RISK ALERT

16 MAY 2022

First thing every Monday morning as a text and audio note

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SA's reform prospects

In his weekly newsletter of 9 May, President Cyril Ramaphosa wrote: 'Many of these [structural] reforms are complex, involving new ways of working and even the establishment of **new institutions.** In some cases, it will take time for us to see their full impact.' However, it is our view that the reforms currently on the table are **unlikely** to substantively improve South Africa's performance.

A report-back on the government's flagship economic reform programme — **Operation Vulindlela** — stated that the government had prioritised **26 structural reforms.** Of these, 8 were marked 'completed', while another 11 were labelled 'progressing well'. But these reforms tinker at the margins of what needs to be done. They focus on the **regulatory and institutional environment** of the water, power, communications, and transport infrastructure, while ignoring more critical issues such as expropriation without compensation, stricter race-based labour legislation, greater **state control** over schools, more protectionism, and the National Health Insurance.

Without sweeping labour and education reform, the jettisoning of **protectionist policies,** and the strengthening of **property rights** across the board, South Africa's GDP growth rate will remain stuck below 2%. This means that unemployment will continue to escalate, **frustration and anger** in the population will mount, and the threat of **violent unrest** and political instability will continue to grow.

Where to next for loadshedding?

With South Africa once again in the throes of loadshedding, a **reliable electricity supply** seems both a distant memory and a distant prospect for the future. To end loadshedding, South Africa would need an additional 4 000–6 000 megawatts (MW) of generating capacity immediately and **40 000–50 000MW of new capacity** within the next 15 years, as old equipment is taken out of service and the country's energy needs grow. This is equivalent to adding new generating capacity the size of the entire existing capacity, rated at around 54 000MW, to the grid over the next decade and a half.

However, Eskom is **saddled with debt** of R392 billion and needs regular bailouts just to maintain operations. It cannot afford the required expansion of capacity. Furthermore, the company is owed over R40 billion by municipalities and faces the additional challenges of combating **widespread electricity theft** and vandalism of its physical infrastructure.

The only way for capacity to be expanded at scale is through the private sector. And indeed, **mining companies** are reported to have committed to 4 000MW of renewable energy projects, although it is unclear when this will come onstream. Eskom is also hoping to start buying power from **Independent Power Producers (IPPs)** from the middle of 2023. Although businesses are now allowed to generate up to 100MW without a licence, they still need to register with the National Energy Regulator of South Africa (NERSA) and obtain various other approvals. This process is **cumbersome,** and the possibility is that only those with the necessary political influence will succeed.

Overall, the measures undertaken are **too modest,** too few and too slow to make a noticeable difference in the short term. You should therefore prepare for **several more years** of loadshedding and low growth.

SA mining — the hobbled giant

South Africa's mining sector delivered **strong returns** and made a significant contribution to the country's trade balance and tax revenue during the pandemic. Even so, its performance could have been significantly better. According to the Minerals Council, bulk mineral miners lost revenue of R35 billion in 2021 due to the decline in South Africa's **rail and port capacity.** And in what the Minerals Council called 'an **alarming wakeup call** that we are moving in the wrong direction', the Fraser Institute listed South Africa among the world's ten least attractive mining destinations, ranking 75 out of 84 jurisdictions surveyed.

Furthermore, the Department of Mineral Resources and Energy has allowed a backlog of over **4 000 mining and prospecting rights** as well as mineral transfer applications to pile up — a major contributor to low investment in mining exploration. The backlog is largely a result of the department's decision in 2011 to introduce a self-built computerised registry known as the South African Mineral Resources Administration System (Samrad) — to manage the **mining cadastre,** the record of South Africa's mining land parcels and who owns associated rights such as prospecting rights or mining licences. As Samrad has been dysfunctional for over a decade, the department reverted to paper-based processes, which are less transparent, slower, and more vulnerable to corruption.

Effective systems are available off-the-shelf, among others from a Cape Town-based company, Spatial Dimension. However, when the department went to market to look for a solution to replace Samrad, it chose to do so under **race-based preferential procurement regulations** instead of applying for an exemption, thereby excluding solutions from market leaders such as Spatial Dimension and its US-listed parent company, Trimble. The tender closed in August 2021 and the process appears to be **completely stalled,** ensnared in red tape and a race-based ideology from which the government will not deviate even when the costs run into the billions. This is emblematic of the ANC government's unwillingness to reform — and of South Africa's **limited growth prospects** even in areas where it should be playing to its strengths.

African countries face fuel shortages

Sub-Saharan African countries, including South Africa, are at increasing risk of fuel shortages. According to Pierre Barbe, head of Africa business at Vitol (the world's biggest independent oil trader), Africa is undergoing its **worst supply crisis in 40 years.** Russia's invasion of Ukraine has driven global oil and fuel prices higher, but African economies are also burdened with numerous **port and distribution inefficiencies** which are exacerbating the problem.

According to the International Energy Agency (IEA), sub-Saharan Africa's **refinery output has dropped by half** over the past decade. On average, the region imports three-quarters of its refined products, while South Africa relies on imports to meet up to 60% of its fuel demand. In South Africa, four out of six refineries are not operational; added to lower refinery capacity was the damage to infrastructure caused by flooding in KwaZulu-Natal earlier this year, which has led to **jet fuel shortages** at OR Tambo International Airport in Johannesburg, resulting in flight cancellations and diversions.

Industry sectors including tourism, agriculture, mining, and manufacturing should take the **risk of fuel shortages** seriously and prepare accordingly. The South African Petroleum Industry Association (SAPIA) has in the past indicated that accommodation for adequate imports would need to take the form of a dedicated shipping route. Without preparation and necessary policy shifts, sub-Saharan countries — including South Africa — will remain **vulnerable to external shocks,** such as war and problems with supply chains.

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