

Briefing of the Standing Committee on Appropriations

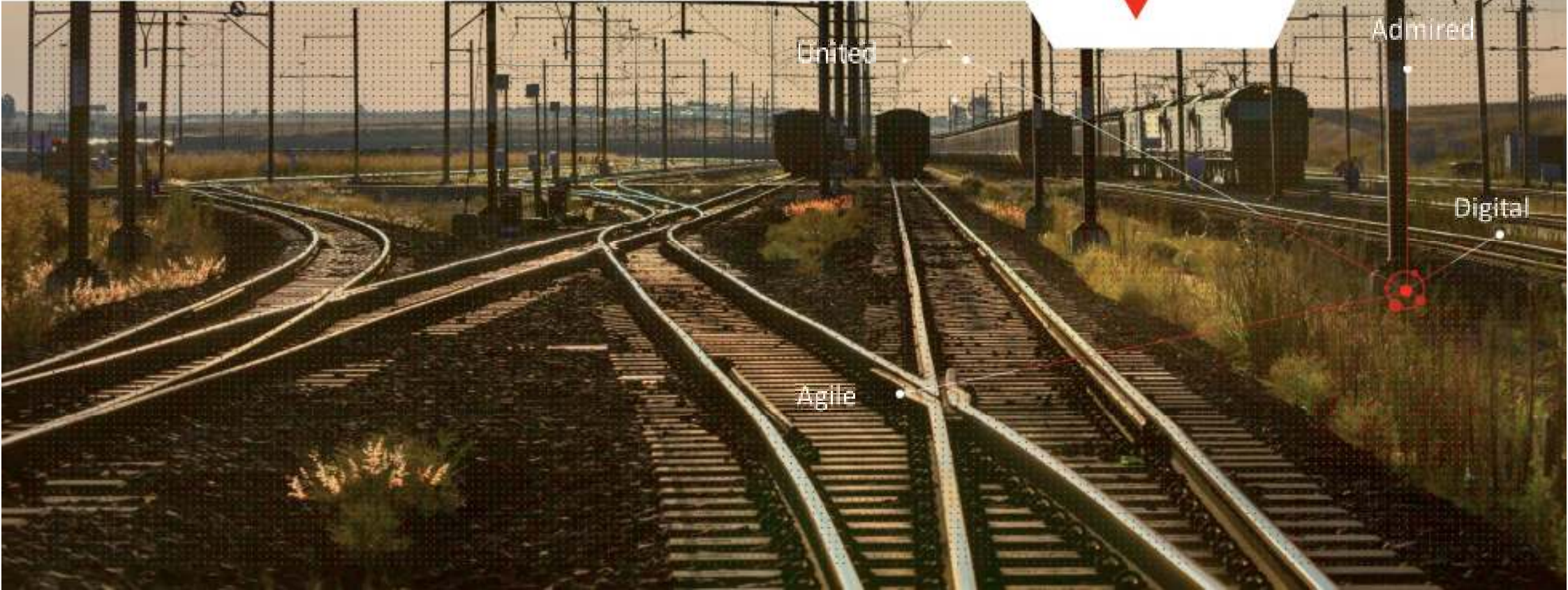


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Executive Summary: 2016/17



Transnet's continued strong financial performance means that the company does not rely on government funding, and has not received government guarantees since 1998. Transnet is able to borrow on the strength of its own balance sheet, with a stand-alone credit rating of bbb.

- ✓ Revenue excluding claw back increased by 6,7% to R66,4 billion
- ✓ Operating expenses were contained at a 5,6% increase to R37,9 billion, a R1,4 billion saving in planned costs
- ✓ Gearing at 44,4% and cash interest cover at 2,9 times, are significantly within loan covenant requirements
- ✓ Cash generated from operations after working capital changes increased by 16,4% to R32,8 billion
- ✓ Capital investment of R21,4 billion brought expenditure during the MDS period to R145 billion
- ✓ EBITDA increased by 5,0% to R27,6 billion, 7,1 times SA's GDP growth of 0,7%* for the financial year
- ✓ Continued focus on operational improvements resulted in the Group operational efficiency increasing by 14,9%. Energy efficiency increased by 1,2% with new electric locomotives regenerating 242 788MWh
- ✓ B-BBEE spend amounted to R37,0 billion – or 103,1% of total measured procurement spend, per the DTI codes
- ✓ The Company spent 3,1% of its personnel costs on training, focusing on artisans, engineers and engineering technicians
- ✓ The Company recorded a Disabling Injury Frequency Rate (DIFR) of 0,69 – bettering the target of 0,75 and the global benchmark of 1
- ✓ R234 million was invested in sustainable community development programmes across South Africa with 438 807 individuals from rural and needy communities, benefitting from the Phelophepa health care trains outreach programmes



Auditor General Outcomes - PFMA and Pre-determined Objectives: 2016/17

Focus area	Detail considered	Transnet's Responses
Independence and conflict of interest	<ul style="list-style-type: none"> • Did all Board members declare interests? • Companies Act section 76 (2)(a) and (b). • Board acted in the best interest of the entity. 	<ul style="list-style-type: none"> • For the period relating to 31 March 2017, Transnet reported PFMA violations totaling R239.7 million (2016: R250.4 million). • A detailed improvement plan for Internal Controls has been put in place and the progress is monitored and reported at various governance forums, including the Board of Directors.
Duties of the Board	<ul style="list-style-type: none"> • Systems and processes in place for controls over financial and risk management. • Adequate procurement processes in place. • Prevented losses, irregular and fruitless expenditure. • Safeguarding of assets. 	<ul style="list-style-type: none"> • Detailed root causes for all PFMA violations have been identified and the actions in the Internal Control Improvement Plan address this. • Consequence Management Processes have been firmed up by Human Resources. • PFMA Forums are hard at work to operationalize the PFMA Compliance Control Plan.
Material findings on the audit of compliance with laws and regulations	<ul style="list-style-type: none"> • Relates to Irregular expenditure. See above 	<ul style="list-style-type: none"> • Compulsory refresher training to all end-users and Supply Chain Management has been implemented. • Monthly reporting and immediate escalation of exceptions for corrective action is in place. • A plan to improve the Delegation of Authority controls i.e. automate the approval process, is in progress.

Auditor General Outcomes - PFMA and Pre-determined Objectives: 2016/17



Focus area	Detail considered	Transnet's Responses
<p><i>Annexure B</i> Insufficient appropriate audit evidence for the reported achievement of the targets of 9 capital projects.</p>	<ul style="list-style-type: none"> • Transnet implemented an automated system called Primavera to calculate the stage of completion of the capital projects. The system was not fully operationalized which led business to manually calculate the achievements. • There were no standardized controls across the Excel spreadsheets 	<ul style="list-style-type: none"> • There is an action plan to fully operationalize Primavera to ensure the outstanding elements are fully functioning by 31 December 2017. • Detailed documented procedures are being finalised to ensure standardization of information across operating divisions covering manual processes on Excel .
<p><i>Annexure D</i> Insufficient appropriate audit evidence for the reported achievement of Supplier Development (SD) targets.</p>	<ul style="list-style-type: none"> • Not all Supplier Development supporting documentation was obtained in order to verify initiatives put in place by suppliers. • This is mainly due to capacity constraints in the SD departs; only material contracts are being verified. 	<ul style="list-style-type: none"> • A formal process to internally verify all Supplier Development commitments is in progress.

Strategic Risks



Each of the Strategic Risks below is allocated to a Group Leadership Team member, to manage and mitigate. Key control strategies are developed and actioned, and progress is monitored and reported at various governance forums, including the Board of Directors:

- ✓ Competitive environment of freight service in commodities:
 - Road-to-Rail strategy, including take or pay contracting and tariff negotiations
- ✓ Inefficiencies in the value chain leading to lower volumes and financial instability:
 - implementation and utilisation of operational and improvement systems in Operating Divisions
- ✓ Deterioration in macro-economic environment due to global economic slowdown and slow recovery leading to capital projects becoming non-viable:
 - Flexibility to adjust Corporate Plan and investment strategy to operations
- ✓ Changes in the regulatory environment (i.e. economic, technical and compliance) – spending on Capex based on assumptions that may be negatively impacted by subsequent changes in regulation:
 - Regular engagement with NERSA; DoT; DPE; Cabinet to ensure alignment between strategies
- ✓ Not realising the benefits from the capital investments
 - Continuous portfolio update and monitoring on a quarterly basis to assess impact of changes in macro-economic factors

- ✓ Inability to attract and sustain additional volumes as new capacity is created and to protect current volumes against new entrants, customer activism:
 - Strategic customer engagement plans, including speed of new customer on boarding, with service consistency and proactive customer communication
- ✓ Misalignment between operational readiness and new assets
 - Operational readiness plans developed and monitored throughout project execution
- ✓ People management – inadequately skilled staff in operations, not skilled for future operations
 - Strategic workforce plan to determine long term and temporary skills requirements
- ✓ Sustainability risks - energy supply, water shortage and adverse weather patterns
 - Continuous identification of opportunities for the introduction of renewable energy sources
- ✓ Inadequate ICT infrastructure and technology to enable business and to deal with disruptive innovation:
 - Effective implementation plans (people, systems, processes) for the IT Strategy

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