

SPECIAL APPROPRIATION BILL FOR ESKOM

Briefing of Select Committee on Appropriations

Presenter: DG National Treasury, Dondo Mogajane | September 2019



national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

BACKGROUND

- Well-functioning and financially stable Eskom is vital to economy and society
- Eskom experiencing serious financial and operational challenges which to large extent were caused by governance challenges and malfeasance that entity previously experienced resulting in decline in investor confidence
- Strong and sustainable Eskom is essential for ensuring that energy security supply for the country is maintained so as to support economic growth and development
- Eskom is currently financially unsustainable based on its high levels of debt, which exposes Eskom to high levels of liquidity and going concern risk
- Without major changes to Eskom's business model & financial assistance from Government, the company will be unable to meet its financial obligations in 2019/20 financial year

Eskom's financial challenges

- Eskom is in debt reliant liquidity situation that has resulted from:
 - low tariffs determinations from National Energy Regulator of SA (NERSA)
 - decline in sales volumes year-to-date
 - primary energy and employee benefit costs increasing
 - continuing cost escalations of new build programme due to its persistent delays
- Financial ratios announced by Eskom in their recent annual results for 2019/20 financial year illustrates size of its financial challenge
- Eskom now has to borrow increasing amounts to service its debt obligations, placing it in unsustainable position

Eskom's financial challenges (cont)

- Eskom is also experiencing challenges in raising its required funding due to lenders' concerns about:
 - its future sustainability
 - uncertainty of Government's restructuring plan
 - lack of clarity on policy direction of energy sector
- Failure to manage short-term liquidity will result in Eskom defaulting on its debt repayments and this will result in possible call on its Government guaranteed debt
- Key to improving liquidity position is entity's ability to successfully secure all its identified funding initiatives
- However, given lower tariff determination by NERSA (tariff discounted by fiscal allocation) and slower implementation of cost-saving measures, projected Eskom revenues will not be adequate to cover its interest payment, debt repayments & capital expenditure requirement
- Hence, Government decided to provide Eskom with financial support to assist with its financial challenges

Government intervention

- Minister of Finance (Minister) announced in his budget speech proposed allocations of R23 billion a year over medium term to support Eskom during its reconfiguration
- Allocated amounts were intended to enable Eskom to service its debts and meet redemption requirements, while making resources available for urgent operational improvements
- It had been anticipated at time that shortfalls in capital structure of Eskom could be dealt with through normal appropriation process and the money was envisaged that it will be disbursed in October 2019
- This approach was partly premised on assumption that Eskom will continue to raise required funding
- Hence, NT did not submit Special Appropriation Bill for consideration by Parliament before it rises as there were no indication that Eskom will experience difficulty in raising required borrowing

Government intervention (cont)

- On 31 March 2019, Eskom experienced challenges in drawing its intended facilities and could not honor its obligations
- Failure to meet its obligations could have had negative consequences for Eskom and fiscus, hence, Minister intervened
- On 2 April 2019, Minister of Finance invoked section 16 of Public Finance Management Act (PFMA) to approve maximum allowable amount for Eskom, i.e. R17,652 billion
- The section 16 approval accelerated part of the R23 billion allocation announced in February 2019 budget

Government intervention (cont)

- To date, Government has transferred R13,5 billion to Eskom of the R17,652 billion approved under section 16 of PFMA
- Disbursement of remaining R4,1 billion of the R17,652 billion to be disbursed in line with Eskom's cash flow requirements
- Remaining part of R23 billion (announced in budget) may be disbursed from (i) contingency reserve under 2019 Appropriation Act or (ii) appropriation in the 2019 Adjustments Appropriation Act (envisaged to be law in Dec/Jan)
- NT & Department of Public Enterprises (DPE) continue to work closely with Eskom's treasury to monitor Eskom's daily cash flow requirements & its financial position

Special Appropriation Bill

- In June 2019 State of the Nation Address (SONA), President announced that Special Appropriation Bill will be tabled by Minister to propose allocation of significant portion of the R230 billion that Government proposed over the next 10 years in the early years according to Eskom's requirements
- This he said was to be done because Eskom is too vital to our economy to be allowed to fail
- On 19 June 2019, Cabinet approved additional funding allocation to Eskom for the 2019/20 and 2020/21 financial years to assist company with its financial challenges
- For this purpose, on 23 July 2019 the Minister tabled in Parliament a Special Appropriation Bill

Special Appropriation Bill (cont)

- Special Appropriation Bill proposes following additional financial support for Eskom:
 - Additional R26 billion in 2019/20 financial year
 - R33 billion in 2020/21 financial year
- NT is developing conditions to be imposed before and after transfers are made to Eskom
- This financial support also addresses going concern status which enabled external auditors to sign off Eskom's annual financial statements on going concern
- However, this financial support is based on Eskom's ability to execute its funding plan of R46 billion for 2019/20 which 58% has already been secured
- ***Failure to execute funding plan may result in Eskom experiencing liquidity shortfalls at 31 March 2020 and require additional funding in addition to funding provided through the Special Appropriation Bill***

Eskom reconfiguration

- Government recently announced the appointment of Mr Freeman Nomvalo as the Head of the Chief Restructuring Office (CRO)
- CRO is responsible for developing financial turnaround of Eskom and will be vital in development of sustainable turnaround strategy
- Government is working on a Special Paper to be released in September on Eskom to outline roadmap for reform of Eskom. This paper seeks to outline:
 - roadmap and more details on transformation of Eskom
 - clarity on measures Government will implement to resolve Eskom's financial challenges
 - consolidate outcomes of various processes that have been undertaken and provide clarity on reforms to be implemented in sector to ensure sustainable electricity future

Conclusion

- Government's ability to restructure Eskom, manage its finances, reduce its reliance on fiscal support and at same time, ensure energy security to all is crucial for economic growth and maintaining sovereign investment grade rating
- Failure to urgently strengthen Eskom's balance sheet while Government is working on long term sustainable solutions may likely have a negative systemic impact as Eskom is largest non-bank corporate debt issuer in South Africa and any default will result in crisis for Government and to some South African banks given that Eskom is largest exposure to some banks and Government

Thank You