

# Analysis of Water Boards

Presentation to Parliamentary Portfolio Committee on Water & Environmental Affairs

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**national treasury**

Department:  
National Treasury  
REPUBLIC OF SOUTH AFRICA

# Outline

1. Role of National Treasury
2. Key Focus Areas
3. Tariff Proposals and Comments
4. Financial Analysis
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6. Municipal Debt
7. Government Transfers
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# Role of National Treasury

- The role of National Treasury is prescribed through the **PFMA**<sup>1</sup> and **MFMA**<sup>2</sup>
- PFMA requires the following to be submitted to National Treasury
  - Annual Report *(for review)*
  - Corporate Business Plan *(for review)*
  - Requests to borrow *(for approval by Minister of Finance)*
- MFMA requires Water Boards to submit to National Treasury
  - Tariff proposals *(for comments)*
  - Monthly report on municipal debt payments *(for monitoring)*
  - Details of any dispute with municipalities regarding payments *(for monitoring and intervention where requested)*

<sup>1</sup> *Public Finance Management Act*

<sup>2</sup> *Municipal Finance Management Act*

# Key Focus Areas

## 1. Municipal Debt

- Four Water Boards owed between 90% and 150% of their total annual sales
- Botshelo; Bushbuckridge; Lepelle Northern; Sedibeng

## 2. Borrowings

- Water Boards who borrow from the financial markets to fund their capital projects
- Rand; Mhlathuze; Umgeni

## 3. Capital Plans

- Water Boards presently maintaining financial viability but unable to fund new capital requirements and refurbishments, thus their infrastructure is deteriorating.
- Amatola; Bloem; Magalies

## 4. Structure and Sustainability

- Uncertainty for the future given their small size: Overberg and Pelladrift

# Proposed 2012/13 Bulk Potable Water Tariffs

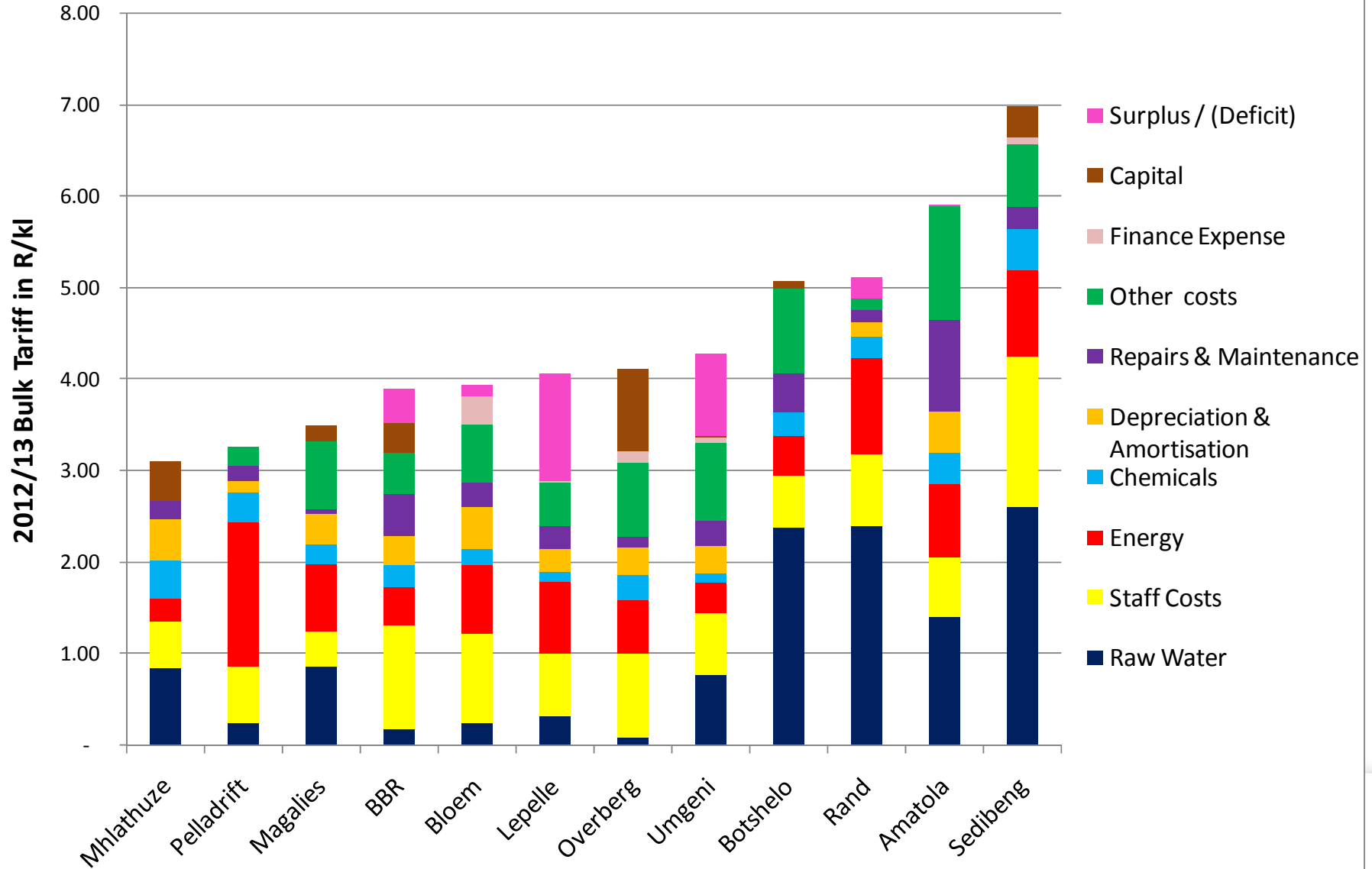
	Proposed Tariff in 2012/13 R/kl	% increase
Amatola	5.90	10.1%
Bloem	3.94	12.6%
Botshelo	5.07	13.2%
Bushbuckridge	3.90	5.4%
Lepelle Northern	4.06	8.9%
Magalies	3.49	8.9%
Mhlathuze	3.10	9.5%
Overberg	4.11	9.6%
Pelladrift	3.12	20.0%
Rand	5.11	13.6%
Sedibeng	6.90	8.5%
Umgeni	4.24	16.6%

The following are noted:

- Umgeni Water raw water costs increased sharply and now include the Capital Unit Charge for the Spring Grove Dam
- The highest increase is Pelladrift as the water board has an agreement with the Khai-Ma municipality to increase the tariff by 20% annually to bring the tariff in line with costs.
- Lowest increase in Bushbuckridge however Bushbuckridge Local Municipality, is currently paying a fixed monthly amount due to the absence of water meters and illegal connections.
- 4 year trend in increases:

	2009/10	2010/11	2011/12	2012/13
<b>Average % Increase</b>	8%	12%	10%	11%

# Tariff breakdown



# Tariff Comments: Debt Repayment

- *These are water boards which are currently undertaking major capital expenditure financed through borrowings*
- *Analysis considered the impact of the proposed tariff on their capital structure and ability to raise and repay debt*

<b>Water Board</b>	<b>Main Concerns</b>
Mhlathuze Water	No major concerns as the tariff covers costs and increase was reduced to below 10% at the municipalities request.
Rand Water	Decline in expenditure on maintenance. Financial surplus and increasing financial reserves despite growth in capital expenditure.
Umgeni Water	Increasing costs particularly raw water which are contributing to declining profits; Umgeni will also have to impair significant investments in rural infrastructure due to shortage of grant funding; Demand from its largest client is decreasing due to water conservation initiatives being implemented by eThekweni Metro.

# Tariff Comments: Future Sustainability

- *These are water boards whose reserves are insufficient for capital requirements*
- *Presently maintaining financial viability but unable to fund new capital requirements and refurbishments, thus their infrastructure is deteriorating*

<b>Water Board</b>	<b>Main Concerns</b>
Magalies Water	Insufficient financial information provided which leads to suspicion of inadequate financial planning. Key concerns around low budget for repairs and maintenance and inability to fund capital plan.
Amatola Water	Proposed a step tariff for Buffalo City which is not allowed. Deteriorating financial position due to increasing costs, particularly labour, and low returns on secondary activities.
Bloem Water	Final decision and contract with Mangaung LM outstanding. The proposed tariff covers operational costs but not total finance costs and capital requirements however Bloem has committed to using financial reserves to fund the shortfall.
<b>Water Board</b>	<b>Main Concerns</b>
Overberg Water	Long term sustainability of the Water Board due to insufficient funding for major capital infrastructure requirements.
Pelladrift Water	Uncertainty on the future of the Water Board due to possible closure of the Black Mountain Mine



# Tariff Comments: Municipal Debt

- *Outstanding debt issues 'outweigh' the tariff process*
- *Issues relate to placement of meters, tariff calculation disputes , WSA powers and functions, etc.*

<b>Water Board</b>	<b>Main Concerns</b>
Botshelo Water	Debt owed by municipalities particularly Ditsobotla and Ngaka Modiri Molema LMs. DWA had not responded to Botshelo's queries on the raw water charge at the time of Botshelo's consultations. Municipalities did not attend consultation. Transfer of water infrastructure assets to Botshelo still unclear.
Bushbuckridge Water	Debt owed by municipalities , outstanding service level agreements and uncertainty regarding short term financial viability
Lepelle Water	Debt owed by municipalities, declining capital budgets coupled with increasing accumulated surpluses.
Sedibeng Water	Debt owed by municipalities particularly Matjabeng and Nala LM. Increasing chemical costs.

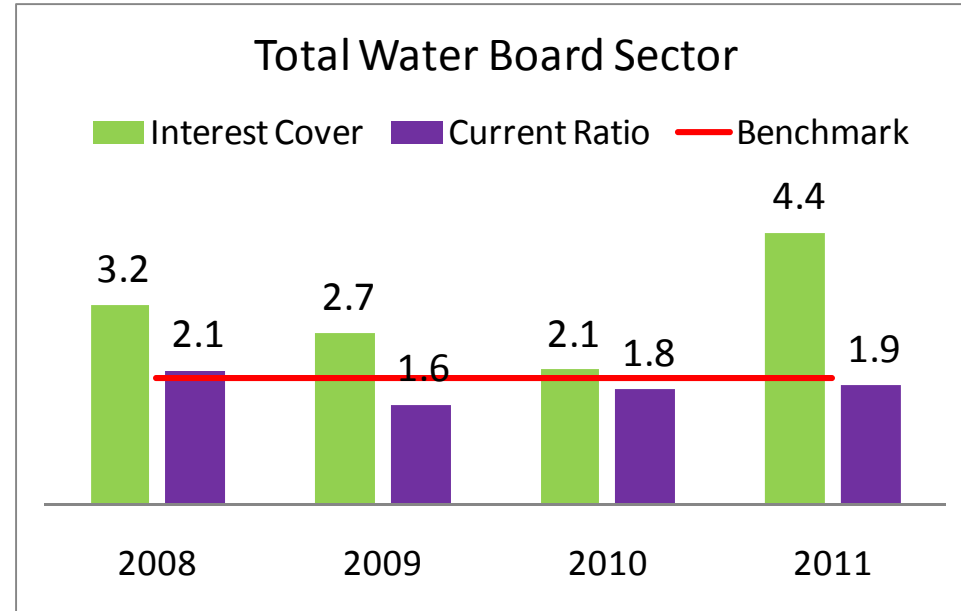
# Financial Analysis (1)

2011	Net Profit/ (Loss)	Net Profit Margin*	Return on Operating Assets**	Annual growth in Total Income	Annual growth in Total Costs
Unit:	R'000	%	%	% (y-o-y)	% (y-o-y)
Amatola	-15,506	-10%	-5%	15%	13%
Bloem	43,803	18%	8%	16%	-7%
Botshelo	<i>Information Outstanding</i>				
Bushbuckridge	-12,332	-14%	-10%	22%	49%
Lepelle Northern	42,462	15%	6%	11%	-5%
Magalies	27,966	12%	1%	21%	4%
Mhlathuze	67,061	26%	11%	16%	-3%
Overberg	4,012	15%	10%	21%	10%
Pelladrift	1,639	12%	3%	9%	15%
Rand	536,473	9%	7%	17%	14%
Sedibeng	25,538	6%	2%	15%	21%
Umgeni	428,441	29%	14%	-3%	5%
<b>Total</b>	<b>1,149,557</b>	<b>13%</b>	<b>7%</b>	<b>12%</b>	<b>10%</b>
<b>Median</b>	<b>27,966</b>	<b>12%</b>	<b>6%</b>	<b>16%</b>	<b>10%</b>
<b>Average</b>	<b>104,505</b>	<b>11%</b>	<b>4%</b>	<b>15%</b>	<b>11%</b>
<i>Notes:</i>					
* <i>Net Profit Margin: The profit made for every Rand of water sold</i>					
** <i>ROA: The profit made for every Rand of assets owned</i>					

- Profitability and Efficiency Indicators: The top 2 indicators are highlighted in blue and the lowest two indicators in yellow

# Financial Analysis (2)

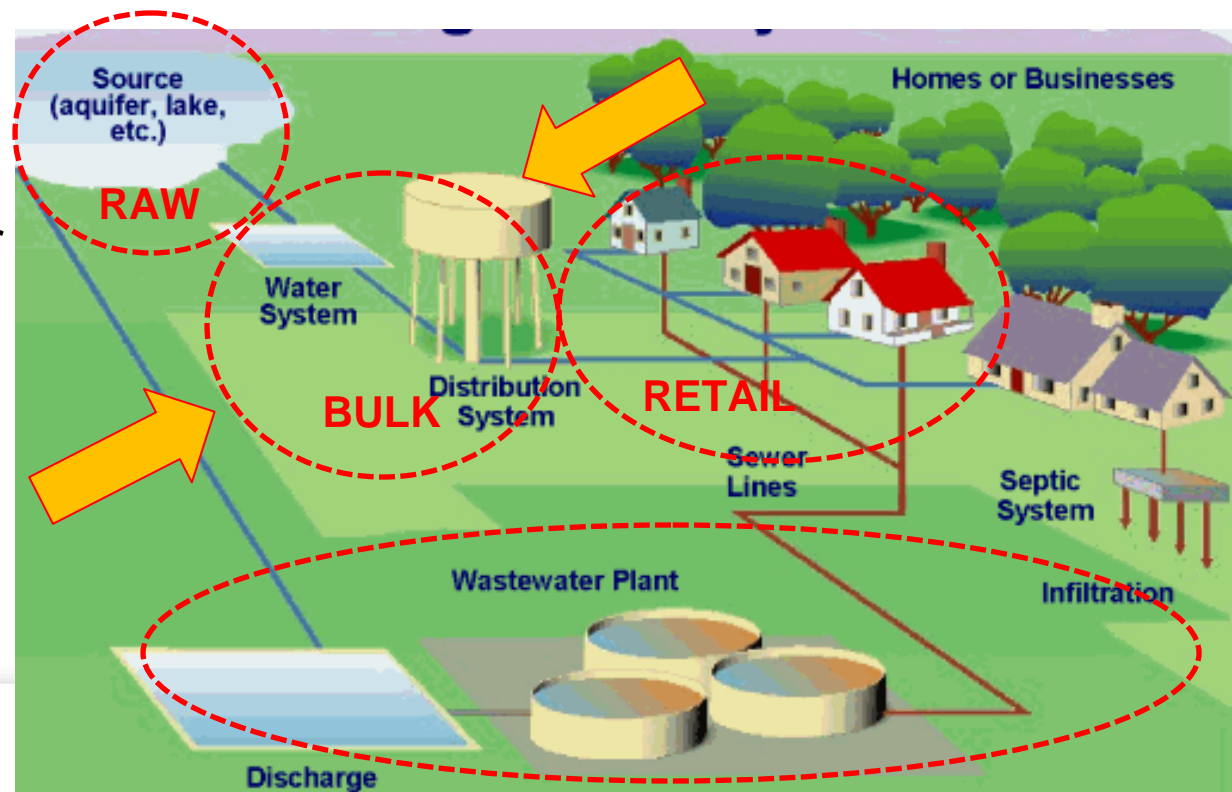
- Generally, Water Boards are able to repay their interest obligations as indicated by the increase in Interest Cover ratio.
- However, the low Current Ratio indicates potential cash flow constraints.
- Because the benefits of infrastructure investments can usually be derived over a long period of time, infrastructure investments should be financed primarily through debt, rather than current expenditure.
- This promotes inter-generational equity as the initial cost of the infrastructure asset is gradually paid off over its lifetime.
- Water Boards can only access debt financing if they are financially sound.



- **Interest cover:** The ability to pay interest obligations from operating profits. (operating profit/ finance expense)
- **Current ratio:** The number of times current assets can 'cover' current liabilities. (current assets/ current liabilities)

# Operational Analysis: SWOT

- Strengths: High quality of water
- Weakness: Deteriorating and ageing Infrastructure
- Water Boards operate in the 'middle' of the water value chain which makes them subject to external threats and opportunities
- Opportunities:  
Business growth and expansion
- Threats: Poor raw water quality and availability.  
Poor contractual agreements with municipalities



# Municipal Debt (1)

- NT and PTs and other stakeholders will continue to facilitate engagements between the Water Boards and relevant municipalities to assist parties in the solution of financial dispute and arrears.
- To prevent ongoing disputes, National Treasury has made the following recommendations to DWA:
  - Clarifying the roles and the responsibility of the Water Boards, governance and oversight over and by the Board, performance of its CEO and CFO to address customer, client issues with a view to implementing policies as articulated in legislation and as addressed by oversight authorities.
  - The performance contracts of the CEO's of Water Boards be reviewed on an annual basis to address gaps and weaknesses in their operations, such as implementation of measure for the timely collection of arrears and resolution of disputes, proper administration over the credit control policies and actions taken thereafter.

# Municipal Debt (2)

- To prevent ongoing disputes and long arrears, National Treasury has made the following recommendations to DWA:
  - DWA to prioritise assistance to those Water Boards and Municipalities so they have in place appropriate and adequate signed contracts (service level agreements).
  - These must be effectively monitored and implemented consistent with the legal framework.
  - Contract management should be strengthened and monitored from an implementation perspective.
  - Provide processes for dealing expeditiously and within strict timelines for all contractual issues, such as fixing of technical faults, correct placement of bulk and other meters and regular reading, jointly of such meters, by the Water Board and Municipalities, etc.

# Equitable Share Transfers to Local Government

- The LGES allocates subsidies for water and sanitation to poor households (using 2001 Census data).
- For water the subsidies are R138.88 per serviced household and R62.50 per unserved household, and a further sanitation subsidy of R138.88 per serviced household and R62.50 per unserved household is provided
- In the 2012 MTEF R960 million has been added to the LGES formula in 2013/14 and 2014/15 to alleviate the cost of anticipated above inflation increases in basic services costs. (Cost increases in 2012/13 were funded through previous additions to the LGES.)
- The local government equitable share formula is being reviewed during 2012 and a new formula (using 2011 Census data and more realistic cost estimates) should be phased in from 2013/14. All municipalities and stakeholders will be consulted during the review process.

<b>Local government equitable share allocations for water and sanitation, 2010/11-2014/15</b>				
<b>R millions</b>	<b>2011/12</b>	<b>2012/13</b>	<b>2013/14</b>	<b>2014/15</b>
<b>Equitable share: total allocation</b>	<b>30,224</b>	<b>33,483</b>	<b>35,879</b>	<b>38,538</b>
<i>% increase</i>		<i>10.8%</i>	<i>7.2%</i>	<i>7.4%</i>
<b>Water</b>	<b>6,494</b>	<b>7,201</b>	<b>7,717</b>	<b>8,297</b>
<i>% increase</i>		<i>10.9%</i>	<i>7.2%</i>	<i>7.5%</i>
<b>Sanitation</b>	<b>5,593</b>	<b>6,204</b>	<b>6,648</b>	<b>7,149</b>
<i>% increase</i>		<i>10.9%</i>	<i>7.2%</i>	<i>7.5%</i>

# Conclusions

- Historical municipal debt in 4 Water Boards is hampering those Water Boards ability to be sustainable and grow their business.
- Debt resolution is primarily the responsibility of the Water Boards.
- Whilst the larger Water Boards are reporting healthy profitability, cash flows need to be monitored to ensure they can pay their creditors.
- Water Boards tariffs need to recover operations and maintenance costs to ensure assets are maintained and rehabilitated before it's too late.
- Financing for capital expansion is critical for those Water Boards who are operating 'on the margin'.
- The sector needs leadership from DWA on particularly the Pricing Strategy Review; the Institutional Realignment and Reform; and the Legislative Review.

Thank You