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GROWING DEMAND FOR SERVICES IN MUNICIPAL SECTOR BUT FUNDING REMAINS A CHALLENGE

Considerable progress has been made in the municipal sector over the past decade in terms of the rollout of basic services, with key measures of service delivery and living standards having improved across all of South Africa's geographies particularly in larger urban areas.

This is according to Eyal Shevel, Head of Corporate and Local Authority Ratings at Global Credit Ratings (GCR), who says that in some ways, this success has fuelled the recent spate of service delivery protests.

"Ongoing urbanisation has seen growing indigent populations migrating to major city centres, driving the demand for basic services. This has placed increasing pressure on ageing infrastructure assets (requiring upgrade, rehabilitation or replacement)."

Despite the general improvement, Shevel says local authorities have not utilised resources in an efficient manner. "The level of fruitless and wasteful expenditure, though declining, remains unacceptably high, and employees often lack the skills to implement large and complex projects."

As such, he says the infrastructure backlogs remain significant. "While this is true across the country, performance by smaller municipalities in terms of operational efficiencies and infrastructure developments has been worse, as they are more acutely affected by funding constraints and the lack of skilled personal."

Shevel says what is further compounding this situation is the sluggish economic growth over the past two years. "Unemployment levels remain high and even within the employed sector of the economy, an increased level of financial distress is being reported."

Whilst the social welfare grants are distributed by national government, Shevel says most of the burden of providing everyday services such as water, sewerage and electricity to indigent populations falls on the municipalities. "The national government does provide grants to cover much of this expenditure, but municipalities also need to rely on internally generated revenue through the provision of services."

Shevel says municipalities have become increasingly pro-active in respect of their debtors' administration, but affordability issues are likely to affect both the debtors' performance and the demand for indigent services. "Having improved in the three

years to FYE2012, debtors performance has begun to deteriorate for local authorities as a whole, with substantial provisions having to be made for non-collection.”

“With fiscal indebtedness now approaching the levels last seen in the mid-1990s, capacity of government for further borrowing is constrained and could limit capital grant funding to municipalities beyond the medium term (to which central government is already committed),” explains Shevel.

Accordingly, Shevel says municipalities are increasingly expected to be self-sustaining in terms of servicing other residents and the rollout of new income generating fixed assets/infrastructure.

“Municipalities are also being forced to seek alternative sources of funding and borrow off their own balance sheets. The diversity of funding available to them has been bolstered by strong appetite from capital markets investors for different fixed income instruments, as well as from commercial banks seeking to lend to lower risk clients.”

“To date bond issuances have only been undertaken by four metros, but at least two more Metros are looking to inaugural bond issuances during 2014,” explains Shevel.

Apart from the other benefits, Shevel says accessing bank or capital market funding, has exposed municipalities to the more rigorous reporting standards required in the private sector.

“There has been vast improvement in terms of municipal reporting, and transparency, which in turn has bolstered the financial strength and sustainability of the municipalities.

“Nevertheless, there is a clear trend of improving service delivery from the municipal sector, if somewhat slower than can be achieved. This is very much in line with central governments mandate to create a self-sustaining municipal sector that is increasingly corporatized and efficiently operated,” concludes Shevel.