor, 2014) and beyond Africa, oil-abundant Kuwait (Herb, 2014), merchant classes with capital bases outside the purview of the state exist and have existed since before oil was discovered. Nonetheless, the point is still generally valid for the group of countries of concern here. Political leaders of resource-rich states are generally less dependent on domestic actors for financing. This gives the latter group less leverage to demand the enforcement of financial institutions than would be the case if domestic sources were crucial to the state.

Following the above-mentioned logic, one would expect that in resource-rich countries like Angola, where banks and markets are in an inferior position in comparison to the state, political leaders would have few incentives to enforce institutions on which financial sector development relies. This is indeed what the small literature dealing with the political economy of financial development in resource-rich countries suggests. Bhattacharyya and Hodler (2014) argue that the inclination of resource-rich governments is to survive on unproductive rent seeking when sizable resource revenues are available. If resource-rich governments are not held accountable through political institutions – modelled as the competitiveness and regulation of political participation, the openness and competitiveness of recruitment, and constraints on the executive – they will not have any incentive to establish and promote financial institutions. The authors find that resource rents are negatively associated with financial development in countries with weak political institutions, but this negative effect decreases in absolute value and eventually vanishes as the quality of political institutions improves (Bhattacharyya and Hodler, 2014).

The empirical findings of this thesis suggest that even if political leaders do not rely on the financial sector as a source of finance, this does not mean that they will disregard the financial sector. The significant change of Angola's financial sector, as described in the introductory chapter and elaborated upon in the subsequent chapters, supports this claim. Political leaders in the country have intermittently prioritized investing in financial institutions, even if according to the existing studies, they did not have to do so. Barth et al. (2008, p.285) acknowledges such a possibility, recognizing that although unaccountable political leaders might choose to act in a damaging fashion towards the financial sector, they might also choose to act in a manner more conducive to growth. Yet the authors do not incorporate the latter possibility into their model.

Existing political economy models, whilst central to bringing in the political dimension to the current financial development debate, leave unanswered the question of what induces political leaders of resource-rich countries to act in a manner more conducive to growth in the absence of quality political institutions. Financial sector development in resource-rich countries is assumed only to come about in the presence of already strong political institutions or as a result of countries democratizing. Existing studies argue that the positive relationship between strong political institutions and financial sector performance is due to the point that strong political institutions force leaders to prioritize investing in financial institutions, thus laying the foundation for financial development. The theory rests on the assumption that if political leaders are not held accountable through formal political institutions they are not held accountable at all. As the subsequent section will show, it is rarely true that political leaders act unconstrained. Formal political institutions are likely not the sole factor impacting the way political leaders act towards the financial sector.

4. Challenging established assumptions

In order to better account for the experience of resource-rich countries like Angola, we need to move away from the assumption, largely held in the current political economy literature,¹³ that an interdependence between political leaders and domestic financiers, drives financial sector change. This because resource-rich states support themselves chiefly through external rents (Karl, 2007). I will now demonstrate how the revenue base of resource-rich countries differs significantly from that of states who rely on domestically generated income for their survival. Adjusting the assumptions of our model to the realities

¹³ As argued by Calomiris and Haber (2014), financial sector outcomes reflect a deal struck between political leaders in need of financing and financiers seeking government guarantees (p. 38-41). Similar reasoning is presented by Haber et al. (2003); Rajan and Zingales (2003); Girma and Shorthand (2008).

of resource-rich states matters because, as other studies have shown, the source of a state's income influences "the state's institutional development, its abilities to employ personnel, subsidize social and economic programmes, create new organizations, and direct the activities of private interest" (Karl, 1997, p.13).

There is a comprehensive literature dealing specifically with the political economy of resource-rich countries. An influential strand of this literature originated with the study of oil-rich states in the Middle East. It showed how the presence of ample resource rents renders an exceptionally dominant role to the government as the main overseer of state income, in turn generates two interrelated effects: the detachment of the state from the domestic economy and the state assuming the role of allocator rather than that of production promoter (Mahdavy, 1970). Particularly, in resource-rich countries, access to externally derived revenues in the form of rents¹⁴ puts power in the hands of the state as the main manager of this income.¹⁵ A rentier state is a country that "derives a substantial part of its revenue from foreign sources and under the form of rent" (Beblawi, 1987, p.11). The state's ability to trade primary exports means that the collection of domestically sourced revenues is less important for the state's survival (Ross, 2001). The freedom from having to raise income domestically, typically through taxation, is key. It implies that the state is largely liberated from its domestic fiscal base and instead sustained by the economic base of the countries that import its oil (Luciani, 1987).

¹⁴ The definition of mineral rents (oil, gas, gasoline, silver, diamonds and copper) used in the World Investment Report on Extractive Industries by UNCTAD (2007, p. 154) is the "difference between the market price of the minerals and the relevant costs, including the costs of exploration, production and any necessary processing (processing or treatment required to make transportation economically feasible), as well as a certain ("normal") return on investment."

¹⁵ Because oil valorization implies a relationship with the rest of the world, it tends naturally to fall within the responsibility of the state (Luciani, 1987).

The freedom from levying taxes furthermore “releases the state from the accountability ordinarily exacted by domestic appropriation of surplus” (Anderson, 1987, p.10). Whereas the story of modern western democracies is one of citizens demanding political representation in return for taxation, the opposite is held to be true in rentier states since here states do not rely on the “surplus production of the population” (Karl, 2004, p.1). This in turn provides political leaders of rentier states with greater autonomy in decision-making. Since these states are less reliant on extracting revenues from their domestic base, “there is a risk that political institutions become more preoccupied with managing and sustaining these rent flows than developing a more productive and diversified national economy” (Niño and Le Billion, 2014). Rentier states can afford to expand their presence in the economy without having to resort to taxation. Political leaders can spend their externally derived revenue on strengthening of the domestic economic base but it is not required, for the expansion of the state is independent of the strength of the domestic economy (Luciani, 1987).

Whilst the majority of citizens of rentier states are excluded from the process of wealth generation, more are engaged in the “distribution and utilization of this wealth”(Beblawi, 1987, p.51–52), giving rise to what Luciani (1987) labels the allocation state. In the allocation state, the majority of the population derives its income from the state itself as the state allocates external rents to citizens on whose contributions it does not rely. As argued by Mehlum et al. (2006) positioning oneself favourably within the state’s distributive structures becomes the favoured way of citizens of rentier states to secure a slice of the cake. This in turn impacts on the ethics of work as income is no longer seen as a reward for work but rather becomes associated with circumstances, chance, and location, what Beblawi (1987) describe as a ‘rentier mentality’. “To the individual who feels his

benefits are not enough, the solution of manoeuvring for personal advantage within the existing setup is always superior to seeking an alliance with others in similar conditions” (Luciani, 1987, p.76).

Rentier theory is important for understanding resource-rich countries like Angola, where the availability of substantial resource revenues renders tremendous power to the state to the detriment of other actors in society, including independent economic elites and business entrepreneurs. A consequence of this is that political elites and economic elites in the countries of interest here, often overlap (Ferreira and Soares de Oliveira, forthcoming; Malik, 2017; Johnson, 2000). These features which resource-rich countries frequently display – of the nature of the state and the resource-rich state in relation to society – need to be included when dealing with questions of development and change.¹⁶

The second assumption that needs modification to fit the purpose of this study is that concerning the nature of accountability structures assumed in the political economy studies reviewed in the last section. The existing scholarship assumes that political leaders that are not held accountable through formal competitive political institutions are not held accountable at all.¹⁷ As a consequence, political leaders of resource-rich countries with weak political institutions¹⁸ are expected to act in a self-maximizing way, typically to the detriment of the economy. External rents produce financial leeway for the state and the citizens of resource-rich states are thus believed less likely to hold their rulers to account

¹⁶ As the last chapter already made clear, I do not argue that these features are unique to resource-rich countries. Arriola (2013) underscores how strong states and weak economic elites have been a feature in many African countries post-independence. What is special about resource-rich countries, however, is that political leaders’ access to resources also renders it less likely for opposition coalitions and entrepreneurs independent of the state to emerge, as Arriola (2013) shows in the case of oil-rich Cameroon (in contrast with Kenya).

¹⁷ As is the case in for instance Bhattacharyya and Hodler (2014).

¹⁸ As was demonstrated in the introductory chapter, the majority of resource-rich countries fall into the category of having weak political institutions (see Appendix 1).

(Moore, 2004).¹⁹ The following quote by Karl (2007, p.264) summarizes this way of thinking well, “Because petrodollars are not “their” money, citizens are not motivated to ensure that state revenues are well spent; they are not engaged; and they seldom demand better monitoring of the utilization of revenues”.

Yet a number of studies show that weak political institutions coupled with resource abundance does not necessarily produce all-encompassing state autonomy. Rather, as Schubert (2017, p.171) asserts, “relations of power in any society are diffuse and ubiquitous, and never as totalizing as power, embodied in a party, government or individual political leader would have it.” As argued by Geddes (1994), most politicians face a dilemma; political survival is the main ambition for political leaders of both autocracies and democracies but leaders also want to do something with the power they hold. This could be the accumulation of private wealth, the gaining of individual and/or factional benefits (Geddes, 1994). But to achieve these goals, political leaders must remain in power. Political leaders are thus forced to reconcile two conflicting logics of securing immediate political survival versus the longer-run interests in economic performance and regime stability (see also Whitfield and Buur, 2011).

As Hertog (2010) demonstrates in the case of Saudi Arabia, whilst large increments of oil income initially increased the menu of institutional options available to the elite, over time, the regime built up large-scale fiscal obligations towards its supporters with the result that political leaders’ fiscal space contracted significantly over time. Similarly stressing the role of interest groups, Saylor (2014) shows how policy space is far from automatic but rather

¹⁹ For a discussion of the importance of the ‘fiscal social contract’ proposition more generally see Moore (2004). Ross (2001; 2012) and Karl (2007) apply this proposition specifically to the case of the oil-rich state.

a function of country's coalition politics. How political leaders respond to the demands that are placed on them depends on the nature of their power base and more specifically, who is included in the ruling coalition or not. Finally, one must not forget that external dominance and control of capital and technology in resource-rich countries forces these governments to engage in negotiations with foreign companies in addition to any bargaining that they do with their own populations. As pointed out by Shafer (1994), companies in the rent-generating sectors are often highly organized and these extractive firms can exert pressures on resource-rich states, in turn undermining state autonomy.

Country examples also challenge the existence of an autonomous rentier state sheltered from popular demands, oil-rich Bahrain being a case in point. Even if the Bahraini state only imposes negligible tax demands on its population – the Bahraini people are amongst the richest in the Middle East – the political leaders of Bahrain faced sizeable anti-government protests in 2011 over lack of representation (McEvers, 2012). Popular uprisings in Angola after 2012, Algeria, Ghana and Venezuela further corroborate the claim that resource-rich states are not necessarily sheltered from the electorate.

Moreover, rulers usually rule in coalition (Levi, 1988). In their analyses of financial sector outcomes in a number of dissimilar developing countries, Saylor (2014) and Arriola (2013) confirm the central role of coalition politics to explain development outcomes. Both authors show how the composition of countries' ruling coalition matters for how the financial sector performs, whether it is in the form of banking expansion (Arriola, 2013) or through an extension of credit (Saylor, 2014). As Lewis (2007) demonstrates in the case of Indonesia, remarkable developmental initiatives under Suharto stemmed from the need of the regime to mitigate class-based political tensions. In Malaysia, Di John and Putzel (2009) show how

substantial clientelist and populist pressure existed to redistribute income and assets away from the dominant economic groups toward the more economically marginalized but majority ethnic Malay population.

The above examples show how political leaders, even in the presence of weak formal institutions, still answer to certain groups that ensures their position of power. As Bueno de Mesquita et al. (2003, p.28) notes, “no leader rules alone. Even the most oppressive dictators cannot survive the loss of support among their core constituents.” What constitutes the critical mass of support necessary for a political leaders to maintain power? “In democracies, the winning coalition is the group of voters who elect the leader; in other systems, it is the set of people who control enough other instruments of power to keep the leader in office” (Bueno de Mesquita et al., 2003, p.7). Common to both regime types is that for a ruling coalition to maintain political order the distribution of resources must be in line with the underlying distribution of power in a society. The nature of institutions is central in this regard because institutions determine the flows of resources to different groups and individuals in society (Khan, 2010).

Institutions consist of formal rules but they can also be informal. Helmke and Levitsky (2004, p.727) distinguish the two forms of institutions in the following way, “formal institutions are openly codified, in the sense that they are established and communicated through channels that are widely accepted as official ... informal institutions are socially shared rules, usually unwritten, that are created, communicated, and enforced outside of officially sanctioned channels”. In developing countries, formal institutions rules are often only partially enforced (Khan, 2010). Developing countries often share many of the formal features of advanced countries: they have property rights, they have courts enforcing these

rights through the rule of law, and they often have institutions of democracy. But formal institutions do not always behave in the way we expect them to or they are not implemented impersonally (Khan, 2010).

By exaggerating the role of formal institutions, prevailing political economy of finance explanations discount the distributional demands and/or direct threats raised against political leaders in developing countries, which may also derive from outside formal institutional channels. In these countries, personalized and informal exercises of power are often widespread. Stokes et al., (2013, p.10) describe how such informal exercises of power are generally characterized by non-programmatic distributive strategies, meaning that “there are no public criteria of distribution” or if there are “the public criteria are subverted by private, usually partisan ones.” When the ruling coalition offers benefits on the condition that recipients return the favour with a vote or through other forms of political support, this constitutes clientelism.²⁰ Once clientelism is directed at party members, typically through the intra-party flow of benefits such as public employment, it is identified as patronage (Stokes et al., 2013). Because of the weight of informally organized political power in many developing countries, non-programmatic distributive strategies including clientelism and patronage are assumed critical in ensuring ‘social order’ (Khan, 2010).

5. The theoretical framework

In the thesis I will refer to the above-mentioned social order as a political settlement. The political settlement concept is often used in a loose sense to refer to the prevailing political

²⁰ If the distribution of benefits is not directly linked to the return of the favour with political support but rather meant to generate goodwill among recipients who may, as a consequence, be more likely to support the benefactor candidate or party, then that constitutes *unconditional partisan bias* (Stokes et al., 2013).

order or to specific peace agreements that emerge at the end of war.²¹ A political settlements approach, however, offers a much more specific reading of the term. Developed initially in the work of Mushtaq Khan (1995; 2010; 2017), a political settlement is defined as “a combination of power and institutions that is mutually compatible and also sustainable in terms of economic and political viability” (Khan, 2010, p.4). The political settlement approach seeks to address two related questions; One, what kind of institutions are likely to emerge in different contexts and two, how effective will they be in achieving the objective they were set out to address (Khan, 2017)? For the objective of this study — to understand the drivers of institutional change in the financial sector — the first question is of most relevance.

The political settlements approach developed initially as a critique of new institutional economics (Khan, 2010). According to new institutional economists, Douglass North and others,²² the role of institutions are seen as central to solving particular problems related to political, economic and social interaction. Specifically, institutions emerge out of the need to “create order and reduce uncertainty in exchange” (North, 1991, p.97). This early institutional literature often ignored the “dual character” of institutions; that each institutional rule involves a fundamentally different distribution of net benefits across individuals and groups (Khan, 2010, p.19).²³ On the contrary, the political settlement literature emphasized that an institutional rule, in addition to having a potential effect on

²¹ The UK Department for International Development (DFID) used political settlements in the former way to refer to a political order, defining a political settlement as a “forging of a common understanding between a country’s elites that their interests are served by acquiescing to a particular form of state”(DFID, 2009, p.26). Parks and Cole (2010), and Dudouet and Lundström (2016) use the term political settlement more loosely to refer to the social order that emerges following conflict.

²² The term ‘new institutional economics’ originates from Williamson (1975). In addition to the early work of North (1990, 1995), other prominent works which are often characterized as new institutional economics include Ostrom (1990); Olson (1997); Bates (2001); Acemoglu, et al. (2001).

²³ See for instance, North (1990) and North (1995).

efficiency and growth though its impact on the costs of making decisions, also defined the distribution of net benefits (Khan, 2010).

The conflicting aspects of institutions as a fundamental determinant of the path of institutional change (Khan, 2017, p.4) is now widely accepted in the political economy scholarship.²⁴ As is the idea that institutions work in different ways in developing and developed countries (North et al, 2009; Khan, 2010). The political settlements framework has thus come to share many similarities with more recent thinking in new institutional economics, particularly North et al. (2009; 2013) and these authors' work on violence and social order. Both the political settlement framework and the framework presented in North et al. (2009) go beyond a fixation on regime type to focus instead on the deeper forms of politics and power relations that underpin institutional performance. Power struggles are here central to explaining institutional outcomes. Whilst both frameworks emphasise how institutions work differently in developing and developed countries,²⁵ they also demonstrate that countries who do not qualify as "rule-following and impersonal 'Weberian' state[s]" (Khan, 2010, p.10), are still able to support "durable institutional structures for the state" and "elite organizations outside the immediate framework of the state" (North et al., 2009, p. 47).²⁶ Consequently, even where formal rules are not observed, political stability can be achieved which can facilitate economic growth and development.

²⁴ Acemoglu et al. (2005) and North et al. (2009;2013).

²⁵ North et al. (2009) divide countries according into two distinct social orders, the Limited Access Order and the Open Access Order. In Limited Access Orders, which include all developing countries, social order is maintained by "limiting access to economic and political organizations and thus creating rents. These rents are then distributed to powerful groups to incentivize their peaceful cooperation within the existing order" (Gray, 2016, p.53). In contrast, in open access societies "competition, open access to organizations and the generalized rule of law" ensures social order and minimizes violence, promotes stability and breeds economic growth (Gray, 2016, p.53). Khan (2010) differentiates between the clientelist political settlements found in developing countries, where 'personalized' or informal exercises of power, dominates. And the capitalist political settlements that characterize societies where the formal productive sector dominates the economy.

²⁶ Organizations are by both North et al. (2009, p.7) and Khan (2017) conceptualized as a structured way of coordinating the actions of several individuals and groups.

Notwithstanding the resemblances of the two frameworks,²⁷ I proceed more closely with the political settlement framework. I do so because I believe the latter framework to be more helpful in explaining institutional change in the resource-rich countries, the main aim of this thesis. Although the North et al. (2009) framework provides important insights,²⁸ this framework provides relatively little guidance on understanding evolution between different types of natural states (the designation given to all developing countries). This is problematic as it is the group of countries in which most resource-rich countries fall. As North et al. (2009, p.xii) acknowledge in the preface to their 2013 paperback edition, the conceptual framework as it was initially developed, was primarily concerned with explaining countries' transition from natural states to open access order. In their subsequent book, North et al. (2013) engaged more explicitly with the development problem that is the development from fragile natural states to more mature ones. Still, the authors do not provide a clear framework for assessing the kind of development applicable in these contexts, pointing rather to processes which they suggest are key for the maturation of natural states (North et al., 2013).²⁹

²⁷ For a further discussion about the two frameworks, their similarities and differences, see Gray (2015).

²⁸ Rather than institutional change, the conceptual framework as presented by North et al. (2009) focuses on the institutional outcomes which characterizes the different typologies of natural states. The authors describe how countries progress from natural states, characterized by simpler institutions and less sophisticated organizations, to becoming more mature states with power based on more complex institutions and more sophisticated organizations, before eventually graduating to becoming open access societies, characterised by open competition in the economic and political sphere (North et al., 2009). This latter focus provides us with noteworthy insights into how these states work and are organized.

²⁹ To be clear North et al. (2009; 2013) underscore how bargaining between public and private organizations is key to driving institutional change. The authors state that, "When elite organizations [which enjoy some degree of independence from the state and freedom of action] have an enhanced ability to discipline (or reward) the state for violating (honouring) its commitments, then natural states are better able to credibly commit to more sophisticated public organizations as well... If and when limited elite rights to form organizations emerge, basic natural states move closer to mature states. *Mature natural states cannot develop without more sophisticated private organizations*" (North et al., 2009, p.49, my emphasis. See also North et al., 2013, p.15). How such elite organizations, capable of challenging the state, emerge is less clear.

In this regard, the political settlement framework is more helpful. According to Khan (2010, p.4),

“A political settlement that reproduces itself over time must have institutions whose benefits are consistent with the distribution of organizational power and which also achieves the minimal levels of political stability and economic performance required to be viable. If powerful groups are getting a distribution of benefits that is too low given their relative power, these groups will strive through different means including conflict to change institutions till they are satisfied or they give up. While this conflict is going on the contestation can directly affect political stability or it affects economic performance by affecting the implementation of institutional rules. A serious incompatibility can make the political settlement unviable. But a compatible combination of institutions and power can also be unviable if economic performance is too poor.”

The relative power of different groups is referred to as their holding power. Holding power can be conceptualized as the ability of individuals and groups to “hold out” in contests with others when seeking to influence institutional outcomes (Khan, 2017, p.5; Knight, 1992). Holding power does not derive solely from economic means of an individual or organization but equally on the latter’s capacity to organize, the capacity of their leadership to mobilize support, and their skill in identifying and rewarding the right people through formal or informal networks (Khan, 2017).

The kind of institutions that a ruling coalition will be able to establish and sustain is moreover understood as depending on its internal structure (that is, the strength of lower-level elite factions, also called the vertical distribution of power) and the ruling coalition’s position within society (that is, the strength of excluded factions, also called the horizontal

distribution of power). When horizontally excluded factions are powerful, the vulnerability of the ruling coalition increases. Threats from external factions in turn reduces the ruling coalition's time horizon which affects the types of economic strategies it will be willing to support through formal and informal institutions. But ruling elites also have to organize factions below them to give them the holding power necessary to rule. The stronger the lower-level factions, the less the capacity of political leaders to enforce institutional changes that lower-level factions may contest (Khan, 2010). "This is because given the pyramidal structure of patron-client organizations, the more powerful lower level factions become, the greater the number of points at which the enforcement of particular rules can be blocked. Enforcement and implementation now requires much greater collective action and the distribution of rents to many or all lower-level factions to ensure their cooperation. Otherwise, those who are adversely affected by a rule simply have to buy in a small number of lower-level factions to block its implementation" (Khan, 2010, p.65).

The early ideas of Khan (1995; 2001; 2010) are increasingly being used to study a multiplicity of policy issues and a variety of contexts.³⁰ The wide application of the concept is likely to be one reason why the framework has been accused of being underspecified (Van de Walle, 2016) and analytically redundant as a concept (Moore, 2012). However, if we return to the original framework as proposed by Khan (2010) and discussed in this chapter, it is clear that it can help us analyse institutional emergence through looking at the likely time horizon of political leaders and their implementation capacities. It is to this latter purpose to which I will apply the framework in this thesis.

³⁰ Notable studies applying the political settlement framework include Di John and Putzel (2009; 2014); Whitfield et al. (2015); Abdulai and Hickey (2016); Gray (2018). In the Angolan context, Croese (2017) applies the political settlement framework to study state-led housing delivery.

There are also limits to what the political settlement framework can explain. As was acknowledged in the introduction of this chapter, particular changes in policies or institutions do not always reflect of the distribution of power in a society in a straightforward manner (Khan, 2017). It is also necessary to take into account the agency of governments and other organizations to shape policy, which may depend on other things than internal politics including ideology, the personal characteristics of leaders, and international factors. Earlier studies of political settlements have often underplayed the role of international factors in shaping political deals and subsequent outcomes.³¹ To focus on internal political variations, international dynamics are often held more or less constant in the political settlement literature. In doing so, these studies underplay the fact that elites “actively seek to position themselves within transnational flows of power and opportunity” and that this in turn shapes internal political dynamics as well as domestic policy outcomes (Hickey, 2013, p.20). This is especially true in the case of resource-rich countries, where the states by definition depend on external rather internal sources to sustain power (Beblawi and Luciani, 1989). In this regard, the framework presented by North et al. (2013), extending the framework presented in North et al. (2009), could be helpful. The authors include a global dimension in the form of how domestic elites use transitional organizations/corporations and global markets to deal with the issue of providing a reliable third party to enforce agreements. An example of this is what Lewis (2007) describes in the case of Indonesia, where the fact that Indonesia had open capital accounts (which meant that investors could easily move their money out of the country if they wanted to) had a disciplining effect on the rule of President Suharto and his team.

³¹ As is the case in the work of Khan (2010), Whitfield et al. (2015), and Gray and Whitfield (2014).

To better account for how international forces combined with a country's geopolitical position "fundamentally alters the character of bargaining both between elites and between elites and lower-level groupings" (Hickey, 2013, p. 20) this thesis does not hold external factors constant but rather seeks to understand how the bargaining power of domestic vis-à-vis external actors shape the political bargaining domestically as well as political leaders ability to define domestic institutions and policy. In recognizing that international factors also play a pivotal role in forging institutional outcomes, the thesis moves beyond the common emphasis of the political settlement framework to better fit the experience of the resource-rich state.

With the extended political settlement framework as the guide, the goal of this study is to build on the political economy of finance analysis surveyed so far to shed light on financial sector change in the authoritarian resource-rich case of Angola. The thesis will extend beyond the current literature by incorporating what I see as particular features of resource-rich authoritarian states, features which previous studies have failed to take into account.

6. Central arguments

The argument that I present in this thesis is that changes in Angola's financial sector have come about as political leaders seek to ensure that the distribution of resources is aligned with the distribution of power. It follows from this that reforming existing institutional structures was necessary when these structures came under strain and/or were no longer able to support the required distribution of resources. When does this happen? Institutions come under strain when the level of economic performance is too low. What is considered sufficient economic performance is moreover relative and depends on the historical context

and importantly, the expectations of powerful groups (Khan, 2010). As the following chapters will demonstrate, in the Angolan case, institutions and the distribution of resources that they support, have ceased being viable both in moments of regime weakness but also in moments of regime strength. Let me elaborate on each scenario, starting with the former.

In the case of extraverted resource-rich economies, a group to which Angola belongs, changing external conditions can have momentous impact on domestic economic performance. External changes, such as fluctuations in the global price of oil, impact the financial capacity of the Angolan state through access to export revenues. It also affects the rest of the economy indirectly through reduced economic activity. In the late 1980s, changed external conditions meant that existing institutional structures — on which the distribution of resources in Angola was based — was unworkable. Political settlement theory predicts that in such instances, powerful groups will strive to change the underlying institutional structures so that these institutions can again produce an economic outcome deemed satisfactory (Khan, 2010).

The fact that the MPLA party managed through the latter period, one marked by profound institutional change, whilst ensuring political continuity suggests that political leaders were not responding to internal pressure nor were they driven by mobilization from excluded factions. If the latter was the case, and the issue was that the relative distribution of resources was unaligned with the distribution of power, then it is unlikely that political continuity would have prevailed. Rather, the issue of the late 1980s was that the economic situation had significantly deteriorated. For political leaders to preserve power, the most obvious solution at the time was to liberalize economic policies. Political leaders'

determination to ensure the economic viability of the political settlement thus drove change in this instance.

Financial sector change need not only come about in moments of weakness, however. In 1999 the Angolan political leadership decided to move ahead with a number of important economic reforms that laid the foundations for macroeconomic stability generally and private sector banking more specifically. Earlier accounts largely attribute institutional reform to the desperate economic situation in which the country found itself in the late 1990s. On closer inspection, however, it is clear that the economic and political situation that the MPLA found itself in was more favourable than often assumed. Importantly, with some of the largest offshore oil discoveries in the world having been made in Angola during this time, foreign investments into the country were surging (Shaxson, 1999b). Politically and diplomatically, the MPLA was moreover ahead of its rivals. Rather than coming from a place of weakness, I therefore argue that the economic reforms of the late 1990s should be interpreted as a sign of far-sightedness on behalf of the regime. For political continuity to be ensured, institutional structures needed to be reformed and the economic crisis of the late 1990s was an occasion for political leaders to do just that.

After theorizing about the reason why political leaders instigate financial sector change, the next step is to consider why financial sector change took the direction that it took as well as political leaders ability to pursue these changes. Let us first consider domestic factors. Here my argument builds on the claim by Khan (2010), that in order to understand the time horizon of political leaders and their capacity to implement policies, it is necessary to account for the different pressures exerted on them from domestic factors. These can be pressures mounted at the political leaders horizontally, from excluded elite factions, or

vertically, from lower level supporters. Specifically, with the threat from a powerful excluded faction, like UNITA in the case of the MPLA, ruling coalitions are likely to adopt a short time-horizon. This fits the Angolan case where financial sector policy between 1975 to 1999 was — not unlike most policies in the country – marked by a lack of planning and the absence of any longer-term view. Faced with a strong excluded faction, the immediate survival of the state was the main objective of the ruling coalition during this period. Only in 2002, when UNITA was defeated, did the MPLA no longer face any meaningful external faction. The eclipsing of UNITA as a systemic threat to MPLA rule allowed political leaders to proceed without fear and to adopt longer-term policies which would further cement the governing party in power.

Political leaders ability to pursue changes were not only conditioned by domestic factors. External factors, most notably the global price of oil, were also critical for understanding political leaders' ability to carry out their political agenda. Oil revenues have, in the period studied here, dominated both Angola's export revenues as well as total revenues accruing to the state. For the argument presented here, the global market for Angola's primary commodity is crucial in two interrelated ways. Firstly, as already mentioned, the global oil price directly influences Angola's economic performance and thus the ruling elites' ability to please critical constituencies within the existing institutional set-up. When oil prices fall, economic performance suffers. Secondly, the global oil price is a key factor in the forthcoming analysis because it directly impacts on political leaders' power to pursue their policy agenda, what I in this thesis refer to as policy space following Dafe (2017; see also Winter, 1994). When the state controls a low level of resource revenues, political leaders' policy space is reduced as the reliance on external financing heightens. Political leaders' policy space contracts because they feel pressured to implement policies which are

responsive to the interests of their financiers – in a resource-rich economy typically external – or risk much needed capital being withdrawn (Lindblom, 1977). In Angola’s case, major financiers traditionally have been the IFIs, bilateral lenders and foreign banks as creditors. As will become clear in the course of the thesis, the policy stance of external financiers need not necessarily be opposed to the interests of the elite. This is not the essence of my argument, however. Rather, the point is that political leaders room to mediate demands from financiers tends to diminish when resource revenues decline. And resource revenues decline when the global price for oil falls. The opposite is true when the global price of oil increases and the revenues to the state mount. In such a situation, the influence of financiers over domestic policy is expected to decrease as the need of the state for external financing decreases (Winters, 1996). As a result, political leaders policy space to pursue their own policy agenda, expands.

Building on the above theoretical and empirical insights, in the next four chapters I will use the Angolan case to illustrate my claim that having a modern financial sector is useful for resource-rich countries even if the state does not rely on this sector to provide it with the revenues necessary for survival. I will show how the Angolan financial sector has become important to the MPLA regime’s hold on power by supporting the distribution of rents as well as becoming a centre for rent generation itself. Having a modern banking sector opens up new avenues for rent distribution, which is useful for allocating selected benefits to political supporters and in that way retaining loyalty to the state. The creation of a modern banking system equally allows for the generation of new rents, rewarding business networks with close connections to the regime. Both functions of having an operational financial sector can be useful in a clientelist system like that of Angola, where political leaders need to offer backers, existing or potential, benefits in return for votes or other

forms of political support. The type of financial sector changes that takes place and the institutions that are encouraged is furthermore contingent on the kind of supporters that political leaders hope to mobilize. The argument presented in this thesis differs from what scholars have hitherto argued as I emphasize the role of the state as the leading driver of the financial sector outcomes that we have witnessed in the Angolan case.

7. Conclusion

The objective of this chapter was to critically review the existing literature in order to lay the theoretical foundation for what is the argument and contribution of this thesis. As stated initially, the literature concerned with financial development in resource-rich developing countries shows that these countries perform comparatively poorly in deepening and broadening their financial systems. Our knowledge of what drives financial sector outcomes across resource-rich developing countries is still limited, however.

Structural explanations of financial sector development in resource-rich countries produce important insights but leave politics out of their models. Instead, a growing body of scholarship that adopts a political economy approach to the study of financial sector outcomes, acknowledges the role of politics in shaping the institutions and laws that underpin economic life and also financial systems. Yet this chapter identified two limitations in the existing literature with regard to the experience of resource-rich developing states.

Firstly, the fiscal base of resource-rich countries is fundamentally different from resource-poor countries, as the former group of countries derive significant resources from abroad.³²

³² Other countries who are not rich in resources can also exhibit certain rentier qualities, including aid-dependent countries (Brautigam and Knack, 2004)

The external dominance and control of capital and technology has meant that resource-rich political leaders engage primarily in negotiations with foreign companies rather than bargaining with their own citizens. The implication for this study is that the demand driven development assumed in prevailing political economy studies of finance cannot be easily transferred to the case dealt with here, where the state rather than any private sector is the driving force in financial development. Secondly, I argue that existing studies overemphasize the role of formal political institutions. Existing studies consequently discount the pressure on political leaders arising from informally organized political power and informal institutional configurations. This leads these studies to incorrectly assume that political leaders of authoritarian resource-rich states will act unconstrained and discount the financial sector.

I introduce the political settlement framework in an effort to address some of the above shortcomings. Crucially, the political settlement framework can help us understand why political leaders act the way they do through studying at the external and internal pressure asserted against them and their support base. It was also pointed out that the political settlement is less helpful in understanding the external pressures that also influence institutional change. I therefore introduce to the framework an international dimension in an effort to better explain what shapes institutional outcomes.

In the last section, the argument of this thesis is elaborated upon. It highlights the financial sector's role in supporting new forms of rent distribution in addition to becoming a rent generator itself. Drawing on the case of Angola, I argue that financial sector change resulted from the unviability of existing financial sector institutions, making it necessary for political leaders to respond to the demands for resources by powerful groups. The way that

political leaders responded, the policies they adopted, was the outcome of political conditions at the time. In the beginning, the MPLA was a vulnerable ruling coalition under pressure from a strong excluded faction. By the end of the 1990s, however, as the threat from UNITA waned, the ruling elite grew increasingly confident. As the coming empirical chapters will confirm, the emergence of the country's modern financial sector has contributed to the MPLA regime's hold on power in instances when the ruling coalition has acted out of weakness but also out of strength. Yet, before we turn to the empirical chapters, let us first situate the political economy of Angola's financial sector change in the wider political and historical context of the country.

Chapter 3

The political economy of early post-independence Angola

1. Introduction

This chapter lays out the historical context for my thesis. The chapter centres on the first decades immediately following Angola's independence in 1975, but it also demonstrates how developments that took place during this early period of Angola's independence influenced political and economic developments in subsequent decades. The idea that history matters is in line with the theoretical underpinning of this thesis, which stresses the importance of historical roots to understanding the contemporary distribution of political and economic power in a country (Behuria et al., 2017). I argue that understanding the nature of the Angolan state and how this nature is embedded in the country's historical, political and economic context before 1991 is vital for understanding financial sector changes that took place in more recent decades. The current chapter is consequently more than a historical chapter as it seeks to explain the foundation for and the persistence of power and state society relations that has come to characterize Angola throughout the period on which this thesis focuses.

This chapter allows us to delve deeper and justify some of the central assumptions that underline the thesis. Firstly, this chapter demonstrates that authoritarian political leaders do not discount the need for support. As this chapter shows, building the party machine and a

redistributive system to go with it was a main undertaking of the MPLA from the early post-independence period onwards. Secondly, the chapter also underscores the importance of the oil sector for state survival. It thus dismisses any significant role for non-oil private capital in Angola's early post-independence period. Private capital accumulation, with its roots in Angola's post-1975 informal sector, was always under the control of the party state apparatus.

In the following analysis, I focus on three historical dimensions which I consider pivotal to understanding the Angolan political leadership's outlook and their ability to pursue their policy agenda over time. First, I emphasize the structural impediments faced by the MPLA and threats coming from UNITA, which conjointly limited political leaders' policy space. I highlight the weak state structures inherited by Angola upon independence and the consequences of Portugal's lack of contingency plans, which meant that the African population was particularly badly prepared to take over the political and economic structures that the colonizers abandoned in 1975. The mounting challenge posed by UNITA meant that the MPLA was forced to continuously defend its precarious grip on power, depriving the party of control over large parts of the national territory. Other state responsibilities, including economic planning, was discounted.

Second, I show how the MPLA's particular position vis-à-vis society must be understood in terms of the movement's social and cultural background. The MPLA was formed mainly by educated Angolans who had enjoyed certain privileges under the colonial system. This differentiated the MPLA leaders from the majority of Angolans who had consistently been deprived of similar opportunities. This however did not prevent political leaders from successfully using the state party apparatus to mobilize and to reward followers. The

elaborate economic arrangements that followed independence further reinforced the central role of the state to economic opportunities, in the informal sector as well as in the formal sector, with those closest to power having the greatest opportunities to accumulate wealth.

Third, I elaborate on the institutions that made regime survival possible, namely the national oil company Sonangol and the national armed forces. In contrast to all other sectors, oil and defence were largely shielded from the general devastation that inflicted the rest of the country, as well as the mismanagement that engulfed almost all economic sectors. The oil sector was pivotal in providing capital to sustain basic government operations and importantly, for fighting the war. The military became increasingly dominant both as an economic and a political force. All this was possible because of parallel power structures (Soares de Oliveira, 2015), meaning command structures that developed outside the formal government and party structure. These parallel power structures granted considerable discretion to President José Eduardo dos Santos over the sectors at the expense of the formal party apparatus.

2. Implosion at independence

Angola officially obtained its independence from Portugal on 11 November 1975. At the time, the country's former colonial master, Portugal, had just ended a 13 year-long colonial war in its overseas territories, starting in Angola in 1961, Guinea-Bissau in 1963 and Mozambique in 1964 (Chabal, 2002). It was the April 1974 Carnation Revolution in Portugal, in which a faction of the Portuguese army toppled the dictatorship led by Marcello Caetano,¹ that brought the long-running colonial wars to an end. The process of

¹ In 1968, Marcello Caetano replaced the long-time prime minister of Portugal's Second Republic, António de Oliveira Salazar. Salazar had held the position of prime minister from 1932 to 1968 (Birmingham, 1993).

decolonizing Portugal's overseas territories was initiated shortly afterwards (MacQueen, 1997).

Angola's decolonization process was difficult for several reasons, two of which stand out and help explain why the transition continued to have such a profound impact on the Angolan state and society in the following decades. Firstly, at the time when Portugal decided to decolonize following the 1974 revolution, little consideration had been put into how this decolonization would actually unfold (Dos Santos, 1990). Portugal had long refused to decolonize its empire. The African territories were defended as "an integral part of Portugal" (Cooper, 2002, p.139), and the Portuguese presence in the colonies presented as fundamental to the preservation of the modern multiracial societies it had helped create (Bender, 1978, p.xxi).² Adding to this, Angola in the 1950s was experiencing an economic expansion, having started extracting diamonds, oil, copper and iron ore, which complemented the country's already abundant cash crops (Guimarães, 2001; Ferreira, 1999).³ Angola boasted a relatively diversified economy: in addition to agricultural production and mining, the country had one of the largest manufacturing sectors in sub-Saharan Africa (Ferreira, 2002a; Ministry of Finance, 1990).⁴ Economic opportunities attracted a growing number of Portuguese immigrants to Angola (like in Mozambique) in the 1950 and 1960s. While Angola had always had a sizeable white population, by 1974 it had an estimated 335 000 Europeans, the second largest such presence in Sub-Saharan

² In 1951, in what has been interpreted as a pre-emptive measure on behalf of the Portuguese against international pressure for decolonization, the status of the Portuguese colonies was officially changed from colonies to 'overseas provinces' (MacQueen, 1997, p.11).

³ Scholars, amongst them Clarence-Smith (1985), questions the economic value of the African colonies to Portugal. As Clarence-Smith (1985) convincingly argues, whereas the African colonies were more profitable to Portugal after 1950 (although never as profitable as Brazil), Portugal could potentially have benefitted more had it chosen to integrate with its European neighbours instead of holding on to its colonial empire (the latter precluding the former).

⁴ This did not mean that the economy was self-sufficient, however, as Angola's industry was largely dependent on imported inputs (Ferreira, 2002).

Africa after South Africa (Pimenta, 2012, p.178; see also Castelo, 2007). Consequently, as other European powers started to plan for self-government in the colonies (Cooper, 2002) the Portuguese clung on to power.

This links to the second reason as to why Angola's decolonization process was particularly complex and destructive, which is the lack of any unified national elite to take over control of the state apparatus that the Portuguese left behind. As Cahen (2012, p.15) argues in the case of Angola, Mozambique and Guinea- Bissau, "there was almost no social space for the emergence of a new urban (as well as rural) African elite, because whites occupied the whole sphere of wealth creation" (see also Clarence-Smith, 1985).⁵ Despite a late colonial effort at expanding educational opportunities, the overall results of Portuguese colonialism was that it did not contribute to a trained African workforce of any significance (Hodges, 1993; Bender, 1978). As described by Sommerville (1986, p.131), the Portuguese "monopolized all managerial and technical jobs and most skilled occupations right down to the level of truck and taxi drivers and street vendors." Still, the presence of settlers did not prevent PAIGC⁶ of Guinea-Bissau and FRELIMO⁷ of Mozambique from emerging as political parties and taking over power from the Portuguese as independent governments in 1974 and 1975 (Williams, 2012, p.236). Unlike PAIGC and FRELIMO, the urban based MPLA never emerged as a broad nationalist-front to fight for Angola's independence (Péclard, 2012). In Angola, the prospect of a pan-national elite had been undermined by amongst other things the divide between the urban and the rural parts of the country, enforced through very different experiences of colonial rule and relationships to the

⁵ In the settler exodus that followed independence, the vast majority of Angola's trained personnel vanished (Rocha et al., 2014).

⁶ The African Party for the Independence of Guinea and Cape Verde, *Partido Africano da Independência da Guiné e Cabo Verde*.

⁷ Mozambique Liberation Front, *Frente de Libertação de Moçambique*.

colonial state (Soares de Oliveira, 2015, p.9).⁸ On the eve of Angola's independence in 1975, there was therefore not one but three different nationalist movements ready to succeed the Portuguese government. In addition to the MPLA, there was the Frente Nacional de Libertação de Angola (FNLA), created in 1957, and the União Nacional para a Independência Total de Angola (UNITA), founded in 1966 as the result of a split within the FNLA (Péclard, 2012).⁹

2.1 Diverging movements, disagreeing visions

Several characteristics have been highlighted to differentiate the three nationalist movements that emerged in Angola in the late 1950s and 1960s: their ethnicity (Marcum, 1978),¹⁰ their connection to the church (Péclard, 2012),¹¹ how the movements interacted with the colonial structures in different ways (Messiant, 2006) and relatedly, whether the movements adopted a “modernist” ideologically progressive view or more “traditionalist” view tied to prevailing African social-political orders (Chabal, 2002, p.5-6).

Notwithstanding their differences, the three movements accepted the state apparatus established by the Portuguese as the structure with which to govern the new country (Soares de Oliveira, 2015).¹² Yet, in the end, the movement's different notions of what post-

⁸ Whereas Angolans living in the long colonized areas of the Mbundu hinterland of Luanda enjoyed some colonial modernity, for those living in the rural areas the situation was considerably more precarious (Soares de Oliveira, 2015).

⁹ The year the MPLA was created remains open to dispute. The official version states that the party was founded in 1956 (MPLA, 2017), which would make it the oldest nationalist movement in the country. This claim has now been widely discounted (Newitt, 2007), with a more likely date being 1960 (Péclard, 2012). For more on the debate of when MPLA was founded, see Marcum (1969) and Guimarães (2001).

¹⁰ The Bakongo elites of northern Angola founded the FNLA, the Ovimbundu elites of the central highlands funded the UNITA and the MPLA was founded by elites originating from the Mbundu dominated area in and around the capital of Luanda (Soares de Oliveira, 2015).

¹¹ The FNLA connected to the British Baptist Missions, the MPLA to the US Methodist and the UNITA to North American Congregationalist missions (Péclard, 2012)

¹² As noted by Clapham (1999; 1996), African states are typically defined by their recognition and acceptance by the international community, granting them certain rights and privileges, rather than by their monopoly of

independence Angola should be, and who should lead it, meant that they were irreconcilable. A power-sharing agreement between the three movements and the Portuguese government, aiming to ensure a peaceful transition of power, broke down almost immediately after its ratification in January of 1975 (Weigert, 2011, Birmingham, 2002; 2015).¹³ In the spring of that same year, the Angolan civil war formally commenced between the three nationalist movements, who had already been fighting sporadically during the colonial war (MacQueen, 1997).

What changed post-1975 was not only the purpose of the fighting but also the international presence. Soon Zairian, South African and Cuban forces filled the military and political vacuum left by the departing Portuguese (Weigert, 2011). With the help of Soviet-supported Cuban expeditionary forces,¹⁴ the MPLA won the battle for Luanda and established itself at the helm of the state apparatus in 1976 (Soares de Oliveira, 2015). The Cuban forces also helped the MPLA disperse competing movements and their allies across the country (Weigert, 2011). Shortly after 1976, the FNLA ceased to exist as a major military-political movement. The UNITA, on the other hand, enjoying the backing of the United States and South Africa, did not surrender. After withdrawing from the towns of the central highlands,¹⁵ the movement regrouped in the rural areas and mobilized masses, first

force over a territory and a population. Particularly, recognition by the outside world affords political elites access to state monopoly on extracting “surpluses from the flow of resources between the domestic and international economies” (Clapham, 1999, p.527).

¹³ The Alvor Agreement, signed by the MPLA, FNLA, UNITA, and the Portuguese government 15 January 1975 (Weigert, 2011).

¹⁴ For an comprehensive account of the Cuban military role in Angola, see George (2005). Hatzky (2015) offers an interesting account of Angolan-Cuban civilian cooperation post-independence. Like the military component, Angolan-Cuban civilian cooperation was substantial and provided much needed political, medical, administrative, and technical expertise to the country (Hatzky, 2015).

¹⁵ In the late 1970s and 1980s, the MPLA gained controlled over certain towns in the Central Highlands. The actual territory that the MPLA controlled was restricted to ‘pockets’ of territory centred around towns (Pearce, 2015).

in the more remote south-eastern areas of Angola and from late 1976 in the central highlands (Pearce, 2015).

By late 1977, revived UNITA forces were threatening government forces along the South African protected borders of the South West (Collelo, 1991). From 1978, hostilities between the two movements intensified and was spreading to all provinces of the country (Weigert, 2011).¹⁶ Whereas the MPLA would remain in control of Luanda and other cities along the coast throughout the civil war, UNITA commanded the south-east and the rural parts of the central highlands from its headquarters at Jamba. The rest of the country was continually disputed by the two movements. The unwavering campaign launched by the UNITA to contest as much territory as possible underscored the precariousness of the MPLA's hold on power at the time. The geographical limits to the MPLA's "ability to construct the apparatus of statehood" (Pearce, 2015, p.69)¹⁷ was further undermined by UNITA's many acts of economic sabotage, primarily in the countryside, which contributed to halting government's programmes (Heywood, 2001).

In the decades of fighting, Angola came to consist of two distinct authoritarian societies; the urban enclave that was the MPLA society and an isolated and rural UNITA society (Messiant, 1992). Both parties held large parts of the Angolan population under their authoritarian control,¹⁸ and both parties had state-building ambitions. Some modern state responsibilities were carried out by the MPLA and the UNITA, including the provision of

¹⁶ In comparison, the colonial war had been largely limited to isolated and thinly populated areas of the country (Weigert, 2011).

¹⁷ For instance, Pearce describes how "Towns were defensible, while any state presence outside the city limits was liable to attack after UNITA resumed its offensives in 1981" (2015, p.69). Soares de Oliveira (2015, p.15) points out how, by early 1993, UNITA controlled 80% of the country.

¹⁸ Messiant (1994, quoted by Pearce, 2015, p.123) distinguished between UNITA who was "properly authoritarian" and the MPLA, which "tolerated neither basic civil rights nor autonomous organisations or associations but which was nevertheless not quite totalitarian."

basic public services and defence (Pearce, 2015; Soares de Oliveira, 2015; Heywood, 1989). Contrary to the MPLA's depiction of UNITA as backwards and a proxy for foreign interests in the country (Heywood, 1989; 2000), the movement was led by an educated elite, able to sway external allies as diverse as Maoist China, apartheid South Africa and anti-communist United States in their favour (Soares de Oliveira, 2015). The party's fight against the MPLA was furthermore expressed in a xenophobic tone, as a fight against the "mulatto-dominated postcolonial state" (Heywood, 2001, p.209), said to be "heirs, both genetically and culturally, of the Portuguese colonizers, and whose roots in Africa were questionable" (Pearce, 2012, p.204).¹⁹

3. The MPLA: The exclusive mass party

To understand why the MPLA would be branded as *foreign* by its enemies and why this narrative resonated with its opponents' supporters (Heywood, 2001), we need take a closer look at the history of this liberation movement turned hegemonic party. Through such an exercise we can also start to better understand the relationship between the party and society, and between the political leadership and the Angolan population.

As is often pointed out, the founding members of the MPLA largely consisted of mixed race (*mestiço*) and assimilated (*assimilado*) Angolans (Mabeko-Tali, 2001a; Birmingham, 1998; Clarence-Smith, 1980). The movement is widely held to be made up historically by two factions. Messiant refers these groupings as the "old creoles" and the "newly assimilated" (1992, p.17-19). Whilst distinct, both groups shared a strong relationship with

¹⁹ Observers of Angola in the 1990s took note of UNITA leader Savimbi's xenophobic rhetoric, "revealing the 'non-Angolan' origins of many government leaders, including the President, whom he refers to as a São Toméan. (Cornwell and Potgieter, 1998, p. 2).

colonial structures which differentiated them from the majority of Angolans (Messiant, 1992, p.17).

The old creoles were the product of centuries of cross-cultural exchange and intermarriage between the European and African populations. Before the 20th century, few Europeans actually resided in Angola and the coastal cities, which represented the backbone of Portuguese interests in the colony at the time, were effectively ruled by creole families. Powerful creole families, often of mixed-descent but with “Portuguese identities”, dominated economic and social life in the colony (Newitt, 2007, p.50; Wheeler, 1969). It was only in the late 19th and early 20th century, with the revival of more formal Portuguese colonial efforts,²⁰ that Portuguese immigration to Angola started to grow. The old creoles were consequently declassed, losing their economic positions and marginalized from the social positions that they had come to occupy in the colonial apparatus (Messiant, 1992, p.16; Schubert, 2017). Angolans were now to be considered assimilated to the extent that they could prove their mastery of “an almost pure, unmitigated Portuguese culture, barely modified by the slightest trace of their own numerically dominant cultures” (Bender, 1978, p.28).²¹ The novel colonial policies led to a new group of assimilated Angolans emerging in the 20th century. These Angolans descended mainly from the “uncivilized” segment of

²⁰ The Portuguese monarchy was toppled and a Republic was initiated in 1910. In 1926, the republic was replaced with military rule and, shortly afterwards, Antonio Salazar's *Estado Novo* civilian dictatorship commenced, lasting until 1974 (Clarence-Smith, 1985).

²¹ The Portuguese Colonial Act of 1930 formally established the legal status of the native population, separating the population of the colonies into two distinctive juridical categories; “indígena (also referred to as uncivilized, unassimilated, or native), which included all Africans and mestiço not adjudged to be civilized; and não-indígena (or civilized), which included all whites and assimilados (mestiço and Africans considered civilized)” (Bender, 1978, p.150). In order for black and mixed-race Angolans to gain the same status as whites, “the individual had to be eighteen years old, demonstrate the ability to read, write, and speak Portuguese fluently, earn wages from trade, eat, dress, and worship as the Portuguese, maintain a standard of living and customs similar to the European way of life, and have no record with the police” (Bender, 1978, p.150).

the Angolan population of mixed-race and blacks, who had acquired assimilated status mainly from education provided by missionary churches (Messiant, 1992, p.17).

The official, legal division within Angola's colonial society was not strictly racial as much as it was socio-cultural (Messiant, 1992). Yet, by the 1950s, less than 1% of Africans had achieved the status of "civilized" (Bender, 1978, p.28).²² Those Angolans who had reached assimilated status faced constant obstacles to their aspirations under the Portuguese regime, although they fared much better than the majority of Angolans who did not enjoy the same legal standing or privileges. In the 1950s, the economic and social injustice of the colonial system encouraged the group of assimilated Angolans to object to the colonial regime (Marcum, 1969).

The future leaders of the MPLA started organizing in the late 1940s and 1950s in Lisbon, where a number of mixed-race and assimilated Angolans obtained their university degrees (Marcum, 1969). Due to the political climate in Portugal and Angola at the time, many early members of the movement were imprisoned, pushed underground or into exile (Guimarães, 2001). During the colonial war of the 1960s, a divide therefore came to exist between the intellectual and assimilated leadership of the MPLA, of which many remained in exile during large parts of the colonial war, and the party's "fighting social basis", consisting of rural black with little formal education who had joined the movement and were now running the liberation struggle on the ground (Schubert, 2017, p.87; Mabeko-Tali, 2001b). Some tension between the exiled leaders and the social basis of the party was

²² The socio-economic situation for some Africans in the Portuguese colonies improved (albeit from a very low base) in the late 1950s as a result of new colonial policies that were officially adopted in response to international criticism of as well as growing domestic opposition in the colonies (Marcum, 1969). According to Vidal (2002, p.136), "Primary education grew 400% from 1960/61 to 1972/1973. Secondary education grew 500% within the same period and superior education was open in Angola in 1963 with the foundation of the Luanda University."

resolved in 1964, when the black Agostinho Neto was appointed leader of the MPLA, replacing the mix-raced Angolan and co-founder of the movement, Viriato da Cruz. Yet the issue of whether the predominantly mixed-race and assimilated leadership could credibly represent the Angolan population remained open (Mabeko-Tali, 2001; Birmingham, 2002, p.149-150). The tensions came to the fore in the 1977 attempted coup led by Nito Alves, a black military leader,²³ against the leadership of President Neto.²⁴ After the coup attempt and the violent state repression, issues of race and class identity became taboo (Pawson, 2014; Shubert, 2017) but endure under the surface till the present day. When José Eduardo dos Santos, another black Angolan with overseas education, took over the presidency when Neto passed away in 1979, the visibility of the whites and mixed-race in the state apparatus was lowered, but their political influence remained (Soares de Oliveira, 2015, p. 41).

3.1 Party and state organisations: From people's power to presidential power

Vary of the privileged status of the movement leaders, in the lead up to to independence, the MPLA sought to brand itself as a national party crossing boundaries of class and race. Political campaigning was effective in gaining the support of the Kimbundu people and others residing in the urban and peri-urban areas, although the MPLA was less successful in the countryside (Heywood, 2001). In the city, the MPLA effectively co-opted urban grassroots organizations that had emerged during the struggle for liberation, known as *poder popular* (people's power) (Croese, 2014; Mabeko-Tali, 2001b).²⁵

²³ As Schubert (2017, p.89) notes, many Angolans do not believe in this racial interpretation of the 1977 attempted coup, as it contradicts the conventional telling of Angola's post-independence history as a post racial one.

²⁴ The brutal oppression initiated by the government of the coup makers and their alleged supporters after 27 May 1977 is the subject of Pawson (2014).

²⁵ People's power not only contributed to building the party's urban base. With the arming of people's power militias in the months leading up to the civil war, people's power served to enhance the party's military supremacy and helped counter increasing attacks by the FNLA on MPLA positions in Luanda (Heimer, 1979; Mabeko-Tali, 2001b).

It did not take long before the more open debate driven by “people’s power” was stifled in favour of “establishing a more unitary ideological driving force” in the MPLA (Birmingham, 1978, p.555). This streamlining of the party line accelerated markedly after the attempted coup of 1977 when efforts to eliminate rival internal factions intensified (Pawson, 2014). The party rectification that followed saw party membership drop from 110,000 in 1977 to 31,000 members in 1980 (in a population of an estimated 8 million) (MPLA, 1982; Vidal, 2002). As membership criteria tightened, the party base became skewed towards the educated urban populace at the cost of the majority rural and illiterate people (Vidal, 2002).²⁶

During this time, the relationship between the party and population became more ordered through the establishment of mass organizations (Hatzky, 2015; Pearce, 2015).²⁷ The emergence of mass organizations did not signify popular participation, however. Before long, institutions that had been established to ensure the participation of the organized masses were side-lined in favour of institutions that safeguarded legislative control in the hands of the upper echelons of the party (Vidal, 2002). In the place of People’s Assemblies serving as the supreme legislative organ, a Revolutionary Council, constituted of “members of the MPLA political bureau, the military chief of staff, cabinet ministers designated by the MPLA party, [and] provincial governors”, performed both executive and legislative

²⁶ As described by Vidal (2002, p.180) “members of the new party would need a minimum of education and preparation to study and defend socialist principles, especially during the interview set to approve or reject the candidate.”

²⁷ These mass organizations were reorganized after the coup attempt of 1977 (Vidal, 2002). New leaders, especially of the MPLA youth organization, were carefully groomed by President Neto through studies and training abroad. “They became politically well behaved young members of the party, loyal to any given protector expecting benefits and retributions in exchange for loyalty and political correctness” (Vidal, 2002, p.170). Some of the leaders of the youth organisations were later recruited by president dos Santos and became part of the President of the Republic’s Cabinet (Vidal, 2002).

functions until 1980 (Faria, 2013, p.150; Collelo, 1991). When People's Assemblies were introduced in 1980, the President and the Council of Ministers were simultaneously given new powers to control and revoke all executive or legislative acts of these new organizations be it at central or local level (Vidal, 2002).²⁸

In the course of the war, the concentration of control in the upper echelons of the party was justified by the almost constant threat posed to the regime's grip on power by UNITA (Vidal, 2007). As has been the case in other countries, the threat from a common enemy is likely to have increased MPLA members support for "heightened state power and tightened authoritarian controls" (Slater, 2010, p.5). Central in this regard was the power over the state's foreign economic affairs and over the war effort, both of which had previously been under party control but in the early 1980s came under the direct control of the president (Vidal, 2007; Hodges, 2001). In line with a new Presidential Decree (Decree 25-A/80), the President and the presidential administration²⁹ were now officially permitted to engage in undisclosed, direct negotiations with private and public entities abroad (Vidal, 2002). Adding to the process of administrative centralization and concentration of power in the presidency, in 1982 a unanimous vote of the Central Committee granted the President sweeping emergency powers in view of the grave military situation facing the country (Vidal, 2002). The following year saw the establishment of regional military councils (Law no. 5/83) as an "exceptional and temporary measure" to coordinate political, military, economic and social leadership in areas "affected by armed acts of aggression, vandalism

²⁸ The appointments of People's Assemblies was done directly from Luanda, allegedly due to the war and the difficulties of compiling electoral rolls (Bhagavan, 1986).

²⁹ "A new subsidiary organization - the President of the Republic's Cabinet [Gabinete do Presidente da República] - was created on 1 April 1980, directly dependent on the President, and that was to support him in the exercise of his functions as Head of State" (Vidal, 2002, p.285) The President's Cabinet had their own secretaries in line with their different areas of activity: socio-economic, juridical, defence and security, information, foreign affairs. The President's Cabinet is not to be confused with the Party's top organs, mainly the Central Committee.

and banditry" (Collelo, 1991, p.213). The councils took over state affairs in all parts of the country affected by the activities of armed opposition groups, consequently effectively side-lining formal party and state institutions, including the judiciary (Amnesty International, 1984; Vidal, 2007).³⁰ Eleven of Angola's eighteen provinces were immediately subject to regional military councils headed by senior military officers who reported directly to the Commander-in-Chief of the Armed Forces, i.e. the President (Collelo, 1991). The presence of regional military councils lasted until 1988 when they were replaced by provincial defence councils (Law 6/88) which continued the process of reorganizing territorial administration into military regions.

The transfer of power from the party organs to the executive, which started with Neto,³¹ accelerated under dos Santos. President dos Santos and his closest allies, including many without a formal role and excluding some who did hold senior positions, have until recently often been referred to as the "Futungo" after the Futungo de Belas, the Presidential complex in the outskirts of Luanda from which the President and other senior figures came to run the state administration for much of the war (Sogge, 2006; Soares de Oliveira, 2015). The centralization of power in the Presidency transpired at the expense of party organizations and the state administration more broadly, with the latter organs possessing little real decision-making power (Soares de Oliveira, 2015). Institutional power and resources came to depend on the connection that leading individuals of party organs and state institutions enjoyed with the President rather than on any formal accountability structure, a feature of

³⁰ In the areas where Regional Military Councils came to rule, "military courts were given jurisdiction over a wide range of political and "economic" offences and empowered to try cases involving civilians as well as military personnel" (Amnesty International, 1984, p.8).

³¹ Already in 1976, President Neto had started to absorb into the presidency the powers of the prime minister. The following year, he assumed the role of head of government before he abolished the post of prime minister in 1978 (Vidal, 2002, p.128).

Angolan politics that endures to this day.³² In an interview with a senior civil society leader, he described the organisation of Angola's elite in terms of several circles surrounding the president. The inner circle is the president's immediate family and the circle after that are those who invest capital on behalf of the president. Following that, at a wider radius, are several circles of politicians, military and police officials, bureaucrats, appointees, and others who depend on the president directly or indirectly for their positions, and access to state resources.³³ One important upshot of this personalization of power, which characterises the entire period studied in this thesis, is that the standing of different institutions has constantly been in a state of flux, ultimately resting on the discretion of the supreme authority, the president. Economic policy making in the post-independence period is an clear example of how responsibilities have been constantly shifted between state institutions, mainly the BNA, the Ministry of Finance and Planning (Hodges, 2001). This divide-and-rule strategy, employed by the Angolan presidency, ensured that no single institution grew too influential, yet it also fostered a large degree of uncertainty, undermining coherent policymaking (Shaxson, 2009).

4. The party state as a tool for mobilization and distribution

The side-lining of party institutions in the course of the 1980s did not mean that the MPLA as a party became irrelevant, however. The party structure remained an important vehicle for legitimating the regime of President dos Santos (Soares de Oliveira, 2015). The party furthermore aided in mobilizing support, as would be later apparent in the country's first

³² Interview, professor public university, Luanda 22.10.2015. Shaxson (2009) uses the analogy of a queue to explain the access to power and wealth in rentier economies. "Politicians in a rentier economy are first in line, followed perhaps by lobbyists, bankers, contractors, and a long line of others – while ordinary citizens stand right at the back, with few chances of breaking into the front" (Shaxson 2009, p. 84),

³³ Interview, civil society leader, Luanda 6.11.2015.

multiparty election in 1992 when dos Santos and the MPLA faced the polls for the first time. At that time, a rehabilitation of the party machine and a large distribution of material benefits contributed to the party membership growing from about 65.000 in 1990 to over 500.000 in 1992 (Vidal, 2007, p.139). Prominent MPLA figures, celebrated for their role in the liberation struggles, including Lopo de Nascimento and Lúcio Lara, were brought forward to heighten the MPLA's claims to legitimacy during the electoral campaign (Vidal, 2007).

The party structure was also highly relevant to people living under MPLA control because of the former's control over access to resources. The MPLA monopolized all aspects of the post-independence state apparatus, from the ministerial to the provincial level. The armed forces and the secret police also became part of the party organisation, thereby blurring the distinction between the party and the state further (Pearce, 2015).

After independence, the public sector experienced significant expansion (Roque et al., 1991), growing "not only in terms of an increased number of businesses and economic activities, such as commercial farms and various industries, but most of all in terms of administrative bureaucracy" (Vidal, 2002, p.199). As argued by Vidal (2002, p.199), this expansion of the public sector "partly satisfied the aspirations of the urban masses in obtaining work for the State, jobs they had long hankered for and which had been the most highly prized during colonization." Associating with the party soon became the way that the urban population sought to safeguard their access to basic social services, including education and health care (Bhagavan, 1986).³⁴ Party allegiance also became an access point

³⁴ Although as the country spiralled into civil war, investments in social development virtually came to a halt while military spending went up, amounting to up to half the national budget each year throughout the 1980s or in 1990 about four times the expenditures on health and education combined (Sogge, 1992: 117-118; Pereira, 1994: 10).

for state distribution of positions and (consumer) privileges. Favoured members of the party were positioned to run the state bureaucracy, media and state-owned enterprises, forming what Pearce termed an “administrative bourgeoisie” (2015, p.74).³⁵ Still, whilst the wide-ranging provision of jobs and distribution of basic social services was the policy of the newly socialist state, the economic realities of the time meant that this remained an ideal rather than the practice (Gonçalves, 2010). Those, on the other hand, who were not MPLA members or lacked family connections, were habitually excluded from state employment and forced to turn to the informal market (Birmingham, 2002:2015, Vidal, 2002, p.199).

In Angola’s early post-independence years, a distributive relationship therefore developed between the upper and the lower layers of society; between workers (workers in the declining manufacturing industry, state agriculture and public administration) and the state, as the main employer (Vidal, 2002, p.210). Given the economic uncertainties of the time, including a rapid deterioration of the non-oil economy and fast accruing military expenditure, both placing a huge financial strain on the state, the distributive relationships as described in this section were constantly under strain (Gonçalves, 2010). The lower social strata were thus encouraged to seek out opportunities in the informal sector. The ruling elite, eyeing the opportunities that the informal market generated, followed.

4.1 The rise of the informal economy

The informal sector became a staple feature of Angolan urban life shortly after independence,³⁶ a role that it has continued to play in the life of many Angolans to this day.

³⁵ These tendencies, visible throughout post-independence Angola, persisted after 2002. Aligning with the regime continued to open doors and business opportunities (Schubert, 2017).

³⁶ Contraband operations of petty merchants and a black market for foreign currency existed pre-independence (Dos Santos 1990:162). See also Gonçalves (2010).

The breakdown of the colonial economy and the MPLA's post-independence economic policies contributed to the enlargement of informal trading (Bhagavan, 1986; Waldorff, 2014).³⁷ Central reasons as to why demand vastly outstripped supply in the country were the insufficient domestic production caused by the state's failure to revitalize the agricultural sector after independence, small-scale agriculturalists' refusal to sell their surplus crops for a valueless national currency,³⁸ and the government's difficulties in distributing goods while fighting a civil war. Efforts to meet demand through imports was only partly successful, owing in part to the loss of much of these goods due to a lack of know-how, inefficiencies, and theft in the trade system (Gonçalves, 2011). The severe shortages in food and essential basic staples resulted in a premium on these goods as was evident in the huge price discrepancy between the formal markets, which were subject to price controls, and the informal market, where prices moved according to market forces.

The discrepancies between the formal and informal market provided ample opportunities for arbitrage to those able to access goods at the official price.³⁹ In the new socialist economic system these were the people with connections to the state and party. State employees had access to heavily subsidized goods at people's stores (*lojas do povo*), in accordance with their position within the socio-political hierarchy of the state and party (Vidal, 2002).⁴⁰ Goods purchased at the people's stores could be resold or exchanged for

³⁷ Ferreira (1999) provides an apt explanation of how inappropriate and failed MPLA economic policies help explain the country's poor economic performance, which in turn established the foundation of the informal market.

³⁸ The national currency, the Kwana, was first issued in 1976, at parity with the Portuguese Escudo and maintaining the same exchange rate in relation to the US dollar (just under 30 Escudos to U\$1.00) (Gonçalves, 2010).

³⁹ It was also common practice for factory workers to appropriate part of the output that they produced to sell it on the informal market (Vidal, 2002). This practice became so widespread throughout all of the state's production units that the MPLA Central Committee in 1980 saw it necessary to officially condemn such practices (MPLA, 1982).

⁴⁰ Prices for basic commodities were the same in all shops, what distinguished the shops was the type, quantity and quality of the products available (Bhagavan, 1986).

merchandise on the informal market where prices were from 30 to 100 times higher (Bhagavan, 1986, p.22).

By the mid-1980s, the national currency, the Kwanza, had lost all its value and become, as Bhagavan (1986, p.22) puts it, “mythical.”⁴¹ The Kwanza had no nominal value outside the state-run stores and even in these stores, the Kwanza was at times replaced by coupons as the medium of exchange (Birmingham, 2002:158). On the informal market, bartering became the preferred practise. At one point a six pack of beer became the pseudo currency and a physical measure of exchange and value (Birmingham, 2002; Waldorff, 2014). That Angolans had lost faith in the national currency was also evident in the high level of dollarization, which became increasingly prominent from the late 1980s. The tendency to resort to the US dollars in everyday transactions is a practice that is still alive in Angola today,⁴² speaking to the public’s general mistrust of the local currency if not the economy in general.⁴³

For many people, as emphasized by Vidal (2002) and Waldorff (2014), informal trading activities became a main source of livelihood when surviving on official salaries and privileges proved unmanageable.⁴⁴ The increasingly common practice of straddling

⁴¹ By the time the currency was devalued in early 1991, the difference between the official exchange rate and the exchange rate on the informal market had reached more than 9000 % (IMF, 1995).

⁴² Throughout the 1990s to 2000s, Angola was amongst the most dollarized economies in the world as measured in terms of domestic bank deposits (which remains a common way to measure dollarization in the comparative literature) (Yeyati, 2005; See also Reinhart et al., 2014). The IMF (2003) estimated that 80% of demand deposits were dollar-denominated and that this number had been higher in proceeding years when inflation was higher.

⁴³ As Nicolo et al. (2003) show, credibility of macroeconomic policies is a key determinant of dollarization.

⁴⁴ People had to build their own *esquemas*, translated as schemes (Dos Santos, 1990, p.161). As Waldorff (2014, p.135) explains, “in the 1980s, official State employers were notorious for not paying salaries on time, or even paying salaries at all.” Additionally, even though low income state employees were ensured access to goods in the people’s stores, these shops frequently experienced shortages forcing state employees to resort to the informal market to access consumer goods that were not available on the official market (Waldorff, 2014). In 1990, Dos Santos wrote that “unofficial activities are so important that the population devotes at least one third of its productive time to them on an everyday basis” (1990:162; the same argument has been put forth by Tvedten 1997:78).

informal and formal markets resulted in a vicious cycle where “the more the parallel economy grew through predatory practices, the more the official economy weakened and the more the purchasing power of official salaries eroded due to the hidden inflation of the black market; leading to a renewed need to join the parallel economy in search for an extra income” (Vidal, 2002, p.214). Yet this vicious cycle also benefited a minority for whom straddling the formal and informal markets became a means of self-enrichment (Morice, 1985). People at the top of the party state hierarchy had access to more and better products through the people’s stores, impacting the amount of profit that they could make through reselling these goods on the informal market (Birmingham, 1988). Members of the ruling elite were also more likely to benefit from favoured access to scarcer commodities, ranging from highly prized items such as apartments and cars to more mundane objects including generators, motorbikes and refrigerators (Vidal, 2002). Like ordinary consumer goods many of these scarcer goods also ended up being resold on the informal market for a considerable mark-up. A final privilege that differentiated elite members from the lower social strata was their access to foreign currency at the official rate (Dos Santos, 1990; Hodges, 2001). At the official market, the parity between the kwanza and the US dollar was fixed at 30 to 1 from 1977 until 1991. On the informal market, however, a US dollar on the black market sold for between 1500 to 2000 kwanza (Dos Santos, 1990, p.170). For those with access to foreign exchange, round tripping was extremely lucrative. Currency arrangements such as these continued to be principal mechanisms for private enrichment by the political elite in the 1990s (Hodges 2004).⁴⁵

⁴⁵ It is important to keep in mind that the privatization of wealth, although it started during the 1980s, was still quite modest during this time. As noted by Bhagavan (1986, p.44), “They [Angolan elites] are “privileged” only in comparison with the masses in Angola. But in comparison with the elite of the other African countries, they are nowhere - their privileges seem to shrink into nothing. This should be borne in mind to keep a proper perspective.”

Insofar as the party state dictated the division of society according to rank, which in turned dictated access to the main supply channels (privileges and benefits), the party also exerted control over the informal sector and the extent to which individuals benefited from straddling the informal and formal market. Accordingly, as Vidal (2002, p.219) argues, the “informal sector became an integral part of the centralized system of Party control and domination over the whole emerging framework of economic relationships. “Informal activities could not provide significant economic power independently from the party,” as people relied on their party connections for access to goods that could be resold (Vidal, 2002, p.219). By virtue of its control over the main revenue generating body in the economy, the oil sector, the state also controlled the means by which goods (legal or illegal) could be imported and the degree to which the informal market should be stimulated.

5. The rise of efficient parallel structures

The picture that has been painted thus far highlights the short-sightedness that characterized the policy making of the MPLA in the post-independence years. Yet in areas of structural importance to the state – resource extraction and defence – the emergence of a longer-term strategy was evident. In the oil and defence sector, the building of state capacity and capable institutions were prioritized, aided by a significant degree of foreign know-how (Soares de Oliveira, 2015; 2007). In the literature, such arrangements is often referred to as “pockets of effectiveness”, defined as “public organisations which provide public services relatively effectively in a context of largely ineffective governance” (Roll, 2011, p.1).⁴⁶ In Angola’s case, the structures that developed in the extraction and defence sectors, what Soares de Oliveira (2015, p.40-46) terms Angola’s “parallel system”, have remained pivotal to the

⁴⁶ I.e. effective bureaucratic organizations. For further discussion of the concept see Leonard (2010, p. 92).

rule of President dos Santos from its creation in the seventies up until today. The parallel system supported the running of the informal sector as much as it supported the official sector (Vidal, 2002).⁴⁷ It was the parallel system that eventually aided the ruling coalition to tilt the power balance in favour of the MPLA and away from the UNITA in 2002 (Soares de Oliveira, 2015).

The main organization in Angola's parallel system is the national oil company, Sonangol. Founded in 1976 as the exclusive concessionaire for oil exploration and development, Sonangol, short for Sociedade Nacional de Combustíveis de Angola, was the upshot of the MPLA leadership's pragmatic decision to protect the country's oil sector from the transformation and chaos that afflicted the rest of the Angolan economy upon independence (Soares de Oliveira, 2007). By the time Sonangol was established, oil had already been produced in the country for two decades, acquiring a growing importance in the economy from the 1960s onwards (Graph 3.1).

In the colonial period, the country's oil production was dominated by the Cabinda Gulf Oil Company, a subsidiary of American Gulf Oil,⁴⁸ with other western oil companies including Texaco and Petrofina operating smaller fields (Le Billion, 2001). Oil was produced in the geographically sheltered areas off Angola's coast in relatively shallow waters, making it easy for the operators to reach.⁴⁹ The fact that the oil sector was physically insulated is significant as it meant that oil could be extracted largely uninterrupted for the majority of the civil war (Chabal, 2007).⁵⁰

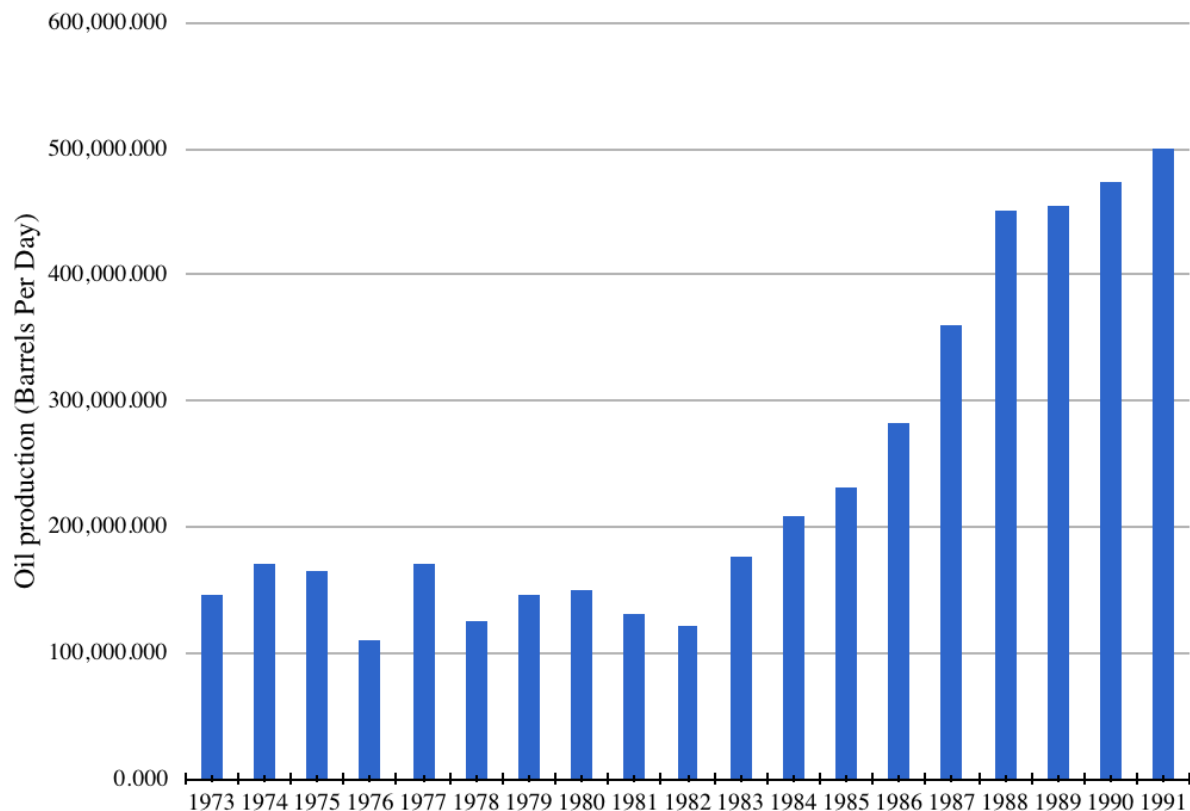
⁴⁷ The bulk of products feeding and stimulating the informal market were paid with US dollars (Gonçalves, 2010).

⁴⁸ Gulf Oil ceased to exist as an independent company in 1985 when it merged with Standard Oil of California. After the merger, the new company re-branded as Chevron.

⁴⁹ Exploration further offshore mainly took place from the mid-1990s (Heller, 2012).

⁵⁰ Only once, in 1993, did UNITA manage to occupy and destroy oil facilities (Heller, 2012).

Graph. 3.1: Angola crude oil production, 1973-1991



Source: U.S. Energy Information Administration (2015); Directorate of Intelligence (1987).

When independence came in 1975 political uncertainty led the foreign companies to flee the country. Yet it did not take long before the MPLA under the leadership of President Neto — who appreciated the importance of the oil sector to the survival of the state — managed to convince foreign companies to return (Soares de Oliveira, 2007, p.599). An important reason why Angolan political leaders were able to persuade foreign oil companies to re-invest in the country in the midst of civil war, was the establishment of Sonangol. From the very beginning, Sonangol was unique. As one former manager in the company recalled, “Sonangol was always different from other state institutions. The financial and human resources it had at its disposal, gave the company an edge.”⁵¹ As the

⁵¹ Interview, manager oil service company, Luanda 3.11.2015.

rest of the Angolan economy was subject to socialist planning, Sonangol was encouraged to accumulate technical expertise and know-how in close partnership with western oil companies and consulting firms (Soares de Oliveira, 2007). This allowed the company to nurture a dynamic and steadfast oil sector that would be able to operate at a high level of productivity (Heller, 2012). The technocratic nature of Sonangol provided assurance to the foreign oil companies who trusted the enterprise to maintain a business-friendly attitude (Soares de Oliveira, 2007).

The technocratic expertise of the organization also meant that Sonangol enjoyed strong political support from the MPLA leadership (Soares de Oliveira, 2007). Still, Sonangol's role was never just technocratic.⁵² The company always had a political edge owing to the centrality of the oil sector in the country coupled with the enterprise's superior capacity to meet its mandate "despite operating in an environment in which public service delivery is the exception rather than the norm" (Roll, 2011, p. 2). In addition to leading tough negotiations with foreign oil companies — so as to maximize the share of petroleum revenues accruing to the state — Sonangol was also called on to perform a variety of functions on behalf of the state beyond what is normally expected from an oil company (Heller, 2012). From the mid-1980s onwards, amongst the most important functions performed by Sonangol in *addition* to managing the oil industry, was as intermediary of oil-backed loans.⁵³ "Sonangol negotiated the loans (primarily with international banks), which were channelled to government accounts in Angola and abroad. Angola's oil deposits served as collateral, and Sonangol repaid the loans with the delivery of oil shipments to international trading companies that channelled the proceeds into offshore

⁵² As Soares de Oliveira (2007, p.601) notes "Key figures in Sonangol's core team were well-networked MPLA party members who enjoyed the confidence of President Neto."

⁵³ A 1987 report from the CIA's Directorate of Intelligence provides an interesting overview of the Angola's oil-backed loans.

accounts – a routing designed to bolster the confidence of the state’s creditors” (Heller, 2012, p.866). Sonangol’s solid international reputation allowed it to access commercial credit on behalf of the state, thus providing the state with much needed revenue to fund the war effort and other running expenses.⁵⁴ Sonangol’s ability to mortgage on behalf of the state became increasingly important from the late 1980s, when global oil prices collapsed and the MPLA state apparatus found itself under financial strain, unable to access credit on the international market directly.⁵⁵

Currency deriving from Sonangol and the oil sector provided the MPLA government with the hard cash with which to fund its war efforts against UNITA (see Le Billion, 2001). This leads us to the second pillar of the MPLA regime which was its “militarily effective and politically compliant” army (Chabal, 2007, p.12).⁵⁶ The formation of the People's Armed Forces for the Liberation of Angola (Forças Armadas Populares de Libertação de Angola—FAPLA) was announced in 1974, transforming the MPLA’s army from “lightly armed guerrilla units into a national army capable of sustained field operations” (Collelo, 1991, p. 210). The Soviet-Cuban intervention of 1975 and subsequent UNITA insurgency further contributed to the transformation of FAPLA. The “sudden and large-scale inflow of heavy weapons and accompanying technicians and advisers”, introduced by the foreign patrons, were instrumental in building up a disciplined army and security apparatus in the country (Collelo, 1991, p. 211). The defence force furthermore allowed the MPLA to retain control over the urban areas in the 1980s (Chabal, 2007). In the course of the 1980s, the FAPLA

⁵⁴ Interview, senior civil servant Ministry of Finance, Luanda 30.9.2015.

⁵⁵ The financial hardship that the Angolan state found itself in by the late 1980s will be discussed in chapter 4.

⁵⁶ It is important to point out that throughout the war up until present day, considerable variation exist within the armed forces both when it comes to effectiveness and access to resources. Certain units of the armed forces were of lesser strategic importance and consequently received lesser resources. Then there was the centrally important “operational structure” of the armed forces, “studded with mercenaries, foreign consultants, and state-of-the-art equipment” (Soares de Oliveira, 2015, p. 45-46). This latter part of the army was “well fed and resourced”(Soares de Oliveira, 2015, p.226).

continued to grow, incorporating a regular army and a supporting militia, navy and the largest air force in sub-Saharan Africa (Weigert, 2011; Collelo, 1991).⁵⁷ The armed forces also gained a greater political role during this time, contributing to the increasing militarization of the state, a legacy which would endure into Angola's post-war period.⁵⁸ After independence, the army became institutionalized at every level of government. The defence and security forces were heavily represented in the highest organs of the party and government, including the Revolutionary Council before 1980 and in the first national People's Assembly, which replaced the Revolutionary Council in 1980 (Collelo, 1991).⁵⁹

The expansion of the MPLA's military force came at a heavy price. Defence quickly came to consume the bulk of national wealth and revenue in Angola's post-independence period.⁶⁰ By 1986, defence accounted for over 40% of the government budget and almost 30% of GDP (Collelo, 1991, p.234). Arms imports also grew dramatically. In the 1980s, arms imports cost the state more than US\$1 billion on average annually, constituting between 45% and 88% of total imports. The high volume of arms imports made Angola the seventeenth largest arms importer in the world at the time (Collelo, 1991, p.234).⁶¹ The large-scale spending on defence was possible due to the state-controlled oil sector and assistance from the Soviet bloc. After the 1980s, when the latter subsided, the oil sector came to represent as much as 90% of government revenue in certain years, underscoring

⁵⁷ MacFarlane (1992, p.13) provides an overview of the growth of the Angolan military from 1981 to 1990.

⁵⁸ Angola's defence budget would continue to increase in peacetime. In 2013, spending on defence reached \$6 billion, making Angola the biggest military spender in sub-Saharan Africa, overtaking South Africa (The Economist, 2014). Military spending accounted for 17.6% of the country's total budget, with the Ministry of Defence being allocated the largest share of the budget of all the ministries (Marques de Morais, 2013).

⁵⁹ In the People's Assemblies, defence and security personnel constituted 10% of the membership (Collelo, 1991).

⁶⁰ "Luanda's defence spending nearly quadrupled from \$343 million in 1978 to \$1.3 billion in 1986 (in constant 1980 dollars)" (Collelo, 1991, p. 234).

⁶¹ It was little wonder then, when Angolan government officials estimated the country's external debt at the end of the 1980s, most of the \$4 billion outstanding was for military procurements (Collelo, 1991, p.234). For further comparative statistics see Collelo (1991, p. 234-235).

the crucial role of the sector in the post-independence period and how effective was the management of it (Hodges, 2004).⁶² The success of Sonangol and of the defence apparatus was feasible because these institutions were largely shielded from the “dominant (both predatory and centrally planned) logic of Angola’s political economy” (Soares de Oliveira, 2007, p.595). The creation and running of the parallel system was in turn possible because of the gradual concentration of power in the upper echelons of the party, where the army and oil company exerted a strong influence.

The delegation of sweeping powers to the executive from the early 1980s onwards, as discussed above, was central in this regard (Vidal, 2002). Like senior military officers, the managers of Sonangol reported directly to the President (Heller, 2012; Soares de Oliveira, 2015). These direct lines of command between the institutions and the President’s inner circle, granted the ruling elite considerable policy autonomy when it came to the supervision of these key sectors, at the expense of the party-state’s formal accountability structures. This special rapport gained an added dimension when from the mid-1980s, Sonangol became gradually more important for accessing external credit, “creating a system of parallel finances not subject to public scrutiny or even the purview of senior officials in the Ministry of Finance: (Hodges, 2001, p.140). Despite their growing political weight or rather because of it, the daily management of the parallel system was largely left up to the politically dedicated leaders of Sonangol and the military establishment, a large majority of whom were from the extended kinship networks of Neto and dos Santos. Managers and senior military officers enjoyed the discretion that they needed to run the

⁶² A large part of oil income never entered the official state budget, however. According to Hodges (2004), between 1998 and 2002, on average 36% of government expenditure was off-budget.

sectors efficiently, although always at the service of the MPLA regime (Soares de Oliveira, 2007; 2015).

6. Conclusion

This chapter has sought to historically contextualize my thesis argument by offering an analysis of Angola's political economy, focusing the first years of independence. The chapter moved beyond the purely historical, however, by emphasising the political, institutional and economic features that characterise Angola to this day. Based on the analysis of this chapter I argue that three features of the country's post-independence history should be emphasized as they shed light on the underlying assumptions of this thesis which deals with state society relations and the distribution of political and economic resources.

First, the chapter shows that the implosion at independence was a mixed-blessing for Angola's political leaders. On the one hand, the breakdown of the economy following independence and the civil war that immediately followed had a profound impact on the country's political and economic institutions in the decades that followed. The conditions at independence meant that the MPLA's ability to run the economy in a sustainable way was very weak. The mounting challenge posed by UNITA furthermore meant that there was little space for political leaders to think of the long term when it came to economic policies. On the other hand, the state of emergency that consumed Angola in the years after independence meant that political and economic structures had largely to be taken over by the party state. President dos Santos moreover enjoyed significant discretion to concentrate control over politics and the economy in parallel structures, which answered only to the

Presidency. This centralization of power came at the expense of formal party state structures, which became notably side-lined during this period.

Second, the chapter underscores the complexity of Angola's state society relations. From the start, the MPLA was a narrow urban movement. The party did manage to reach a wider following, but this was due mainly to its inclusive discursive, emphasising multiracialism and universalism, rather than any broad-based results. More importantly, as the party came to monopolize all aspects of the post-colonial state, associating with the party became indispensable for accessing state distribution of goods and privileges, including employment, in the cities. Still, state distribution of goods and privileges was far from equal. In the end, individuals' proximity to the upper echelons of the MPLA movement determined their ability to access the benefits of the party state which in turn determined their power to accumulate wealth in Angola's thriving informal market.

Third, in independent Angola, oil quickly became the only revenue-generating sector of any significance. The importance of oil revenues to the MPLA regime made it vital for political leaders to shelter the sector from the general implosion of the economy after independence. One consequence of this dual economic structure was that few opportunities for the accumulation of economic resources existed outside of the oil sector. Rather, the state mediated distribution of oil revenues, through the party state apparatus, became the main way of accumulating wealth during this time. In a pattern that would last into the next decades, private wealth became not separate from the state but integrated with it.

The above-mentioned factors must be taken into account when considering the Angolan case and the rise of the country's financial sector. It is to the evolution of the financial

sector that the thesis now turns, starting with the transition from a centrally based to a market led, but nonetheless state- and party-controlled, economy in the early 1990s when Angola's emerging financial sector came to play a critical role as an enabler of political continuity.

Chapter 4

Financial sector continuity in Angola's transition from socialism to capitalism

1. Introduction

The previous chapter analyzed Angola's political economy during the immediate post-independence period. It argued that understanding this period in Angola's history is pivotal, as it was during these decades that the foundations for the distribution of political and economic power were laid. In this chapter I will examine the first major change in the country's financial sector institutions since the establishment of the socialist system in the mid-1970s: the transition from a centrally based to a market led economy in the early 1990s. Understanding the process of change at this important moment will form my first contribution towards answering the central question of this thesis, namely why do authoritarian resource-rich countries choose to introduce institutional change in the financial sector? I argue that in the case of the early 1990s' reforms, a transformed international political climate meant that the institutional structure characteristic of Angola's centrally planned economic system was reaching a breaking point. In order to stave off a potential breakdown and enhance economic performance, it was necessary for political leaders to respond to external calls to liberalize the country's economy, including financial sector institutions.

Yet what the chapter also shows is that the advancement of the financial sector in the early 1990s – by means of financial liberalization – allowed President dos Santos and his

associates to restructure economic institutions without risking political discontinuity. Comparable to what happened in other transitional economies, the establishment of a state-controlled commercial banking system in Angola (following the transition to capitalism) allowed political leaders to continue subsidising the economy by means of soft credit and foreign currency, thus ensuring the loyalty of politically important constituencies.¹ The redistributive function that financial sectors can serve is something that existing studies which focus on the role of banks as financiers of the state, raisers of money and mobilizers of savings, have frequently overlooked. Taking into account the financial sector's redistributive function also help us explain a related empirical question, which is why Angola's financial sector never became subject to privatization.

The chapter starts by describing the take-over of the Angolan economy by the MPLA controlled state following the country's independence in 1975. The current chapter overlaps with the previous chapter to some extent in terms of time period, yet the focus and aim of the two chapters differs. Whereas the previous chapter focused on the broader political economy dynamics in post-independent Angola, in order to clarify how political leaders related to society and to the economy, this chapter centres more explicitly on economic and financial sector policies, the dominance of the state in the economy after independence and particularly the pervasiveness of state-owned enterprises (SOEs). The aim of the historical backdrop in this chapter is to underscore the incentives faced by political leaders to safeguard the existing system as it helped ensure the survival of the MPLA. Moreover, whilst the previous chapter did not explore the issue of sustainability when it came to Angola's post-independence economic system, the poor-performance of Angola's socialist

¹ See Bonin, et al. (1998) on Eastern Europe, Kovested et al. (2005) on Vietnam. Similar use of selective credit allocation is described by Hutchcroft (1998) in the case of Philippines after 1950.

economic system is a central issue in this chapter. The current chapter describes how an increasingly difficult economic situation by the late 1980s compelled the government to commit to a general liberalization of economic policies. This process was far from straightforward and reforms were in principle at odds with the interventionist policies that the government had pursued in the post-colonial period. Finally, in the last section of this chapter, I show how the creation of a state-controlled commercial banking sector aided the continuing domination of the state in the economy, importantly through the extension of SOE funding. This allowed the state to continue underwriting the SOEs well into the 1990s, even when this came at a high cost for the country's embryonic banks.

2. The state take-over of the economy

When the Portuguese fled Angola in 1975, the country's nascent economic achievements were undermined by an acute lack of trained personnel prepared to take over the administrative and economic structures that European settlers left behind (Ferreira, 2002a; Carvalho, 2012).² As the last chapter described, prior to independence, the African population had largely been excluded from modern sectors of the economy.³ Together with the onset of war, the shortage of manpower contributed to Angola's economic collapse. By 1977, Angola's GDP had fallen by 43% from its 1973 levels (Le Billon, 2001). The economy was in a state of crisis and the policy space of the country's new leaders, the Soviet-supported MPLA, was limited. It was the MPLA who, according to the country's new constitution of 1975, was in charge of the "political, economic and social leadership

² As noted by Birmingham (1988, p.3) "The private sector in Angola had been dominated by white migrants from Portugal until 90% of them fled in the panic of 1975." The exodus of Portuguese settlers has vividly been portrayed by Polish writer Ryszard Kapuściński in his 1976 non-fiction book "Another Day of Life". The book depicts the journalist's stay in Angola at the outbreak of the civil war in 1975.

³ A partial exception was the small group of mixed and 'assimilated' Angolans who, due to their social status, did enjoy a more privileged lifestyle, including greater access to formal employment (Soares de Oliveira, 2015).

of the nation” (Law no. 1/75, article 2). One of the party’s first moves in power was to take control over strategic sectors in a bid to salvage the country’s production and employment levels (MPLA, 1979). This dramatically expanded state control over the economy.

Economic nationalization in Angola should not be understood simply as a solution of last resort in response to the wide-spread abandonment of property following the country’s independence. Economic nationalization was gaining traction within the developing world and beyond, including in Portugal following the Carnation Revolution of 1974 (Birmingham, 1993; Pitcher, 2002). Across Africa, countries of different ideological convictions and types of regimes had been nationalizing their economies since the 1960s, habitually through the nationalization of foreign owned productive assets (Diamond, 1987). In socialist Tanzania, 80% of the medium and large enterprises were parastatals by the early 1980s (Young, 1994).⁴ Likewise, economic nationalization became a major theme in Mobutu’s Zaire with most of the economy vested in SOEs, notwithstanding the regime being a strong ally of the capitalist West. Even in Nigeria, where Diamond (1987) argued the indigenous private enterprise was more developed than in the rest of Africa, considerable expansion of the economic role of the state took place. In Nigeria, “statutory corporations at both the federal and state level came to figure in or dominate not only petroleum, but almost every aspect of production and distribution: mining, steel, agriculture, printing, banking, insurance, shipping, supplying, hotels, electricity, construction, telecommunications, radio and television” (Diamond, 1987, p.573; Joseph, 1983). For many of Africa’s political parties post-independence, including the MPLA, making “the nation-state a meaningful part of people’s lives” was central to their vision of development (Cooper, 2002, p.67). In Angola, the state dominated economy came to be

⁴ See also Gray (2018).

seen as “an instrument of the working class and its allies, the main factor in the development and fair distribution of wealth” (MPLA, 1977). Yet, in moving towards a socialist economy, African states were at the same time fundamentally altering the “distribution of economic power away from pre-socialist economic actors through nationalization, the creation of state owned enterprises and constraints on private sector activities” (Gray, 2018). That such an economic transformation was underway in Angola soon became evident.

After independence, Angola received assistance from Soviet advisors on making the transition to a socialist economy.⁵ In line with the 1976 Law on Nationalization and Confiscation (Law no. 3/76), enterprises of strategic importance were taken over by the state as were those companies abandoned by their owners. By mid-1977, over 85 % of enterprises (agricultural, industrial, mining and trading) had come under Angola’s system of central planning (Sommerville, 1986). Nationalization also took place in the banking sector, which soon after independence became the sole domain of the MPLA state (Law no. 4/78). Between 1976 and 1978, the government nationalized Angola’s two main banks and liquidized a number of small banks (Hodges, 1993). Banco de Angola and Banco Comercial de Angola was replaced by a central bank the Banco Nacional de Angola (BNA), and a savings bank, Banco Popular de Angola (BPA). The BNA assumed the role as central bank as well as the country’s only commercial bank while the BPA became a deposit-taking bank whose resources were all deposited in the BNA (Tjipilica and Valerio, 2015).

⁵ Interview, senior civil servant Ministry of Finance, Luanda 30.9.2015.

As in other socialist financial systems⁶ and in many African countries (Van de Walle, 2001, p.140), formal financial policies of directing and subsidizing credit were widespread in Angola. The Angolan Ministry of Planning made decisions regarding the volume and allocation of credit (World Bank, 1992). Predominantly, credit was channelled by the BNA to the Government — through money creation — in order for the latter to finance budget deficits (World Bank, 1991). Deficit financing was a main source of inflationary pressure in the 1980s⁷ and it was also a main trigger of the hyperinflation Angola experienced between 1993 and 1996.⁸ During the socialist years, credit from the BNA to the government was of unlimited duration and was generally never repaid, making the World Bank (1992, p.5) at the time remark that “most lending of the banking system should be viewed as intra-government account transfers.”

Throughout the socialist period, the MPLA government maintained an apprehensive position on the role of the private sector (Ferreira, 1999). According to official rhetoric, the subsistence of the private sector was contingent on its total devotion to the socialist cause (Neto, 1976). In reality, however, the government was willing to condone establishments of non-Portuguese foreign companies who, if willing to work on the government’s terms, would not be subject to expropriation. The most important of these foreign businesses were those active in Angola’s oil and gas sector, the origin of the country’s principal exports since 1973 (Soares de Oliveira, 2007). Additionally, as noted by Bhagavan (1986, p.38),

⁶ Gray (2018) demonstrates how the use of credit to prioritized sectors was central to financial policy in Tanzania and Vietnam under socialism (and in Vietnam’s case also after economic liberalization in the 1990s). State-owned, state directed credit programmes have also been an important feature of the socialist economic system of China (Kotz, 2000).

⁷ Throughout the Marxist-Leninist period, prices were fixed in the official markets and supplies limited. The growth in money stock, due to Government borrowing from BNA to finance the budget deficit, therefore fuelled inflation in the parallel market and created extremely large relative price distortions between official and parallel markets (Interview, senior civil servant Ministry of Finance, Luanda 7.10.2015).

⁸ The overall rate of inflation reached 500 per cent in 1992, 1838 per cent in 1993, 972 per cent in 1994, 3783 per cent in 1995, 1650 per cent in 1996 (Rouque, 1997).

“The nationalization measures did not touch some fifty large manufacturing enterprises, owned by non-Portuguese capital from West Germany, Britain, South Africa and Belgium. They were left in the hands of their former owners, except for the minority shares held by the departed Portuguese, which were taken over by the [Angolan] state.”

The MPLA’s ambivalent position on the foreign-owned private sector was also acknowledged by the World Bank, who stated that “The country has maintained a relatively open policy on cooperation with foreign companies, including major multinationals. The foreign investment law, passed in 1979, permits foreign equity in Angola *provided* that the country's independence and interests are respected” (World Bank, 1991, p.28. Emphasis added by me). The official goal was to make the private sector superfluous, as noted by the MPLA at its first party congress in 1977 (MPLA, 1979). This would be achieved through creating “conditions which makes it possible gradually to replace private concerns in respect of products and services regarded as strategic” (MPLA, 1979, p.32).

For the private sector companies that endured Angola’s socialist period, survival was made difficult by the state’s overbearing presence. As one informant, who was a member of the government reform team in the late 1980s, recalled, private firms were to be “frozen out” through administrative interference and lack of financing, with the ultimate objective that they would “die out”.⁹ In line with the overall party line of quelling private initiative, access to bank credit for the majority of companies was negligible throughout the late 1970s and 1980s (World Bank, 1991, p.21).¹⁰

⁹ Interview, previous member of government’s reform team (1980s), Luanda 14.10.2016.

¹⁰ Consequently, private companies, mainly engaged in the manufacturing industry, agriculture and transportation, remained significantly smaller than their public counterparts throughout the socialist period (World Bank, 1991, p.23).

In this section I have shown how the Portuguese left in Angola a fast growing but feeble economy. When Portuguese settlers fled in 1975, nationalization was viewed as the necessary response by the MPLA government to preserve the economy. Yet, this section also showed how nationalization aligned with the ideological conviction of the government at the time and was being pursued by countries broadly across the continent and beyond. The result was a large-scale nationalization of the Angolan economy following independence in which the private sector came to play a negligible role.

3. The role of the state in the economy

By the early 1980s the state dominated Angola's formal economy. At the height of central planning in 1984, the economy comprised approximately 600 enterprises of which approximately 400 were public (World Bank, 1991). While taking into account the fact that total domestic production was by the mid-1980s significantly reduced from its pre-independence levels, SOEs still accounted for over two thirds of national output and dominated all significant economic activity in the modern sector of the economy (IMF, 1990). The SOEs' dominance of the Angolan economy lasted at least until the late 1990s (Rocha et al., 2016).

Angola's economy at this point was fast becoming what Gonçalves (2011, p.121, my translation) terms a "mono producer", reflecting the dominance of the oil sector in the national economy. Oil exports financed the imports needed to make up for lost domestic production in addition to provisions required for the intensifying war effort (Gonçalves, 2011). External borrowing had been modest until the early 1980s but increased significantly in and after 1986 when global oil prices started falling. By the mid-1990s, external financing had become increasingly important for meeting the state's financing

needs.¹¹ Most external loans came from other socialist countries with the Soviet Union being the largest creditor (Ministry of Finance, 1990).

By the mid-1980s, however, other countries had also joined in lending to Angola. Brazil and Portugal were two key creditors but other Paris Club members also extended loans to the country (Ministry of Finance, 1990). By 1989, according to the Angolan Ministry of Finance (1990), approximately 40% of credit originated in non-socialist countries and international organisations whereas the rest accrued from socialist countries. What characterized the loans from non-socialist countries was that many of these were backed by oil, meaning that future oil deliveries were used as collateral, what is often called oil-collateralized credits.¹² During the war, oil-collateralized credits were serviced through the direct transfers of oil money from creditors to a Sonangol bank account and repaid at a fixed barrels-per-day rate (Vines et al., 2005). These loans posed a low risk to the lender who was guaranteed repayment in oil cargos. As Angola's debt burden increased and external arrears amassed from late 1980s onwards, oil-collateralized credits became the preferred loan mechanism of commercial and bilateral lenders (Hodges, 2004).¹³

Because of the sharp fall in domestic production following the departure of European settlers and the outbreak of civil war in 1975, imports became the mainstay of Angola's postcolonial economy (World Bank, 1991).¹⁴ Import of military equipment and consumer goods was critical to the war effort as well as to meet the needs of the fast growing and

¹¹ Interview, senior civil servant Ministry of Finance, Luanda, 30.09.2015

¹² According one senior civil servant in the Ministry of Finance, who dealt with bilateral debt negotiations in the 1980s and 1990s, the practice of oil-collateralized credit started in 1986 (senior civil servant Ministry of Finance, Luanda, 30.09.2015). This was confirmed in a top secret report (now partly declassified) from the CIA's Directorate of Intelligence (1987), describing how Angola by 1987 was increasingly obtaining Western loans and export deals on the promise of future oil deliveries as collateral.

¹³ Interview, senior civil servant Ministry of Finance, Luanda, 30.09.2015

¹⁴ As Ferreira (1999) shows, the governments misguided industrial policies contributed to a de facto import promotion.

politically important urban populace (Aguilar and Zejan, 1990). With the exception of the oil and diamond sectors, which were ruled by a special regime,¹⁵ foreign trade was monopolized by the state from 1976. From that date, virtually all foreign trade was managed by the state through dedicated state-owned enterprises (MPLA, 1980). The MPLA government rightly acknowledged the power derived from policing “citizens’ access to the wealth that lay outside” (Cooper, 2002, p.160).¹⁶ The state monopoly in external and domestic trade facilitated privileged access to the enterprises fortunate enough to possess a licence, which was the case for state-owned foreign trade enterprises (Ferreira, 2006).

The state and the state-owned enterprises played another significant role in Angola’s centrally planned economy, which was that of employer. As Herbst (1990) notes, state-owned enterprises were important source of patronage for political leaders since these companies often employed large numbers of people. In the 1980s, Angolan public enterprises were on average employing 480 workers per company compared to below 49 workers for firms in the private sector (Rocha et al., 2016; World Bank, 1991), attesting to the social function of these enterprises. The general decay of the modern sectors in the economy after independence meant that formal sector employment gradually became limited to jobs in the public administration, the police and armed forces, and in state-owned enterprises (Vos, 2014).

¹⁵ Sonangol and Endiama, the national oil and diamond companies, enjoyed foreign exchange autonomy and thus were able to import equipment directly (World Bank, 1991).

¹⁶ Angola was what Cooper (2002, p.5) calls a “gatekeeper state”. The post-colonial state survived on policing the intersection between the domestic and the international market whilst having only weak instruments for penetrating the larger national territory. See also Bayart (2000).

By 1986, the majority of workers working for enterprises in the formal sector were employed by state-owned enterprises and state-owned enterprises accounted for three quarters of total formal sector employment (Hodges, 1993, p.34). Together, civil service and public enterprises accounted for 45% of total employment in Luanda, where public sector jobs were concentrated (Hodges, 1993, p.60). In comparison, public sector employment in Africa during the same period accounted on average for about 50-55% cent of all non-agricultural jobs. In Asia and Latin America, the numbers were considerably lower, 36% and 27% respectively (Young, 1994). The important role played by SOEs together with the civil services in employment provision is confirmed by the fact that even though enterprises across all sectors of the economy contracted considerably in the post-independence period,¹⁷ the state-dominated sectors of industry, commerce, transport and administration, increased their number of workers from approximately 10% of the economically active population in 1970 to 35% by 1985 (World Bank, 1991).

Looking at statistics from the mid-1980s it becomes clear that the employment opportunities mentioned here were largely confined to the part of Angola controlled by the MPLA government (World Bank, 1991). MPLA-controlled areas were the country's urban and peri-urban areas, and especially the capital of Luanda, with large swathes of the countryside unsettled or under UNITA control. Indeed, while almost half of the registered workforce in the provinces excluding Luanda was engaged in the primary sector in 1984, the corresponding number in Luanda was 5%, signifying the greater availability of formal sector jobs in the capital (World Bank, 1991). In Luanda, as noted by the World Bank (1991), the services sector was by far the largest employer, employing 61% of the

¹⁷ The oil sector being the notable exception.

workforce. For a large majority of urban Angolans,¹⁸ this signified the informal sector (Vos, 2014), but for a critical fraction of the urban population it meant employment in government administration or in the SOEs with their associated privileges and benefits. These state employees shared in the challenging living conditions that characterized Angola in the 1980s but as reasoned by Birmingham, “Their standard of living, which surely dropped in the 1980s, still remains far above that of the average Angolan urbanite” (1988, p.4). Self-consumption entitlements for employees, as discussed in the previous chapter, ensured the right of state employees to buy a given quantity of goods at negligible official prices (Aguilar and Zejan, 1990, p.19).

The formal employees who made up the urban workforce were overwhelmingly MPLA supporters of Kimbundu background joined by the mix-raced and assimilated of the coastal towns (Heywood, 2000). As has been noted elsewhere, “While party membership was not in itself sufficient for access to certain opportunities (such as employment, higher education, and housing) it became a condition for access” (Neto, 2001 p.44). Loyalty to the ruling party conditioned “access to professional education and upward mobility” (Vidal, 2008, p.130). State enterprise managers were selected from party ranks and the MPLA was formally represented on each enterprise’s board of directors (Aguilar and Zejan, 1990; World Bank, 1991).

The concentration of economic activity in the cities is not surprising, as these were geographic zones that were under MPLA control whereas the UNITA’s mainstay was in the rural areas. The urban areas were also the historical support bases of the MPLA. Hence

¹⁸ In 1975, 18% of Angola’s population lived in urban areas but by 1990s this had increased to half of Angola’s total population (Minter, 1994).

the importance of provision of formal employment opportunities to urban dwellers. Indeed, during the Marxist-Leninist period, the state-owned enterprises did not lay off workers but were rather tasked with absorbing surplus labour (Aguilar and Zejan, 1990). The political function that the state-owned enterprises were serving contributed in no small part to the difficult economic situation that many of these companies struggled with well into the 1990s (Aguilar and Zejan, 1990).

This section sought to demonstrate how, as the state came to gradually dominate in the Angolan economy following independence, the role of SOEs grew increasingly significant. This was not because of production, as little was actually produced domestically during this time. Rather, SOEs grew important because they controlled all foreign trade and were the country's main formal employer. As the proceeding section will show, however, the model with the SOEs at its centre, was unworkable in the long run.

4. Preserving an unworkable system

By the mid-1980s, the flaws in the MPLA's Marxist-Leninist project were apparent and the system of resource distribution became increasingly strained. Continuous warfare and the acute lack of manpower made it difficult for the authorities to assert the kind of control over the economy that it had envisioned at independence, which was considered in the first part of this chapter. Poor management of many SOEs and rigid bureaucracy resulted in production slowdowns and shortages in goods (Ferreira, 2002a). A cumbersome system of price controls, introduced after independence, meant that SOEs were tied to fixed selling prices on its outputs of goods and services, leading to chronic shortages and rationing (Hodges, 1993). Moreover, rigid labour regulation rendered it impossible for SOEs to lay off personnel. Enterprises were therefore forced to continue paying salaries even if their

production subsidized (Hodges, 1987). In line with Law 17/77 on State Owned Enterprises, enterprises were required to surrender 80% of their operating surpluses to the central government (Law 17/77; World Bank, 1991).

Policies such as the above-mentioned contributed to SOEs being inefficiently run and loss-making. The financing model of these enterprises, relying on transfers from the state, additionally meant that they had little incentive to be efficient. The system of soft credit constraints meant that firms, upon encountering financial difficulties, would receive government support (World Bank, 1991). In most cases, however, prices were set too low for any substantial profits to be made. Instead of reaping profits, most state-owned enterprises became dependent on transfers over the government budget to cover their net losses (Hodges, 1993). Writing for Economist Intelligence Unit, Hodges (1993) estimated that subsidies to Angolan SOEs totalled \$21 million in 1991,¹⁹ or 23.8% of total state expenditure. Another \$11 million was needed to cover state wage arrears (Hodges, 1993).

An intensification in the war effort, coupled with the excessive debt accumulated by certain state-owned enterprises meant that by the early 1980s the Angolan state budget was in significant deficit. By 1986 this deficit became unmanageable (Ministry of Finance, 1990). From 1986, capital inflows were insufficient to finance the current account deficit and Angola began to accumulate arrears in its external payments.²⁰ By 1988, external debt had reached \$5.2 billion, compared to Angola's GDP which amounted to \$1 billion that same year (OECD, 2000). The 1986 fall in global oil prices was an important contributor to Angola's worsening fiscal stance as was the intensifying war against UNITA.²¹ The end of

¹⁹ Exchange rate used Kwanza 4000: \$1.

²⁰ According to the World Bank (1991), \$378 million at the end of 1986 and \$648 million at the end of 1988.

²¹ Military expenditure doubled from 1980 to 1986 and by 1987 accounted for almost 50% of total recurrent expenditures (World Bank, 1991, p.xix).

the Cold War and collapse of the Soviet Union also meant that support for Angola from Eastern Bloc allies started to dry up (MacFarlane, 1992; Le Billion, 2001). As one senior civil servant in the Ministry of Finance at the time recalled, whereas the government had until the mid-1980s cultivated its international creditworthiness, met its commitments and honoured those loans acquired before independence, it was now struggling to service its debt payments. Consequently, arrears on these loans were accumulating.²²

Already by the second congress of the MPLA in December 1985, the Central Committee of the party recognized the deficiencies of the socialist model it had pursued over the last decade (MPLA, 1985). When President José Eduardo dos Santos launched the *Program de Saneamento Económico e Financeiro* (SEF) in 1987,²³ the first in a series of economic reform programmes, it was clear that changing the direction of the Angolan economy towards a market economy was seen as inevitable. “The President stressed that there was no way we could continue in the soviet way”, recalled one central member of the government’s first reform team.²⁴ Rather, it was best to proceed in a capitalistic fashion, “before people started forgetting what it meant to be capitalist”.²⁵ The SEF-programme was the first reform programme launched by the government emphasizing the need to reform the country’s economic institutions, an effort to reduce the scope and extent of state intervention in the economy (Roque, 1994).

Reform and modernization of the banking system was a central goal of the SEF programme. Angola’s system of mono-banking formally ended with the enactment of new financial legislation in 1991(Law no. 5/91) and the official termination of the BNA as commercial

²² Interview, senior civil servant Ministry of Finance, Luanda, 30.09.2015.

²³ English translation: “Programme for Economic and Financial Purification.”

²⁴ Interview, former member of the government’s economic reform team, Luanda 14.10.2016.

²⁵ Interview, former member of the government’s economic reform team, Luanda 14.10.2016.

bank that the same year (Law no. 4/91). Three new state-owned financial institutions were established in 1991 as a response to the changes. Banco Popular de Angola was transformed into a commercial bank under a new name, Banco de Poupança e Crédito (BPC). The new state-owned bank, Banco de Comércio e Indústria (BCI) was created subsequently with the mandate to service the needs of enterprises (Tjipilica and Valerio, 2015). Finally, a specialized credit institution Caixa de Crédito Agro-Pecuário e Pescas (CAP) was established in 1991 as a spin-off of the agricultural portfolio of BNA (World Bank, 2002). CAP's function was to promote the development of the agricultural and fishery sector through the granting of credit to small enterprises (World Bank, 2002). In addition to CAP, smaller 'autonomous funds' were set up to promote medium sized private enterprises, including the Fundo de Apoio ao Empresariado Nacional (FAEN) (De Vletter, 2002).

Further liberalization measures in early 1992 moreover saw the entrance of a number of foreign banks, including two Portuguese banks, Banco Totta and Açores (BTA)²⁶ and Banco de Fomento Exterior (BFE),²⁷ which had been present in the country during colonial times (Nunes et al., 2010). However, the exposure of these banks to the domestic economy, as measured in credit to the economy was negligible for most of the 1990s (see table 4.1). Foreign banks did not extend any significant volume of credit before the late 2000s and when they did, it was overwhelmingly in the form of short-term credit to the trade sector (Kyle, 1998).

²⁶ BTA ceased to exist in 2004 and became Banco Totta de Angola following an acquisition by the Spanish financial group Santander. In 2009, the bank changed name to Banco Caixa Geral Totta de Angola, following the entry of a new shareholders, Portuguese Caixa Geral de Depósitos. In 2015, Banco Santander Totta sold its shares in Banco Caixa Geral Totta de Angola and the bank became known by its current name, Banco Caixa Geral Angola (Banco Caixa Geral Angola, 2018).

²⁷ BFE was acquired by Portuguese Banco Português de Investimento (BPI) in August 1996 and renamed Banco de Fomento Angola (BFA, 2009).

Table 4.1: Credit structure by Bank (percentage of total)

	Ownership	1998	1999	2000	2001	2002	2003	2004	2005
BAI	Domestic private	1,92	9,6	23,15	23,82	26,83	19,82	18,42	14,22
BCA	Domestic private		0,25	2,19	3,88	2,8	2,95	3,55	3,17
BCI	State	19,79	17,24	14,53	18,08	14,98	9,67	7,13	5,64
BFA	Foreign private	7,49	14,19	20,48	19,5	19,68	22,85	26,14	28,64
BCP	Foreign private	1,53	2,33	1,78	0,79	1,59	2,09	1,78	1,78
BPC	State	30,58	41,62	32,01	31,44	30,63	33,74	26,98	22,41
BTA	Foreign private	3,94	4,39	5,57	2,48	2,02	4,38	5,44	4,28
CAP	State	34,75	10,39	0,28	0	0	0	0	0
SOL	Domestic private					0,4	0,98	1,37	1,7
BESA	Foreign private					1,08	3,36	6,99	9,6
BRK	Domestic private						0,17	2,12	2
Novo Banco	Foreign private							0,08	0,16
BIC	Domestic private								6,4
Of which national currency		100	60,38	47,18	42,46	40,69	53,06	57,25	55,81
Of which foreign currency		0	39,17	52,82	57,54	59,31	46,94	42,75	44,19

Source: BNA (2007)

As one senior civil servant later admitted, the fact that the MPLA government adopted the SEF-programme at the same time as the country applied for full membership of the IMF and World Bank and commenced negotiations with the Paris Club over debt restructuring,

was not a coincidence (Dowden, 1987).²⁸ In the light of the economic downturn that Angola experienced in the late 1980s, international financial institutions enjoyed greater leverage in their negotiations with the Angolan authorities and greater influence over the government's reform programme.²⁹ In a speech on the occasion of Angola's application for membership of the IMF, President dos Santos stated that Angola could not afford to be seen at odds with the IFIs agenda given the national reconstruction needs of the country (President dos Santos cited by Dowden, 1987). What is more, the fall of the Soviet Union and the rise of the neo-liberal consensus meant that the policy prescriptions touted by the IFIs were fast becoming the only game in town (Pitcher, 2012).³⁰ Angola's embrace of the free market system in the early 1990s, coupled with the President's readiness to introduce financial sector change must therefore be seen in this context. As one of the last African countries to join both the IMF and World Bank³¹ on the 19 September 1989, Angola accepted that the recognition of the international financial institutions was a necessary step to ensure regime survival and solvency (Hodges, 1993).³² A nominal commitment to free market principles was moreover required to help ease the burden of its external debt and facilitate the country's access to international financial markets, evident by the fact that Angola's entry into the IMF and World Bank was a condition set by the Paris Club for initiating debt rescheduling with the country.³³

²⁸ As Africa Editor, Dowden, reported in the Independent that Angola had been in contact with the IMF since 1984 and "increasingly invited help from Western financial institutions" (Dowden, 1987).

²⁹ Interview, senior civil servant Ministry of Finance, Luanda, 30.09.2015. Interview, former member of the government's economic reform team, Luanda 14.10.2016.

³⁰ Pitcher (2002, p.130) makes a related point for Mozambique and the influence of neo-liberalism on economic reform in the country after 1992.

³¹ After Angola joined in 1989, Namibia joined the IMF and the World Bank in September 25, 1990, Eritrea on July 6, 1994 and South Sudan on April 18, 2012 (IMF, 2017; World Bank, 2018).

³² Interview, former member of the government's economic reform team, Luanda 14.10.2016.

³³ Interview, senior civil servant Ministry of Finance, Luanda, 30.09.2015. In the end Angola was able to reschedule its debt before it became a member of the Bank and the Fund.

Whereas Angola avoided a structural adjustment programme with the IMF at the time, and would do so until 2009, the IFIs nonetheless maintained a degree of sway over the country's economic policy making. This is evident in the number of economic reform programmes adopted by the Angolan government in the 1990s, embodying the IFIs standard prescriptions for reform.³⁴ IFI prescriptions encompassed the established remedies of currency devaluation, abolition of administrative credit instruments, elimination of capital controls and liberalizing the financial sector (Callaghy, 1990). The IMF advocated a greater role for free markets and private enterprises relative to the public sector in Angola, including “a drastic and early reform of the public-sector enterprises” (IMF, 1990, p.9). The privatization of state enterprises was seen as “an appropriate mechanism to reduce the burden on the budget” (IMF, 1990, p.9; World Bank, 1991).

Yet, it soon became clear that for the MPLA government reform would not take the form of outright privatization. Rather, reform came to concern the re-dimensioning the Angolan economy (MPLA, 1991; Ferreira, 1999).³⁵ According to the SEF programme, the restructuring of the state sector would proceed “by privatizing small and medium-size public sector companies and opening up the economy, *with the exception* of certain specified strategic sectors”, which remained reserved for the state (Ministry of Finance, 1990, p.15, emphasis added by me). By the end of 1994, the government had privatized 192 of 564 SOEs and placed 87 under private management contracts (IMF, 1995).³⁶ Although the degree and pace of privatization may be impressive, it is important to highlight the type and value of companies that remained with the state, a point Pitcher

³⁴ See Hodges (2004, p.114-115) for an overview of Angola's economic reform programmes 1987-2000

³⁵ SOEs, public-private enterprises and the private sector companies were all envisioned to co-exists in what the MPLA referred to as a “mixed economy” (MPLA, 1991).

³⁶ Privatized enterprises were largely in the industrial and construction sectors (46%), followed by commerce (19%) (IMF, 1995). Additionally, the state sold off much urban housing that had been nationalized or confiscated after the settler exodus in 1975.

(2002) has also observed in the case of Mozambique. Importantly, the Angolan state continued to own the bulk of the country's medium and large-scale enterprises well into the 1990s (Hodges, 1993).³⁷ This strategy was in line with the Law on State Enterprises of 1988, which made it clear that "state-owned enterprises that carry out activities of public interest, as well as those that are fundamentally interested in national defence" should remain under state control (Law no. 11/88).³⁸ This included enterprises involved in strategic sectors such as the realization of weapons, basic sanitation, the media, air, rail and sea transport, port and airport administration. Given that Angola was at war when privatization was launched, it appears reasonable that the MPLA government wished to maintain control over key supplies to the war effort. Although arms were not manufactured domestically, Ferreira (2002a) explains how the national economic sector was still called upon to supply certain goods, services and technology for the consumption of the state's armed forces. Additionally, a number of enterprises developed around the assembling of imported weapon components.³⁹ The financial sector was not included in the list of strategic sectors⁴⁰ but nonetheless remained state-dominated throughout most of the 1990s. Angola's mono banking system was substituted not by private but by state-owned banks, which remain fully public to this day.

³⁷ Angola has gone through several rounds of privatization throughout the 1990s up until this day. The process has been slow and various companies intended for privatization since the early 1990s remain under state control to this day (see Roque, 1997, p.167-169).

³⁸ Enterprises that were active in certain geographic areas were also included (Decree no. 32/89).

³⁹ Some of the main enterprises engaged in the sector were Empresa de Reparação e Recuperação de Equipamento Militar, Aerovia, Bricomial and Ecomil (Ferreira, 2002a).

⁴⁰ Activities reserved for the state included: central banking, weapons, basic sanitation, the media, air, rail and sea transport, urban mass transport, port and airport administration. It included companies like Sonangol (state oil company), Endiama (diamonds), TAAG (national air carrier), ENATEL and EPTEL (telecommunications), ENE and EDEL (electricity) and ANGONAVE (shipping) (Hodges, 1993). International trade was kept under total control through a licensing system for imports and exports (Aguilar and Zajan, 1991). ENDIAMA, Public Television of Angola (TPA), National Radio of Angola (RNA), Jornal de Angola, Sonangol, Angola Telecom, Port of Luanda, Enana Airports, Angola airlines (TAAG).

Other enterprises were strategic because they represented what Pitcher (2002, p.174) refers to as “cash cows”, to the government.⁴¹ One such enterprise was the state-owned telecommunication company, Angola Telecom,⁴² which acted as Angola’s sole supplier of all telecommunications, fixed line telephone, international connections, and mobile, until 2001(World Bank, 2005). Angola Telecom was able to make “an attractive return due to its monopoly status and ability to charge exorbitant rates on international calls” (Kyle, 1998, p.27). A more prominent example, national oil company Sonangol remained key to state survival through its role as coordinator and supervisor of the petroleum sector since its foundation in 1976. Throughout the war years, Sonangol was able to achieve “business success” in the oil sector at the same time as the rest of the domestic economy imploded, establishing oil exports as the state’s primary revenue stream (Soares de Oliveira, 2007).⁴³ Sonangol together with the national diamond mining company had another strategic importance, which was that of major net providers of foreign exchange to the country.

State owned companies were also strategic in that they provided subsidies to consumers, a common method of regimes in Africa and beyond to foster approval and maintain political stability (Herbst, 1990). These subsidies were in turn largely reserved for the country’s urban upper income classes, as these were the main groups with access to cars, municipal water, and electricity. In total, Kyle (1998) estimates that subsidized basic goods provided by the state-owned companies cost the Angolan government \$400 million in 1995. As Aguilar wrote in 1995, “Today, gasoline is worth less than 1 cent a litre in Luanda. The subsidy covers 99.8 percent of the cost of fuel” (Aguilar, 1995). Other major providers of

⁴¹ Interview, senior civil servant Ministry of Finance, Luanda 30.09.2015.

⁴² The product of the merger of ENATEL and EPTTEL in 1992.

⁴³ For Sonangol’s role see Soares de Oliveira (2007). Unlike other Angolan state-owned enterprises, Sonangol was able to access foreign credit on the back of its solid reputation internationally.

subsidies included air carrier TAAG and the electricity company ENE (Aguilar and Stenman, 1996).

A final critical function of the SOEs continued to be that of employment provider, as discussed in previous sections. Although the initial privatization of small and medium-sized firms meant that a number of workers were laid off, the larger enterprises employing the most workers remained in state hands also after Angola abandoned the socialist model (Hodges, 1993). The MPLA government worked deliberately to fight unemployment and kept SOEs in operation and maintained payrolls even when productivity dwindled (Roque, 1997).⁴⁴ Low-qualified civil servants were sheltered from the downsizing efforts of “each and every IMF and World Bank restructuring programme in the late 80s and throughout the 90s” (Vidal, 2008, p.149).

Dismissing workers likely came at too high a political cost, as these were individuals frequently recruited on the basis of their MPLA affiliation, a point that was raised earlier in the chapter (Aguilar and Zejan, 1990; Birmingham, 1988). Sackings could furthermore contribute to heightening political instability in a context where unemployment already presented a major problem to the government, something Pitcher (2002) shows to be a salient factor in the case of Mozambique. As the MPLA government was preparing for the country’s first multiparty election in 1992, it is unlikely that the party would engage in reforms that would threaten to alienate important constituencies and cause upset in an already volatile political climate. In fact, a Financial Times article from 1991 confirms such a sentiment, explaining how “members of the ruling MPLA party who believe they have a

⁴⁴ The observation by Rocha et al. (2016) that Angolan SOEs on average employed 480 workers even as company performance suffered, confirms the problem of overstaffing.

chance of winning the country's first free democratic election are extremely nervous of the impact of austerity measures and adjustment on their popularity, especially in the urban areas” (Financial Times, 1991).

Not ready to cut back on its political use of strategic enterprises, the MPLA needed to reduce the negative financial burden of these companies, on the state budget, through other means. Public enterprises, as already discussed, had up until that point relied solely on subsidies from the central government for financing (Hodges, 1993).⁴⁵ With the introduction of SEF, the aim was to “give greater autonomy to state enterprises” both financially and operationally,⁴⁶ thus putting an end to SOE financing over the state budget (Ministry of Finance, 1990, p.3). The latter was in line with the 1988 Law on State Enterprises, endorsing the accumulation of extra investment and working capital by SOEs including permission to retain a larger share of their profit (Law no. 11/88). Now, financing of the activities of SOE would be done “basically through own means” (Law no. 11/88, article 9).⁴⁷ SOEs were free to “use bank or commercial credit” to meet their obligations (Law no. 11/88, article 22) although they would no longer be enjoying the guarantee of the government (Law no. 11/88, article 28).

As the next section will show, state financing of state-owned enterprises did not disappear, however. Rather, given that many SOEs and especially larger ones were considered too important to the MPLA government to privatize, the state needed to safeguard its interventionist role in the economy, at the same time as being seen as to comply with new

⁴⁵ Endiama and Sonangol being exceptions here because these enterprises were allowed to borrow abroad.

⁴⁶ Under the new law enterprises would additionally have more autonomy in their price and labour policies. It was noted however, that this applies “within constraints established by the government for the protection of consumers and workers” (World Bank, 1991, p.136).

⁴⁷ The state would not cover losses of state enterprises but rather state companies would become corporate entities liable for corporate tax (Hodges, 1993).

external pressures. The government found its solution in the country's nascent financial sector.

5. The role of the financial sector

Under the new financing regime for state-owned enterprises, it was expected that the commercial banking sector would offset the state's previous role as financier of the enterprises' operational costs and investments (Law no. 11/88). In this way, the enterprises would survive and continue executing their important functions in the economy, without being a drain on state coffers. The reality, however, was that Angola had no functioning financial sector capable of taking such a role. What is more, by 1991 it was clear that the bulk of credit extended to borrowers, be they enterprises or individuals, was not commercially viable (World Bank, 1991).⁴⁸ To safeguard the political settlement, it was clear that the subsidising of the economy through government transfers needed to continue like it had before. The difference was that it would now take place behind the facade of a market based financial sector, so as to ease external pressure for economic reform. The result was that measures ostensibly aimed at liberating the financial sector in Angola did not substantially weaken the government's overall role in mediating access to capital.

5.1 Public banks and private interests

In 1991, the World Bank expected that with the official end to mono banking, Angola's commercial banks would make credit decisions on the basis of sound financial considerations (World Bank, 1991). Yet, from the beginning it was not clear how the newly created commercial banks were to achieve the task granted to them, namely to extend

⁴⁸ Nashashibi (1998) shows how in the Algerian case, the privatization of state-owned banks was similarly slowed down by the fact that these banks were weighed down by sizeable non-performing loans.

financing to state-owned enterprises to help the latter replace the subsidies previously granted to them by the government. The following year, at the start of a World Bank funded \$21 million project on financial institutions modernization in the country, it was noted that “the transfer of public enterprise accounts is proving difficult because many have long overdue debts or are likely to become problem loans for banks. In fact, many public enterprises do not even satisfy the formalities for opening an account with a commercial bank, because they were never legally constituted” (1992, p.8). The World Bank report went on to describe how the “Government has decided to retain these accounts [of state-owned enterprises] until the enterprises are either liquidated or privatized” (1992, p. 8).

Earlier it was revealed how the liquidation and privatization of enterprises in Angola was slow and, in some cases, did not take place. State policy to keep SOEs afloat, for several different reasons discussed above including strategic importance and the enterprises’ role in providing employment, allowed enterprises to access loans although some were no longer economically viable (IMF, 1997; World Bank, 1991). Consequently, a flow of subsidized credit from the BNA to help finance SOEs persisted at least until 1996 (Roque, 1997). The latter was made possible by the fact that the BNA’s commercial operations did not end in the first years following the official termination of mono banking, as originally intended when the new central bank law was passed in 1991 (Law no. 4/91). As a 1995 IMF report noted, “the consolidation of the two-tier banking system established in 1991 has not yet been completed”, adding that the “phasing out of BNA commercial operations has taken much more time than initially envisaged” (1995, IMF, p.23). The BNA’s role in steering monetary policy was undercut by its role in keeping the Angolan economy afloat (Lavrador, 1997).

Additionally, the Angolan authorities continued the practice of administratively setting interest rates until May 1999. The artificially low interest rate, which in reality was negative in real terms due to the high rates of inflation, meant that credit was heavily subsidized by the BNA and by the state-owned banks (Hodges, 2004). State-owned enterprises additionally benefitted from subsidized foreign exchange loans from the BNA, which were intended to support imports of food and production inputs (IMF, 1997).

The result of such arrangements was that sizeable debt continued to accumulate in public sector companies, representing an increasing burden on the BNA (IMF, 1995; Coelho, 2000). In 1995, the IMF noted that “the BNA's portfolio still includes assets not-related to its central bank functions; these assets consist mostly of doubtful and nonperforming loans contracted earlier and not yet liquidated or sold to the commercial banks” (IMF, 1995, p.23). By the time of the IMF’s report in 1995, the BNA accounted for 74% of outstanding credit to the economy, a large proportion of these loans assumed to be non-performing. Rather than reducing lending to the economy, in line with the recommendations of the IFIs, central bank credit to government and public enterprises expanded after 1992 until 1996 (Coelho, 2000). At the time, the decision to expand central bank credit was interpreted by the IMF as “an attempt to sustain production and employment, particularly in the state enterprises” (1995, p.24). Because it allowed the subsidies to be transferred through the banks instead of over the state budget, the state-owned banking institutions made it possible for the government to continue subsidizing the state-owned enterprises. This was so even when international pressure for economic liberalization mounted and, as described in the last section, Angola had officially transitioned to a market economy, which meant that the granting of soft credit was technically no longer an acceptable policy tool.

The ability to subsidize state-owned enterprises was not the only reason why political leaders held on to the control of the bank sector. As one senior Angolan banker confided, many people within the BNA at the time were privately profiting from the continued commercial activities of the central bank, such as the ability to grant subsidized loans.⁴⁹ Such practises added to the number of parties who saw the partial-equilibrium situation of the 1990s, with the continuation of the BNA's commercial arm as one clear example, to be in their interests. With control over the banking sector, the Angolan state remained in command over the principal forms of accumulation in the post-transition period, asserting a considerable degree of influence over who could access to capital and on what terms (Hodges, 2001).

One of the principal mechanisms of elite accumulation at the time was the buying of foreign exchange from the domestic banks at an administratively set, artificially low rate (Hodges, 2001). The official rate had since 1994 been determined at irregular fixing sessions at the BNA, where commercial state-owned banks, BPC and BCI, and subsequently private banks, participated (IMF, 1995; BAI, 1999). The BNA's monopoly on foreign exchange meant that the fixing sessions were the only official source of foreign exchange available to commercial banks,⁵⁰ allowing authorities to control who could access foreign exchange at the official price. Banks received political instructions designating to whom they could sell foreign currency, a practise that benefited the politically well-connected (Hodges, 2004).

⁴⁹ Interview, representative foreign bank, Luanda, 13.10. 2016.

⁵⁰ Interview, former central bank governor, Luanda 28.9.2016.

Because Angola's foreign exchange rate remained at an artificially low level throughout the 1990s, demand for foreign currency constantly outstripped supply.⁵¹ Only relatively small amounts were allocated at the fixing sessions (IMF, 1995). Most people were required to resort to the informal market to access foreign exchange, where during 1991-1998 the rate was on average 2.9 times higher (Gelbard and Nagayasu, 1999: 3). The gap between the formal and informal exchange rates generated a considerable amount of arbitrage, as well-connected individuals and groups, fortunate enough to obtain foreign exchange at the official rate, could sell their foreign exchange at Angola's informal market for a considerable premium. As described by Shaxson (2007, p.52):

“By early 1994 the kinguilas [A Kimbundu term for those involved in the informal exchange of currency in Luanda (Lopes 2006)] were offering 120,000 Kwanzas per dollar, 20 times the official rate of 6,000. A powerful official could then change \$1,000 on the street and get 120 million Kwanzas in a shoulder bag from the kinguilas. With the right connections, he or she could then go to the central bank and ask for the official rate, at 6,000 to the dollar, yielding \$20,000 of what was, in effect, free oil money from the bank. This was normally not taken in cash; instead the central bank would pay it to a foreign supplier, who would deliver \$20,000 worth of goods. The happy official would collect these from the port and sell the goods in the market, with another mark-up, and repeat the cycle”.

Angola was caught in a vicious cycle where the continued overvaluation of the national currency exaggerated the country's reliance on imports, as it contributed to making imports cheaper than domestically produced goods.⁵² Whereas the war had already hurt domestic production, it suffered a second blow from having to import intermediary goods with

⁵¹ As evident by the consistent divergence between the informal and formal exchange rate (Gelbard and Nagayasu, 1999).

⁵² Other factors also contributed to the high price of local produce including the Dutch Disease effect and poor infrastructure for production and distribution due to decades of conflict.

foreign exchange often bought at exorbitant prices on the informal market (Hodges, 2004). Adding to the drain on government resources from worsening import dependence, it is clear from Angola's low rates of saving at the time that negative deposit interests rate, due to the administratively fixed interest rate, discouraged private savings (BNA, 2007). If at all, Angolans preferred to save in foreign currency, which meant that by 2002 foreign currency deposits accounted for about 80 percent of total deposits in the country (IMF, 2002).

Another mechanism through which the state used the state-controlled banking sector to reward its political allies were by means of credit at fixed interests rates (Hodges, 2001). Throughout the 1990s the interest rate continued to be administratively set below the rate of inflation, which in the course of the 1990s reached hyperinflation levels (Aguilar, 2001). Like in the case of foreign exchange, credit was allocated on an administrative basis by state-owned banks, following the instructions of central bank officials or higher authorities.⁵³ Because credit was given on a short-term basis, not unreasonable given the high-risk operating environment, there was a strong bias in favour of short-term operations on behalf of the banks. Consequentially, the World Bank noted in 1996 that:

“Credit allocations mirror those of foreign exchange through the official market and are often tied to foreign exchange trading operations. While in theory the sale of foreign exchange would involve the payments of counterpart funds in Kwanza, some clients obtain bank credit (at negative real interest rates) to pay the already subsidized foreign exchange. Because the amount of foreign exchange sold through the market is small and the rents appropriated through its allocations are large, there is fierce competition for these funds” (1996, p.18-19).

⁵³ Interview, former BNA governor, Luanda 28.9.2016.

State intervention in the credit and foreign exchange market represented a de facto transfer of resources from the state to private pockets. In depicting the process, Hodges (2001) and IMF (2002) describes how state-owned banks accumulated bad debt from engaging in connected lending, granting credit at subsidized interest rates or on conditions in which repayment was not expected. The non-performing loans of public banks were in turn covered by the state through bailouts from the treasury, an action that contributed towards depleting of state coffers (Hodges, 2001; IMF, 2002).

The allocation of resources through state-owned banks gradually eroded the capital base of these same banks (Hodges, 2004; World Bank, 2002; IMF, 2001). However, because the abovementioned arrangements benefitted well-connected individuals handsomely, beneficiaries of these schemes represented a strong barrier to further liberalization of the sector (Soares de Oliveira, 2015). It would consequently take over five years from when it was first discussed by the authorities until the BNA transferred all commercial banking activities to CAP (BNA, 2017; Mowatt, 2001). The transfer of BNA commercial activities to CAP made the latter specialized financial institution the largest provider of credit to the economy, ahead of the two other public commercial banks BCI and BPC (See table 4.1; BNA, 2007). Before the transfer and throughout the 1990s, CAP had in effect functioned as department within the BNA; the IMF noting that the bank's lending represented a de facto "expansion of credit by the central bank" (IMF, 1996 quoted in Hodges, 2002, p.133). The transfer of the commercial lending portfolio of the BNA thus added to the already large stock of non-performing loans that CAP had acquired from extending concessionary and occasionally interest free loans, many of these to SOEs, over the years (Mowatt, 2001). By 1999, the World Bank estimated that nearly 97 % of CAP's loans were non-performing (World Bank, 2002). An audit of CAP's accounts from the same year revealed, according

to newspaper reports, “a \$100 million hole in the bank's finances” (Africa Confidential, 1999a).⁵⁴

Following pressure from the IFIs, CAP was liquidated in 2002 (IMF, 2003b). Liquidating the bank was not an uncontroversial decision, as CAP was a central supplier of credit on behalf of the authorities throughout the 1990s (BNA, 2007). CAP is also like to have had an important standing as an institution, something that is confirmed by the fact that from 1996 until its liquidation in 2002, BNA covered all of the institution’s operational expenses, including severance payments and retirement benefits, without ever debiting the government (IMF, 2003b). When CAP ceased its operations in 2000, the majority of CAP’s 1125 employees were transferred to the payroll of the BNA (World Bank, 2002).

The extension of subsidized credit by state-owned commercial banks was during this time not limited to CAP, however. Even though CAP was the largest provider of credit domestically in the late 1990s (Table 4.1), the BPC and the BCI were similarly “allocating credit on the basis of administrative directives received from the central bank or higher political authorities” (Hodges, 2002, p.133). As pointed out by the IMF in 2001 (2001, p.9), the latter included “loans made at subsidized interest rates or under conditions in which repayment would not be expected and/or demanded”, contributing to the erosion of the capital base of these state-owned banks. Yet, there are reasons to believe that the BPC and BCI were more conservative in their lending practises than CAP, taking into account the low repayment rates that the two banks encountered on their loans whilst neither enjoyed the same privileges as CAP (Economist Intelligence Unit, 1999c). Moreover, because these were commercial banks, the BPC and BCI were not able to extend the same amount of

⁵⁴ At this point total assets of CAP were \$70 million (IMF, 2003b).

credit as the CAP due to prevailing banking regulations. By law, Angolan commercial banks were required to redeposit 20 % of their deposits as reserves in the central bank at interest yields that were highly negative in real terms (World Bank, 1992). The requirement was at one point increased to 40 % (Instructive no. 01/99).⁵⁵ That CAP enjoyed a privileged position is also a view held by former BPC employees, stating that their bank “remained rather careful” in its credit allocation throughout the 1990s.⁵⁶ As is common in high-risk environments, BPC and BCI mainly engaged in lower risk short-term financing in the 1990s with the trade sector by far the main receiver of credit in the economy by the late 1990s (BNA, 2007). As director of BPC Amilcar Azevedo da Silva admitted in an interview with the Financial Times in 1997, competing with BNA (and by extension the CAP) was unreasonable as the latter was “a player” and thus “could not, naturally, supervise itself.” The latter, da Silva added, left the BPC and BIC with a competitive disadvantage (Da Silva, 1997).

Neither BPC or BCI could avoid being used for the extension of heavily subsidized loans on behalf of the ruling elite, however. Like in the case of CAP, BPC and BCI were used to extend credit to strategic clients, including state-owned enterprises, on conditions that guaranteed losses for the banks (Kyle, 1998). By late 1990s, the cumulative effects of the above-mentioned arrangements had led to an erosion of the capital base of state-owned banks. The IMF reported that the “banks continue to be badly managed, are recapitalized, have almost 50 per cent of non-performing loans, lack reliable internal controls, divert income to the privileged few, do not observe prudential norms and are a source of

⁵⁵ Whereas banks in most countries are required to redeposit (usually without interest) a certain fraction of their deposits as reserves at the central bank for precautionary reasons, excessively high levels such as those required by the BNA are indicative of state-owned banks’ deposits going directly to finance the central government (Beim and Calomiris, 2001).

⁵⁶ Interview, banker previously with Angolan public bank, Luanda, 20.9.2015.

continuous quasi-fiscal losses” (IMF, 2001 quoted in Hodges, 2004, p.134). By 2002, both BPC and BCI were set for recapitalization (World Investment News, 2002a).⁵⁷ Notwithstanding numerous pledges to the contrary, the government’s intention to privatize fully or partially the ownership of the two banks never materialized, however. The strategic function of the banks, as previously discussed and here attested to, likely meant that the banks were too politically important to transfer out of state hands.

6. Conclusion

This chapter explored the onset of Angola’s postcolonial financial sector and its role as an extension of the state in the country’s transition from centrally planned to a market-based economy in the early 1990s. As was explained in the first sections of the chapter, Angola’s official transition from centrally planned to market based economy was very much marked by the economic reality that had gone before it, namely the lack of a robust private sector and the take-over of the economy by the state after independence. The history of state ownership and central planning meant that the state was responsible for the bulk of the formal economy, in which the state-owned enterprises played a major part. The state-owned enterprises besides employed the MPLA regime and its supporters, thus making it that much more important to salvage these enterprises regardless of their economic viability.

Yet as the chapter showed, financing the centrally planned system became increasingly difficult as economic output waned in the 1980s. By the early 1990s, Angola were trying to find a way to continue subsidizing its ailing economy at the same time as President dos Santos and his team were aware that moving the country towards a liberalized, commercially oriented financial sector was inevitable. The solution, I argue, came in the

⁵⁷ In 2005, the Bank received a capital injection of 15 million (Macauhub, 2006).

form of a state-owned financial sector. As the chapter has shown, the public commercial banks became central to the upholding of the state-dominated economy throughout the 1990s and thus to the continuing hold of the MPLA over the economy. The state-owned banks provided subsidized credit and foreign exchange to keep flagging state-owned enterprises running. This allowed the state to continue subsidizing the SOEs as it had during the socialist days, allowing enterprises to maintain their strategic role in Angola's political economy. Equally important, the state-owned financial sector became the centre of accumulation in the 1990s as the politically well-connected were making considerable profit on the basis of their privileged access to foreign exchange and credit at a heavily discounted price. These accumulation strategies came at the detriment of the nascent banking industry, however. By the end of the decade, the state-owned banks were overwhelmed by non-performing loans.

This chapter has contributed a first example of the usefulness of the financial sector to the Angolan regime. It highlighted political leaders' incentive to safeguard the state dominated economy to explain institutional change in the financial sector. Accounting for the external pressure for reform in Angola late 1980s on the back of a failing command economy, it is important to understand why financial sector change took the form that it took. Yet as also become clear in the course of the chapter, the ruling elite were not passive receivers of the external recommendations, which is why the financial sector change did not follow standard IFI prescriptions. Rather, the ruling party made financial sector changes work for them and their political objectives. The latter point will become increasingly central in the subsequent chapters where the role of external pressure features less prominently and rather internal political impetus for change becomes key to the financial sector reform story.

Chapter 5

Laying the foundations for financial sector expansion in the late 1990s

1. Introduction

In the last chapter I showed how external factors help explain the financial sector change that formed part of the liberalization of Angola's economic policies in the late 1980s early 1990s. Throughout the transition period and into the late 1990s, I emphasized the vital role of the state-owned banks in ensuring political continuity on behalf of the MPLA party in the face of significant economic change. In this chapter, I explore the institutional changes that made possible the expansion of Angola's financial sector beyond the state-owned banks. Significant changes to the country's financial and monetary policies in the late 1990s further liberalized the Angolan financial sector, opening up the sector to private profit-seeking banks.

In the latter part of the 1990s, external pressure for financial sector reform was no longer as salient as it had been in the earlier parts of the decade. Therefore, the explanation offered in the last chapter focusing on external pressures is not sufficient to explain why, by the late 1990s, President dos Santos and his team authorised to initiate further change to the financial sector. In this chapter, I argue that financial sector changes did not come about because dos Santos and his team were forced. Rather, I offer the explanation that political leaders initiated change because their political position was changing. Specifically, the ruling coalition was feeling more confident and wanted to secure their position not only

short term but also into the future. The latter, I argue, required a change in accumulation strategy away from the precarious financial sector policies of the 1990s. The direction that change took was not random, as a view had been emerging in recent years in favour of reform and modernizing the economy on the party's terms and in a manner that protected, indeed advanced, the interests of the elite.

The chapter adds to the thesis' overall aim of theory building by demonstrating how financial sector change during this period was not necessarily a response by political leaders to crisis, as was the case in the period studied in last chapter. Rather, financial sector change can also come as a response from political leaders who find themselves in a relative position of strength, seeking ways to cement their position further. By tracking two decades of financial sector change, I show that change is a product not of a sole factor, but of several factors which may matter to different degrees according to different conjunctures. Additionally, the chapter contributes by explaining the changes that took place in 1999, which were fundamental in laying the foundation for Angola's modern financial sector and the financial sector expansion that would follow in the subsequent decade. Whilst the end of the civil war is often portrayed as the key driver of Angola's financial expansion (Shaxson, 2009) and 2002 as "year zero" when it comes to the country's institutional development (Schubert, 2015),¹ on closer inspection it is clear that already in 1999, during the last phase of the country's civil war, institutional and legal reforms which would make the expansion of the financial sector possible started in earnest. Several of my informants confirmed the importance of the 1999 reforms for the development of Angola's financial sector. A senior official at the BNA described the period 1999-2002 as "at the height of

¹Interview, IFI representative, Luanda 8.10.2015.

changes” to the financial sector.² Similarly, a banker who worked at state-owned BPC at the time, stated that, “the liberalization of the financial sector happened in phases. First in early 1990s, second in 1996 and the last ‘wave’ of liberalization in 1999 was the most important”. With the changes of 1999, the “framework was set” for the new financial sector.³

Assuming the importance of the late 1990s events for the advancement of the banking sector, the chapter starts by describing the changes that took place in the Angolan economy from 1999 in order to underscore their significance to financial sector advancement. Whilst earlier explanations centre on poor economic conditions as the decisive factor leading Angola’s political leaders to institute financial sector change, I show how the president and his advisors had more political legroom during this period than often assumed. Consequently, I argue that political leaders did not make the financial sector changes because they had to but because they wanted to on the presumption that the changes would help strengthen their position in power.

2. Reform measures

The previous chapter discussed how administrative measures used by the Angolan regime — including the fixing of exchange rates and setting of interest rates — produced grave distortions (if enabling ones for insiders) in the domestic economy throughout the 1990s (Hodges, 2001). Bank business was made difficult by an unrealistic exchange rate and strict capital requirements (Da Silva, 1997). Access to dollars was erratic, with *The Economist* revealing how importers complained “that that they can no longer extract any dollars from

² Interview, senior civil servant BNA, Luanda 23.10.2015.

³ Interview, banker previously in Angolan public bank, Luanda 20.9.2015.

the bank” (1998). The lack of dollars meant that production suffered, as local producers were dependent on foreign exchange to import inputs needed for production (World Bank, 1991). In May 1999, the Financial Times reported “Many businesses in Luanda have ground to a halt this year because of a local shortage of dollars...Businesses operating in Luanda complain of the almost complete lack of dollars in the economy and claim that the “fixing” system, by which dollars are distributed to favoured interests through the banks at preferential exchange rates, has frozen” (Shaxson, 1999a). The demanding situation faced by local businesses was not made better by the administratively fixed interest rate and the administrative allocation of credit.

The expansionary financial policy pursued by the BNA, comprising loose monetary policy, lax regulation of banks and subsidized credit, meant that domestic banks were largely loss-making operation for their owners, which in most instances was the Angolan state (Hodges, 2001; IMF, 2001 cited in Hodges, 2004).⁴ The loose monetary policy pursued by the BNA during the 1990s moreover reduced commercial banks’ interest earnings, disincentivizing banks from mobilizing savings (Brownbridge et al., 1998). Banks were at the time not lending money to the government by means of buying treasury bonds.⁵ The lack of a securities market meant that borrowing money from the BNA (i.e. money creation) was the method of choice of the Treasury when the government needed to finance its sizable fiscal deficits. This money creation in turn generated inflation (World Investment News, 2002a).

⁴ Foreign banks, largely present in the country as representative offices during the 1990s, were active mainly as correspondent banks facilitating currency exchange, handling business transactions and trade documentation, and money transfers. Such operations entailed less risk for the foreign banks and they were able to make “big money on simple transaction”. Interview, banker previously in Angolan public bank, Luanda, 20.9. 2015.

⁵ The Ministry of Finance launched treasury bonds and bills first in July 2003 (IMF, 2007; CEIC, 2009).

The above-mentioned administrative arrangements, including the dominant role of the BNA in the economy, were in large part a consequence of the delays and distortions that had followed Angola's official transition to capitalism in 1991.⁶ In this respect, the country's reform process was not too different from that of other post-communist countries, especially in Central Asia, where slow and sporadic transitions had similarly produced distorted financial markets (Hellman, 1998). Like these other post-communist transitions, piecemeal reforms in Angola produced substantial benefits to a "narrow range of groups while imposing substantial costs on the rest of the population" (Hellman, 1998, p.i). Predictably, beneficiaries of such arrangements in Angola — as elsewhere — developed a powerful opposition to reforms (EIU, 1999; Hellman, 1998). As Renato Aguilar, who reported on Angola's economic reform programmes throughout the 1990s, noted "Successive reform programmes have repeatedly broken down, and economic management has been chaotic. In part, this reflects the strength of reform's opponents—many of whom personally benefit from market controls" (Aguilar, 2001, p.1).

Angola's transition period to a market based economy also stood out from the experience of countries elsewhere, in part due to the civil war. War is generally held to have a negative effect on economic reform (Horowitz, 2003).⁷ As argued by Horowitz (2003, p.28), in these situations "Priorities are likely to shift to dealing with the immediate military emergency. Economic reforms will tend to be delayed or deformed, at least for the duration of military hostilities". Angola's reform experience also stood out because of the government's frequent policy reversal (Hodges, 2001). "Between 1990 and 1996, the Government of Angola issued a total of nine economic programs, with different policies meant to stabilize

⁶ Hodges (2001;2004) provide an overview over these administrative arrangements.

⁷ It does not mean that countries that are at war will not undertake economic reform. Mozambique pursued structural adjustment during the last years of the civil war. See Pitcher (2002).

the economy. On average, this resulted in 1.3 programs per year, with each lasting less than 11 months” (World Bank, 2002, p.16). One senior civil servant in the Ministry of Finance recalled, “Economic reform programmes during this period were changed before they had been properly executed. This made the situation very difficult for us, not to mention the process of liberalization [of the economy] and devaluation. There were so many points where the leadership had a change in heart, which made it impossible to have a straight line in policy.”⁸

The severe macroeconomic uncertainty and economic mismanagement that the protracted reform period produced, limited opportunities beyond the enclave oil sector, as pointed out by Vallée (2008) and Ferreira and Soares de Oliveira (forthcoming). Angolans who had branched out restricted their investments to commercial services – including banking services from 1996 – and activities connected to imports (Aguilar, 2001).⁹ Yet also in these sectors investors were facing limitations, as the earlier example of dollar shortages demonstrated. Africa Confidential (1998) noted how business not only had to deal with foreign exchange shortages but also inflated prices on important goods, which had helped make “Luanda the most expensive city in the world after Tokyo”. Expectedly, as will become clear in the coming sections, discontent with existing financial and monetary policy started to grow.¹⁰

⁸ Interview, senior civil servant Ministry of Finance, Luanda 7.10.2015

⁹ Studying the backgrounds of some of Angola’s main business profiles, it becomes clear that many of country’s most successful businessmen launched their official businesses careers in the import-export sector, including import of automobiles. These imports could then be resold on the local market for a considerable mark-up. Two of Angola’s wealthiest businessmen Jaime Freitas and António Mosquito became involved in the import of automobiles around 1991, according to Angolan business magazine Rumo (Rumo, 2016). See also Dinheiro Vivo (2013). Prominent Angolan entrepreneur Bartolomeu Dias also started his business with importing cars in the early 1990s, in addition to importing computers from Brazil (FNEWS, 2016).

¹⁰ Still it should be mentioned that elites are likely to have felt ambivalent about these changes as they meant putting an end to the administrative measures that many of them benefitted handsomely from. See Hodges (2004).

In 1999, the administrative arrangements described thus far were brought to an end. The year prior, at the 4 December 1998 Party Congress of the MPLA, party leaders acknowledged the increasingly precarious economic situation that the country was facing;

“The country is in a situation characterized by the destruction or poor state of affairs of most economic and social infrastructures, the fragmentation of the business fabric, the incipient educational system, a very precarious financial system, a distorted price system, a large number of state-run enterprises with very low efficiency rates and a worrisome unemployment rate. It is a fact that the public administration in Angola is weak and inefficient, and ill with vices that cause it to intervene in society much beyond the limits of what its role should be, it is no less true that the market mechanisms are very much fragile and incipient, incapable of making the economy function on a competitive basis” (MPLA, 1999, p.119).

The party pledged to tackle macroeconomic uncertainty through further reform: “Intervention will have to be conducted through structural market policies that lead to an improved functioning of the mechanisms of the market with the objective of promoting the modernization of macroeconomic management, competition between companies and price stability” (MPLA, 1999, p.119). A new economic team with a strong reform agenda was installed shortly after, in January 1999 (Africa Confidential, 1999b). With the support of the World Bank, the new team overhauled the 1991 Financial Institutions Law on the 23 April 1999, making the new law broader and creating openings for new financial products and institutions (World Bank, 2002; Law no. 1/99).¹¹

¹¹ Law no. 1/99 still excluded insurance companies, pension funds managers and investment fund managers, which were to be governed by their own law.

On 4 June 1999, the gap between the formal and informal exchange rates narrowed when the national currency was allowed to float, i.e. to be determined by demand and supply through an inter-bank foreign exchange market (Notice no. 1/99). Whilst the broader effect of letting the currency float was the easing of pressure on Angola's foreign exchange reserves (authorities were no longer forced to defend the unrealistic exchange rate) the change in policy also had important bearings on the politics of the banking sector. Importantly, in conjunction with additional laws passed that year, the new law reduced the BNA's dominance over the foreign exchange market, opening it up to domestic and foreign banks and to exchange houses (Notice no. 1/99; Notice no.2/99; Notice no. 3/99). Up until 1999, the market for conducting operations in United States dollars, the main foreign currency, had been fully controlled by the BNA. In this earlier period, the foreign exchange market had moreover been mainly about channelling oil export revenues directly towards imports (Gelbrad and Nagayasu, 1999).

From 1999, commercial banks and exchange houses were permitted to buy and sell foreign currency at freely negotiated exchange rates, at sessions held by the BNA or between the banks themselves outside the sessions held by the central bank (Notice no. 1/99). Banking institutions domiciled in the country could open current and foreign currency deposit accounts in the name of residents and non-residents (Notice no. 4/99), they could carry out credit operations with exporters (Notice no. 5/99) and capital restrictions were significantly eased (Notice no. 10/99; Notice no. 11/99). Specifically, the requirement of prior BNA approval of foreign exchange purchases for imports was abolished; limits on purchases of foreign currency for travel and transfer abroad were substantially relaxed; some capital account transactions were pre-authorized up to maximum amounts specified in United States dollars; and external tariffs on imports and exports were drastically reduced (IMF,

2000). Commercial banks were not slow to act on the changes. Already the same year other changes were introduced and 40% of loans by commercial banks were granted in foreign currency (BNA, 2007). Foreign currency sales quickly became the main operation of Angola's commercial banks (Bank for International Settlements, 1997).

Another important area of economic reform was that concerning interest rates. Also, in June 1999, the BNA liberalized interest rates allowing deposit and lending rates to be freely negotiable between banks and its clients (Notice no. 7/99). According to the Economist Intelligence Unit (EIU, 1999d), the objective was for interest rates, previously negative in real terms, to adjust to the market in order for banks to attract more money into the financial system. Practises described in the earlier chapter combined with several years of high inflation had eroded the capital base of the commercial banks (World Bank, 2002; IMF, 2001). The repayment rates on banks' loan portfolios was overall low due to poor loan practises and the lack of a legal system which made it possible for the banks to recover bad debts (Hodges, 2001). Low asset quality was mainly a concern of state-owned banks, however. Private banks, who did not suffer from the same pressure to provide financing, did not start extending any meaningful amount of credit before 1999 (BNA, 2007).¹²

Where private banks were more active was on the deposit side. With the easing of foreign exchange restrictions that year, depositing in foreign currency accounts became increasingly popular amongst private individuals and companies seeking to hedge against macroeconomic instability (World Investment News, 2002b; IMF, 2000; IMF, 2002). The receipts of oil bonuses in the second half of 1999 permitted a significant accumulation of government deposits in the banking system for the first time in many years (IMF, 2000). In

¹² Refer to table 4.1 page 127 of this thesis.

addition to the oil dividends, the exchange market was boosted with revenues from exports of diamonds and other mineral resources when the BNA in December 1999 passed legislation ordering “The settlement of exports and imports of goods, receipt and payment of current invisibles and exports and imports of capital of all companies and associations of the mining sector, producers and exporters of diamonds and other mineral resources, shall be compulsorily carried out through banks domiciled in the country” (Notice no. 13/99).¹³

Finally, in 1999 the Kwanza was introduced as the national currency, replacing the 'Kwanza Reajustado'.¹⁴ With the new currency, the Angolan government vowed to restore trust in the national currency after many years of hyperinflation had weakened the public's confidence in the domestic financial system and the overall economy (Africa Confidential, 1999d). Prior to the 1999 currency changeover, conditions of hyperinflation lasted for over two years, reaching its peak in 1996 at 5,421% (Hanke and Krus, 2012; Aguilar, 2001).¹⁵ There were only three denominations of banknotes in the country, 500,000, 1 million and 5 million Kwanza Reajustado (Giedroyc, 2000). For most people, the \$100 note was the most common instrument for savings, underscoring the lack of trust in the financial system at the time and in the Angolan economy more generally (Aguilar, 2003). With the currency changeover, inflation in the country slowly started to fall (Gasha and Pastor, 2004). The launch in 1999 of short-term Central Bank bonds, named Títulos do Banco Central, further helped reduce inflation (Bureau of Economic and Business Affairs, 2009).

¹³ Similar legislation for the oil sector would only be passed in 2012, the subject of chapter 7.

¹⁴ 'Kwanza Reajustado' was introduced in 1995.

¹⁵ From the data provided by Hanke and Krus (2012) it is clear that Angola's hyperinflation period was particularly severe, lasting years whereas in several other post-communist countries, including Russia, Georgia, Kyrgyzstan, Kazakhstan, the periods were considerably shorter.

The above-mentioned reforms closed down important strategies for direct and indirect elite accumulation used in Angola in the post-Marxist-Leninist period, including the manipulation of exchange rate policy, interest rates and access to subsidized credit (Hodges, 2001). Yet the reforms also presented new opportunities for rentier activities, defined as politically mediated opportunities for obtaining wealth through non-productive economic activity (Boone, 1990, p.427). Like in 1980s Nigeria (Lewis, 1994), entrepreneurs in Angola responded to policy change by seeking new rental havens in finance and other non-tradable sectors, investing in “arrangements for appropriating wealth which has already been produced rather than in arrangements for actually producing it” (Andreski, 1983 quoted in Hutchcroft, 1998, p.19). Importantly, the 1999 reforms opened up a new role for Angola’s nascent banking sector, allowing it to venture into areas previously reserved for the state, as described above. Whilst the state-owned banks would remain extensions of government and continue with soft lending also after the 1999 reforms, the new private banks positioned themselves to profit from the liberalization that took place in Angola’s financial sector in and after 1999.

Yet whilst in hindsight the transition from one economic order to another appears sensible, at the time, moving to a renewed (even if fundamentally rentier) form of capitalism (Vallée, 2008) was not uncontroversial seeing that it came at the expense of prevailing economic arrangements through which a number of Angolan elites had benefited greatly financially (Soares de Oliveira, 2015). Further liberalization of the Angolan financial sector was not inevitable, as the next section will demonstrate. To understand what ultimately drove financial sector change at this point, we need to take a step back and ask what is likely to have motivated and emboldened political leaders to change the rules of the economic game in 1999 after having delayed the abolition of administrative measures for several years.

3. Explaining political leaders' changed mind-set

Accounts of why countries initiate reform programmes are frequently linked to political leaders responding to financial crises (Lewis, 2007). This was indeed the case in the previous chapter where I argue that a fall in oil prices in the mid-1980s coupled with years of unsuccessful socialist economic planning left the Angolan state with high indebtedness and a low level of revenue in the early 1990s. The authorities were thus left with little choice but to employ a policy stance reflecting the preferences of the IMF and other major financiers (Dowden, 1987). When oil prices fell from \$25 per barrel in early 1997 to below \$10 in 1998 (BP, 2017), Angola again faced major economic challenges. The shortage in foreign exchange earnings, resulting from the fall in export earnings, was moreover amplified by the return of the government to all-out war against UNITA in December 1998 (Africa Confidential, 1999c).¹⁶

As if the economic situation was not grave enough, by the late 1990s Angola's relationship with the IMF was under serious strain. Tellingly, in 1999, Africa Confidential (1999a, p.6) reported that, "Western governments, and Washington in particular, have been pressing the International Monetary Fund to be kind to Angola." Since 1995, the IMF and the Angolan government negotiated two staff monitored programs but these fell through due of lack of high-level approval on the Angolan side (Hodges, 2004).¹⁷ One of the IMF programmes lasted only a few weeks (Africa Confidential, 1999a). The World Bank was at the time similarly frustrated by the Angolan leadership's lack of commitment to peace and economic

¹⁶ The return to all-out war marked the end to the peace process that began with the Lusaka Protocol in Zambia in November 1994 (Messiant, 2007).

¹⁷ The staff monitored programme of 1995 was agreed upon but later abandoned by the Fund. A new staff monitored programme was negotiated in 1998 but never signed (Hodges, 2004).

reform, holding back \$1 billion in assistance (Cilliers and Dietrich, 2000).¹⁸ Angola’s poor relationship with the international financial institutions (IFIs) meant that foreign financing was increasingly difficult for the government to access whilst commercial lending was already restricted because of the country’s meagre repayment record (Africa Confidential, 1997). In 1999, almost half of Angola’s debt stock was in arrears (IMF, 2000).

Yet for reasons I will now elaborate upon, neither economic crisis nor external pressure from IFIs and western donors is sufficient to explain the political will to reform that emerged in the late 1990s, paving the way for further financial sector change and liberalization. Firstly, economic performance had already been poor for several years. Whilst the economic crisis of 1998-1999 was devastating (Hodges, 2001; Shaxson, 2009), the country’s low levels of foreign exchange reserves, often held up as a main reason for reform onset, was actually lower in the years prior to 1999 (IMF, 2003b). Moreover, looking at the ratio of gross international reserves weighted by imports of goods and services in Angola compared to the average for similar African countries, it is clear that the situation in the country had been grave for a number of years and not only in 1999 (Table 5.1).

Table 5.1: Ratio of international reserves to imports

	1997	1998	1999	2000	2001	2002
Angola	1,83	1,17	1,91	4,57	2,65	1,12
Average Other Countries ¹⁹	7,42	5,77	4,86	6,59	7,46	7,99

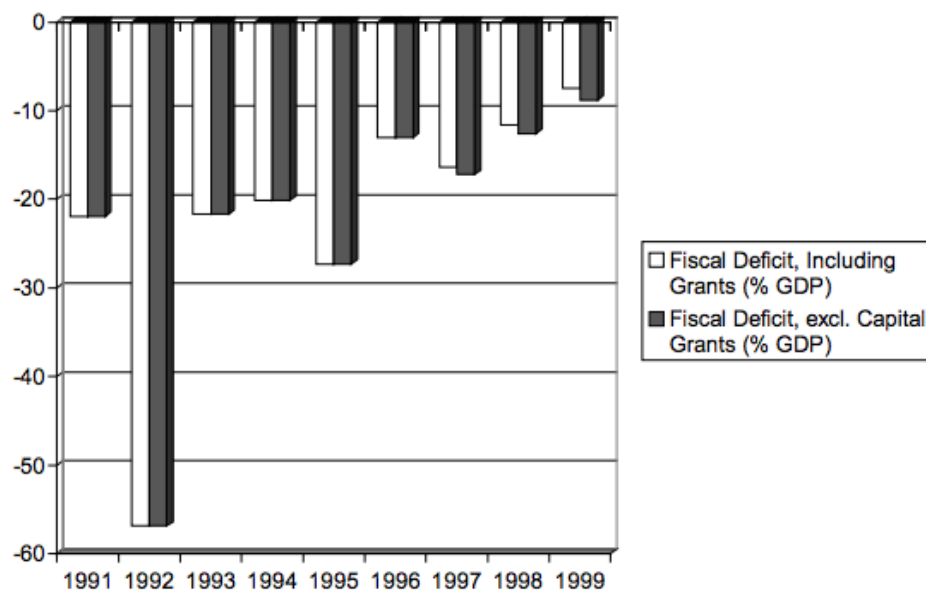
Source: IMF (2003b)

¹⁸ The occurrence happened as the IMF and World Bank were starting to push a more explicit political agenda in their lending activities. At the time, the President of the World Bank, James David Wolfensohn, talked about the need to fight “the cancer of corruption” (Africa Confidential, 1996).

¹⁹ Other countries include Algeria, Burundi, Ghana, Guinea, Nigeria, Rwanda and Zambia.

The fiscal deficit, whilst it was still substantial in 1999, had shrunk considerably compared to its early 1990s levels (Graph 5.1).

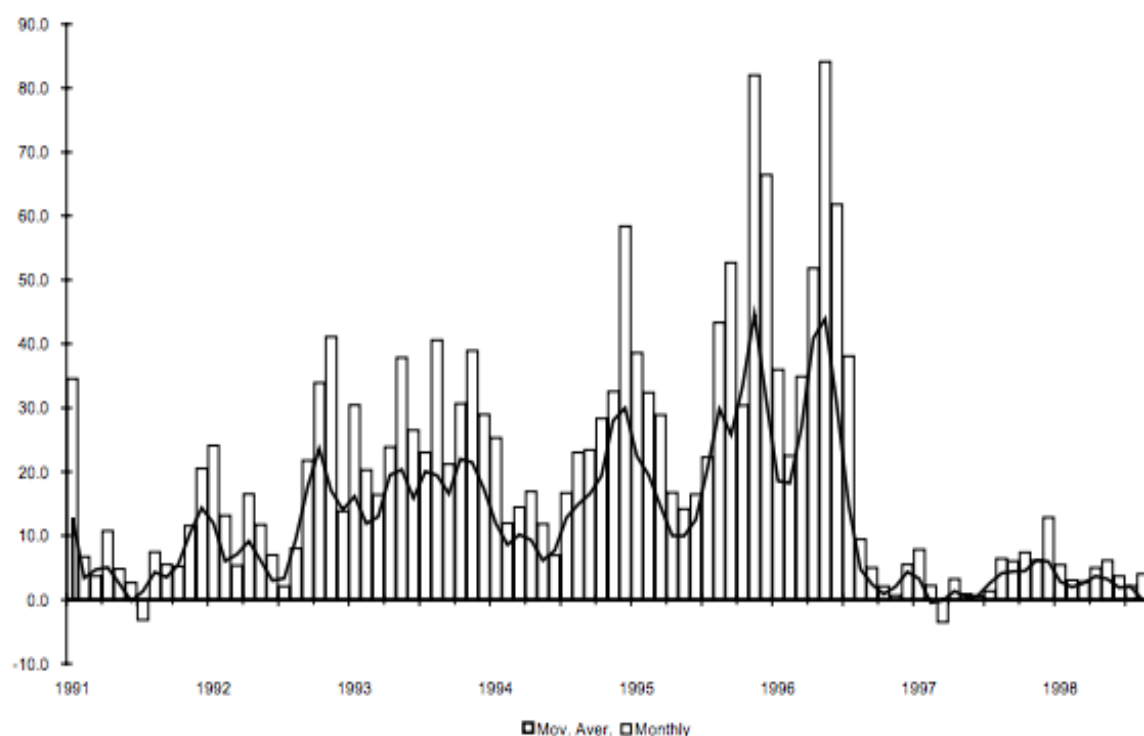
Graph 5.1: Public fiscal deficit, 1991-1999



Source: Aguilar (2001).

Angola had witnessed three hyperinflationary episodes since 1990, the latest in 1996 when inflation reached 5421%. By 1997, inflation had started to fall, maintaining a downward trend (Graph 5.2).

Graph 5.2: Inflation (monthly percentage change), 1991-1998



Source: Aguilar (2001).

The point I want to make here is that whilst the economic situation in Angola was dismal in 1999, it is not clear that the year stands out as unparalleled in comparison to previous years. Considering economic performance over the decade, it is clear that the economic situation was bad for several years. As noted by Aguilar, already at the “end of 1997 and beginning of 1998 it became increasingly clear that the mentioned instruments [harder cash controls in fiscal policy and a relatively pegged exchange rate] were close to exhaustion. There were delays in the payment of wages and the accumulated arrears in domestic debt had increased. The kwanza had appreciated and the international reserves were at very low levels” (1998, p.25). Why political leaders chose to enact considerable liberalization

measures in 1999 and not sooner is therefore not clear when looking at the economic situation alone.

What is more, the dire economic situation is likely to have been offset somewhat by the spectacular oil finds off Angola's coast (Africa Confidential, 1998). As argued by Dafe (2017), an increase in a government's resource revenues is expected to undermine the power of financiers whilst enhancing government's policy space. In the late 1990s Angola, along with other West African countries, became the centre of increasing oil-exploration activity, forming part of what became known as the "Golden triangle" of deep-water oil together with the Gulf of Mexico and Brazil (Clark, 2009, p.77).²⁰ Beginning with the discovery of the billion-barrel Girassol oil field in 1996 by French oil company Elf Aquitaine, more new reserves were discovered in Angola at this time than in any other country (Shaxson, 1999b). As a result, inwards investments rose markedly. Total foreign direct investments into Angola in 1998 amounted to more than that of the three previous years combined. By 1999, the total FDI had more than doubled from 1998 (UNCTAD, 2006). Oil revenues also more than doubled from 1998 to 1999, from \$1.3 billion in 1998 to \$2.9 in 1999 (IMF, 2003b), notwithstanding the historically low oil prices in late 1998 and early 1999. Particularly noticeable were the signature bonuses²¹ received by the Angolan government from international oil companies for exploration rights. In 1999 these signature bonuses reached \$870 million (compared to \$41 million in 1998), representing an industry record.²²

²⁰ Interview, senior manager Sonangol, Luanda 5.11.2015.

²¹ Other bonuses include exploration bonus, commercial discovery bonus, first oil bonus and sometimes bonuses delegated to particular social and development projects (IMF, 2003b).

²² Bonus payments started increasing significantly in the 1990s as IOCs started competing for a limited number of oil fields (Van Niekerk and Peterson, 2002).

New oil discoveries did not only bring increased foreign investments to Angola. The oil sector was also pivotal in ensuring the Angolan state had access to new external loans from international syndicates in lieu of official financing.²³ Following the resumption of war in 1993, national oil company Sonangol was the sole channel through which the government could access fresh external financing as international lenders lost confidence in the guarantees offered by the BNA.²⁴ The company had successfully “carved out its own area of credibility in international financial markets”, securing “fresh loans based on the promise to repay them with oil cargos” (Shaxson, 1999a). These oil-backed loans remained heavily subscribed throughout the war, indicating the ability of Angolan authorities to access financing through Sonangol, should they desire (Shaxson, 1999a).

Considerable oil wealth and the opening that greater revenues from the oil sector presented to unconditional oil-backed financing suggests that the IFIs and donors were less influential in the Angolan of the late 1990s. The Angolan authorities were not reliant on financial assistance from the IMF, as evident by the fact that the two staff monitored programmes negotiated earlier did not involve financial contributions from the Fund (EIU, 1999a).²⁵ It was clear that the authorities had developed a preference for relying on expensive short-term debt rather than agreeing to the conditionality of the IFIs (Africa Confidential, 1999a). Based on the evidence presented here it is therefore deemed unlikely that economic reforms, including financial liberalization, were the result of the MPLA government having their hands tied, as insinuated by amongst others Hodges (2004) and Shaxson (2009). If anything, the developments discussed here — including a number of substantial oil discoveries – should have made reform less urgent than it would have been during the early

²³ Due to continuous defaults on these loans and its inability to pay arrears.

²⁴ Interview, senior civil servant Ministry of Finance, Luanda 30.9.2016.

²⁵ If successfully implemented, the six-month staff monitored programme could lead to an enhanced structural adjustment facility, which would include funding (EIU, 1999a).

or mid-1990s, as the government gained increased leverage over international actors. Indeed, by the time the financial sector changes discussed in the first part of this chapter were implemented in the summer of 1999, the EIU reported, “the rise in oil prices and a new injection of funds from loans and signature bonuses have removed the sense of urgency” (EIU, 1999c). In the remainder of the chapter I will contribute an alternative explanation to this renewed emphasis on reform in the financial sector.

4. Paving the way for financial sector expansion

Whilst earlier accounts emphasize Angolan political leaders’ lack of choice when it came to the reforms of the late 1990s due to financial constraints, the enhanced fiscal position that the country found itself in at the time – in the wake of substantial oil discoveries – makes it unlikely that the latter explanation is sufficient. Rather, as the previous section demonstrated, as revenues to the state increased following the oil discoveries, the state could more easily access external financing, including oil-backed loans. Elsewhere, greater access to resource revenues have been shown to bestow political leaders with greater policy autonomy, which sometimes leads them to act at odds with the wishes of external financiers (Dafe, 2017).²⁶ Instead of the change being forced on them, I argue that Angola’s political leaders chose to reform monetary and financial policy towards greater stability and openness in 1999, paving the way for financial sector expansion. The question is why and the answer I propose is linked to shifting political circumstances.

²⁶ Dafe (2017) shows this to be the case in Nigeria in the early 2000s when political leaders used the increased revenue and enhanced policy space to promote more expansive financial sector policies against the recommendations of the donors and creditors.

4.1 Elite interests changing

As the following section will show, budding aspirations amongst Angolan elite members to move beyond more primitive forms of rent seeking became evident from 1996-97. Following initial liberalization of the economy in the early 1990s, by the end of the decade, Messiant (2001, p.295) described a situation where “very few beneficiaries [of state largesse] are content only with redistributing or reselling on the informal market those assets which come their way”. As had been the case in other transition economies, ‘the winners’ of the initial phases of reform were prepared “to give up a concentrated stream of rents generated by the initial market distortions for a share of the overall efficiency gains associated with further market reforms” (Hellman, 1998, p.220). A 2005 Chatham House report corroborated the existence of such a tendency, describing how “forward-thinking members of the élites” saw the inherent limitations in the current arrangements and acknowledged that change was inevitable (Vines et al., 2005, p.13).

Notable members of Angola’s elite had begun voicing their disapproval of the short-termism typifying economic policy at the time. As the following public records demonstrate, short-termism was seen as impeding Angolan business prospects, sometimes even hurting them. In 1997, then director of state-owned bank BPC and former BNA official, Amilcar Azevedo da Silva, stated, “We at BPC believe that the system is excessively closed. It needs to be modernized in order to be able to respond to the boom that will necessarily follow the conclusion of the peace process”. He continued, “In the not very distant past we had serious credibility problems and we have to restore it. Without it, the system will be unable to develop”. And finally, speaking to the benefits of modernizing the sector, “Credibility is the key to promoting foreign investment, increased modernity, increased dynamism, and means that exchanges take place faster and more easily. The flow

of goods and money is also faster and more intense” (Da Silva, 1997). Speaking with the Times in 1997, former Minister of Planning José Pedro de Moraes and director at the IMF (and soon to be Minister of Finance) similarly recognized that measures were needed in order to further normalize the economy and the financial sector. Such reforms, he argued, were necessary to "mobilize domestic and external resources to close the financial gap" (Lavrador, 1997).

As a final example, consider the statement by the then Chairman of the Board of Directors of Angola’s first domestic private bank, Aguinaldo Jaime, on the 25 January 1999, four days before his reinstatement in government as governor of BNA (having previously served as Finance Minister). Jaime insisted on the need to establish a “modern efficient financial system in Angola in which indirect control predominates, thus shifting the decision making from the state to the banks and corporates, as is *normal* in a two-tier system” (BAI, 1999, p.2, emphasis added by me). In BAI’s annual report, the bank raised concerns over the Angolan government’s prevailing short-term policy stance, which it believed hurt the bank’s development prospects. “There is no doubt that variables such as the exchange and monetary policy and the political-military situation do not create a favourable environment for the development of our activity, and may even be considered restrictive for the normal expansion of the Bank’s activity” (BAI, 1999, p.3). “Angola needs to improve the use of the banking system, so that the banks that operate in Angola, amongst which BAI is the most recently incorporated, can operate in the monetary, financial and foreign exchange markets, together with depositors, borrowers and those clients requiring foreign exchange transactions” (1999, p.6). Conclusively, the report noted “the prospects for BAI for 1999 are entirely dependent upon the priorities of economic policy pursued within the key-areas of economic stabilization and recovery”. It also commented on the ability of the bank to

make an institutional contribution in this regard, drawing on its know-how and international network (1999, p.19).

The elite's call for a normalization of the economy did not emerge independently of the state. The persons quoted above all benefited from strong political connections when they made the above comments and are likely to have channelled evolving views at the summit of power. All had previously held positions of decision-making power, either through working for the BNA or in the ministries. Both José Pedro de Morais and Aguinaldo Jaime were leading figures in the reform efforts of the early 1990s (Hodges, 2001). Although all had subsequently moved on to take up positions outside the state apparatus, in the state-owned or private sector, they remained part of the circles of power around President dos Santos (Africa Confidential, 1999c).²⁷

It is therefore not surprising that the above appeals from elite members were very much in line with the evolving thinking inside the presidency itself at the time. As one observer noted in May 1998, "The rhetoric of the GOA [Government of Angola] has radically changed over the last ten years. The previous emphasis on a planned and tightly controlled socialist economy has been replaced by one giving emphasis to an open, market-oriented economy of a capitalist nature" (Kyle, 1998, p.19). Key documents in this regard were the Economic and Social Policy Program of Government for 1997²⁸ and Medium-Term Program for Economic Stabilization and Recuperation 1998-2000²⁹, also known as the Medium-term program (Aguilar, 1998). Especially the latter programme emphasized the

²⁷ As has been the typical political configuration in post-independence Angola, elite members are often circulated within the system of power but they are seldom completely removed from it.

²⁸ Programa de Política Económica e Social do Governo para 1997.

²⁹ Programa de Estabilização e Recuperação Económico de Médio Prazo 1998-2000.

government's intention to redirect the economy towards a market-oriented system (Aguilar, 1998).

The Presidency and top government officials were also indicating that they were growing wary that prevailing economic arrangements were getting out of control. At an MPLA Central Committee meeting in February 1996, President dos Santos criticised the “wild capitalism that has taken root in the country over the last three years”, insisting on greater regulation of the economy (quoted in Marques de Moraes, 2012, p.5). In an address to the nation that same year, the President called for transparency in government alongside measures to prevent corruption and influence peddling. He promised that he would “put a definitive end to high-level crime, to organized theft and to the pillaging of state assets” (quoted in Marques de Moraes, 2012, p.5). The concerns expressed by the President echoed that of other government officials. Upon his inauguration, as central bank governor in 1997, Sebastião Lavrador commented, “The state had no control over the [foreign exchange] rate, nor the possibility to intervene in the market” (Lavrador, 1997). He continued, “When I took over [as governor in 1997], I confirmed what I already suspected before – that the balance of payments was totally out of touch with reality all those years. A billion dollars' worth of goods would enter the country, but there would be no registers because all the payments would take place outside the financial circuit” (Lavrador, 1997).

It was not just the rhetoric of government and elites that started to change in disapproval of short term schemes. Private investment was also increasing, mainly in the oil sector but also elsewhere, reflecting a shift in attitude towards a more long-term perspective

(Aguilar, 2001). Whilst economic activities continued to be rentier in nature,³⁰ the new strategies differed from those of the war economy of the 1990s in important ways.

Whereas in the early 1990s, strategies of elite accumulation involved minimal investments in the domestic economy, from the late 1990s onwards, the elite started channelling accumulated wealth into new domestic ventures, although slowly (Hodges, 2004; Ovidia, 2013).

Investments throughout the 1990s were largely directed to the services sector and activities connected to imports (Aguilar, 2001). In 1997, Angola's first two private banks were established, BAI³¹ and Banco Comercial Angolano (BCA). Both banks had financial backing from the state, either as an official partner (BAI) or under the table (BCA) (BAI, 1999).³² BAI was at the time of establishment 37.5 % Angolan owned with local private entrepreneurs amongst its owners; national oil company Sonangol was the main owner with 17.5 % shares alongside state diamond company Endiama with another, albeit smaller share (1.5 %) (Times, 1997a). BCA, on the other hand, had no state enterprises amongst its shareholders but counted prominent Angolans amongst its owners (EIU, 1999b), including former central bank governor Sebastião Lavrador, former MPLA Secretary Lopo do Nascimento and an ex-Prime Minister, José França van-Dúnem (Africa Confidential, 1999a). When asked where the initial capital of shareholders came from, a former shareholder of the bank confessed that it had been granted to private individuals by the state and more specifically, by “caixa numero dois [the second treasury]”, signifying Sonangol. He specified that “Sonangol was instructed to give

³⁰ I follow Boone (1990, p.426) when I use ‘rentier in nature’ to imply the failure to invest in “productive activities (that is activities that create surplus value through the on-going combination of capital and wage labour, such as industry or capitalist agriculture)”

³¹ Banco Africano de Investimentos changed name to Banco Angolano de Investimentos in 2011 (International Banker, 2017).

³² Interview, former BNA vice-governor, Luanda 28.9.2016

money”.³³ In the banking sector, like in other sectors,³⁴ it appeared as if individuals were thinking more long term than in earlier years, and wanted to secure a stake in the new ventures. Often this was done with the aid of official resources.

The analysis so far suggests that from 1997 there was considerable momentum towards modernizing segments of the economy and removing the most cumbersome administrative controls, which amongst other things hindered financial sector expansion.³⁵ Judging on the evidence presented thus far, there was a growing consensus among the ruling elite by the late 1990s in favour of further liberalisation of the economy, even when this meant ending partial reform arrangements and associated loopholes that had proven immensely profitable for a privileged few. The truth of it was that the short-term survival strategy that had dominated decision making throughout the 1990s, which had made these partial reform arrangements possible, had also meant that the economy had remained significantly below potential (Hodges, 2001).³⁶

Yet despite the notable shift in rhetoric and to a lesser extent economic activity, the prevailing economic arrangements persisted, in effect deterring the expansion of the financial sector. As noted, the administrative arrangements discussed here did not end before 1999. Therefore the reform initiatives in 1997-1998, whilst promising to ease administrative measures and restore macroeconomic stability, did not bear fruit. Described as the first reform programme embracing a medium-term horizon, the 1998 reform

³³ Interview, banker previously in Angolan public bank, Luanda 20.9.2015. Interview, professor public university, Luanda 22.10.2015.

³⁴ As described by Birmingham (2002, p.184) “Officers invested their wealth in Luanda’s housing market, earning large fortunes as landlords to foreign employees of oil companies, diplomatic missions and international aid agencies”.

³⁵ It is important to note that full modernization and deregulation was never the objective, as the state would continue to assert considerable control over the economy, as we will see in the forthcoming chapters.

³⁶ Please refer to the chapter 4 for an overview of these arrangements.

programme like previous programmes was characterized by sudden shifts and lack of any political backing from the higher echelons of the ruling coalition (Hodges, 2004). As noted by Aguilar, “the government is still reluctant with regards to the issue of economic reforms, prioritizing administrative controls” (Aguilar, 1998, p.27).

And whilst important figures within the government and in non-state elite circles called for modernization of the economy at the time, the reforms were not undisputed. Importantly, this suggests that contrary to the sentiment that was presented in the official discourse, senior people in the higher echelons of the ruling coalition were still sceptical of putting an end to the partial reform measures from which they continued to benefit (EIU, 1999b;1999c). For instance, economic liberalization measures formulated in 1998 aimed at stabilizing the economy, including a staff monitored programme with the IMF, was abandoned due to “presidential objections” (Hodges, 2004, p.107). The EIU attributed the opposition to the fact that President dos Santos was “trained in the Soviet Union” and thus “remains sceptical of the merits of market-based reform” (EIU, 1999b). However, the President was not the only one hostile to restructuring the economy. A stepwise devaluation of the overvalued Kwanza, declared by the Minister of Finance in early 1998 in an effort to tame inflation, was similarly blocked by the Council of Ministers. In addition to the President, members of the Council of Ministers were amongst the few people who could access foreign exchange at the official price (The Economist, 1998).

With centrally placed people in opposition to broader economic reforms, the government appeared reluctant to take the political risk that upsetting their supporters would represent. In 1997-1998, Angola was oscillating between war and quasi-peace. The war against UNITA rendered the government vulnerable to a violent overthrow (Birmingham, 2002).

UNITA controlled large segments of the diamond trade, allowing the party to maintain substantial military strength (Comerford, 2005). The unstable situation facing the MPLA was augmented by rising discontent within the party itself, especially in the cities, which was the party's main support base (Hodges, 2004). Concurrently observers spoke of "discontent with the MPLA government increased inside and outside of the party as well as within the army" (Croese, 2017, p.89).³⁷

The insecurities that the ruling party faced at the time can help explain why political leaders were hesitant to act on any economic reforms that could risk upsetting the distribution of resources to its core supporters. From a political perspective, reform is likely to have appeared politically unsafe. As Khan (2010) points out, the strength of excluded factions depends also on whether ruling coalitions are able to keep their own supporters satisfied within it, in order to prevent supporters from defecting to the opposition. With signs of rising discontent amongst MPLA supporters (Croese, 2017, p.89), political leaders were disincentivized from making any changes that could potentially upset their supporters.

The vulnerability that Angola's ruling coalition suffered at the time presents a conceivable reason why the precarious economic situation of the 1990s was allowed to prevail for as long as it did, despite a growing consensus from 1997 onwards in favour of reform. Multiple threats from different fronts are likely to have shortened the time horizon of the MPLA and its leadership (Horowitz, 2003). The damaging monetary and financial policy prevalent in the country during the 1990s speaks to the latter being the case as political leaders had few incentives to think beyond the short-term. Discussing the experience of developing countries in general, Barma et al (2010) show how political leaders who believe

³⁷ A tendency also noted by The Economist (1998).

the risk of being removed from office is high often discount the future because they do not necessarily bear the long-run economic consequences of their choices. Accumulating unsustainable amounts of debt and using inflationary policies are examples of such short-sighted thinking (Cukierman et al., 1992). Both policies were frequently used in Angola during the 1990s. One can even draw parallels to Mancur Olson's (1993) portrayal of the 'roving bandit', favouring a smash and grab approach to the economy with little care of its negative effects. Whereas the Angolan political system was considerably more stable than the archetype that Olson describes — the at times turbulent Nigerian political system being perhaps a clearer case for Olson's typology (Lewis, 2007) — the point is that the continual threat that the country's ruling coalition faced for much of the 1990s meant that political leaders were not encouraged to secure more resources than were necessary for their immediate survival, with the result that damaging economic arrangements prevailed. It was not before 1999 when the political circumstances changed that President dos Santos and his government were presented with the conditions on which it was safe to pursue reforms.

5. Changing political circumstances

By late 1998, the dynamics of conflict in Angola had changed considerably. Addressing the December 1998 Party Congress, President dos Santos stated that the only way to peace was war, calling for "the total isolation of Jonas Savimbi and his movement" (dos Santos quoted in Human Rights Watch, 1999, p.28). By this time, the political and diplomatic leverage of MPLA had significantly increased (Messiant, 2001). In 1999, Messiant (2001, p.291) described how "Angola's [foreign] partners had clearly understood, as had Angolans themselves, that the MPLA's grip on power was a firm one, and that anyone wishing to pursue an interest – including some of great importance – was obliged to deal with the

party". UNITA, on the other hand, was increasingly losing ground. Even if the party still controlled significant rural areas in 1998, the loss of foreign allies, diminishing control over diamond resources and tightening of sanctions increasingly alienated the movement both economically and diplomatically (Le Billion, 1999). The UN Security Council sanctions of 1993 and 1997 moreover froze the movement's financial assets, diamond trade, and international travel and representation.³⁸ UNITA members who had agreed to take up their seats in the National Assembly in Luanda, following the signing of the Lusaka protocol in 1994, were either co-opted by the MPLA or gradually forced out (Human Rights Watch, 1999; Hodges, 2004). The combined effects of the militarization of government policies and isolation of UNITA allowed the Government forces to take over opposition strongholds in the central highlands by the autumn of 1999. By that time, an estimated 80 % of UNITA's military power had been destroyed (Tvedten and Nordås, 2000). It was clear that, at a heavy cost, the war had turned in the MPLA's favour.

In parallel with MPLA gaining the upper hand in the conflict, the ruling party was reasserting its power over core constituencies in the urban areas (Croese, 2017). In a process which had already been ongoing for much of the 1990s, greater powers were vested in the executive branch exceeding the already strong presidential power bestowed by the 1991 constitution (Tvedten and Nordås, 2000). Angola transformed from a "single party state with a disaffected opposition thinly scattered in the provinces and abroad" to becoming a "presidential state in which power emanated from the palace" (Birmingham,

³⁸ In September 1993 UN Security Council resolution 864 established an arms embargo, as part of a package of sanctions, intended to prohibit all supplies of arms and related materiel to the UNITA organization including weapons and ammunition, military vehicles and equipment and spare parts for the aforementioned. In the resolution, the Security Council condemned actions by UNITA that contravened the peace accords while praising the steps taken by the Government of Angola to implement the same accords. From 1998, the UN extended the sanctions to cover UNITA's diamond trade, recognizing the role of diamonds in the continuation of the war. The UN also banned travel to UNITA areas. (BBC News, 2000).

2002, p.177). Openings for effective opposition to the party disappeared following the resumption of war in 1998 and tougher media laws made criticising the party and its leadership increasingly difficult and dangerous (The Economist, 2000). Finally, at the 1998 Party Congress, high-ranking MPLA figures, including party secretary Lopo do Nascimento and former prime minister Marcolino Moco, were side-lined, in a bid to fortify the standing of dos Santos' faction. Prime Minister Fernando França Van-Dúnem was dismissed as prime minister and the position vanished with him, representing a strengthening of the executive's position (Action for Southern Africa, 1998).

In light of the above-mentioned changes, as the millennium approached, the MPLA found itself in a position where threats against the party and its leadership had significantly decreased. In such a situation, where threats to the ruling coalition from excluded factions decline, political leaders are likely to adopt a longer-term perspective (Khan, 2010). Actors with long time horizons are in turn expected to commit to longer-term agreements, typically seen as fundamental for economic growth (Barma et al., 2010).

Whereas earlier it was claimed that Angolan political leaders discounted the future, given that the risk of being removed from office was high, by late 1998-99 the time horizon of President dos Santos appeared to have grown. The first sign of political leaders extended time horizon was the appointment in January 1999 of a "heavy-hitting" new economic team tasked with cleaning-up the economy (Africa Confidential, 1999b). At the helm of the team was Finance Minister Joaquim David, previous director general of state oil company Sonangol between 1989 and 1998. David was reportedly chosen over a dozen other candidates on account of his positive standing amongst foreign firms (Africa Confidential, 1999c). Throughout his time at Sonangol, which represented a significant chunk of the civil

war, the company had “provided the conditions in which operational companies could make technical decisions with confidence that political interference would be minimal, which encouraged foreign operators to make massive long-lived capital investments” (Heller, 2012, p.837). Whereas shifting policy priorities stifled other sectors of the economy Sonangol remained focused on international business, staying clear of “domestic policy fads”, as discussed in chapter 3 (Soares de Oliveira, 2007, p.600). The new government were keen to spread the ‘Sonangol-model’ to other parts of the economy (Soares de Oliveira, 2015, p.136) and the appointment of Joaquim David facilitated this.

The credibility of the government’s reform commitment was further underscored by the appointment of Aguinaldo Jaime as BNA governor (Africa Confidential, 1999b). Like David, Jaime enjoyed a good reputation in international circles, having served as Chief of Staff at the African Development Bank before returning to Angola in 1996 to launch BAI on behalf of a group of international investors (Times, 1997a). Finally, Ana Dias Lourenço (the wife of dos Santos’s successor, President João Lourenço), “well- regarded in the IMF and World Bank's Washington headquarters” (Africa Confidential, 1999b, p.5), joined David and Jaime as minister of planning.

With the new economic team in place, all esteemed by foreign investors and IFIs alike, the MPLA ruling coalition was in a position to make the longer-term vision a reality and within few months the reform programme to liberalize the financial sector was underway. Within their first year in office, the reformers had scrapped the fixed exchange rate as well as the fixed interest rate and opened up for greater competition in the financial sector.

With the threat of excluded factions declining, the risk of alienating supporters within the movement represented less of a danger to the leadership of dos Santos and few avenues existed for voicing popular frustrations (Messiant, 2001). More importantly, people increasingly recognised the “tremendous and reliable advantages of staying in the party-state compared with the uncertain and cash-poor existence of dissidents or challengers” (Soares de Oliveira, 2015, p.99). The joint interest of elites emerging in favour of the established political order granted considerable power to dos Santos. Importantly, it allowed the president with his new government to discontinue the economic arrangements of the 1990s, which an increasing number of people were coming to see as a hindrance to economic expansion. After 1999, “The government had more financial breathing space and could sponsor new economic ventures” recalled a manager working at Sonangol at the time.³⁹ As corroborated earlier in the chapter, the drive to modernize the economy was not new but had developed over a few years. What was new was that by 1998-1999, due to changed political circumstances, the political leadership had the necessary political clout to carry out the necessary reforms. It was in this new political context that president dos Santos and his team decided to go ahead with reforms and lay the foundation for the expansion the financial sector.

6. Conclusion

In this chapter I continued to probe the question of what drives institutional change in the financial sector by looking at the financial liberalization that took place in Angola in the late 1990s. The chapter started by establishing the relevance of the reforms for financial sector expansion in the country. Whilst the reforms put an end to dominant forms of elite accumulation, at the same time they opened up new avenues for accumulation. Specifically,

³⁹ Interview, manager oil service company, Luanda 3.11.2015.

banks went from being loss making businesses, concerned chiefly with redistributing a limited amount of foreign exchange and credit, to being able to take part in activities previously a state preserve, including foreign exchange transactions, deposit gathering and buying treasury bonds. As will be further elaborated upon in the coming chapters, whilst openings for private individuals to benefit from state resources grew the opportunities continued to be available to a select few.

The remainder of the chapter then dealt with the question of what prompted political leaders to instigate financial sector changes in 1999. I questioned earlier accounts focusing on economic adversity as to why president dos Santos and his advisors chose to initiate reform at this time. Rather I argue that the political leadership were not pressured to instigate changes as they had been in the late 1980s and early 1990s. I argue that President dos Santos and his team chose to instigate financial sector changes because there was a growing sentiment that the current economic arrangements were holding the ruling coalition back, possibly hurting their prospects. Reforming the financial sector, primarily by introducing financial sector liberalization measures, helped the MPLA ruling coalition to strengthen their power by improving the economy, whilst also providing new avenues for enrichment to the ruling elite. The chapter helps substantiate the overall argument of the thesis that financial sector change is not only a sign of weakness but can also be initiated when political leaders find themselves in a position of strength, in turn allowing them to take a longer-term view. Specifically, it was when the MPLA gained the upper hand in the conflict against UNITA that President dos Santos authorized the new government to go ahead with reforms that facilitated financial sector advancement. Changing the strategy for elite accumulation had become politically feasible and, as we will see in the next chapter, laid the foundation for financial sector expansion in peacetime.

Chapter 6

Uneven development in boom time, 2002-2009

1. Introduction

The last chapter focused on the drivers of the 1999 financial sector changes, arguing that it was in the interest of a politically stronger ruling coalition to initiate financial sector reform towards greater stabilization of the economy and away from the arbitrariness that ruled the financial sector in the 1990s. This chapter seeks to take stock of the characteristics of Angola's modern financial sector and describe the purpose that the sector served in the country from 2002 until 2009. 2009 serves as a cut-off point for the analysis in this chapter because it was the year that the impact of the global financial crisis of 2008 really hit Angola, causing a balance-of-payment crisis in the country. Whilst economic growth did resume in Angola after 2009, the financial sector came to play a somewhat different role in the country's economy following the crisis. The period after 2009 will be treated separately in the next chapter.

Examining Angola's financial sector from 2002 until 2009 is important in order to establish why it would be in the interest of the MPLA ruling coalition to establish a basic functioning financial sector, as it runs counter to the expectations of existing political economy of finance studies reviewed in chapter two. Moreover, by establishing how the financial sector in Angola post-2002 served a political purpose, one gets closer to understanding why the sector ended up looking like it did; heavily focused on banking and with minimal emphasis

on non-banking institutions. Sparked by an unprecedented GDP growth surge,¹ the assets of Angolan banks mushroomed from \$3 billion in 2003 to an estimated \$35 billion in 2008 (Wallace, 2014; Angop, 2010a). In stark contrast to the growth of the banking sector was the virtual absence of a non-banking financial sector, most notably capital markets (beyond the primary market for public securities) but also insurance companies, pension fund management companies, and microcredit institutions.² I argue that the latter features of the financial sector have three interconnected explanations.

Firstly, in post-2002 Angola, politically powerful people needed to be accommodated within the new post-war economic order.³ Banking was particularly attractive due to its low start-up cost and potential rewards.⁴ Yet access to such opportunities needed to be carefully controlled so as not to risk the emergence of an autonomous business class not beholden to President dos Santos or the ruling party.⁵ The development of credit and of debt capital markets in particular has been shown to strengthen public participation in economic activity elsewhere, for instance in the Middle East and North Africa region (Snaije, 2017). I argue that the need to regulate entry to the financial sector skewed the ruling coalition in favour of banks as opposed to non-bank financial institutions. In the former, restricting entry is easier. Restricted entry into the banking sector moreover ensured that bank profitability remained high. In the case of non-bank financial institutions, conversely, such as a stock exchange, the very idea of controlling ownership defeats the

¹ Angola's post-2002 growth spurt was not only unprecedented in the country's history but was also exceptional from a comparative perspective. Fuelled by one of the highest GDP growth rates in the world at the time — an average of 15.4% a year between 2003 and 2008 (Making Finance Work for Africa, 2017a).

² After several false starts, a non-banking sector failed to materialize during the 2002-2008 period.

³ Similar processes had taken place in other countries. As Boone describes in the case in Senegal, in an effort to politicize local wealth accumulation, the country's political leaders channelled the ambitions of a frustrated local private sector by creating new avenues for state-mediated rent seeking (1992).

⁴ Interview, banker public bank, Luanda 20.9.2015; Interview, former BNA vice-governor, Luanda 28.9.2016.

⁵ This point has been emphasized by Soares de Oliveira (2015).

purpose of establishing an exchange to begin with, as the buying and selling of shares of stock, bonds, and other securities is intrinsically about spreading ownership. For the purpose of accommodating political allies, non-bank financial institutions therefore had less appeal to the ruling coalition at this point.

Secondly, a central role of the banking sector in Angola's post-war reconstruction period was securing the connection to the outside.⁶ Being able to move money outside the country is likely to be important to ruling coalitions for several reasons. For one, wealth becomes easier to hide than would be the case if these monies were invested or consumed domestically. Additionally, moving funds abroad provides a form of asset protection, as domestically invested rents may be easily appropriated in the event that the ruling party was to lose power (Andersen et al., 2017). As a main concern of Angola's rich in the 2002-2008 period was to ensure outward capital flows, establishing a stock market became less pertinent as it is rather seen as an instrument for attracting capital from locals and from abroad (Moss, 2003).

Thirdly, the use of the financial system in expanding the physical reach of the state and thus mobilising support for the MPLA help explain why the financial sector in the 2000s remained skewed towards the banks at the cost of non-bank financial institutions. Here I argue that whilst non-bank financial institutions such as microfinance institutions and stock exchanges would likely better serve the poor or the economically autonomous middle-class, the MPLA was interested in building an urban middle class loyal to the regime. This

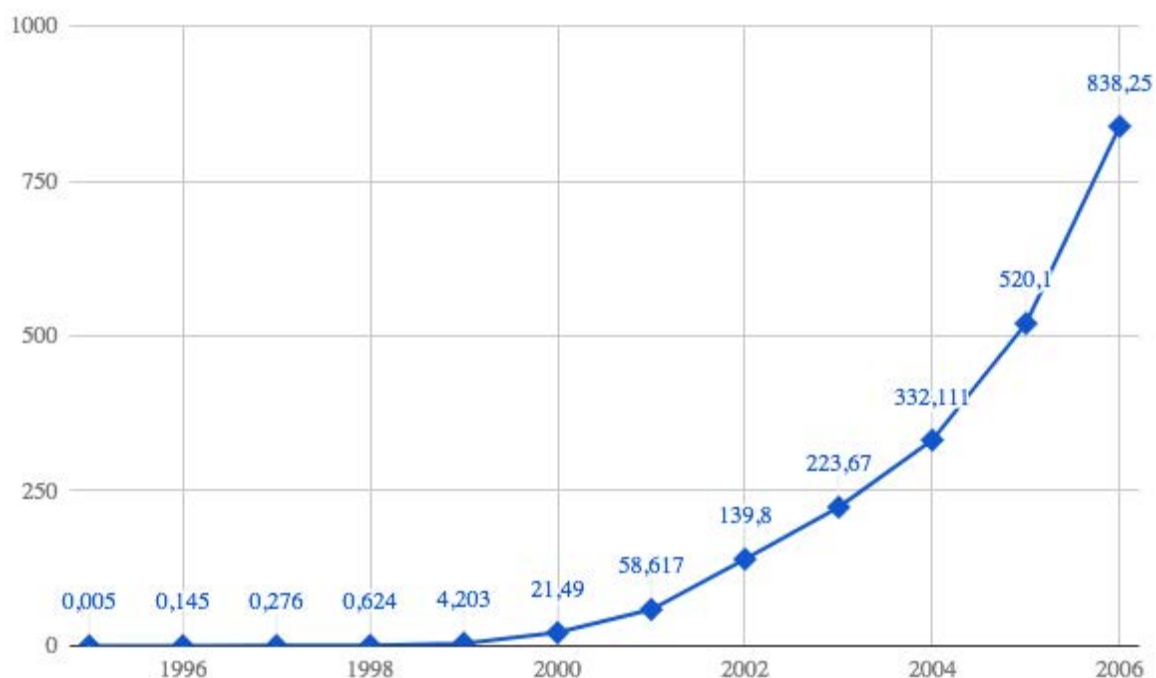
⁶ Capital outflows increased post-2002 as foreign exchange restrictions loosened (authors own calculations based on net capital outflow report by the IMF 2002-2014). Moving money out of the country is a common way in which elite members hedge against political uncertainty and the insecurity of their position. Several studies have shown how political uncertainty (Alesina and Tabellini, 1988) and weak institutions (Cerra, Rishi and Saxena, 2005) spur capital flight.

constituency could be reached through the banking system, thus decreasing the relevance of non-bank institutions. By explaining the lack of non-banking financial institutions, the chapter contributes to illuminating an issue that is not only prevalent in Angola but also in other resource-rich countries (Beck, 2010) and African countries in particular (Beck et al., 2016).

2. The rise of banks

For most of the civil war, as described in the previous chapters, the role of domestic banks was primarily to distribute public capital in ways that ensured support for the MPLA state. With the second round of financial liberalization in 1999, the banking sector was set to play a larger role in the economy. As restrictions were lifted from 1999, including on foreign exchange transactions and interest rates, the balance sheets of banks started to grow, albeit from a low base (Graph 6.1).

Graph 6.1: Total assets in the banking sector (in billions of kwanza), 1995-2006



Source: BNA (2007); IMF (2000); IMF (2005); IMF (2007)

Yet, the full effect of the 1999 round of financial liberalization would only arrive a few years later, delayed by the continuation of war and the political uncertainty that fighting produced. By 2002, Angola was still waiting to reap the full benefits from the deep-water oil fields discovered off the country's coast in the late 1990s. International oil companies continued making large deductions in their payment to the government to make up for the high exploration costs on new fields.⁷ The MPLA government was also faced with a considerable foreign debt overhang built up over years of costly fighting (Human Rights Watch, 2004).

⁷ This is known as 'cost oil'. Under a production Sharing Agreement (the main contractual agreements used by Sonangol in its associations with other companies are joint ventures) a foreign oil company will make an initial investment to explore or produce oil in a particular block, and can deduct a share of the oil that is produced and sell it to cover their investment costs. This 'cost oil' is deducted from the total crude oil that is produced in the oil block (OSISA, 2012).

It was after 2004 that the state's financial situation changed significantly. Commercial banks and bilateral credit lines against future oil revenues became more readily available. Whilst some of these loans came from western banks,⁸ which throughout the 1990s had lent heavily to Angola, a more important development was the country's new loan partnership with China. The \$2 billion loan from China Export Import Bank in 2004 marked the beginning of a number of loans that would flow to Angola from private and public Chinese entities.⁹ By 2007, China alone had provided credit lines to the country for possibly as much as \$11 billion.¹⁰ However, because of the structure of these loans, as described by Corkin (2013), there was no clear role for the Angolan financial sector. Chinese companies carried out the projects and were paid directly from an offshore escrow account, in which monies from Angolan oil sales were deposited (Corkin, 2013). Beyond the increased economic activity that these 'oil for infrastructure' loans contributed to, the Chinese loans had little direct impact on Angolan banks.

Of greater direct importance to Angola's financial sector was the growing financial muscle of the state from 2004-2005 onwards. The increase in revenues was linked to developments in the country's oil sector, which by 2004 was providing the state with significant tax revenues. Angola's oil production increased by 15% annually between 2002 and 2008, peaking at almost two million barrels per day before the global fall in oil prices in 2008.¹¹ Over the same period, oil prices rose from \$20 per barrel in 2002 to reach \$147 in July 2008 (BP, 2017; Macalister, 2008).

⁸ In 2004, a loan of \$2.35 billion was made to Angola's state oil company, Sonangol by a consortium of European banks including Barclays and Standard Charter. Repayments over five years were guaranteed from future oil production (Reed, 2005).

⁹ See Corkin (2013) for a comprehensive coverage of the relationship between Angola and China. Brautigam (2009) and Soares de Oliveira (2015) also offer interesting insights on China in Angola.

¹⁰ Exact amounts remain open to speculation (Russell, 2007).

¹¹ The production level meant that Angola was producing almost the same amount as Nigeria, making Angola the 13-14th biggest oil producer in the world. See Trading Economics (2017).

Buttressed by growing oil revenues, the MPLA regime initiated an ambitious reconstruction plan. The war had left 98% of bridges, 80% of factories, 60% of schools and 80% of hospitals destroyed and particular emphasis was placed on rebuilding the physical infrastructure of the country (Soares de Oliveira, 2015). Between 2000 and 2008, public investment per inhabitant increased from \$21 to \$665 (See table 6.1; CEIC, 2008).

Table 6.1: Public investments, 2003-2008

	2003	2004	2005	2006	2007	2008
Public investment (million \$)	281 263	86 842	1 531 447	5 403 010	7 146 106	11 901 333
Public investment as % of GDP	2,08	0,46	6,31	11,27	11,78	14,18

Source: CEIC (2009)

In the financial sector, increased economic activity driven by increased government spending soon became visible. On the deposit side, monies flowed rapidly into commercial banks from the state and the oil-service sector. However, these increases were often short-term, as the latter used domestic banks mainly for storing money in current accounts for making payments (BNA, 2007).¹² For instance, the state would pay the salaries of state employees together with the rest of the state budget through BPC, which meant that prior to the payday the bank would experience a sizeable increase on the deposit side (EIU, 2008).¹³

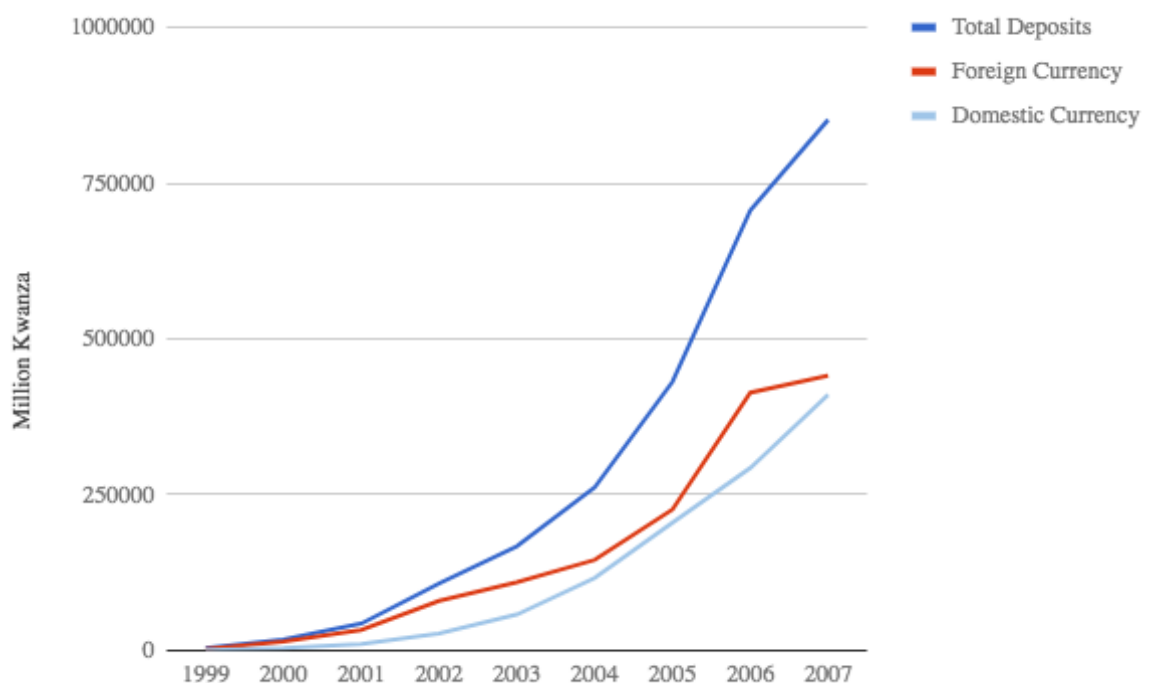
The 1999 reforms meant that banks could receive deposits in both local and foreign currency (see Graph 6.2), and the largest increase on banks' balance sheets was in foreign

¹² Following the 1999 round of legislative changes, commercial banks were permitted to establish accounts in foreign currency.

¹³ Interview, representative of international financial institute (IFI), Washington DC, 8.12.2016.

exchange deposits. The dominance of foreign exchange was not surprising given that deposits came from the state and oil service companies, which in turn received chiefly dollar-denominated revenue from the international oil companies. The disposition amongst firms and individuals towards foreign exchange was likewise prompted by Angola's history of inflation, which in 2002 was still above 100% (World Bank, 2006).

Graph 6.2: Bank deposits (in million kwanza), 1999 – 2007

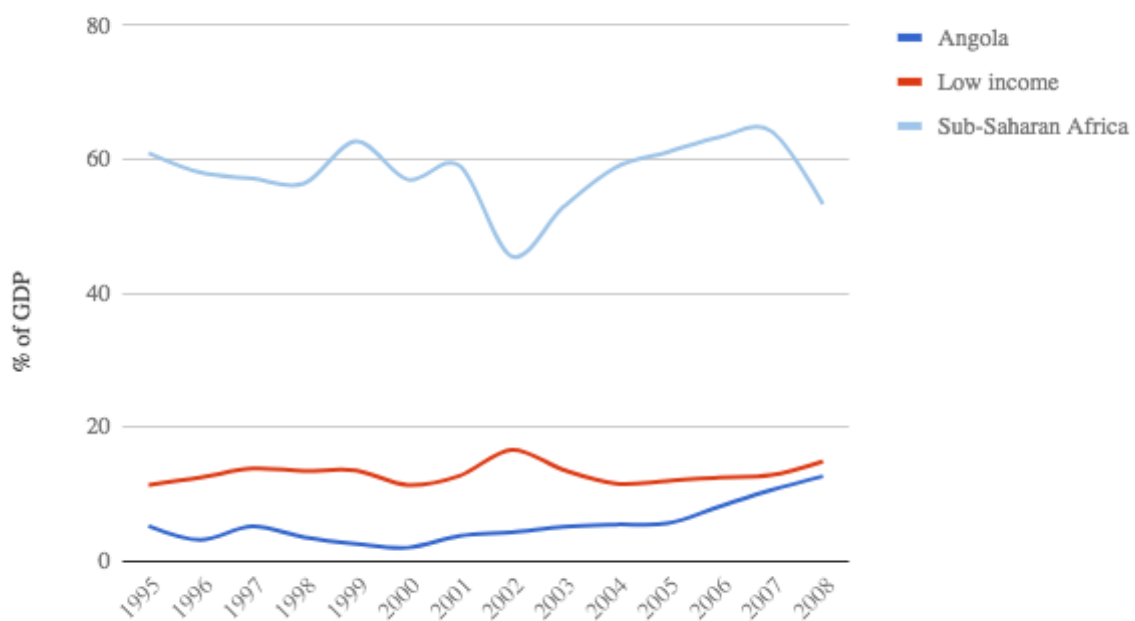


Source: BNA (2007)

With rapid economic growth and deposits accumulating, banks were left to find profitable outlets for the added financial resources. Ideally, this would mean lending more money to customers, investing in government papers, engaging in interbank lending or keeping cash holdings. But as discussed in chapter two, banks in resource rich countries are generally found to dedicate lower shares of their assets as loans to private firms and individuals (Beck, 2010). This was also true in Angola where banks often complain that the basic

framework for making credit operations is completely lacking, discouraging banks from engaging in these forms of operation.¹⁴ By 2007, credit to the private sector amounted to only 7.2% of GDP in the country, compared to 64% in Sub-Saharan Africa on average¹⁵ (Graph 6.3).¹⁶

Graph 6.3: Domestic credit to private sector (% of GDP), 1995-2008



Source: World Bank Development Indicators (2012).

Yet these above figures conceal the significant credit growth in Angola's post-war period, albeit from a very low base. At the end of the war, Angolan banks had had approximately \$3billion of assets between them (Wallace, 2014), a level comparable to that of smaller

¹⁴ Interview, administrative director, foreign bank, Luanda 1.10.2015.

¹⁵ This number is fairly high and is largely driven by outlier South Africa, where domestic credit to private sector as percentage of GDP constituted 160% in 2007, according to the World Development Indicators (2017). In second place were Mauritius at 72%, and third place Namibia at 48%. The World Bank Development Indicators database does not provide averages for the continent which exclude South Africa (World Bank, 2017).

¹⁶ The short-term nature of the deposits moreover limited the ability of Angolan banks to use these resources for long-term financing. Interview, banker, Angolan private bank, Luanda 28.10.2015.

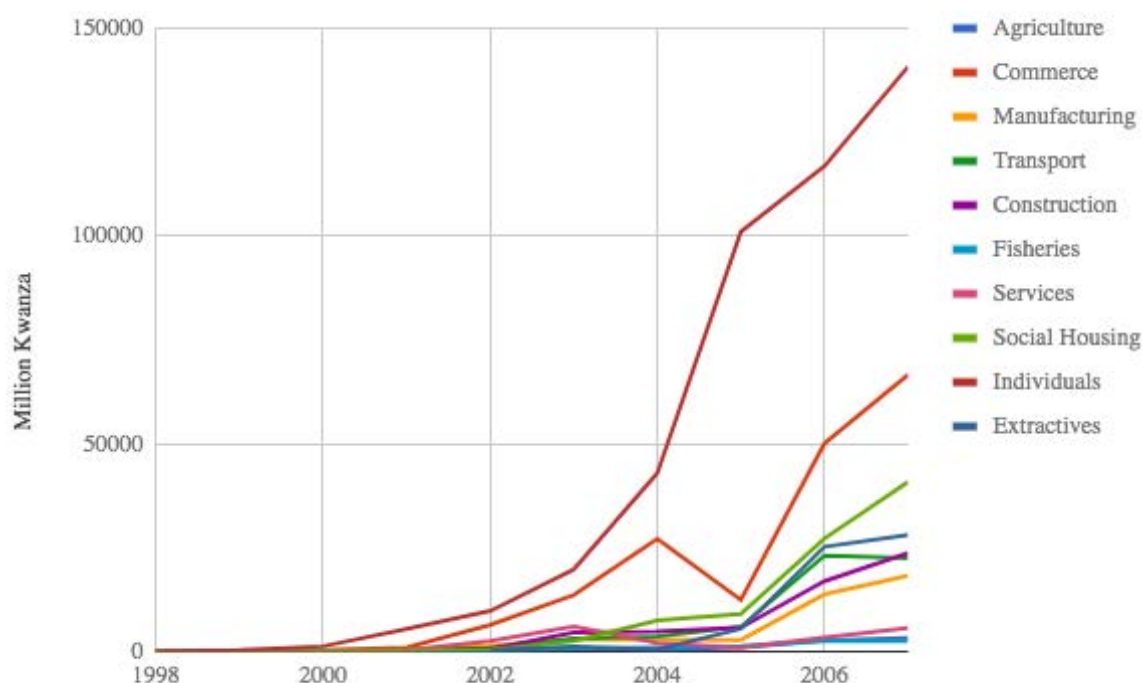
African countries (Boone, 2005). The amount started to grow after liberalization in late 1999 and more steadily from 2004 (see Graph 6.1). Some of the new assets were interest-earning loans to the private sector. The loan portfolios of banks were dominated by short-term loans, aimed largely at trade operations. Whilst the inclination for short-term loans was widespread in sub-Saharan Africa in general (IMF, 2003), bankers alleged that the situation was particularly bad in Angola due to the lack of collateral and a highly uncertain operating environment for banks.¹⁷ Yet as the 2000s progressed, it became clear that banks were increasingly interested in extending loans beyond the import-export sector in search of other high yielding opportunities (See Graph 6.4). This mainly took the form of credit to companies in construction, transportation businesses and commerce. Lending to high-earning individuals increased considerably (IMF, 2007; BNA, 2007).¹⁸ Something that is not clear from looking at Graph 6.4 is that fact that commercial banks invested heavily in Angola's booming post-war real estate market.¹⁹ A fast-growing demand for high-end housing in Luanda from expatriates in the oil and adjunct sectors meant that real estate prices in the country were amongst the highest in the world (Grant, 2015).

¹⁷ Interview, banker Angola private bank, Luanda 6.11.2015.

¹⁸ Interview, IFI representative, Washington DC, 8.12.2016.

¹⁹ Interview, representative Angolan private bank, Luanda 20.11.2015.

Graph 6.4: Domestic credit per sector, 1998-2007



Source: BNA (2007)

Despite substantial growth, overall lending to the private sector remained a small share of banks' total assets so that excess liquidity in the domestic banking system endured. As highlighted by the Economist Intelligence Unit (EIU), the Angolan government successfully tapped this excess liquidity by selling securities to the banks (EIU, 2003). As of mid-1999, the BNA issued central bank bills with 28-day maturity, for monetary policy purposes, and the Ministry of Finance launched its first issue of domestic securities, treasury bonds and bills, in July 2003 to generate internal savings and finance public investment programs (IMF, 2007; CEIC, 2009). Central bank and government securities quickly became popular with the banks, representing a low risk means of investment with nearly zero transaction costs. In this respect, Angola's experience was similar to that of

other developing countries. Across Africa, banks typically held large shares of assets in the form of government securities (IMF, 2003). In addition to being low risk, the securities offered relatively high average interest rates, occasionally as much as 50%-60%, reflecting the government's need for money in the early reconstruction period. As the government's need for borrowing diminished, as it did in 2006-2007, the yield on securities dropped to 10-15%. The lower yield was still more attractive to banks than the alternative of earning 8% on dollar denominated or dollar-linked commercial credit to customers (USAID, 2008). Consequently, the demand for government issued bonds remained strong throughout the period.

An examination of the banking sector post-2002 is necessarily incomplete if one only considers the role of Angolan banks as intermediaries between savers and borrowers. An equally important function of the banking sector was one of "intermediary of currency transactions" (Deloitte, 2006). Angola in the early 2000s was one of the most dollarized economies in the world, due in large part to high and persistent inflation but also the dominant role of the oil sector in the economy.²⁰ By the mid-2000s over half of deposits (80% in 2003 according to the IMF (2003)) and half of loans to the public and private sectors were denominated in foreign currency (BNA, 2007). Foreign currency exchange services were in high demand (World Investment News, 2002a).

The activities described above were attractive from the side of the Angolan banks. Banks were extremely profitable in the post-war era, with sector-wide return on investment taking

²⁰ Throughout the 1990s to 2000s, Angola was amongst the most dollarized economies in the world as measured in terms of domestic bank deposits (which remains a common way to measure dollarization in the comparative literature) (Yeyati and Di Tella, 2005; See also Reinhart et al., 2014).

two and half years in 2005 (Ferreira and Soares de Oliveira, forthcoming).²¹ As described by United States Agency for International Development (USAID, 2008, p.9), “The banking system in Angola has certainly been generating handsome returns on equity for shareholders, even above the norm for Africa, where shareholders tend to require a premium return to compensate for perceived risks”. A large amount of bank profits was (and remain) derived from fees. The importance of fees is clear when studying Angolan banks’ complementary margin, defined as the commissions banks earn on banking services and exchange gains. In certain years, banks earned more on these fees than they did from transforming deposits into loans and investments, known as the financial margin,²² which is the traditional way that banks make money (see Table 6.2). The consequence was that Angolan banks in the period 2002-2008 profited to a large degree by charging high fees and thus had few incentives to change their *modus operandi*. As summed up by the former head of one foreign bank, “In most countries, the most important aspect for banks is their financial margin. In Angola, this is not the case. Here, what is most important is the complementary margin of banks. Mainly this consists of foreign exchange trade, which is why I say that Angolan banks are *Caixas de Câmbio* [currency houses]”.²³

Table 6.2: Profitability indicators (% of average assets), 2004-2009

	2004	2005	2006	2007	2008	2009
Financial margin	6,4	5,6	4,2	4,8	4,6	3,6
Complementary margin	7,3	3,9	4,6	3,7	3	4,1

Source: Deloitte 2006; 2008; 2010

²¹ For comparison, the authors state that the same time in 2015 (when competition in the sector had increased notably) was six and half years (Ferreira and Soares de Oliveira, forthcoming).

²² Also known as the interest rate spread = Interest rates on loans – interest rates on deposits.

²³ Interview, former administrative director foreign bank, Luanda 14.10.2016.

This section described the post-war expansion of the banking sector, following from the reform measures of 1999 onwards. Of particular importance was the MPLA government's liberalized stance on foreign exchange, which allowed commercial banks to move into business operations that had previously been the purview of the state. This allowed those who controlled the banks to benefit handsomely. Yet as the next section will show, the expansion of the banking sector did not replicate in other parts of the financial sector. Rather, non-bank financial institutions were largely absent.

3. The underdevelopment of the non-bank sector

The rapid development of Angola's banking sector from 2002 stands in stark contrast to the lack of development in the country's non-banking system and non-bank institutions over the same period. According to the IMF, Angola's non-bank financial sector was smaller than in comparable countries; the assets of insurance companies represented only 2 % of GDP in Angola in 2010, lower than the average for sub-Saharan Africa (5 %) and in upper-middle income countries in general (10 %) (IMF, 2015, p.38). Angola's insurance and pension sectors only started gaining traction in recent years, having been a state monopoly until 2005.²⁴ Even after 2005, insurance companies were not allowed to operate freely within certain segments of the economy, including the highly profitable oil sector, diamond industry, and aviation insurance, which were reserved for the state (World Bank, 2002). Comparative studies have found that having monopolistic market structures based on state insurers negatively impacts market development (Outreville, 2013; Feyen et al., 2011) Indeed, the majority of Angola's insurance companies have concentrated on

²⁴ In 2005, state insurer ENSA and Sonangol-owned AAA - Serviços Financeiros were joined by three new companies; Nova Sociedade de Seguros de Angola (NOSSA), established by private bank BAI, Saham Angola Seguros, by Morocco's Saham Group, and GA Angola Seguros by South African Global Alliance.

“skimming the market”,²⁵ in the words the chairman of one foreign bank, focusing on low expense coverage for “few but profitable clients”.²⁶ Neither are pension funds prevalent in Angola, their assets representing less than 0.5% of GDP in 2009 (KPMG Angola, 2012). In Nigeria, the assets held by pension funds constituted 5.5% that same year (Federal Reserve Bank of St. Louis, 2014). The lack of development of Angola’s insurance and pension fund sector is not unexpected given that the demand for such financial products is expected to be low in countries with a large share of poor in their population (Feyen et al., 2011).

A more noticeable non-development in Angola’s financial sector was the absence of a domestic capital market and a stock market where stock, bonds, and other securities could be traded. Already in 2003 there were 15 stock exchanges in sub-Saharan Africa, the oldest dating back to 1887 (Moss, 2003). Notwithstanding the size of the Angolan economy relative to other countries on the continent, attempts at establishing a domestic market for stock, bonds, and other securities proved unsuccessful (World Report International, 2005; afrol News, 2005; Reuters, 2013a; Redvers, 2015).²⁷ Efforts date back to 1998 when the Angolan government first announced their plans to establish a stock market in the country (EIU, 2005b). In 2005, the National Assembly approved the necessary legislative framework on which the stock market would be based, the Securities Law,²⁸ and the Financial Institutions Law,²⁹ aimed at modernizing the financial sector (EIU, 2005a).

²⁵ The skimming strategy gets its name from skimming successive layers of “cream”, or customer segments, as prices are lowered over time.

²⁶ Interview, administrative director foreign bank, Luanda 1.10.2015. Up until recently, the overwhelming proportion of the insurance sector (over 90% of total) was non-life insurance, with shorter duration, as opposed to life insurance which has higher liquidity needs and unpredictability of the claims (KPMG Angola, 2012).

²⁷ Only in 2014 was the Angolan Debt and Stock Exchange launched. As of December 2017, the only trade on the exchange is in public securities (Reuters, 2013a).

²⁸ Law no. 12/05.

²⁹ Law no. 13/05.

A commission to oversee the creation of the exchange was appointed, made up of representatives of several ministries and assisted by the Stock Exchanges of São Paulo, Johannesburg and Amsterdam, as well as the chairmen of several commercial banks from the United States (EIU, 2006).³⁰ Ambitions for the Angolan bourse were grand but its launch continuously delayed; in 2005, it was reported that the stock exchange, known as the Bolsa de Valores e Derivativos de Angola, would open later that year with “an initial offering of ten companies and a capitalization of £3.3 billion” (World Report International, 2005). The exchange would be at the forefront of the government’s privatization efforts; offering shares in certain state-owned companies, amongst them Sonangol and the state diamond company Endiama (Bureau of Economic and Business Affairs, 2009). The following year, in 2006, the coordinator of the Centre for Capital Markets, António Cruz Lima, told the press “The Angolan Stock Exchange will likely be launched in the third trimester of this year with ten listed companies and an initial capitalization of more than \$ 6 billion” (afrol News, 2005). The plan was that the number of companies would increase to 40 within 5 years (EIU, 2005b). Amongst other companies, Manuel Vicente, then president of Sonangol, announced that several Sonangol subsidiaries were ready to be floated on the exchange (EIU, 2005b). A year later, official sources stated that the stock exchange, now with an expected launch in 2008, “has 27 subscribers and funding of \$16 million for its launch” (Macauhub, 2007).³¹ Similar statements by the authorities followed in the subsequent years (Almeida, 2009) until in January 2011 the long-standing plans were postponed indefinitely (EIU, 2011a; Making Finance Work for Africa, 2017a).

³⁰ Interview, administrative director Angolan private bank, Luanda 28.10.2015

³¹ In comparison, the capitalization of other African stock exchanges per end of 2000 was typically in the range of \$0.1-1.3 billion, the exception being Nigeria (\$4.2 billion) and Zimbabwe (\$2.4 billion), which were amongst the oldest stock markets on the continent (Moss, 2003).

The stock market receives special attention here because of the importance of domestic capital markets in complementing countries' banking sector in domestic resource mobilization, enhancing the supply of long-term capital, encouraging the efficient use of existing assets and last but not least, attracting foreign investment and integration into the global financial marketplace (Dailami and Atkin, 1990; Steil, 2001). Additionally, efforts to establish a stock market have dominated the non-banking financial sector discourse in Angola, as has already been attested to. The expansion of domestic capital markets has historically been emphasized by the World Bank, chiefly through its affiliate the International Finance Corporation (IFC), as part of the financial sector liberalization programmes that took place across the developing world from the 1970s. Stock market expansion was viewed as a natural progression for countries' financial sector development by the IFIs and economists more generally (Singh, 1991; Moss, 2003). This was the case also in Angola (World Bank, 1992). Nonetheless a stock exchange failed to emerge in the country.

Some would argue that the non-existence of a stock market in Angola is in fact not puzzling. The limited number of private firms in Angola by the early 2000s who could list on the exchange spoke against the feasibility of a stock market in the country (Albuquerque de Sousa et al. 2016).³² The country's small domestic investor base also represented a weakness with domestic investors more attracted to international markets than investing domestically.³³ In their study of a sample of Latin American and Asian countries, Garcia and Liu (1999) demonstrated that the level of domestic investment was determinative of

³² Albuquerque de Sousa et al. (2016) show how stock markets that start out with few listings and low trading activity fail to attract a considerable number of listings and thus spur adequate trading activity at a later stage. Stock exchanges in these cases quickly run the risk of becoming dormant.

³³ As already mentioned, capital outflows from Angola increased post-2002 as foreign exchange restrictions loosened.

stock market development. Stock market development is furthermore positively correlated with stronger protection of shareholder and creditor rights (Pistor et al., 2000) and financial openness and liberalization (Bekaert and Harvey, 2000; Henry, 2000). These are all indicators on which Angola performed below the average for sub-Saharan Africa (Jover et al., 2012; Boone, 2005).

Yet, as stressed by Lavelle (2001) and Moss (2003), other factors than the market forces, emphasized above, have likely been salient in driving the development of stock exchanges across Africa and the developing world. Importantly, as both Lavelle (2001) and Moss (2003) demonstrate, throughout the period of fast growth of stock exchanges across the continent, the state played a central role in leading this development. These were states that in turn responded to the pressures of donor states and international financial institutions who, as already established, were in favour of stock markets (Singh, 1991). In her study of the Abidjan Bourse, Lavelle (2001) demonstrate how the Ivorian state created a stock exchange to achieve the political goal of diversifying and spreading ownership of large (foreign) companies in Cote d'Ivoire. Establishing the Abidjan Bourse allowed the country's government to respond to external pressures for privatization whilst at the same time carving out financial market access for its own citizens (Lavelle, 2001). Moss (2003) similarly highlights political economy factors in explaining the emergence of Africa's stock markets. Amongst the strong political reasons for establishing a stock market, Moss (2003) underlines that the stock market has become a powerful symbol of modernization and international legitimacy, in turn possibly helping countries attract foreign investors.

It is against the more contextual understandings offered by Moss (2003) and Lavelle (2001) — of why it might be in the interest of political leaders to establish a stock exchange even

if the economic reasons do not appear obvious — that the non-development of Angola's stock exchange appears puzzling. Other countries, including Ghana and Cote d'Ivoire, share Angola's challenge of having a small investor base and few listed companies (Moss, 2003), yet political leaders in these countries have decided to establish these non-bank financial institutions regardless.

In the two last sections, I have offered an overview of the development — but also the non-development — characterizing Angola's financial sector 2002-2008. In the rest of this chapter I will endeavour to account for abovementioned pattern, explaining why it was in the interest of the elite to advance the banking sector in the way that they did whilst the non-banking sector was largely bypassed.

4. Cementing elite support through ownership

By the late 1990s, as argued in chapter 5, a longer-term vision was evident in the business undertaking by members of the MPLA. This was encouraged mainly by changes in the war. The opportunity to enter the financial sector was not lost on Angolan elite members who gradually positioned themselves in the service sectors towards the end of the 1990s (Messiant, 2001). As the institutional changes from 1999 onwards meant the end to a prevailing way of distribution resources amongst Angola's powerful, there was a need to find new mechanisms through which patronage could be dispensed and accumulation enabled in the new post-war era. Business opportunities in the banking sector were one of these mechanisms that the Angolan regime employed.

The ‘second wave’ of liberalization in the banking sector coincided with the distribution of a number of bank licenses by the BNA.³⁴ Following the establishment of BAI and BCA in 1997, both with state financial backing and prominent elite members amongst their shareholders,³⁵ two new banks with Angolan owners were established in 2001 and 2003; Banco Sol and Banco Regional do Keve (Angop, 2003).³⁶ The majority owners of the two banks, Sebastião Lavrador and Amílcar Silva, hailed from powerful positions in the public sector. Lavrador had served as BNA governor for two periods in the 1990s and Silva came from the position of president of public bank BPC. In the years that followed, several more Angolan private banks were created. Banco BIC, owned by Isabel dos Santos, daughter of president dos Santos, and Américo Ferreira Amorim, an industrialist and previously Portugal’s richest person, in addition to Banco Privado Atlântico (BPA) and Banco de Negócios Internacional (BNI) (Ferreira, 2005). 2006 also marked the first year of Angola’s new state-owned development bank, Banco de Desenvolvimento de Angola (BDA).

Not all licences were directly in the hands of Angola’s elite members. In the early 2000s a few foreign banks, which were keen to take advantage of the peace dividend, upgraded their representative offices and branches to become full-fledged Angolan banks (Reuters, 2010).³⁷ These were Portuguese Banco de Fomento Angola (BFA) and Banco Totta & Açores (BTA). Banco Espírito Santo Angola (BESA), a subsidiary of Portuguese Banco Espírito Santo (BES), joined as a new bank in 2002. Foreign banks were not needed for their capital,³⁸ but rather, as argued by Ferreira and Soares de Oliveira (forthcoming, p.11)

³⁴ Law no. 5/91.

³⁵ The establishment of BAI and BCA is discussed in chapter 4.

³⁶ Banco Sol vowed to take advantage of the so far overlooked micro-credit segment of the economy, Banco Regional do Keve was Angola’s first regional bank seeking to extend also into the province surrounding Luanda. Interview, former IFI representative seconded to BNA, via Skype 2.06.2016.

³⁷ Other banks, including Citibank, which had been represented in the country since 1994, did not go ahead with its plan to expand its presence in the country but closed down its operation in 2001 following concerns of corruption. Interview, banker previously in public bank, Luanda 20.9.2015; Reuters, 2010; EIU 2010d.

³⁸ Interview, senior civil servant BNA, Luanda 23.10.2015.

the presence of foreign banks was pivotal on the grounds of their sectoral expertise and their ability to help shape “Angolan banking in the image of international banking.” Additionally, foreign banks were “important on account of their (and their home jurisdictions’) credibility” (Ferreira and Soares de Oliveira, forthcoming, p.11). The superior standing that the foreign banks enjoyed helps explain why they remained the main counterparts of multinational companies in Angola, who were hesitant do business with smaller and less known domestic banks.

It did not take long, however, before minority and majority stakes in foreign banks were sold to Angolan counterparts. As noted by the IMF, “The legal framework allows foreign banks to have 100 percent equity stakes; in the boom years in the run-up to the crisis, they were *encouraged* to seek local partners and divest their shareholdings to 51 percent stakes” (2012, p.16, emphasis added by me). Two years after its establishment, BES sold 19% of BESA to GENI, a company controlled by Isabel dos Santos, the daughter of president dos Santos. Another 24% of the bank was sold to Portmill in 2009, a company linked to Vice-President at the time Manuel Vicente and General Manuel Hélder Vieira Dias Jr. ‘Kopelipa’, chief of the Security Intelligence Bureau of the Presidency and one of President dos Santos’ closest allies (Reuters, 2014). In 2008, Portuguese Banco Português de Investimento (BPI) sold 41.1% of BFA to Angolan telecom company UNITEL, whose majority shareholder is Isabel dos Santos (BPI, 2008). The following year, the owners of Caixa Geral Totta de Angola, Caixa Geral de Depósitos and Spanish financial group Santander, sold minority shares in the bank to Sonangol (24%), and two Angolan entrepreneurs with close connections to the ruling party and presidential family, António Mosquito (12%) and Jaime de Freitas (12%) (Martins, 2009; Dinheiro Vivo, 2013; Africa Confidential, 2012).

Similar to the case of Nigeria, where bank liberalization started in the late 1980s,³⁹ the bank licensing process in Angola was thoroughly politicized. Licences were allocated to politically influential people within the MPLA circle, many of whom had served in senior public positions during the 1980s and 1990s. One Angolan reporter explained how “the politically connected get licences to operate banks. It’s about who you know. Even if they [the politically connected] do not need it, they know that they can sell the licences later.”⁴⁰ If and when initial shareholders sold their shares, ownership was passed on to people within elite circles. As the administrative director of one Angolan private bank explained, “When our bank sells shares, there are rules. First, we sell to existing shareholders. If they do not want them, you can sell the share to whoever you want. In reality we are talking about a few people, a small group who hold shares in the banks. The banking business is a closed business and shareholders usually buy each other’s shares.”⁴¹

In contrast to Nigeria, where Lewis and Stein (1997) described a diverse group of investors, originating in the military, trade activities, civil service but also academia and journalism, entry into the Angolan financial sector appears to have happened on a smaller scale. An explanation for this may be the lesser number of people in Angola who were able to meet necessary capital requirements, as power and resources remain more narrowly distributed in the latter case as compared to Nigeria. Even though initial capital requirements were not high by comparative standards, \$4 million in the 1990s,⁴² few private Angolans had access to this amount of money and the ones who did often relied on Sonangol or other state institutions to provide such initial capital. As one former BNA official noted, “most private

³⁹ See Lewis and Stein (1997).

⁴⁰ Interview, reporter Angolan newspaper, Luanda 1.10.2015.

⁴¹ Interview, administrative director Angolan private bank, Luanda 26.11.2015.

⁴² Later changed to \$25 million. Interview, administrative director private bank, Luanda 26.11.2015.

initiatives come from people with power.”⁴³ Adding to this, he explained that the state frequently *assisted* well-connected Angolans with start-up capital either directly as shareholder or indirectly through loans.⁴⁴ Restricted access to the banking sector moreover meant that the few ventures that were granted a licence became extremely profitable.

The early licensing process was also characterized by the granting of licences to institutions whose technical capacities and international standing was necessary to get the Angolan banking sector on its feet, only to pressure them to transfer parts of their shares to Angolan private owners at a later date.⁴⁵ This was the case with the Portuguese banks, as described earlier, whose initial presence was desirable from an Angolan viewpoint on account of both their technical expertise and the credibility offered by their home jurisdictions. In contrast to the English and French banks, taking on foreign partners did not conflict with the entry strategy of Portuguese banks. The latter group were willing to accept stricter conditions due to the significance of the Angolan market to Portugal.⁴⁶

The need for capital and expertise can also help explain the use of Sonangol “to promote local businesses”, in the words of a former Sonangol manager.⁴⁷ Sonangol became the biggest shareholder of Angola’s first private bank, BAI, only to transfer its majority of its shares to Angolan private owners at a later date.⁴⁸ The company enjoyed the international credibility that the Angolan state lacked and political leaders had stated their enthusiasm for exporting the company’s business model – ostensibly based on neutrality and

⁴³ Interview, former vice-governor BNA, Luanda 28.9.2016.

⁴⁴ Interview, banker private bank, Luanda 6.11.2016; Interview, former vice-governor BNA, Luanda 28.9.2016; Interview, reporter Angolan newspaper, Luanda 1.10.2015.

⁴⁵ Interview, banker Angolan private bank, Luanda 6.11.2015

⁴⁶ Interview, reporter Angolan newspaper, 1.10.2015

⁴⁷ Interview, manager oil service company, Luanda 3.11.2015.

⁴⁸ BAI initially also had Portuguese shareholders who jointly held 33 %, including Caixa Central de Credito Agricola, Banco de Investimento and Banco Pinto & Sotto Mayor, and two construction groups; Soares de Costa and the Mota group (The Times, 1997a).

professionalism, although later revelations threw doubts on this narrative – to other parts of the economy (Soares de Oliveira, 2015). The role of Sonangol was about more than expertise and credibility, however, as evident by the fact that the company on the one hand disinvested in certain banks and financial institutions whilst at the same time it bought shares in others. By virtue of Sonangol's vastly superior financial means as well as human resources, Angola used the company to maintain strategic control over the financial sector (Soares de Oliveira, 2007)⁴⁹; selling off banking shares to elite members (example BAI), buying into profitable ventures (as in the case of Banco Millennium BCP and Banco Totta de Angola) or rescuing banks when the pillaging had gone too far (as in the case of BESA in 2014) (Marques de Morais, 2012a; Africa Confidential, 2008; Lusa, 2015).

Through the allocation of banking licenses and stakes in bank ventures, the regime of President dos Santos' ensured that strategic allies would continue to benefit as the economy liberalized. An important attraction of banking in Angola appears to be that entry into the sector can easily be restricted through the licensing processes, which is controlled by the BNA. The rents created by the restricted access to the sector were in turn sizeable. The stock market differs in this respect. An often-cited rationale for establishing a stock exchange is to widen ownership (Moss, 2003;). Frequently this has happened through selling shares of newly privatized enterprises on stock exchanges, so as to spread ownership whilst also to gain greater public support for the privatization process (Moss, 2003). Kenny and Moss (1998) gives the example of Cote d'Ivoire where in 1990 the government leased the power sector grid to a private firm, *Compagnie Ivoirienne d'Électricité*, which was subsequently floated on the Abidjan Stock Exchange. 49% of the shares were sold to 4000 small investors and foreign investors held the controlling share. Stock markets are

⁴⁹ Interview, professor public university, Luanda 22.10.2015.

moreover likely to create new sources of competition to bank lending since companies have easier access to an alternative source of funds (Hutchcroft, 1998). In his study, Levine (1996, p. 45) shows how stock markets increase companies' access to capital both in breadth of choices and depth of monies available.

Whilst the stock exchange could be an avenue for privatization in Angola, as indeed was the stated intention in the mid-2000s, it never occurred because the MPLA ruling coalition appeared unwilling to give up control of strategic enterprises. Moreover, the idea of using the stock exchange to foster a “new emerging business class that does not rely on state intervention for survival, but is instead connected to the global economy through financial markets” (Kerny and Moss, 1998, p.839), runs counter to the MPLA's logic of building a business class subordinate to the regime, as will be further discussed in the last section of this chapter. One former banker summed it up well, establishing a stock exchange “is a fundamentally democratic process, it would jeopardize government control. There is a lack of willingness to genuinely open up the [Angolan] economy for broader participation.”⁵⁰

5. Ensuring connections to the outside

The external orientation of the Angolan economy meant that securing smooth interactions with ‘the outside’ was always of crucial importance to the state. The financial sector, in turn, became central in facilitating such a relationship. Initially, during the early post-independence years, a main concern was enabling international trade in a time when the economy was undergoing considerable turmoil (Ministry of Finance, 1990). Because international trade exposes exporters and importers to substantial risks, firms are likely to want to mitigate these risks through specialized trade finance products offered by financial

⁵⁰ Interview, banker previously with Angolan public bank, Luanda 20.9.2015.

institutions (Niepmann and Schmidt-Eisenlohr, 2014). Such bank products did not exist in Angola prior to 1991 (World Bank, 1991).⁵¹ ⁵² Consequently, following initial liberalization of trade and investment in the early 1990s, a handful of foreign banks with the necessary expertise came to dominate the provision of these services, including the acceptances and guarantees related to international trade. Like multinational banks elsewhere,⁵³ the banks that arrived in Angola in the early 1990s followed their clients (Weller and Hersh, 2002). The multinational banks in Angola, including Citibank, Equator Bank (later HSBC Equator Bank) and BNP Paribas, focused their operations on multinational corporations in the country's oil sector. Portuguese multinational banks, on the other hand, took advantage of the considerable interest shown by Portuguese companies in the Angolan market following the latter's transition to a market economy (The Times, 1997b). The banks' focus on a small number of large clients in combination with superior technology and know-how meant that their operations were extremely profitable, as mentioned above.

Whilst the multinational banks remained vital to facilitate international trade, from the late 1990s, the new Angolan banks joined in the lucrative export/import business. Of the Angolan banks, the most important was BAI. With Portuguese and Sonangol amongst its shareholders, BAI offered a greater degree of credibility than other domestically owned banks. The emergence of BAI and other Angolan banks coincided with the financial

⁵¹ Interview, banker previously with Angolan public bank, Luanda 20.9.2015

⁵² In many cases, the central bank guaranteed the external debt of Angola importers (World Bank, 1991). Some projects were guaranteed by export credit agencies, but these differ from banks. Export Credit Agencies are public agencies and entities that provide government-backed loans, guarantees and insurance to corporations from their home country seeking to do business overseas in developing countries and emerging markets that are considered too risky for conventional corporate financing. Unlike commercial banks that seek a market return on their loans or insurance, ECAs only seek to recover their operating and financing costs.

⁵³ Multinational banks are those banks that physically operate in more than one country. In contrast, international banks engage in cross-border operations and do not set up operations in other countries (Weller and Hersh, 2002)

liberalization measures of 1999 onwards, from which point banks were allowed a greater role in international transactions (as discussed in chapter 4). Up until 1999, due to foreign exchange restrictions, Angola's financial system had been largely insulated from the rest of the world. Controls of foreign exchange and capital account transactions were strict by international standards and similar to other statist banking systems such as Tanzania and Ethiopia (Boone, 2005; Ndikumana, 2003). In Angola during in the period from independence until 1999, most aspects of international banking were reserved for the BNA including the opening of foreign currency accounts and extending foreign currency loans. From 1999, commercial banks and exchange houses were allowed to buy and sell foreign currency at freely negotiated exchange rates, at sessions held by the BNA or between the banks themselves outside these sessions (Notice no. 1/99). Banking institutions domiciled in the country could open current and foreign currency deposit accounts in the name of residents and non-residents, abroad and in Angola (Notice no. 4/99), they could carry out credit operations with exporters (Notice no. 5/99) and capital restrictions were significantly eased (Notice No. 10/99; Notice no. 11/99). Specifically, requirements of prior BNA approval of foreign exchange purchases for imports were abolished; limits on purchases of foreign currency for travel and transfer abroad were substantially relaxed; some capital account transactions were pre-authorized up to maximum amounts specified in United States dollars; and external tariffs on imports and exports were drastically reduced (IMF, 2000). Commercial banks were not slow to act on the changes. Already in the first year (1999), 40% of loans by commercial banks were granted in foreign currency (BNA, 2007). The importance of foreign exchange operations to the banks was already emphasized in the previous section and became increasingly central to the economy as it grew from 2004 onwards.

The greater integration of the financial system with global finance offered more opportunities to externally oriented Angolans. Angola was already a dollarized economy prior to 2002, due to a history of economic uncertainty and the prominence of the oil sector in the economy. “Investing in dollars worked as a source of security”, one banker explained.⁵⁴ At one end of the spectrum, members of the ruling coalition, in fear that they might be ousted from the ruling circle, would keep their money in a ‘safe haven’ abroad. “People were concerned that they would attract negative attention if they kept their money in the country, thus it was safer for them to transfer money out of the country” explained the head of a local oil service company. “Similarly, to what we saw in Russia, people were afraid that the government would confiscate their assets if they grew too big”.⁵⁵ A reporter for one of Angola’s leading newspapers confirmed that the lack of entrepreneurs in the country had to do with this political uncertainty.⁵⁶

Still, for most people, depositing in foreign exchange accounts was a way of hedging against political uncertainty and inflation. The changes of 1999 meant that it became easier for people wishing to buy foreign currency for the purpose of saving to do so. It also made it easier to buy foreign currency for other purposes, such as travelling. Because people did not necessarily have foreign exchange accounts or credit cards, this would result in a request for paper money from the banks.⁵⁷ Revealingly, a United States Senate investigative report showed how the sale of United States dollars by multinational bank HSBC to its local partner BAI, increased exponentially over a few years, from \$6 million in 1998, to \$30 million in 2005, to \$490 million in 2007 (United States Senate, 2010).

⁵⁴ Interview, banker Angolan private bank, Luanda 23.11.2015.

⁵⁵ Interview, oil service company representative, Luanda 5.11.2015.

⁵⁶ Interview, reporter private Angolan newspaper, 1.10.2015.

⁵⁷ Interview, oil sector consultant, Luanda 17.11.2015.

Angolans were also moving money abroad at an increasing volume. Financial resources that were not invested domestically, most often in government bonds, were held in foreign assets abroad (World Bank, 2007). This trend became especially pronounced following the end of the war in 2002, when resources from the fighting were freed up. From 2002, the value of outward direct investment from Angola rose from less than 1 % of GDP in 2002-2003 to 4% by 2004 (World Bank, 2017).⁵⁸ The equivalent number for sub-Saharan Africa in 2004 was 0.5% (World Bank, 2017).⁵⁹ The banking system was moreover key to the growing number of labour migrants, arriving in Angola as contract workers for the industry and mining sectors (See Table 6.3; IOM, 2005). Many of these workers received their payments locally, in local currency, and needed to make use of the local banking system to exchange their kwanza and then to remit their payments using the local banking system.

Table 6.3: Outward remittance flows (in million \$), 2003-2008

	2003	2004	2005	2006	2007	2008
Outward remittance flows	230	296	215	413	603	669

Source: World Bank (2011)

Through the facilitating of trade and outward capital flows, this section demonstrated the central role of the banking sector not only to the Angolan ruling coalition but also to the broader public. Again, the rationale of Angolan authorities for developing a banking sector is not easily applied in favour of establishing a stock exchange. Whilst banks proved central for the Angolan elite to move capital out of the country, the rationale for establishing a stock exchange appears rather to attract foreign capital (Moss, 2003). As Moss (2003)

⁵⁸ Angolan nationals invested more abroad than foreigners invested in Angola, between 2008-2016. Angolans invested \$154 billion whilst FDI to Angola accounted for \$134 billion. Following the fall in oil prices investments in both directions have declined (dos Santos, 2018).

⁵⁹ See World Bank Development Indicators (2017), Foreign direct investment, net outflows (% of GDP).

explains, stock markets can encourage greater inflows of foreign investment. Additionally, “there is the potential role of the stock market in re-attracting capital owned by Africans living abroad or money stashed overseas by nervous domestic investors” (Moss, 2003, p.32). Angola’s oil wealth, especially pronounced in the 2004-2008 period, put the country in a situation distinctly different from most other developing countries, as attracting foreign investments was not a preoccupation for either the political leadership nor for entrepreneurs (these were often the same people), who might otherwise have lobbied for the establishment of a stock exchange. As was already pointed out, the banking sector opening up for foreign investments was mostly about attracting foreign expertise and credibility rather than capital, the latter frequently provided by the Angolan partners (Soares de Oliveira, 2015). Also emphasized earlier, exporting capital was part of the ‘survival strategy’ of elites. These elite members would thus be unlikely to bring their monies back home to invest in the domestic stock market. Because of the state’s comfortable financial situation, it was neither a priority to make elites do so.

6. Banking to the people?

Observers typically brand the post-2002 growth of the Angolan financial system along the lines of “growth without development”.⁶⁰ Yet, on closer inspection it is clear that the period did see the extension of financial services to greater segments of the Angolan population than had previously been the case. In this section I will argue that this is due to banking sector expansion being part of the MPLA government’s effort to cement its position through extending its control over the territory and by fostering a loyal, primarily urban, support base.

⁶⁰ Interview, banker public bank, Luanda 20.9.2015

With the takeover of the entire national territory by the MPLA government at the end of the war, banks stood free to expand their operations outside of the capital. Some explicitly expressed their intent to do so, notably the two new Angolan banks, Banco Keve and Banco Sol (Angop, 2003).⁶¹ The physical expansion of the branch network could be a natural reaction of the banks as they sought to mobilize capital. Deposits had been growing quickly after 2002, and banks would have likely been keen to capture some of those funds (BNA, 2007). Yet a more probable explanation, given that wealth and economy activity remained concentrated in Luanda and the other coastal cities and provincial capitals, is that the initial push to expand banking across the country was driven by the state and not market forces. As one BPC banker at the time recalled, “The Angolan government wanted to establish their presence in the areas where they had so far not enjoyed control and the spread of banking services was one part of this. Banks were told to open up branches across the country and BPC was in charge. We were nervous but it went surprisingly well. People rushed to open bank accounts and deposited their money.”⁶²

The central role of state-owned BPC in extending banking across the country underlines the part played by the state in endorsing the physical outreach of the banks. Banks appear to have formed part of the MPLA’s post-war drive to provide basic infrastructure and services to rural areas previously under opposition control, so as to establish the authority of the party-state across the territory. Although the state-owned banks had the largest branch networks, the expansion was not confined to state-owned banks. As the decade evolved, private banks became increasingly involved in the geographical expansion, reflecting the MPLA’s “recurrent use of non-state actors to guarantee territorial coverage

⁶¹ Interview, former IFI representative, via Skype 30.11.2016.

⁶² Interview, banker previously in Angolan public bank, Luanda 20.9.2015.

and extraction” (Soares de Oliveira, 2013, p.180). In interviews, representatives of private banks acknowledged that they were strongly encouraged by government officials to expand their branch network. Being understood to provide banking services across the country was “politically well seen”, as the administrative director of one private bank, confessed.⁶³ The result, as noted by USAID in 2008, was that the physical outreach of the banking system was greater than expected; “Data provided by BNA show that every provincial capital now has at least three bank branches, and seven cities outside Luanda have ten or more” (2008, p.38). The IMF noted “The number of branches per 100.000 adults in Angola increased from 3 in 2005 to 13 in 2013, compared to 7 in sub-Saharan Africa and 28 in upper-middle income countries. The number of ATMs per 100.000 adults in Angola also rose, from 2 in 2005 to 21 in 2013, compared to 10 in sub-Saharan Africa and 45 in upper-middle income countries” (IMF, 2015, p.37).

Whilst noteworthy, the expansion of banking services witnessed throughout the country was concentrated on the deposit side (Ferreira and Soares de Oliveira, forthcoming). The largest extension of banking services was still focused in the MPLA heartland of Luanda and to a limited number of other urban centres where the ruling party enjoyed a stronger foothold. It is estimated that Luanda residents (30% of Angola’s population) had about 90% of all credit and deposits in the country (IMF, 2015).

The emphasis on urban Angolans was in line with a key concern of the MPLA in the post-war era, to carefully nurture a loyal and state-dependent urban class so as to avoid crafting “the conditions for the spontaneous emergence of an unattached and unreliable middle class” in the long run (Soares de Oliveira, 2015, p.83). It was not long after the war ended

⁶³ Interview, administrative director Angolan private bank, Luanda 28.10.2015

that banks in Angola stood ready to reap the benefits of the country's emerging middle-class. Banks offered banking services to go with the middle-class lifestyle, including debit cards and credit cards, car loans and to a lesser extent, mortgages. The more risk averse private foreign banks generally stuck to employees of multinational companies and other high net worth customers. Public banks and to some extent the Angolan private banks were prepared to take higher risk customers by also extending credit "to public sector institutions and workers" (IMF, 2012b). Banks such as BPC and to some extent BAI (handling the payroll of state employees and Sonangol employees, respectively) offered long-term finance on the basis of repayments being tied to the salary account of the civil servants.⁶⁴ In another bid for customers, Banco BIC launched "Crédito Fácil"⁶⁵ in 2007, which made it possible for bank clients to access loans of up to one million kwanzas (\$12 000) in the course of a couple of hours, on condition that customers could provide the necessary paperwork (Angop, 2007). As one former BIC employee explained, "The loans were not dependent on the approval of bank directors, rather lower level managers could approve them. This gave a lot of power to the managers who were also lending to friends and to themselves."⁶⁶

As had been the case in the 1980-1990s, state-owned enterprises remained important customers for the public banks (IMF, 2015).⁶⁷ Public banks engaged in riskier (and often loss-making) business with the explicit guarantee that the state would cover any losses. As later admitted by Minister of Finance, Armando Manuel, granting concessional credit for the importation of goods and services was seen as imperative for national reconstruction

⁶⁴ Interview, banker foreign bank, Luanda 19.10.2015; Interview, representative IFI, Washington, DC, 8.12.2016; Interview, representative oil service company, Luanda 3.11.2015.

⁶⁵ Translated as 'Easy Credit'.

⁶⁶ Interview, banker foreign bank, Luanda 19.10.2015.

⁶⁷ Interview, IFI representative, Washington, DC, 8.12.2016.

(Manuel, 2014). The existence of a state credit guarantee was also clear, albeit indirectly, in the private bank sector. This made private banks more willing to take risks, most notably in lending to the construction sector and developers in the real estate market (IMF, 2015).⁶⁸ None of the banks were especially interested in financing small and medium enterprises, preferring “larger, more well-established firms over smaller start-ups” (World Bank, 2013, p.29).

In the state’s effort to amplify its physical presence and weight in the economy, it is not obvious why the prospect of developing a non-banking financial sector did not appeal to the government. Here I am not thinking about a stock exchange, which appears less appropriate in terms of extending the regime’s physical presence throughout the Angolan territory. Microfinance institutions, on the other hand, would seem a suitable non-bank institution to contribute to the geographical expansion of the financial sector. Microfinance have been promoted globally as a way of spreading financial services also to low-income clients, who typically do not qualify for formal banking services (Morduch, 1999; Brau and Woller, 2004).⁶⁹ There was moreover a significant demand for microfinance services, as evident from the sizable informal microfinance market in the country.⁷⁰ The use of Kixikilas, a rotating savings and credit associations system,⁷¹ was widespread, especially in urban areas (Wilson, 2002). A few microfinance institutions emerged in Angola from

⁶⁸ Interview, IFI representative, Luanda 4.10.2016.

⁶⁹ The effectiveness of microfinance institutions in alleviating poverty and spreading financial services has been debated for over a decade. The thesis will not go into this discussion but refers to extensive literature on the topic, see Brau and Woller (2004) for an overview. By 2016, the World Bank had moved away from promoting the establishment of microfinance institutions in the developing world, due to the high costs involved. Interview, IFI representative, Washington DC 8.12.2016.

⁷⁰ The significant demand for microfinance services was also confirmed by the Angolan Government (Government of Angola and UNDP, 2003).

⁷¹ Kixikila is an informal system of mutual money lending within a group, according to which each member of the group receives in turn contributions from the other members, in order to lend money, for instance to buy a stock of goods (Human Rights Watch, 2013).

the late 1999s, some run by non-governmental institutions or as private initiatives,⁷² other by commercial banks, most notably Banco Sol, who remained partially dedicated to microfinancing (Banco Sol, 2008).

Still, the market for microfinance never thrived in Angola, remaining small throughout the 2000s. One factor holding microfinance institutions back was the unclear regulatory framework governing the sector (Karim et al., 2011; Government of Angola and UNDP, 2003). Until the passing of specific regulations for microfinance companies in February 2011,⁷³ microfinance institutions were regulated as non-bank financial institutions under the Financial Institutions Law of 2005. The 2005 law had, like earlier laws governing non-bank financial institutions, failed to take into account the specificities of the microfinance industry (Angop, 2010b),⁷⁴ typically including the high costs of administering small loans and the perceived high risks associated with this type of credit.⁷⁵

The sector was also restrained by the high costs for providing microfinance services.⁷⁶ This became particularly evident with the introduction of the new law in 2011, when smaller institutions were expectedly barred from participating in the formal market due to high minimum capital requirements.⁷⁷ Larger commercial institutions, on the other hand, never dedicated too much of their overall attention to the microfinance industry. For instance,

⁷² Novo Bank started as a corporate responsibility project by oil company Chevron. The bank does not exist anymore but is now part of BAI's microfinance operations: Banco BAI Micro Finanças.

⁷³ Presidential Decree 28/1136.

⁷⁴ For an overview of how laws proceeding the 2005 Financial Institutions Law also failed to take into account the specificities of the microfinance sector, see Cerqueira (2002).

⁷⁵ The perception of microfinance as high risk was common internationally among bank regulators who equated such loans with uncollateralized consumer lending. The counter argument often presented in this regard is that microcredit presents a different, less risky profile than consumer lending and tends to present very little risk to depositors or to the financial system (Government of Angola and UNDP, 2003).

⁷⁶ The high costs associated with microfinance are not unique to Angola, but a challenge of microfinance initiatives generally due to the high transactions costs involved compared to the frequently small amounts (Yee, 2015; Interview, representative IFI, Washington DC 8.12.2016).

⁷⁷ \$450.000 (Decree no. 28/11). Minimum capital for commercial banks was \$6 million (Karim et al., 2011).

microcredit only constituted 14.7% of Banco Sol's total loans in 2008 although it remained a "strategic pillar" of the bank (Banco Sol, 2008, p.15).

Microfinance institutions were furthermore inhibited by the lack of access to affordable funds as they were by law not allowed to mobilize deposits, having to rely on wholesale funding (where equity and retained profits are not enough) (Decree no. 28/11).⁷⁸ Also on the lending side, clients were met by the high costs. Whereas interest rates on commercial loans were reported to be 12% on dollar loans and up to 25% on kwanza loans in 2008, the interest rates on micro-lending was reported to be as high as 60% (The Services Group, Inc. and Nathan Associates, 2008). The problem of high interest rates has been a critique of microfinance worldwide, yet Kneiding and Rosenberg (2008) calculated that the global average in 2008 was about 35%, compared to Angola's 60%.

Taken together, the significant demand for microfinance institutions and the suitability of these institutions in helping extend the physical reach of the MPLA government would have one expect that it would be in the interest of the regime to promote the expansion of the microfinance industry. Nevertheless, as the last section has made clear, this was not the case. To understand why political leaders chose to prioritize the establishment of a sizable banking sector while ignoring the expansion of microfinance institutions it is necessary to appreciate the purpose for which a functioning financial sector was desired in the first place. More specifically, to keep in mind the part of the population that the MPLA wished to appease. Other authors have pointed out how different bases of social support can lead to different financial sector outcomes. Haggard and Lee (1993) emphasize how different

⁷⁸ The prohibition on taking deposits would not apply to Banco Sol as it was first and foremost a commercial bank.

political realities and particularly business-government relations in Korea and Taiwan, to name two, led the governments to use preferential credit programmes differently, one to forge ties with business elites (Korea), the other one by disadvantaging the business elites (Taiwan) (Haggard and Lee, 1993, p.17).

In the Angolan case, the MPLA ruling coalition wanted to enlarge its constituency by creating a middle class loyal to the state, by relying on a system of reputation-based exchanges where access to capital was tied to political allegiance, the party was able to do this through the use of the banking system. At the same time, the state was able to use the banks in its bid to assert control over the rural areas. According to this political calculus, the leadership did not need microfinance institutions to appease the party's core constituency of political elites and a supportive urban middle class. The disregard for microfinance services that would target the poorer segments of the population therefore fits the general lack of attention that has been devoted in Angola to poverty reduction and the poor segments of the population post-2002 (Soares de Oliveira, 2015).

7. Conclusion

In this chapter I described the remarkable expansion of Angola's banking sector in the post-war period of 2002-2008. The expansion followed significant liberalization of the country's banking sector in the late 1990s and took place on the back of an unprecedented economic boom in the country. The impressive development of Angola's banking sector was contrasted with the non-development of the rest of the financial sector. Specifically, after years of delay Angola remains, at the time of writing, one of few African countries without a domestic stock exchange.

I argue that the reasons why Angola's financial sector developed in the way that it did in the post-war period is closely linked to the role and purpose that the MPLA regime envisioned for the sector. Faced with a new political and economic reality following the end of the 27-year civil war, the party and its leadership needed to accommodate politically powerful people within the new economic order. The creation of a tightly knit and profitable banking sector was well suited for this purpose whereas the creation of a stock exchange was not. Another main concern of wealthy Angolans was to move money out of the country, a task for which banks were well suited. Stock markets, on the other hand, are more concerned with attracting capital, which was of less concern to the elites. Finally, I highlight the burden facing the regime in the reconstruction period, the pressure to establish the MPLA's presence in the wider Angolan territory and the need for the party to widen its support base. Again, the banks proved more suitable than other institutions, such as microfinance for instance, in contributing to the MPLA's post-war reconstruction vision of a middle class loyal to the state. Appreciating the role that the financial sector came to serve in Angola during the 2000s is necessary to make sense of the changes that took place in the sector from 2009, which is the focus of the next chapter. Still, the development of the banking sector described here would soon come to an abrupt stop, as global oil prices dropped from a historic high in mid-2008 following the global financial crisis later that year. As the next chapter will explore, the price slump and the significant impact it had on the Angolan economy forced the ruling regime to reconsider the role of the financial sector in the country's political economy.

Chapter 7

Post-crisis regulatory reform, 2009-2014

1. Introduction

The last chapter explored how the financial sector changes that took place during the first decade of Angola's transition from centrally-planned to a market-based economy evolved after 2002, the era known as the post-war reconstruction period. Understanding the role of the financial sector in Angola during peace time is crucial given that establishing the usefulness of having a functioning financial sector for the ruling coalition is a primary motivation of this thesis. Additionally, understanding the role that the financial sector came to play in the 2000s is also critical for clarifying the drivers behind financial sector change during peacetime. The most consequential changes to the financial sector in the post war era were introduced in the latter part of the 2000s, following the global financial crisis. It is on these changes that this chapter will focus.

After years of lacklustre efforts to regulate the banking sector, the balance-of-payments crisis of 2009 marked the beginning of heightened efforts to bring the Angolan financial sector in line with international best practice. This chapter explains how political leaders' willingness to reform the sector was in part due to the fragile economic situation following the global financial crisis, making them more susceptible to the pressure of external factors including the IMF and international investors. Additionally, politicians and regulators alike understood that the role the financial sector had come to play in the post-war reconstruction era — as a facilitator of outward capital flows — could only be salvaged if the country at

least paid lip-service to the mounting pressure for greater compliance with best practise laws and regulations in the financial sector. Yet as the chapter makes clear, whilst responding to external pressure was central in explaining financial sector change at this point in time, it could not have been the only reason for why the government decided to increase regulatory efforts in the banking sector from 2009. I argue that in addition to external factors, one also needs to take into account the internal impetus for the kind of regulatory reform discussed here. Specifically, I argue that the regulatory reform drive was in the interest of Angolan government as it allowed them greater control over the economy and monetary policy in particular. Additionally, strengthening the regulatory framework of the sector contributed to improving the credibility of the banks, thus opening up banking sector transactions that previously were inconceivable. To corroborate the latter claim of an internal reform momentum, I build on the example of the foreign exchange law for the oil sector which serves as a particularly good illustration of how the Angolan authorities were able, on the back of a more advanced and better regulated financial sector, to broaden accumulation opportunities for the country's elite in the banking sector. The implementation of the foreign exchange law allowed the ruling coalition not only to strengthen the state's control over the economy but also to channel more business to the Angolan domiciled banks.

Focusing on the post-2009 regulatory reform efforts, the chapter corroborate the thesis argument by providing another example of how the banking sector reform was not simply the result of a weakened ruling coalition responding to external pressure. Rather, the financial sector changes from 2009 onwards were also internally driven by regime insiders who saw the aftermath of the global financial crisis as an opportunity to strengthen the

MPLA's grip over the economy whilst also modernizing the financial sector and expand business opportunities.

The post-2009 regulatory reform stands out from the financial sector changes described in previous chapters, making the period important to study in its own right. Specifically, as the 2000s progressed and Angola's financial sector became increasingly interwoven into the international financial fabric, it was no longer possible for the country to ignore international demands in the banking sector as had been the practise in previous years. Doing so could have risked the country becoming isolated from international financial markets. Consequently, whilst politicians and banks still enjoyed some policy space in the late 2000s, their room to manoeuvre at this later point diminished because of stricter international rules confronting the country's financial sector. A main contribution of the chapter is that it shows how dwindling policy space influenced the choices of political leaders although they continuously enjoyed some scope for negotiation. In doing emphasising the constrains on political leaders' policy space, the chapter substantiates the claim put forward in the introductory chapters, namely that even when faced with ample resource revenues, political leaders in resource-rich countries like Angola rarely act unconstrained.

2. Cracks appearing in the status quo

When Angola entered into its first Stand-By Arrangement with the IMF in the autumn of 2009, safeguarding the position of the financial sector was a main priority of the Angolan authorities and a key pillar of the \$1.4 billion programme (IMF, 2009b). The regulation and supervision of Angola's banks had not kept up with the fast expansion of the sector in the years prior to the 2009 balance-of-payments crisis (Wallace, 2014; IMF, 2012). Basic

regulations governing banking sector activities had been put in place, including regulation to avoid large risk exposure by banks (Notice no. 5/96), a minimum capital adequacy ratio for commercial banks (Notice no. 4/07), a reserve requirement ratio (Instructive no. 02/00) as well as requirements concerning bank's loan loss provision (Notice no. 4/92).¹ Yet the IMF (2012b, p.27) noted that, "Despite key formal elements of the regulatory framework being in place, the sanctions framework is weak and enforcement is inadequate." For instance, the Fund showed that when it came to banks' provisioning for potential loan losses including bad loans, "the regulations on provisioning that appropriately require detailed evaluation of a loan's true worth are not being properly implemented by some banks. This has led to the situation where problem loans, which carry a government guarantee, have been neither properly recognized nor provisioned" (IMF, 2012b, p.27).

That the sector regulator, the BNA, had not been able to contribute to reducing financial sector vulnerability, and indeed lacked the monitoring mechanisms to do so, became obvious following the 2009 balance-of-payments crisis. Despite little direct credit exposure to the oil sector (de Morais, 2016),² the fall in global oil prices and the subsequent balance-of-payment crisis had a substantial impact on Angolan banks' balance sheets through trickle-down effects. From a high of \$147 per barrel of oil in July 2008, by December the price had dropped to only \$39.19 (Macalister, 2008). With oil revenues falling, in the first months of 2009 Angolan authorities faced sizeable financing needs and defaulted on payment obligations to domestic suppliers. The increase in government expenditure arrears in turn hindered domestic suppliers from servicing their loans, leading to a significant increase in non-performing loans (NPL) to those companies (IMF, 2012; IMF, 2015). From

¹ See online report by the Secretariat of the Committee of Central Bank Governors (2013).

² Commonly, large international oil companies would not rely on the domestic market for financing given their sizeable financing needs. Adding to this, Angolan service companies would often use foreign joint-venture partners to access cheaper financing abroad. Interview, oil service company, Luanda 5.11.2015.

2010 the rate of NPL in the banking sector increased with the situation worst in the public banks (see Table 1).³

Table 7.1: Non-performing loans to gross loans, 2003-2013

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
NPL to gross loans	9	8,1	6,4	4,8	3,8	4,7	4,2	6,5	6,8	7,8	9,7
NPL to gross loans public banks						5,1	4,9	9,3	21,95	16,65	23,85

Source: IMF (2015); IMF (2009).

The 2009 crisis also made it clear that little progress had been made in shielding Angola's banking sector from the significant risk linked to the large volume of foreign currency operations. In 2007, 70% of loans and over half of deposits were denominated in foreign currencies, mainly United States dollars (IMF, 2009; BNA, 2007; see also Castro e Silva, 2014). As mentioned in the last chapter, the high degree of dollarization largely came down to Angola's history of high inflation, and the dominant role of the dollar-based oil sector.⁴ The challenge arises if and when the local currency weakens, as it did in Angola in 2009 when the price of oil dropped. Locally-domiciled banks had lent substantially in dollars to domestic borrowers and most of these banks had not hedged their positions against exchange-risk. As the Economist Intelligence Unit (EIU) reported in the autumn of 2009, with the local currency sharply depreciating in October 2009, borrowers were facing

³ As noted by the IMF, "Analysis of NPL data is compromised by the fact that many loans are guaranteed by the state; when they become overdue they are not recorded by banks as such. BNA does not properly monitor this issue and banks could not provide consistent data to the FSAP. Moreover, there are indications that, even when lending is not directly backed by explicit state guarantees, certain banks may have adopted "ever greening" practices for government suppliers" (2012, p.12).

⁴ In the context of high and arbitrary inflation, holding assets in dollars can have advantages. As shown by de Nicolo et al. (2003), dollarization may help limit the impact of macroeconomic volatility on the broader economy. High rates of financial dollarization also contribute to systemic solvency and liquidity risks, and may seriously undermine the effectiveness of the government's monetary policy. See de Nicolo et al. (2003).

significantly larger repayments in kwanza terms (EIU, 2009b). The foreign currency shortage was further exaggerated by the lack of foreign currency in circulation, leading to a rationing of dollars from 2009 (EIU, 2009b). As Angolan private debtors struggled to service their dollar denominated debt, the volume of NPLs on banks' balance sheets rose (see table 1).

Simultaneously with the manifestation of fragilities in the banking sector stemming from the 2009 crisis, there was a growing unease amongst the country's international partners concerning the lack of compliance amongst Angolan banks. In February 2010, the United States Treasury endorsed a report by the inter-governmental anti-money laundering body, Financial Action Task Force (EIU, 2010a), which carried serious implications for Angola. The report blacklisted Angola, as one of five countries, on account of the risk that the country posed to the international financial system due to risk of money laundering and financing of terrorism (Financial Action Task Force, 2010). The same month, the United States Senate Permanent Subcommittee on Investigations issued a report demonstrating how international banks including HSBC and Bank of America had facilitated efforts to transfer Angolan state funds into private bank accounts, using the United States banking system (United States Senate, 2010). The report also showed how HSBC had breached United States law by allowing the Angolan bank BAI, access to the United States financial system even though HSBC did not have complete knowledge of BAI's owners (United States Senate, 2010).⁵ A few months after receiving criticism in the Senate report, HSBC cut correspondent banking ties with its Angolan counterparts and closed all banking branches in the country (Reuters, 2010; EIU, 2010d). This was followed by the decision of

⁵ Pursuant to the USA PATRIOT Act and final rules issued by the United States Department of the Treasury, United States financial institutions are required to obtain certain information from any foreign bank that it maintains a correspondent account with (Tompkins, 2002). Issues with getting information and corruption suspicions had led Citibank to exit Angola in 2003 (Reuters, 2010; EIU 2010d).

Bank of America in November 2010 to close the bank accounts of the Angolan embassy in Washington DC against the embassy's will.⁶

The difficulties faced by the Angolan financial sector were compounded by the fact that the BNA's credibility was particularly weak in the months ensuing the balance-of-payment crisis. During this time, information was emerging which implicated the sector regulator in a number of scandals. In late November 2009, investigations were launched into the illegal transfer of \$137 million from the BNA and the Ministry of Finance into offshore bank accounts, between 2007-2009. The incident led to the arrest of eighteen (lower level) officials from the two institutions and the confiscation of assets including luxury houses and sports cars (Human Rights Watch, 2010). Another case involved the stealing of \$1-2 million in cash from the BNA's safes over the 2009 Christmas holidays (EIU, 2010a). Adding to this, the US Senate report revealed that in 2002 the then-governor of Angola's central bank, Aguinaldo Jaime, had attempted to move \$50 millions in state funds into a private account in the United States through the HSBC (Reuters, 2010).

Jointly, the above-mentioned incidents contributed to confidence in the BNA's ability to effectively regulate the banking sector reaching a nadir. None of the highly ranked individuals implicated in the aforementioned incidents were formally penalized. In 2009, the same year that ex-governor Jaime became implicated in the Senate investigations (United States Senate, 2010), he was appointed chair of the National Private Investment Agency (ANIP), the government's then entity responsible for the execution of the national policy on private investment, including promotion, coordination, evaluation, approval and

⁶ Other embassies also had their accounts closed but Angola was the first foreign embassy to have all its accounts closed (Rogin, 2010).

supervision (Human Rights Watch, 2010).⁷ Arrests in the aftermath of the incidents targeted lower level officials in the BNA and the Ministry of Finance (EIU, 2010a).⁸ There was a need for the judiciary to be seen as doing something in pursuit of the lawbreakers, yet there were political limitations as to whom they could pursue and implicate in the crimes.⁹

This section showed that not only were the Angolan-domiciled banks taken aback by the effects of the 2009 balance-of-payments crisis, the banks also faced increasing scrutiny from the international community who questioned the financial sector's viability and its inclusion in the network of international finance. It was increasingly clear that something needed to be done to salvage the economic performance of banks and their standing. It therefore should not come as a surprise that in the aftermath of the crisis, notable reform measures targeting the broader economy and the banking sector specifically followed, as outlined in the next section.

3. Angola responds

Following the BNA scandals in 2009, the management team of the central bank was reshuffled in 2009 and then again in 2010. The appointment of José de Lima Massano as BNA governor in October 2010 was interpreted as an effort to reform the financial sector (Reuters, 2012; Reuters, 2011; Central Banking, 2010).¹⁰ Massano came from the position of chief executive of Angola's biggest private bank (by assets), the Banco Africano de Investimentos (BAI), as well as heading Angola's bankers' association (Bank Editor,

⁷ ANIP was after a few years replaced by the Agency for the Promotion of Investment and Exports of Angola (APIEX) (Lusa, 2015).

⁸ Interview, oil service sector representative, Luanda 03.11.2015

⁹ Interview, law professor public university, Luanda 22.10.2015.

¹⁰ Interview, banker foreign bank, Luanda 15.10.2015.

2009). The appointment of Massano was commended by the banking industry and international representatives alike (Reuters, 2011; EIU, 2010d). Massano joined another private banker at the helm of the central bank, Ricardo Viegas de Abreu, who had taken up the position as vice-governor the year before (Cruz, 2016). Together the private bankers turned civil servants overhauled the senior management of the BNA (EIU, 2011a). The appointment of a reformist team to lead the BNA was taken to signify a shift in influence back to the institution after it had “seen power ebb away from it in recent years” (EIU, 2010d). Moreover, observers saw the decision to shift the BNA’s management team in a more technocratic direction as a signal of the government’s seriousness in reigning in the financial sector (Reuters, 2011).¹¹

Following the change in the central bank management team, the Angolan authorities launched a number of financial sector reform measures from 2010 onwards. The aim of these efforts was to strengthen the banking sector and enhance its international credibility “as the country seeks to expand access to international financing” (EIU, 2011a; IMF, 2011). The reform drive happened in connexion with the IMF programme, which was initiated in the autumn of 2009. Within the central bank, a Department for Risk Management was created in 2010 with the purpose of creating mechanisms to support the management of liquidity, exchange rate and operational risk in the banking sector, after the 2009 crisis had revealed the high systemic solvency and liquidity risks facing Angolan banks (EIU, 2011a). A Monetary Policy Committee was established in August 2011 to oversee Angola’s overarching monetary policy (EIU, 2011b). Through the use of a ‘reference interest rate’, based on the new LUIBOR (Luanda Interbank Offered Rate), the committee (comprised of Board members of the BNA) was to help the BNA better manage domestic money supply

¹¹ Interview, banker foreign bank, Luanda 15.10.2015.

(World Bank, 2013). In May 2012, a Financial Stability Committee was introduced, which would act as an advisory body to the BNA Board of Directors (World Bank, 2013).¹² The Financial Stability Committee's responsibility was to support financial-sector stability through the development of guidelines and strategies for mitigating systemic risks, including a crisis-management framework (BNA, 2012).

Regulatory reform in the post-2009 crisis era also sought to reduce the dollarization of the Angolan economy and the exposure of locally-domiciled banks to foreign exchange risks (IMF, 2009b). The Angolan central bank had set de-dollarization as one of its goals at the end of 2009 (IMF, 2009a), subsequently launching several policies to support the process. Regulations introduced in 2011 imposed a capital charge on foreign exchange transactions and prohibited foreign exchange loans for certain purposes (such as consumer goods, car purchases, overdrafts, and short-term loans) (Lariau et al., 2016). The most notable effort at de-dollarization, however, was the new Foreign Exchange Law for the Petroleum Sector, placed before the country's National Assembly in November 2010 (Macauhub, 2010). Under the new law, locally domiciled banks would be obliged to hold a minimum 80% of capital in kwanza (previously, banks could hold all their capital in foreign currency). More drastically, the new law ordered oil companies to use locally registered financial institutions to pay subcontractors and service companies in Angola (Law no. 2/12 of 13 January 2012).

In November 2011, after at least nine years in the making,¹³ the National Assembly passed the foreign exchange law (Law no. 2/12), implementing it in two phases. In the first phase,

¹² Interview, senior civil servant Ministry of Finance, Luanda 30.9.2016.

¹³ Several informants told me that the law was proposed already in the 1990s. I have not been able to confirm any date in this regard so I will refer to the 2003 proposal as the initial date.

which came into force in early 2012, all oil companies operating in Angola were required to pay taxes to the Angolan treasury through local banks. In the second phase, in force from July 2013, oil companies had to make all payments through locally-domiciled banks, including payments to suppliers and contractors located outside of Angola. All payments were moreover to be executed in kwanza (IMF, 2012b).¹⁴

The post-2009 regulatory reform drive in the country also saw considerable emphasis being placed on modernizing the country's financial regulatory framework so as to be seen to conform to international best practice. Reform followed years in which Angolan policy makers and regulators alike had shown little concern with signalling their alignment with international best practice in the financial sector (Engebretsen and Soares de Oliveira, forthcoming). Upon his inauguration, BNA governor Massano stated his intention to bring "the banking sector up to international standards quickly" (Wallace, 2014). Already before taking up the position as BNA governor, Massano, then CEO of BAI and head of the Angolan Banking Association, had stressed the need to "put Angola in the context of today's developed financial industry" and "comply with international rules" (Bank Editor, 2009). According to the Association of Angolan Banks (ABANC), in 2010 an Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) action plan was announced following political commitment to address the deficiencies noted by the abovementioned 2010 FATF report (Association of Angolan Banks, 2017). The action plan was followed by the announcement of a AML/CFT Law in 2011 (Law no. 34/11 of 11 December). Gradual implementation of the International Financial Reporting Standards (IFRS), a single set of accounting standards recognized globally, started in 2014¹⁵ (KPMG,

¹⁴ Interview, administrative director Angolan private bank, Luanda 12.11.2015.

¹⁵ As of February 2017, seven of Angola's largest banks were implementing IFRS (Interview, partner in international accounting firm, Luanda, 11.10.2016).

2016). Less was done to align Angola's regulatory framework with the Basel international banking standards, with efforts remaining piecemeal and rudimentary until 2014 (see Engebretsen and Soares de Oliveira, forthcoming; IMF, 2012).

In contrast to the speed with which changes happened in Angola's banking sector, in the non-banking financial institutions sphere, progress was significantly slower. After having postponed the launching of a stock exchange open-endedly in 2010 (see chapter 6), the appointment of a new Board of Directors for the Capital Markets Commission¹⁶ in early 2012 led to the decision to "liquidate the old exchange (BVDA) and start over" (BODIVA, 2017). Capital invested in the old stock exchange was transferred back to its private investors and the plan was to start over with public money.¹⁷ New regulation covering the new stock and debt markets were published by the Capital Markets Commission and approved by Presidential decree in October 2013 (Presidential Decree no. 04-07/13 of 13 October). A new debt and securities exchange was launched in 2014 under a new name, BODIVA (BODIVA, 2017). Trading on the bourse did not start before May 2015 and in the subsequent years would include only government securities (Redvers, 2015; Macauhub, 2017).

Like the delays in the development of the capital markets, it was not before 2013 that steps were taken to further develop the market for insurance and pension fund services (KPMG, 2012). In order to address the outdated regulatory framework for the two sectors and attract new investors, Angola's Council of Ministers replaced the old sector regulator, the Instituto de Supervisão de Seguros, in 2013 (Angop, 2013). The new body, the Agência Angolana

¹⁶ The Capital Markets Commission is the regulator of the capital market, established in 2006.

¹⁷ Interview, representative Capital Market Commission, Luanda 18.11.2015.

de Regulação e Supervisão de Seguros (ARSEG), represented “a new body, with greater institutional weight and reinforced market intervention powers”, according to Aguiñaldo Jaime, coordinator of the working group appointed by the President to carry out the diagnosis and restructuring of insurance and pension funds (Ja, 2013). The regulatory update failed to stimulate much development in the sectors, however. The sectors remained small with narrow customer bases after the regulatory upgrading of 2013 (IMF, 2015).¹⁸

Although the domestic capital market remained underdeveloped, Angola did establish a sovereign wealth fund (SWF) in 2012 (Minto, 2012). Through the Fundo Soberano de Angola (FSDEA), the country was better placed to tap global capital markets and channel windfall earnings overseas (Wright, 2014).¹⁹ The initial endowment of \$5 billion made the FSDEA the fourth biggest SWF in Africa (Sovereign Wealth Fund Institute, 2018). The fund was moreover scheduled to receive annual inflows equivalent to 50.000 barrels per day (Presidential Decree No. 48/11 of 9 March).

The move by the government to establish the SWF was welcomed by the IMF as an appropriate tool for saving and investing Angola’s non-renewable resource wealth (IMF, 2014b).²⁰ IMF’s praise for FSDEA endured even if at the time of its creation, the SWF had been stripped of a mandate to stabilize the economy against fluctuations in global oil prices, a common function served by commodity-based SWFs (World Bank, 2013; Dixon and Monk, 2011). FSDEA quickly claimed adherence to international best practice in the

¹⁸ The Angolan state, through state-owned ENSA and Sonangol-owned AAA, dominated the insurance sector. The insurance companies in turn held significant stakes in the pension fund market (Samuel, 2015; Angop, 2017).

¹⁹ The intention to establish a SWF had already been announced by President dos Santos in 2008 (Wright, 2014).

²⁰ Up until this point, Sonangol had acted as the “de facto sovereign wealth fund, using billions of dollars to pursue an increasingly ambitious external investment policy” (Soares de Oliveira, 2015, p.49; Africa Confidential, 2008).

sector, including the Generally Accepted Principles and Practices or "Santiago Principles" created by the International Working Group of Sovereign Wealth Funds in addition to the Linaburg-Maduell Transparency Index, a rating established by the Sovereign Wealth Fund Institute (EIU, 2012).

In sum, the regulatory reform drive and financial sector changes in the aftermath of the 2009 balance-of-payments crisis marked a distinctive approach by the Angolan authorities to managing the financial sector. For the first time, it appeared as if political leaders were taking the concerns of international financial institutions, and international banks and their home regulators, seriously. Angolan public and private sector actors furthermore appeared eager to reap greater financial rewards through integrating into global financial markets. Yet, as this section has shown, the regulatory reform efforts were not even. Regulatory efforts were marked by delays and some parts of the financial sector being prioritized over others. The non-bank financial institutions stand out as an area where little work was done. Additionally, as will become gradually clear in the subsequent sections, there were political limitations as to what regulators could feasibly accomplish within the political mandate that they were given to rein in the banking sector.

4. Explaining the post-2009 regulatory drive

How to make sense of the government's willingness to bring a measure of reform to the financial sector, as witnessed in the aftermath of the 2009 balance-of-payments crisis? Politically, the MPLA was in a relatively strong position, having won the 2008 election with an overwhelming majority (Soares de Oliveira, 2015; Dugger, 2008). The party enjoyed strong popular support and there was little effective opposition from excluded factions. The new Constitution, approved by Angola's Parliament in early 2010, had further

concentrated power in the hands of President dos Santos (Jensen and Paulo, 2011; Dugger, 2010). Still, as the preceding sections have hinted at and the next section will more clearly show, everything was not well when it came to the country's economic performance.

4.1 Getting the economy back on its feet

In stark contrast to the solid political setting, the post-war economic model that the MPLA had based its power on, was considerably less robust in the aftermath of the 2009 balance-of-payment crisis, as the earlier sections of this chapter alluded to. Initially, many African countries appeared to have avoided the full impact of the global financial crisis of 2007-2008 (Moss, 2009). Whilst the crises in the US subprime mortgage market was turning into a full-blown international banking crisis in mid-2008, the Angolan economy was still riding on a wave of optimism. Oil prices were still relatively high and the country's GDP growth rates amongst the highest in the world (The Economist, 2011a). In an article from that year, the World Bank's Senior Economist in Angola predicted that only a marginal impact would be felt on Angola's financial sector from the global crisis, given amongst other factors; the absence of a stock exchange, the limited transaction flows with international markets and the low level of banking services (Gazel, 2008).

Yet by late 2008 Angola's economic situation had changed radically for the worse. Lower international prices meant that the Angolan state's tax income from oil (which accounted for 90% of total taxes) fell to \$14.6 billion in 2009, one third less than the revenues the state had obtained from the sector in 2007 (Jensen and Paulo, 2011; Ruhaak, 2010).²¹ In early 2009, Angola found itself in a balance-of-payments crisis, meaning that the country

²¹ Angola's foreign exchange reserves also dropped as the MPLA government struggled to ensure macroeconomic stability and avoid devaluation. Reserves went down from \$20.4 billion in November 2008 to \$12.5 billion in June 2009 (EIU, 2010a).

was unable to pay for essential imports and service its debt repayments (EIU, 2009a). The country's foreign exchange reserves had been cut by almost half, falling from \$20.4 billion in November 2008 to \$12.5 billion in June 2009 (EIU, 20010a). By June 2009, Angola had less than three months of import coverage left.²²

With economic performance considerably reduced, the political leadership found itself in a delicate situation. Pressure was strong to keep state spending high, with the MPLA government determined to maintain macroeconomic stability and high levels of public investments (EIU, 2009b). Yet attempts to attract new financing from both domestic and international sources were unsuccessful as the demand for Angolan government securities was weak both domestically and internationally (EIU, 2009a). The weakly developed capital markets, as described in last chapter, limited domestic financing opportunities for the Angolan state (IMF, 2009b).

In a bid to save resources, the state started accumulating arrears to domestic and foreign suppliers.²³ As the economic situation became increasingly precarious, the government was faced with few other options than to call on external assistance. Opening up to the international financial institutions (IFIs) was not without consequences, however. Angola would have to forsake some of its policy space, as borrowing from the IMF meant that the government agreed to adjust its economic policies so as to overcome the problems that had led it to seek financial aid from the international community in the first place (IMF, 2017).

²² According to The Economist (2011b), "One common rule of thumb is that reserves that can cover three months' worth of imports are adequate," although many countries hold considerably more to buffer against external crisis, including China and Russia, whose reserves cover more than two years' worth.

²³ The BNA calculated that the amount of arrears accumulated between 2008 and 2009 to be \$6.8 billion (World Bank, 2013). The IMF reported total arrears to be \$7.5 billion (IMF, 2012).

Historically, Angola had been reluctant to relinquish policy space.²⁴ Yet by late 2009 it seemed as if the government were faced with few other options than to go ahead with an IMF programme, which also meant subscribing to the fund's policy conditionality. As the next section shows, the conditionality included strategies to safeguard the stability of the financial sector.

4.2 'Foreigners' gaining increasing sway over reform agenda

With Angola signing up to external support in the form of an IMF programme in 2009, the country also opened itself up to greater external interference in its economic policies. This was also true for financial sector policies. Whereas the post-war reform agenda saw less direct influence by foreign entities, post-2009 saw the opening up to external support and engagement with international financial institutions, most notably the IMF. In the light of Angola's deteriorating economic situation, opening up to the IMF financing package was judged necessary to deal with the economic adversity that the country was facing (Soares de Oliveira, 2015, p.178). Angola was finding it increasingly difficult to access commercial loans as international investors were concerned about the long-term creditworthiness of the government, as the latter had built up several billions of dollars in arrears²⁵ to local suppliers and public-sector workers in an attempt to save resources (EIU, 2009d). The IMF loan would help ease the financial pressure that Angola faced, not only through the liquidity injection from the Fund itself but also through the seal of approval that the IMF agreement would provide, positively helping the authorities to access additional financing on the international bond market. Negotiations with the IMF commenced in 2009 and on November 23rd the same year, the IMF Executive Board approved a 27-month stand-by-

²⁴ As evident from the analysis of the IMF Angola relationship discussed in the earlier chapters. See Hodges (2004) and Soares de Oliveira (2015).

²⁵ Between \$6.8 billion and \$7.5 billion in arrears (World Bank, 2013; IMF, 2012).

agreement for Angola worth \$1.4 billion, one of the biggest IMF loans to be awarded to a Sub-Saharan African country (Soares de Oliveira, 2015).²⁶

As with all IMF packages, the IMF loan to Angola came with conditionality and an agreed plan for reform. Disbursements happened in stages given satisfactory progress by the Angolan authorities in carrying out the agreed programme (IMF, 2017). A key part of the stabilization and reform plan agreed by the two parties was Angola's commitment to strengthen the financial sector in the face of economic slowdown and to safeguard the sector from future possible crisis (IMF, 2009b). The agreed measures moreover focused on boosting the regulatory and supervisory capabilities of the BNA and limiting the banks' exposure to bad debt, by amongst other means, reducing the dollarization of the financial sector (IMF, 2009b).

At the same time as the country went ahead with the IMF programme, Angolan economic agents and policy makers were growing increasingly wary of the growing pressure on the country's banks deriving from regulatory pressure globally, as discussed earlier. Since the passing of the USA PATRIOT Act in 2001 (following the 9/11 terrorist attacks) international banks were forced to adhere to stricter regulation in what became an increasingly global effort to prevent money laundering and terrorist financing. At the centre of anti-money regulations was the requirement to 'Know Your Customer', obliging banks to verify the identity of their customers and the source of their funds (Global Witness, 2009). Whilst banks had to adhere to stricter regulations already in the early 2000s,²⁷ it was not until after the global financial crisis of 2008, the US Senate report of 2010 and the

²⁶ The loan was one of the largest IMF financing packages for a sub-Saharan African country during the 2008 global crisis (Leigh et al., 2009).

²⁷ Under the 1970 Bank Secrecy Act, US banks were already required to perform due diligence on their customers (Global Witness, 2009).

FATF blacklisting that same year, that Angola's compliance deficiencies appear to have become a serious concern for international banks doing business in the country or with Angolan entities abroad.²⁸

Angolan authorities appeared stunned when two major international banks decided to cut business with Angola, as mentioned earlier in the chapter, following revelations by US authorities in 2010. The magazine *Foreign Policy* reported that the Angolans felt insulted and were considering reciprocity measures, including "closing the bank accounts of the U.S. embassy in Angola, refusing to receive the credentials of incoming U.S. Ambassador Christopher McMullen, or closing the bank accounts of U.S. companies in Angola, such as Chevron, Exxon, BP, and Boeing."²⁹ The general anxiety following the global financial crisis is likely to have added to international banks' decision to reduce exposure to the Angolan market. Yet, banks' de-risking was likely also driven by heightened reputational concerns on the part of the international banks in the face of increasing pressure from home regulators. "Banking business has become dominated by compliance and this is related to fear, because the consequences are so high," complained the administrative director of one Portuguese bank. Most cautious, the administrative director added, were the Anglophone banks. The description matches what the United States Senate noted in their 2010 report, "some U.S. financial institutions have decided to subject Angolan accounts to enhanced due diligence and monitoring; some have decided not to open such accounts at all" (United States Senate, 2010, p.247).

²⁸ An exception is Citibank who pulled out of Angola already in 2003 (Reuters, 2010; EIU 2010d)

²⁹ For clarification BP is a well-known British multinational. That Angolan officials felt insulted by the maltreatment in the United States was confirmed by *Africa Confidential* (2010).

Given the external orientation of the economy and the importance of ensuring local banks' access to international financial markets, the actions taken by international banks in the light of increased regulatory pressure globally, is thought to have prompted Angolan bank regulators and banks alike into action. As the administrative director of one private bank put it, "in Angola, we can have economic and political independence but in order to be part of the international financial market we need to adapt. *We cannot afford to be loners.*"³⁰ There was a need to respond to international concerns over the lack of compliance amongst locally-domiciled bank's or face the risk of being alienated from international finance circles. In order to guarantee the connection to global financial markets, Angolan banks could not afford to be seen as not adhering to (in cases even acting in conflict with) international best practice. The statement by another private banker further corroborates this claim, "it was only in the years after the crisis that banks started getting proper compliance departments. Foreigners were instrumental in driving this. International banks pressured local banks to heighten their compliance standards. Angolan banks were not necessarily doing it because it was good in its own right, or because it made good business sense. Rather, they did it because they knew that if they didn't they would be shut out from international finance."³¹

As the examples above illustrate, with Angolan authorities in a more precarious economic situation, the government had less power to resist external pressure for greater regulation and supervision of the financial sector, particularly of the banks, in line with international best practice. External pressure therefore stands out as an important driving force behind the regulatory drive that helped advance the sophistication of Angola's financial sector

³⁰ Emphasis added by me. Interview, administrative director of Angolan private bank, Luanda 12.11.2015.

³¹ Interview, banker Angolan private bank, Luanda 22.9.2016.

post-2009. Yet, for reasons described in the next section, external pressures are not sufficient to explain why Angolan political leaders were ready to institute changes in the financial sector after 2009.

4.3 External pressure: A necessary but not sufficient condition

Whilst external pressures in the form of IMF conditionality and demands for greater compliance by banks to conform to international best practice certainly are important in explaining the regulatory drive in the financial sector after 2009, I argue that these pressures were not sufficient in themselves. Firstly, whilst the Angolan authorities found themselves in a position where they were required to seek the help of the IMF, the authorities still enjoyed some leeway vis-à-vis the Fund. Importantly, as the third largest economy in Africa, Ministry of Finance representatives confirmed that the fund had been eager to set up its first programme in Angola.³² “The IMF” writes Soares de Oliveira (2015, p.178), “keen on becoming involved in one of Africa’s star economies, had grown tolerant of Angolan particularities”, offering the country more generous terms than it had to other African countries. The post-2009 regulatory reform can therefore be seen less as a case of the IMF imposing a ready composed policy agenda on the country but rather, the Angolan authorities having the power to select the reform policies that aligned with regime priorities (Shaxson, 2009; Ferreira and Soares de Oliveira, forthcoming).³³ Such a careful selection of policy alternatives also took place within the financial sector. As Engebretsen and Soares de Oliveira (forthcoming) describe, when the IMF and World Bank carried out a Financial System Assessment Program in the country in 2012, a prominent Angolan official

³² Interview, senior civil servant Ministry of Finance, Luanda 26.10.2015.

³³ Angola was picking and choosing reform efforts also in the proceeding decades. Shaxson described how, prior to 2009, Angolan policy makers would consider the advice offered by IMF, Brazilian, Portuguese, Chinese, and other consultants and then select the advice (and technical support) that they liked while rejecting the rest (2009, p.54; EIU, 2008a).

commented that the exercises represented first and foremost “a [diagnostic], not a roadmap for reform”.

A second factor that speaks in favour of external pressures being important in explaining reform momentum whilst not being the decisive factor is that whilst international pressures on countries like Angola were intensifying — in an effort to improve regulation and supervision of banks and on the domestically domiciled banks to better their governance — such pressure did not yet pose a serious threat to the interconnects of the Angolan financial system and the larger economy.³⁴ At this point, oil prices were still high. Whereas some international banks, most notably HSBC, concluded that doing business in Angola was no longer worth the risk, other international investors did not share this concern and continued doing business in the country. Standard Bank of South Africa gained their banking licence in the country in 2010, Standard Charter and pan-African bank Ecobank in 2014 (Deloitte, 2014).³⁵ As the chief executive of Togo-based Ecobank, Albert Essien, stated to Bloomberg in 2014, “We have to be in Angola”, adding that “Angola is one of the big four revenue generators” in Africa (Bloomberg, 2014). Similarly, Robert Lewis, the then head of the second-largest insurance provider in Angola, GA Seguros, explained in an interview with Forbes how, “The world is Angola mad right now” (Forbes Africa, 2012). GA Seguros was bought the following year by Moroccan insurance company Saham Finances for an undisclosed sum (Reuters, 2013b).

All this to say that while there was a heightened emphasis by Angolan authorities on strengthening the country’s regulatory and supervisory framework along the lines of

³⁴ The pressure only became overbearing following the oil price fall in 2014.

³⁵ Interview, representative foreign bank, Luanda 1.09.2016.

international best practice from 2009, the Angolan government are likely to have had only weak incentives to push ahead with implementation at this time considering the considerable interest of foreign investors, discussed above. Before 2014, Angola's regulatory deficiencies were not seen as jeopardizing the country's cross-border banking relationships.³⁶

Finally, an explanation which only considers the external pressure that the Angolan government faced post-2009 fails to take into account that whilst the effect on the broader economy from the balance-of-payment crisis was severe, it was also brief. By the second half of 2009, the Angolan economy was already improving (EIU, 2009d) and by mid-2010 the country's foreign exchange reserves had already reached comfortable levels, exceeding \$15 billion (EIU, 2010b; Gumbo, 2018). As for the banks, one IFI representative explained, it "took them 1-2 years to clean up, then they enjoyed good years again. By 2010 the [financial] system had resumed and soon it accelerated."³⁷

Yet even as the urgency prompted by the crisis started to disappear by 2010, the reform momentum endured. Central reforms, including the new foreign exchange law for the oil sector, was passed by the National Assembly in 2012, after the Angolan economy had started to recover. This suggests that a reform momentum was building up internally even after the performance of the bank and the economy more broadly had rebounded. Poor economic conditions and the external pressure that resulted from it, can therefore not by itself explain why the regulatory reforms took place. To fully understand the regulatory

³⁶ This political calculus would change after 2014, however, as Angola's cross-border banking relationships increasingly came under threat. For more on the change in regulatory emphasis see Engebretsen and Soares de Oliveira (forthcoming).

³⁷ Interview, representative IFI, Washington DC 10.12.2016.

drive after 2009, internal politics must also be considered, which will be the objective of the final section.

4.5 Internal impetus for financial sector reform

The persistence of a reform drive in spite of circumstances listed in the last section — assumed to have reduced the leverage of external actors pushing for regulatory reform in line with international best practice — points to the emergence of a momentum for financial sector reform that went beyond responding to external pressure as economic performance worsened. The existence of an internal reform momentum has also been pointed out in other studies, notably Soares de Oliveira (2015), Ferreira and Soares de Oliveira (forthcoming), and Engebretsen and Soares de Oliveira (forthcoming).

Yet, the above-mentioned authors do not elaborate on how a regulatory upgrading of the financial sector post-2009 aligned with the goals of the regime, in turn rendering the government willing to pursue regulatory reforms beyond what was necessary in response to the crisis. In the last section of the chapter, I make a first attempt at demonstrating how strengthening regulation and supervision of the banking sector was beneficial for the ruling elite, which in turn is likely to have encouraged the government to pursue regulatory reform also when the danger posed by the balance-of-payments crisis started to wane shortly after 2009. Strengthening the regulatory framework allowed authorities to better control the financial sector. Moreover, regulatory reform opened up opportunities to the financial sector, and the ruling coalition, that had previously been unavailable.

When explaining the post-2009 regulatory reform drive, one needs to consider the MPLA ruling coalition's desire to regain control over the economy after the 2009 balance-of-

payment crisis destabilised the country's macroeconomic balance. An important part of MPLA's post-war legitimacy was based on the party's ability to ensure macroeconomic stability after years of currency fluctuations, large debt burdens, and unmanaged inflation (Soares de Oliveira, 2015). The 2009 crisis as outlined so far in this chapter threatened the post-war macroeconomic stability that the MPLA had worked hard to ensure. The oil price fall of 2008 left the Angolan government exposed to a point where they were forced to seek external assistance, a situation that the country had not found itself in since the late 1980s. The general consensus was that the financial sector had added to this in a negative way, exacerbating financial instability (Wallace, 2014). It was thus not unexpected that in the aftermath of the 2009 crisis, the government were eager to regain control over the economy, including stricter financial sector regulation. The inclination of the government to regroup was confirmed by one IFI representative, who recalled that "The [2009] crisis was a wake-up call... The authorities were ill prepared for the situation that the country found itself in and they understood that they needed to be better prepared in the event of a future crisis if not to lose control again".³⁸

One area of particular concern to the authorities and external actors alike was the vulnerability of the economy as a result of the excessive dollarization. The high dollarization meant that the Angolan domiciled banks (and indirectly the state) faced considerable liquidity and solvency risks over which the BNA as regulator had little control (IMF, 2009).³⁹ Limits on foreign exchange positions and capital requirements for open foreign exchange positions were consequently established soon after 2009 (IMF, 2012).The

³⁸ Interview, IFI representative, Luanda 8.10.2015.

³⁹ According to the Heysen, "Liquidity risk in dollarized systems occurs when there is inadequate backing for the dollar liabilities of banks... The main solvency risks in partially dollarized financial systems result from currency mismatches in balance sheets and the effects that large depreciations of the local currency can then have on net worth" (2005, p.44-45).

high degree of dollarization was also undesirable for the government from the perspective of monetary policy because it limited their ability to influence the latter through the adjustment of the money supply (Yeyati, 2005) The administrative director of one bank explained how, controlling inflation was inherently difficult for the government as long as the use of dollars was widespread.⁴⁰ Efforts to de-dollarize the economy and the financial sector was therefore also an issue of the state wishing to strengthen their control of the economy. As one former top official in Sonangol explained, “to be against it [de-dollarization] was to be seen as being unpatriotic”.⁴¹

In addition to a desire for greater control over the sector, President dos Santos and his government undoubtedly appreciated that better regulation of the financial sector would bring added benefits to the country’s financial sector by opening up opportunities that had previously been out of reach due to the Angolan banks’ poor governance and lack of credibility (Soares de Oliveira, 2012).⁴² Up until this point, Angolan domiciled banks had limited access to foreign exchange markets and the lack of an AML/CFT regime allegedly hindered the banks’ ability to engage in cross border activities (EIU, 2010d). For example, attempts at transforming Angola into a financial sector hub for the region had been met by limited enthusiasm (IMF, 2012).

Broadening opportunities in the financial sector is expected to have been important to the regime as the profitability of locally domiciled banks had started to wane around the 2009 crisis. As noted by KPMG, “the Angolan banking sector presents, since 2010, a decreasing

⁴⁰ Interview, administrative director Angolan private bank, Luanda 12.11.2015.

⁴¹ Interview, representative oil service company, Luanda 5.10.2015

⁴² According to Soares de Oliveira (2012, [online]), the regime acknowledged that “many of the measures suggested were good in their own right and would greatly improve the system’s managerial and technical capacity.”

tendency of profitability levels.” Return on average assets,⁴³ a common measure of banks’ profitability, fell from 4.1% in 2005, to 3.4% in 2010, to 1.6% in 2012 (Deloitte, 2006; Deloitte, 2011; KPMG, 2015b). From enjoying particularly high profitability levels at the start of the 2000s, Angolan banks were now close to the African average (IMF, 2010, p.15). One reason for the falling profitability of banks was that banking business was changing. Following the end of the civil war, bank activities had largely been state-connected. Whilst some credit was extended to SOEs, real estate, construction, and trade finance,⁴⁴ the majority of banks’ assets were held in the form of government securities. As pointed out earlier, initially these securities generated extremely high interest rates, as much as 50%-60% return, reflecting the government’s need for money in the early reconstruction period (EIU, 2006b). Yet by 2006-2007 the yield on securities had dropped to approximately 10-15%, as the government’s need for borrowing diminished (USAID, 2008). As encapsulated in the words of António Henriques, chief executive of Banco Millennium Angola,⁴⁵ “The [banking] industry is facing huge challenges because traditional, safe sources of revenue have decreased” (Wallace, 2014, p.6).

Another factor asserting pressure on the profitability of the banks was the growing number of new banks entering the Angolan market. The concentration in the banking sector lessened from 2009, as the assets of Angola’s five largest banks as a percentage of total assets started falling (Deloitte, 2013).⁴⁶ With greater competition in the sector, it was clear that levels of profitability that had characterised the initial reconstruction period were not

⁴³Return on Average Assets (ROAA) measures the efficiency of a bank in using its assets to generate net income. ROAA is calculated by taking net income and dividing it by average total assets.

⁴⁴ Interview, representative IFI, Washington DC 8.12.2016.

⁴⁵ From 2016 known as Banco Millennium Atlântico following the merger of banks Banco Millennium Angola and Banco Privado Atlântico in 2015 (Angop, 2016).

⁴⁶ The concentration of system-wide assets in the five largest banks was still high, however, accounting for 70 % of the total in 2011 (IMF, 2012b).

sustainable (Ferreira and Soares de Oliveira, forthcoming). Taken together, falling interest rates and increasing competition meant that banks' profitability ratios peaked in 2008 (Wallace, 2014). For the Angolan financial sector to extend its reach and attract new business, it was necessary to address issues of compliance and their poor reputation.⁴⁷ A representative of the capital market commission explained, "Previously, there was no need to attract FDI [foreign direct investments] or discipline the banks and therefore policy makers did not pay much attention to compliance. This was the prevalent mind-set until 2008. But it changed. After 2008 there was increasing pressure to abide by international standards so as to attract investors."⁴⁸

The quest to attract external financing and banking partners raised particular challenges for the Angolan-domiciled banks. As the administrative director of one Angolan private bank emphasized, "The bad reputation that the country's banks suffer, contribute to a pressure for compliance from foreign counterparts."⁴⁹ The new regulations issued by BNA governor Massano, aiming to bring Angolan banking regulation in line with international best practice, saw Angola's biggest banks make the first steps towards strengthening AML/CFT regulation and risk management from 2010. These efforts were rewarded. In January 2014, BAI received a credit rating from credit rating agencies Fitch and Moody's, becoming "the first company in the Angolan private sector to gain such international credentials."⁵⁰ The credit rating was an important first step as the bank sought to tap into international credit markets.

⁴⁷ The dominant focus of Angolan domiciled banks had always been to take advantage of international markets rather than penetrating internal ones although the bank penetration rate increased from 2009 when bank services became more accessible. By 2015 the country boasted the second highest commercial bank branch penetration rate on the continent (KPMG, 2015b, p.3).

⁴⁸ Interview, representative from capital market commission, Luanda 18.11.2015.

⁴⁹ Interview, administrative director Angolan private bank, Luanda 12.11.2015

⁵⁰ Theodore Giletti, Director of BAI, speaking at Chatham House (2015). See also BAI (2014).

Aligning with international best practice was also important for the newly-created SWF. The FSDEA was set up as a vehicle for government strategic investments (Redvers, 2014; Pitcher, 2017), with over a third of the fund's portfolio destined for securities and currencies. The remaining two thirds of the fund were placed in seven open-ended private equity funds, reserved for investments in everything from hotels to timber, in Angola and abroad (FSDEA, 2016). To successfully access markets abroad, it was crucial for funds like FSDEA to assure host states of the fund's proper governance and alignment with international standards (Hancock, 2013). Existing concerns that SWFs had been used as foreign policy tools or producers of market distortions had led recipient states of sovereign investments "to intensify their screening procedures for the admission of sovereign investments" (Bismuth, 2017, p. 74).⁵¹

Boasting a stronger legal and regulatory framework, Angolan financial sector institutions and regulators were more importantly able to sway international oil companies (IOCs) to channel their financial transactions through the domestic financial system from 2012, thus helping to boost transactions in the banking sector (IMF, 2009). Prior to 2009, Angolan authorities had tried to push through regulations that would ensure the financial sector reaped greater benefits from the foreign currency flows generated by the oil sector.⁵² In late 2003, the BNA announced the government's intention to pass a law that would require oil companies operating in the country – including national oil company Sonangol - to pay

⁵¹ The political and economic concerns of recipient states was part of what motivated the Santiago Principles (Bismuth, 2017). "The Santiago Principles promote transparency, good governance, accountability and prudent investment practices whilst encouraging a more open dialogue and deeper understanding of SWF activities" (International Working Group on Sovereign Wealth Funds, 2008).

⁵² The issue of altering the system, so as to encourage multinationals to bring their financial operations into the country, had already emerged with the establishment of a market economy in 1991 but foreign oil companies were quick to dismiss the initiative at the time. Interview, September 2015, Luanda, Angola.

taxes owed to the Angolan state through domestic commercial banks.⁵³ This thinking was in line with the government's broader policy of increasing local content in Angola's petroleum sector, including requiring procurement of Angolan goods and services (Ovadia, 2012). For the banking sector and its proprietors, such a law would vastly increase the assets under its control. The senior executive of one IOC explained the country's situation in the following terms, "billions of dollar transactions were being done outside of Angola. The sale of oil was happening outside, cash calls, all payments for services, also that being provided by Angolans. When we rented property for expats we would pay the Angolan owner in accounts he was holding outside of the country. The government wanted to change this, naturally."⁵⁴

From the time the idea was floated in the early 2000s,⁵⁵ IOCs quickly dismissed the proposed law (Ovadia, 2012).⁵⁶ IOCs complained about the simplicity and lax regulation of the Angolan banking sector, describing the proposed law as the "most significant threat to oil company operations in Angola for many years" (Deloitte, 2013; EIU, 2014, p.18).⁵⁷ The Angolan banks were deemed incapable of handling the volume of and sophistication of transactions that the oil companies required. The IOCs' concerns were backed by the IMF, who in their 2005 Article IV report on the country cautioned that "the annual flows in questions are several times greater than the banking system's current deposit base" (2005).

⁵³ Interview, BNA representative, Luanda 23.10.2015. See also Ovadia (2012) for a description of the early efforts to push through the foreign exchange law for the oil sector.

⁵⁴ Interview, managing director foreign oil company, Luanda 10.11.2015.

⁵⁵ Several of my informants claimed that the idea had already emerged with the establishment of a market economy in 1991 but I was not able to verify this claim.

⁵⁶ Interview, manager of a local service company, Luanda 3.11.2015; Interview, BNA representative, Luanda 23.10.2015.

⁵⁷ Like other local content initiatives, the financial regulation was accused of contradicting the terms of the original contracts, thus threatening to make operating more expensive (Ovadia, 2012).

Nonetheless, given the more demanding situation that the banks and the economy in general faced by 2009, the earlier discussion of securing greater local content in the oil sector regained momentum following the crisis. The law was proposed afresh by the new BNA leadership in 2010 under the name of Foreign Exchange Law for the Petroleum Sector (IMF, 2012). This time the BNA leadership enjoyed the backing of high-level officials from the inner circle of the Presidency, amongst them former BNA-governor Aguinaldo Jaime (EIU, 2008a;).⁵⁸ Jaime was in late 2008 appointed by the President to head a new commission responsible for boosting foreign investments in the non-oil sector, including revising existing foreign exchange incentives (EIU, 2009c). At this point, opposition from the IOCs to the implementation of the law was notably less, leading to the approval of the law in 2011. Speaking to the Dow Jones Newswire, the Vice President of IOC Maersk Oil, active in Angola since 2005, even went as far as stating that the new law was going “in the right direction”.⁵⁹

How does one account for the IOCs’ changed standpoint leading to the passing of the foreign exchange law for the oil sector in 2011? By 2011 it had become clear that in contrast to previous attempts, post-2009 Angolan authorities were able to offer IOCs the credible commitment that their business in the country would not be compromised with the implementation of the law. Crucially, efforts to modernize the financial sector after 2009 meant that biggest banks were capable of handling the type and size of transactions that the oil sector needed.⁶⁰ BNA’s regulation and supervision of the sector was seen by the IOCs

⁵⁸ At an industry conference in June 2006, Aguinaldo Jaime then deputy prime minister criticized foreign oil companies for holding their deposits in offshore accounts, a practice thought to be highly advantageous for the oil companies and enabling them to maintain high levels of secrecy over payments.

⁵⁹ Jon Ferrier, Vice-President of Maersk Oil, quoted by Agyeman-Togobo (2011).

⁶⁰ The IOCs played an important part in helping the banks modernize their services to fit the needs of the banks (Sobrinho, 2012; Reuters, 2012; Interview, administrative director of Angolan private bank, Luanda 12.11.2015; Interview, representative of Angolan private bank, 20.11.2015).

as having improved, helping to put the latter at ease (McClelland, 2012).⁶¹ Even the IMF, which generally disapproves of administrative measures such as “forced de-dollarization”, was overall sympathetic to Angola’s efforts to strengthen the banking sector, viewing it as part of the efforts to lessen the country’s exposure to foreign currency (Staines, 2014).

Overall, the foreign exchange law accomplished two important objectives on behalf of the regime. Firstly, through the de-dollarizing of the economy, the Angolan state gained greater control over the foreign exchange flows from the oil sector and the efficiency of monetary policy could thus be enhanced, as discussed above. Secondly, the law helped deepen Angola’s financial markets, contributing to an expansion of assets under the control of Angolan banks (IMF, 2014). This was the original objective when the law was proposed in 2003. In the post-2009 environment, as locally-domiciled banks were facing declining profit margins, requiring the oil sector to direct billions of dollars into the country’s banking system, was particularly welcomed. By 2015, the foreign exchange law had boosted flows into the Angolan banking system by \$30 billion (George, 2015). The same year, the IMF reported that the dollarization of Angola’s banking system has substantially decreased as a result of the BNA’s aggressive de-dollarization policies in which the foreign exchange law was a central part (IMF, 2015).

5. Conclusion

This chapter has focused on the post-2009 regulatory reform drive, which saw the Angolan financial sector becoming more “transparent and sophisticated”, in the words of industry magazine *The Banker* (Wallace, 2014). Initially, it appears straightforward why the

⁶¹ Interview, managing director foreign oil company, Luanda 10.11.2015; Interview, administrative director of private Angolan bank, Luanda 12.11.2015.

government would wish to reform the sector at the time. The difficult economic situation that the country found itself in following the balance-of-payments crisis in 2009 drove the authorities to seek the help of the IMF, bringing with it a set of conditionalities on how the financial sector should be regulated and supervised. Adding to this, foreign investors were growing increasingly wary of the Angolan financial sector's poor credibility and weak regulatory framework.

Yet as the chapter makes clear, the above factors do not fully explain why the government chose to initiate financial sector change at this time. Reform momentum prevailed also after the economy started recovering and the reliance of the Angolan state on the IMF lessened. Adding to this, the chapter shows that the pressure exerted by the IMF and foreign partners was strong but never overbearing. I therefore argue that in order to explain financial sector change one needs to also consider the internal impetus for such change. In the last section of the chapter I move beyond existing scholarship to suggest what these internal motivations may have been. Firstly, I show how the regulatory drive post-2009 aligned with the government's desire to reclaim control over the economy and importantly, its monetary policies. The ability of the MPLA to assert power over the economy in the post-war area was key to building the party's legitimacy. The unchecked growth of the banking sector appeared to undermine this control and thus it was in the interest of the MPLA to contain the sector and better supervise it. Secondly, a seemingly better regulated, more credible, financial sector presented opportunities that previously had been out of reach of the banks, even if the record of implementation overall continued to be erratic. The example of the foreign exchange law for the oil sector stands out in this regard. The foreign exchange law not only boosted business opportunities of certain banks, it also contributed towards

achieving the authorities' goal of de-dollarization, which in turn allowed authorities to strengthen their control over the Angolan economy.

By 2014, Angola's financial sector looked changed. After a short slump, the growth of the Angolan financial sector had not only resumed its pre-2009 level but it had accelerated.⁶² Observers were optimistic that the banking sector seemed headed down the right track, with international investors increasing their stakes. Yet two happenings in 2014 challenged the view that the sector had really transformed. The collapse of one of Angola's biggest banks, Banco Espírito Santo Angola (BESA), subsidiary of Portuguese Banco Espírito Santo, exposed the political limitations of the financial sector regulatory drive. Angola's second largest bank,⁶³ BESA managed to accumulate over \$5.7 billion in bad loans before the mismanagement was disclosed in the summer of 2014 (CNBC, 2014; Africa Confidential, 2014).⁶⁴ BESA could not identify many of its customers, although it emerged subsequently that many were part of the ruling elite and the President's inner circle (Reuters, 2014; Africa Confidential, 2014). The political contours of the case, including direct presidential involvement, meant that regulators were reluctant to intervene at an earlier stage even though "It was obvious to everyone that something bad was going on."⁶⁵

Additionally, the fall in global oil prices that began in 2014 made it clear that the high risk for operating in Angola was less appealing to foreign banks. Prior to 2014, international banks were willing to overlook growing compliance costs. Sector regulators and bankers

⁶² Interview, representative of IFI, Washington DC 8.12.2016.

⁶³ Late 2013, BESA was the leading lender in Angola with a market share of 27% (Africa Confidential, 2014).

⁶⁴ According to the EIU (2014), BESA had over-extended loans—reportedly equivalent to about 220% of its deposits. In December 2013 the Angolan government extended a state guarantee to support \$5.7 billion of its \$8 billion credit book.

⁶⁵ Interview with representative of international financial institution, Washington DC, December 2016.

alike largely enjoyed the policy space to approach financial sector regulatory reform in their own time (and according to their own political agenda), as this chapter has shown. With the global fall in oil prices the volume of transactions in Angola's financial sector decreased and investments in the country were no longer generating sufficient returns to make up for the sizable risk. As a result, several banks chose to withdraw. Reflecting on the analysis of this chapter it thus appears as if the policy space of the government was shrinking, exerting greater pressure on regulators to bring the financial sector into line with international best practice so as to allow the sector to continue operating. What the outcome of this process will be remains to be seen as the developments of the post-2014 era is still unfolding. Recent developments do, however, call into question the sustainability of the financial sector model described in the thesis in the wake of the greater pressure for financial sector compliance globally. In the final chapter, the conclusion, I will look back at some of the characteristics of the case described in the course of the thesis and consider its applicability to a broader set of cases that share Angola's features.

Chapter 8

Angola and beyond: Wider theoretical and comparative lessons

1. Introduction

This thesis focused on financial sector change in the context of resource-rich authoritarian countries. It has shed light on the question of what drives authoritarian resource-rich countries to introduce financial sector change, building on the case of Angola. The research question was chosen after it was established that existing scholarship appears unable to account for the significant variance in financial sector performance and characteristics that exist over time within the countries that in the introductory chapter was defined as resource-rich and authoritarian. Existing scholarship has also fallen short in accounting for the variation between countries that are often clustered together based on the weakness of their formal political institutions and/or abundance of resource wealth. Whilst the thesis sheds light on both gaps in the literature, the emphasis is on the former.

The thesis has presented an in-depth study of Angola and the evolution of the financial sector in the country post-independence. The emphasis has been on the years between 1991 to 2014, the period when the foundations of the country's modern financial sector were laid. 2014 was chosen as the end-point of this study as it is the year that the current weakening of global oil prices started, a process that is still unfolding. Given the little existing knowledge of the politics of finance in authoritarian and resource-rich contexts, a heuristic case study approach was deemed appropriate as it allows one to inductively

identify new hypotheses, variables and causal mechanisms to explain the outcome of interest (George and Bennett, 2005). Angola was chosen for the case study as the country represents a typical case of a resource-rich authoritarian country, as discussed in the introductory chapter. As a typical case, it is assumed that the study of Angola will produce insights into what drives financial sector institutional change in an authoritarian and resource-rich country that will resonate with other countries that share its characteristics.

The objective of this concluding chapter is to synthesize the findings of the thesis and to provide an overview of the main implications of the study, demonstrating the wider relevance of the findings from the Angolan case to the theoretical debates identified at the beginning of the thesis as well as to shed light on other country case studies. Finally, I will reflect on the limitations of the study and avenues for future research.

2. The Angolan case: Challenging existing explanations and the predominant notions of financial sector performance

The thesis seeks to present a new explanation of the drivers of financial sector change, drawing on components of the political settlements framework as developed by Khan (1995; 2010; 2017). Specifically, I make use of the political settlement framework to understand why and when financial sector change takes place. The political settlements framework posits that for social order to prevail, the distribution of resources from a society's prevailing institutional structure needs to be aligned with the distribution of power. According to the framework, institutional change transpires if the distribution of resources becomes misaligned with the distribution of power. Change can also occur if the economic performance of prevailing institutional structures no longer meets the expectations of those in society on which political leaders depend on for support. The type

of institutions that the ruling coalition favour is moreover understood to depend on its internal structure (that is, the strength of lower-level elite factions also called the vertical distribution of power) and the position of elites and their supporters within society (that is, the strength of excluded factions also called the horizontal distribution of power) (Khan, 2010). Scholarship building on the framework as presented by Khan (2010) has been criticized for understating the role of international factors in shaping a country's political settlement (Hickey, 2013). Recognising that international forces combined with a country's geo-political position "fundamentally alters the character of bargaining both between elites and between elites and lower-level groupings" (Hickey, 2013, p. 20), it was considered necessary in this thesis to go beyond the prevailing political settlement framework as presented by Khan (2010) to also consider how external actors influence why and when financial sector change happens.

Based on the above approach, the thesis argued that Angola's political leaders instigated institutional change in the financial sector to ensure the political support of their constituency, consequently maintaining MPLA regime's position in power. The direction of institutional change and the regime's ability to pursue their policy agenda in turn depended on the policy space that the latter enjoyed vis-à-vis domestic and international actors. In both instances, resource revenues were a central factor, as these represent the bulk of state revenues and thus significantly impact on the state's ability to spend. In the case of domestic factors, the power of the threat posed by UNITA until 2002 was deemed central to explain whether the MPLA preferred short-term policies or was able to take a longer-term view. Access to oil revenues was one important reason why the MPLA managed to eradicate UNITA as a military threat from the late 1990s. When it came to external factors, I argued that the government's ability to pursue their own policy agenda

depended on the state's access to resource revenues. When the global price for oil was low, Angola's dependence on external financiers grew, leaving the latter greater sway over the country's policies. On the contrary, when oil prices were high, the regime's policy space widened as the influence of external financiers dwindled, empowering the former to follow their own policy agenda with little external interference.

The logic of the argument becomes clearer as we turn to the empirical chapters, which each focus on Angola's postcolonial financial sector. The chapters suggest how the causal mechanisms played out in order to produce the outcome of interest, namely financial sector change.

Chapter 4 explains how extremely poor economic performance was threatening the viability of Angola's political settlement in the late 1980s. Several factors contributed to producing this situation. Global oil prices fell considerably in the mid-1980s, cutting Angola's government revenues drastically. Additionally, the end of the Cold War had severe economic impact on countries like Angola, who depended on the Soviet Union and to a lesser extent its allies for financial assistance. The adverse external conditions were exacerbated by the unsuccessful economic policies that Angola had pursued since independence. In order to ameliorate the economic situation and appease political supporters, altering economic policies was inevitable. Adverse economic but also the political circumstances at the time meant that the only viable option for the government was a measure of political and economic liberalization, including financial sector opening. However, even when faced with a particularly adverse economic situation, Angolan political leaders influence over the procedure of financial liberalization was notable. Unlike other African states during this period, Angola had not agreed to a structural adjustment

programme with the international financial institutions,¹ offering the country greater policy autonomy than its peers.² The government used their power vis-à-vis external actors to appease important constituencies, resulting in a situation of partial liberalization in the financial sector.

By late 1990s, the focus of chapter 5, Angola's economic situation had improved yet the MPLA regime again found themselves in a situation where the satisfaction of their supporters appears to have been weakening. Specifically, the chapter points to economic performance falling short of the expectations of the MPLA's core constituency as evident by the growing dissatisfaction amongst elite members with the economic uncertainty produced by partial liberalization. Initially, the government did not have the space to act on these grievances. The military threat which UNITA constituted at the time mean that the regime could not afford to think beyond short-term survival. Only after the political situation improved in 1998-1999 and the MPLA gained the upper hand in the civil war, did the political leadership have the necessary confidence to take the steps required to normalize the economy and provide a stable foundation for the financial sector. By allowing for the expansion of the financial sector, Angola's ruling coalition ensured their position not only in the short term but also into the future.

Chapter 6 accounts for the direction that the financial changes took in Angola in the post-war reconstruction era. Post-2002 was a time of unprecedented policy space for the MPLA, free from both domestic and international threats. With minimal interference, the party was

¹ Angola was the only African country to not have sought a structural adjustment programme at the time (Aguilar, 1999)

² Even if the Angolan government had faced the same conditionality as other African countries, it is questionable whether partial reform would have been avoided. Van de Walle (2001) convincingly shows how African governments got away with partial reform even after committing to reform programmes.

able to dictate the development of the financial sector in line with the wishes of its support base. This led to a financial sector that was concentrated on banking, which were attracting in part due to the ease by which they could be used as rents generators for a small constituency. Additionally, the banks helped the MPLA extend the state's reach, outwards to connect with global financial networks, as well as nationally. For these purposes, non-banking financial institutions such as the stock exchange and microfinance institutions were less useful, building as they did rather on a different philosophy of diversifying and extending financial services. This was not in the interest of the MPLA leadership and so the developments of these latter types of institutions remained dormant.

Finally, chapter 7 describes how the 2009 balance-of-payments crisis exposed the inherent limitations of Angola's post-war reconstruction economic model and the way that the regime used the financial sector to garner support during this time. Specifically, after 2009 it became clear that the policy space that the government enjoyed vis-à-vis external actors in financial sector policies, was subsiding. Firstly, the balance-of-payments crisis Angola experienced in 2009 pressed the country to request a Stand by Agreement with the IMF in the autumn of that same year, the first such programme in the country's history. Secondly, the Global Financial Crisis of 2008 meant that foreign banks were requiring greater compliance from its Angolan partners. For the financial sector to continue serving its political purpose, regulators and banks were required to play by a tighter set of rules. The fact that the Angolan regime was able to turn stricter regulatory requirements to their advantage shows that the government had some space to manoeuvre, although it was noted conclusively that this policy space again might be shrinking with the onset of the oil-price fall in 2014.

Financial sector change in Angola is explained by the regime's need to appease supporters coupled with the former's ability to balance the pressure of excluded factions as well as external actors. When political leaders were not able to satisfy their supporters, they favoured financial sector change. Their ability to do so in turn depended on authorities' ability to balance the pressures exerted on ruling elite by domestic actors including excluded factions, notably UNITA, and external actors.

In arguing this, the thesis challenges existing scholarship on resource-rich countries and the political economy of finance in important ways. The study parts with earlier scholarship that portrays resource rich authoritarian countries as generally autonomous from societal demands because of these government's access to external resources of whose use they were not held accountable (Mahdavy, 1970; Luiciani, 1987; Yates, 1996; Bhattacharyya and Hodler, 2014). The common assumption of rentier state theory is that fiscal rents sever the taxation-representation bargain, thus leaving citizens "less likely to demand accountability from — and representation in — their government" (Ross, 2001, p.332). Recent studies, such as that of Hertog (2010a) and Saylor (2014) seeks to revise this common held assumption, demonstrating how the picture is more complex and that decision-makers are not only influenced by factors at the macro level but also by demands arising from components within the state as well as low-level interactions between state and society.

The study of Angola presented here contributes to the latter group of revisionist scholarship by demonstrating how political leaders needed to keep the interests of politically important constituencies in mind when weighing policy options. The composition and interest of these key constituencies in turn influenced the financial sector policies that political leaders

pursued. Consequently, although the government enjoyed greater political leeway at certain points in time, they did not stay aloof from *all* domestic political pressures. The finding from Angola relates to what Hertog (2010a, p.267) argues to be the case in Saudi Arabia, “rent distributions means incurring obligations, even if individualized, and these can reduce a regime’s leeway over time.” As the example of chapter 6 shows, even when external interference was minimal and the confidence of the MPLA was at a height, the nature of the political elite support base (and these groups’ demands on the state) still had significant implications for the type of financial sector policies pursued in the country.

Challenging the common assumption of the resource-rich state’s all-encompassing autonomy relates to a second central contribution of this thesis, which is demonstrating why it would be in the interest of an authoritarian resource-rich regime to promote financial sector change and advancements. The thesis highlights the various functions that financial sectors fulfil in resource rich countries, including a distributive function, rent generating function as well as connection to the outside. In doing so, the thesis adds to current studies in political economy of finance who tend to only focus narrowly on outcomes. An issue with existing literature is that it assumes that in the absence of taxation-induced political bargaining, political leaders are not only incapable but also uninterested in implementing policy that promotes the advancement of the financial sector (Bhattacharyya and Hodler, 2014). This thesis finds this logic to be incorrect. Contrary to the existing scholarship, the thesis argues that having an operative financial sector was in the interest of Angola’s resource-rich authoritarian leadership. Specifically, the thesis showed how the financial sector proved advantageous for the MPLA in the party’s bid to maintain power. In the case of the early 1990s (Chapter 4), Angola’s state-controlled banking sector for instance helped ease the transition from a centrally-planned to a market-based economy, ensuring that key

constituencies were never left disadvantaged. Other studies of post-communist regimes have shown the banking sector to play a similarly important role in these contexts as a tool of continuity (Bonin et al., 1998; Kovsted et al., 2005), yet in the political economy of finance literature this mechanism has remained overlooked.

The important distributive function played by state-owned banks and specialized credit institutions has largely been discounted, although as Malik (2017, p.8) argues, bank's distributive function "often trumps the productive logic in highly centralized, extractive regimes." State involvement in Angola's financial sector, by means of state-owned banking institutions facilitated the transfer of resource rents to Angolan elite groups, often in the guise of claims by ailing state-owned enterprises (Chapter 4).³ In addition to distributing rents, the financial sector also generated new rents by means of an arranged provision of lucrative contracts and bank licences to regime insiders (Chapter 5), evolving into a "controlled form of accommodation" where credit was directed mainly at non-productive investments in consumption and real estate (Chapter 6; Malik, 2017, p.9).

In the above described manners, financial systems represented a major asset not only to the Angolan regime but as Malik (2017) and Henry and Springborg (2010) attest to, also to resource-rich regimes across the Middle East and North Africa (MENA). Even without mentioning the usefulness of the banking system in expanding the physical presence of the state (Chapter 6) or its role in ensuring the resource-rich state's connection to global financial networks (Chapter 6 and 7), it is clear that dismissing the financial sector solely on the grounds of the sector's poor track record of facilitating intermediation between savers and borrowers, one risks missing important points concerning the attractiveness of

³ See Malik (2017) who makes the same claim about Algeria.

an operative financial sector to authoritarian resource-rich regimes. An important contribution of this thesis is therefore to alert political economy of finance scholars to the latter uses of the financial sector for regime survival. The study of Angola's financial sector moreover provides a convincing case for going beyond simple aggregate indicators of financial advancement. Whilst readily accessible and useful for making comparison, quantitative indicators, commonly measured as the ratio of private sector lending to GDP or of broad money to GDP, do not capture the nuances that have come to light through the case study of Angola's financial sector. The lack of attention to nuances beyond those captured by quantitative indicators has led previous studies to dismiss financial sectors in countries in Angola as underdeveloped, rather than to explore how these nuances matter and how they have changed over time.

3. Beyond the Angolan case

The last section recapitulated the case study of Angola. It considered some of the lessons learned from the study of financial sector change in the authoritarian and resource-rich context to the broader literature on the political economy of finance. The next section will discuss the applicability of the casual mechanisms identified in the Angolan case to the wider constellation of resource-rich and authoritarian cases. It is clear that explaining financial sector change is relevant also in other resource-rich countries whose financial sector evolution, like in Angola, often has been dismissed due to the sector's comparatively poor track record of facilitating intermediation between savers and borrowers (Beck, 2010).

Moreover, as I argued to be case for Angola, it is unlikely that private sector demands — a main explanatory factor in political economy of finance literature — are central to

explaining financial sector change in other resource-rich and authoritarian countries. A literature review suggests that the weak role of the private sector is not limited to Angola, although it could be argued that the country's experience is an extreme one.⁴ Other resource-rich post-communist countries also had little resembling an autonomous business class, including Azerbaijan and Kazakhstan, where private sector traditions had more or less vanished after decades of Soviet rule (Dowling and Wignaraja, 2006). In other resource-rich authoritarian countries, the position of private capital has historically differed from the Angolan case and therefore the existence of autonomous capitalists cannot be dismissed. Oil-rich Kuwait, for instance, enjoys a strong tradition of merchant politics (Hertog, 2013). Strong pre-oil merchant traditions have also been the case in the United Arab Emirates (UAE) (Almezaini, 2013). Similarly, in Nigeria, national private business interests date back to at least to 1945, from the heyday of the country's export-oriented agriculture (Saylor, 2014). Yet even in the latter group of countries, studies suggest that the political influence of the private sector has been limited and that "co-optation rather than an even-handed relationship ... characterize state-business relations" (Hertog, 2013, p.6). Elaborating on the UAE and Kuwait cases, Hertog (2013, p.10) writes that "While business elites have a more solid social standing in the monarchies, their political status is less clear." Scholarship suggest that Nigeria's private capitalists have been even worse off, "coalitions led by nationalist political elites repeatedly ignored export-oriented actors' public goods requests and instead preyed upon export wealth" (Saylor, 2014, p.191). Rather than constituting an independent voice asserting demands on the state, Nigerian "state elites and private sector interests have converged around patron-client relationships and rentier

⁴ Angola's particular colonial legacy and the authorities' general resentment towards private sector activity in the post-independence period has left the country with particularly weak private sector traditions and a statist legacy (Boone, 2005). Angola's experience in this regard perhaps resembles most closely that of Algeria, whose local elite and indigenously businesses was similarly undermined by decades of destructive colonialism followed by centralized planning (Henry and Sprinborg, 2001).

activities, largely skirting formal institutions and competitive markets” (Lewis, 2007, p. 81).

What the country comparison highlights then is the wider tendency across resource-rich countries for imbalanced state-business relations, with local capitalists becoming intertwined with the state rather than acting as its counterweight. This is not surprising as the state remains a prime driver of economic activity in the economies in question here. Yet it runs counter to the underlying assumptions of existing political economy of finance theories, strengthening the claim of the need for a new explanation to account for financial sector outcomes in resource rich authoritarian states goes beyond Angola.

The thesis has identified a number of mechanisms which helped explain financial sector change in the Angolan case. From the identified mechanisms follows several testable hypotheses. In the remainder of this section I will briefly discuss the relevance of these mechanisms to the other cases. As the focus of this thesis is on theory building, I will leave it up to future studies to test the applicability of these mechanisms to explain the outcomes in other countries that share Angola’s characteristics.

The theoretical framework centred around two variables, which when combined help explain the drivers of financial sector change in the distinctive time periods. The two variables were the need of the political leadership to satisfy their constituency *and* the policy space in which they could carry out their policy agenda.

In the first empirical chapter, I showed how poor economic performance prompted the Angolan government to open up to financial sector change to enhance sector performance.

Because of the country's ready access to oil wealth they still enjoyed some policy space vis-à-vis external actors, however. This mean that the Angolan government was not required to fully abide to donor prescriptions. Rather, the government at the time took the new policy prescriptions coming from the IFIs into account but implemented them only to the degree that they were still able to serve political alliances established in the earlier period by means of incomplete financial sector liberalization. The process described in Angola, echoes the partial-reform experience of other African countries, implying that the causal mechanism identified in the country has wider applicability. In the MENA region and elsewhere in Africa, looming debt crises at the end of the 1980s meant that economic reform appeared unavoidable to governments (Malik, 2017; van de Walle, 2001). At the same time, countries wanted to escape having to "compromise state control over banking sector assets or credit allocation" (Boone, 2005, p.402). As described by Boone (2005, p. 407), building on the work of Hibou (1998) and van de Walle (2001), "when incumbent African rulers confronted mounting external pressure to liberalize national economies in the 1990s, they modified long-standing strategies for governing and managing the private sector but rarely abandoned them altogether. This argument holds true in the financial sector." Similarly, "Several MENA countries introduced privatization and economic liberalization on a limited scale. This was done in such a way as not to disrupt the status quo" (Malik, 2017). A hypothesis that arises from the Angolan case is that countries with greater bargaining power vis-à-vis external actors were more successful in lessening external pressure for financial sector opening and shape policies so that political could balance external pressures with the need to please internal constituencies. The ability to fend off external pressures for financial liberalization was particularly strong amongst the

resource-rich countries in Boone's sample of African countries (2005),⁵ signifying the role of the financial sectors as tools of continuity and control in these countries just like in Angola.

The second, perhaps more novel insight arises from the causal mechanism elaborated in chapter 5 of the thesis, where I argue that greater demands from politically important constituencies coupled with greater state autonomy produced financial sector change away from partial liberalization towards greater continuity and new rent-generating opportunities for regime insiders in the financial sector. Whilst the motivations for the more stable and long-term financial sector strategy might appear quite specific in the Angolan case (as I argued in chapter 5, the shift in regime outlook was inherently connected to the changing trajectory of the war), it appears that political leaders elsewhere also likened long-term survival of the ruling coalition with moving towards greater continuity in the financial sector away from the instability associated with partial liberalization. In the early 2000s Nigeria, Dafe (forthcoming) explains how the transition to multiparty democracy after decades of military rule coincided with efforts to reform the domestic banking sector, encouraging the financial sector's expansion away from merely redistributing public rents. In Azerbaijan, consolidation of the banking sector in the early 2000s coincided with President Aliyev declaring "state building and regime consolidation the overriding objective of his remaining years in power" (before transferring power to his son Ilham Aliyev) (Radnitz, 2012, p.62; Menaldo, 2017; Conrad, 2012). Beyond the Angolan case, then, efforts to ensure regime survival appear associated with financial sector advancements, meriting further investigation in this direction.

⁵ In her analysis of banking liberalization across Africa, Boone (2005) assumes external pressures for reform constant across cases. On closer inspection, however, it becomes clear that resource-rich countries included in her sample were amongst the most 'successful' in fending off external pressures.

Thirdly, to what extent do the processes highlighted in chapter 6, which seeks to account for the pattern of financial sector change in post-war in Angola, shine light on similar outcomes in other cases? One testable hypothesis stands out based on Angola's experience, which is that banking sectors advance in resource-rich authoritarian regimes because they help regimes cultivate the support of critical constituencies. The other side of the story is that non-banking financial institutions tend to not develop because they are not useful to the regime for their purpose of maintaining power. Specifically, it was argued that the fundamental rationale behind developing non-banking financial sector institutions with emphasis on the stock exchange went against the aspirations of the ruling party.

Angola financial sector pattern generally fits the pattern of bank-centric financial sectors and poorly developed non-banking financial sectors, which was pointed out as a common feature of resource-rich economies (Beck, 2010; Beck and Poelhekke, 2017). The existence of such a pattern in resource-rich countries has been substantiated by comparative studies. Creane et al. (2003, p.10) for instance, shows how in the Gulf Cooperation Council (GCC) countries, "the banking sector is well developed, profitable, and efficient" whilst non-banking financial institutions are limited, "characterized by high concentration, relatively few listings resulting in low levels of liquidity, and no separate regulatory authority." Even as the weight of stock markets in GCC financial sectors increased in the years prior to the 2008 crisis, the share of banks has dominated (Kern, 2012; Snaije, 2017). The situation in the GCC echoes that of African countries, where Moss (2003) writes that the non-banking financial market is small in size and stock markets characterized by low levels of liquidity. One of the oldest stock markets on the continent, the Nigerian Stock Exchange is dwarfed

by the banking sector, which controls almost 80 % of assets in the financial sector (IMF, 2013).

One of the arguments presented in chapter 6 to explain the dominance of banks to the detriment of non-financial institutions like the stock market in Angola, was that the latter is essentially about diversifying ownership and opening up economic opportunities for new investors, an idea that runs counter to the Angolan ruling elite's goal of retaining control of economic opportunities. Specifically, the hypothesis would be that countries with a higher degree of concentration in financial sector ownership tend to have a lower degree of non-bank financial sector development. The motivation for diversifying ownership is comparatively low in these countries. Without fully testing this explanation on the other countries mentioned here one cannot say for certain that this factor is at play elsewhere, but a reading of the literature suggests that concentration of ownership might play a role in explaining the lower degree of non-bank financial sector development, meaning that this hypothesis could hold also for other cases than Angola. Across the MENA region (although less so in the GCC countries) state ownership of banks remained very high, in some cases accounting for more than 70 % of total bank credit (Snajie, 2017). As Snajie (2017, p.137) writes about the latter region, "access to financial and economic opportunity remains a 'closed' process. The ownership of banks validates the consensus of power in place and keeps gatekeeping privileges in the hands of those close to the ruling structures in MENA. This slows down the entry of new participants into the economy unless those individuals possess substantial amounts of capital and, thus, do not need to access credit."

In the countries mentioned so far, non-bank financial sector development has habitually been slow. Beck (2010) shows how, on average, economies that rely more on natural

resources have notably less liquid stock exchanges, which means that buyers and sellers are few.⁶ In the MENA region, “the nonbank financial sector—comprising the stock market, corporate bond market, insurance companies, pension funds, and mutual funds—needs further development. Where such markets exist, trading is usually quite limited (Creane et al., 2003, p.6). Where non-bank financial sector development has taken place, it appears as if stock market development has been largely unsuccessful in opening up the capital market to more investors. This is evident from looking at the case of Nigeria, where the Economist magazine (2016) noted that the markets remain highly concentrated with a third of the market being controlled by one conglomerate, the Dangote Group. A hypothesis that derives from this country experiences is that a higher degree of concentration in financial sector ownership and lower degree of non-bank financial sector development could be correlated. Future research would have to test the causal mechanism identified in the Angolan case.

The exception to the pattern described above of weak non-banking financial markets is Angola’s sovereign wealth fund (SWF), FSDEA. As opposed to other non-bank financial instruments, FSDEA serves to maintain and even strengthen regime control by permitting the Angola to realize higher returns from investments, placing funds in financial markets and channel windfall earnings overseas (Pitcher, 2017; Clark et al., 2013). The existence of FSDEA suggest that the division between expansion of banking contra the non-development of non-banking institutions is not as clear cut as often assumed in the literature. The popularity of SWFs amongst resource-rich countries in general talks to the exceptional status of this specific type of non-banking financial institutions also beyond

⁶ As noted by Creane et al. (2003, p.5), “Liquidity or the ease of transacting, as opposed to the size of stock markets, is important because it facilitates the exchange of information and assets, thus improving resource allocation and growth.”

Angola warranting special attention. 23 resource-rich and authoritarian countries⁷ have established SWFs, and the 3rd, 4th and 5th largest funds are owned by the oil-rich Gulf states (Sovereign Wealth Fund Institute, 2018). In other countries like in Angola, states recognised the usefulness of SWFs not only to maintain wealth and ensure the status quo within the rentier states but equally, to “potentially provide higher returns that further increases the rentier state's capacity to maintain domestic sovereignty for even a longer period of time” (Clark et al., 2013).

Fourth and finally, chapter 7 of this thesis argued that financial sector advancement in the form of a regulatory upgrade post-2009 was in part driven by the Angolan government's desire to better control the sector, with the ultimate aim of preserving regime control. Financial sector fragilities were becoming increasingly obvious after the global financial crisis. The banking sector, whose redistribution of resources had increased as the benefactors of the regime grew, was exposed. Stricter regulation also facilitated the generation of new opportunities in the politically controlled economy, such as routing a greater share of the oil industry business through the economy as well as attracting greater foreign investment into the sector. Efforts to tighten financial regulation in a bid to enhance control over the sector does not appear limited to Angola. Neither the pursuit of regulatory reform in a bid to expand financial sector opportunities in the face of increasingly international financial markets. A process of regulatory upgrade driven by similar motivations as those emphasised in the Angolan case seems to have taken place in China. Knaack (2017) shows how policymakers' over-compliance with new global prudential banking standards in part was linked to the authorities' bid to reassert control over the banking system after a period of expansive policy lending following the global financial

⁷ Please refer to Appendix 2.

crisis. Equally, seeking greater compliance with international standards was also part of Chinese efforts to improve the reputation of the country's financial sector globally, in turn facilitating the sectors expansion. Developments in Azerbaijan and Nigeria both suggest that Angola's experience can be relevant for explaining the combination of reform and regime preservation in other resource-rich countries.⁸ Regulatory upgrades in the financial sector in Azerbaijan and Nigeria appear to have been driven in part by government's interest in better controlling their financial sectors whilst also generating new openings for the sector, which previously had been unavailable to them. In Nigeria, regulatory upgrade and consolidation of the banking sector in and around 2004 sought to address what were considered vulnerabilities in the sector and undesirable conduct of banks by regulators. Equally, banking sector reform was seen as "imperative for the entry and expansion of Nigerian banks in other markets" (Dafe, forthcoming). Like Nigeria, Azerbaijan went through a period of banking sector consolidation in the early 2000s, allowing the concentration of financial sector control in the country's most powerful politically connected banks.⁹ More recent efforts to bring Azerbaijan's financial sector regulatory framework in line with international best practices furthermore resonates closely with the experience of Angola, as Azeri banks similarly rely on correspondent relationships with banks domiciled in the United States. Adding to the impetus for reform, Azeri banks like Angolan, have in later years become increasingly interested in attracting investors from abroad (United States Commercial Service, 2016).

⁸ The combination of change and political continuity has been aptly described by Pitcher (2002, p.6) as a process of "transformative preservation".

⁹ Azerbaijan's largest banks hold 85 % of total banking assets. The International Bank of Azerbaijan (IBA) remains the leading bank in Azerbaijan, and the government continues to be its largest shareholder (United States Commercial Service, 2016).

This section has shed light on selected comparative aspects of Angola's experience. A cursory look at the data strongly suggests that Angola's experience has resonance beyond the country to the wider set of countries, some of which have been referenced here. As the proceeding chapters have shown and as has been underlined in this section, the hypotheses explored in the Angolan case are plausible and thus worth exploring by others in other country contexts. In the next and final section of this concluding chapter will highlight some of the shortcomings of this thesis and also point to possible openings for future research.

4. Limitations and avenues for further research

The chapter has so far demonstrated how the theoretical and empirical insights identified through studying the Angolan case can be applied to the explain similar phenomena in a larger group of countries typified here as resource-rich and authoritarian. This is also what the thesis set out to do; to inductively identify new variables, hypotheses and causal mechanisms that could subsequently be applied to other single case studies or comparative studies.

A first question is whether the findings from Angola's case might not be relevant to a broader set of cases and thus whether the criteria of countries' being resource-rich and authoritarian is necessary. The example drawn from China earlier indicates that the latter might be the case. The broader criteria that define resource-rich and authoritarian countries, as outlined in chapter 2 of the thesis, might also hold true for other cases that do not necessarily fit neatly into either the resource-rich or authoritarian category. China is a case in point where the state is dominant in the economy, but for other reasons than its resource-

wealth. Similarly, some of the findings identified here might also be relevant to cases who have largely survived on external rent but in other forms, such as international aid. Tanzania is a case in point where aid has helped maintain a dominant state in the economy with the ruling coalition having weak incentives to promote the productive sector (Khan, 2010; Boone, 2005). Furthermore, if, as some scholars suggest, a similar effect as resource-rents and aid might be found in the case of international remittances (Ahmed, 2012), findings from the Angolan case might have even wider applicability. Acknowledging this to be the case – that what typifies resource-rich and authoritarian countries might characterise other countries as well – I still believe it to be the right choice to limit this study to the already large group of resource-rich and authoritarian. Specifically, this is because the overreliance on external rents over domestic fiscal resources is something that sets these countries apart from say, China. Resource rents also differ from other forms of unearned income including aid and remittances. Resource rents are unrestricted finance for governments, allocated on a near-random basis. By contrast, aid allocation is purposive both between countries and within countries (Collier, 2006). International remittances are often distributed widely to non-state sources, making them very different to large resource windfalls which are typically collected by the central state. In sum, resource-rich countries are distinctive, yet studying this group of countries may still offer plausible hypotheses that might shine light on similar outcomes elsewhere.

Future research should also seek to test and strengthen the claims made in this thesis when and if further information on the subjects investigated here becomes available. In the course of thesis research, I have encountered numerous hurdles in acquiring the necessary data on which to build my arguments. Reliable data on the financial sector covering certain periods, especially between 1992 and up until the 2000s, is extremely difficult to find and in many

instances, simply not obtainable. Certain data is only possible to acquire through dedicated field research. For instance, what amounts were involved in the recapitalization of the state-owned banks after the end of the civil war? Current available information provides only estimates based on a mixture of guesswork and calculation. It is my hope that future field research will be able to fill the knowledge gaps on Angola's financial sector evolution that I have found during the course of my thesis research. The general opening up of the country and greater access to information witnessed in recent years is encouraging in this regard.

There are topics which have not been given sufficient attention in this thesis due to time and space constraints. Importantly, the thesis has concerned itself primarily with the domestic deployment of resource rents through the financial sector, which I argued helped ensure the support of key constituencies. Whilst clearly a major concern, rent distribution to domestic constituencies is only one component of the distributive regime. As Malik (2017) states in the case of the MENA region, the distribution of resource rents domestically is complemented by a significant outflow of rents to appease strategically important external constituencies. "While overseas investments are a natural response to the limited absorptive capacity of the domestic economy, the export of capital is also partly geared towards aligning the interest of the external constituencies with domestic political continuity" (Malik, 2017). Angola's sovereign wealth fund is a clear example of how Angola has deployed financial instruments in order to achieve the "internationalization of rent management and the redeployment of state resources in the international sphere for regime and personal advancement" (Soares de Oliveira, 2015, p.183-184). The pattern of Angola's foreign involvement moreover fits the general notion that such investments are not purely driven by economic returns but, equally, by geopolitical logic that treats these investments as instruments for buying leverage in important foreign capitals. This is

perhaps most clearly the case with Angola's financial interests in Portugal (see Louçã et al, 2014). Angolan investors have come to play an unusually large role in the economy of its former colonizer for economic reasons but also to profit from the latter's international credibility (Soares de Oliveira, 2015; Louçã et al., 2014). The thesis has mainly dealt with Portuguese interest in Angola but the role of Angolan foreign investments abroad, including in Portugal, is a fascinating development of the last decade which deserves further scrutiny. As Malik (2017) points out, the deployment of resource rents "to appease strategically important external constituencies" is an important dimension of rent recycling to which the literature studying resource-rich countries have devoted insufficient attention. Like is the case with deployment of rents domestically, the investment of rents abroad is not simply about economic returns but also follows a logic of distributing resources to politically important *external* constituencies who in turn develops an interest in regime survival. As net exporters of capital, resource-rich countries like Angola are increasingly using their resource wealth to "project their financial and diplomatic power abroad" (Malik, 2017); the country's SWF, FSDEA, being a perfect example. As Angola's financial sector continues to grow and becomes increasingly international, studying the external as well as the internal political economy effects of the sector's advancement is therefore pertinent if we are to comprehend fully how a resource-rich authoritarian regime like Angola's uses the financial sector to win the support of critical constituencies and thus further cement the regime's position of power.

Appendix 1:

List of resource-rich countries

	Type of resource	Natural resource exports (% of merchandise exports 2010-2016 average)	Natural resource fiscal revenue (% of total revenue, 2006-2010 average)	Freedom House (2017)
DR Congo	Minerals, Oil	94*	30	Not free
Niger	Minerals	47		Partly free
Guinea	Minerals	74	23	Partly free
Mali	Minerals	75*	13	Partly free
Chad	Oil	89*	67	Not free
Mauritania	Minerals	46	22	Not free
Lao PDR	Minerals	57*	19	Not free
Zambia	Minerals	78	4	Partly free
Mongolia	Minerals, Oil	73	29	Free
Vietnam	Oil	9	22	Not free
Yemen	Oil	83	68	Not free
Cameroon	Oil	43	27	Not free
Sudan	Oil	97	55	Not free
Papua New Guinea	Minerals	55	21	Partly free
Uzbekistan	Minerals			Not free
Bolivia	Gas	74	32	Partly free
Congo, Rep of	Oil	72	82	Not free
Iraq	Oil	99	84	Not free
Botswana	Minerals	66*	63	Free
Suriname	Minerals	11	29	Free
Indonesia	Oil	30	23	Partly free
East Timor	Oil	99*		Partly free
Syria	Oil	49	25	Not free
Guyana	Minerals	20	27	Partly free
Turkmenistan	Oil	91	54	Not free
Angola	Oil	96	78	Not free
Gabon	Oil	83*	60	Not free

Equatorial Guinea	Oil	99*	91	Not free
Ecuador	Oil	53	24	Partly free
Algeria	Oil	96	73	Not free
Iran	Oil	71	66	Iran
Peru	Minerals	50	19	Free
Azerbaijan	Oil	93	64	Not free
Kazakhstan	Oil	73	40	Not free
Mexico	Oil	12	36	Partly free
Russia	Oil	68	29	Not free
Venezuela	Oil	89	58	Not free
Libya	Oil	98	89	Not free
Chile	Minerals	59	23	Free
Bahrain	Oil	63	82	Not free
Trinidad and Tobago	Oil	66	49	Free
Brunei Darussalam	Gas	64	90	Not free
Saudi Arabia	Oil	86	79	Not free
Oman	Oil	77	83	Not free
United Arab Emirates	Oil	49	76	Not free
Norway	Oil	65	29	Free
Qatar	Gas	74	58	Not free
Kuwait	Oil	78		Partly free
Nigeria	Oil	88	76	Partly free

*: Data for 2010-2016 not available

Sources: World Bank (2017a) indicators “*Ores and metals exports (% of merchandise exports)*”, “*Fuel imports (% of merchandise imports)*”; IMF (2012)

Countries where data on natural resource exports and revenues is not available but is likely to belong to the above group of resource-rich countries: South Sudan (not free), Uzbekistan (not free), Liberia (partly free), Côte d'Ivoire (partly free).

Appendix 2: List of interviews by date

1. 16.03.2015, representative civil society organisation, Luanda.
2. 17.03.2015, reporter Angolan private newspaper, Luanda.
3. 18.03.2015, professor private university, Luanda.
4. 19.03.2015, lecturer private university, Luanda.
5. 19.03.2015, diplomat foreign embassy, Luanda.
6. 20.03.2015, IFI representative, Luanda.
7. 23.03.2015, representative foreign NGO, Luanda.
8. 23.03.2015, representative civil society organisation, Luanda.
9. 22.06.2015, former correspondent, London.
10. 20.09.2015, banker previously Angolan public bank, Luanda.
11. 30.09.2015, senior civil servant Ministry of Finance, Luanda.
12. 30.09.2015, banker foreign bank, Luanda.
13. 1.10.2015, administrative director private bank, Luanda.
14. 1.10.2015, reporter Angolan private newspaper, Luanda.
15. 2.10.2015, senior representative civil society organisation, Luanda.
16. 7.10.2015, senior civil servant Ministry of Finance, Luanda.
17. 8.10.2015, representative IFI, Luanda.
18. 9.10.2015, representative development bank, Luanda.
19. 9.10.2015, representative international oil company, Luanda.
20. 15.10.2015, banker foreign bank, Luanda.
21. 19.10.2015, banker foreign bank, Luanda.
22. 20.10.2015, senior civil servant Ministry of Foreign Affairs, Luanda.
23. 22.10.2015, professor public university, Luanda.
24. 22.10.2015, civil servant Ministry of Petroleum, Luanda.
25. 23.10.2015, senior civil servant BNA, Luanda.
26. 23.10.2015, state secretary, Luanda.
27. 26.10.2015, senior civil servant Ministry of Finance, Luanda.
28. 27.10.2015, senior manager international accounting firm, Luanda.
29. 28.10.2015, administrative director Angolan private bank, Luanda.
30. 30.10.2015, senior representative civil society organisation, Luanda.
31. 3.11.2015, senior representative oil service company, Luanda.
32. 4.11.2015, senior civil servant BNA, Luanda.
33. 5.11.2015, senior representative oil service company, Luanda.
34. 6.11.2015, senior representative civil society organisation, Luanda.
35. 6.11.2015, director Angolan private bank, Luanda.
36. 9.11.2015, director Angolan private bank, Luanda.
37. 10.11.2015, diplomat foreign embassy, Luanda.
38. 10.11.2015, director foreign oil company, Luanda.
39. 12.11.2015, representative Angolan Banking Association, Luanda.
40. 13.11.2015, oil industry consultant, Luanda.
41. 13.11.2015, human rights activist, Luanda.

42. 17.11.2015, oil industry expert, Luanda.
43. 17.11.2015, director retail market Angolan private bank, Luanda.
44. 18.11.2015, representative Capital Market Commission, Luanda.
45. 20.11.2015, representative Angolan private bank, Luanda.
46. 22.11.2015, representative Angolan private equity firm, Luanda.
47. 23.11.2015, director Angolan private bank, Luanda.
48. 23.11.2015, managing director foreign oil service company, Luanda.
49. 25.11.2015, local agent for foreign companies investing in Angola, Luanda.
50. 26.11.2015, administrative director Angolan private bank, Luanda.
51. 27.11.2015, opposition politician, Luanda.
52. 27.11.2015, director foreign oil company, Luanda.
53. 1.12.2015, banker foreign bank, Luanda.
54. 2.12.2015, reporter Angolan private newspaper, Luanda.
55. 2.06.2016, former IFI representative seconded to BNA, via Skype.
56. 20.09.2016, director foreign oil company, Luanda.
57. 21.09.2016, administrative director Angolan private bank, Luanda.
58. 21.09.2016, oil industry expert, Luanda.
59. 22.09.2016, director Angolan private bank, Luanda.
60. 27.09.2016, banker foreign bank, Luanda.
61. 28.09.2016, senior civil servant BNA, Luanda.
62. 28.09.2016, former BNA governor, Luanda.
63. 30.09.2016, senior civil servant Ministry of Finance, Luanda.
64. 4.10.2016, representative IFI, Luanda.
65. 5.10.2016, representative oversight body BNA, Luanda.
66. 7.10.2016, politician opposition, Luanda.
67. 10.10.2016, banker former Angola public bank, Luanda.
68. 11.10.2016, ambassador foreign embassy, Luanda.
69. 11.10.2016, partner international accounting firm, Luanda.
70. 12.10.2016, representative of oil service company, Luanda.
71. 13.10.2016, director Angolan private bank, Luanda.
72. 14.10.2016, previous member of government's reform team (1980s), Luanda.
73. 14.10.2016, director foreign bank, Luanda.
74. 29.11.2016, IFI representative (missions to Angola late 1980s early 1990s), Washington DC.
75. 5.12.2016, representative IFI Africa focus, Washington DC.
76. 8.12.2016, representative IFI Financial Markets focus, Washington DC.
77. 9.12.2016, representative IFI Africa focus, Washington DC.
78. 1.03.2017, banker former Angolan public bank, London.

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