Eskom MYPD 4 Application 2019/2020, 2020/2021, 2021/2022

Public Hearing, 17 January 2019, ICC, Durban

PIETERMARITZBURG CHAMBER of BUSINESS
Economic & Enterprise Development

Introduction

- Third largest chamber in South Africa
- Representing 800+ members of all sizes and across all sectors
- Representative and unified organisation – amalgamation of 3 organisations in 2002 – Pietermaritzburg Chamber of Commerce & Industry; Midlands Black Business Chamber and the Pietermaritzburg Sakekamer
- Significant manufacturing in and around the city (mining & manufacturing – 60% of electricity consumption)

3./ Financial Snapshot: Eskom: A Grim Picture

Salient Metrics: Eleven Years	2007	2018	Change %
Total Sales (GWh)	218120	192953	-11.5%
Nominal Capacity (MW)	42618	43488	2%
Revenue (R'bn)	40	177	343%
Net Debt (R'bn)	30	348	1013%
Total Assets (R'bn)	143.70	739	414%
Net Finance Cost (R'bn)	1.70	23.09	1258%
Profit for the Year (R'bn)	4.60	-2.3	-150%
Employees	32674	48628	49%

Eskom Basis for Increase Countered

Key elements of allowed Revenue: Electricity Regulation Act no 4 of 2006 : "must enable an **efficient** **licensee** full costs of it's licensed activities".

With a qualified audit and questions about its going concern status; with several of Eskom's top executives being asked to appear before the judicial commission of inquiry into state capture, energy experts speculating that over R500 billion has been lost to corruption in the last 10 years, the current state of our electricity infrastructure and the load shedding that has been imposed on citizens, it would be remiss of any of us not to question the "efficiency" of Eskom. No private sector business's shareholders would ever tolerate results like this – decreasing sales; bloated staffing; ballooning debt (over 1000% in 10 years) and financial losses. Quite honestly, it's shameful and it's embarrassing for all South Africans.

Eskom cannot, in its current state, be considered an efficient licensee. I must on this basis, start then by questioning whether this is then even a valid application?

PCB
Pietermaritzburg Chamber of Business
Economic & Enterprise Development

Recovery of Efficient Costs: Primary energy costs: own generation; IPP's and imports

- Coal procurement practices are questionable – reports of emergency procurement (bypassing tender regulations); paying inflated prices; the eroding of stockpiles; supply issues; quality of supply issues; incurring unnecessary transport costs etc. What % are actually efficient costs?
- We object in the strongest terms to the indefensible IPP contracts, expensive energy that Eskom must buy when it is available regardless of whether or not we need it. It's 13% more expensive than self-generation. Eskom has the generation capacity, so what is the justification? These contracts should be investigated, terminated or renegotiated. This expenditure cannot be considered to have been efficiently incurred.

Recovery of Efficient Costs: Operating Costs

- Majority attributable to employee costs - the World Bank calculated that Eskom needs a workforce of 14244, which means that there are estimated to be more than 30 000 too many staff members employed. The policy of shedding staff by natural attrition is not acceptable under these circumstances. Eskom should only be entitled to recover salaries attributable to the recommended number of staff for the customer base.
- Average cost per employee was R708000 in 2018/2019 (wow) - excessive salary spend estimated to be R 21 240 000 000.

Recovery of Efficient Costs: Operating Costs

- Eskom say that they've made "every effort to control operating costs" – their AFS's cite fiduciary duty breaches; irregular contracts; providing of guarantees for private enterprises - there were even evidently over-priced tea contracts?! So, my question is how? How've they made every effort to control operating costs?
- Cost reflective tariffs are what they say they are asking for, but their expenses are clearly inflated and therefore inefficient and they shouldn't be allowed to recover them in full.
- The submission refers to elements "outside of Eskom's operational control e.g. debt service costs and IPP costs" – what are they saying? They can't control their borrowings or debt levels and they are not responsible for the contracts that they are signing? All these paid executives with no control?

Earning a Reasonable Return on Assets

- Due to "inadequate capacity and financial limitations" mid-life refurbishment and plant maintenance hasn't been performed and there has been a decline in plant availability – what have the 30 000 extra people been doing all this time?
- Massive over-spending on capital projects, which is totally unacceptable – inefficient and imprudently incurred costs should be disallowed.
- The revaluation of the Regulatory Asset Base is unacceptable, we believe that the assets are now substantially overstated. While this may make the Balance Sheet look more attractive, it is unrealistic and punitive for consumers. The "phasing in" approach does not in any way make this more palatable. Eskom's reference in the application to making "sacrifices" in the interests of the economy would be laughable if it wasn't so insulting.

PIETERMARITZBURG CHAMBER of BUSINESS
Economic & Enterprise Development

Revenue Recovery

- Cost reflective revenue that covers efficient and prudent costs and that allows a reasonable return that matches the debt service commitments. Two problems. I think we've established that a % of the costs are neither efficient nor prudent. Debt has grown to R419 billion and we are servicing long-term capital requirements with short-term loans. The capital spend program is unjustified in the context of falling demand. The debt levels are reckless and irresponsible and it doesn't sound like they can be fully Justified from an operational perspective (are we paying interest on maladministration and/or corruption?).

Electricity Price Impact

- Eskom maintains that consumers had below inflation increases in recent prior years. This is ludicrous – between 2008 and 2013 electricity prices more than doubled in real terms (inflation-adjusted) rising by a cumulative 114%. For MYPD3 ± CPI + 2%
- A phased, smoothed increase of 15% PA is now proposed for MYPD4. Compounded, this is 52% in 3 years in addition to claw-backs from the RCA process.

This is ridiculous in the current economic context. It's not economically viable and it's unaffordable.

- World Bank: SA Anticipated growth rate of 1.3% in 2019;
- PCB at the coalface watching large companies, as well as small, closing down;
- A large proportion of our factories process metal, so electricity is a high input cost – often second to labour;
- Costs cannot be passed on in pricing to customers – rendering firms uncompetitive;

PCB
Pietermaritzburg Chamber of Business
Economic & Enterprise Development

- Foreign investors are hesitant to invest further in view of the political, policy & economic uncertainty – global companies are very unlikely to prop up ailing divisions, more likely to relocate to other more conducive environments;
- It is simply not affordable and we can't afford to make ourselves more unattractive from an investment perspective. Increases of this level will put a number of businesses out of business.

Proposed Increase is not fiscally responsible and it's unsustainable for Eskom

- By Eskom's own admission, their sales are decreasing annually. A lot of this was self- inflicted by unreasonable price hikes and load-shedding - businesses have invested in alternative energy like solar plants to ensure security of supply and to mitigate costs. The price elasticity of electricity demand was considered fairly inelastic when price hikes were reasonable, but when the price of electricity (in real terms) started to rise sharply post 2007, price elasticity of dd was significant and negative: 1% increase in price ⇨ between 0.2% and 0.5% decrease in electricity dd - Deloitte, 2017.
  Eskom's actions have significantly contributed to the decreased demand and the more they put unrealistic tariff increases in place, the fewer customers Eskom will have in the future.
- The compound effect of these kinds of increases will negatively impact growth and there is a strong correlation between GDP growth and electricity sales in South Africa (1% increase in GDP ⇨ 1% rise in electricity demand – Deloitte, 2017).
- While low growth can account for some of the fall in sales, it's nonsensical to exacerbate the situation with exorbitant tariff increases. Eskom is eroding its own customer base by it's actions – it's self-defeating.

PCB PIETERMARITZBURG CHAMBER of BUSINESS
Economic & Enterprise Development

Conclusion

- How can Eskom's "Balance Sheet problem" be our shared responsibility to resolve? Sorry Eskom, but your apology is not accepted. You've created this problem, presumably with the blessing of your shareholder, and between you, you need to sort it out. The business community cannot and will not fund inefficiency and corruption. Unlike you, we run a tight ship, because we are forced to compete. Get your house in order before you look to us. You can't expect us to mop up the mess.
- This means restructuring the organisation (massive retrenchment); halting of new-build programs (until demand justifies build), interrogation of coal contracts; cancellation/freezing and/or re-negotiation of IPP contracts – should be delayed until capacity is required and pricing equals self-generation costs.
- I think that Eskom tariffs should be limited until there has been a full forensic investigation and appropriate costs have been established, the guilty have been charged and the wheels set in motion to recover the South African citizens lost billions and the SOE is restructured and operating efficiently.
- Any increase that is above inflation in any period is rejected by business, because it can't be justified and it is unaffordable – it is economically unviable – for the country and for Eskom.

PCB
PIETERMARITZBURG CHAMBER of BUSINESS
Economic & Enterprise Development