TRADE & INDUSTRIAL POLICY STRATEGIES

POLICY BRIEF: 1/2020

The crisis at the state-owned enterprises

INTRODUCTION

This policy brief starts with an overview of the economic position of the national state-owned companies, in terms of their main socio-economic functions and size as well as their financial position and support from the state. A second section reviews their broader developmental outcomes against their mandates. The final section outlines their oversight structures in government.

ECONOMIC OUTCOMES

1. Functions

This review covers 25 national state-owned companies (SOCs) and development finance institutions (DFIs). Annexure 1 gives more detail on the criteria for selecting the entities included in the brief.

Table 1 provides an overview of the functions of the main public enterprises. They engage in three kinds of activity: supplying infrastructure and related services; producing a miscellany of other goods; and providing development finance. Annexure 2 lists each enterprise's asset size, 2019 profits and employment, and main functions.

2. The building blocks

As a group, the public enterprises account for a fifth of all capital stock but only a seventh of annual investment and around 1% of employment. Figures for investment and direct employment vastly understate their impact on the economy, however, since several provide inputs that are crucial for national growth and job creation.

The public enterprises vary greatly in size. In assets and employment, the group is dominated by the main infrastructure companies – Eskom, Sanral, Transnet and Prasa – and, if we consider managed funds, the Public Investment Corporation (PIC).

Table 1. Core SOC and DFI functions

INFRASTRUCTURE GOODS AND SERVICES	PRODUCTION OF OTHER GOODS OR SERVICES	DEVELOPMENT FINANCE INSTITUTION
Air Traffic and Navigation (manages air traffic)	Alexkor (diamond mining)	Development Bank of SA (DBSA) (infrastructure finance)
Airports Company of SA (manages national airports)	Armscor (procures armaments for state agencies)	Export Credit Insurance Corporation (ECIC) (insurance for exports and investments)
Broadband Infraco (provides broadband access)	Central Energy Fund (various energy activities)	Industrial Development Corporation (IDC) (industrial finance)
Eskom (electricity)	Denel (armaments)	Land Bank (agricultural finance)
Prasa (commuter rail)	Independent Development Trust (manages construction projects for government departments)	Public Investment Corporation (PIC) (manages social security funds)
SA Airways (national and international air travel)	SA Broadcasting Corporation (national broadcaster)	
SA Express Airways (domestic and regional air travel)	SA Nuclear (produces nuclear products)	
SA Post Office (postal services and savings bank)	Safcol (forestry)	
Sanral (national roads)		
Sentech (carrier for broadcasters)		
Telkom (ICT services)		
Transnet (rail transport)		

Trade & Industrial Policy Strategies (TIPS) is a research organisation that facilitates policy development and dialogue across three focus areas: trade and industrial policy, inequality and economic inclusion, and sustainable growth

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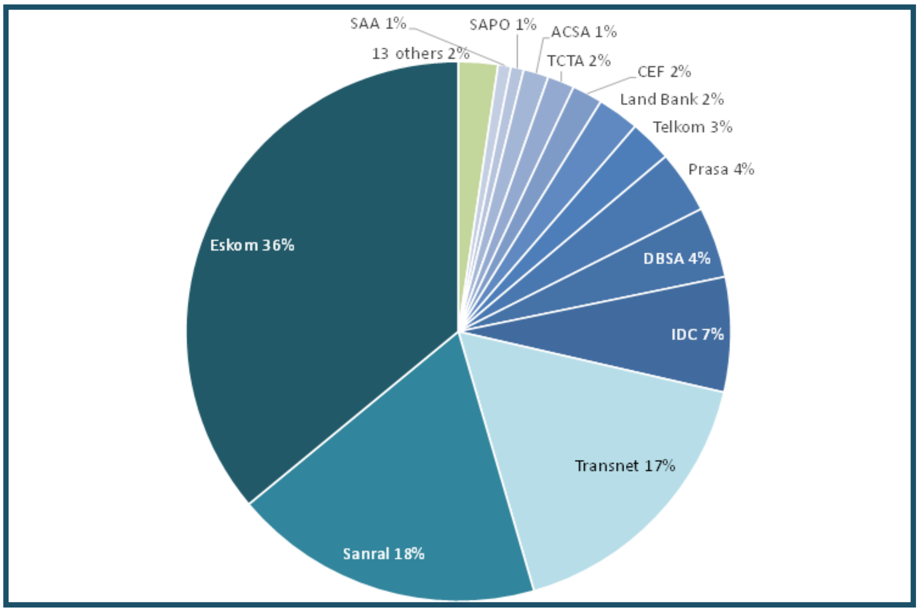
Graph 1. Assets by SOC and DFI (excluding PIC)(a), in billions of rand, 2019



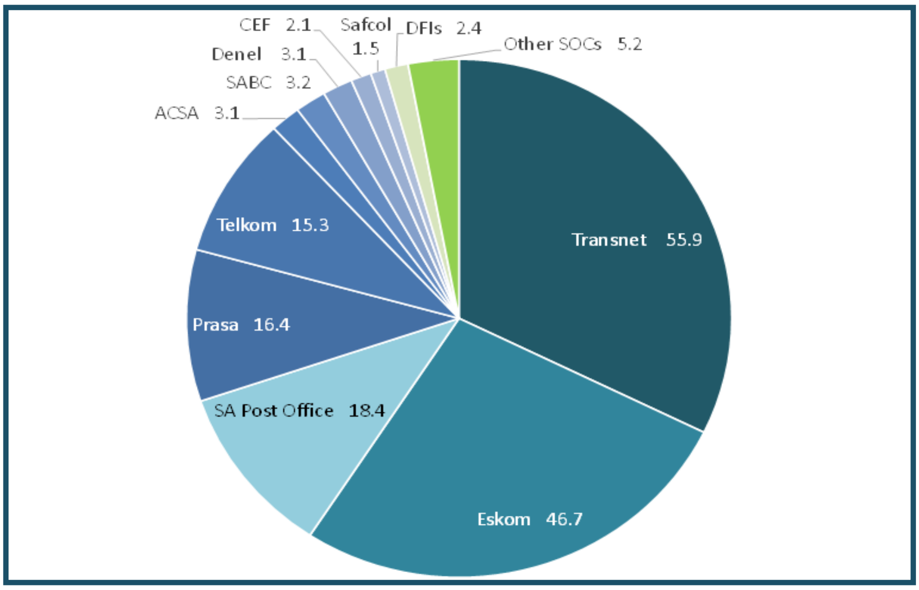
Note: (a) Excludes PIC because its own assets are only R3 billion, but it manages almost R2 trillion in assets, mostly from the Government Employees Pension Fund. *Source:* Most recent Annual Reports.

Graph 1 shows the distribution of assets among the public enterprises. It excludes the assets that the PIC invested on behalf of the Government Employees Pension Fund (GEPF) and other state agencies. At R2 trillion, these resources approximated the value of all the other enterprises put together. If they are excluded, Eskom, Sanral and Transnet alone held 70% of public enterprise assets.

In addition to their asset ownership, the DFIs support investment through equity holdings and long-term loans. Again, excluding the PIC's managed funds, in 2018 their total investments equalled around 5% of the gross domestic product (GDP). The PIC's managed funds equalled two thirds of the GDP. They financed around a fifth of government bonds (down from half in 1994), and close to a tenth of the equity on the Johannesburg Stock Exchange.

The public enterprises directly employ 175 000 people (Graph 2). That was tiny compared to their indirect impacts on South Africa's total employment of over 15 million. As with assets, their size in terms of jobs ranged widely, from around 50 000 at Transnet and Eskom to under a hundred at the ECIC. Transnet, Eskom, the Post Office and Prasa accounted for four fifths of the public enterprises' total employment. In contrast, Sanral largely contracted work to construction companies, so it directly employed only 400 people. It estimated that its contractors had around 13 000 workers in 2019.

Graph 2. Direct employment by SOCs and DFIs in thousands



Source: Most recent Annual Reports

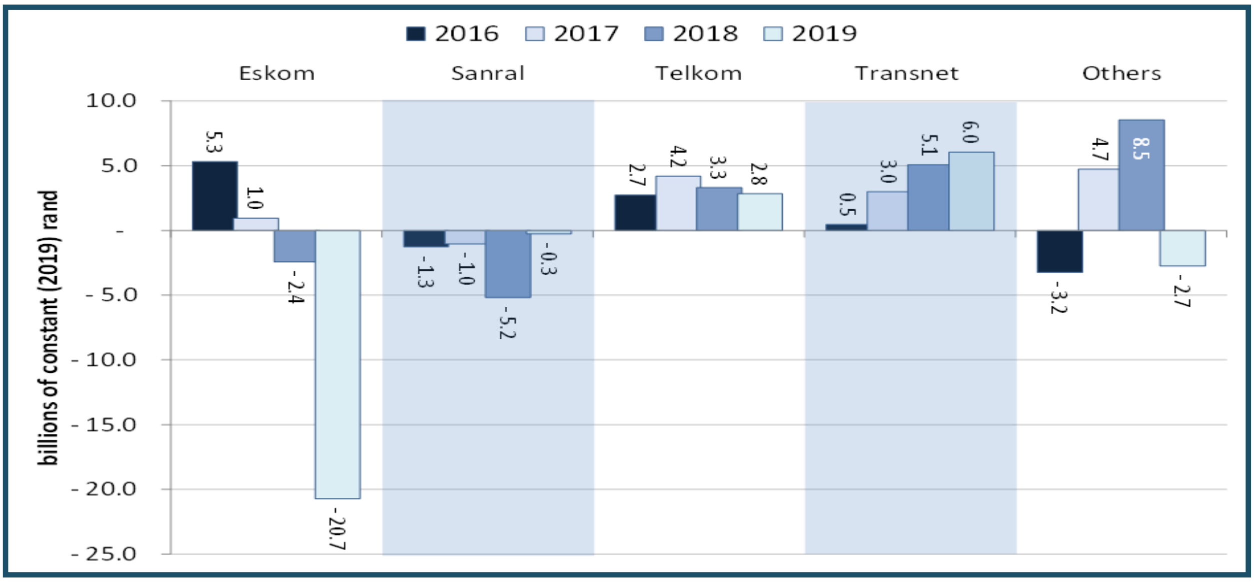
3. The financial crisis

In financial terms, the public enterprises saw a sharp decline in their performance from 2015. That reflected the broader economic slowdown, as metals and coal prices hit a low and South African exports dropped. In these circumstances, public enterprises as a group suffered falling revenues. They also had to write down some assets because the expected demand did not materialise.

As a group, in 2018/19 the national public enterprises reported R15 billion in losses, with a rate of return on assets of -0,7%. Eskom alone lost R20 billion. Sanral has also made continuous losses, mainly because motorists mostly did not pay the tolls on the Gauteng freeways while Sanral still had to service debt incurred to improve them. In contrast, Transnet has seen rapidly rising profits over the past four years (Graph 3).

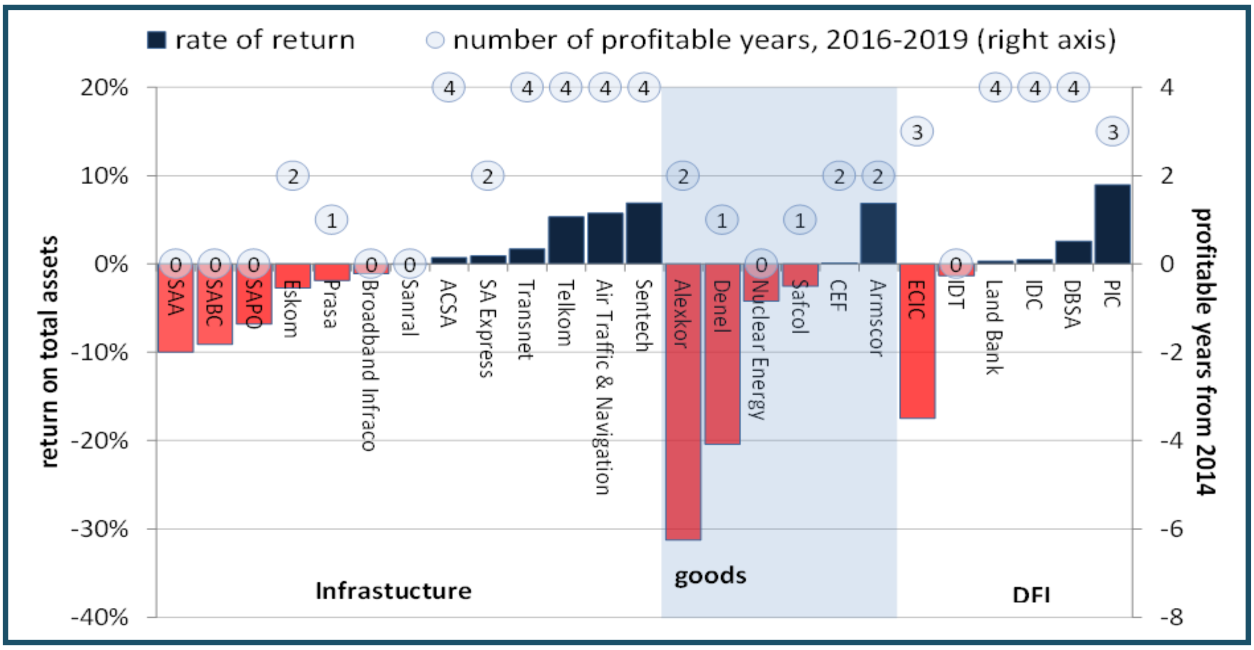
Graph 4 provides information on the financial position of all the public enterprises reviewed. From 2016 to 2019, 15 out of the 25 companies made losses in at least two years, and seven made losses in all four. In late 2019, South African Airways (SAA) was placed in business rescue and Alexkor was under administration because it no longer qualified as a going concern. SA Express has not published an annual report since 2017, but it was apparently piling up losses.

Graph 3. Profits and losses of the public enterprises, 2016 to 2019



Source: Most recent Annual Reports

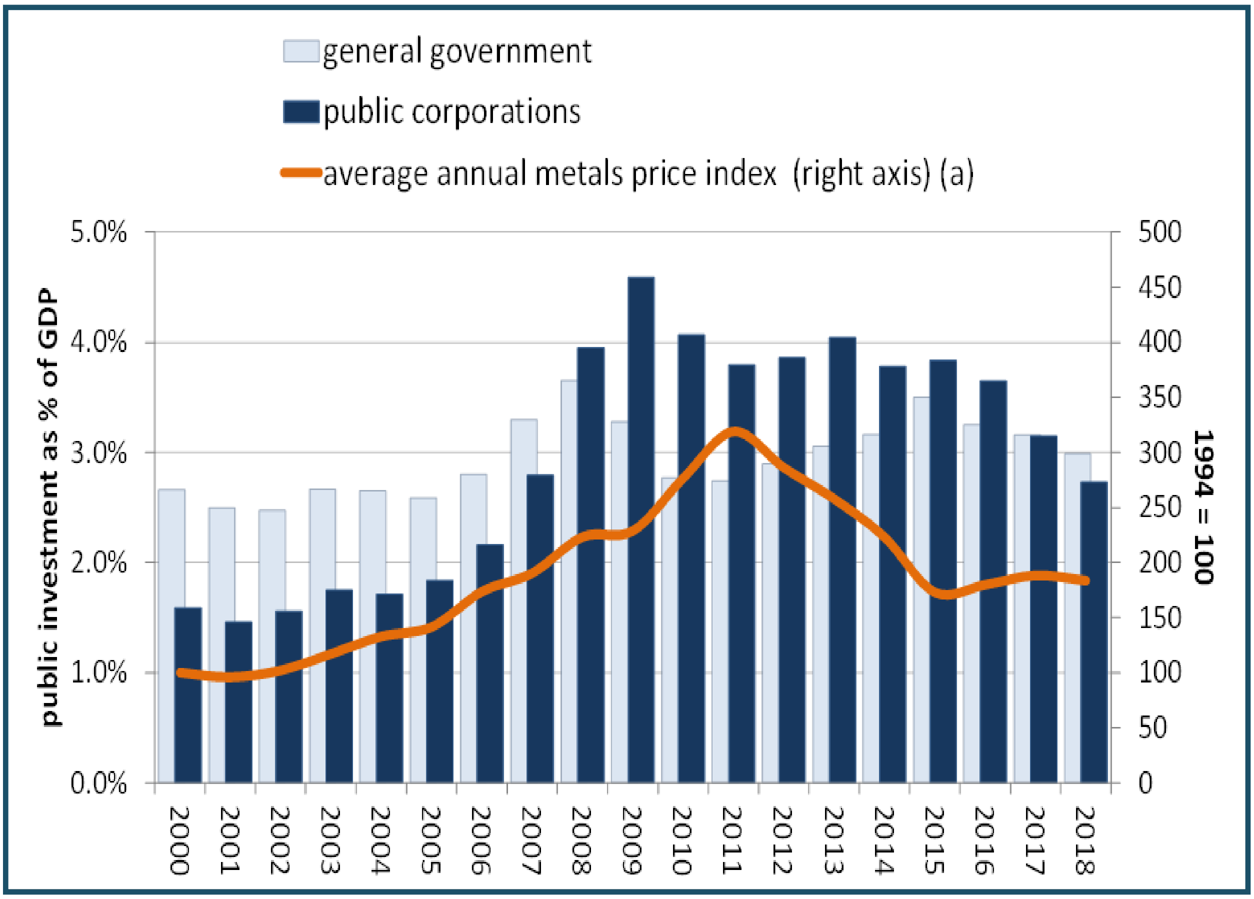
Graph 4. Rate of return on total assets in 2018/9 (a) and number of profitable years



*Note: (*a) 2016/17 reports for Broadband Infraco, SAPO, SAA, SA Broadcasting Corporation (SABC), Central Energy Fund (CEF), Denel, Alexkor, NECSA, NEF, Safcol and the State Diamond Trader; 2017/8 for all others. *Source:* Latest published Annual Reports for each enterprise.

Overall, the public enterprises' investments mostly facilitated growth in established industries, especially in mining and auto, rather than driving economic diversification

Graph 5. Growth in government consumption and investment, 2011 to 2019, year to second quarter



Note: (a) Annual average of monthly international prices in U.S. dollars for coal, iron ore, gold and platinum, weighted by share of each commodity in South Africa's exports of all four commodities. *Source:* Investment as percentage of GDP calculated from South African Reserve Bank. Interactive dataset. Downloaded from www.resbank.co.za in December 2019. Price index calculated from monthly data from Index Mundi for South African coal exports and iron ore c.f.r. to China. Downloaded from www.indexmundi.com in December 2019, and Kitco, historical data on platinum and gold London prices. Downloaded from www.kitco.com in December 2019.

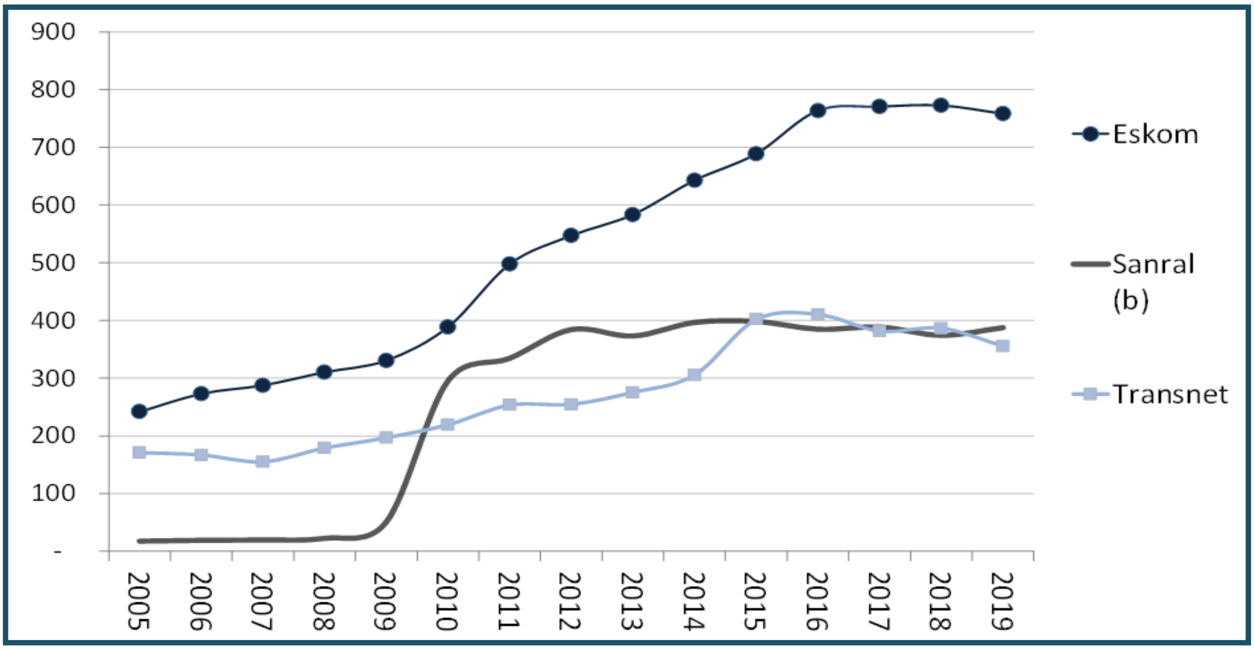
The public enterprises' financial performance can also be measured by their asset value over time. That in turn largely reflects the trends in their investment. When international commodity prices were high, the public enterprises rapidly increased their investments and consequently their capital stock. They aimed to meet the demands of the growing economy and specifically the mines and refineries, and found it easy to get credit. From 2015, however, the economy slowed and their investments also tended to stagnate. Moreover, they faced the burden of paying off the interest on earlier loans while their revenues stagnated. In short, the public enterprises' investments were largely pro-cyclical (see Graph 5).

Overall, the public enterprises investments' mostly facilitated growth in established industries, especially in mining and auto, rather than driving economic diversification. Of course, reliable and affordable infrastructure assisted all of the economy, but there was only limited focus on establishing new services in forms and areas that would facilitate new activities, small business, rural development, or township enterprises.

Large new investments in electricity, roads and rail over the past 15 years mainly, although by no means exclusively, facilitated expansion in the mines and refineries. A partial exception was Transnet's provision of specialised roll-on, roll-off facilities for auto manufacturing, which underpinned the industry's extraordinary growth over the past 20 years.

As a group, the public enterprises saw a decline in the value of their assets in real terms from 2015. Most of the losses resulted because Transnet, Sanral and Eskom all wrote down assets on a significant scale.

Graph 6. Transnet, Sanral and Eskom assets in constant (2019) rand (a), 2005 to 2019



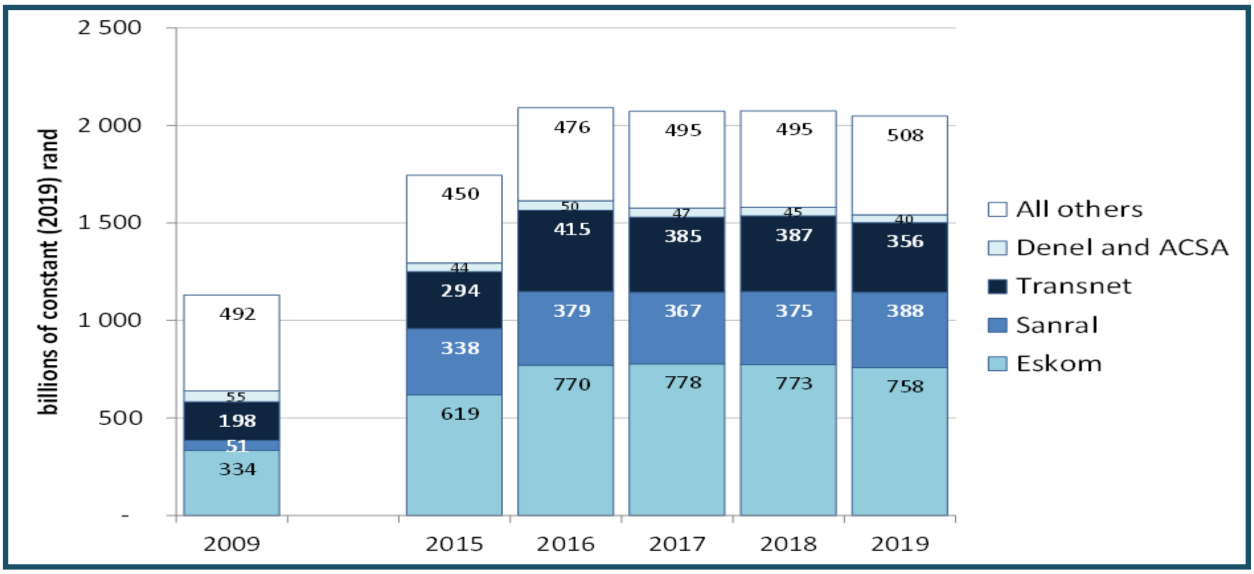
Notes: (a) Deflated with CPI for March, rebased to 2019. (b) Sanral apparently did not include older assets on non-toll roads. *Source:* Annual Reports for relevant years.

As Graph 6 shows, Transnet wrote off R55 billion in assets, in constant 2019 rand terms, from 2015 to 2019. The write offs reflected its valuation method, which took into account the fall in returns on its investments because of slower demand from 2015. Sanral wrote off R11 billion in assets from 2015 to 2019, mostly because it did not make the anticipated income from the Gauteng toll roads. Eskom only wrote off depreciated assets, irrespective of returns or demand. It reported a decline in its total capital stock of R14.5 billion from 2018 to 2019.

If Eskom had written off assets at the same rate as Transnet, the value of its holdings would have fallen by R100 billion. Instead of reducing the value it placed on assets that were not fully used, however, it sought to increase its rate of return by raising its tariffs at close to 10% above inflation despite falling demand.

Although they were relatively small, Denel and the Airports Company of South Africa (ACSA) reported even sharper declines in the value of their assets. They wrote off R10 billion, or 20%, in constant rand terms from 2016 to 2019. SA Nuclear, SAA and SA Express could not finalise financial statements for 2018/19, but they likely also saw a decline in their net worth. Excluding these companies, the collective assets of the public enterprises, as reported in their annual reports, climbed 4.6% from 2016 to 2019, or R40 billion in constant 2019 rand (see Graph 7).

Graph 7. The value of public enterprises' assets, year to March, 2016 to 2019



Note: (a) Deflated with CPI for March, rebased to 2019. *Source:* Annual Reports for relevant years.

The major SOCs faced escalating financing costs in the late 2010s, especially at Eskom and Transnet (see Graph 8) Figures were not available for SAA, but its losses mean it probably faced an escalating debt service burden. In some cases, debt service costs constituted a major factor behind reported losses. Eskom alone paid R25 billion in finance costs in 2018/19, which was R5 billion more than its reported losses in that year. Sanral paid R3 billion, compared to losses of R260 million.

In contrast, although Transnet paid R11 billion, it nonetheless made a profit. For all the other SOCs combined (excluding SAA), debt service came to R4 billion in 2018/19, which was four times their joint losses in that year.

The increase in the SOCs' debt-service costs arose from debt incurred primarily to finance investments during the global metals price boom. Repayment would normally be financed either from revenues on the project or because it would stimulate overall growth, in turn increasing revenues for both the public enterprises and the government. Instead, the slowdown in the economy, and especially mining, after metals prices crashed from 2011 meant that the revenues that were supposed to pay for the new projects often did not fully materialise. The financing burden also grew where the new projects suffered from unnecessary escalations in costs, delays or faulty performance on completion, due to a combination of poor procurement practices, inefficiency, poor design and/or corruption.

Finally, the past decade saw growing corruption in the public enterprises. The biggest sums were associated with the major procurement programmes arising from large-scale investments, notably in railroad rolling stock and electricity plants, as well as coal procurement by Eskom.

For users, corruption brought worse services and higher tariffs as well as deteriorating financial results. In some cases, it led to the adoption of faulty technologies and lower levels of local procurement as well as inflated costs. For instance, it reportedly meant Eskom purchased lower quality coal, which in turn contributed to equipment breakdowns, and to lower quality locomotives at Transnet.

4. State financing

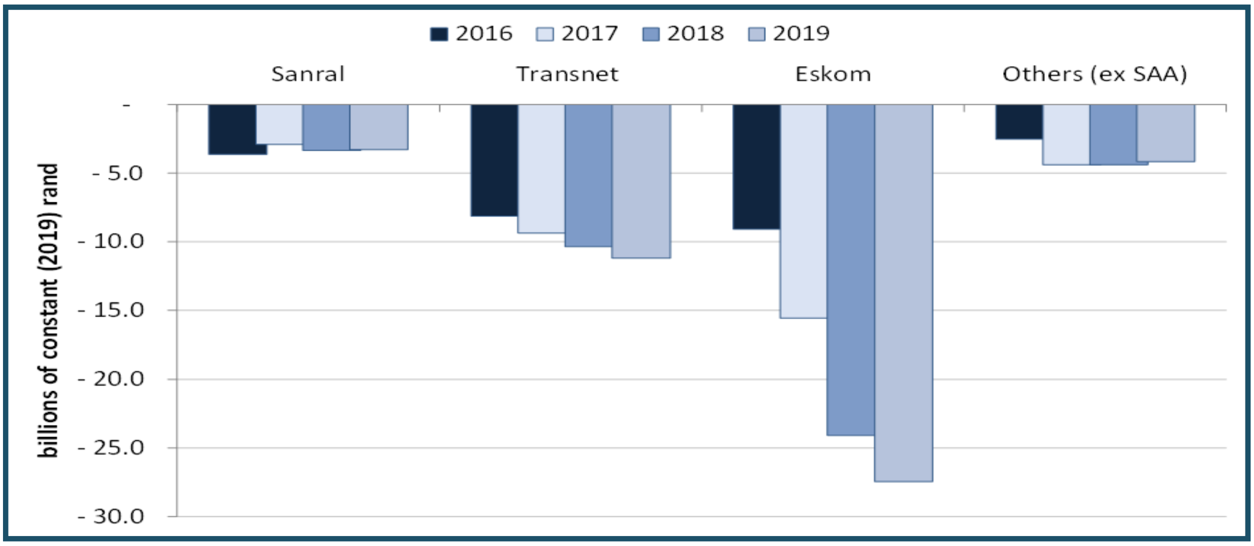
The public enterprises' financial position can also be understood in terms of the cost to the state, in the form of transfers from the budget and guarantees for borrowing. These costs should be weighed against the benefits that the state obtains when it supports the public enterprises. Frequently, however, these benefits are not reflected in revenue streams and may not have a money value at all. It is difficult to put a price tag on measures to avoid loadshedding or improve security on commuter rail.

Analysis of the financial costs to the state points to the disproportionate weight of Eskom on government resources, and to the importance of transport subsidies. As shown in Graph 9 on page 7, Eskom escalated its share in the national debt and budget in recent years. In contrast, the other national public enterprises declined as a percentage of both state spending and debt guarantees.

In constant 2019 rand, budget transfers and subsidies to the public enterprises stabilised at R45 billion in the late 2010s, but were projected to climb to R65 billion from 2019/20. The budget did not present these payments in aggregate form, but rather distributed across the votes of the relevant departments. In functional terms, they fell into two categories: long-term planned funding for socio-economic mandates, and assistance with unplanned losses.

The state has long provided annual subsidies for public enterprises to provide services for low-income

Graph 8. Financing costs for SOCs in constant (2019) rand (a), year to March, 2016 to 2019



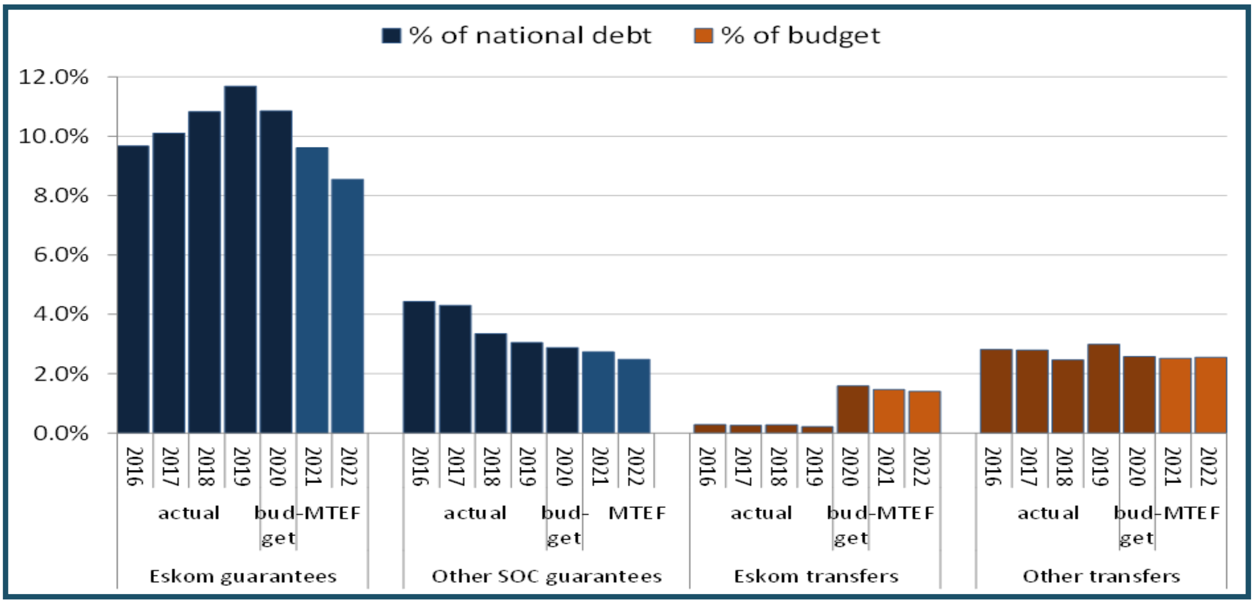
Note: (a) Deflated with CPI for March, rebased to 2019. *Source:* Annual Reports for relevant years.

communities and to promote inclusive industrialisation. In the late 2010s, two thirds of these planned subsidies went to Prasa and Sanral. Subsidies to Prasa supported commuter transport, a critical service to mitigate the effects of apartheid spatial planning. Prasa operated, however, almost exclusively in Cape Town, Johannesburg and Tshwane. Subsidies to Sanral aimed to maintain and improve non-toll roads, financed by the petrol tax. Eskom's electrification programme got another tenth of all subsidies to public enterprises. The remaining, much smaller, sums went to the Industrial Development Corporation (IDC) and Land Bank to reduce the cost of borrowing or investment for strategic industries or enterprises, for instance small businesses and agro-processing; Armscor, for defence procurement; and SA Nuclear, to deal with hazardous waste and produce medical products.

In addition, the state periodically provided large lump sums to address unplanned losses or to support restructuring. It budgeted R23 billion a year in nominal rand from 2019/20 to 2022/23 for Eskom's restructuring. In 2018/19, it used R6 billion to increase equity at SAA and SA Express. It also provided resources to Sanral to cover losses arising from the impasse around tolls on the Gauteng freeways.

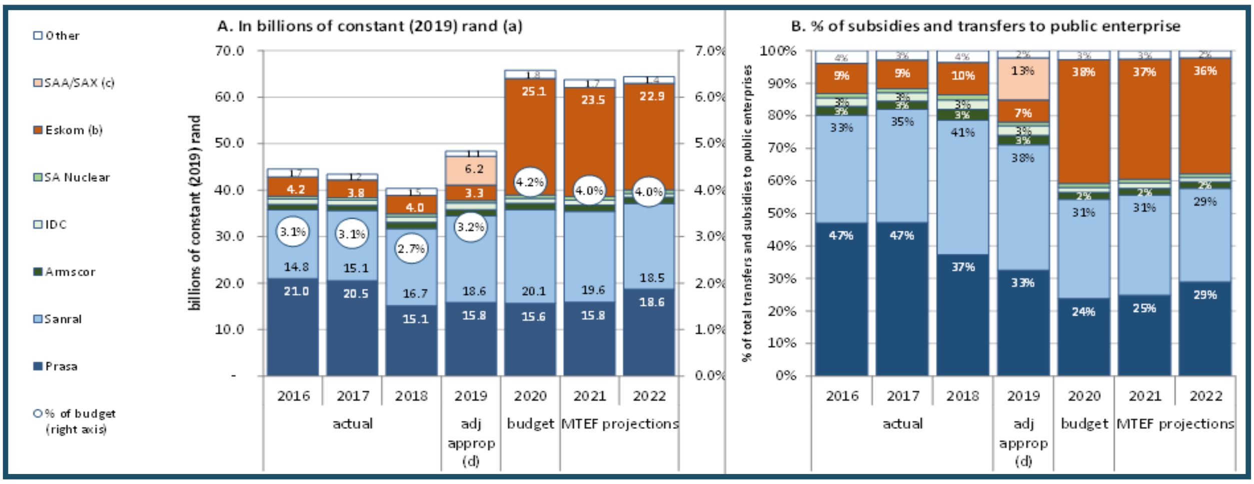
Graph 10 shows subsidies and transfers by company.

Graph 9. Eskom and other public enterprises' share in net national debt commitments and in total government expenditure, year to March, actual from 2016 to 2019 and



Source: Calculated from National Treasury. *Estimates of National Expenditure 2019/20.* Print version and excel spreadsheets. Pretoria.

Graph 10. Budgeted transfers and subsidies by public enterprise, in billions of constant 2019 rand (a) and as a percentage of total budgeted for public enterprises, year to March (actual 2016 to 2019 and budget or Medium Term Economic Framework (MTEF) projections 2020 to 2022)



Notes: (a) Deflated with March CPI rebased to 2019. (b) Transfers before 2019 for electrification; after 2019 for restructuring. (c) The 2019 figure for SAA and SA Express reflects the once-off purchase of shares to stabilise them in 2019. *Source:* Calculated from National Treasury. *Estimates of National Expenditure 2019/20.* Print version and excel spreadsheets. Downloaded from www.treasury.gov.za in December 2019.

In practice, many public enterprises did not have well-defined developmental mandates for their productive activities

Government guarantees for public enterprises' borrowing, which National Treasury counted as part as of the total national debt, were substantially larger than the subsidies. Again, they went disproportionately to Eskom (Graph 11). Like subsidies and transfers, the guaranteed debt had two functions. First, it financed investments that were expected to generate increased revenues over time either directly, as with toll roads or electricity sales, or indirectly, by raising productivity more broadly. Eskom's debt rose to over half the total guaranteed debt after 2008, as it began to invest in the new Medupi and Kusile power plants. Second, public enterprises borrowed when they made unplanned losses, as in the case of SAA and likely some recent Eskom debt.

5. Summary and conclusions

An overview of the public enterprises points to their great diversity in functions – distributed across infrastructure provision; an eclectic mix of goods and services; and development finance – as well as size and financial outcomes. Overall, their financial performance has been mediocre at best, with a particularly sharp downturn in 2019, again led by Eskom. Here too, however, substantial diversity emerges, with Transnet being significantly more financially responsible than its peers.

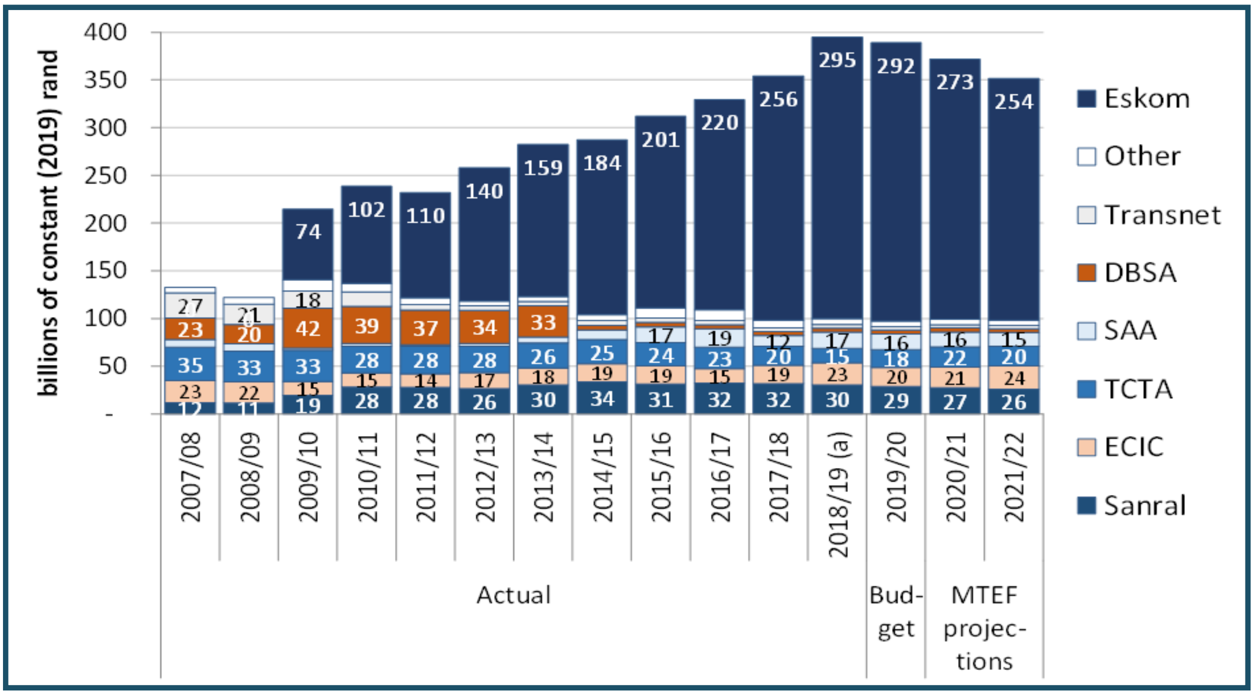
SOCIO-ECONOMIC AIMS AND OUTCOMES

Public enterprises are primarily expected to contribute on the one hand to industrialisation, with reduced dependence on exports from the mining value chain, and on the other to faster growth in decent work and small business; increasingly representative ownership and control; and rising living standards. In particular, as a group they are expected to achieve the following.

To provide infrastructure and financing that are both adequate and affordable enough to support business growth, especially where it would generate employment. For infrastructure in particular, this involves finding a balance between improvements in quality and the increase in user fees required to achieve them. Because SOCs are often effectively monopoly suppliers, they often find it difficult to identify demand in advance, which can lead to over investment in order to achieve "world class" quality at a cost that users argue they cannot afford.

In practice, expansion in SOC investment during the metals price boom was financed in large part by above-inflation increases in tariffs for infrastructure inputs, particularly for electricity, as Graph 12 on page 9 shows. In real terms, electricity tariffs almost tripled from 2008 to 2019.

Graph 11. Government-guaranteed debt of public enterprises, year to March, in constant (2019) rand (a)



Note: (a) Deflated with March CPI rebased to 2019. *Source:* Calculated from National Treasury. *Budget Review 2019/20.* Statistical Annex. Table 11. Excel spreadsheet. Downloaded from www.treasury.gov.za December 2019.

Water tariffs climbed over 60% In the same period, while Transnet rail freight rose 20%. When export prices slumped, companies often found that the higher tariffs undermined their competitiveness, leading to a fall in demand for electricity and write offs for some rail assets.

To sustain high levels of public investment in projects that would support inclusive growth. In effect, as industrial policy requires, public enterprises should invest ahead of the market to make it possible for new projects to emerge. This role necessarily increases the risk compared to private-sector imperatives, since it requires public investors to identify areas of potential growth rather than simply serving established business with incremental improvements.

To support a gradual move away from dependence on commodity exports, particularly ores and metals, toward manufacturing, advanced agriculture and value-adding services. As with efforts to promote inclusive growth, this requires innovative and therefore riskier investments.

To assist in improving infrastructure in historically underserved communities (although most national SOCs and DFIs provide bulk services to municipalities and businesses, rather than serving households directly). Again, if the infrastructure inputs are unaffordable, the benefits will be limited irrespective of improvements in quality.

To enhance the ecosystem for small businesses and co-operatives and more broadly to increase opportunities for historically excluded and vulnerable groups, especially black people, women and youth. The main way to achieve this aim is to provide lower-cost, higher-quality infrastructure and funding designed to serve smaller businesses especially in townships and under-served rural areas. Local procurement can also play a role, but not if it leads to significantly higher costs or lower quality in the public enterprises' provision of goods and services.

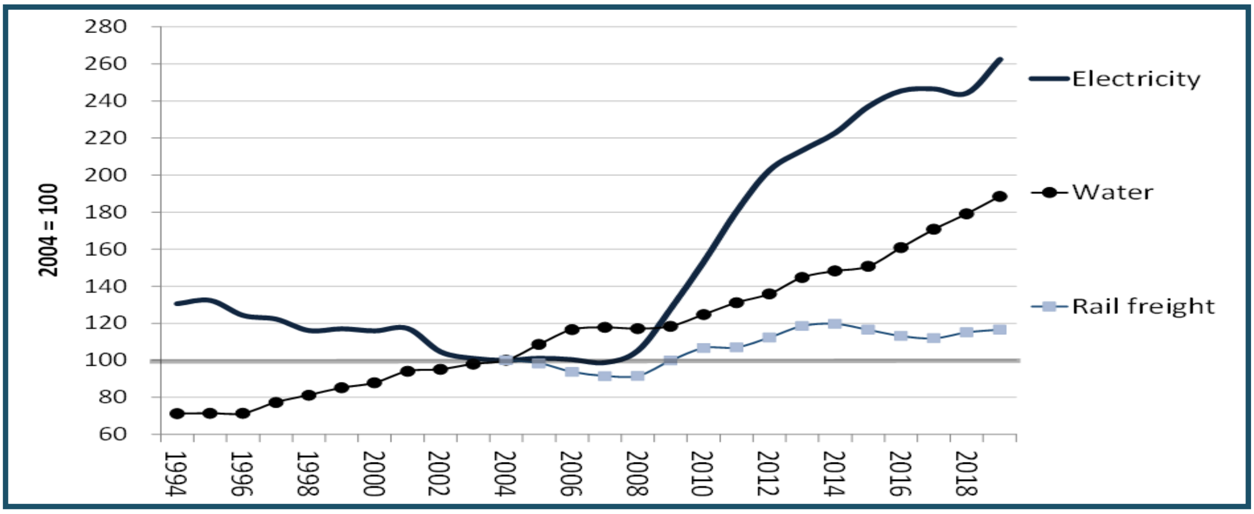
To promote a greener and more sustainable economy. Important roles for the public enterprises in this context include shifting away from coal-based energy and more broadly dependence on the mining value chain; moving freight from road to rail; and improving public transport.

To maintain their own financial sustainability. Their operations may require planned subsidies to help meet developmental mandates, but should not make sustained unplanned losses or see continually rising costs due to inefficiency or corruption.

State-owned enterprises are expected to achieve these outcomes primarily through the goods and services they produce. They also influence socio-economic development through their procurement especially of capital goods; innovation and skills development; and hiring. These effects, however, necessarily have a far smaller impact on socio-economic development than their core functions.

In practice, many public enterprises did not have well-defined developmental mandates for their productive activities. Table 2 on page 10 indicates the potential developmental value add compared to actual non-financial outcomes for 12 major entities. It finds that only four had clearly defined developmental mandates. The main outputs of the entities and their financial position are included for context.

Graph 12. Indices of electricity, water and rail freight price changes in constant rand (a), 1994 to 2018, 2004=100



Note: Deflated with CPI for November. Figures for water and rail are year to November; for rail freight, year to March. *Source:* Electricity and water calculated from Statistics South Africa. Producer Price Index. Series from 1990 to 2019. Excel spreadsheet. Series for electricity and water chained for different time periods. Transnet freight rail calculated as average revenue per tonne from information on rail revenue and freight carried in tonnes from Annual Reports for relevant year.

Table 2. Potential developmental value add, actual non-financial outcomes and clarity of mandate of some major public enterprises, 2019

NAME	MAIN OUTPUTS	FINANCES	POTENTIAL DEVELOPMENTAL VALUE ADD	ACTUAL NON-FINANCIAL OUTCOMES	CLARITY OF MANDATE
Eskom	Generates around 90% of South African electricity, mostly from coal, and manages the national grid.	Substantial losses in past two years.	Provide affordable, reliable electricity, which is critical for the economy as a whole. Invest to meet future demand. Help shift away from coal in order to reduce emissions, cut costs and avoid international trade challenges.	Sustained loadshedding in three of past five years even though electricity demand has dropped 4% (and Eskom's demand has fallen 10%) since 2010. Cost of electricity has doubled in real terms since 2008, more double-digit increases for next few years.	Notes both quality and affordability in aims, but no KPIs for affordability.
Transnet	Provides rail freight as well as pipeline and port services. In the late 2010s, bulk metals and coal accounted for around 60% of its total freight shipments by weight.	Sound, but has written down assets on a large scale.	Efficient, affordable rail freight and port services especially to promote diversification into manufacturing and agriculture. Invest to meet future demand. Help shift freight from road to rail.	Substantial improvement in efficiency without much increase in tariffs over past ten years Investments largely to promote exports of ores and coal, which in some cases reduces scope for local processing Limited services for agriculture Containers cost more than bulk, which arguably undermines local manufacturing compared to mining.	Annual Report refers to efficiency, affordability and road to rail, but not diversification; business model depends on profits from low-cost bulk freight.
Sanral	Maintains and improves the designated national road network.	Losses in past four years.	Quality, affordable national roads. Investment to meet future demand. Promote public transport and shift of freight from road to rail.	National roads are world class. Conflict around Gauteng toll roads as users saw originally proposed tariffs as unaffordable Not clear if or how Sanral promotes road to rail or public transport.	No reference to affordability.

NAME	MAIN OUTPUTS	FINANCES	POTENTIAL DEVELOPMENTAL VALUE ADD	ACTUAL NON-FINANCIAL OUTCOMES	CLARITY OF MANDATE
IDC	Provides industrial finance through loans and investment.	Sound	Provide funds to promote inclusive industrialisation. Efficient and responsive services especially to small and emerging business.	In constant rand, loans and investments climbed from R100 billion in 2006 to R140 billion in 2014, but fell to R110 billion in 2018 mostly due to decline in revenues from mining value chain with end of the international boom. Significant effort to promote diversification but largest investments still in mining value chain and established companies.	Clearly defined in mission
DBSA	Mobilises development finance principally for infrastructure in South Africa and the region.	Sound	Financing and capacity support for municipalities, especially for historically under-served communities.	Share of lending going to under-resourced areas declined from 2015.	KPIs give limited weight to serving poor communities
Prasa	Provides commuter rail in Cape Town, Johannesburg and Tshwane, and to a lesser extent eThekwini.	Poor although heavily subsidised	Integrated, affordable, reliable and safe commuter transport. Investment to meet future demand.	Only serves around 4% of commuters but gets 25% of transport subsidies Trains are unreliable, unsafe and often unpleasant, and ridership has fallen consistently over past decade.	Not clear how rail fits into longer-term commuter strategy.
Land Bank	Financial support for commercial and emerging farmers.	Sound	Support agricultural production to sustain domestic food security and exports Promote more equitable and representative ownership in agriculture.	Provides over a quarter of all loans to agriculture. Most loans go to established farmers but has been able to provide some support to black emerging and commercial farmers. Cannot promote land reform or support very small producers.	Difficulty of balancing support for growth in agriculture with transformation

NAME	MAIN OUTPUTS	FINANCES	POTENTIAL DEVELOPMENTAL VALUE ADD	ACTUAL NON-FINANCIAL OUTCOMES	CLARITY OF MANDATE
Central Energy Fund	Various energy-related products and services including PetroSA (which owns Mossgas and the Strategic Fuel Fund.)	Poor	Arose before 1994 to circumvent oil sanctions, so role in democratic SA in hard to define.	Unauthorised sale of strategic oil fund leading to criminal investigation. Mossgas winding down as runs out of gas; wrote off billions in unsuccessful efforts to find more feedstock.	Entirely unclear.
ACSA	Owns and operates the nine principal SA airports.	Sound	Provide affordable, efficient airport services. Invest to meet future demand.	Airport services are efficient and provide world class facilities, but based on high fees for airlines.	No mention of affordability.
SA Post Office (SAPO)	Provides mail and courier services, operates a savings bank and transfers social grants.	Poor	Efficient and reliable transfer of social grants to 8 million beneficiaries (around half of the total) Provide mail services and savings facilities especially to low-income and rural households.	Took over grants transfer in 2019 with some hiccups, which affect highly vulnerable people. Mail services in decline.	Does not articulate developmen-tal aims other than improving financial inclusion by opening more accounts.
SAA	Provides full-service domestic and international air transport; low-cost services through Mango; air freight; and airline maintenance and catering.	Very poor	Promote international tourism, business and social engagement through affordable, safe and efficient air transport Enable air transport to secondary centres that might not be profitable enough for private carriers.	Costs and prices are higher than for competitors in most cases, except for Mango, which is an obstacle to tourist, business or social travel domestically and internationally. Provides direct travel to some destinations, especially other African countries, that other carriers neglect.	Does not articulate socio-economic aims or indicate its value add for society compared to private carriers.

NAME	MAIN OUTPUTS	FINANCES	POTENTIAL DEVELOPMENTAL VALUE ADD	ACTUAL NON-FINANCIAL OUTCOMES	CLARITY OF MANDATE
Export Credit Insurance Corp	Provides credit insurance for South African exporters and some major investment projects in the region.	Loss in 2018/19 but no pattern of losses.	Enable South African exporters to compete with foreign companies that get state credit and insurance especially for capital goods exports.	Coverage has fluctuated but rose from around R20 billion in 2005 to R25 billion in 2018 in constant 2018 rand terms Covers only around 0.005% of SA exports, which is far lower than many competitor countries.	Well defined
Denel	Manufac-tures armaments for domestic use and export, largely to the Middle East.	Very poor	Established under apartheid to circumvent arms sanctions, and value add for democratic SA is hard to define. Retains significant technological expertise and capacity, but is it the best way for government to support technological advances given unsustainable business model?	Has developed a limited range of internationally competitive products. Limited domestic demand means it cannot easily compete with larger foreign competitors that can reach larger economies of scale. Focused on sales in Middle East, with ethical as well as financial challenges (unable to deliver on contracts, leading to severe cash-flow issues).	Very unclear
SA Nuclear Energy	Uranium enrichment for domestic energy and medical use and manu-facture of equipment for electricity generation for SA and foreign markets, plus management of nuclear waste.	Very poor	Maintain safety of nuclear facilities. Avoid loss of expertise and capacity. Note: Developmental role depends on national strategy on nuclear power.	Regulatory role appears sound. Has had some success exporting uranium-based medical inputs and electricity-generation equipment. Financial difficulties largely due to over-expansion in anticipation of major nuclear build programme that then did not materialise.	Very unclear, largely because of lack of clarity about future of nuclear programme overall.

NAME	MAIN OUTPUTS	FINANCES	POTENTIAL DEVELOPMENTAL VALUE ADD	ACTUAL NON-FINANCIAL OUTCOMES	CLARITY OF MANDATE
SABC	Operates television and radio stations funded through a combination of licencing fees and advertising sales.	Poor	Provide news and entertainment geared especially to historically excluded. Give a voice to the voiceless and build national South African culture and engagement.	Local broadcasts largely reflect international norms rather than actual local realities, mostly displaying very high-income lifestyles. News has been under-resourced, so unable to undertake investigations or sustain coverage in the public interest. Some evidence of political interference and bias.	Very unclear except for political independence.
PIC	Manages funds for public entities, with 85% from GEPF.	Sound	Use managed funds, in alignment with mandates from investors, to promote economic diversification, black industrialists and broader ownership.	Non-commercial "impact" investing accounts for small share of total and includes virtually no agriculture or mining, or support for small producers. Explicitly saw SOCs as too risky for investment. Allegations of favouritism in investments.	Act amended early in 2019 to include job creation and industrialisation as objectives.
Alexkor	Mines mostly alluvial diamonds in the Richtersveld in the Northern Cape.	Very poor	Sustainable mining to promote development in the Richtersveld.	Richtersveld residents complain that they are largely excluded and disadvantaged by Alexkor mining activities.	Notes developmental role but does not list Richtersveld community as stakeholders.

Government's systems for monitoring and engaging with public enterprises are fragmented, focused largely on outputs rather than mandated outcomes

OVERSIGHT SYSTEMS

Government's systems for monitoring and engaging with public enterprises are fragmented; focused largely on outputs rather than mandated outcomes; and often associated with inconsistent responses. These shortcomings help explain the failure to define or meet developmental objectives as well as their at best inconsistent financial performance.

As Table 3 shows, public enterprises have divergent systems of oversight by national departments. The table reviews 13 enterprises that were either very large or very problematic. Half of them had a different shareholder from their main policy department.

Three of the enterprises in the table fall under the Department of Public Enterprise (DPE), out of six in its mandate, and another four under National Treasury (NT). Of these seven enterprises, six operated in a different policy area from their shareholder. An exception was the Development Bank of Southern Africa (DBSA), which fell under Treasury. In addition, most of the state-owned enterprises significantly affected the economic cluster because they provided critical infrastructure or financing, or had a profound impact on their suppliers. Save for the IDC, however, the economics departments had no formal role in their oversight. Finally, Eskom, Prasa, Sanral, Transnet and the DBSA operated largely in or through municipalities, which had virtually no say in setting their performance targets.

Shareholder departments were responsible for monitoring the public enterprises. For the SOCs that the Department of Public Enterprises (DPE) oversaw, it entered into shareholder compacts that included a range of financial and performance indicators. It appears that most other shareholder departments adopted a similar model, although the Department of Telecommunications and Postal Services did not publish any key performance indicators (KPIs) at all for Telkom.

In addition, the Public Finance Management Act (PFMA) required SOCs and DFIs to publish annual reports on the model of listed companies. These annual reports incorporated standard financial statements as well performance against selected KPIs from their shareholder compacts. The enterprises presented their annual reports to the relevant Portfolio Committees.

This monitoring system reflected the fragmented nature of oversight, leading to significant shortcomings in SOC and DFI governance.

First, there were no structures to ensure that shareholder departments engaged on shareholder compacts with other affected departments, much less with provincial or municipal governments. The resulting KPIs frequently did not reflect priority national outcomes. This shortcoming, among others, meant that public enterprise targets often did not reflect either the performance plans of policy departments or the Medium Term Strategic Framework (MTSF).

In many cases, enterprises' published KPIs did not support the mandates printed in their own annual reports. From around 2016, for instance, both Eskom and Transnet included lowering the cost of doing business in their mandates, but neither published specific KPIs to moderate their impact on producer costs.

Table 3. Oversight of priority SOCs and DFIs

COMPANY	SHARE-HOLDER	POLICY DEPARTMENT	OTHER DEPARTMENTS AFFECTED	OTHER SPHERES AFFECTED
Eskom	DPE	DOE	Economic departments; DEA	Municipalities
Sanral	NDOT	Same	Economic departments; DEA	Municipalities and provinces
Transnet	DPE	NDOT	the dti, DMR, DAFF	Municipalities and provinces
Prasa	NDOT	Same	DCOG, dti	Gauteng metros, Cape Town
SAA	NT	NDOT	Tourism	Municipalities with airports
CEF	DOE	Same	The dti	
Denel	DPE	Dti	Defence, DIRCO	
SABC	DOC	Same	GCIS	
SAPO	DTPS	Same	DSD	Provinces and municipalities
PIC	NT	Same	Economic departments	
IDC	EDD	Same	the dti, DSBD (oversees sefa)	
DBSA	NT	Same	DCOG	Municipalities
Land Bank	NT	DAFF	DRDLR	Provincial agriculture

The oversight system for many public enterprises set up parallel systems of authority and often excluded the most affected agencies and spheres of government.

Second, as noted, in six of the 13 enterprises analysed the oversight department was not directly affected by the operations of the enterprise. This disjuncture made it easier for enterprises to ignore policy directives and to forum shop. For instance, when a public enterprise made persistent losses, Treasury was affected but not the shareholder department; if it ignored local procurement requirements, the Department of Trade and Industry (the dti) saw the impact on manufacturing but the oversight and policy departments often only perceived reduced costs; where critical economic infrastructure was dysfunctional or overpriced, the economics departments heard from business and labour, but the shortcomings frequently had no direct effect on the work of the oversight and policy departments.

Third, none of the SOCs and DFIs published estimates of the expected external benefits from their operations. As a result, it was virtually impossible to determine if losses or low rates of return derived from fulfilment of national mandates or from inefficiency.

Fourth, the state as shareholder did not respond consistently when an enterprise failed to meet financial or operational targets. As shown in Graph 4 on page 3, many public enterprises did not make profits for several years in a row. At least until 2018, however, there appeared to be virtually no consequences for their leadership. Bonuses for executives as well as job security for managers and board members were largely delinked from the financial and operational performance of the enterprise. That said, the failure to clarify and cost developmental mandates made it difficult to distinguish between poor management, the burdens of meeting government directives, and economic factors beyond enterprise control.

It is instructive in this context to compare the use of financial KPIs by Eskom and Transnet, both of which were overseen by the DPE. Transnet set rigorous financial KPIs, including its gearing ratio, return on total assets and earnings before interest, tax, depreciation and amortisation (EBITDA). These KPIs helped it identify when the end of the commodity boom in 2011 reduced demand for new capacity from mining. As a result, it cut back on investments that were no longer viable. This approach likely contributed to slower investment and mining growth after 2011, but Transnet avoided stranded assets and a debt crisis. In contrast, Eskom appeared to treat poor financial returns as a problem for its customers and Treasury, to be dealt with through higher tariffs and/or subsidies. As a result, by the late 2010s its business model was no longer sustainable.

Finally, the monitoring and evaluation system was difficult for both political leaders and the public to access and understand. That in itself undermined accountability and democratic governance. Shareholder compacts were not published widely or in full, if at all. Moreover, the KPIs included in public enterprises' annual reports frequently related to narrow, technical outputs with no indication or quantification of how they would affect outcomes. In many cases, as when Transnet reported on average crane movements per hour, they were in fact associated with overarching aims – in this case, improving port efficiency. But they did little to facilitate oversight by outsiders.

Annual reports often obscured the extent of difficulties and state subsidies. For some of the most troubled enterprises, such as Alexkor, the most recent reports were available only as submissions to Parliamentary portfolio committees rather than on the entity's website. More seriously, public enterprises frequently reported in one year that they were profitable and operationally sound, only to plunge into deep losses in the next. Eskom made a modest profit in 2016/17, but lost over R2 billion in 2017/18 and R21 billion in 2018/19. Denel reported profits in the four years from 2014 to 2017. In 2018, however, it faced such severe cash-flow problems that its unions reported it could not meet its wage bill, and it had to delay its annual report due to irregularities. In 2018/19, it reported R1.7 billion in losses. Prasa restated its 2017/18 returns to move from a R1 billion loss to a R1.5 billion profit, which was a factor behind the auditor general's decision not to give an opinion on its financial statements.

In sum, the oversight system for many public enterprises set up parallel systems of authority and often excluded the most affected agencies and spheres of government. Their KPIs often did not help define, quantify or oversee core socio-economic mandates or adapt to changing economic circumstances. Oversight departments frequently did not react to financial or operational challenges until they reached crisis point. Reporting systems, including some public enterprises' annual reports, were at best opaque and at worst misleading. All of these circumstances enabled corruption on a large scale. Even more important, they meant that some public enterprises persisted with unworkable business models that entailed long-run losses, which they could not justify by pointing to well-defined developmental benefits.

ANNEXURE 1. DEFINING PUBLIC ENTERPRISE

The legal definition of state-owned enterprise is surprisingly murky. The Companies and Intellectual Property Commission (CIPC) registers entities as "state-owned companies" if the PFMA defines them as a "state-owned enterprise". But the PFMA does not actually refer to state-owned enterprises. Instead, it distinguishes between "government businesses", which are primarily self-funding, and other "public entities". It lists public entities in two schedules: Schedule 2 for "major public entities" (which are not defined) without separating out businesses; and Schedule 3 for others, which distinguishes government businesses from other public entities as well as national from provincial bodies.

This review includes all of the government businesses in Schedule 2 plus Sanral. Sanral is not listed as a business in the PFMA, but it relies on user fees to build and maintain toll roads, which make up about half its portfolio. Telkom is also included because the state owns 39%, although it is not managed as a state entity. Excluded, however, are the water boards and the TransCaledon Tunnel Authority; very small agencies and enterprises; and regulatory and research agencies like the South African Bureau of Standards and Mintek.

ANNEXURE 2. STATE-OWNED CORPORATIONS AND DEVELOPMENT FINANCE INSTITUTION ASSETS, PROFITS AND EMPLOYMENT IN 2019, AND MAIN FUNCTIONS

COMPANY	ASSETS (R BNS)	PROFITS (R BNS)	EMPLOYMENT	FUNCTIONS
Air Traffic & Navigation	3.3	0.19	1 260	Manages air traffic control.
Airports Company	31.5	0.23	3 110	Owns and operates the nine principal SA airports, with revenue from airline fees as well as retail and parking.
Alexkor	0.5	-0.15	1 090	Mines mostly alluvial diamonds in the Richtersveld in the Northern Cape.
Armscor	3.4	0.24	1 470	Procures arms for the SA National Defence Force and, if required, other government agencies (e.g. SA Police Service).
Broadband Infraco	1.3	-0.01	170	Builds on Eskom's fibre-optic network and shares in undersea cable to UK to expand broadband access.
Central Energy Fund	38.0	0.05	2110	Various energy-related products and services, including PetroSA and the Strategic Fuel Fund.
Denel	8.6	-1.70	3 010	Manufactures armaments for domestic use and export, largely to the Middle East.
Development Bank	89.2	2.28	600	Mobilises development finance principally for infrastructure in South Africa and the region.
Eskom	758.0	-20.72	46 670	Generates around 90% of South African electricity, mostly from coal, and manages the national grid.
Export Credit Insurance Corporation	9.6	-1.68	80	Provides credit insurance for South African exporters and some major investment projects in the region.
Independent Development Trust	2.0	-0.3	280	Manages infrastructure projects mostly for the Public Works Department, principally schools, hospitals and clinics, and court buildings.
Industrial Development Corporation	144.6	0.72	850	Provides industrial finance through loans and investment; owns Foskor, which historically was a key source of revenue.
Land Bank	52.4	0.17	490	Financial support for commercial and emerging farmers.

COMPANY	ASSETS (R BNS)	PROFITS (R BNS)	EMPLOYMENT	FUNCTIONS
Prasa	78.5	-1.50	16 350	Provides commuter rail in Cape Town, Johannesburg and Tshwane, and to a lesser extent eThekwini.
Public Investment Corporation	3.2 (a)	0.29	410	Manages funds for public entities, 85% of which comes from the Government Employees Pension Fund.
South African Broadcasting Corporation	5.3	-0.48	3 170	Operates television and radio stations funded through a combination of licensing fees and advertising sales.
SA Nuclear Energy (c)	6.9 (2018)	-0.3 (2018)	1 950	Uranium enrichment for domestic energy and medical use and manufacture of equipment for electricity generation for SA and foreign markets, plus management of nuclear waste.
South African Post Office	16.1	-1.1	18 360	Provides mail and courier services, operates a savings bank and transfers social grants through 1500 branches and 750 retail postal agencies.
Safcol	4.6	-0.12	1 550	Manages 18 forestry plantations covering almost 200 000 hectares, with two sawmills.
Sanral	387.7	-0.26	430	Maintains and improves the designated national road network (around 25 000 kilometres) funded through a combination of government subsidies and, on specified routes, tolls.
Sentech	2.6	0,18	530	Common carrier for licensed broadcasters, for which it provides infrastructure.
South African Airways	15.9 (2017)	-1.69 (2017)	5260	Provides full-service domestic and international air transport; low-cost services through Mango; air freight; and airline maintenance and catering.
Telkom	52.9	2.83	15 300	Provides ICT services; 39% state-owned.
Transnet	355.5	6.05	55 950	Provides rail freight as well as pipeline and port services. In the late 2010s, bulk metals and coal accounted for around 60% of its total freight shipments by weight.

Notes: (a) Rounded to nearest 50. From Annual Reports for Airports Company, Central Energy Fund, Development Bank, Eskom, the Industrial Development Corporation, Land Bank, Public Investment Corporation, Prasa; SA Airways; SA Broadcasting Corporation; Sanral; SA Post Office and Transnet. For other companies, figures are from Who Owns Whom notes on each company, and may date from before 2019. (b) No published annual reports since 2016.