



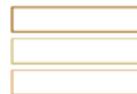
# PRESENTATION TO APPROPRIATIONS COMMITTEE

DPE and ESKOM  
12 June 2015



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Introduction

Cabinet approved support package

Conversion of the subordinated loan

Nersa selective reopener

Conclusion



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# Eskom management will primarily focus on 3 primary issues in the short term over the next 100 days

## Liquidity

Eskom will focus on its liquidity position to ensure financial viability

## Operational performance

Eskom will focus on improving operational performance by prioritizing critical maintenance, with the aim of doing maintenance without load-shedding

## Governance

The third issue of Governance will be dealt with by the CE and Board



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# In 2014 Eskom made an application to Government for a support package

Option Rank	Solution Option				Tradeoff						
	Capital Spend Rbn	% Eskom Savings Achieved	% Average Price increase 2015/16/17	Government Contribution Rbn	Impact on Credit Rating	Impact on Cash Flow	Affordability/ Competitiveness (Ave Price c/kWh Real by 2018)		Reasonable ROA by 2018		Long term sustainability
1	300	75	13 x 3	R50bn Equity	✓	✓	81	✓	4.70%	✗	✓
2	300	75	13 x 3	R38bn Equity	✓	✓	81	✓	3.70%	✗	✗
3	300	75	11 x 3	R55bn Equity	✓	✓	77	✓	2.40%	✗	✗
5	300	75	19 x 3	-	✓	✓	95	✗	7.7%	✓	✓
7	300	75	16,14,14	R16bn Equity	✓	✓	85	✗	4.70%	✗	✓
8	300	75	16,14,14	R30bn Equity	✓	✓	85	✗	4.80%	✗	✓
9	250	75	11 x 3	R15bn	✗	✓	77	✓	2.40%	✗	✗
Base Case	250	100	8 x 5	-	✗	✗	71	✓	1.10%	✗	✗



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# On 11 September 2014 Cabinet approved a R23bn equity support package for Eskom

## Tariffs

- Approved **support** for Eskom in applying for an **overall tariff increase** as **determined by NERSA** for the remainder of MYPD3
- The support takes into account the **R7.8bn** already approved by Nersa in terms of the **regulatory clearing account**

## Equity

- An **equity injection of R23bn** will be given to Eskom to help **relieve the impact on electricity customers**

## Subordinated loan and debt

- **Conversion of the subordinated loan to equity** was granted
- In addition to R200bn debt in MYPD3, Eskom will have to **raise additional debt of R52bn**

## Eskom efficiency

- Eskom will implement **cost containment program**
- **Effective manage the build programme**
- Eskom should **not invest in future coal mines**
- **No provision to be made for the additional R50bn Capex requirement**
- Eskom must **better manage its working capital**
- Eskom needs to ensure that **effective maintenance of its generation plants** is carried out and **efficient procurement** is achieved, amongst others



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SOURCE: *Cabinet-Approved Package to Support a Strong Eskom and the Attainment of Energy Security* - Letter from the Minister of Public Enterprises to the Eskom Chairperson, 16-Sep-2014



# Early projections indicate that the Eskom financial position is under pressure

## Key performance metrics updated based on Government support package

KEY FINANCIAL PERFORMANCE METRICS		Investment grade	Investment				
			'13/14	'14/15	'15/16	'16/17	'17/18
Profit after tax	R'mill		5 446	2 796	-5 191	393	16 456
Liquid assets (cash- Nominal)	R'mill		12 842	12 787	20 430	20 174	32 159
Leverage ratio (FFO : Total debt)	%	> 20	5.2%	2.4%	4.6%	8.1%	14.2%
Total debt : EBITDA	Ratio	< 3	11.0	13.3	13.3	8.6	5.6
Debt : Equity (incl provisions)	Ratio		2.7	2.7	2.3	2.5	2.3
Debt service coverage ratio	Ratio	> 2.5	0.4	0.8	1.0	1.9	2.5
Interest cover	Ratio		0.8	0.4	0.2	0.7	1.4
Debt drawdowns	R'mill		52 752	49 300	58 029	44 328	35 006
Equity	R'mill		-	-	20 000	3 000	-

## Insights

- A Government equity support package for R23bn was approved
- The combination of price increases, business efficiency savings through BPP success, extra borrowings and equity injection will result in an improvement of financial metrics over the period with favourable ratios being reached in 2017/18

Based on original modelling data



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- Red (not met)
- Orange (current single B)
- Risky/Yellow (1 notch up)
- Met/Green (2 notch up)



# In 2008 a subordinated loan was granted to Eskom which is viewed by rating agency Moodys as 50% equity

## History of subordinated loan

- Eskom was granted a subordinated loan facility by Government of R60bn in December 2008
- Eskom pays a fixed interest rate on each tranche of the loan, but only if the leverage and interest cover ratios as defined are favourable

## Liability vs. equity

- On initial recognition R30.5bn was classified as equity and R29.5bn as a loan liability based on Eskom's assumed financial ratios
- The valuation of the liability gets reviewed on an annual basis and, if deemed appropriate, re-measured
- The liability was valued at R27bn as of 31 May 2015

## Conversion of the loan

- Should this loan get converted to equity - the shareholder effectively "forgives the debt"
- Eskom's financial position (debt/equity ratio) will improve as debt reduces and equity increases
- Eskom does not have to repay this loan, thus, freeing up borrowing capacity



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## In 2008 the subordinated loan was required to support and stabilise credit ratings

- In August 2008 Eskom was **downgraded by Moodys** by an unprecedented 4 notches in local currency (3 in foreign currency) and left the **credit outlook on negative** view. In addition, **S&P** had placed Eskom on **Negative Credit Watch**
- Main reasons for the downgrade were
  - large scale **capital expenditure**,
  - with **little contribution to incremental earnings** in the medium term,
  - **tariff increases below those requested by Eskom** and required for the capital expenditure, and
  - positively, present strong support by the Government, with an element of **uncertainty as to future behavior towards Eskom**
- Eskom's **ability to source its funding requirements** was **hugely dented** by these actions
- In order to **support and stabilise the credit ratings** and assist Eskom's financial sustainability, **Government** agreed to provide **approved a R60 billion subordinated loan to Eskom**, flowing over 3 financial years

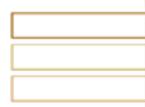


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# Conversion of the loan will improve key financial ratios and help defend the vulnerable credit ratings



- The loan is subordinated to Eskom's senior debt, receiving 100% equity credit from S&P and 50% equity credit from Moody's
- The Government could convert the loan outright to equity to show their commitment to further support Eskom, but the conversion will not have a material effect on Eskom's rating since it receives substantial equity treatment already
- The loan does not generate any incremental revenue nor cash or debt service relief as it is currently not being serviced, however, were Eskom's financial situation to improve an estimated R86bn could be reduced in future cash interest expense
- From Eskom's perspective a conversion to equity would help defend and over time recover investment credit ratings (current ratings: Moody's (ba1 Stable) and S&P (BB+ Negative Outlook))
- Over the remainder of the MYPD3 the impact on the financial ratios are estimated to be an increase of:
  - 0.03 - 0.11 on the interest cover ratio
  - 0.88 - 0.92 on the debt / equity ratio



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# Conclusion

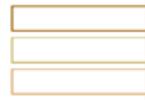
- **Conversion of the subordinated loan is critical to Eskom as it will**
  - improve the **balance sheet position**
  - improve financial ratios which affect the **position with rating agencies**, and
  - free up **additional borrowing capacity**
- Implementation of the selective reopener is critical to ensure the business is in a positive financial position in FY16 in terms of **liquidity and profitability.**



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# Thank You



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