

**AFRICA RISK CONSULTING****South Africa Monthly Briefing July 2019**

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**South Africa Summary 25 July 2019**

*President Cyril Ramaphosa (2018-present) backs public enterprises minister Pravin Gordhan in his legal battle against public protector Busisiwe Mkhwebane, who has called for Ramaphosa to discipline Gordhan. Mkhwebane appears to be targeting Ramaphosa and his allies, moving Ramaphosa's focus away from policy that could help South Africa and toward fighting internal battles that will hurt South Africa as well as Ramaphosa's chance for another term. Finance minister Tito Mboweni announces that an extra R59 billion (\$4.2 billion) will be allocated to state-owned energy company Eskom over two years so it can meet its financial obligations. United States (US)-based beverage producer PepsiCo and car manufacturer Ford both plan to make large investments in South Africa, which is seen as a vote of confidence for South Africa's struggling economy. PepsiCo acquired South African food company, Pioneer Foods, for \$1.7 billion while Ford's South African subsidiary, Ford Motor Company of Southern Africa, plans to hire 1,200 new employees and increase production to 168,000 vehicles per year.*

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**Ramaphosa backs Gordhan and goes head-to-head with public protector**

President **Cyril Ramaphosa** (2018-present) has backed public enterprises minister **Pravin Gordhan** in his legal battle against public protector **Busisiwe Mkhwebane**, who has called for Ramaphosa to discipline Gordhan over unconstitutional actions she alleges he committed while commissioner of the **South African Revenue Service (SARS)**.<sup>1</sup> Mkhwebane also claims that Gordhan misled the national assembly (legislature) regarding his meeting with the **Gupta** family.<sup>2</sup> The Gupta family is at the centre of the state capture investigations and allegedly worked with former President **Jacob Zuma** (2009-2018) to take control of key ministries in order to further the Gupta's business empire. Mkhwebane appears to be targeting Ramaphosa and his allies, moving Ramaphosa's focus away from policy-making that would help **South Africa** and toward fighting internal battles that will hurt South Africa as well as Ramaphosa's chance for another term.

Mkhwebane released a report on 5 July into an alleged "rogue unit" within SARS.<sup>3</sup> Mkhwebane alleges that Gordhan, who was SARS commissioner at the time, set up the SARS spy unit in 2007, in violation of the constitution.<sup>4</sup> Mkhwebane directed Ramaphosa to take disciplinary action against Gordhan by 4 August.<sup>5</sup> This is Mkhwebane's second finding against Gordhan, having directed Ramaphosa to take disciplinary action against him in May over Gordhan's approval of an early retirement package for former SARS commissioner **Ivan Pillay** in 2016.<sup>6</sup>

Former President Zuma used the "rogue unit" as an excuse to dismiss many top SARS officials and install senior managers who were loyal to him.<sup>7</sup> A leaked **KPMG** report in 2015 indicated the existence of the unit, but KPMG retracted the report and apologised to Gordhan in September 2017.<sup>8</sup>

Ramaphosa has taken Gordhan's side against Mkhwebane. Ramaphosa filed court papers in the **North Gauteng High Court** on 15 July asking the court to declare that he had complied with the suggested

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<sup>1</sup> Daily Maverick, 23 Jul 2019

<sup>2</sup> Business Day, 7 Jul 2019

<sup>3</sup> Business Day, 22 Jul 2019

<sup>4</sup> Business Day, 22 Jul 2019

<sup>5</sup> Business Day, 7 Jul 2019

<sup>6</sup> Mail & Guardian, 24 May 2019

<sup>7</sup> Business Day, 22 Jul 2019

<sup>8</sup> Times Live, 15 Sep 2017

remedial action in the Pillay retirement case.<sup>9</sup> The court is set to rule on 30 July whether Ramaphosa complied with Mkhwebane's suggested remedial actions.<sup>10</sup> In regards to the rogue unit case, Gordhan has asked the **Pretoria High Court** to suspend Mkhwebane's remedial orders. Mkhwebane responded that under normal circumstances she would not oppose this application, but given the fact that Gordhan disrespected her and the public protector's office, she would oppose the review.<sup>11</sup> Gordhan alleges that Mkhwebane is trying to undermine Ramaphosa's administration and is working with those who are trying to defend state capture.<sup>12</sup> The court has reserved its judgement until a later date.<sup>13</sup>

The opposition **Economic Freedom Fighters (EFF)** party is capitalising on the opportunity to discredit the ruling **African National Congress (ANC)** and belittle it in an attempt to steal supporters. The ANC has joined the case against Gordhan<sup>14</sup> in order "*to protect the office of the public protector*".<sup>15</sup> EFF leader **Julius Malema** has been outspoken against Gordhan, stating that

*"...we want the president [Cyril Ramaphosa] to take decisive action in dealing with Pravin [Gordhan]. Pravin must be fired."*<sup>16</sup>

What is less clear is whether Mkhwebane is fighting Gordhan and Ramaphosa out of a desire to fulfil her role as the public protector or whether her actions are politically motivated. Zuma appointed Mkhwebane in October 2016 after former public protector **Thuli Madonsela's** tenure ended.<sup>17</sup> Madonsela investigated the many indiscretions of Zuma and his allies, including the state capture allegations; Mkhwebane appears to be doing the same to Ramaphosa, though on less credible grounds as there was significantly more evidence relating to Zuma's indiscretions while in office. The rehashing of the rogue unit allegations appears to be vindictive rather than based on law. Mkhwebane's cases against Zuma allies, such as her February 2018 report on the **Estina** dairy farm in **Vrede**, "*points either to ineptitude or gross negligence in the execution of her duties.*"<sup>18</sup> The report investigated allegations of procurement irregularities and corruption regarding funding for dairy farmers in the **Free State**, but was reportedly siphoned to Gupta family-linked companies and ANC members, including current ANC secretary-general, **Ace Magashule**.<sup>19</sup> Mkhwebane's first report did not look closely at Magashule, who was Free State premier at the time of the corruption, but she plans to release an updated report at the end of August.<sup>20</sup>

For Ramaphosa and his allies, Mkhwebane's report is another battlefield as they struggle to fight off numerous wars against them within the ANC, while attempting to implement policies and actions to help move the country forward. Having the public protector against them will not help and, thus far, Ramaphosa's enemies are winning. There is a risk that Ramaphosa will spend his next four and a half years in office handling internal battles rather than being able to implement meaningful policies to help South Africa, thus giving his enemies the justification to remove him as ANC leader.

### **Mboweni allocates extra funding to Eskom**

Finance minister **Tito Mboweni** announced on 23 July that an extra R59 billion (\$4.2 billion) will be allocated to state-owned energy company **Eskom** over two years to allow it to meet its financial obligations.<sup>21</sup> Mboweni was conscious that the new bailout would come "*at a significant cost to the fiscus and to South African taxpayers*"<sup>22</sup> and is likely to substantially increase government borrowing

<sup>9</sup> Mail & Guardian, 15 Jul 2019

<sup>10</sup> IOL, 17 Jul 2019

<sup>11</sup> Daily Maverick, 23 Jul 2019

<sup>12</sup> Daily Maverick, 23 Jul 2019

<sup>13</sup> Times Live, 24 Jul 2019

<sup>14</sup> Daily Maverick, 23 Jul 2019

<sup>15</sup> Mail & Guardian, 24 Jul 2019

<sup>16</sup> Citizen, 23 Jul 2019

<sup>17</sup> Mail & Guardian, 24 Jul 2019

<sup>18</sup> Mail & Guardian, 24 Jul 2019

<sup>19</sup> Mail & Guardian, 9 Feb 2019

<sup>20</sup> EWN, 11 Jul 2019

<sup>21</sup> Mining Weekly, 23 Jul 2019

<sup>22</sup> Mining Weekly, 23 Jul 2019

as government revenue is forecast to be significantly lower than budgeted for 2019.<sup>23</sup> The R59 billion (\$4.2 billion) is in addition to the R69 billion (\$4.9 billion) that President Ramaphosa announced during his 2019 **State of the Nation Address (SONA)** in June.<sup>24</sup> The extra funding is crucial: if Eskom fails to meet its debt obligations, much of which is government guaranteed, it triggers immediate repayment and could lead to a call-in of debt from other state-owned enterprises such as **South African Airways** and **Denel** on fears that the government will begin to default.

Mboweni introduced the special appropriation bill in parliament to help Eskom and stated that R26 billion (\$1.8 billion) would be for the 2019/2020 financial year and R33 billion (\$2.3 billion) for the 2020/2021 financial year.<sup>25</sup> Mboweni and public enterprises minister Pravin Gordhan have struggled to steer Eskom in the right direction after decades of mismanagement. Mboweni admitted that Eskom faces a high risk of systemic failure, but that a new chief restructuring officer is expected to be announced on 30 July.<sup>26</sup>

Ramaphosa, Mboweni and the government are at a fork in the road with Eskom and there is financial strain on either side. On one hand, the government can fast-track the planned restructuring of Eskom and make hard decisions on its future, which will likely see an increase in the price of electricity, partial privatisation and reduced employment. This would be an unpopular decision, but necessary in order to reform Eskom into a functioning entity that does not rely on government bailouts. On the other hand, the government can continue to bail Eskom out and not make the unpopular reforms, but face a very real risk that international ratings agencies, such as **United States (US)**-based ratings agency **Moody's**, would downgrade South Africa's debt to junk and lose the confidence of international investors, which would also hurt the economy as foreign direct investment could decrease along with jobs. With an election behind him, the first option is the logical and less risky one for Ramaphosa, but he is unlikely to choose it given the issues he faces within the ANC (see above). Instead, investors and citizens should ready themselves for more bailouts and fewer reforms, as well as getting used to the term "*too big to fail*".

### **PepsiCo and Ford's investments in South Africa a vote of confidence in economy**

US-based beverage producer **PepsiCo** and US-based car manufacturer **Ford** both plan to make large investments in South Africa, which is seen as a vote of confidence for South Africa's struggling economy. The investments are a signal that some international investors still see opportunity in South Africa, both domestically and as a gateway to **sub-Saharan Africa**, despite the political and socio-economic risks.

PepsiCo agreed on 21 June to purchase South Africa-based food company **Pioneer Foods** for R24.4 billion (\$1.7 billion) as part of a strategy to expand into sub-Saharan Africa.<sup>27</sup> PepsiCo offered a 56% premium on Pioneer Foods' shares in order to buy out the local company.<sup>28</sup> Pioneer Foods has several beverage and food brands in South Africa as well as in **Nigeria** and **Kenya**, but has struggled with the consumer-spending slump in South Africa over the past few years. The acquisition is PepsiCo's second biggest acquisition outside of the US in 10 years after the \$3.2 billion deal for **Israel**-based **SodaStream** in December 2018.<sup>29</sup>

Ford's South African subsidiary, **Ford Motor Company of Southern Africa**, said on 17 July that it would employ 1,200 new employees from August to meet growing international and local demand for its vehicles.<sup>30</sup> This increases Ford's local employment to 5,500 employees, in addition to adding up to 10,000 jobs in supplier companies.<sup>31</sup> The new employees will work a third shift in the newly

<sup>23</sup> Mining Weekly, 23 Jul 2019

<sup>24</sup> MoneyWeb, 20 Jun 2019

<sup>25</sup> City Press, 23 Jul 2019

<sup>26</sup> City Press, 23 Jul 2019

<sup>27</sup> Fin24, 21 Jun 2019

<sup>28</sup> Fin24, 21 Jun 2019

<sup>29</sup> PepsiCo, 5 Dec 2018

<sup>30</sup> BusinessTech, 17 Jul 2019

<sup>31</sup> BusinessTech, 17 Jul 2019

renovated **Silverton Assembly Plant in Pretoria (Gauteng Province)**.<sup>32</sup> Ford's R3 billion (\$216.2m) investment in 2017 will increase production capacity from 124,000 vehicles to 168,000 vehicles per year.<sup>33</sup>

These large investment deals should be seen as a vote of confidence in South Africa. Rather than viewing South Africa's flagging economy as a reason to head to other countries, many investors see it as an opportunity to purchase companies at below-market rates. Pioneer Foods' shares, for example, have dropped from R210 (\$15.14) in 2015 to around R70 (\$5.05) at the time of PepsiCo's announcement. PepsiCo is purchasing the company at R110 (\$7.93) per share, almost half of Pioneer Foods' value in 2015.<sup>34</sup> According to a South African-based investment manager,

*"...these companies are willing to take on the political and socio-economic risks in South Africa because they are taking very long-term investment views compared to local investors."*<sup>35</sup>

The investments could also be a sign that Ramaphosa's investment drive has begun to work and illustrates that international investors view Ramaphosa as a credible partner in South Africa. Ramaphosa needs to take advantage of this opportunity and use these two case studies to show other international companies that South Africa is still open for business.

### Planner

17-19 Sep 2019 **South African Reserve Bank (SARB)** Monetary Policy Committee meeting  
 Oct 2019 Medium Term Budget Policy Statement  
 9-11 Oct 2019 Africa Oil & Power conference, Cape Town  
 19-21 Nov 2019 **SARB** Monetary Policy Committee meeting  
 2024 Scheduled general election

### Chronology

23 Jul 2019 **Cape Town (South Africa)** *Cape Times*. Finance minister **Tito Mboweni** says that tax revenues could be significantly lower than budgeted for and **South Africa** may need to borrow more than planned;

23 Jul 2019 **Johannesburg (South Africa)** *Business Day*. The **International Monetary Fund** revises its growth forecast for South Africa to 0.7% for 2019, down from a previous 1.2% forecast;

22 Jul 2019 **Johannesburg (South Africa)** *Reuters*. The government plans to allocate an extra \$4.24 billion in funding over two years to state-owned energy company **Eskom** to help service its debt;

19 Jul 2019 **Johannesburg (South Africa)** *Reuters*. **United States**-based beverage company **PepsiCo** agrees to buy **Pioneer Food Group** for \$1.7 billion;

18 Jul 2019 **Johannesburg (South Africa)** *FT*. The **South African Reserve Bank** (central bank) cuts interest rates to 6.5% and decreases its 2019 economic forecast to 0.6%, down from a previous forecast of 1%;

16 Jul 2019 **Johannesburg (South Africa)** *The Citizen*. **Ford Motor Company of Southern Africa**, subsidiary of **United States**-based automobile manufacturer **Ford Motor Co**, plans to

<sup>32</sup> BusinessTech, 17 Jul 2019

<sup>33</sup> BusinessTech, 17 Jul 2019

<sup>34</sup> MoneyWeb, 22 Jul 2019

<sup>35</sup> Source, investor, South Africa

hire 1,200 people to stay an extra shift and increase production to 720 units per day;

15 Jul 2019 **Johannesburg (South Africa)** *Business Day*. President **Cyril Ramaphosa** files a legal challenge against public protector **Busisiwe Mkhwebane**'s remedial actions against public enterprises minister **Pravin Gordhan**;

15 Jul 2019 **Johannesburg (South Africa)** *News24*. Former President **Jacob Zuma** is expected to appear before the **Zondo Commission of Inquiry into Allegations of State Capture** on 15 July;

12 Jul 2019 **Johannesburg (South Africa)** *Sowetan*. The **Randburg Magistrates Court** finds **Duduzane Zuma**, son of former President **Jacob Zuma**, not guilty of culpable homicide in a fatal 2014 car crash;

12 Jul 2019 **Johannesburg (South Africa)** *Business Day*. Justice minister **Ronald Lamola** applies to set aside the extradition of **Mozambique**'s former finance minister, **Manuel Chang**, and may extradite Chang to the **United States**;

12 Jul 2019 **Cape Town (South Africa)** *Sowetan*. The **South African National Defence Force** will deploy to parts of the **Western Cape** to stop gang-related violence;

11 Jul 2019 **Cape Town (South Africa)** *FT*. Opposition **Economic Freedom Fighters** party members physically threaten public enterprises minister **Pravin Gordhan** in parliament, amid concerns that the EFF is backing **African National Congress** members who oppose President **Cyril Ramaphosa**;

11 Jul 2019 **Cape Town (South Africa)** *News24*. Finance minister **Tito Mboweni** plans to table a bill on 23 July to allow new funding for state-owned electricity company **Eskom** to alleviate liquidity issues;

11 Jul 2019 **Johannesburg (South Africa)** *ThisDay*. **Nigeria**'s Senate warns the **South African** government that Nigeria will no longer tolerate killing of its citizens in South Africa;

10 Jul 2019 **Johannesburg (South Africa)** *FT*. President **Cyril Ramaphosa** reappoints **Lesetja Kganyago** as governor of the **South African Reserve Bank** (central bank) for a five-year term;

4 Jul 2019 **Johannesburg (South Africa)** *Business Day*. **Prudential Authority** chief executive **Kuben Naidoo** says the **South Africa Reserve Bank** (central bank) will sell its 50% stake of **African Bank** in the coming two years;

4 Jul 2019 **Johannesburg (South Africa)** *Mining MX*. **United Kingdom**-based **Vedanta Resources** attempts to move its legal battle with the **Zambian** government to **South African** courts;

3 Jul 2019 **Johannesburg (South Africa)** *Business Day*. Deputy finance minister **David Masondo** says the government will not use quantitative easing to help struggling state power utility company **Eskom**;

3 Jul 2019 **Johannesburg (South Africa)** *Bloomberg*. The **Chamber of Commerce and Industry** says business confidence rose in June but remains below last year's levels;

3 Jul 2019 **Johannesburg (South Africa)** *Reuters*. **South Africa**-based **Paramount Group** and **Saudi Arabia**'s state-owned defence company **Saudi Arabian Military Industries** sign a collaboration agreement;

1 Jul 2019 **Johannesburg (South Africa)**. *Business Report*. **JSE**-listed **Nampak** to receive \$57m from the **Reserve Bank of Zimbabwe** (central bank) in a legacy debt settlement;

1 Jul 2019 **Johannesburg (South Africa)** Public protector **Busisiwe Mkhwebane** accuses President **Cyril Ramaphosa** of failing to uphold the constitution by not complying with remedial action against public enterprises minister **Pravin Gordhan**;

25 Jun 2019 **Johannesburg (South Africa)** *FT*. State-owned defence company **Denel** says it is unable to pay salaries in full in June due to liquidity issues;

25 Jun 2019 **Johannesburg (South Africa)** *BusinessTech*. Home Affairs acting director-general **Thulani Mavuso** says that the new e-visa system will launch in October;

25 Jun 2019 **Johannesburg (South Africa)** *Business Day*. Public enterprises minister **Pravin Gordhan** says the unbundling of state-owned energy company **Eskom** will continue despite rumours to the contrary;

25 Jun 2019 **Johannesburg (South Africa)** *Business Day*. The **Public Investment Corporation** will take disciplinary action against 11 staff members for their decision to invest in **Ayo Technologies**.