Report of the Portfolio Committee on Public Enterprises on the Budget Vote 9: Public Enterprises and the annual performance plan for 2016/17 of the Department of Public Enterprises, dated 20 April 2016

The Portfolio Committee on Public Enterprises, having received a briefing from the Department of Public Enterprises on the strategic plan and the budget vote reports as follows:

1. Introduction

Guided by the Rules of Parliament, promulgated in terms of the Constitution, the Portfolio Committee on Public Enterprise plays an oversight role on the Ministry, Department and the entities. The Committee has to scrutinise the strategic plan and annual performance plan of the Department and its entities in order to see if the funds requested are aligned to the objectives as stated in the respective strategic plan documents.

1.1 Background

The State has a developmental role to play and uses state-owned companies as the primary tools to deliver on its developmental role. The developmental role should support a number of economic and development goals including; delivery of strategic infrastructure that will unlock growth potential in the country; support of the wider economy and marginal business sectors and support of economic recovery where needed. The State requires strategic, organisational and operational capacity to play its developmental role. SOCs fulfil the States operational role in this requirement, acting as the implementing agents for national strategy.

1.2 Strategic Context

The current state of the economy presents a major challenge that needs to be actively addressed by the State. The poor performance of the global economy has exposed weaknesses in the domestic economy, which include:

Economic Outlook

- Greater dependency on the commodities that are vulnerable to changes in the global economy;
- Level of concentration in the economy that undermines new entrants;
- Infrastructure network that is geared for commodities and not support regional integration and industrialization;
- Limited participation of the larger part of society which limits the vicious cycle of sustained growth;

Investment in the Economy

- Investments in the economy has remained below the National Development Plan target;
- The productive sectors of the economy has been worst affected with investments in mining and manufacturing leveling off;
- This present a major challenge for the economy and the investment driven growth approach presented by Government in the New Growth Path and National Development Plan;
- This is requiring Government and its institutions to play a leading role in the short to the medium term;
- In 2005 investment by the public sector amounted to just over R80 billion per annum;
- Over a period of 10 years this has increased to R261 billion;
- While private sector investment still represents a greater proportion of total investment in the economy;
- In 2013 private sector invested R412 billion but this has declined between 2014 and 2015 and falling below the R400 billion level;
- Private sector investments still dominated by mining and financial services;
- Investment by manufacturing remains weak.

2. Strategic Plan of the Department of Public Enterprises

The Department of Public Enterprises presented their Strategic Plan to the Portfolio Committee on Public Enterprises and elaborated a separate Annual Performance Plan. The department described the overarching policy and strategic direction and priorities of Government, as articulated in the State of the Nation Address by the President, Budget Speech, and National Development Plan.

2.1 Mandate of the Department of Public Enterprises

The mandate of the Department is to ensure that state-owned companies within its portfolio are directed to serve Government's strategic objectives as outlined in the National Development Plan and further articulated in the New Growth Path, and the Industrial Policy Action Plan. The Department exercise shareholder responsibility over the six state-owned companies. The Department aims to ensure the financial sustainability of the state-owned companies and supports the government's strategic priorities of economic growth, expanding employment and developing infrastructure.

2.2 Strategic Objectives of the Department

The strategic objectives of the department has changed to place greater emphasis on supporting the re-industrialisation programme of Government; strengthening inter-governmental relations; greater joint planning and execution between the Department and its portfolio of SOCs; active engagement with society to make SOCs and Department more accountable to the public as part of building confidence in the state and its institutions; pursuing fewer high impact targets with greater influence in the transformation of the economy and capacity building programmes to support other spheres of Government.

The Department is focusing on implementing the National Development Plan during the 2015/16 financial year. The main goal of the Department is to ensure that the state-owned companies support the implementation of the National Development Plan and contribute to the achievement of outcomes outlined in the plan.
The Department's strategic goals over the medium term are to:

- focus on improving the performance of the portfolio to ensure that the companies can efficiently and effectively carry out their mandates;
- recognise the role that SOCs needs to play in the current economic context to support the aspirations of the developmental state;
- build on the progress that has been made in the Department to promote good governance to turnaround the portfolio;
- Build the capacity of the shareholder through internal re-organisation using existing resources;
- Review the shareholder oversight to ensure alignment of SOC to developmental outcomes;
- Promote good corporate governance;
- Stabilise SOCs by the strengthening of balance sheets and funding options;
- Drive economic infrastructure investment to enhance the capacity of the economy with emphasis on the Strategic Integrated Projects;
- Leverage SOCs procurement spend to support industrialisation and transformation.

Table 1: Illustration of Strategic Objectives, Outputs and Impact

Strategic Objectives	Outputs	Impact
Ensure SOC financial sustainability	Improved SOC balance sheets Funding options identified and implemented	SOCs are enabled to fund build programmes and general business operations
Ensure SOCs maintain commercially viable operations	Increased electricity reserve margin Improve productivity at the ports The shift from road to rail for the transportation of road friendly freight Improvement in the performance of strategic corridors	Increased productivity of SOCs Increased shareholder value
Accelerate capital project delivery	Increased infrastructure investments as a percentage of GDP Monitoring of the current build programme to ensure delivery within provided timeframes Assessment of the SOCs investment plans to ensure alignment with the NDP	Enhanced infrastructure, thus greater economic capacity
Accelerate the transformation of the South African economy	Development and implementation of transformation programme in line with the current BBBEE Codes SOCs Skills Development Programmes	Accelerated deracialisation of the economy Increased number of learners trained in critical and scarce skills
Explore initiatives to support development of SMMEs, cooperates as well as rural and township enterprises including businesses owned by targeted groups1	Development of support packages for the targeted enterprises within the value chain in which the SOCs participate MOU with Small Business Development Department concluded	Increased participation of targeted enterprises in the SOCs value chain

Strategic Objectives	Outputs	Impact
Advancing the re-industrialisation of the South African economy	Review of the competitive supplier development programme (CSDP) Assessment of the current procurement legislation framework and their impact on localisation Increase the local content on the build programme in line with the Industrial Policy Action Plan (IPAP) Identify industrialisation opportunities in the aerospace and other industrial sectors in which SOCs operate Build a business case for the access of industrial incentives for SOCs involved in manufacturing	Reduction in import leakages Development of new industrial capabilities Improvement in the performance of productive sectors of the economy
Accelerate development of skills to support the needs of the economy	Accelerate the current skills development programmes Develop financing options to support the scaling up of the skills development initiatives	Increased number of skilled people to support the broader development of the economy
Strong shareholder	Reorganised shareholder model Repositioning of the DPE through improved internal processes Competent and capable board appointed Knowledge sharing platforms created Performance management system implemented	Improved SOC management Improved performance and consequence management
Alignment and efficiency across institutional model	Shareholder policy Revised shareholder model and role	Increased ability to manage SOCs Clearly defined roles and responsibilities Improved decision-making

2.3 Policy Priorities for 2015/16

As a shareholder representative of Government, the Department does not have the mandate for developing policies. However, some of the powers and duties of the Department are intertwined with those of other Government Departments who are key role players in the SOC regulatory environment. These include the Department of Energy, the Department of Transport, and the Department of Mineral Resources, among others. However, the Department and its SOCs are

required to align with various other economic policies such as the National Development Plan (NDP), the New Growth Path (NGP), the Industrial Policy Action Plan and various other charters.

The Department does not directly execute programmes but seeks to leverage off state ownership in the economy to support the delivery of key outcomes outlined in the NDP and government's 2014-2019 Medium Term Strategic Framework. Through its mandate, the department contributes to the NDP's objectives through outcome 4 (decent employment through inclusive economic growth) and outcome 6 (an efficient, competitive and responsive economic infrastructure network). Over the medium term, the Department has oversight of Alexkor, Denel, Eskom, The South African Forestry Company (SAFCOL), South African Express (SAX) Airways and Transnet.

The Department's medium term focus will be on facilitating a conducive environment for repositioning SOCs to advance their developmental mandate, and enhance their financial ability. It will also prioritise enhancing the efficiency of strategic transport corridors, including monitoring Transnet's Market Demand Strategy (MDS) to expand rail and pipeline capacity and improve ports' productivity. The Department will also prioritise the implementation of government's support package for Eskom. Government's support package to Eskom is intended to both improve Eskom's financial sustainability and ensure that the build programme is delivered within the timeframes specified. The stability of the electricity grid and the finalisation of the build programme was highlighted in the President's State of the Nation Address in February 2015. The Department will oversee the implementation of catalytic projects that form part of strategic integrated projects, and it will oversee the Competitive Supplier Development Programme (CSDP) as part of deepening industrial capabilities.

The programme Administration gets the largest portion of the budget with 57.7 per cent, down from 59.3 per cent in the previous year. This is due to the labour intensive nature of the Department, where most of the sub-programmes located here cuts across all the programmes. Programme 3: Portfolio Management and Strategic Partnerships makes up the second largest budget at 32.8 per cent, an increase on the 31.8 per cent received in the previous financial year. The programme oversees the implementation of the strategic integrated projects as well as the CSDP. The programme budget increases to R93.9 million over the medium term. The Transnet and Eskom oversight function is also located in this programme. Programme 2: Legal and Governance receives the least with R26 million or 9.5 per cent of the R274 million budget received in the 2016/17 financial year.

The majority of the Department's spending is on compensation of employees at 60.5 per cent over the medium term. The number of personnel is expected to remain constant at 226, excluding graduates and interns, over the medium term.

The Department had similar policy priorities for the previous financial year of 2015/16, however the current priorities are more defined and aligned with the priorities outlined in the State of the Nation address, including the identification of non-core assets for disposal in order to strengthen the balance sheets of the SOCs. This outcome will have to be added to the Department's 2016/17 Annual Performance Plan, as it is a new objective and was not mentioned in the 2015/16 Annual Performance Plan.

3. Programmes of the Department

3.1 Programme 1: Administration

The purpose of this programme is to provide strategic leadership, management, and support services to the Department.

The Department's core functions require significant administrative support, and a substantial portion of the budget is in the Administration programme, which has cross-cutting sub-programmes providing for intergovernmental and international relations, strategic planning, monitoring and evaluation, and communications.

Over the medium term, the majority of the allocation is within compensation of employees, which will provide technical and administrative support to the Department. Expenditure on compensation of employees constitutes 51.2 per cent over the medium term. Expenditure on compensation of employees increased between 2012/2013 and 2015/16 by 10.8 per cent due to funding received for improved conditions of service. Over the medium term, expenditure on compensation of employees grows by 4.4 per cent from R77.2 million to R87.9 million. The number of personnel is expected to remain constant at 127 employees over the medium term.

Spending on consultants is expected to decrease by 12.6 per cent over the medium term due to Cabinet approved reductions, however, consultants remains 7.8 per cent of the budget over the

medium term. Goods and services constitute 46.3 per cent of the budget over the medium term. Travel and subsistence constitute 10.2 per cent of the budget, and increases by 4.7 per cent over the medium term, which is required by the programme to carry out its oversight function of the state-owned companies, situated throughout South Africa.

3.2 Programme 2: Legal Governance

The purpose of this programme is to provide legal services and corporate governance systems, as well as facilitating the implementation of all legal aspects of transactions that are strategically important to the Department and state-owned companies', and ensures alignment with Governments strategic intent by, among others, monitoring the performance indicators of SOCs.

The spending focus over the medium term will be on increasing the programme's capacity to provide legal services, and transactions and contract management support; and on facilitating the creation of a legislative framework for the Department's mandate to ensure compliance with applicable legislation and enhance corporate governance procedures by state-owned companies. The programme's average budget has stayed the same over the 2012/13 - 2015/16 period. The programme's budget is expected to increase by 5.8 per cent from R23.5 million in 2015/16 to R27.9 million in 2018/19.

The sub-programme Legal constitutes the largest unit of the programme at 53.9 per cent of the budget over the medium term, followed by the sub-programme Governance at 33.6 per cent. The Legal unit increases by 7.2 per cent from R12.2 million in 2015/16 to R15.1 million in 2017/18.

Over the medium term, 75.6 per cent of the programme's budget is allocated to be spent on compensation of employees over the medium term, with the number of personnel expected to remain constant at 20 employees over the medium term. Compensation of employees increases by 3.3 per cent over the medium term, from R18.5 million in 2015/16 to R20.4 million in 2018/19. Expenditure on consultants is expected to increase by 24.2 per cent over the medium term from R1.7 million in 2015/16 to R3.3 million in 2018/19. Legal services increase by 6.2 per cent over the medium term, from R2.1 million in 2015/16 to R2.5 million in 2018/19. Travel and subsistence decreased by 27.5 per cent from 2012/13 to 2015/16, travel and subsistence however, increases by 11.5 per cent to R1.5 million over the medium term.

3.3 Programme 3: Portfolio Management and Strategic Partnerships

The purpose of the programme is to align the strategies of the SOCs with government policy and strategy, and monitor and benchmark their financial and operational performance and capital investment plans. Align shareholder oversight with overarching government economic, social and environmental policies and build focused strategic partnerships between the SOCs, strategic customers, suppliers and financial institutions.

Over the period 2011/12 and 2014/15, Energy Enterprises and Manufacturing enterprises constituted approximately 90 per cent of the programme's budget. This was due to the following transfers:

- R118.3 million in 2012/13, R57.3 million in 2013/14, R63.1 million in 2014/15 and R33.1 million in 2015/16 to Denel for indemnity claims and a further R700 million in 2012/13 to recapitalise the company in the Manufacturing sub-programme; and
- R350 million in 2012/13 to Alexkor in order to address obligations in terms of the deed of settlement in the Manufacturing sub-programme.
- Eskom will receive R23 billion for the enhancement of electricity generation capacity and security of supply, as mentioned above.

Over the medium term, the programme's budget decreases by 84.0 per cent from R23.1 billion in 2015/16 to R93.9 million in 2018/19. The decrease is due to the Department projecting not to make any further transfers to the state-owned companies in the foreseeable future. The programme, however, remains the department's most significant programme, with a budget of R275.2 million over the medium term. Through this programme, the department will support government's build programme and the overall strengthening of the SOCs balance sheet by developing innovative funding structures and designing the associated compacts with SOCs. The Department will also support the IPAP by enhancing the CSDP as part of government's localisation scheme.

3.3.1 Sub-programmes

The sub-programme Energy Enterprises purpose is to strengthen the department's oversight role by ensuring the alignment of shareholder strategic intent in relation to the SOCs role in achieving

government objectives in the energy sector, on an on-going basis. The Department will oversee Eskom's support package and ensure that the entities build programme contributes to the countries growth objectives. The budget for Energy is expected to decrease by 90.7 per cent over the medium term, from R23 billion in 2015/16 to R18.4 million in 2018/19. The budget decrease over the medium term is skewed due to the once-off Special Appropriation of R23 billion in the 2015/16 financial year. Over the next three financial years until 2018/19, the programme constitutes 19.7 per cent of the total programme expenditure.

The sub-programme **Manufacturing Enterprises** oversees the SOCs in the defence, mining and forestry sectors, these being Denel, Alexkor and SAFCOL. The budget decreases from R52.7 million in 2015/16 to R21.7 million in 2018/19, a decrease of 25.6 per cent in nominal terms. The decrease is due to the R33.1 million the sub-programme received during the Adjusted Appropriations for the indemnity payment to Denel. Thus the budget of R20.7 million in 2016/17 may not be a true reflection of the sub-programme's budget if another indemnity payment is made to Denel during the 2016 Adjusted Estimates of National Expenditure (AENE).

The sub-programme **Transport Enterprises** oversees the Transnet and South African Express Airways. The Department has prioritised enhancing the efficiency of strategic transport corridors which includes the monitoring of Transnet's market demand strategy to expand rail and pipeline capacity and improve ports' productivity. They will continue to enter into compacts with Transnet on improving efficiency and on capital projects aimed at creating capacity. In consultation with the Department of Transport and Transnet, the Department will review the impact of pricing in freight logistics.[1] The budget for the sub-programme constitutes 27.1 per cent over the medium term of the programme budget. The sub-programme budget increased in nominal terms by 2.7 per cent from R23.1 million in 2015/16 to R25.1 million in 2018/19. The nominal increase is due to the shift of South African Airways to the National Treasury.

The sub-programme **Economic Impact and Policy Alignment** ensures policy alignment of SOCs sustainability, economic and social transformation agendas, and compliance with environmental laws, conducts macroeconomic modelling and research as well as economic impact assessments of the SOCs. The sub-programme's budget constitutes 15.9 per cent of the programme's budget over the medium term. The sub-programme's budget increases in nominal terms by 2.2 per cent from R14.3 million in 2015/16 to R15.3 million in 2018/19.

The sub-programme **Strategic Partnerships** oversees the implementation of catalytic projects, the implementation of innovative funding structures, and implementation of the competitive supplier development programme. It also supports the coordination of the strategic infrastructure projects led by the SOCs in its portfolio. The sub-programme constitutes 14.3 per cent of the programme over the medium term. The sub-programme's budget increases in nominal terms by 10.6 per cent from R10 million in 2015/16 to R13.5 million in 2018/19.

Compensation of employees constitutes 70.9 per cent of the programme's budget over the medium term, with goods and services accounting for 29.1 per cent. Compensation of employees increases by 4.3 per cent from R57.5 million in 2015/16 to R65.2 million in 2018/19. Personnel in the programme is projected to remain constant at 79 over the medium term. Goods and services is expected to increase by 3.2 per cent over the medium term from R26.1 million in 2015/16 to R28.6 million in 2018/19. The Department makes use of consultants for specialised services in transport, manufacturing and energy sectors, which is still a necessity, thus consultants increase by 9.5 per cent over the medium term from R16.1 million in 2015/16 to R21.1 million in 2018/19. Consultants accounts for 21.0 per cent of the budget over the medium term. This increase in consultants is allowed by the decrease in consultants in Programme 1: Administration.

3.4 Budget

As stated above over the medium term the Department will focus on strengthening its oversight functions, increasing the public sector's investment in the economy, reducing SOCs' reliance on the fiscus, and ensuring the financial sustainability of SOCs.

Table 2

Programme	Budget				Nominal Rand change	Real Rand change	Nominal % change	Real % change
R million	**2015/16**	**2016/17**	**2017/18**	**2018/19**	**2015/16-2016/17**		**2015/16-2016/17**	
Programme 1: Administration	151.9	158.0	161.4	168.2	6.1	- 3.7	4.02 per cent	-2.42 per cent
Programme 2: Legal and Governance	23.5	26.0	26.7	27.9	2.5	0.9	10.64 per cent	3.79 per cent
Programme 3: Portfolio Management and Strategic Planning	23 107.2	90.0	91.4	93.9	- 23 017.2	- 23 022.8	-99.61 per cent	-99.63 per cent
TOTAL	**23 282.6**	**274.0**	279.5	289.9	**- 23 008.6**	**- 23 025.6**	**-98.82 per cent**	**-98.90 per cent**

Table 2 describes the changes in allocations from the years 2015/16 and 2016/17, and the outer years of the MTEF. From this the following can be concluded. Programme 1: Administration, has a nominal increase of 4.0 per cent in 2016/17, with real decrease of 2.4 per cent. Programme 1 accounts for the largest allocation of the Department's overall budget with 57.7 per cent of the budget in 2016/17. Programme 2: Legal and Governance receive the smallest allocation of 9.5 per cent in 2016/17. The programme increases by 10.6 per cent in 2016/17 or in real terms by 3.8 per cent. Programme 3: Portfolio Management and Strategic Partnerships accounts for the second largest allocation of the budget, accounting for 32.9 cent of the budget in 2016/17. Programme 3 allocations has decreased by 99.6 per cent in nominal terms and 99.6 per cent in real terms from R23.1 billion in 2015/16 to R90.0 million in 2016/17. This large decrease is due to the Special Appropriation of R23 billion received by the Department in aid of Eskom. Overall the Department's budget decreases by 98.8 per cent in real terms from R23.3 billion in 2015/16 to R274.0 million in 2016/17.

Compensation of employees amounts to 60.5 per cent of the total budget over the medium term, with goods and services amounting to 38.0 per cent over the medium term.

4. Committee Observations:

4.1 The Committee made the following observations:

4.1.1 the personnel budget of the department is too biased towards the administration rather than sector specific specialists required for oversight.

4.1.2 the process of introducing the Shareholder Management Bill has been too slow, and nothing has been brought to Parliament since the tabling of the Presidential Review Committee (PRC) recommendations.

4.1.3 SOCs have not done enough to create black industrialists and local industries, furthermore there is a need for a more radical approach to advance localization and beneficiation.

4.1.4 SOCs are excluded from incentives provided to the private sector for job creation and do not receive any assistance from development finance institutions.

4.1.5 the absence of remuneration standards for SOCs exacerbates the inequalities and inconsistencies in parastatals as a whole.

4.1.6 the non-issuing of shareholder compacts to the Committee have an adverse impact on the oversight work of the Committee.

4.1.7 the vacancies in the executive positions of SOCs need to be filled expeditiously as they have an impact on the stability of the companies.

4.1.8 the corporate social investment programmes of SOCs have not yet adequately reached out to rural and poor communities.

4.1.9 the high level of policy uncertainty created by the non-implementation of the Presidential Review Committee recommendations jeopardises the future of the Department of Public Enterprises.

4.1.10 the department is still too dependent on the use of consultants, and expenditure will be increasing over the medium term.

4.1.11 there is a lack of progress in the implementation of the recommendations of the Presidential Review Committee on SOCs.

4.1.12 there is a lack of public communication strategies by the SOC to inform the country of the work they are doing to assist the South African economy.

5. Recommendations

The Committee recommended that the Minister of Public Enterprises should ensure that the Department of Public Enterprises:

5.1 implements all the recommendations of the Presidential Review Committee that are relevant to the Department of Public Enterprises, in particular the remuneration standards of SOCs.

5.2 considers fast-tracking the shareholder management bill to empower the Department to execute its shareholder management responsibility and oversight over SOCs.

5.3 considers introducing a comprehensive plan to expand the corporate social investments of SOCs to rural parts of the country.

5.4 develops a communication strategy for all SOCs, in order to promote the companies, educate and inform the public and rural communities about the work of SOCs and opportunities that they offer.

5.5 considers reallocating part of the budget allocated for the programme administration to the sector oversight programmes, specifically regarding compensation of employees.

5.6 fills all vacancies in executive positions of SOCs and within the Department of Public Enterprises within an agreed timeframe.

5.7 reduces the use of consultants and invests in building internal capacity through incentivizing scarce and critical skills and investing in a skills development programme to ensure that the department is properly resourced.

5.8 makes the shareholder compacts available to the Committee to enable the Committee to effectively execute its oversight responsibility over SOCs.

5.9 engages the National Treasury and the Department of Trade and Industry with regard to SOCs accessing the incentives provided to the manufacturing sector and developmental finance institutions.

6. Conclusion

Having considered the budget vote and the strategic plan of the Department of Public Enterprises, the Committee recommends that the House passes the budget.

Report to be considered.