



Synopsis of the Transnet's Annual Financial Statements 2020

16 November 2020

1. Background

Transnet provides and operates freight transportation services and infrastructure. The company's current operating model is geared towards lowering the cost of doing business in South Africa. As such, Transnet aims to improve the competitiveness of South African goods and services to stimulate economic growth and ensure the security of supply in providing ports, rail and pipeline infrastructure in a cost-effective manner. To sustain and expand its capacity, over the five-year period ending 2024/25, Transnet plans to invest R153.5 billion in capital expenditure, particularly in rail, port and pipeline infrastructure, across its operating divisions. The company is also addressing operational challenges with regards to rail and ports, with the aim of improving performance and increasing the volume of freight transported by rail. The department is investigating the implications of giving effect to the National Ports Act (2005) to ensure that this is done in a manner that is prudent and responsible. This is especially in light of volumes transported on rail by Transnet having decreased from 226.3 million tons in 2017/18 to 215.1 million tons in 2018/19, and port container volumes decreasing from 4.7 million 20-foot equivalent units in 2017/18 to 4.5 million 20-foot equivalent units in 2018/19. Revenue increased by 1.6 per cent, from R72.9 billion in 2017/18 to R74.1 billion in 2018/19, mainly due to a 9.1 per cent increase in petroleum volumes. The company generated a net profit of R6 billion in 2018/19, increasing from R4.9 billion generated in 2017/18, and has remained self-sustaining. Transnet contributes significantly to public infrastructure investment. In 2018/19, R17.9 billion was spent on capital projects, bringing the company's total investment over the last 7 years to R183.5 billion.

2. Financial Performance

Revenue increased by 1,3% to R75,1 billion, due to a weighted tariff increase of 2,9%, partially offset by a 1,3% decline in rail freight volumes and a 2,4% decline in port container throughput. Net operating expenses increased by 1,9% to R41,1 billion, which is especially pleasing when considering that the prior year cost level had shown zero growth on the year before that. EBITDA increased by 0,7% to R34,0 billion, with the EBITDA margin decreasing from 45,6% to 45,3%. Gearing of 47,6% and cash interest cover at 2,9 times are both within loan covenant requirements. Net profit decreased by 34,9% to R3,9 billion, primarily due to fair value adjustments in the prior year being R2,5 billion higher than in the current year. Cash generated from operations increased by 2,1% to R35,9 billion. Capital investment of R18,6 billion represents a 3,5% increase compared to the prior year. B-BBEE status maintained at level 2 with spend amounting to R31,31 billion or 111,82% of total measured procurement spend, as

defined by DTIC codes. 2,7% of labour costs was spent on training, focusing on artisans, engineers and engineering technicians. DIFR performance of 0,73, which is the tenth consecutive year that a ratio below 0,75 has been achieved against a global benchmark of 1,0.

3. Independent Auditor's Report

Transnet received a qualified audit opinion. The basis for the opinion is irregular expenditure. According to the auditor general, *“the public entity did not have adequate systems in place to identify and account for all irregular expenses as required by Section 55(2)(b)(i) of the PFMA. Payments made in the contravention of supply chain management requirements resulted in irregular expenditure that was not always identified and reported. As in the prior year, we were unable to determine the full extent of the understatement of irregular expenditure stated in note 39 of the consolidated and separate financial statements as it was impracticable to do so”*.

4. Shareholder Compact Performance

The performance against Shareholder's Compact is outlined in the below listed tables.

Annexure A: Financial sustainability

Key performance measure	Key performance indicator	Unit of measurement	2020 target	2020 actual
Financial sustainability	Cash interest cover (CIC)	times	≥2,5	2,9
	EBITDA margin (%)	%	≥45,3%	44,7%
	Return on invested capital (%)	%	≥5,2%	4,4%
	Debt to equity ratio (%)	%	≤50,0%	46,6%
	Net debt to EBITDA	times	≤4,0	3,5%

Annexure B: Operational excellence

Key performance area	Key performance indicator	Unit of measure	2020 target	2020 actual
Volume growth	General freight business	million tons	≥93	80,99
	Eskom coal	million tons	≥10,3	7,54
	Container port volumes	TEUs	≥4 863	4 424
	Pipeline volumes	billion litres	≥17,20	17,78
	DIFR	total ratio	≤0,75	0,73
Operational efficiency and productivity	Transnet Freight Rail			
	General freight	GTK/routekm	≥5,74	4,71
	Natcor	GTK/routekm	≥10,14	7,97
	Capecor	GTK/routekm	≥6,93	5,09
	Southcor	GTK/routekm	≥6,67	6,18
	Transnet National Ports Authority			
	Average ship turnaround time	DCT Pier 1	≤55	74
		DCT Pier 2	≤63	79
		CTCT	≤32	37
		NCT	≤30	37
	Average anchorage waiting time	DCT Pier 1	≤25	64
		DCT Pier 2	≤30	80
		CTCT	≤25	49
		NCT	≤28	53
	Transnet Port Terminal			
	Container moves per ship working hour	DCT Pier 1	≥50	41
		DCT Pier 2	≥65	46
		CTCT	≥56	38
		NCT	≥56	37
	Transnet Engineering			
	Manufacturing	Number of locomotives manufactured	≥105	38
		Number of wagons manufactured	≥450	865
		Number of coaches manufactured	≥106	0
	Transnet Pipelines			
	NMPP – actual usage: capacity at the time (ME/Week)	ratio	124:148	106:148
	Ordered vs delivered volumes (%)	%	≥95	98
Geographic expansion	Cross border revenue (TIH, TE, TFR, TPT and TNPA) excl TPL	R million	≥3 602	3 002
	Maritime connectivity	index %	≥40,11	34,58
Operational efficiency	Average tariff increase (containers)	%	≤6,0	5,5
	Average tariff increase (automotive)	%	≤6,0	5,4

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Committee Section: 021 403 8478

Report of the directors

for the year ended 31 March 2020

Key performance area	Key performance indicator	Unit of measure	2020 target	2020 actual
Maintenance	Number of kilometers screened on the rail network	km	≥105	115,3
	Number of turnouts replaced on the rail network	number	≥80	28,0
	Number of sleepers installed on the rail network	number	≥309 815	320 127
	Number of kilometers replaced on the rail network	km	≥250	46,6

Annexure C: Capital programmes and strategic initiatives

Key performance area	Capital project	Key performance indicator	Unit of measurement	2020 target	2020 actual
CAPITAL PROGRAMMES					
General freight programme	Acquisition of 1064 locomotives	Number of locomotives accepted into operations		105	46
	Wagon new-builds	Number of wagons accepted into operations		340	0
Coal programme	Waterberg – phase 2	Number of project milestones completed	number	4	2
	Overvaal solution	Number of project milestones completed		2	0
Pipeline programme	New Multi-Product Pipeline (NMPP) phase 1B *	Number of project milestones completed		6	3
Natal Corridor and Port of Durban programme	DCT berth construction, deepening and lengthening	Number of project milestones completed		4	4
STRATEGIC INITIATIVES					
Operation Phakisa	Implement floating dock at Richard's Bay	Number of project milestones completed	number	5	0
PSP programme	Tambo Springs intermodal gateway	Number of project milestones completed		2	0
Revenue initiatives	Rand value generated from fibre commercialisation		R million	≥200	132,1
	Rand value generated from diversification initiatives		R million	≥80	0
Property	Transnet Property strategy finalised and approved		date	30 September 2019	Not achieved

* One of the milestones that were included as part of the target for the 2020 financial year was achieved in March 2019, this was due to timing of the compacting process. This achievement has not been included as part of the actual performance.

Annexure D: Socio economic development outcomes

Key performance area	Key performance indicator	Unit of measure	2020 target	2020 actual
Skills development	Artisan trainees		≥200	288
	Engineering trainees	number	≥60	60
	Technician trainees		≥200	200
	Training spend	%	≥2,5	2,7
Community development	Number of patients receiving health services		≥120 000	105 565
	Number of schools participating in the whole schools development programme	number	≥110	147
	Number of teenagers receiving a package of health services		11 000	45
Environmental stewardship	Group weighted energy efficiency (electricity and fuel) year on year (YOY) improvement (%)	%	≥0,3	0,31
	Carbon emission intensity (kgCO ₂ /ton) reduction YOY improvement	%	≥0,5	0,48
Research and development	Research and development spend	R million	≥250	234,3
	Number of innovative products launched	number	≥6	2
	Number of innovative products commercialised	number	≥6	0
Industrialisation	Local content	%	70	8,6
	Supplier development (SD) value	% of TMPS subject to SD	≥10	3,00
	Rand value spent on training incubator suppliers at the hubs	R million	≥20	49,2
	Number of incubation graduates integrated into the supplier value chain	number	≥16	18
	Black women-owned		≥5	37,26
Transformation	Black-owned		≥15	55,89
	Black youth-owned		≥1	2,70
	Qualifying Small Enterprises	% of TMPS	≥5	10,84
	Exempted Micro Enterprises		≥7	12,78
	People living with disabilities		≥0,125	0,24
	BBBEE		≥70	111,82
	BBBEE status level	Certification level	6	2

5. Issues to Consider

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The following issues listed below could be considered by the Committee:

- Has Transnet sufficiently addressed the going concern assessment due to Covid 19 pandemic?
- What are the corrective actions that Transnet has taken in addressing what the auditors have deemed as *“effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R108 million (2019: R 484 million), as disclosed in note 39 of the consolidated and separate financial statements, as required by section 51(1)(b)(ii) of the PFMA? The majority of the fruitless and wasteful expenditure was caused by poor contract management and inappropriate delegation of authority”*.
- **On Consequence management, the auditors** were unable to obtain sufficient appropriate audit evidence that disciplinary steps were taken against officials who had incurred irregular expenditure as required by section 51(1)(e)(iii) of the PFMA. This was due to proper and complete records that were not maintained as evidence to support the investigations into irregular expenditure. Disciplinary steps were not taken against some of the officials who had incurred and/or permitted irregular expenditure, as required by section 51(1)(e)(iii) of the PFMA. The auditors were unable to obtain sufficient appropriate audit evidence that disciplinary steps were taken against officials who had incurred fruitless and wasteful expenditure as required by section 51(1)(e)(iii) of the PFMA. This was due to proper and complete records that were not maintained as evidence to support the investigations into fruitless and wasteful expenditure.
- **On Procurement and contract management**, Sufficient appropriate audit evidence could not be obtained for three contracts that were awarded in accordance with the legislative requirements as management indicated that for one of the contracts the information was requested from a storage service provider but documents could not be located and for the other two contracts the information could not be found. Similar non-compliance was also reported in the prior year.
- What is Transnet doing to address this finding?
- What corrective action is Transnet taking against non-performance in the Shareholder’s Compact?

6. Conclusion

The Committee notes Transnet’s performance has been significantly affected by the pandemic. The Committee commend Transnet for performing well under a distressed economic environment. The Committee urges the department to continue monitoring Transnet as there are still challenges emanating from the previous year’s report on irregular and fruitless expenditure. The efficiency and effectiveness of the port systems and rail system could be enhanced for improved performance. The Committee further observes that Transnet’s asset valuation capacity could be enhanced and improved.