national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

RESPONSES FROM SOUTH AFRICAN AIRWAYS SOC LTD (SAA) TO QUESTIONS FROM PARLIAMENT'S STANDING COMMITTEE ON APPROPRIATIONS (SCOA)

Presentation to SCOA and request by SCOA for additional information

SAA appeared before SCOA on 21 November 2017 to update the committee on how SAA has allocated the R10 billion capital injection as well as update the committee on the Long Term Turnaround Strategy (LTTS) implementation.

Response to SAA Presentation to SCOA and request by SCOA for additional information

R10 billion debt relief and recapitalisation funding sufficiency

1. SAA stated that even with the R10 billion debt relief and recapitalisation, SAA indicated that the balance sheet of the airline remains weak with negative equity of approximately R9.2 billion. SAA further stated that the airline therefore required an additional R9.8 billion to settle its outstanding debts to get to a zero base (equity value of R0).

2. Furthermore, SAA indicated that the zero equity base would just be a starting point and does not restore the company's capital structure. Moreover, SAA has stated that the business has to be restructured in order to return to profitability and generate free cash flow. The current LTTS projects that SAA will only generate free cash flow in 2021/22. Therefore, SAA has indicated that it will require working capital support until it completes its business transformation programme. Consequently, the R10 billion recapitalisation already provided by Government is insufficient for SAA's needs in the short-to-medium term.

Call Centre in Miami

3. SAA has stated that the Fort Lauderdale (Miami) call centre is part of the North American Regional Office and is responsible for all inquiries, reservations and direct sales for the USA, Canada and the Caribbean. The call centre was relocated from New York City to Fort Lauderdale in 2012 and a 10 year lease was entered into. SAA indicated that at the time, it was projected that the move would result in an increase of approximately USD1.3 million per annum in sales or USD13 million over the term of the 10 year lease.

4. SAA also indicated that the total lease payments over the 10 years are estimated at USD4.874 million with USD1.961 million paid from September 2012 to date. SAA also stated that the call centre has a staff complement of 18 and the year-to-date costs of operating the call centre is USD1.033 million.

5. Furthermore, SAA indicated that the continued operation of the call centre is under review with the aim of establishing the most optimal way of maintaining SAA's presence and protecting its revenue in the North American region. SAA state that this review would be concluded by the end of March 2018.

Root causes of operational challenges

6. SAA stated that the airline has had numerous strategies with limited implementation and that together with the highly competitive environment has led to SAA's operational failures.

7. SAA further indicated that a recent assessment of the LTTS by independent aviation experts noted that some of the reasons for failure to implement included unstable C-suite leadership[1]; inability to retain talent and specialised skills; quality of management; lack of analytics in the decision making; and that no hard decisions were made.

Root causes of operational challenges/failures since 2012 and Profitability of current routes

8. SAA has stated that the route profitability of the airline remains a major concern. At C4 level (profit level excluding overheads), only 50% of the route network makes a positive contribution. With full allocation of costs including overheads, only 20% of the network makes a positive contribution.

9. SAA has indicated that this is an area of focus for the executive team and the CEO has already proposed and implemented initiatives on how best to structure the airline in order to remediate the network challenges.

Citibank loan

10. SAA indicated that the loan from Citibank amounted to R1.785 billion and that R1.019 billion of that amount has been repaid. Furthermore, SAA stated that as per the arrangement with Citibank and SAA's other lenders, the balance of R766 million has been ring-fenced and will be repaid on 22 March 2018.

Payment of suppliers

11. SAA has indicated that it has utilised R2.4 billion of the R10 billion recapitalisation for working capital purposes. SAA also stated that the executive team is also focusing on revenue stimulation and tighter working capital initiatives and that these will alleviate the liquidity constraints facing the company.

Staff complement and remuneration

12. SAA has indicated that it has a staff complement of 10 669 employees with an annual cost of R6.1 billion, inclusive of all employee benefits and training.

[1]The C-suite is considered the most important and influential group of individuals at a company. The suite is usually the top of the echelon at a lot of companies: the highest career point which cannot be reached without leadership skills.

Moreover, SAA indicated that this is in areas where the airline can still achieve efficiency gains.

13. SAA has also stated that an Employee Engagement Framework is being finalised which will ensure that all employees are engaged to deliver on the Turnaround Plan. The CEO has also had a series of engagements with employees and organised labour on the state of the airline.

14. Furthermore, SAA indicated that, as part of the broader public relations strategy, the CEO, as the face of the organisation, has undertaken interviews with both electronic and print media.

Forensic and Investigative Reports

15. SAA indicated that the Board has considered the forensic report by Open Waters on procurement practices at SAA as well as the technical and investigative reports by Edward Nathan Sonnenberg and Ernst and Young on the reasons for continued financial losses at SAA.

16. The Board also instructed that the implementation of the recommendations, especially on areas of financial losses, should form an integral part of executing the Turnaround Plan.

17. SAA also stated that Cliff Dekker Hofmeyer has been retained to assist management with the implementation of the recommendations, especially those around processes and appropriate corrective measures.

18. The Minister should note that SAA has not provided details of the conclusions of the forensic and investigative reports, nor of the implementation plan to address findings from the report.

Laundry Facilities in London

19. SAA indicated that it undertook an in-depth review of continuing to outsource laundry services at various destinations or to centralise this function in Johannesburg. The review concluded that it was more efficient for SAA to continue with laundry services in London. SAA stated that the costs savings to be achieved at the time were less than ZAR100 000 per annum, which was not considered to be worthwhile given the effort required to centralise the services in Johannesburg.

20. SAA indicated that the contract for these services expires on 31 December 2018 and that a further study will be conducted closer to the contract expiry date in order to determine whether there is a business case to centralise.

21. It should be noted that SAA has not provided any information regarding the actual costs to outsource laundry services in London.

SAA Technical (SAAT) Financial situation

22. SAA indicated that SAAT posted Year-to-Date (YTD) profits of R153 million against a budgeted net profit of R24 million for the first half of the 2017/18 financial year (1 March 2017 to 31 August 2017).

23. The Minister should note that the latest SAA Management accounts (December 2017) show that YTD Profits for the first 10 months of the 2017/18 financial year (1 March 2017 to 31 December 2017) amount to R78 million. This indicates that SAAT has incurred losses amounting to R75 million from 1 October 2017 to 31 December 2017, which has eroded the profits that was generated during the first half of the 2017/18 financial year.

Transformation and Employment Equity plans

24. SAA stated that the Employment Equity Plan for the period 1 April 2017 to 31 March 2022 has been developed and approved and reports on it will be tabled with the Department of Labour in accordance with the Employment Equity Act.

25. It should be noted that SAA has not provided any additional information with regard to this matter.

Movable and Immovable Assets

26. In response to SCOA's request for a list of movable and immovable assets, SAA stated that the net book value of movable assets is R2.6 billion and immovable assets are R2 billion. SAA also indicated that asset registers are maintained at group and subsidiary levels.

27. The Minister should note that the response from SAA does not address the information request by SCOA.

ENDS