



MINISTRY OF FINANCE
REPUBLIC OF SOUTH AFRICA

MINISTER OF FINANCE, HON T MBOWENI, MP

TUESDAY, 23 JULY 2019

NATIONAL ASSEMBLY: 10:00

Honourable Speaker

Honourable Members

I am pleased to present the Special Appropriation Bill to provide additional financial support to Eskom for the current and next financial year.

On 11 July 2019, I stated in my Budget Vote 7 for the National Treasury, that Eskom presents the biggest risk to the fiscal framework because of its financial problems and negative impact on the economy. Given the high risks of a systemic failure if Eskom were to collapse, government is urgently working on stabilizing the utility, while developing a broad strategy for its future.

Eskom faces serious financial and operational challenges, which to a large extent were caused by the governance challenges that the entity previously experienced which resulted in a decline in investor confidence.

Eskom is not financially sustainable based on its current high levels of debt and its inability to generate sufficient revenue to meet its operational and capital obligations, which exposes the entity to high levels of liquidity and balance sheet risks. Therefore, without major changes to Eskom's business model and financial assistance being provided by Government, the company will be unable to meet its financial obligations through the 2019/2020 financial year. At a strategic level, we must thus face the reality that a large, vertically integrated energy company is an outdated model in a changing industry, both domestically and internationally.



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Honourable Members should also be reminded that the fiscal support we are announcing today will come at a significant cost to the fiscus and to South African taxpayers. In addition to the financial support to Eskom, there is also a preliminary indication that tax revenue could be significantly lower than budgeted for in the 2019 Budget. This could substantially increase the government borrowing requirement for 2019/10, which will require government to revise its funding strategy and current weekly bond issuance levels before the MTBPS in October.

It is important that the House notes that Eskom's debt reliant liquidity situation is a result of the poor interest coverage of its revenue, the decline in sales volumes year-to-date, as well as the cost of primary energy, high employee costs and the continuing cost escalations of the new build programme due to its persistent delays. This situation has resulted in Eskom having to borrow increasing amounts to service its debt obligations, placing the entity in an unsustainable position.

Although Government has committed R23 billion to be allocated to Eskom over the next 3 years in the current fiscal framework, Eskom's funding plan is dependent on Eskom raising additional finance from the market, which in turn requires Eskom to be a going concern. It is therefore important to note that the proposed financial support for 2019/20 and 2020/21 financial years addresses the going concern status and enables Eskom to honour its obligations.

Therefore, this Special Appropriation Bill request approval for additional financial support for Eskom as follows:

- a. Additional R26 billion in 2019/20 financial year; and
- b. R33 billion in the 2020/21 financial year.



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However, the future sustainability of Eskom will have to address the debt and the restructuring of Eskom.

In this regard, I must inform the House that a team of officials led by the Director-Generals of National Treasury and Public Enterprises have considered a number of options as a solution to the company's debt challenge in order to ensure its sustainability, and the most viable of these will be communicated in due course. The Chief Restructuring Officer, who will be appointed shortly, will be mandated to test these options with the ratings agencies to establish what impact each will have on the fiscus and recommend the appropriate one for implementation.

National Treasury in consultation with the Department of Public Enterprises have developed the terms of reference and scope of work for a Chief Restructuring Officer and I will be making the appointment soon.

I wish to repeat what I said in my Budget Vote Speech: "*We really and truly cannot go on like this*". Therefore, it is important that Government urgently implements the restructuring of Eskom into three entities - Generation, Transmission and Distribution. Separating Eskom will have numerous benefits such as:

- Allowing strong parts of the business to raise funding more cheaply;
- Creating higher transparency across the value chain and reduce opportunities for fraud, corruption and rent-seeking;
- Creating clear performance incentives in each business;
- Reducing systemic risk South Africa faces by having one very large entity, where problems in one part of the electric value chain now affect the entire value chain. Instead, it will isolate problems and deal with them where they arise, without compromising the entire system;



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- Positioning the electricity sector to embrace clean technology, distributed generation and respond to other industry changes;
- Reducing support required from the government in the form of capital outlays and sovereign guarantees, mainly due to increased private sector participation and funding over time;
- Generating competition in the electricity market that is expected to drive improvements in efficiency and put downward pressure on prices;
- Providing open access to the grid and remove conflicts of interest to the procurement of power, both conventional and renewable, from IPPs;
- Diversifying the generation of electricity across a multitude of power producers, thereby reducing the country's reliance on a single supplier; and
- Providing a stable platform for transparently contracting least-cost and most secure power.

However, failure to strengthen Eskom's balance sheet urgently while the Government is working on long term sustainable solutions may likely have a negative systemic impact as Eskom is the largest non-bank corporate debt issuer in South Africa and any default will result in a crisis for Government and to some South African banks given that Eskom is the largest exposure to some banks and Government.

CONCLUSION

As I conclude, Honourable Speaker, let me remind members that government remains committed to supporting and strengthening Eskom in order to ensure that the entity achieves business and financial sustainability and maintains adequate liquidity levels to continue operating as a going concern and ensure the security of electricity supply.

However, without major changes to Eskom's business model, the company will not be financially sustainable and may not be able to ensure security of electricity supply



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beyond the medium-term, with significant consequences for the economy. The frequency of the power shortages has risen in recent years, and government needs to act boldly and decisively. We are therefore committed to a significant reform agenda for the entity.

Honourable Speaker, I hereby table the Special Appropriation Bill for consideration by Parliament and I look forward to a constructive debate.

ENDS