Report of proceedings

Envisaging a New Path for State-Owned Enterprises

A Dialogue organised by the Strategic Dialogue Group and the Public Affairs Research Institute

14 March 2020

PUBLIC AFFAIRS RESEARCH INSTITUTE

SDG Strategic Dialogue Group

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Introduction

The Strategic Dialogue Group (SDG) and the Public Affairs Research Institute (PARI) held a public dialogue to enable leadership from different perspectives and stakeholders (i.e. inside the state (SOE Manager, Presidency), independent analysts, civil society/labour) to comment on the commitment made by President Cyril Ramaphosa on 20 January 2020 in respect of State-Owned Enterprises (SOEs) as articulated below and provide insights on how to give effect to these outcomes.

In the closing remarks of President Cyril Ramaphosa and in the ANC media release following the ANC NEC lekgotla - after significant debate and discourse both within the ANC and in the media - the lekgotla endorsed the following proposals in respect of SOEs:

- *That the commercial and developmental mandates of SOEs and SOCs should be clearly outlined and stated and reviewed where necessary.*
- *The institutional design which will support their developmental mandates should be examined.*
- *There should be greater and more effective attention to the operational efficiency and integrity of SOEs as well as ensuring that people who are fit for purpose are appointed to various positions.*
- *We should look to embark on a consolidation and rationalisation process of our SOEs.*
- *In line with the Resolutions of the 54th National Conference, we must avoid political interference in operational matters, other than interventions in the case of mismanagement and possible company failure.*

The event enjoyed the participation of a number of distinguished guests. The opening address was delivered by Deputy Minister of Finance, Dr David Masondo, followed by commentaries from a panel and an interactive dialogue with attendees. Panel members were:

- Popo Molefe, Chairperson of the Transnet Board;
- Zingiswa Losi, President of COSATU;
- Dipak Patel, Special Advisor to the Minister of Public Enterprises;

- Henk Langenhoven, Chief Economist at the Minerals Council; and
- Khaya Sithole, an independent analyst and academic.

Dr Mbongiseni Buthelezi (PARI) and Dr Sihle Moon (SDG) welcomed participants to the dialogue and introduced the speakers on the panel. In turn, each of the speakers gave their inputs. The next sections seek to capture their main points in such inputs.

Summary of inputs by panel speakers

Opening address by Dr David Masondo – Deputy Minister of Finance

Dr Masondo welcomed the dialogue and the role of civil society particularly since the battle to save SOEs is ongoing and the President is to set up an SOE Coordinating Council. He provided a vision of the government in relation to SOEs.

There are a number of strategic questions that arise in relation to SOEs. When we talk about envisaging a new path, we need to ask: this is a path to what? To where? What are the problems that we seek to resolve in relation to these SOEs? What is the goal/mission for these SOEs? – if we know this, then it is easier to understand the path ahead.

There are approximately 715 SOEs (including provincial ones) in South Africa including those that:

- Provide services (i.e. Eskom, Prasa, SAA, Post Office, SANRAL);
- Provide goods (i.e. Alexkor, Armscor, Denel, SABC);
- Provide development finance (i.e. DBSA, PIC, Land Bank);
- Promote investment (at provincial level).

Whether the SOEs provide what they were set up for is a different question. Each SOE is established for a particular purpose. In analysing a new path, we should not fall into a traditional position that the market is bad, and the state is inherently good. The work of Mariana Mazzucato is very influential on the involvement of the state.

There are many reasons why SOEs are not working, in particular:

1) SOEs are not supporting economic growth because they are not providing goods as we expect them to;
2) SOEs should be financially sustainable yet many of them are not; they cannot meet their financial obligations (i.e. Eskom has a debt of R500billion, against total debt of government standing at R2.5trillion).

The country needs to stabilise debt levels, and SOEs are meant to help us to do this and to grow the economy. Debt has a very negative redistributive effect – we are taking money that should go to goods and services in health, schools and we are giving it to SAA, for instance.

However, debt is a symptom of the problem. In respect of the debt of Eskom – the costs are high; revenue is very low, and it keeps borrowing money. SOEs need to look at their cost structures. Eskom's cost structure is driven by primary sources of electricity.

For other SOEs, it is about the business model (like SAA). There is no airline that makes money out of aircrafts only – many airlines' business model is integrated into the hospitality industry (car rental, hotels, etc.) therefore when one unit is not making money, it can be cross-subsidised by another. Throwing money into SOEs is not sustainable.

So, what is to be done? We need to ask whether we need all SOEs. If not, what are the criteria according to which we need to decide which to keep and which to get rid of? Criteria can include:

- Whether the entity is cross-cutting as far as the economy is concerned;
- Can it render a unique service that can't be performed by the private sector e.g. PRASA or Transnet?
- Is it important for national security or in the national interest e.g. Denel and Armscor?

If we maintain SOEs, how do we make sure that they are run like a business (i.e. cost structure and revenue are balanced) to at least break even? Against the failure of SOEs to meet some of these parameters as an entity (i.e. generate revenue, review cost structure), government must be able to take hold of them and make decisions to rationalise some of them or create equity partnerships. For instance, some of the entities are insulated from market forces: what kinds of incentives does this generate and how do we ensure that they operate efficiently?

In relation to governance, we need good management. Work is underway to stabilise SOEs at board and management levels. Many of the SOEs experience leadership instability. The establishment of the SOE Council is at an advanced stage and should assist with this process.

In conclusion, while technocratic progressivism is important, it is not enough. We need to make sure that we continue shifting the balance of power and forces - institutions on their own without an active civil society can get easily captured. We therefore need an active civil society to rebuild SOEs as well as leadership education such as is provided by the OR Tambo School of Leadership.

Remarks by Dipak Patel – Special Advisor to the Minister of Public Enterprises

Patel started by emphasising that stable management of SOEs is critical for their turn-around. The SOEs that have tended to be a drain on the fiscus, and economy were subject to state capture and corruption which have significant impacts on the lives of our people (Eskom, PRASA, SAA, Transnet, SABC, Denel, PIC, etc.). Very few of our SOEs are net assets; the majority have negative net asset values and present fiscal/systemic risks to the country's state of affairs. Since 2018, there has been frustration in that we have not been able to fix some of these SOEs and stabilise them (i.e. PRASA).

There has been an erosion of the fundamental fabric of these institutions. While the Department of Public Enterprises uses a logical planning framework to manage SOEs, we need to deal with corruption and bring back an ethical mind set, which is a long-term project.

To date, we have uncovered areas of malfeasance to begin to stabilise these entities, but we need a programme to rebuild them. The wheels turn slowly to hold accountable those who are responsible. However, we hope to develop traction.

In a mixed economy, large state institutions can play a role in development (social, economic) by facilitating/catalysing things, including where market failure exists. However, in the current condition in which SOEs find themselves, there is scepticism whether they can play a catalytic role to deal not just with market failure but also with how they can contribute towards growth and development.

The Presidential Review Commission has undertaken one of the most thorough reviews, addressing the notion of the developmental state and providing a scan of models internationally. As South Africa, we have not yet made a choice about the model we want to follow. We are moving towards a hybrid approach, where attempts are being made to cluster SOEs by sector and answer a series of questions (i.e. role SOE plays in developmental state; in mixed and diversified economy, etc.). The process of forming a Presidential SOE Council is underway but we have many broken platforms in SOEs that require urgent attention.

If we look at South African Airways (SAA), some argue that there is nothing strategic about it. However, government wants a national flag carrier with domestic and international services. It is very easy to say 'let it fail' but we need to ask: 1) Is there potential to fix it? or 2) What is the cost of simply letting it go?

The latter is not an option, so we need to do what is necessary to stabilise it and make it more efficient. SAA is in business rescue now while the COVID-19 epidemic is growing, and countries are shutting down borders as a result. It is difficult to determine a path when the environment is constantly shifting.

Eskom presents a systemic risk. It is dysfunctional at an operational level and its balance sheet is insolvent. We have no choice but to fix operations at Eskom (management got decimated and therefore need to rebuild it; its board must be reconstituted to make it functional) and we need to deal with its dire financial situation. It needs fiscal support and other mechanisms to relieve it from its balance sheet deficit over the next year to 18 months. We are currently building platforms of stability.

Remarks by Popo Molefe – Chairperson of Transnet; former board chairperson of PRASA

Popo Molefe undertook a cursory look at the historical context under which SOEs were born and the challenges that they were intended to address. What were the critical ingredients to ensure that SOEs deal with the challenges that they face today?

SOEs emerged after the South African war to deal with the issue of job creation of poor whites, the development of the economy and service delivery at a time that the economy began shifting from agriculture to manufacturing.

The requirement to create self-reliance which led to the creation of institutions such as Sasol and the Strategic Fuel Fund was driven by the Broederbond. This political centre embraced the cause not for itself but because it supported the growth of the economy and building as much wealth as much as possible. We inherited functioning SOEs. We need government to be committed to a growth programme in a similar way.

There is some research that has been done on the demise of our institutions when the democratic government took over. SARCC was unbundled and PRASA was formed. In this process, we lost appreciation of the fact that PRASA provides critical services. There is no railway business that does not depend heavily on state subsidies. We need to accept that it will need to be heavily subsidised – trains carry people who drive growth in the economy. At present, people do not pay whereas during apartheid, one would not get through without going through ticket examiners – such discipline got lost.

We have failed to deal with the integrated approach to governance when we unbundled Transnet and PRASA. When government takes a share in modernisation for PRASA and similarly for Transnet – it decides where it will go to procure. There is no centre that controls how the funds will be applied. As a result of this, invariably people begin to choose and weigh the possibility of getting more into their own pockets without focusing on the quality of equipment required.

There is a need, therefore, for strategic thinking on how we coordinate the services. There would be no problem with National Treasury indicating that it is willing to make the funds available but that, instead of transferring the funds for procurement, National Treasury will work with an entity to procure services/goods and, when satisfied, National Treasury will bid for these things. If this system were in place, the problems faced by SOEs might be lessened.

Molefe described PRASA as a broken organisation. He noted that when the Board wants to shake the trees, the political office interferes. He recalled his experiences of taking a stand to disrupt patterns of looting and yet no politician had the courage to stand up and say that he was doing the right thing – it was only civil society which spoke up. He added that the political centre is not playing the role it should play, namely that of making SOEs beholden to them. In many instances, the political centre is not carrying out orders of the government but rather of persons who hold office in the governing party. It is therefore vital to deal with the political centre and to develop strategies to persuade people in government to do things differently.

Molefe highlighted a number of challenges facing PRASA at the time, which included:

- There is no coordination between the procurement of locomotives and participation of Transnet technical services.
- PRASA cannot maintain its infrastructure. The infrastructure network should go to Transnet. PRASA is for all intents and purposes, dead. It has an administrator. There does not seem to be an intention to change PRASA; there is no demand for a CEO to be appointed.
- PRASA is sitting on buses which it cannot operate effectively, while the terminals of those buses sit with Transnet.

He highlighted some of the measures that Transnet is undertaking. He noted that the HR function had been used as a critical facilitator of the reproduction of those who were captured. Many of those people are entrenched and it is necessary to take measures to exit some of these individuals so that the system can be changed. The board of Transnet is giving management its space – there is no overreach – but it is holding management accountable. In addition to dealing with HR issues, Transnet is also considering how to partner with the private sector on terms that Transnet would agree on. Molefe also noted that there is a need to focus on changing existing laws and frameworks which are not only at times contradictory but also give too much power to politicians.

Remarks by Zingiswa Losi - President of COSATU

Zingiswa Losi noted that COSATU represents the majority trade unions in most SOEs. She highlighted that many of the SOEs have been run into the ground. They have been hollowed out by politicians, together with those who have been appointed into office. She noted that politicians try to defend what is wrong because they are defending themselves, but it will be traced back to them. SOEs have been looted at an industrial scale, mismanaged at incredible levels, hollowed out and left with unsustainable levels of debt with the threat of South Africa running to the IMF, while workers are at the coalface of this state of affairs.

There is a need for forensic audits of expenditure and contracts. While the Zondo Commission is carrying out important work, we need to move to prosecute and attach assets. One of the key problems is that, at present, there are no consequences – there are golden handshakes. Lifestyle audits need to be conducted on new managers. New business models are also required; it is necessary to rethink what it means to be an SOE today as the 1950s models do not work. COSATU is becoming a political football, many promises are being made but things are not happening.

She noted the need for full mobilisation of public financial resources from the PIC. Moreover, 90% of workers' pension funds are invested in the JSE, in stock exchanges overseas and there is no development out of workers' money. Those who are benefiting are far away. In order to build socialism now, workers must be in control of their money, yet investment returns are not coming back to workers.

South Africa also needs 'just transition' plans for each sector of the economy. For instance, SA should undertake the building of solar panels (move workers from coal sector to solar), but one cannot just close off mines. Workers need to get the skills necessary for the shift and thus be prepared for a just transition. The country cannot afford to have ghost towns or migration to urban cities; we cannot forget about the rural areas.

As social partners, government, labour and business need to work together through social compacts to save our jobs and pensions. There are interventions in Eskom to save jobs. COSATU made proposals in relation to Eskom to deal with looting, mismanagement and overpricing in supply. Business must invest in alternative forms of energy and reduce reliance on coal by Eskom. Similarly, companies like Denel should focus on producing armoured vehicles that conform to climate change.

To build a capable state, we must work together to fight corruption. As Losi pointed out, all of us have to take a stand against corruption. As an example, she said, if the process is not correct, do not press the 'enter' button to process something – we need to protect whistle-blowers. As to the culture of non-payment, we need to go back to the culture of paying. Indigent households must not pay but those who can afford to, they must pay.

Remarks by Henk Langenhoven - Chief Economist, Minerals Council of South Africa

Langenhoven focused on the role of SOE's for business. In past years, there was avid competition amongst SOEs for the best people. Eskom is the third largest utility in the world – it is the oil of our economy. Approximately 45% of intermediary inputs are bought from SOEs or the state; it is therefore vital for these SOEs to work properly.

The Electricity Availability Factor (EAF) is vital for industry. When supply is disrupted, a whole process is disrupted (i.e. week-long operations), investment is limited, and plants get scrapped, which results in worker retrenchments. The economy needs 29 gigawatts of electricity to be available. However, Eskom often operates below 25 gigawatts.

The longer it takes to deal with this crisis, the more idle machinery and employees that this will generate. Langenhoven's slides demonstrated that mining production slows down and weakens as supply worsens. He noted that smelters are idle or close and that PGM operations have suffered significantly. He explained that smelters run all the time and therefore if there is not enough wattage, they need to be shut down. If they cool down, they can crack, rods crack and they burn up. Therefore, they can either be on or off. Manganese smelters are at risk of closure due to limited wattage.

Industry cannot respond fast enough to changes in international commodity prices because of the constraints that it faces. It takes us 12 to 18 months to respond to better commodity prices.

Approximately 80% of the costs of transport are incurred with Transnet and thus there is an urgent need to resolve issues with the rail network and efficiencies of the ports. He also noted that, even if the mining sector is given the go-ahead to generate their own electricity, it will likely take a period of 9 to 36 months to be able to do so. He stressed the importance of the structural reforms in respect of network industries proposed by the National Treasury.

The mining industry is also facing major issues with water in the Northern Cape. If there is limited water, companies will mine until the end of their mining licence and then shut down rather than expand operations. In this regard, he noted that the construction of mines and expansion of mines has been declining since 2011. The sector could expand and contribute to growth and employment if it is able to invest more; however, without electricity, it is not possible to pursue this path.

Remarks by Khaya Sithole - independent analyst and commentator

Khaya Sithole enjoined the audience to think about the different dimensions of the crisis facing SOEs, and posed a number of relevant questions:

- What is the crisis of? What are the dimensions of the crisis?
- Crisis of purpose – why do we have them?
- Crisis of function – what do they do and don't do?
- Crisis of design and contradictions in respect of the design – for instance, the Information Regulator both regulates PAIA and also restricts access to information;
- Crisis of legitimacy – not clear why an SOE exists and why the state is involved; and
- Crisis of governance?

The fundamental question that we must seek to answer is: Why do we need SOEs and what do they seek to serve? When answering this question, we need to appreciate that the cost of rolling out social infrastructure is prohibitive; the private sector could not do it, or the cost of recovery would be prohibitive to use it. In contrast, the taxpayer never dies and can support these services, which enables the state to step in.

SOEs are meant to aid and support economic growth. However, in some cases there are inhibitors (i.e. SOEs not knowing what they are doing, etc.). Yet, in the absence of the entity, what would the picture look like in terms of economic growth? The lack of economic growth is a crisis on its own that has been occurring for a long time. At present, we speak of recession since we have had two consecutive quarters with a contraction of the economy. In linking to economic growth, there is often an inability to correlate the global to the granular level.

To illustrate a possible crisis of function, regulators play a key role – but do they understand their function? For instance, ICASA's ability to understand the spectrum, what it is and how it is supposed to implement it. Similarly, he noted that in a recent interview with the SABC Chair, the latter seemed unwilling to adapt to conditions in the country.

In relation to the payment of TV licences, the emphasis is on 'taxpayer benevolence' or patriotic duty, but this does not really exist as shown by the non-payment of e-tolls. The focus continues to be on TV licence fees, without focusing more broadly on any broadcasting activity, including radio – every device should generate a fee, and this would increase the revenue. Another possibility is to charge a once-off TV licence fee when a TV is bought (regardless of whether watch SABC or not).

In terms of a crisis of design, there is some evidence that this might affect some SOEs, such as Transnet where there is a contradiction between what is the legislation and in their Memorandum of Incorporation. Similarly, in relation to SAA, which is undergoing business rescue, it is difficult for anyone at the moment to identify the legal framework that takes precedence (i.e. whether it is practitioners or the Minister who can decide on the shutdown of SAA).

As to a crisis of legitimacy, the example of the SABC serves to illustrate this. For instance, why pay for SABC TV licence when people watch DSTV and not SABC channels?

Importantly, we need to ask whether we need all of these entities. It is unlikely that even 100 SOEs meet their requirements. This, in turn, poses the question of why the state seems to be obsessed with managing things that it cannot manage. Shareholders (state) have tended to be passive and they need to step in and become active shareholders, if management is failing to carry out its work.

The recent PIC report does not deal, for instance, with the question of how Dan Matjila became its CEO in the first place. Why was he selected? This requires us to go back to the drawing board. The crisis of governance experienced by many SOEs is not accidental. Instead, it has served a particular purpose. Since the state owns them, they decide who runs them (political favours), guided by the right factions and not by the best person for the job. We must move away from the notion that President Zuma was the problem and rather consider that any political party that can allow a person like him to run the country is a fundamental problem.

Inputs from the audience

Following the above inputs, the audience raised questions and comments including:

- How do we not repeat the mistakes of the past?
- The respective roles of the public and private sectors;
- Should citizens buy shares in SOEs?
- The critical role of governance, compliance with the rule of law, ethics and risk management and capacity. While some issues like solving financial and operational issues may require long term solutions, governance can be immediate and does not need an injection of resources.
- The need to clean up SOE’s at the top and the bottom – in respect of junior employees;
- The difference between taking decisions, taking wrong decisions and not taking decisions at all;
- The requirement to shift to renewable energies, from road to rail and develop new industries
- The critical relationship between technology and employment moving towards the future; and
- The socialisation of consequences against the individualisation of rewards.

After this exchange all panellists were given an opportunity to respond and the Deputy Minister of Finance was given an opportunity to close the dialogue.

Closing remarks by Dr David Masondo, Deputy Minister of Finance

Dr Masondo noted that in addressing the issues faced by SOEs and moving forward, the capacity of the state is a central issue. In particular, it is important to frame the issues around two key features of the developmental state, namely: subsidy and discipline. We need to use the resources of the state to discipline business to have developmental outcomes. We need to use the provision of cheap electricity to boost industrialisation and use the power of Transnet for subsidies for those who cannot afford it.

In addition, we must address internal and external capacity issues of the developmental state. Internal capacity issues revolve around people, systems, policies, etc. How far are we in dealing with these issues since 1994? We have conflictual laws, limited planning capacity (i.e. no planning boards/proper projections). How far are we in building this? Are we making decisions towards an aspirant development state? Decisions are being taken.

As much as we would want people who are guilty to be arrested, the President cannot instruct the criminal justice system on what to do. We also need to be careful as a number of these individuals are well-resourced to fight their battles. We need to distinguish between different kinds of politics; we need to move away from the notion that technocrats are great, and politicians are bad. A board takes political decisions; they are not apolitical. The issue is getting our politics right.

He recognised that, as politicians, we have taken bad decisions – but politics is not inherently bad. Institutions do matter and we need to work to rebuild them. Yet, rebuilding institutions without civil society playing an active role will not work. Civil society needs to be proactive in dealing with these issues.

SDG
Strategic Dialogue Group

SDG is an organisation of progressive thought leaders and activists who champion progressive policies, build ethical leadership and mobilise constituencies for change in order to create an equitable and inclusive society. Founded in 2016, the SDG brings together former members of AZASO, NUSAS, SANSCO and SASCO whom it seeks to mobilise into active participants in rebuilding South Africa.

PARI
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PARI studies the effectiveness of state institutions in the delivery of services and infrastructure. In generates high-quality research to better understand drivers of institutional performance in the public sector, improve implementation of policies in relevant fields, and promote informed and realistic solutions to the challenges of governance in South Africa.