

AFRICA RISK CONSULTING

Country briefing – South Africa

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1 Summary

President Jacob Zuma (2009 -present) is under increasing pressure over Nkandla, his potential trial for corruption, a rogue director of public prosecutions, and challenges to the independence of the Hawks in the constitutional court. Contradictory testimonies at the Marikana enquiry and Pallo Jordan's resignation over falsified qualifications spell trouble for the ruling African National Congress (ANC). The corporate governance index shows that South African companies' corporate governance has weakened from 2013 to 2014. The government announces that it will be taking control of the broad-based black economic empowerment vetting process, raising concerns over the independence of the procurement process. The South African Reserve Bank (SARB) bails out the country's largest unsecured loan lender, leading to market concerns over the economic stability of South African banks. The South African economy is still fragile, narrowly avoiding a recession in Q2 of 2014. South Africa imposes travel restrictions to and from Guinea, Liberia and Sierra Leone over the Ebola outbreak, and many companies cease all travel to the area.

1.1 Failures of accountability plague Zuma and the ANC

August has been a bad month for President **Jacob Zuma** (2009-present) and the ruling majority **African National Congress (ANC)** as both have come under fire for issues related to poor political governance. The **Marikana Commission of Inquiry** into the fatal shooting of 34 striking miners at **Lonmin Mines** in August 2012 has yet to produce results. Retired supreme court judge **Ian Farlam** chairs the commission which has been underway since the end of August 2012. It involves legal teams representing a wide range of parties and has taken a large number of statements from witnesses.¹ The enquiry appears no closer to establishing any form of responsibility for police officers' actions at the **Marikana (North West province)** massacre.

¹ Marikana Commission of Inquiry website

In August, key ANC figures gave evidence before the commission. Their testimony was either evasive or contradictory. Deputy-president **Cyril Ramaphosa**, a non-executive director of Lonmin at the time of the massacre, testified from 13-15 August that the entire nation should take collective responsibility for the multitude of failings leading up to the massacre.² Minister for women in the presidency **Susan Shabangu**, then minister for mineral resources, gave testimony that contradicted both Ramaphosa's testimony and her own, throwing both testimonies into doubt.³

The commission is highly publicised and highly political. All parties called to the stand have emphasised the same point: *"It isn't our fault."* Senior ANC figures talk about *"collectivising responsibility"* and jostle to avoid direct blame falling on the ANC and the mining companies, while conditions at the mines have yet to improve. After two years, and with no end in sight, the commission has not resulted in a single prosecution, let alone dismissal.

A lack of political accountability has been the hallmark of Zuma's presidency. Zuma has been dodging corruption charges since 2003. He has systematically misused organs of the state, and dissolved the **Scorpions** anti-corruption investigation unit in order to do so. The Scorpions were an independent investigations unit with a mandate to investigate corruption and organised crime. The constitution guaranteed their existence and independence.⁴ In 2005 they were investigating then deputy-president Jacob Zuma for corruption. The case was linked to the prosecution of Zuma's financial adviser **Schabir Shaik** for corrupt issuing of department of defence tenders. The **Durban High Court (KwaZulu-Natal Province)** sentenced Shaik to 15 years in prison for corruption in 2005.⁵ In an effort to prosecute Zuma, the Scorpions seized documents from his lawyers' offices. These included the so-called 'spy tape' recordings that local media report incriminate Zuma.⁶ Following this, Zuma and his ANC allies launched the **Khampepe Commission of Inquiry** into the Scorpions' constitutional legitimacy. The commission reported in 2006 that the Scorpions had stepped beyond their bounds but were not unconstitutional. In 2008, the ANC majority in the national assembly voted to dissolve the Scorpions unit and replace it with the **Hawks**, a comparable unit contained within the police force (see below).⁷ In 2009, **National Prosecution Authority (NPA)** acting head **Mokotedi Mpshe** announced the dropping of the corruption charges against Zuma, citing *"political interference and*

² Mail and Guardian, 15 Aug 2014

³ Business Day, 27 Aug 2014

⁴ Section 7(2)

⁵ ISS report, 'Countering corruption in South Africa: the rise and fall of the Scorpions and the Hawks'. Jun 2011

⁶ Mail and Guardian, 28 Aug 2014

⁷ ISS report, 'Countering corruption in South Africa: the rise and fall of the Scorpions and the Hawks'. Jun 2011

abuse of power” by key Scorpions figures. The **National Intelligence Agency (NIA)** had spied, on behalf of Zuma, on Scorpions advocate **Leonard McCarthy** to gather evidence of this.⁸

The government formed the Hawks unit, officially the **Directorate for Priority Crime Investigation (DCPI)** of the **South African Police Service (SAPS)**, in 2009. Businessman **Hugh Glenister** brought a court case that year against the government questioning the unit’s independence. In March 2011 the **Constitutional Court** ruled that the constitution required the maintenance of an independent unit to fight corruption and that the Hawks did not meet the requirement for independence. The government then moved the Hawks outside of the SAPS but still under police ministry control. Loyalist ministers appointed to the ‘security cluster’ of the police, justice and intelligence ministries have avoided demands for further independence. Zuma’s allies in the NPA have also blocked attempts by the main opposition **Democratic Alliance (DA)** party to re-open the prosecution into Zuma and to use the ‘spy tapes’.

“These are old problems that should have gone away by now, but Zuma’s ‘talk to my lawyer’ approach and disregard of allegations against him has helped keep these stories going ... he may now face some sort of reckoning.”⁹

Two recent developments show that the situation might be changing:

- The constitutional court on 19 August allowed two more cases to be heard challenging the law underpinning the Hawks. The **Helen Suzman Foundation** and Hugh Glenister both argue in their cases that the unit is still not sufficiently independent.¹⁰
- The DA and Zuma’s lawyers signed an agreement on 27 August permitting the so-called ‘spy tapes’ to be used in court.¹¹ This means the case will go for a ruling before retired KwaZulu-Natal chief justice **Noel Hurt** that both parties have agreed will be final and binding.¹² The **Supreme Court of Appeal** rejected a last minute application from Zuma’s legal team to overturn this on 28 August.¹³ This means that Zuma could finally appear in court on the corruption charges.

A culture of no accountability and political interference with the organs of the state is endemic across government:

⁸ ISS report, ‘Countering corruption in South Africa: the rise and fall of the Scorpions and the Hawks’. Jun 2011

⁹ Source, journalist, Johannesburg

¹⁰ SABC, 19 Aug 2014

¹¹ Business Day, 15 Aug 2014

¹² Mail and Guardian, 27 Aug 2014

¹³ Mail and Guardian, 28 Aug 2014

- The **Special Investigations Unit (SIU)** released its report on the **Nkandla** scandal on 11 August. In an attack on a close Zuma ally, the report holds Zuma's personal architect **Minenhle Makhanya** wholly responsible for R155m (\$14.5m) of non-security spending.¹⁴ The president delivered his response to public protector **Thuli Madonsela's** March report (see *ARC South Africa April 2014 Briefing*) to parliament on 14 August. Zuma said that police minister **Nathi Nhleko** – another Zuma loyalist – should determine how much of the R246m (\$23m) he should pay back.¹⁵ Parliament has set up an ad hoc committee to consider Zuma's response but Zuma's allies have filled the seats and are likely to support his position.¹⁶ Madonsela has since hinted that the matter could go to the courts if parliament's response is unsatisfactory.¹⁷
- The government is trying to force **Director of Public Prosecutions (DPP) Mxolisi Nxasana** to quit. Former justice minister **Jeff Radebe** tried to force him out in May claiming he had failed his security clearance. Zuma tried to remove him directly in July but Nxasana has achieved an indefinite suspension of this action in the courts. NPA employees believe Nxasana is being targeted for re-opening corruption investigations into **Richard Mdluli**, the former head of the **Police Crime Intelligence** unit.¹⁸
- The **Sunday Times (SA)** revealed on 30 July that ANC stalwart **Pallo Jordan** falsified academic qualifications on his CV, including a doctorate from the **London School of Economics**. Jordan is a noted public intellectual and former minister for culture under the government of president **Thabo Mbeki** (1999-2008). Jordan has stepped back from public life following the allegations. In communications with the paper he spoke of the "*faustian pact*" he had made in his political life.¹⁹ The news is a further embarrassment for the ANC.

The lack of accountability means that serious change as a result of these developments is unlikely. However it does increase pressure that Zuma's opponents within the ANC can leverage against him. Failure to contain the corruption charges against him has certainly weakened Zuma's position.

Concerns over the president's health have weakened his position even further. Zuma was committed to hospital from 8-11 June after the election for "*exhaustion*". He was too ill to walk down the red

¹⁴ Mail and Guardian, 15 Aug 2014

¹⁵ Business Day, 14 Aug 2014

¹⁶ Mail and Guardian, 25 Aug 2014

¹⁷ Times, 25 Aug 2014

¹⁸ Mail and Guardian, 25 Aug 2014

¹⁹ Times, 4 Aug 2014

carpet at the parliamentary inauguration ceremony on 17 June (he drove down),²⁰ and cancelled all of his corporate one-on-one meetings on the fringe of the August 4-6 **US-Africa Leaders Summit** in **Washington DC**.²¹ However, Zuma did make his meeting with **United States (US)** vice president **Joe Biden**. He took questions afterwards and denied that he was in ill health.²²

“While Zuma is likely to be able to avoid any punishment the political pressure could give his enemies in the ANC ammunition to pressure him to step down...however so far the party has kept a united front, at least in public.”²³

1.2 Corporate governance falls in 2014

Corporate governance has been an issue the South African corporate world has wrestled with for 20 years. In 1996 the **South African Institute of Directors (SAID)** commissioned **Mervyn King** to write a basic code of corporate governance, known as the **‘King Report’**. The framework is recognised as an international example of best practice in this field.²⁴ The SAID revised the code as **‘King II’** in 2002 and **‘King III’** in 2009 to keep up with changes to South Africa’s corporate legislation.²⁵

Despite having a robust code to guide them, South African companies have a high incidence of corporate governance failure and it is getting worse. The 2014 edition of the **Corporate Governance Index** produced by the **South African Association of Internal Auditors (SAAIA)** shows that corporate governance was less effective in 2014 than in 2013.²⁶ The index showed a decrease from a score of 3.2 in 2013 to 2.9 in 2014 (out of a possible 5). The index measures ethics, compliance, leadership, operational risk, internal audit, performance, and external risk.²⁷ Public sector organisations performed less well overall than private sector organisations. Only 21% of government organisations strongly agreed that ethics was a strong part of organisational culture. The weakest area of corporate governance was the preparedness of organisations for external risks. From 2013-2014 there was a decline in trust in organisational leadership to ensure good governance, from 3.2 to 3.0. Only 51% of organisations surveyed strongly agreed that they complied with all relevant legislation, regulations and standards.²⁸

²⁰ City Press, 17 Aug 2014

²¹ ANC source

²² City Press, 6 Aug 2014

²³ Source, journalist, Johannesburg

²⁴ Institute of International Finance, 6 May 2009

²⁵ South African IOD website, 2014

²⁶ IFLR, 27 Aug 2014

²⁷ Corporate Government Index 2014

²⁸ Corporate Government Index 2014

Despite high profile corporate governance failures, companies and individuals seldom receive more than a slap on the wrist. Public protector Thuli Madonsela has investigated two key organisations in 2014 for major corporate governance failures: the **South African Broadcasting Company** and the **Eastern Cape Gambling Board**. Neither has faced consequences.²⁹ South African banks have been handed R130m (\$12.2m) of fines in 2012-2014 for numerous compliance related failures, demonstrating the light punishments South African courts hand out for compliance breaches.³⁰

*“South African companies get a legal free pass in compliance enforcement....they might get R10m (\$940,000) for mishandling client information where they would get a \$50m fine and possible further charges in the USA or in **Europe**.”*³¹

1.3 Government to control vetting process in new BEE regulations

The new **Broad-Based Black Economic Empowerment (B-BBEE)** regulations are due to come into force in May 2015. The government announced it will take control of the BEE vetting process as part of this change. It will downgrade the current verification agencies to “empowerment partners”.³² The **Department for Trade and Industry (DTI)** will now oversee the process. The government claims that this will help spread wealth more equally and stop the private sector giving certificates to itself.³³

All applications for partnership between black South African and international companies wishing to do business in the country will now have to go through the DTI. Given that public institutions have worse corporate governance records than private ones (see above), local media are concerned about the potential for corruption.³⁴ Many in the ANC have built up significant fortunes through BEE ownership, notably members of Jacob Zuma’s family. While the DTI claims that it can ensure the creation of more black millionaires, sources say this development poses some serious questions about the procurement process.

*“When the government controls the BEE process for procurement for its own projects all external oversight disappears ... it would not surprise me to see more BEE contracts going to figures connected to the government.”*³⁵

²⁹ ‘When corporate governance and ethics fail’, Madonsela, T, 2014

³⁰ Business Day, 28 Aug 2014

³¹ Source, international compliance lawyer, London

³² Business Day, 15 Aug 2014

³³ Business Day, 15 Aug 2014

³⁴ Business Day, 15 Aug 2014

³⁵ Source, international compliance lawyer, London

The new regulations also place additional compliance burdens and regulations on all companies. Smaller companies with turnover of R10m (\$940,000) to R50m (\$4.6m) per year will now have to undertake complex compliance measures that may negatively impact them.

“These new regulations will hurt small and medium enterprises in South Africa more than they will help further the goals of BEE...the last thing companies need is more red tape.”³⁶

1.4 African Bank Investment bail-out leads to market fears

The **South African Reserve Bank (SARB)** has bailed out **African Bank Investments (Abil)**, South Africa’s largest provider of unsecured loans. The state intervened on 10 August after Abil announced a record R6.7 billion (\$629m) loss. The SARB split Abil into a ‘good’ bank and a ‘bad’ bank. South African banks **Barclay’s Africa (Absa)**, **Standard Bank** and **Nedbank** along with the state-owned **Public Investments Corporation (PIC)** have agreed to underwrite R10 billion (\$939m).³⁷ This will be used to re-capitalise the ‘good’ bank which has a total value of R26 billion (\$2.4 billion). The SARB will buy the bad bank which has a value of R17 billion (\$1.6 billion) for R7 billion (\$657m).³⁸

The bail-out has increased market uncertainty over South Africa’s operating environment. Ratings agency **Moody’s** downgraded Standard Bank, Absa, **FirstRand** and Nedbank by one notch each on 21 August. The agency said it reflected the lower likelihood of support from the state to protect creditors following the bail-out.³⁹ However **Standard & Poor’s** has said it has no plans to downgrade the banks, as they are on a stable footing.⁴⁰

“The Abil bail-out shows that the SARB is wary of any further shocks to the economy....many analysts think Moody’s move was unjustified and could have negative consequences in terms of market confidence.”⁴¹

The bail-out and its response were a low point in financial news this month. Finance minister **Nhlanhla Nene** announced on 26 August that the economy grew 0.6% of GDP in the second quarter in 2014, following a 0.6% contraction in the first quarter.⁴² However year-on-year growth could be as low as 1%, down from 1.9% in 2013, as the economy feels the effect of mining strikes and poor electricity supply.

³⁶ Source, business association, Cape Town

³⁷ FT, 10 Aug 2014

³⁸ Mail and Guardian, 15 Aug 2014

³⁹ FT, 19 Aug 2014

⁴⁰ Reuters, 21 Aug 2014

⁴¹ Source, financial analyst, Johannesburg

⁴² Mail and Guardian, 26 Aug 2014

“The economy is not out of the woods yet....the news of 0.6% is a success of crisis management by the finance ministry and the SARB rather than news of a serious recovery.”⁴³

1.5 South Africa restricts travel to and from Ebola countries

South Africa has restricted travel to and from the countries in **West Africa** worst affected by the **Ebola** outbreak. The government announced on 21 August that it would turn away all non-citizens arriving from the ‘high-risk’ countries of **Guinea, Liberia and Sierra Leone**. It would also seek to delay all South African citizens travelling to those countries and will screen all citizens returning from those countries for the virus.⁴⁴ The government said that it would give special permission to those working in the mining, commerce and medical industries. However, many South African corporates have halted all travel to the region over concerns for their employees’ safety.

“For the moment nobody is flying out to West Africa....we’re not the only company with this policy, nobody’s moving until the epidemic gets under control.”⁴⁵

South Africa is, for many companies, the gateway to Africa where they are headquartered when working across the continent. A freeze on travel, despite information technology advances making long-distance communication easier, will have a negative effect on pan-African trade if the Ebola outbreak continues.

2 Implications

There is a growing crisis of political and corporate governance in South Africa under Jacob Zuma’s leadership. Zuma may finally face a reckoning when the contents of the ‘spy tapes’ are revealed. Taking the stand in a corruption trial, especially after having evaded it for over a decade, would be humiliating for the president. However, given Zuma’s past record of getting off charges, the chance of his facing a conviction are slim. Ramaphosa’s testimony at the Marikana enquiry ‘collectivising’ responsibility shows that even reformers in the ANC seek to avoid taking the blame. This makes the prospect of a more responsible and accountable form of government in the future less likely. The culture of disregard for governance that the administration has perpetuated is writ large in the Marikana commission. Its failure to hold a single person accountable shows the extent of the governance and accountability shortfall across political parties, state institutions and in private enterprise. The only forces that have gained from this situation are **Julius Malema’s** vocal minority opposition party the **Economic Freedom Fighters (EFF)** and rogue unions such as the **Association of Mineworkers and Construction Union (AMCU)**. Neither of these groups is interested in effective

⁴³ Source, financial analyst, Johannesburg

⁴⁴ Gov.za, 21 Aug 2014

⁴⁵ Source, corporate employee, Johannesburg

governance – the EFF operates as Malema’s personality cult and union leadership is almost totally unaccountable.

Corporate governance failures continue to attract little punishment from either the mechanisms of the state or the courts. The institutions of state seem powerless to act against any form of wrongdoing in this sphere. The decision of the government to take control of the BEE vetting process is more an invitation to write themselves cheques than to make a more progressive redistributive policy. South Africa has the legal framework and the expertise to hold people and companies accountable. However, it sets a dangerous precedent when the president can ignore the rulings of the Constitutional Court. Zuma’s approach to issues of accountability shows his disregard for ethical governance, South Africa’s legal system, and a duty to the South African people. If he does stand trial then it could signal a change at the top that allows for a shift back to a culture of greater responsibility.

A lack of governance and accountability makes South Africa a less attractive country to invest in. The US-Africa leaders’ summit has drawn global attention to the continent and South Africa should be the natural base for companies operating in **sub-Saharan Africa**. If the government acts above the law and allows corrupt practices to go unchecked, business may look elsewhere. North Africa is increasingly looking south for business and stable countries such as **Morocco** have attractive tax breaks for companies.

As well as investment, South Africa needs companies, both private and state-owned, to exercise effective and responsible leadership to work with the finance ministry and central bank to get South Africa’s economy back on track. More centralised government control of BEE contracts and further compliance burdens will not help small and medium-sized businesses. External factors such as the Ebola crisis, ongoing infrastructure problems, and fluctuating market confidence also threaten to derail a fragile recovery.