

NERSA

**COMMENTS ON
ESKOM'S THIRD MYPD3 RCA FOR YEAR 2 TO 4
(2014/15 TO 2016/17) APPLICATIONS**

TO

NERSA

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by

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(Member of the public)

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Introduction

- **Request for comments welcomed**
- **Challenge taken up as there is no other alternative**
- **Why still experiencing challenges on requirements**
- **Background on Denton, Deloittes, Duvha, Brian Molefe fiasco, Chairman, Lies etc**
- **First strategic considerations**
- **Why is Eskom intent on hiding information?**
- **Nuclear against existing background?**

Strategic considerations

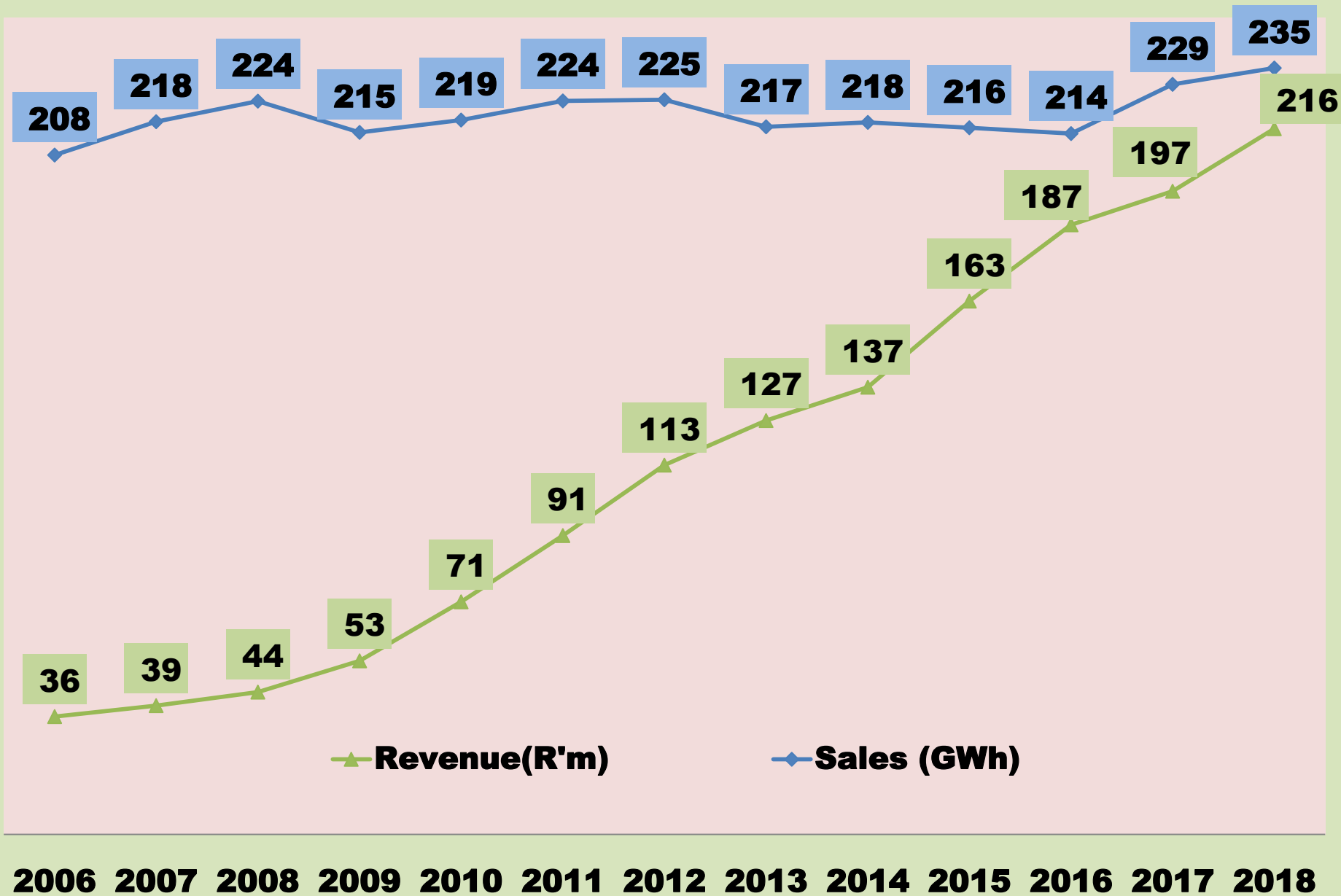
Strategic aspects: Demand?

- **Demand for electricity: No increased trend**
- **Primary energy expenses: growth 22.8% p.a over 10 years**
- **Savings in staff numbers?**
- **Releasing Government Guarantees?**
- **Optimising Capex?**
- **Substitutes? Households finding alternatives?**

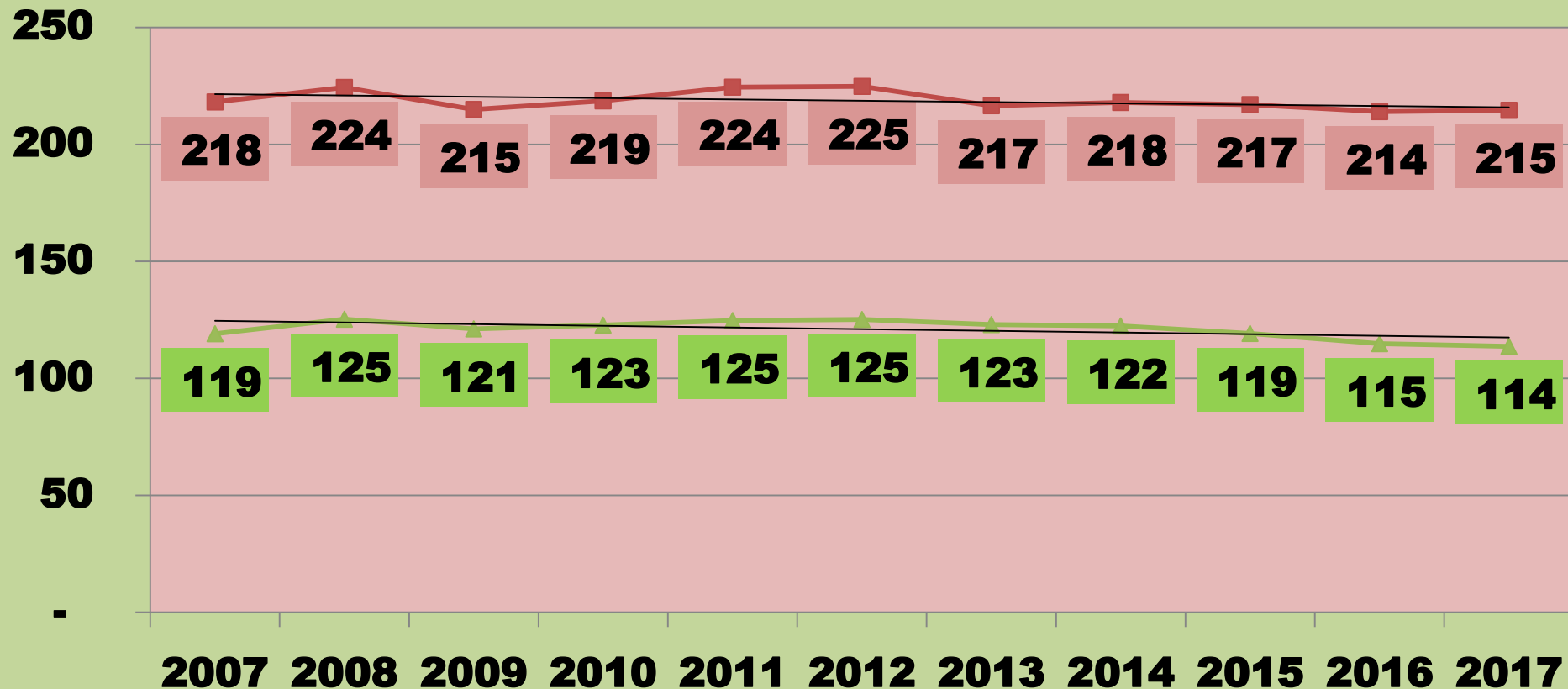
Important and strange aspects observed

- **Eskom applying for 19.9% increase based on lower sales: Due to poor management and projections: Eskom says it should be 44%. Granted 5.23%**
- **RCA increases R66.69 billion: Another 37.65%**
- **Structure of application not acceptable: Piecemeal approach followed and not properly build feasibility**
- **Should be on same basis as project finance**
- **RAB: Ensure cost recovery but not efficiency: WACC calculated on R764 billion: 29% more than Balance sheet**

Sales in GWh vs Sales in Rand plus forecast



Sales versus Total production in GWh plus coal burnt (Mt)



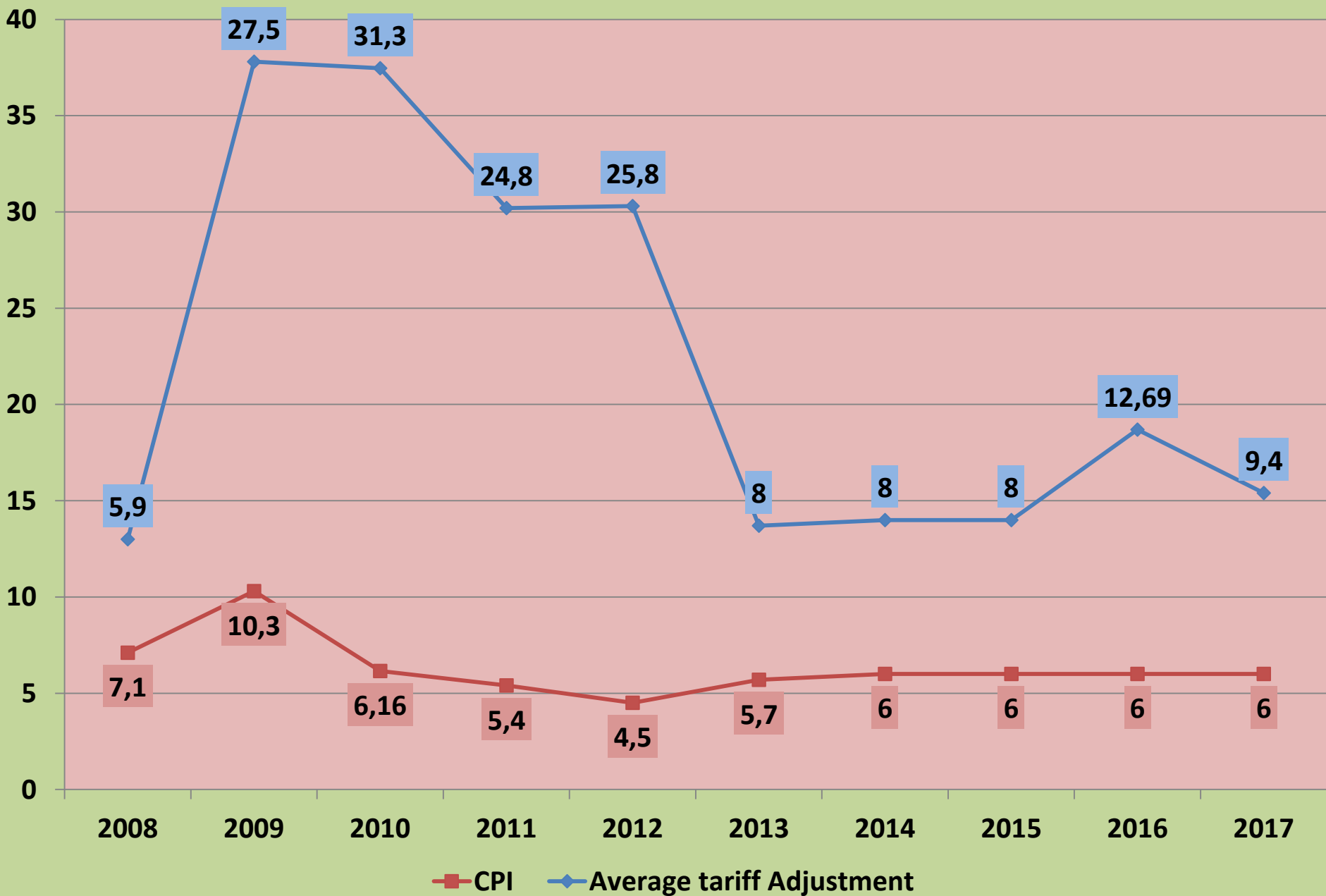
▲ Coal burnt in power stations, Mt

■ Sales (GWh)

— Linear (Coal burnt in power stations, Mt)

— Linear (Sales (GWh))

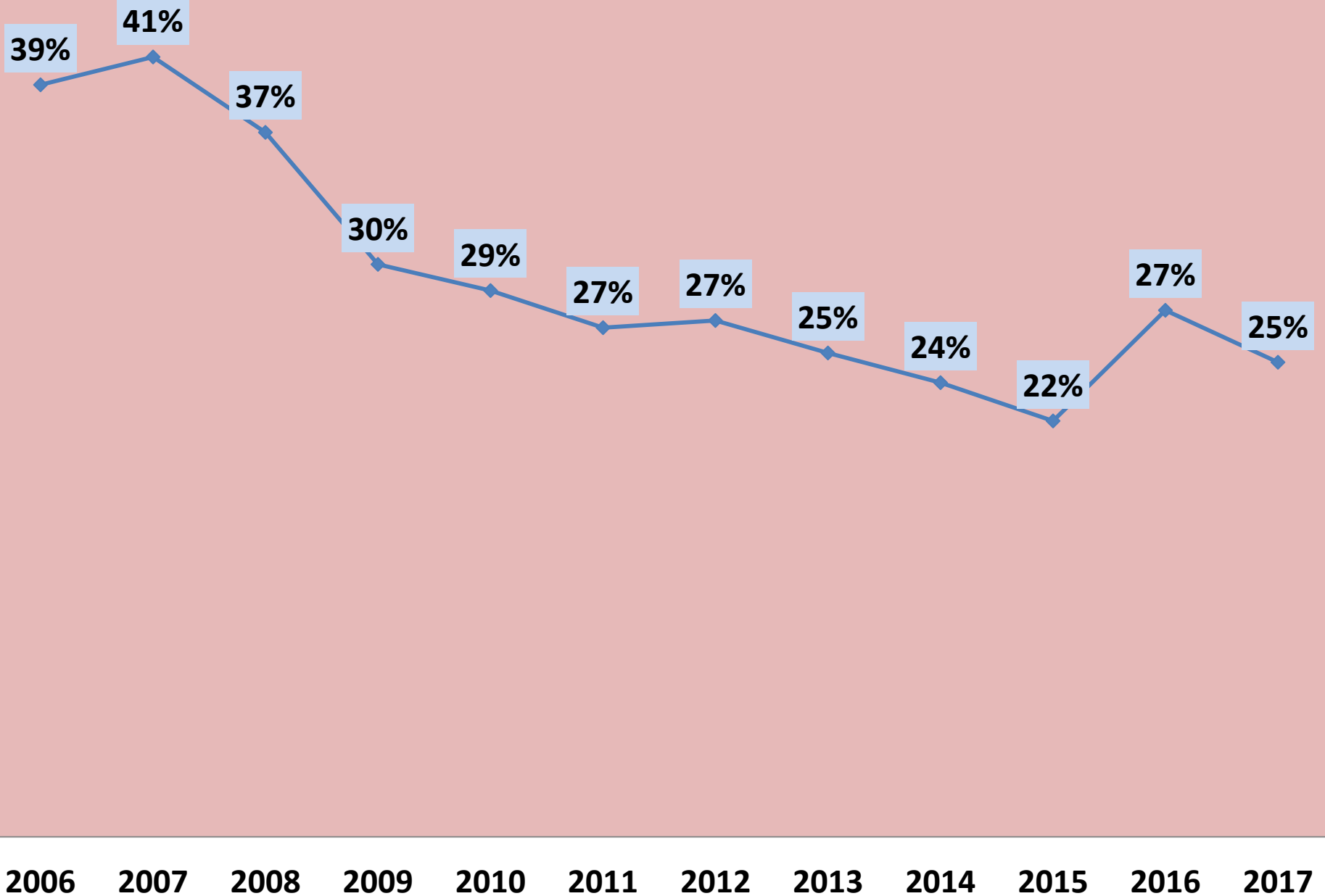
Eskom vs Cpi



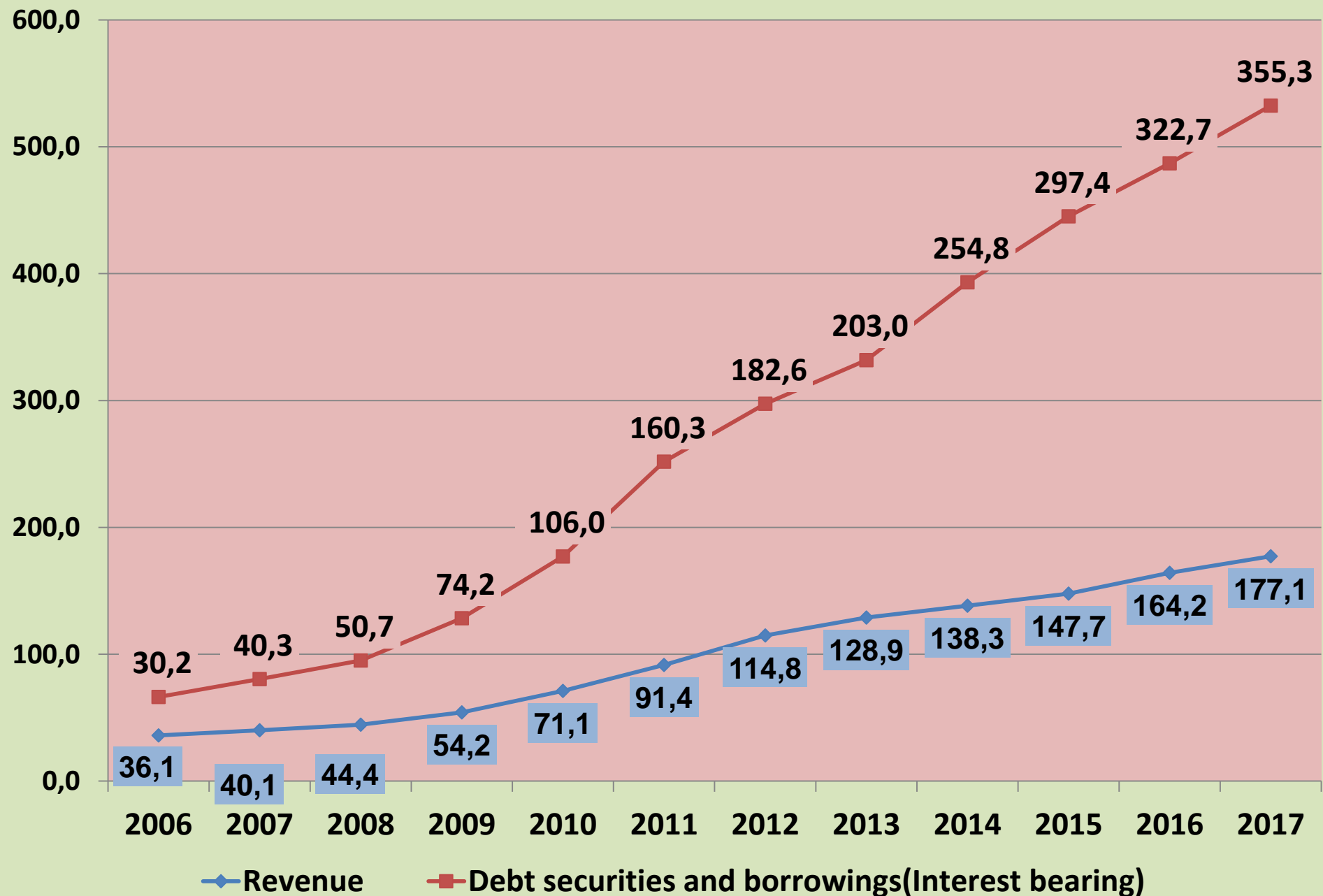
Eskom's Financial Position

- **Balance sheet under pressure**
- **Equity to debt declined from 39% in 2006 to 25% in 2017**
- **Reason: Shareholder did not ensure proper structure**
- **Eskom relies on the ability of the Income Statement:
No proper Long term Plan**
- **Current ratio 1:1**
- **Affordable Capital expenditure not prudently performed: Risk if debt exceeds 50% of Total revenue**

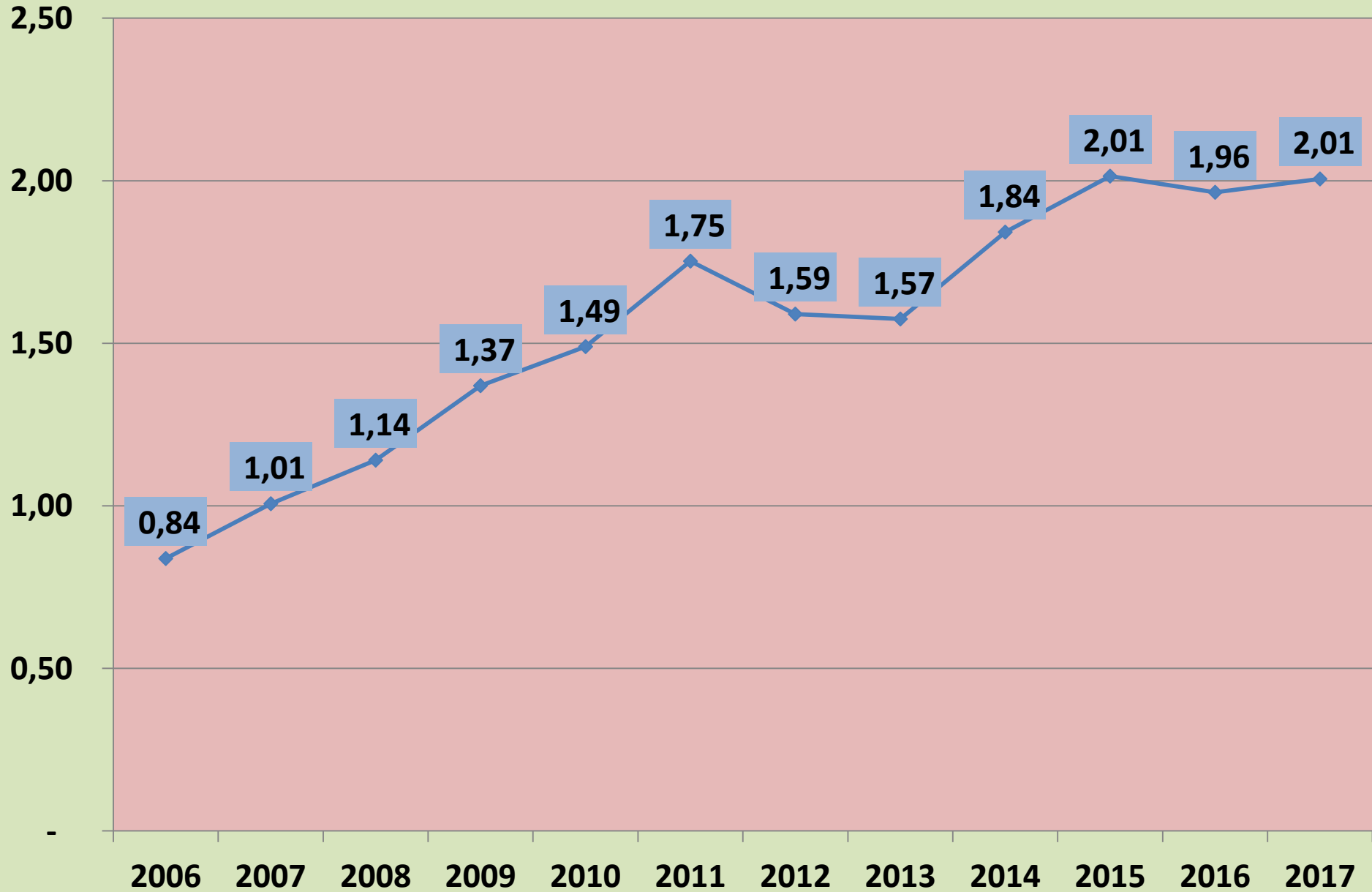
Equity versus debt %



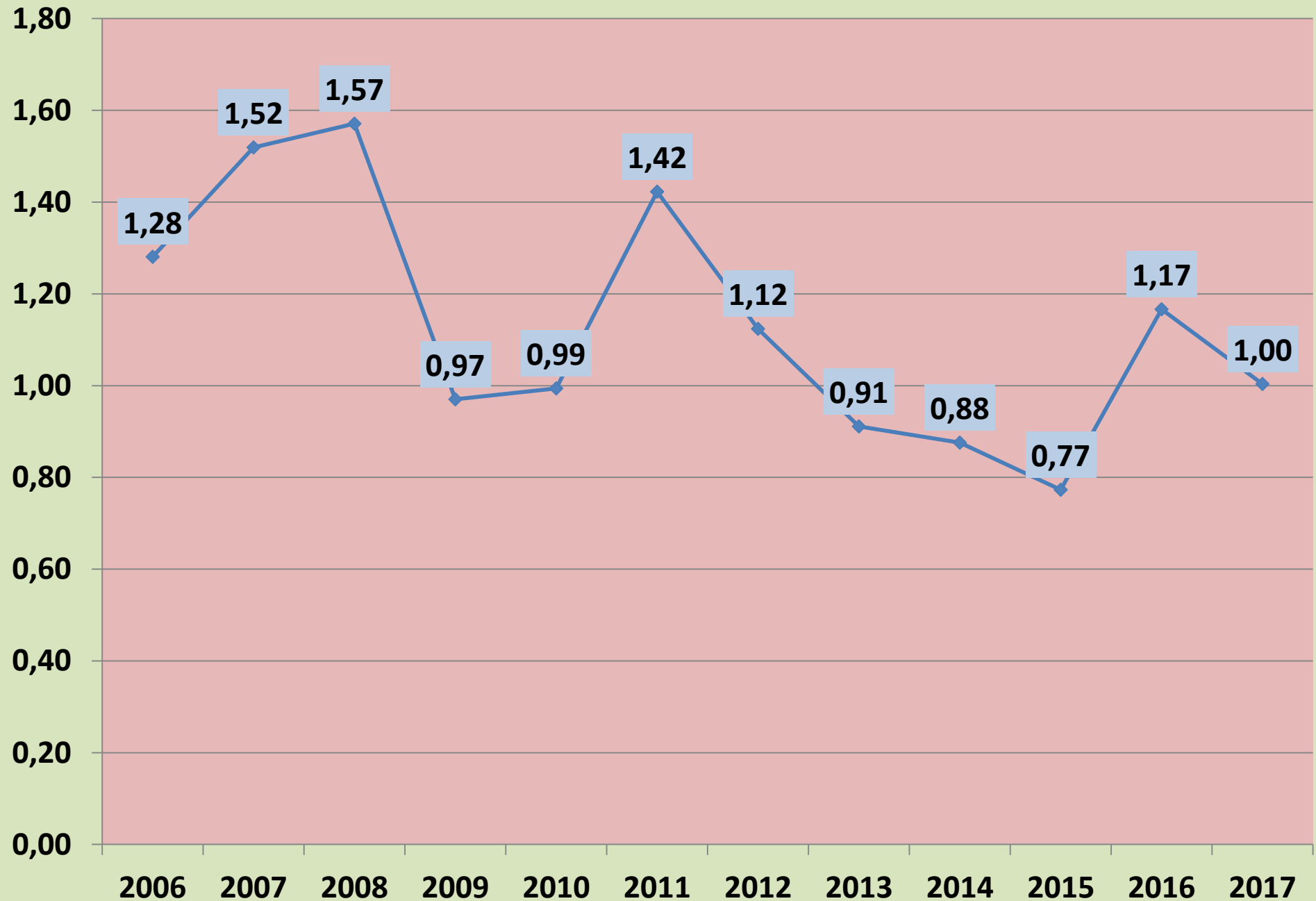
Debt bearing securities to Revenue(R'billion)



Debt securities and borrowings(Interest bearing)/Revenue(Times)



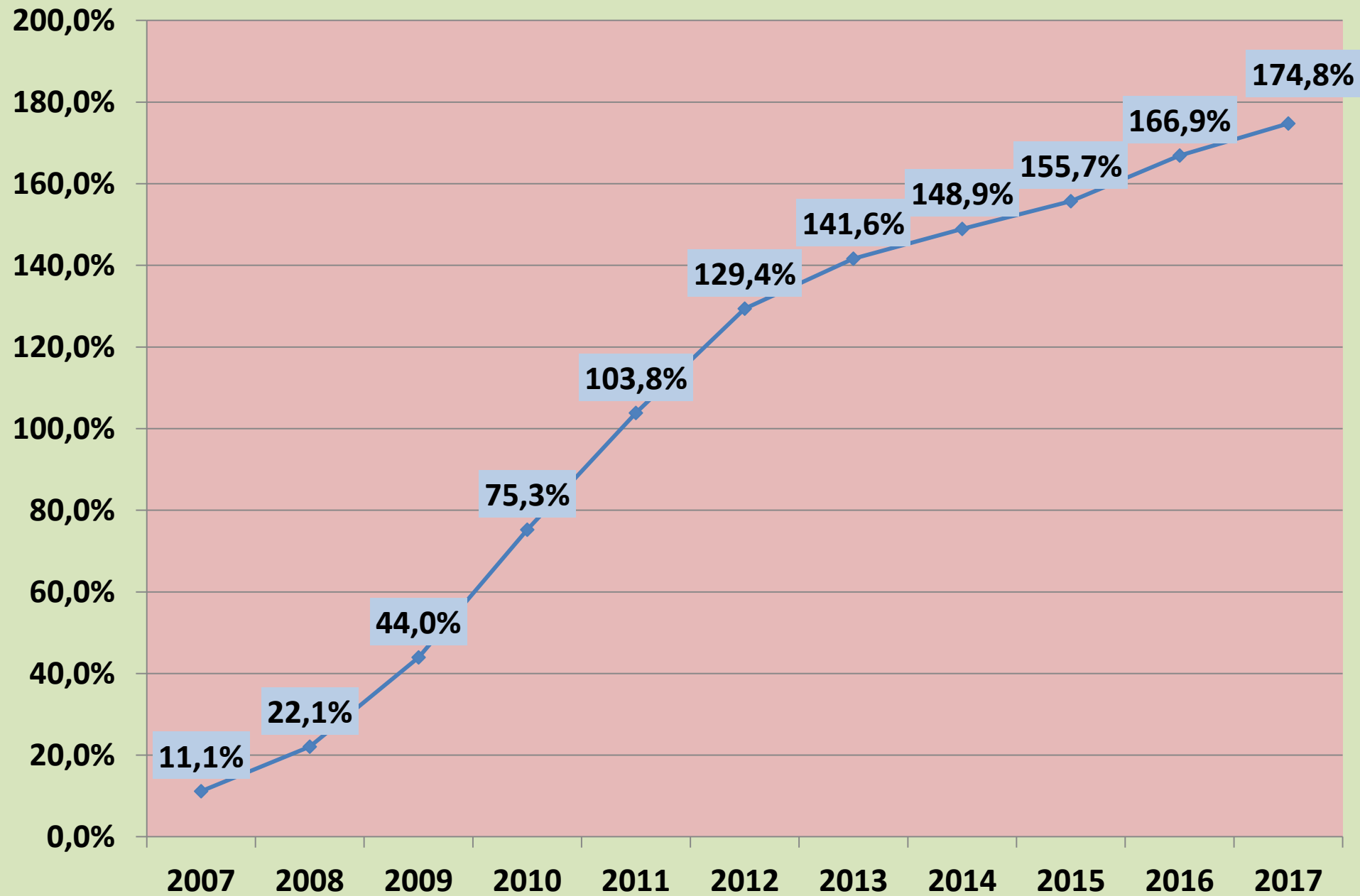
Current ratio



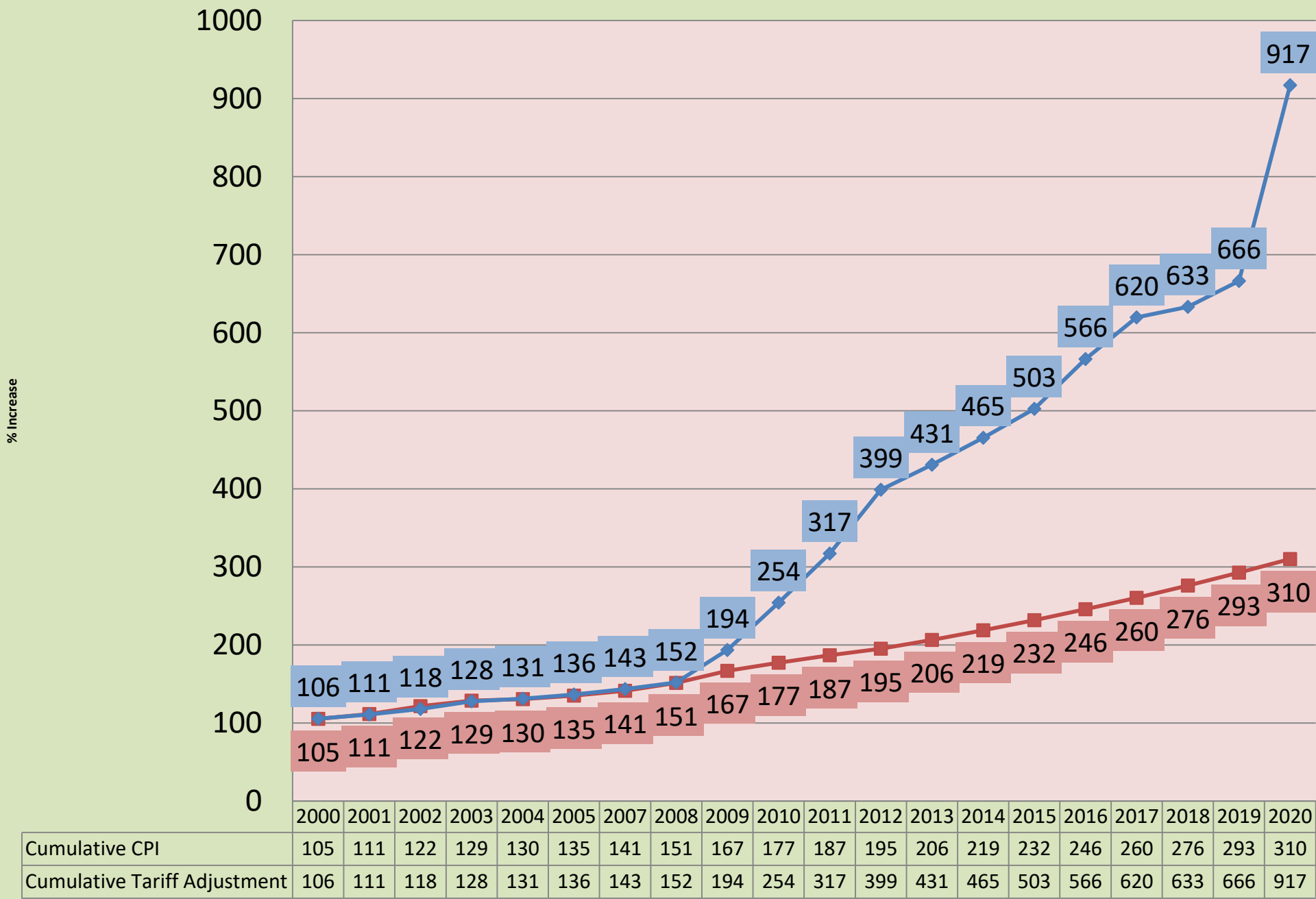
Financial performance of Eskom

- **Profit FYE 2017 R888 mil or 0.5% of Total revenue**
- **Cumulative tariff adjustments vs Cumulative Inflation: factor 2.96: Not affordable to economy**
- **Also destroying households affordability levels**
- **Lines moved apart since 2008: Serious implications**
- **Substitutes or alternatives become more likely**

Cumulative revenue growth %



Cumulative Eskom Tariff Adjustments vs Cumulative CPI (2000-2017)

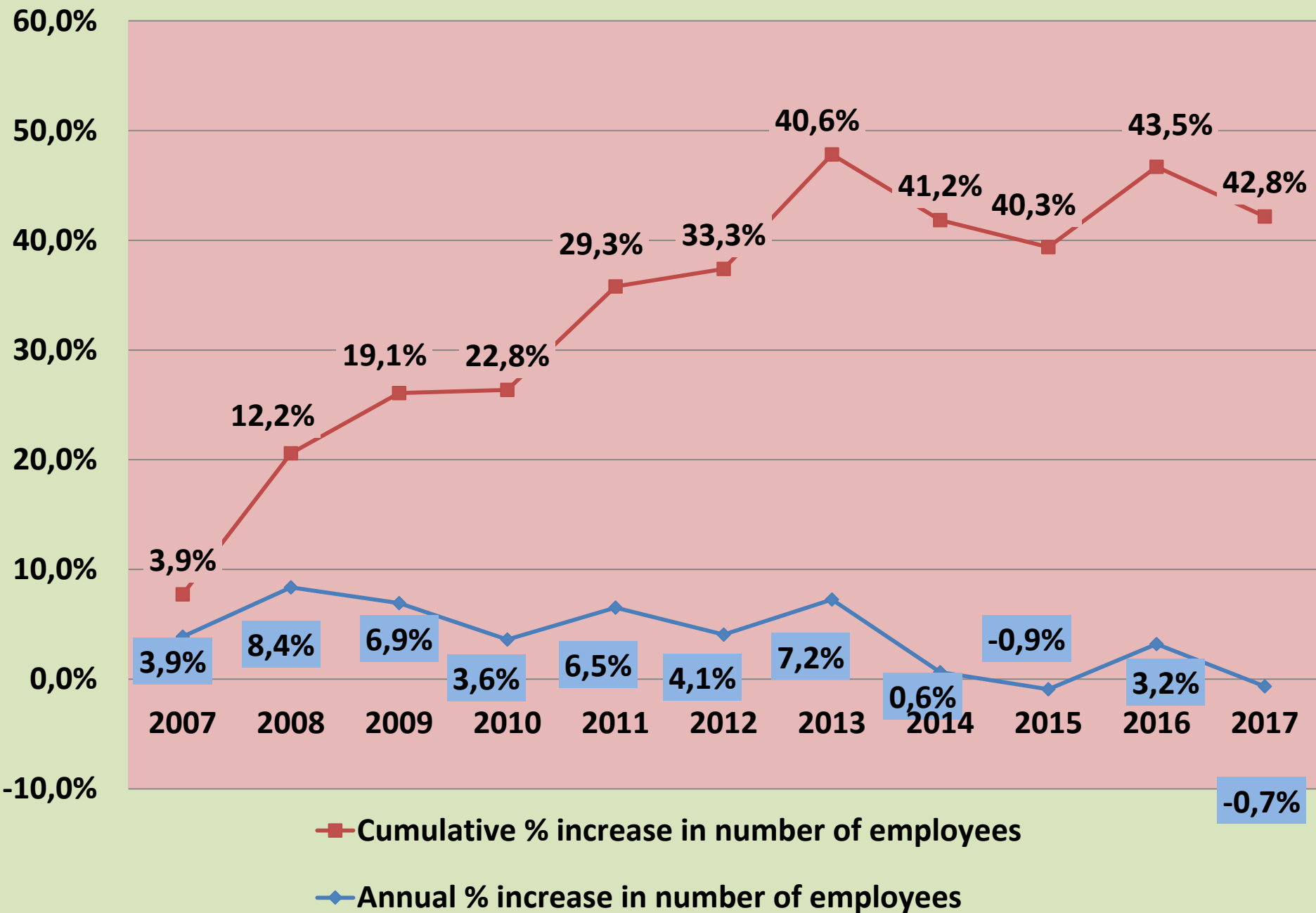


Cumulative CPI	105	111	122	129	130	135	141	151	167	177	187	195	206	219	232	246	260	276	293	310
Cumulative Tariff Adjustment	106	111	118	128	131	136	143	152	194	254	317	399	431	465	503	566	620	633	666	917

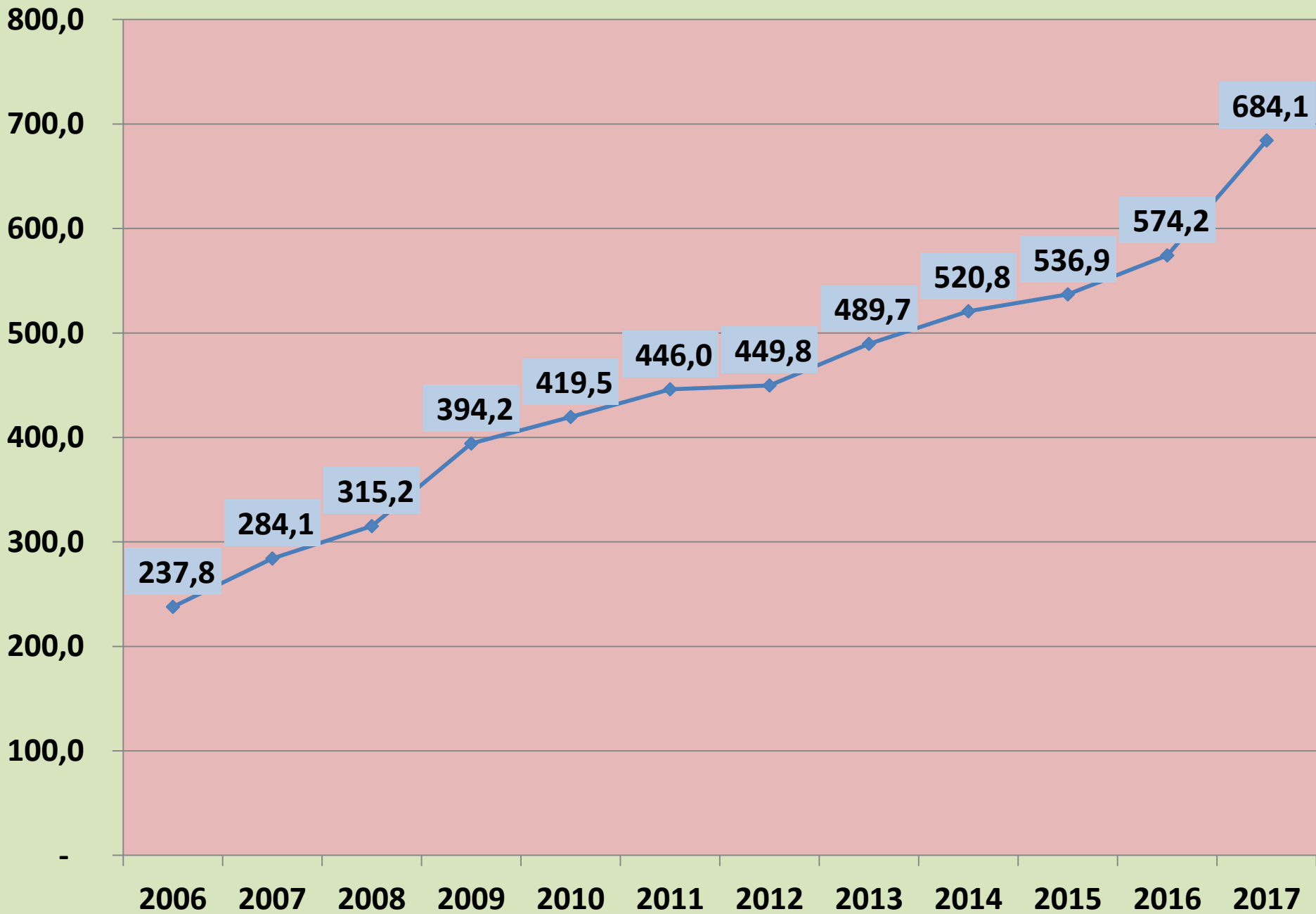
Employee related costs

- **During 2006 to 2017 employees increased cumulatively by 42.58%**
- **Yet sales in GWh stable: Horizontal line**
- **Only conclusion is that Eskom did not manage this**
- **Ave cost/employee up by 19.1% in 2017**

Annual and Cumulative % increase in employee numbers



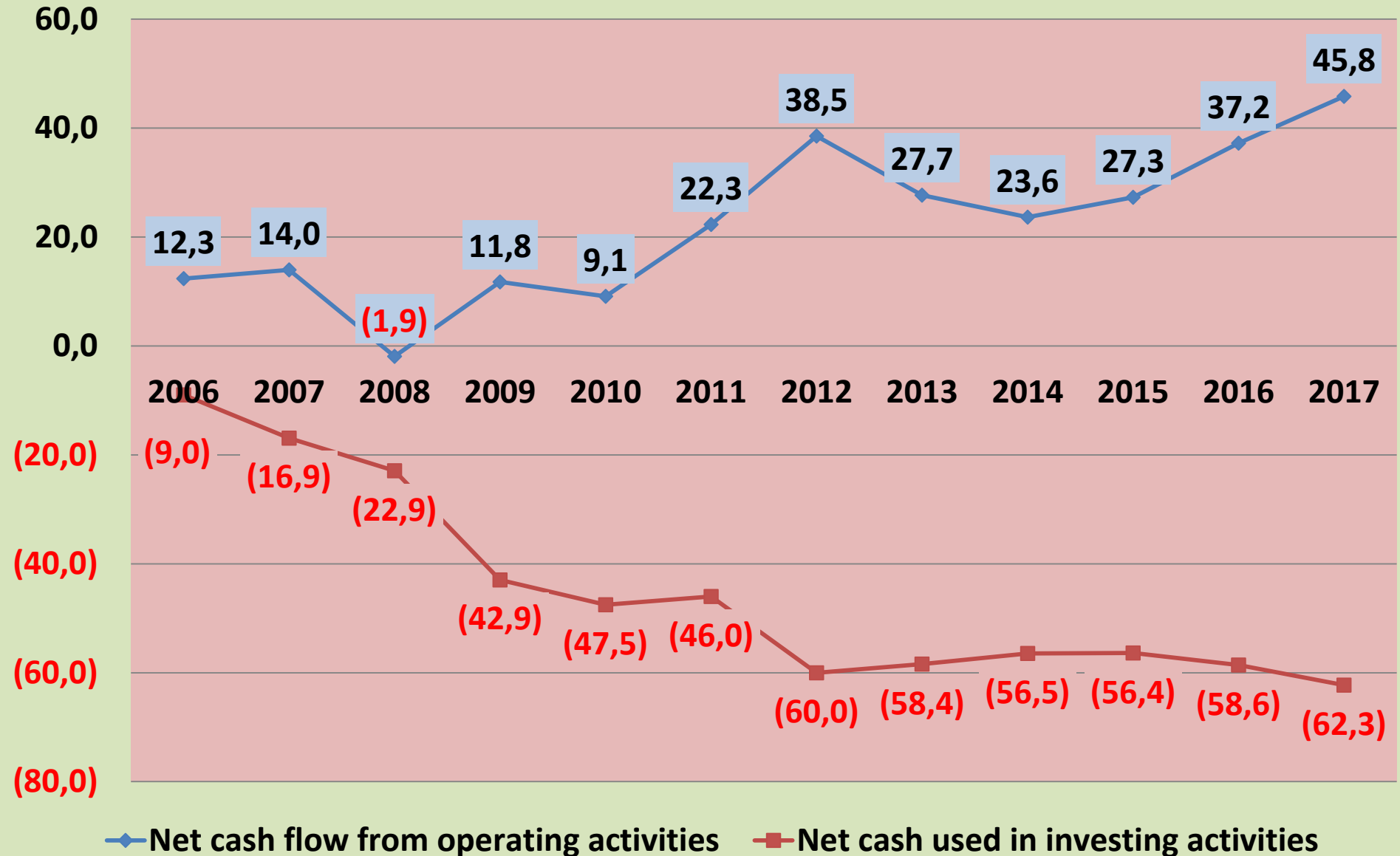
Ave cost per employee (Based on direct costs)(R'000)



Cash flow aspects

- **Reality is that except for 2006 cash flow was negative after investing activities**
- **Major risk if occurs consecutively**
- **Funded by financing of R271.57 billion (Net figure)**

Net cash flow from operating and investing activities (R'billion)

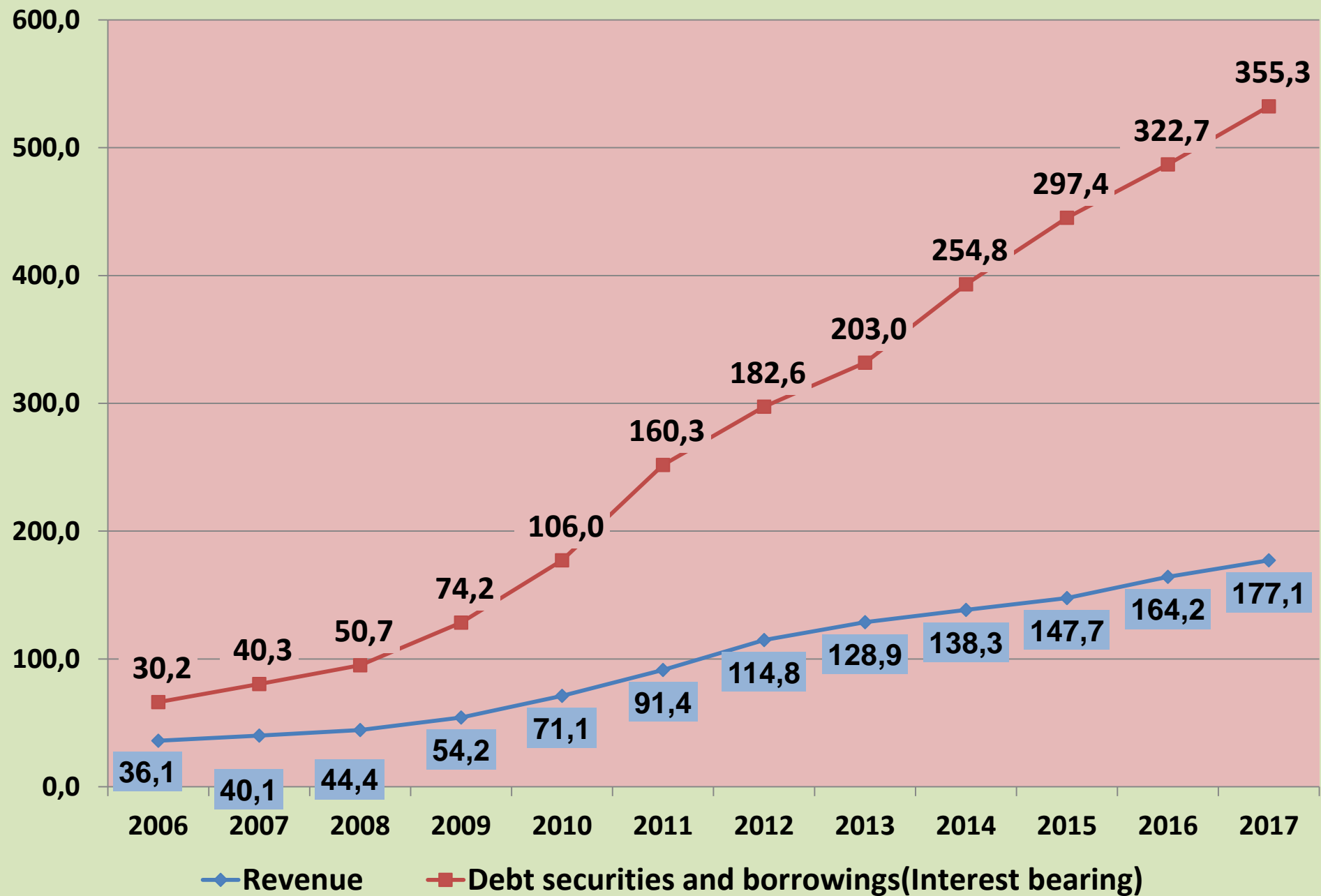


	2009	2010	2011	2012	2013	2014	2015	2016	2017
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Abridged Cash flow statement									
Net cash flow from operating activities	11 764	9 118	22 284	38 522	27 669	23 642	27 311	37 242	45 841
Net cash used in investing activities	(42 945)	(47 524)	(45 995)	(60 013)	(58 408)	(56 461)	(56 386)	(58 590)	(62 286)
Net shortfall before financing	(31 181)	(38 406)	(23 711)	(21 491)	(30 739)	(32 819)	(29 075)	(21 348)	(16 445)
Net cash flow from financing activities	38 871	35 500	20 330	28 727	21 784	41 519	17 954	40 927	7 855
Net (decrease)/increase in cash and cash equivalents	7 690	(2 906)	(3 381)	7 236	(8 955)	8 700	(11 121)	19 579	(8 590)
Cash and cash equivalents at beginning of year	10 893	18 382	15 541	12 087	19 450	10 620	19 676	8 863	28 454
Cash and cash equivalents at end of year	18 583	15 476	12 160	19 323	10 495	19 320	8 555	28 442	19 864
Adjustments	(201)	65	(73)	127	125	356	308	12	561
Cash and cash equivalents at end of year after adjustments	18 382	15 541	12 087	19 450	10 620	19 676	8 863	28 454	20 425

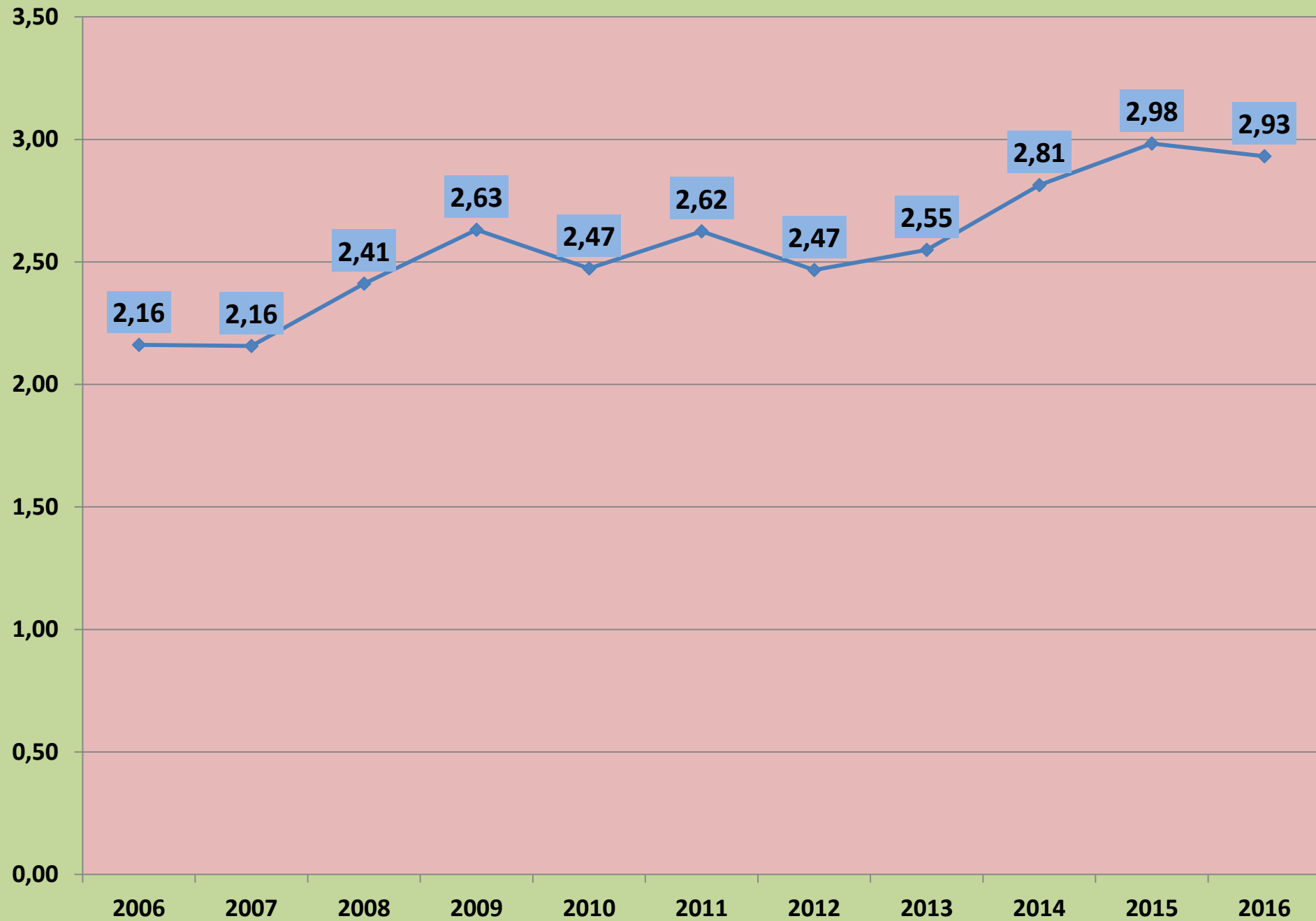
Eskom debt: Guarantees

- **Taking on total debt of R534 billion**
- **Divided by total revenue of R177.1 billion
debt exceeds revenue by factor of 3.02**
- **Even for Eskom this is considered excessive**
- **SUBMITTED STRATEGIC PLANNING IN
AFFORDABLE CAPEX NOT PRUDENTLY
REVIEWED**
- **Risk if total debt exceeds 50% of revenue**

Debt bearing securities to Revenue(R'billion)



Total debt to revenue(Times)



TRUST

- **Good Corporate citizen? History makes it doubtful as well as management capability and practices**
- **Examples: Capex pgm, R&M, Cum Tariffs exceeding Cum inflation 2.96x, 7 CEO's since 2014**
- **Tariffs increase but volume output decreased**
- **Employee numbers increased by 41% without additional sales**
- **Eskom not instilling trust**
- **Reputation: Focus on need for electricity and product rather than Total scenario of country**

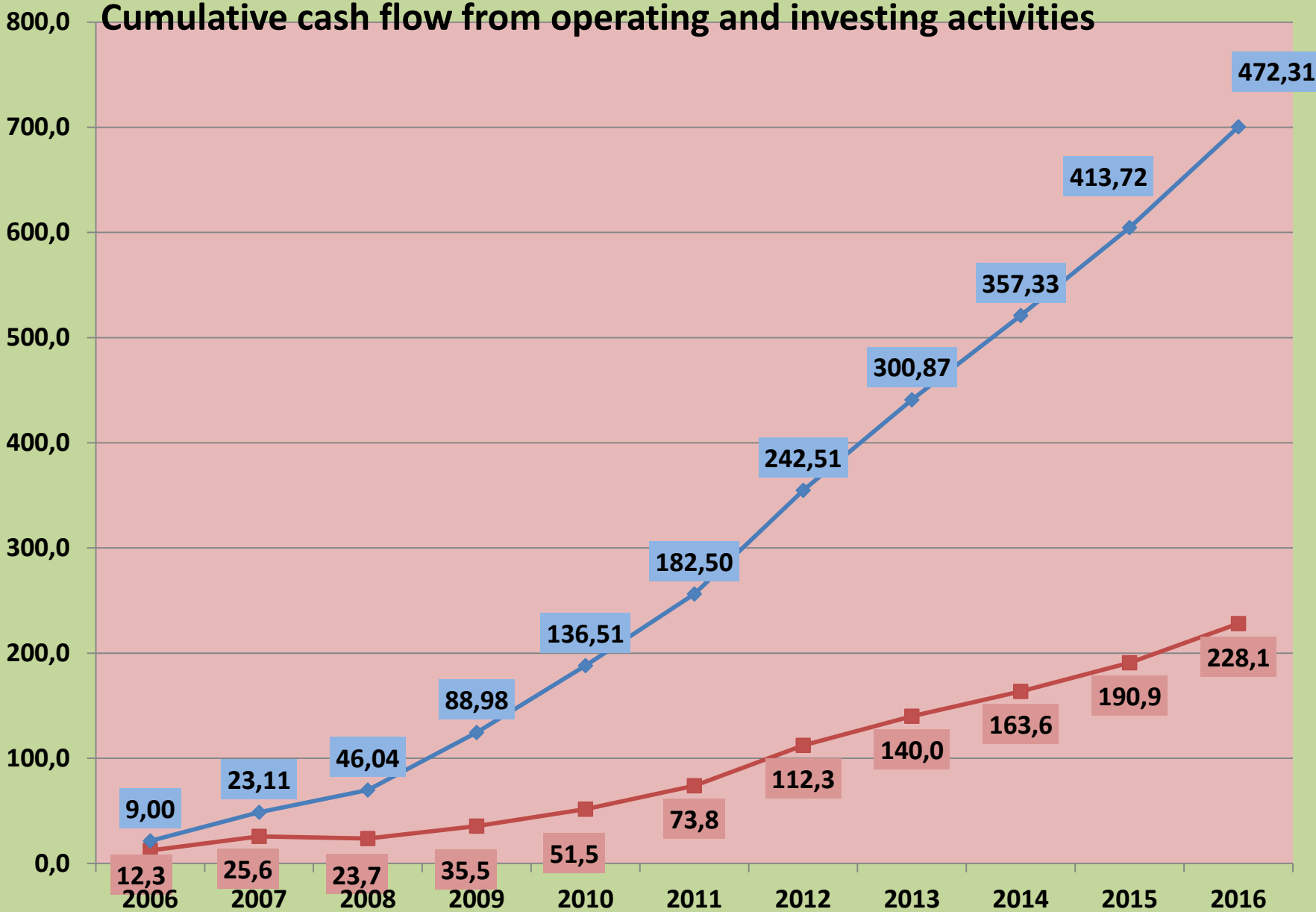
Eskom as a standalone

- **Capex program: Can figures be trusted?**
- **Not investment grade**
- **Raises serious questions on management capacity**
- **Fitch B-, Moody's b3 and S&P ccc+**
- **2015: DSCR below 1**
- **Eskom not sustainable without government support**

Impact on the economy

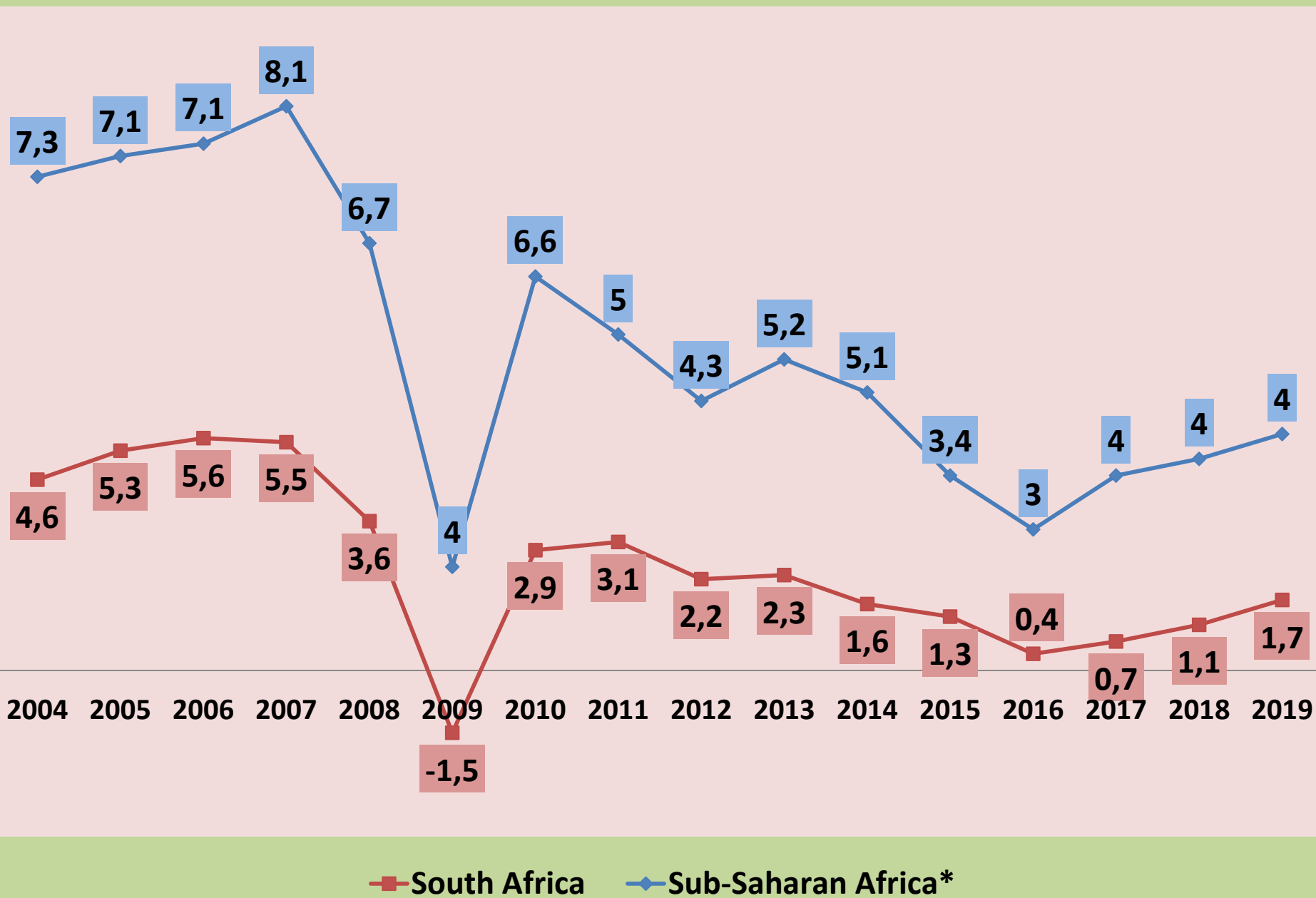
- **Cumulative electricity tariffs 2.96x cumulative inflation**
- **Many businesses forced to close due to Eskom**
- **Consumption and expenditure trends changed due to Eskom tariffs**
- **Away from private sector**
- **DSCR 0.82 (2015) 1.00(2016)**

Cumulative cash flow from operating and investing activities



◆ Cumulative cash flow from investing activities(R'm) ■ Cumulative cash flow from operating activities(R'm)

GDP Sub-Saharan Africa vs RSA



IDEAL STRUCTURE

- **Strategic planning and strategy not performed well**
- **Imperative for hybrid structure not just focussing on Financial position or performance but also cash flow**
- **Require overall framework its balance sheet linked to income statement and debt strategy**
- **Presently seems impossible but this is critical not only for Eskom but also for consumers**

RCA APPLICATIONS

- **Total claim for 3 years R66.685 billion**
- **Revenue claim 84% of total and other aspects**
- **Payback by Eskom is 13%**
- **No steps taken to counter lower sales**
- **Major aspect: Know they can claim it back**
- **IPP only claimable aspect**
- **Eskom not managed as business entity: Claim should be in the order of 5 to 6%**

MYPD3 RCA Trends	Decision RCA 2013/14	Application RCA 2014/15	Application RCA 2015/16	Application RCA 2015/17
Revenue	6 175	8 787	15 578	20 016
Independent PP(IPP)	580	4 346	620	2 452
International purchases	2 700	3 299	3 567	2 282
Coal	2 000	574	3 258	(359)
Open Cycle gas Turbines (OCGT's)	1 252	1 944	689	(1 259)
Other primary energy	72	1 355	728	722
Environmental levy	(312)	(683)	(1 180)	(1 404)
Nuclear decommissioning of R830 m from RCA 2012/13 decision phased in over 10 years	83	83	83	83
Nuclear decommissioning of R361 m from RCA 2015/16 decision phased in over 8 years	0	0	45	0
Energy efficiency & demand side management (EEDSM)	(432)	(149)	(368)	0
Demand market participation (DMP)	(905)	(379)	248	194
Capital expenditure Clearing Account (CECA)	9	91	332	636
Service Quality Incentives(SQI)	339	236	318	343
Inflation adjustment - Opex	33	209	(152)	162
Other income	(353)	(528)	(134)	0
RCA balance R'millions	11 241	19 185	23 632	23 868
Eskom payback	(2 002)	(1 739)	(1 834)	(3 022)
Eskom claiming	7 068	12 137	9 888	6 874
Revenue claim	6 175	8 787	15 578	20 016
Total	11 241	19 185	23 632	23 868
Eskom payback	-18%	-9%	-8%	-13%
Eskom claiming	63%	63%	42%	29%
Revenue claim	55%	46%	66%	84%
Total	100%	100%	100%	100%

POSSIBLE ALTERNATIVES

- **Increase revenue?: Not really appropriate**
- **Reduce cost side: Staff complement, Curbed generation due to demand**
- **Capex: Major contributor to crunch**
- **Financing: Require total review**
- **Stabilising cash flow: 1 st Priority**
- **Government assistance: Strategic plan 5 years**
- **Sell assets to reduce debt where possible and appropriate**

CONCLUSION

- **How poor the management was is shown up in the Soweto figures where payment levels remained at about 16%, and Eskom has not improved the position, but acted to the detriment of other consumers. What may have been politically expedient is now biting, and consumer numbers are not regarded as a fair reflection of the consumer base.**
- **We have to work us out of the predicament over time only but the damage done is considered immense.**
- **The fact that we do not have power outages at present is also testimony to the fact that they have budgeted and forecasted wrongly. The only way out is to take hands and manage us out of this position and try to make Eskom a trustworthy institution for the benefit of consumers, and not only for Eskom.**

Conclusion (cont)

- The following aspects are highlighted:
- A 37.65% increase in tariffs is not affordable: Order should be 5-6%
- Increase should follow and be in line with inflation: This claim not based on this
- Eskom should provide proper submissions on the same basis as for project finance submissions
- Eskom should provide develop a long term strategic plan for at least 5 years
- Information is important regarding the nuclear impact as well as other major projects
- Eskom should provide detail as to why they applied to National Treasury for exemptions of R31.3 billion.
- Eskom's piecemeal applications should be terminated where not a total picture is provided with assumptions.
- Eskom should prepare a sensitivity analysis providing details on the base case, worst case scenario and optimistic scenario.
- Revisit the alternatives outlined above as major aspects

Conclusion(cont)

- **We are at crossroads with Eskom**
- **Heading for serious consequences**
- **Country cannot afford Eskom any longer the way it is run**