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The battle for presidency has begun. The Congress of South African Trade Unions (Cosatu) national congress endorses Cyril Ramaphosa as Jacob Zuma's successor in African National Congress (ANC) presidency elections in 2017. Former president Kgalema Motlanthe (2007-2009) announces the Tripartite Alliance exists only in name. A Cosatu draft document outlines union intentions to pursue merger talks between the Federation of Unions of South Africa (Fedusa) and the National Council of Trade Unions (Nactu). The South African Communist Party (SACP) looks to increase its membership at a central committee meeting. South Africa's state-owned enterprises borrow money to expand infrastructure projects, despite receiving equity injections from government. Parliament reviews requested amendments to South African Airways (SAA)'s 2002 Airbus deal. The South African Reserve Bank (SARB) raises interest rates 25 basis points.

Cosatu's endorsement of Ramaphosa strengthens his position for 2017

The **Congress of South African Trade Unions (Cosatu)** national congress on 24-28 November has shifted the sands in the battle for the **African National Congress (ANC)** presidency elections in 2017. The **South African Democratic Teachers Union (SADTU)**, reportedly the most powerful faction within Cosatu, proposed that the unions back the progression of deputy president **Cyril Ramaphosa** to the position of ANC president in 2017.¹ The ANC president is, by precedent, the next ANC presidential candidate and is likely to succeed **Jacob Zuma** (2009-present) as president of South Africa in 2019. Cosatu has a history of backing specific candidates in ANC internal elections and its endorsement holds sway with the voting delegates. It supported Jacob Zuma rather than then president **Thabo Mbeki** (1999-2007) at the ANC congress in 2007.²

SADTU framed the proposal carefully, noting that it was "a matter of principle" that the deputy president succeeds the president at the ANC national congress.³ Cosatu's largest affiliates **National Education, Health and Allied Workers' Union (Nehawu)**, **Democratic Nursing Organisation of South Africa (Denosa)**, the **Southern African Clothing & Textile Workers' Union (Sactwu)** and the **South African Transport and Allied Workers Union (Satawu)** all supported the motion.⁴

Ramaphosa's long career in business appeared to set him against the interests of organised labour, although the endorsement represents a return to his political roots in the union he co-founded.⁵ Union sources said that ANC chairman **Gwede Mantashe** and the **South African Communist Party (SACP)** are the major powers "pulling strings" to get the congress to back Ramaphosa.⁶ This sets Cosatu against **Nkosazana Dlamini-Zuma**, who is reported to be Zuma's preferred candidate for the ANC presidency, and against the president himself.⁷ This is a surprising turn of events as Cosatu president **Sdudo Dlamini** was close to Zuma. It also sets Cosatu against the premier league, comprised of the premiers of **Free State, Mpumalanga** and **North West Provinces**, and the newly

¹ Business Day, 25 Nov 2015

² Mail & Guardian, 28 Oct 2007

³ Eyewitness News, 25 Nov 2015

⁴ Eyewitness News, 25 Nov 2015

⁵ Source, political analyst, Cape Town

⁶ Source, Cosatu affiliated union, Port Elizabeth

⁷ Source, union members, Johannesburg

elected chair of the **Kwazulu Natal (KZN) ANC, Sihle Zikalala**, who are likely to support Dlamini-Zuma. The KZN ANC election of Zikalala on 7 November has isolated KZN premier **Sencho Mzunu** who is reportedly a supporter of Ramaphosa and an opponent of Zuma.⁸ However, the election was close and the province remains split in its support for the chair and premier.⁹

The congress made several further attacks on Zuma. It named media company **ANN7** as South Africa's worst employer, a direct assault on the **Gupta** family, one of Zuma's key allies and his main financial backer that one source has described as "*a branch of the ANC in their own right*".¹⁰ The SACP also attacked the current administration. Secretary general and higher education minister **Blade Nzimande** condemned the "*parasitic bourgeoisie*" attempting to oust communist leaders from the ANC during his speech to the congress.¹¹ Nzimande also announced that the party intends to increase its membership, currently 243,000 people, with members of Cosatu, following the SACP central committee meeting also on 24 November.¹²

The events at the national congress clearly show the cracks in the ruling tripartite, or revolutionary, alliance. Cosatu and the SACP, led by Mantashe, are backing Ramaphosa to continue their influence. Zuma and his powerful provincial allies are on the back foot. The alliance itself has come under further pressure in November. Former president **Kgalema Motlanthe** (2007-2009), in an interview with **Business Day** newspaper, announced that the alliance existed only in name. He also accused the ANC of ignoring policy and the constitution.¹³ Motlanthe and Cosatu appear to agree that the ANC's internal democracy is impaired, making the alliance redundant. According to one source, "*there is no alliance, there is one organisation [the ANC]*".¹⁴

Divisions in the union movement also threaten the tripartite alliance and the impact of Cosatu's backing of Ramaphosa. Cosatu's power has waned since it expelled the **National Union of Metalworkers of South Africa (Numsa)**, then its largest affiliate, in October 2014.¹⁵ Numsa and former Cosatu president **Zwelinzima Vavi** are attempting to form a rival labour congress that may further split the political influence of the labour movement and attract members away from Cosatu (see *ARC Briefing South Africa October 2015*). However, a draft organisational report released before the Cosatu congress revealed its intention to pursue merger talks with the **Federation of Unions of South Africa (Fedusa)** and the **National Council of Trade Unions (Nactu)**.¹⁶ Nactu president **Joseph Maqhekeni** announced that Numsa has been in discussions with Nactu, but that talks with Cosatu would also be an option. Fedusa general secretary **Dennis George** highlighted the importance of the identity of the federation and noted that "unions and federations should steer clear of politics".¹⁷ Numsa and Vavi are also pursuing talks with Nactu and Fedusa, showing Numsa's intentions to bolster its membership and funding, which will directly clash with Cosatu's agenda to win the same support.¹⁸

SOE's borrow to fund operations while governance issues remain

South Africa's state-owned enterprises (SOEs) are borrowing money internationally to prop up their operations. However, poor management and inefficiency have impacted their credit ratings and therefore their access to international credit.

⁸ Times, 8 Nov 2015.

⁹ Times, 8 Nov 2015.

¹⁰ Source, with ties to NUMSA, Johannesburg; MoneyWeb, 24 Nov 2015

¹¹ Mail & Guardian, 25 Nov 2015

¹² Business Day, 24 Nov 2015

¹³ Business Day, 1 Nov 2015

¹⁴ Motlanthe in Business Day, 1 Nov 2015.

¹⁵ See *ARC Briefing South Africa September 2015*

¹⁶ Business Day, 24 Nov 2015

¹⁷ Business Day, 6 Nov 2015

¹⁸ See *ARC Briefing South Africa September 2015*

National electricity utility **Eskom** has secured \$160.8m in debt financing from the **Agence France de Développement (AFD)** (French development agency) in addition to requesting a 16.6% tariff increase from the **National Energy Regulator of South Africa (Nersa)** to “*retrospectively meet costs*”.¹⁹ Eskom is battling a \$1.6 billion shortfall in the 2013/2014 financial year and is struggling to meet costs despite a series of government bail-outs across 2015. The government has injected \$714m into Eskom so far in 2015 and will inject a further \$928m in January 2016. It is trying both to raise debt capital and to increase revenues but will struggle with both. The AFD finance will help to fund distribution upgrades in Kwazulu Natal (KZN), **Limpopo** and the **Eastern Cape** provinces where Eskom has a long-standing electrification backlog. However, the new distribution grids will incur costs to maintain and will place further strain on South Africa’s electricity supply. This lies behind the tariff increase request. In May Nersa granted a 12.7% tariff increase after Eskom applied for a 25% increase in order to reclaim the \$1.6 billion shortfall in the 2013-2014 financial year (see *ARC Briefing South Africa June 2015*).²⁰

Eskom’s funding problems have worsened, since **Standard & Poor’s** downgraded Eskom’s long-term credit ratings to ‘junk’ (BBB) in March.²¹ This has limited Eskom’s borrowing options. CEO **Brian Molefe** has previously stated that Eskom may turn to capital markets to correct their deficit.²² More recently chief financial officer **Anoj Singh** announced that alternative funding options are to be explored before the international bond market.²³ Ultimately, one senior investment source believes that “*government support for Eskom will become irrelevant*”²⁴ forcing partial privatisation, due to increasing expectations, and continued poor performance. Eskom does not anticipate further load shedding until April 2016 due to low summer demand. This is an improvement from the summer of 2014/2015 when load shedding continued. However, Eskom remains unable to supply South Africa during peak demand in winter and load shedding will return.

SOEs also continue to make headlines due to poor governance. An **Ernst & Young** investigation into the **South African Airways (SAA) Airbus** deal reveals “*major irregularities including poor procurement practices*”.²⁵ The treasury is still reviewing proposed changes to the 2002 Airbus deal, to acquire newer technology.²⁶ Ten aircraft from the original order of 40 remain undelivered.²⁷ **Quartile Capital** has denied involvement in the \$427.6m Airbus deal restructure following a request from SAA chair **Dudu Myeni** to waive tender applications in their favour.²⁸

SAA has attempted to silence criticism by serving Business Day with a High Court order to remove an article containing a private memo to Myeni and details of the Ernst & Young report after initial circulation.²⁹ A parliamentary presentation on 18 November by SAA’s audit committee admitted that \$1.76 billion spent on services had not generated value for money.³⁰ Eskom’s lack of stable leadership continues as SAA pilots at a special general meeting on 16 November, voted ‘no confidence’ in the chair and non-executive directors, illustrating high levels of employee dissatisfaction.³¹

Myeni appointed **Musa Zwane** as acting CEO of SAA on 18 November. He is the company’s seventh CEO since 2011. He was previously head of the maintenance unit and replaces **Thuli Mpshe**, the former head of human resources, who held the acting CEO position for four months from August this

¹⁹ Business Day, 24 Nov 2015

²⁰ MoneyWeb, 18 Jun 2015

²¹ Business Day, 19 Mar 2015

²² Bloomberg, 26 Nov 2015

²³ Bloomberg, 26 Nov 2015

²⁴ Source, senior investment partner, Johannesburg

²⁵ Business Day, 19 Nov 2015

²⁶ Business Day, 25 Nov 2015

²⁷ Business Day, 25 Nov 2015

²⁸ Business Day, 24 Nov 2015

²⁹ Business Day, 24 Nov 2015

³⁰ Business Day, 20 Nov 2015

³¹ Times, 16 Nov 2015

year. Myeni has succeeded in driving off many of SAA's longstanding executives. **Wolf Meyer** has also resigned from his position as chief financial officer (CFO), stating that

*"I resigned because I could no longer associate myself with the conduct of the board and the direction the board was steering the company in."*³²

Some SOEs are managing to fund infrastructure expansion projects. State-owned transport company **Transnet** has signed \$853m in debt deals with five separate lenders, the **Bank of China**, and South Africa-based **Nedbank Group, Absa, Futuregrowth Asset Management, and London Stock Exchange (LSE)-listed Old Mutual Plc.**³³ The deal will fund state-owned ports, and the acquisition of 1,000 rail locomotives from **United States (US)-based General Electric and Canada-based Bombardier.**³⁴ The focus on state-owned ports and infrastructure goes some way to address concerns about South Africa's competitiveness within Southern Africa. However, under union pressure it is unlikely that Transnet will automate any ports, opting instead to offer more employment.

*"South Africa is building its own competition [automated ports] in neighbouring countries [Mozambique], whilst resisting the pressures to automate and streamline its own ports."*³⁵

Wasteful public expenditure is not limited to SOEs. Auditor general **Kimi Makwetu** announced that irregular expenditure totals \$1.8 billion in a report on national and provincial departments and public entities.³⁶ Mpumalanga, **South African National Roads Agency** and **Gauteng Province** human settlements department are named as the largest irregular spenders, with non-competitive or unfair procurement practices contributing to the total. It was noted that *"expenditure does not necessarily mean that money was wasted or fraudulent"*.³⁷

Reserve Bank continues slow interest rate increase

The **South African Reserve Bank (SARB)** increased interest rates on 19 November by 25 basis points to 6.25% that takes the prime commercial lending rate to 9.75%.³⁸ The increase came partly in response to increased currency pressure following a 19% decline in 2015. The move stabilised the rand briefly, registering a 2.8% increase from 19 to 23 November, but the currency still fell 1.74% across the month, reaching 14.28 rand to the dollar on 26 November.³⁹

The SARB increased interest rates in July in order to avoid large increases in inflation (see *ARC Briefing South Africa July 2015*). These have already affected spending. Retail revenue growth has fallen across 2015, despite being up year-on-year in June at 3.2%.⁴⁰ Analysts are concerned that the further increase will begin to hit highly leveraged consumers – primarily in the urban middle classes – who are already facing increases in the cost of living in 2016.⁴¹

SARB governor **Lesetja Kganyago** left the benchmark interest rate at 6% in September demonstrating the cautious approach of the SARB's monetary policy committee (MPC) since it had increased rates by 100 basis points (1%) in January.⁴² The MPC's interest rate increase is an attempt to pre-empt a long-expected United States (US) **Federal Reserve** rate increase.

Financial analysts believe that the increase is not enough. A **Bidvest** investment dealer said that:

³² Business Day, 20 Nov 2015

³³ Bloomberg Business, 23 Nov 2015

³⁴ Transnet, 23 Nov 2015

³⁵ Source, senior investment partner, Johannesburg

³⁶ News24, 25 Nov 2015

³⁷ News24, 25 Nov 2015

³⁸ Eyewitness News, 19 Nov 2015

³⁹ Bloomberg, 10 Nov 2015.

⁴⁰ South African, 25 Nov 2015.

⁴¹ South African, 25 Nov 2015.

⁴² Bloomberg, 10 Nov 2015.

"We are going to be at the mercy of the dollar if they do not do anything next week ... and 25 basis points will not do much for the rand. If they are going to do something they need to act aggressively and do 50 basis points."⁴³

Implications

Support for Ramaphosa from Cosatu and affiliates positions him well for the 2019 presidential race, as a senior member of the ANC, and alternative candidate to Nkosazana Dlamini-Zuma. The real election campaigns have begun and the political manoeuvring will place further pressure on the tripartite alliance. Mantashe and the SACP have declared support for Ramaphosa, who is also dependent upon Cosatu. Limpopo, Gauteng and the **Western Cape Province** also support Ramaphosa. Mantashe also brings support from the Eastern Cape – the second largest provincial ANC. These declarations of support have weakened Zuma and Dlamini-Zuma's early campaign lead. However, Zuma won a key victory in the KZN provincial chair election. The majority of KZN – which accounts for 40% of the delegates – remains in favour of Zuma, along with the premier league states. The choices available to business are between those of *"the devil and the deep blue sea"*⁴⁴ – either Zuma's influence extends beyond his term in office through his ex-wife, or Ramaphosa enters government in an alliance with the SACP. There is still everything to play for this early in the campaign. However, the politics is likely to impact policy making and implementation from now until December 2017.

Cosatu's national congress highlights rising anti-Zuma sentiment and deep fractures in the tripartite alliance. Cosatu is clearly unhappy with the primacy of the ANC within the alliance, as is the SACP. This is despite increased SACP influence under the Zuma administration. Cosatu is faced with a choice. It could abandon the alliance altogether and force the ANC to work with it as an external partner to get its endorsement. This is a plausible scenario as Cosatu is able to support itself financially, despite Numsa's departure, on membership subscriptions. Alternatively, it could remain within the alliance and attempt to renegotiate a more powerful position for the unions. Either way it is entering an arms race with Numsa and Vavi's potential new congress for members and the endorsement of Nactu and Fedusa. The decision to endorse Ramaphosa suggests that the congress would rather keep its inside track to government. However, the labour movement is not the only group in the political landscape to threaten the alliance. The attack by Motlanthe shows that ANC elders see the alliance as a weak point in the Zuma administration and more may come out to criticise it publicly in the coming months.

Private sector investment at an earlier stage could have helped SOEs improve South Africa's infrastructure deficit. The investments into Transnet and Eskom are welcome, but they come at a greater cost than they needed to. Resistance to part-privatisation of SOE's under the Zuma administration – and particularly by Mantashe and the SACP ministers – has forced the government to buy into Eskom debt, increasing pressure upon government spending, as the rand continues to struggle against the dollar. Continued criticism of SOEs, especially SAA, within the media and within the treasury has emphasised the accountability high-level management should bear for poor service delivery. Frustration at poor service delivery may result in an increase in service delivery protests as ANC pressure on SOEs is likely to slip with focus turning inward on internal affairs. The poor operations of SOEs such as SAA, poor procurement practices and unaccountable expenditure, are symptomatic of the Zuma administration. Increasing frustration from customers, employees and investors will place pressure upon the government, which remains willfully blind to increasing regional competition.

The SARB's recent actions may be effective as part of a long-term agenda to slowly increase interest rates. The SARB is keen to avoid sudden increases in interest rates that would hurt consumers and sharply decrease spending, further slowing growth. Inflation is due to increase in 2016, which will add further pressure on consumers and businesses alike. The central bank is stuck between a rock

⁴³ Bloomberg, 10 Nov 2015.

⁴⁴ Source, senior political commentator, London

and a hard place. It needs to stimulate growth but the economy lacks the flexibility to do so and the Zuma administration, apart from the treasury, appears to lack the will and/or ability to avoid a stagflation scenario.

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