Towards a municipal financial and operational sustainability strategy for the Western Cape

A report for the Western Cape Department of Local Government

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Prepared by:

Prof Tania Ajam
(School of Public Leadership)

Prof Johan Burger
(School of Public Leadership)

Prof Geo Quinot
(Department of Public Law)

Ms Melissa Botha
(School of Public Leadership)

Ms Deyana Isaacs
(School of Public Leadership)

Mr Johnny Douglas
(School of Public Leadership)

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Glossary of abbreviations

COCT	City of Cape Town
DM	District Municipality
DDM	District Development Model
GDP-R	Regional Gross Domestic Product
FBS	Free Basic Services
FFC	Financial and Fiscal Commission
LG	Local Government
LGES	Local government Equitable Share grant
LM	Local municipality
RSC	Regional Services Council
SALGA	South African Local Government Association
SALGBC	South African Local Government Bargaining Council
MFMA	Municipal Finance Management Act of 2003
MFPFA	Municipal Finance Powers and Functions Act of 2007
MTREF	Medium Term Revenue and Expenditure Framework
PPP	Public-Private Partnership
WC	Western Cape
YoY	Year on Year

Executive summary

The Hanns Seidel Foundation South Africa NPC (HSF), in partnership with the Western Cape Department of Local Government, has appointed the School of Public Leadership at Stellenbosch University (SPL) to undertake research with the view to design a financial and operational sustainability model/strategy for municipalities, in response to the "new normal" within the post-pandemic Western Cape (WC).

The objective of this study were to:

- capture pre-pandemic fiscal sustainability trends by synthesizing existing research,
- assess the short and medium term impact of the coronavirus pandemic on fiscal sustainability, and
- develop short and medium term strategic options based on the diagnostics above to improve the financial and operational sustainability of municipalities in the WC.

A financial analysis, a regulatory analysis and two rounds of interviews inform the recommendations of this report. The financial analysis covered the following municipalities, based on their category that reflects their powers and functions, and the size of their operating budgets:

- 2 large Category B local municipalities: Stellenbosch, Drakenstein
- 2 medium Category B local municipalities: Bergrivier, Hessequa
- 2 small Category B local municipalities: Swellendam, Kannaland and Laingsburg
- 3 Category C district municipalities: Central Karoo DM, West Coast DM and Cape Winelands
- 1 category A municipality: City of Cape Town

All the financial data used in this report were drawn from quarterly unaudited Section 71 reports and Medium Term Revenue and Expenditure Framework (MTREF) budget documentation from the National Treasury database.

In this report, we also provide feedback and interpretations of two sets of interviews amongst a sample of Western Cape municipalities, in which the Garden Route Municipality also participated.

Short and medium term impacts of the pandemic

Regional gross domestic product (GDP-R) growth rates are a good proxy indicator of the growth of a municipality's rates base, its ability to borrow and trends in relation to bad debt, increased indigence and demand for free basic services.

The Western Cape Treasury's 2020 Municipal Economic Review and Outlook (MERO) shows the slowdown in growth to 0.3% for the Western Cape as a whole in 2019, prior to the pandemic. As a result of the pandemic, the WC province's GDP-R was projected to have contracted by 6.9% in 2020 and is expected to increase to 3.8% in 2021. The City of Cape Town (with its reliance on tourism, hospitality and related industries) was particularly badly affected, as was Drakenstein and Hessequa, with contractions in GDP-R of -7.3%, -6.7% and -6.3% anticipated in 2020 respectively. The GDP-R growth rate in 2021 for both Laingsburg

(0.08%) and Bergrivier (1.8%) is expected to be slow. Stellenbosch (4.3%), Swellendam (4.3%) and the City of Cape Town (3.8%) are expected to rebound much faster. Despite positive job growth between 2014 and 2018, Bergrivier, Kannaland, Stellenbosch and the City were projected to have job losses, potentially increasing the number of indigents and undermining their user tariff and rates bases. Agriculture and agro-processing (e.g. citrus) are projected to be fast growing sectors as they recover from the contraction caused by the drought in the Western Cape. The Central Karoo (Laingsburg) has been particularly hard-hit by persistent drought conditions in recent years which has impacted negatively on growth and employment.

Some of the salient trends which emerged from the financial analysis of quarterly Section 71 quarterly reports and MTREF projections are captured below.

Key themes for local municipalities (LMs)

While the pandemic has exerted short term financial and operational sustainability pressures, sampled WC municipalities on the whole have been more resilient under the circumstances than would have been expected. Their resilience is largely a function of the resilience of their tax bases and the agility of their pandemic responses.

Size and diversity of the revenue base is an important factor for resilience: larger municipalities with more buoyant and diversified rates and service user charge bases fared better than their smaller counter parts. The composition of the local economy also played a major role: those dependent on agriculture where the drought had broken fared better than those reliant on the tourism and hospitality sector. Similarly, those municipalities with a higher proportion of industries designated as essential (such as financial services) and with more skilled residents who could take advantage of working from home arrangements. Smaller municipalities, such as Laingsburg, were placed under severe cashflow pressure with unspent conditional grants virtually the only funds in their bank accounts.

If there were challenges prior to the pandemic, these were magnified during the pandemic. But municipalities with the systems maturity, governance stability, business continuity risk management and financial management capacity in place prior to the pandemic were better placed to respond agilely during the pandemic. Proactive strategies included: working from home, opening revenue offices early in the lockdown, intensifying pre-pandemic revenue enhancement strategies (e.g prepaid meters, e-billing, changes to tariff structures to include flat rate connection fees) and existing cost containment measures.

Hardest hit were the capital budgets of LMs. The uncertainty occasioned by the pandemic cause LM's to adopt more conservative borrowing strategies with increased reliance on internal funds and capital transfers, some ceasing long term borrowing altogether. Drawing down of internal funds will have operational consequences in future, as well as additional pressure to raise tariffs to engender future operating surpluses to replenish capital reserves since borrowing for that purpose is not permitted.

Rates and user charges were not as strongly undermined as they could have been, but smaller own revenue sources were hard hit by the lockdown: fines, penalties, licences, rental of municipal properties etc. The pandemic has made it more difficult to balance sustainability and affordability of tradeable services in the face of large scale loss of jobs and livelihoods. Debt impairment is expected to increase.

Long term sustainability factors appear to be more important than COVID-19 in the near term, although this could change, should the pandemic drag on. These include LGES increases, employment increases and bulk service increases, eroding electricity surpluses. *Most significant expenditure pressures largely driven by systemic factors, not pandemic costs primarily*, including unaffordable national minimum norms and standards, increased costs of landfill services, increase incidence of land invasion.

Cost containment strategies have been stringently applied, and there is decreasing scope for savings as expenditure is pared to the bone. Personnel budgets have the most significant scope for savings.

For most LM's the growth of *FBS costs* and subsidised revenue costs over the MTEF is projected at below the growth rate of the LG Equitable share grant, but the assumptions about increases in indigent households might be under-estimates.

There has been an increased *reporting compliance* during the pandemic, due to the special reporting requirements by National Treasury as well as

The transition to MSCOA remains a challenge as evidenced, for example, by the number of negative balances in the Section 71 quarterly reports where correcting journal entries have been processed. The interviews reflect that MSCOA is not seen as a value add by high capacity municipalities and there are perceptions of insufficient support by the lower capacity municipalities.

The pandemic has also seen innovation from sampled LM's such as Drakenstein's small scale yet rapid and flexible emergency food security programme through partnering with an NGO, where e-vouchers were sent to recipient's mobile phones for redemption at local shops. This was a safer and more creative response than the Department of Social Development's slower food parcel response which exposed recipients to infection by the virus in long queues.

Key themes for district municipalities (DMs)

The sampled DMs were harder hit than LMs in the first quarter of the pandemic 2019/20Q4 in terms of the operating balances, but then showed somewhat of recovery as they intensified expenditure control measures and road agency functions picked up. DMs are highly dependent on the RSC replacement grant, especially those DM's without property portfolios. West Coast's water concession and resort income places it in a more favorable position than the other two DMs. In the past, DM's income from intergovernmental transfers were limited but stable, as SARS's performance backstopped the fiscal framework and created predictability. With fiscal consolidation at national level resulting in declines or slow growth of intergovernmental transfers, the tax collapse as a result pandemic and an imminent national debt consolidation crisis, the fiscal framework is far less stable. For the first 15 years after democracy, subnational grants (especially the Equitable Share) were protected over the MTREF period, which no longer seems the case. The DM's prime income source is therefore likely to be both smaller over the medium term, and more uncertain.

Similar to LM's the largest negative repercussion of the pandemic relates to constrained capital budgets with repairs and maintenance falling below the norm (except in West Coast DM).

Despite this, due to the responses of DM's, short term liquidity and solvency impaired slightly but still satisfactory. The depletion of DM internal reserves and consequently lower interest income will impact on own revenues over the medium term.

There are immense short term pressures from cost of employment budgets and longer term pressures from drivers such as national minimum standards in functions such as environmental health, fire-fighting etc. Agency service agreements appear to be ad hoc and do not create funding certainty over the MTREF but create pressures for expansion of roads function employment (e.g. Central Karoo).

The pandemic also highlighted the social development role of DMs in rural areas, which are at the coalface of community needs and in a better position to respond to community needs – as the COVID-19 pandemic clearly illustrates, despite this not formally being in their mandate.

Key themes for the City of Cape Town

Despite the sharp contraction in the GDP-R of Cape Town's economy (estimated at -7.3% in 2020), it is expected to rebound to a positive growth rate of 3.8% in 2021. While the financial performance of the City has been negatively impacted by the lockdown, many of the measures taken to manage the risks of "Day Zero" and the fall-out of load-shedding as a seemingly permanent and disruptive feature of the South African economic landscape, have enhanced its short term resilience in the face of the pandemic e.g. the transition to fixed access charges, constant updating of customer contact details such as mobile numbers and email addresses permitted extension of e-billing, introduction of prepaid water and electricity meters, etc. Similarly work-from-home policies developed in response to traffic congestion and carbon footprint challenges were also appropriate for the pandemic.

Over the MTREF period, the City intends to continue to run operating deficits of -6%, -1% and -1% of operating revenues in 2020/21, 2021/22 and 2022/23. As the City's overhead and external payments increase (remuneration, finance charges, bulk service charges, creditors), and revenue collection falls with reduced liquidity and depleted internal reserves, the City's financial position is set to deteriorate over the medium term. While some of these trends can be attributed to the impact of the aftermath of the pandemic (e.g increased debt impairment), these are not as prominent causal factors as longer term systemic factors (e.g. the failure to constrain growth in personnel budgets, fiscal consolidation at the national government sphere which results in cutting of local government capital grants to fund, for example, national state owned entities and higher education). Much, however, depends on the duration of the lockdown (and its impact on solvency of businesses in the tourism, hospitality and related industries, for instance), how quickly the urban metropole's economy will rebound and how growth enhancing the City's capital investment will be.

Themes emerging from the interviews

Summary of findings from the first-round interviews

Municipal financial and operational sustainability cannot be confused with short term liquidity. One way of maintaining short-term liquidity is to postpone investment in infrastructure that would ensure longer-term operational sustainability, especially to be able to continue sustainably amidst crises such as droughts and pandemics. This requires both resilience and agility. The Western Cape is not the ideal province to select cases for research to discover the depth and causes of the widely published distress in South African municipalities. Our interviews revealed that Western Cape municipalities so far have shown remarkable resilience, even after the devastating drought and amidst the most devastating pandemic and concomitant lockdown restrictions. This is partly attributable to strong and resilient financial and service delivery positions prior to the pandemic, and the competence, cohesion, continuity and experience of their management teams. In addition, the most resilient municipalities also ascribed their favourable financial and operational sustainability to executive maturity and stability and good working relationships between the officials and politicians.

There are nevertheless serious concerns about longer term operational and financial sustainability, mostly as a result of factors outside the control of the municipalities. The interview panel realised that more in-depth investigations are required to unpack these concerns. The interviews did not reveal widespread optimism for changing either the basket of services or the business models for providing these services and it raises questions about systems agility to face the increasing uncertainties. This matter was therefore flagged for more in-depth investigation.

Findings from the first-round interviews

The results from the interviews with several municipal experts dealing with the realities of keeping municipalities afloat on a day-to-day basis, provided some valuable insights. Many of the responses captured here can be viewed as "the same old story" repeated by the same people that have also responded to many other initiatives and dialogues about sustaining municipalities. It is also possible to interpret the positive financial and operational sustainable position of most responding municipalities as indication that they will always cope (and complain) and therefore the status quo can be maintained.

Such interpretation can be fatal. The feedback captured in this report indicates that most local municipalities, with the exception of the smallest, have so far succeeded to remain sustainable through their resilience and agility. However, there is a sense from the majority of respondents that the status quo will not be enough going into the future. The pandemic may have just accelerated the inevitable, namely that externally induced constraints, the current basket of services for local and district municipalities and arrangements between them, the current business model by which these baskets are operated, the current grant allocation models, the current arrangements around agency services and even the current demarcation of boundaries, especially in the case of small municipalities, need drastic revision.

Summary of recommendations

Four categories of recommendations have been made. These relate to the process for actioning the recommendations of this report, financial sustainability recommendations, institutional recommendations and regulatory recommendations.

Process recommendation

Process to action the recommendations in this report

1. A technical working group should be assigned the task of assessing and prioritizing recommendations over the short and medium term, and assigning appropriate roles, responsibilities and timelines.

Financial sustainability recommendations

The local government fiscal framework and operational intergovernmental transfers

2. The local government functional framework should be reviewed in the light of 25 years of local government experience and the implementation of far-reaching reforms in electricity and water industries. The revised functional framework should inform a fundamental review of the local government fiscal framework.
3. A process of this magnitude should not just involve SALGA, provincial departments of local government and provincial treasuries but also consultation with individual municipalities, so that the differentiated impacts can be understood, and diverse municipal voices can be heard.

Funding of capital programmes

4. In the face of tightening capital budget constraints, Municipalities should review their systems of capital project prioritisation to ensure that they balance social infrastructure (e.g. informal settlement backlogs) with economic infrastructure that can generate revenues and grow the tax base, and balance new infrastructure with rehabilitation and upgrades.
5. Municipalities should establish a pipeline of shovel ready projects in a pipeline and aim to deliver early in the financial year to order to take advantage of additional unplanned capital funding grant opportunities.
6. Municipalities should build up their internal reserves to help finance their capital expenditure and facilitate borrowing once the pandemic has ended. This has implications for tariff setting in order to generate operating surpluses.
7. Municipalities should explore project finance and other forms of off-balance sheet lending where bankable projects can be identified. Cooperation among municipalities with provincial government support to help identify and package bankable projects may be required for projects which transcend the boundaries of any single municipalities like dams, and renewable natural gas projects from municipal solid waste landfills and wastewater treatment facilities.
8. Innovative lending arrangements should be explored e.g. green bonds and concessionary financing from the World Bank's Climate Investment Fund. The City of Cape Town, for instance, has already issued green bonds, and its current small scale embedded generation programme could be scaled up as a bases for a tradeable renewable certification scheme. This would establish markets for both renewable energy and tradeable green energy certificates. If other municipalities were to generate their own renewable energy, these sales and revenue from selling green certificates could ensure the sustainability of this form of borrowing.

9. Drakenstein Municipality should request from the FFC an independent assessment of the fairness of its capital grant allocation relative to similar secondary cities, in terms of the FFC Act.
10. The Western Cape Provincial should support the case for streamlining capital grants to reduce their administrative burden, in a differentiated, risk-based approach which recognises municipalities' track record in delivery and good financial management.

Existing revenue sources: balancing affordability and sustainability

Enhancing the ability to optimise existing revenue streams from rates and tradeable services, revolve around the following possibilities:

11. Enhancing the attractiveness for targeted categories of households to relocate (Municipal strategic planning, but district-wide initiatives may require District Development Model-type planning by all role players).
12. Promoting further advances in optimising existing revenue streams through expanding capacity for data management and considering the mechanisms for increasing revenue from property rates proposed by the South African Cities Network 2018 State of City Finances Report.
13. Better utilisation of dormant capacity in service systems or reducing costs through constraint management combined with alternative delivery models (Municipal tactical planning, but district-wide initiatives may require District Development Model-type planning by all role players).
14. Investigating the feasibility of municipal re-demarcation with a view to amalgamate small rural municipalities (Provincial Department of Local Government and national Department of Cooperative Government), or create single tier rural municipalities.
15. Reviewing the Municipal Property Rates Act and related legislation with a view to make allowance for affordable repayment arrangements for businesses affected by the pandemic
16. Promoting further advances in optimising existing revenue streams of tradeable services through expanding capacity for data management and implementing the "Differentiated Service Affordability Model for the Basket of Services Provided by Western Cape Municipalities" (HS Business Solutions, 2019), with provincial support.

New revenue sources

17. Western Cape municipalities should apply to National Treasury via the Municipal Fiscal Powers and Functions Act to pilot revenue instruments which have been proposed (congestion charges etc) to more accurately gauge their feasibility in terms of impacts, potential revenue and administrative costs.
18. Municipalities (especially those with property portfolios) should investigate the feasibility of implementing land value capture mechanisms.
19. A "virtual municipalities" simulation based on actual data could be set up to enable sensitivity analyses to test the viability and impact of new sources of revenue.

Managing costs of employment pressures

20. Where municipalities cannot fund nationally negotiated agreements on costs of employment, they should apply for exemption.

21. The WC provincial government should propose to the national Minister of Cooperative Government and Traditional Affairs that at least once every five years, municipalities should conduct productivity studies resulting in recommendations to inform the review of staff establishments, organizational design and delegations. These should be tabled at Council which should be required to explain how they intend to respond to the recommendations.
22. Good practice productivity benchmarks for municipality as a whole and individual services should be developed e.g. to balance administrative and core delivery spending. This could not only improve internal efficiency but promote civil society oversight.
23. An impact evaluation of the 2018 upper limits on the remuneration for senior management should be done, with a view to improving the effectiveness of these regulations and minimising unintended consequences.
24. Where practical, work-from-home and online meeting practices developed during the pandemic should be maintained, in order to attract and retain staff with scarce skills and reduce travel and subsistence costs (especially for the more distant, rural municipalities). These can also facilitate the sharing of human resources among municipalities, since travel time between municipalities and travel costs could be vastly reduced.

Free Basic Services

25. Municipalities should ensure that their projected increases in indigent households are realistic.
26. A consolidated provincial data set on households receiving FBS should be created to assist in identifying vulnerable households in the event of a national disaster such as a pandemic, and to track the impact of the free basic services policy with a view to impact evaluation.

Institutional recommendations

Affordability of political support structures

27. The cost of political structures and control support costs can be enhanced by issuing guidelines and norms and, as a last resort, by means of prescripts where excessive compared to own revenue, population size and other guideline benchmarks (Provincial Department of Local Government and national Department of Cooperative Government).
28. The feasibility of municipal re-demarcation should be investigated, with a view to amalgamate small rural municipalities (Provincial Department of Local Government and national Department of Cooperative Government), or create single tier rural municipalities.

Revenue certainty of agency funding arrangements

29. All agency agreements should be formalized and duly gazetted with the aim of providing at least a minimum degree of funding certainty for municipalities over the MTREF period and avoid audit queries.

Alternative delivery models: shared services and co-production

To the extent that shared/joint service delivery may be a more sustainable option, it requires the following reforms:

30. Removing or reducing regulatory impediments to shared services (national reform);
31. Strengthening consequences for council, the political executive and senior management of service delivery failure (national reform);
32. Introducing outcomes evaluation: The 2019 National Evaluation Policy Framework (NEPF) has set the objective of ensuring local government successfully institutionalises the practice of evaluation and this should be encouraged. Evaluation must go beyond compliance-oriented audits of performance for accountability purposes to provide for learning and critical self-reflection;
33. Enhancing capability for shared services by way of seconded personnel, capacity building, risk management and good practice initiatives for successfully introducing shared/joint services as a viable option (provincial responsibility);
34. Creating a community of practice and safe space for small-scale “sandbox”-type controlled experiments on shared/joint services, which bring together highly experienced local government practitioners, sector professionals and researchers to jointly develop innovative solutions (Local and provincial government, regional offices of national departments and research institutions).

Public-private partnerships (an operational perspective)

To the extent that PPPs as range of alternative service delivery models may be more sustainable, the following reforms are required:

35. Removing or reducing regulatory impediments (national reform, implementing National Treasury recommendations);
36. Strengthening consequences for council, the political executive and senior management of service delivery failure (national reform);
37. Institutionalising outcomes evaluation;
38. Providing capacity (including grant funding for feasibility studies) for successfully configuring a PPP as a viable option (provincial responsibility)
39. Creating a community of practice and safe space for small-scope “sandbox”-type controlled experiments on PPPs which bring together highly experienced local government practitioners, sector professionals, legal experts and researchers to jointly develop innovative solutions (Local and provincial government, regional offices of national departments and research institutions).

The social and economic development focus of district municipalities

The options can be summarised as follows:

40. Supporting and widening the scope of options for unique district-specific and district-wide innovations that would enhance the revenue-generation capacity of district municipalities and support district-wide local economic development (Provincial Department of Local Government).
41. Better utilisation of dormant capacity in service systems or reducing costs through constraint management combined with alternative delivery models (District-wide initiatives may require DDM-type planning by all role players).
42. Investigating the feasibility of municipal re-demarcation with a view to amalgamate small rural municipalities (Provincial Department of Local Government and National Department of Cooperative Government), or create single tier rural municipalities.

43. Assessing the feasibility of formalising the social development role of district municipalities in rural areas.

Audit costs

44. The provincial government should propose to the National Treasury and Auditor-General a reform whereby municipalities with clean audits for the last three years, are audited every two years instead of annually. This approach is risk based, grounded in objective criteria, and rewards municipalities which have demonstrated their institutional maturity and the soundness of their control environments.

Regulatory recommendations

General regulatory recommendations

The following reforms are proposed:

45. Rationalise the regulatory environment.
46. Pay closer attention to differentiation between different local government contexts in regulatory regimes.
47. Consider more collaborative operational models and determine the extent to which the regulatory environment facilitate or prohibit such collaborative approaches.
48. Institutionalise meticulous impact assessments of all new regulatory prescripts from an implementation perspective, based on comprehensive, reliable data.
49. Scrutinise all new norms and standards closely to determine whether they in fact represent minimum norms and standards or gold standards.
50. Ensure that findings of impact assessments are adequately internalised across the regulatory framework, including in funding decisions.
51. Move away from a paradigm of national agenda-setting that informs regulatory prescripts that are forced down on local governments to simply implement in favour of a model where local governments drive the regulatory agendas from the bottom up, both in terms of setting the agenda and priorities and in terms of the content of regulatory instruments.
52. Further research on the formulation of regulatory prescripts, including norms and standards, in particular areas is required in order to identify the presence or absence of local government perspectives, and by implication implementation perspectives, in such formation processes. The results of such research will be important to formulate appropriate reforms.

Supply chain management: a regulatory approach

The following reforms should be considered:

53. Adopt a regulatory regime that is more flexible in the way that it should be applied in different municipal contexts. This must include rules that are suitable to the context of rural supply chain management (SCM).
54. Rethink SCM regulatory approaches that are currently focused on individual municipalities rather than any form of collaborative approaches.
55. Design and experiment with mechanisms that encourage greater collaboration, for example by providing for SCM as a shared service or streamlined PPP processes or other mechanisms to collaborate such as through joint municipal entities.

56. Engage in more dedicated capacity development for SCM units at local government level.
57. Develop and implement minimum competency levels for SCM officials, linked to a drive towards greater professionalization of SCM in South Africa in general and in local government as a sub-specialisation more specifically.
58. Encourage greater collaboration between municipalities in SCM, e.g. SCM as a shared service.
59. Adjust the thresholds for the use of competitive bidding procedures upwards (at least to R500 000 if not more), taking into account real figures of contract values and transaction costs. Risk management approach could rather be adopted to thresholds, including maturity levels of individual entities, e.g. clean audits over time as way of determining maturity as opposed to stark contract values.
60. Allow more flexibility in entering into long-term contracts. Reduce the regulatory burden regarding such contracts, e.g. mandatory input from various levels of government.

Regulatory reporting

61. Improved systems should be considered that would enable data to be captured in a manner accessible to all, which would not only enable continuous oversight, but also provide ongoing management data.
62. There should be greater use of technology, such as cloud-based solutions, in this regard. Municipalities should ideally only be responsible for capturing the base data in a system that is generally accessible to other levels of government and organs of state that play an oversight role (such as the Auditor-General) in order for those entities to analyse the data for their own purposes.
63. The attention to capturing data in appropriate systems should also serve to make the data available to the municipalities themselves for management purposes, such as, for example, informing business intelligence solutions.
64. Careful attention should be given to what type of data is really required and in what format to remove redundancies.
65. Attention should be given to differentiated reporting approaches depending on a municipality's own performance. That is, a system of self-regulation based on own performance. Thus, municipalities with a record of good governance over a set period of time could be granted greater leeway in respect of reporting and oversight and effectively be granted greater self-regulation powers. Such a system should be premised on clear, objective criteria that determine a municipality's movement within the system and thus enable municipalities to manage their own affairs in pursuit of a particular self-regulation status. The system should also be dynamic in that any municipality could move in any direction depending on its continued performance in terms of the set metrics. The cost implications of a particular status within this system, i.e. of being more or less self-regulating, should be clearly set out. Generally, having greater self-regulation would be more costly since oversight would be done locally and a municipality should thus be able to afford such self-regulation.

Mandates of municipalities

66. Consider adjusting the approach to municipal mandates, either by way of a constitutional amendment to bring more agility to the system or by way of overarching legislation.
67. Align actual mandates with legal mandates.

68. Explore ways in which newer functions, such as the provision of data services, could be incorporated at appropriate levels within the mandate scheme.

Intergovernmental debt (Eskom, etc)

69. Urgent attention must be given to resolve Eskom's municipal debt problem. This will seemingly only be possible by way of intergovernmental collaboration between all three levels of government.
70. A more reliable and efficient system of resolving intergovernmental debt must be established.
71. In creating intergovernmental mechanisms to deal with problems at local government level, care should be taken not to adopt an approach that routinely results in local powers and capacities being absorbed into higher levels of government, but rather to work with the problem at the local level and with the local capacities.

Financial impact of court orders

72. When service delivery orders are granted, all levels of government should be joined so as to ensure that the burden of implementation can be appropriately shared between the different levels of government.
73. In instances where court orders routinely result in disruption to municipal planning, a process of review should be initiated to establish the underlying reasons for such disruptions, e.g. whether the demands made on municipalities in such cases are inappropriate and thus requiring an adjustment to the entitlements enforced in such cases or whether planning processes and budgeting are inadequate to cater for legitimate claims made on municipalities and thus requiring appropriate adjustments in municipal planning and budgeting. Such a review process could be initiated as part of ongoing local government oversight by bodies such as COGTA or SALGA.

Towards a municipal financial and operational sustainability strategy for Western Cape municipalities:

A report for the Western Cape Department of Local Government

1 Introduction

Over the last decade, economic growth in national economy has stagnated, productive capacity and private sector investment has declined, unemployment and poverty have soared, and fiscal policy has been geared to funding state-owned enterprises, while subnational governments have borne much of the burden of fiscal consolidation. Across South Africa, municipalities have been experiencing financial challenges to varying degrees, due to increased spending pressures, while revenues have declined: both in relation to intergovernmental grants and to own revenue collections. Some Western Cape (WC) municipalities have also been facing sustainability challenges, not only due to factors in the external environment, but due to choices made within the municipality.

The Covid-19 pandemic and national government's lockdown response to this public health crisis have exacerbated this crisis. The impact of the pandemic has resulted unforeseen spending needs but also a substantial decrease in revenue to municipalities, and therefore their ability to deliver basic services. It should be noted that some municipalities in the WC were already in a fiscally stressed state prior to the pandemic. In these cases, the coronavirus pandemic amplified, but did not cause this state, and a speedy return to fiscal health is unlikely. For those municipalities which were in a fiscally health position before the pandemic, Covid-19 may be a serious but temporary shock, and the prospects for financial recovery are commensurately greater.

1.1 Project scope

The Hanns Seidel Foundation South Africa NPC (HSF), in partnership with the Western Cape Department of Local Government, appointed the School of Public Leadership at Stellenbosch University (SPL) to undertake research with the view to design a financial and operational sustainability model/strategy for municipalities, in response to the "new normal" within the post-pandemic Western Cape (WC).

The project aims to contribute to the development of a medium to long term municipal financial and operational sustainability strategy, which will focus on:

- optimising existing revenue streams, and
- identifying alternative revenue streams and
- selecting a prioritised basket of services and minimum level of service delivery to be rendered to communities,

The strategy will have to be sufficiently differentiated to respond to the varying circumstances of municipalities, with concrete, actionable plans in the short and medium term. In the long term, the only guarantor of municipal sustainability is a buoyant, inclusive, productive and growing national economy. The strategy will distinguish between steps which need to be taken by the municipality itself, those which need to be facilitate at provincial level and those which are in the domain of the national government (such as policy and legislative change).

Much research has already done on WC municipalities, but these studies have focused on specific elements of the sustainability conundrum, rather than taking a coherent, holistic view. These studies would also need to be updated in the light of coronavirus pandemic.

1.2 Research objectives and methodology

The objective of this study were to:

- capture pre-pandemic fiscal sustainability trends by synthesizing existing research
- assess the impact of the coronavirus pandemic on fiscal sustainability
- develop short and medium term strategic options based on the diagnostics above to improve the financial and operational sustainability of municipalities in the WC.

Our research strategy was built on the strengths of the team with a view to provide the best comprehensive study within the available time period of eight months. The combined practical experience of the members of the team as well as the regular interaction that individual team members have with a variety of local government practitioners was used constructively to develop appropriate recommendations towards the development of the long-term sustainability strategy for the municipalities. The bulk of the project was done on the basis of a desk top study drawing on existing research, such as quantitative and qualitative analysis of the costing and provision of a basket of services at municipalities in the WC, based on research work which has already been commissioned by the Western Cape Department of Local Government

The strategy was to develop a broad analysis of the current and future local government municipal sustainability trends in the WC, base, and data utilising different skills, which inter alia including a regulatory review, financial analysis and empirical evidence from a sample of WC municipalities for detailed diagnostics, especially of the impact of the coronavirus pandemic.

Our strategy recognised that much empirical work had already been done on different dimensions of the sustainability, inter alia, the basket of services offered, costs of delivery, existing and potential delivery models and tax and tariff structures. The aim of the strategy was to analyse and synthesize the existing research into a holistic strategy in the short, medium and long terms, differentiating between those activities which can be initiated by the municipalities themselves, by the WC Provincial Government and by the National Government (for example, if legislative change is required).

The project started September 2020 and was completed by the end of April 2021. This deadline was contingent on the availability of practitioners from the relevant municipalities to participate in semi-structured interviews and workshops, as well as the availability of the data and information requested.

A financial analysis, a regulatory analysis and two rounds of interviews inform the recommendations of this report. The financial analysis covered the following municipalities, based on their category which reflects their powers and functions, and the size of their operating budgets:

- 2 large Category B local municipalities: Stellenbosch, Drakenstein
- 2 medium Category B local municipalities: Bergrivier, Hessequa
- 2 small Category B local municipalities: Swellendam, Kannaland and Laingsburg
- 3 Category C district municipalities: Central Karoo DM, West Coast DM and Cape Winelands
- I category A municipality: City of Cape Town

In this report, we also provide feedback and interpretations of two sets of interviews amongst a sample of Western Cape municipalities. The first set of interviews, conducted with three district municipalities and six local municipalities, focused on three overarching questions, firstly on overall municipal financial and operational sustainability and its main drivers before and since Covid-19; secondly on cost minimisation efforts and the factors impeding and challenging achievement of a Minimum Efficient Cost for each responding municipality; and thirdly on maximising revenue and factors impeding and challenging achievement of the Maximum Fiscal Capacity by each responding municipality. The second set of interviews targeted one additional district and two local municipalities that volunteered for in-depth interviews during the MinMay meeting on 8 October 2020. The objective was to determine how court judgements, prescripts and compliance, labour regulation, external role players in municipal service delivery, intergovernmental grants and agency services, municipal structures and systems as well as the current basket of services impact on municipal financial and operational sustainability and how municipalities deal with it. Two interviews with City of Cape Town respondents covered the questions from both first round and second round in-depth interviews. An integrated explanation of the responses to each of the two sets of interviews, as well as a consolidated interpretation, is provided.

1.3 Limitations of the study

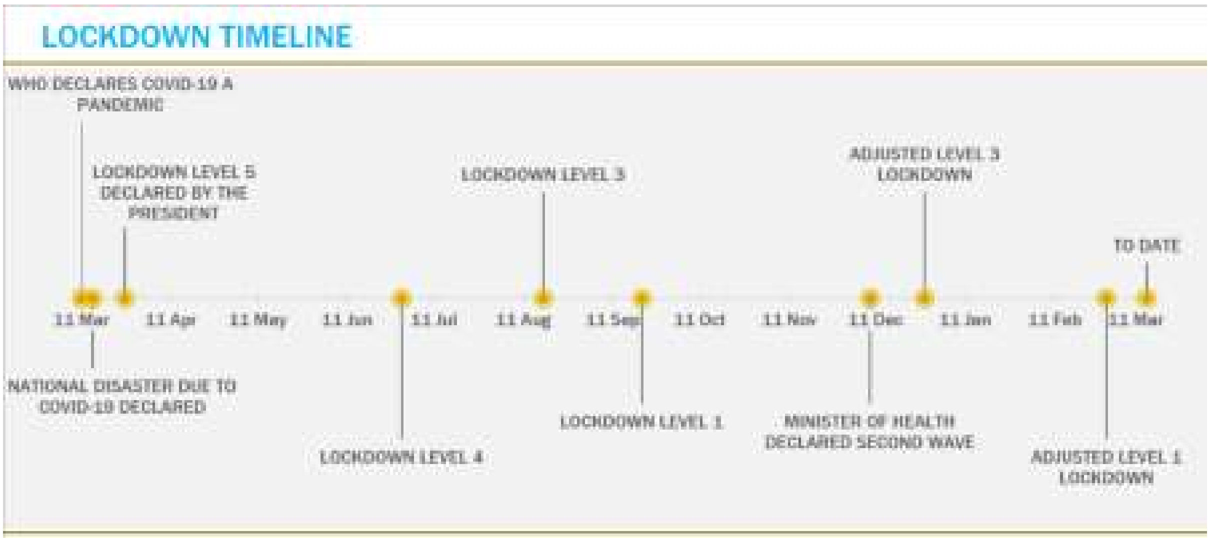
At the time of undertaking the study, there was considerable uncertainty around the duration of the pandemic and recurrence of successive waves. At the time of completion of the study (April 2021), the pandemic was still in progress. Should the pandemic progress much longer it may render the findings outdated and the recommendations based on them less appropriate. Given the large scope of the study within a 6 month horizon during a pandemic, the study is largely static at a point in time. More complex dynamic projection methodologies would require more time to implement, and are an important avenue for further research.

1.4 A timeline of the Covid-19 pandemic

Since President Ramaphosa declared the coronavirus a national disaster on 15 March 2020, over the course of the next year, lockdown stages were eased progressively until 11 December when as second wave was declared.

As a result, lockdown status reverted from adjusted Level 1 to adjusted Level 3 on 28 December 2020, to be eased again to adjusted Level 1 on 1 March 2021. It is expected that municipalities would have been hardest hit in the first 3 months of hard lockdown, April to June 2020, the fourth quarter of the 2020/21 financial year.

FIGURE 1: A TIMELINE OF THE CORONAVIRUS PANDEMIC



Section 2 of this report sketches an analytical framework for the conducting the empirical research. Sections 3 and 4 summarises existing research on the local government functional framework and pre-pandemic sustainability trends in WC municipalities. The financial analysis in Section 5 examines the short term and medium term impact of the pandemic on the sampled municipalities. Section 6 presents the key themes emerging from the two rounds of interviews conducted. A regulatory analysis is contained in Section 7. Section 8 offers a strategic option analysis based on summaries of the various problem statements. Section 9 concludes with a summary of recommendations.

2 Analytical framework

Municipal sustainability is the ability of a municipality to sustain its current spending and revenue policies while delivering on its mandate and meeting its financial obligations, without threatening solvency or default.

The above definition captures both operational and financial dimensions of municipal sustainability. It also introduces an intertemporal element: decisions about expenditure, revenues and debt taken in the present, may impact sustainability in the future. Financial obligations are broadly defined to include expenditures, commitments, liabilities and contingent liabilities.

This report focuses on trying to enhance systemic sustainability across the entire WC province, not just “playing musical chairs “ with unsustainability among municipalities – taking measure which would improve the sustainability of one or more municipalities, but compromising the sustainability of others.

Other important concepts are fiscal need, fiscal capacity and fiscal effort. *Fiscal need* depends on the powers and functions assigned to a municipality, the basket and level of services it offers, the delivery models employed and the minimum efficient cost of delivering those services. The *minimum efficient cost* will differ from municipality to municipality and depends on factors such as varying prices (which may differ between coastal and inland municipalities, urban and rural CPI) and other cost disabilities outside the municipality's control (e.g. distances, population density, geography etc.). Actual expenditure often differs markedly from minimum efficient costs due to inefficient, unproductive, fruitless or wasteful expenditures (e.g. technical losses of water and electricity) and other unsound decisions which are within the control of the municipality. Section 73(2)(b)(i) directs that municipal service delivery aim at the "prudent, economic, efficient and effective use of available resources", which resonates well with the minimum efficient cost ideal. Section 74(d) of the Municipal Systems Act requires that tariffs be cost-reflective and cover costs such as capital, operating, maintenance, administration and replacement costs, and interest charges.

In addition to the direct cost of service delivery, the Municipal Structures Act and the Municipal Systems Act also make provision for political structures and administrative functions (such compliance with legislation and regulations). As a result, there are also governance and administrative costs which are not directly associated with service delivery.

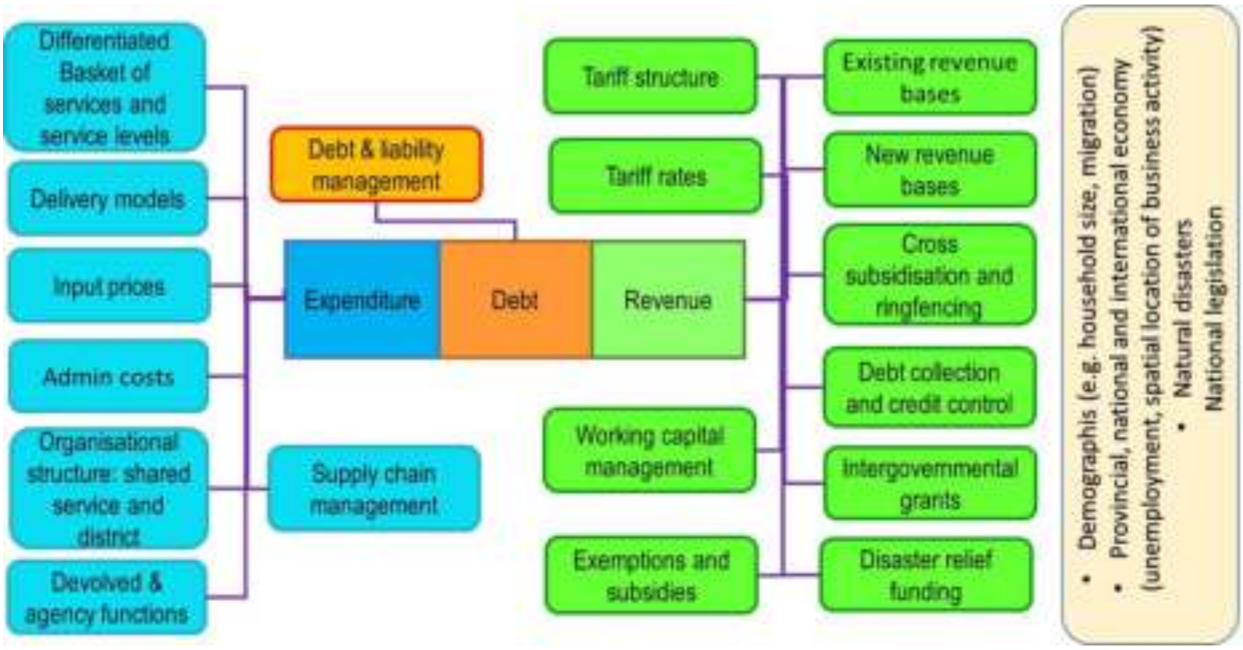
Fiscal capacity refers to the maximum potential revenue a municipality could derive from its revenue bases, which may change over time. Revenue capacity is largely influenced by factors outside the control of an individual municipality: e.g. the level, nature and spatial distribution of economic activity, concentrations of poverty and inequality leading to high levels of indigents and other socio-economic factors, property markets, land tenure (e.g. communal property rights in rural areas vs individual property ownership).

Fiscal effort refers to the extent to which the municipality actually uses the fiscal capacity available to it, i.e. the actual revenues collected by the municipality. The parameters influencing fiscal effort tend to be largely within the control of the municipal council: rates and tariff structures, credit control, revenue management, exemptions etc. Section 74 (e) of the Municipal Systems Act requires that tariffs for services be set at financial sustainability levels, taking into account subsidisation from sources other than the service concerned. Cost-reflective tariffs should take into consideration the initial capital required to deliver the service, the operational costs of delivering the service as well as maintenance, repair upgrade and replacement of the physical assets required for service delivery.

Figure 2 below discusses these concepts in greater detail. The yellow block on the right lists a few of the factors external to the municipality which influence its revenue capacity and its cost disabilities), and by extension its sustainability. This includes legislation and institutional arrangements in the national and provincial spheres. The three broad categories of factors which influence a municipality's operational and fiscal sustainability and which are within the control of the municipality relate to its spending, revenues and debt management.

In principle, revenue collection is supposed to constrain expenditures, but in practice, it is often expenditure which drives revenue. As reflected in Figure 2 below, expenditure needs are driven by the need to provide a minimum level of services, and the quality of services. Section 74(2)(c) requires than "poor households must have access to at least basic services".

FIGURE 2: AN ANALYTICAL FRAMEWORK FOR MUNICIPAL OPERATIONAL AND FINANCIAL SUSTAINABILITY



The delivery model employed by the municipality to deliver the service also influences the cost structure (e.g. in-house production, contracting out, public-public partnerships, public-private partnerships). The organisational structure and salary scales emanating from collective bargaining, as well as the municipality's hiring decisions affecting headcount also are major cost drivers. Input prices are also important (e.g Eskom and Water Service Provider bulk purchase prices). Supply chain management (as regulated by the Municipal Finance Management Act and its regulations) can play an important role in ensuring effective demand management and acquisition of goods, services and assets. Conversely, poor supply chain management can result in inflated costs, irregular, fruitless and wasteful spending, and outright fraud and corruption.

Administrative costs are often driven by the need for regulatory compliance e.g. Auditor General's fees, audit committees, etc. Municipalities often carry out devolved functions such as libraries, and municipal health, and these mandates may be partially unfunded mandates. Similarly municipalities may also perform functions on an agency basis on behalf of provinces, vial service level agreements (e.g. roads).

In relation to the revenue dimension of sustainability, Figure 2 above captures intergovernmental grants (such as the local government equitable share in terms of s214 of the Constitution and conditional grants in terms of the annual Division of Revenue Act). As a result of Covid-19 disaster relief funding may become important. This would refer to MFMA section 29 emergency spending but also look at the contingency reserve as adequate for risk pooling at national level.

As regards existing revenue sources, rates and tariff structures are important determinants of municipal sustainability. Equally important is debtor management and credit control, and the ability to cross-subsidise services. Rising bulk service costs for electricity and water have however eroded trading surpluses, reducing scope for cross-subsidisation. Here the degree and modalities of cross-subsidisation also become important (surcharges and levies).

Finally, new revenue bases may improve financial sustainability prospects, with the parameters set by s229 of the Constitution and the Municipal Powers and Function Act.

The Financial and Fiscal Commission (FFC) has introduced the distinction between a structural funding gap and an actual funding gap, where the structural gap is the difference between a "reasonable level" of expenditure incurred for the effective delivery of a service and the maximum own revenue generated by the municipality. Given the high levels of poverty and pervasive unemployment and consequent inability to pay for services, a structural gap is inevitable and is the rationale for the establishment of intergovernmental transfers in s214 of the Constitution. The actual funding gap experienced by municipalities, however, is larger than the structural gap due to the following factors:

1. A *fiscal effort gap:* when municipalities exert insufficient fiscal effort and collect all the own revenues within their fiscal capacity.
2. *An expenditure inefficiency gap:* when municipal expenditures exceed the reasonable efficient levels required to provide services.
3. *A transfer gap:* when intergovernmental transfers fall short of filling the structural gap and
4. *An unfunded/underfunded mandate gap:* when municipalities incurring spend on services and functions that fall outside their mandates and for which receive no revenue or inadequate revenues to cover the costs of the function (South Africa. Financial and Fiscal Commission, 2011).

The first two factor lie to a larger extent within the control of municipalities themselves, whereas the latter two are structural in nature and would require the cooperation of other spheres of government. These gaps will be considered in the discussion below.

This section has provided a brief overview of the analytical framework. The next section outlines the institutional context in which WC municipalities operate, and which influence their operational and financial sustainability.

3 The local government functional and fiscal framework in the Western Cape

The Constitution establishes 3 categories of municipalities, each with their own powers and functions: Category A (local municipalities - LMs), Category B (district municipalities - DMs) and Category C municipalities (metropolitan municipalities), Category C metropolitan municipalities perform all the duties of LMs and DMs in their jurisdiction. The 24 LMs, 5 DMs and 1 metropolitan municipality in the WC are depicted in the diagram below.

FIGURE 3: DISTRICT AND LOCAL MUNICIPALITIES IN THE WESTERN CAPE

Appendix 2 provides more detailed profiles of the sampled municipalities, illustrating considerable variation in socio-economic characteristics, the services that they delivery and their staffing profiles.

3.1 Local municipality powers and functions

Section 156 (Part B Schedule 4 and Part B Schedule 5) of the Constitution, as well as section 84 of the Municipal Structures Act, 1998 assign the following functions to local municipalities.

Air pollution; building regulations; child care facilities; electricity and gas reticulation; fire-fighting services; local tourism; municipal airports; municipal planning; municipal health services; municipal public transport; municipal public works only in respect of the needs of municipalities in the discharge of their responsibilities to administer functions specifically assigned to them; pontoons, ferries, jetties, piers and harbours, excluding the regulation of international and national shipping and matters related thereto; storm-water management systems in built-up areas; trading regulations; water and sanitation services limited to potable water supply systems and domestic waste-water and sewage disposal systems

Beaches and amusement facilities; billboards and the display of advertisements in public places; cemeteries, funeral parlours and crematoria; cleansing; control of public nuisances; control of undertakings that sell liquor to the public; facilities for the accommodation, care and burial of animals, fencing and fences; licensing of dogs; licensing and control of undertakings that sell food to the public; local amenities; local sport facilities; markets; municipal abattoirs; municipal parks and recreation; municipal roads; noise pollution; pounds; public places; refuse removal, refuse dumps and solid waste disposal; street trading; street lighting; traffic and parking.

Minimum norms and standards for the provision of these services are often set by national government, and poorer, more rural municipalities may not have the revenue base to afford these standards (e.g. the national standards requirement for fire prevention, environmental health standards.).

To finance the provision of services, LMs are empowered to levy property rates and user fees and service charges (e.g. for water, electricity and sanitation) in terms of section 229 of the Constitution. Besides these own revenue sources, LMs are also entitled to an "equitable share" of revenue collected nationally and distributed each year among the 257 municipalities in a revenue sharing process through the local government equitable share formula by the Minister of Finance, after consultation with the Financial and Fiscal commission (section 214 of the Constitution). The Local Government Equitable Share (LGES) grant is unconditional and is meant to finance delivery of free basic services to poor households and subsidises the cost of administration and other core services for those municipalities with the least potential to cover these costs from their own revenues.

Poorer LMs municipalities also receive an unconditional Special Support for Councillor Remuneration and Ward Committees grant to subsidise councillor salaries, over and above the Equitable Share grant, and calculated separately. Based on the size of their population and their total income, municipalities are categorised into 6 grades by the Minister of Cooperative Governance and Traditional Affairs, who also gazettes notices on the determination of upper limits of councillor salaries. The last notice was in December 2018 due to an ongoing review of wages which has frozen wages for 2020/2. The smallest and poorest municipalities in the lowest 3 grades receive the grants. Grade 1 municipalities receive 90 percent of the gazetted maximum remuneration for a part-time councillor, grade 2 municipalities receive 80% and grade 3 municipalities 70%. In addition to this, each LM in grades 1 to 3 also receive a grant to provide stipends of R500 per month to 10 members of each ward committee in their municipality.

LMs also receive conditional grants from various national government departments, which are earmarked for a particular purpose and municipalities have no discretion in how they are spent. They are mainly capital conditional grants for infrastructure finance, but there are also operational conditional grants for capacity building. Both the Equitable Share allocations and the conditional grants are reflected annually in the Division of Revenue Act which is tabled at the same time as the national Budget. The largest capital grant is the Municipal Infrastructure Grant (MIG) which funds provision of infrastructure for basic services, roads and social infrastructure for poor households in all non-metropolitan municipalities. MIG allocations are made via a formula, with vertical and horizontal divisions. Poor households are defined in the MIG formula as those earning less than R2 300 per month (rough twice the value of an old age pension).

The vertical allocations occur across sectors such as basic residential infrastructure (proportional allocations for water supply and sanitation, roads and other services such as street lighting and solid waste removal), public municipal service infrastructure (including sport infrastructure) and allocations for social institutions and micro-enterprise infrastructure. The horizontal division takes account of poverty, backlogs and municipal powers and functions in allocating funds to municipalities.

There are 4 main categories of intergovernmental conditional grants:

- Schedule 4, part B sets out general grants that supplement various programmes partly funded by municipalities.
- Schedule 5, part B grants fund specific responsibilities and programmes implemented by municipalities.
- Schedule 6, part B grants provide in-kind allocations through which a national department implements projects in municipalities.
- Schedule 7, part B grants provide for the swift allocation and transfer of funds to a municipality to help it deal with a disaster or housing emergency.

In the past, local government conditional grant baselines tended to remain stable and predictable over the medium term, creating funding certainty. In recent years prior to the pandemic, the local government grant allocations have seen cuts due to fiscal consolidation at national government level or to fund higher political priorities. For instance in the Budget in February 2018, national government announced a R19.9 billion cut to local government conditional grant to fund free free higher education, a priority so new that it had not appeared in the Medium Term Budget Policy Statement in October of the previous year (South African Cities Network, 2019).

Other less significant revenue sources include rental income and interest on short and long term investments (money market, bonds, repurchase agreements).

In terms of section 230 of the Constitution, municipalities can borrow for capital purposes and bridging finance within a financial year, but not for financing operating expenditure. Lenders include retail banks and the Development Bank of South Africa.

3.2 District municipality powers and functions

The Municipal Structures Act, 1998 envisages that a DM should fulfil a co-ordinating and supporting role with respect to the local municipalities in that district, to:

"achieve the integrated, sustainable and equitable social and economic development of its area as a whole by-

> (a) Ensuring integrated development planning for the district as a whole;
> (b) Promoting bulk infrastructural development and services for the district as a whole;
> (c) building the capacity of local municipalities in its area to perform their functions and exercise their powers where such capacity is lacking; and
> (d) promoting the equitable distribution of resources between the local municipalities in its area to ensure appropriate levels of municipal services within the area."

DM core functions include:

Integrated development planning, potable water supply systems, bulk supply of electricity domestic waste-water and sewage disposal systems, solid waste disposal sites, municipal roads which are part of the road transport system for the district, regulation of passenger transport services, municipal airports serving the district, municipal health services, fire-fighting services serving the district, fresh produce markets and abattoirs serving a major proportion of the local municipalities, cemeteries and crematoria serving a major proportion of the local municipalities, promotion of local tourism for the district, and municipal public works

The responsibility for municipal health (which was not an original function of DMs but conferred later) encompasses: water quality monitoring, food safety control, industrial and domestic solid waste management (including health care risk waste, hazardous waste and effluents), vector/pest control, disposal of the dead, chemical and pollution control (water, air, soil and noise. Interestingly from the perspective of the coronavirus pandemic, the municipal health function also includes surveillance of communicable diseases, aimed at prevention of disease outbreaks in communities (PDG, 2017).

The functions performed by DMs vary in practice differ across provinces and even across districts. DMs may offer value-adding services which are non-core e.g. affordable municipal resorts and camp sites, rural social and cultural activities and infrastructure. West Coast, Overberg and Eden DMs have resorts which generate some income, which are seen as cost recovery assets rather than profit centres. In general, maintenance has not been adequate and significant upgrade is required,

Minimum norms and standards introduced by national Departments are often unaffordable. For instance, DMs are required to have one health practitioner per 15000 people was in place until December 2015, but then this was increased. DMs like Central Karoo DM accordingly have vacancies for Environmental Health Practitioners. Minimum service standards for fire protection are clearly defined in SANS10090 on *Community Protection against fire.* Service levels are specified in terms of response time, personnel required to operate fire-equipment, the number of "appliances" needed to respond to any incident (varied by risk category), and the minimum response times.

Environmental protection is also a relatively new function with norms and standards for biodiversity, coastal management, air quality and waste management embedded in various pieces of environmental management legislation. These include: preparation of a state of the environment report (by DMs and Metros), a strategic environmental assessment as part of the Municipal Spatial Development Framework under Spatial Planning and Land Use Management Act, 2013, development of a coastal management programme with enforcement and compliance dimensions, an invasive alien species control plan, The issuing of air quality licenses for listed activities in the district, along with other planning, coordinating and reporting requirements related to air quality and ensuring the National Environmental Management Act, 1998 principles are applied across municipal operations, and general alignment with an number of provincial and national plans (PDG, 2017).

Rural social development has emerged as a key priority in DMs, since LM gravitate towards an urban focus, given their focus on infrastructure services (PDG, 2017). DMs have also had to assume increased responsibilities in terms of national department sector legislation, which have not always been accompanied by commensurate increases in funding.

Unlike LMs which have access to service charges and property rates revenue, DMs are largely reliant on intergovernmental transfers. They therefore have virtually no control over their revenue sources. The only portion of the Equitable Share grant received by DMs is for providing municipal health services. These amounts are also offset against fiscal capacity of the municipality to raise own revenues so that the more affluent DMS (such as Cape Winelands) receive negligible amounts. Only the Central Karoo DM is eligible to receive the councillor support grant.

The strengths of the current equitable share formula are that:

1. Funding follows the formally assigned functions and treats similar municipalities the same way.
2. It is formula- based and therefore difficult to manipulate.
3. It provides high level of stability and predictability (three-year indicative allocations with 100% guarantee for year one and 90% for year two), and
4. Includes basic services provided.

Criticisms include that:

1. The formula does not capture service delivery progress or migration between censuses.
2. It is strongly population biased (which may be biased against geographically larger provinces with low population densities).
3. It is perceived as difficult to understand and not very transparent.
4. Costing of basic services is not accurate and that the costing does not differentiate (taking into account cost disabilities in certain municipalities e.g. rural municipalities).
5. the functional structure is ineffective, with the majority of the value of allocations determined through the adjustment factor (Western Cape Department of Economic Development and Tourism, 2015).
6. The growth of poor households is factored into the Equitable Share formula but this is done on the bases of projected growth applied to outdated datasets Census 2011 data and Community Survey 2016 data.

While in aggregate municipalities raise 75% of their revenues from own revenue sources, rural municipalities, with greater concentrations of poverty and less economic activity, are more reliant on the Equitable Share grant for up to 80% of their operational budgets and on conditional grants to finance 75% of their capital budgets (South Africa. Financial and Fiscal Commission, 2019).

Based on the need to accommodate household service growth and the reduction of backlog by 15% per annum, 2015 study commissioned by the Financial and Fiscal Commission suggested that the MIG allocation, only met 74% of all municipalities' electricity capital needs, Based on the same assumptions, there was a 37% shortfall for solid waste. While the MIG and USDG grant appeared to be sufficient to finance water service infrastructure, roads and storm water service appeared under-funded (i @ Consulting (Pty) Ltd, 2015).

Prior to 2006/07, DMs and metros raised levies on local businesses through a Regional Services Council (RSC) levy, it was found to be unconstitutional and inefficient, inequitable and poorly administered tax instrument. An RSC Levies Replacement Grant was allocated to them to compensate for the levies forgone. Subsequently, the RSC levies replacement grant for metros was replaced by sharing of the general fuel levy. Since 2010/11, the grant has increased three times faster for DMs authorised for water and sanitation (7.2% in 2020/21), compared to unauthorised DMs. All DMs in the WC are neither authorised as water service authorities nor are not the authority for any household infrastructure services, except for West Coast DM which is a water services authority and received water own revenues. The modest surplus which West Coast DM derives from water own revenues can be used for cross-subsidisation, whereas this is not possible in other DMs.

The RSC Replacement Grant was supposed to be an interim arrangement, but – more than a decade later – no own revenue source for DMs has been designated.

3.3 Agency, delegated and assigned functions

Municipalities may, in addition to their original powers and functions, also perform additional functions through assignment, delegation or agency arrangements[1] which would otherwise fall within the jurisdiction of another sphere.

In firefighting, the demarcation between LM and DM firefighting functions are not clear. Poorly resourced, rural and remote LM's may not be able to afford to operate a fire prevention service, so this function may be fulfilled by DMs.

Some DMs in the WC received the structural fire-fighting services function of LMs in that district in 2005 and thus perform it on behalf of these LMs in addition to their district fire function. These are Overberg District Municipality on behalf of Theewaterskloof, Cape Agulhas and Swellendam local municipalities, and Eden District Municipality on behalf of Kannaland Local Municipality.

In principle, LMs should pay the DM for services rendered under a Service Level Agreement. In practice, LMs may not be able to compensate DMs in full or in part, which results in an unfunded or underfunded mandate for DMs. This inability to recover costs then undermines the sustainability of DMs.

In 1998, the Department of Provincial and Local Government (now known as the Department of Cooperative Government and Traditional Affairs) issued a White Paper on Local Government to look at reform of the structure and functions of local government, including the role of DMs in a 2 tier system. That process was never concluded. Now – 20 years after the introduction of wall-to-wall local government – may be a good time to resurrect that process. Until the local government functional framework is finalised, agreeing on a long term financial framework for municipalities is well-nigh impossible.

3.4 The financial impact of policy and regulatory decisions taken by other spheres of government

As noted earlier, some norms and standards set by national government departments are unaffordable to local municipalities. Policy and legislative decisions are made at the national sphere often have implications for municipal finances which are not given the attention they merit. An illustrative case in point would options for land expropriation. If the expropriated land is transferred to their new owners with all concomitant rights and obligations, it would

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[1] In terms of section 10 of the Municipal Systems Act, 2000, section 238 of the Constitution.10 and the Guidelines on Allocation of Additional Powers and Functions to Municipalities published in G.N. 490 of 2007 (GG No.29844 dated 26 April 2007)

grow municipalities' rates. Conversely, should the state expropriate all eligible agricultural, commercial and residential land, retain ownership but lease it back to users, this would result in loss of rates revenue to municipalities if the state does not assume the liability for property rates ((South African Cities Network, 2019). Similarly, the regionalization of landfill sites is an appropriate response to local municipalities' waste sites reaching capacity, but it entails higher transport costs for participating local municipalities, and hence higher tariffs need to be set. While each national department takes decisions within their own mandated areas in a piecemeal fashion, seldom is the cumulative impact of such decisions on municipalities adequately considered, given that delivery models and cost structures can vary markedly across municipalities.

3.5 National regulation: collective bargaining and bulk serve regulation

Personnel related costs are a major cost driver for municipalities, and they are largely a function of five factors: staff numbers (head count), management of overtime, salary levels, salary increases and benefit increases (e.g. medical aids). Municipalities have more direct control over the first 3 factors whereas salary increases are centrally bargained at the South African Local Government Bargaining Council (SALBC). The current salary and wage collective agreement for the period 1 July 2018 to 30 June 2021 awarded a 7% in 2018/19, 6.5% in 2019/20 (CPI at 5% plus 1.5%) and 6.25% in 2020/21 (CPI of 5% p1.25%). Once annual notch increases are factored in, a 6% increase ends up closer to 9%, to which medical aid and other benefit increases must be added.

As a result of the Covid-19 pandemic, National Treasury presented a proposal to the SALGBC that municipalities be exempted from the third leg of the collective agreements, due to fiscal constraints due to Covid-19 (which has inter alia resulted in a R230 billion tax collapse). Consequently, SALGA attempted to re-open negotiations on the salary increases applicable from 1 July 2020, which was fiercely opposed by SAMWU, the South African Municipal Workers Union (South African Cities Network, 2021)

Thus while the South African system of intergovernmental fiscal relations is fairly decentralized, bargaining in regards to wages and conditions of services is centralized.

Over the past few years, employment costs have escalated in excess of inflation (including those of medical aid, pensions and other benefits), while operating transfers to the local sphere have been curtailed due to fiscal consolidation prior to the pandemic, and then the need to reprioritize funds to direct them towards the Covid-19 response. This situation is exacerbated by annual notch increases, resulting in an untenable situation for smaller, grant dependent municipalities which do not have significant own revenue bases.

Electricity bulk purchase costs are regulated by the National Energy Regulator of South Africa which also regulates the average tariffs municipalities may charge their users. In recent years, bulk purchase costs have been increasing faster than the tariffs municipalities may set for end users, compelling municipalities to absorb these increases. Besides direct revenue losses due to Eskom load shedding which have become an entrenched feature of the economic landscape, disruption in continuity of service and higher electricity prices create an incentive for consumers to migrate off grid and depriving cities of a debt collection instrument, since cutting of electricity to leverage the payment of other services is no longer an option (South African Cities Network, 2019).

Water tariffs have also increased in response to the 2018 drought as a demand management strategy, which has garnered increased revenue in the short term but has resulted in permanently reduced long term consumption and increased bad debt, thereby impacting on municipal revenues.

Given that bulk purchases of electricity from Eskom or water from district municipalities with water concessions, for instance, are a large proportion of municipal operating budgets, the impact of regulatory decisions in these domains have a massive impact on the financial and operational sustainability of local municipalities and metros.

4 Sustainability trends in the Western Cape: Pre-pandemic

This section summarises existing research on municipal sustainability trends prior to lockdown in March 2020.

In 2018/19, two independent surveys rated the WC municipalities as the most financially viable and stable of all nine provinces in South Africa. There is, however, considerable variation across municipalities in the Province.

Ratings Afrika based their assessment on the analysis of municipality's annual financial statements as at 31 June 2019. They define financial stability as the ability to deliver services, develop and maintain the infrastructure required by its residents without unplanned increases in rates and taxes or a reduction in the level of services, as well as to absorb financial shocks caused by external factors, without needing financial assistance from third parties. Table 1 shows that the WC municipalities far exceed the national average, and have generally shown improvements between 2014 and 2017, with a slight regression in 2018.

TABLE 1 RATINGS AFRICA'S MUNICIPAL FINANCIAL STABILITY INDEX, 2014–2018

Average index scores by Province					
Province	2014	2015	2016	2017	2018
Eastern Cape	37	40	37	33	28
Free State	27	24	22	19	17
Gauteng	36	31	34	31	31
KwaZulu-Natal	58	62	56	55	51
Limpopo	55	48	46	44	29
Mpumalanga	27	30	28	28	30
Northern Cape	45	56	54	46	33
North West	30	26	29	23	24
Western Cape	52	59	61	65	63
National average	43	45	43	42	38

Source: BusinessTech, 2018

Swartland (with a score of 86) was found by Ratings Afrika to be the top performing municipality in the province, with Drakenstein, the lowest scoring municipality (with a score of 18).

Good Governance Africa's Government Performance Index for 2019, index ranks 213 local municipalities based on 3 main indicators: quality of administration (e.g whether there are sufficient skilled personnel, financial management and reporting), economic development, and service delivery (e.g. water, sanitation, education, electricity, housing, waste removal, healthcare and policing). They find that Mossel Bay municipality in the WC is the best-run municipality in the country, followed by the Senqu municipality in the Eastern Cape and Swartland Municipality in the WC. Besides taking first and third place, there were also 10 other WC municipalities in the top 20: Bergrivier (8), Cape Agulhas (9), Prince Albert (10), Swellendam (11), Cederberg (12), Matzikama (13), Overstrand (14), Witzenberg (15), Hessqua (19) and Langeberg (20)

Yet there is considerable variation in terms of financial sustainability in the Province, with some municipalities experiencing threats to their sustainability. Sections 138 and 140 of the Municipal Finance Management Act, 2003, sets out indicators of indicators of financial stress in a municipality which could serve as a trigger for a section 139 intervention. National Treasury compiles an annual Financial Distress Trigger Index for each municipality based on these variables: failure to may payments as and when due (more than 90 days); an operating deficit greater than 5% of total direct revenue, negative or outstanding audits, negative cash positions for 2 consecutive years, and a failure to make any other payment more than 2% of operating expenditure to Eskom, water boards or total creditors. As at June 2020, based on these criteria, 4 municipalities in the WC were deemed to be experiencing financial distress: Matzikama, Cederberg, Theewaterskloof and Laingsburg. Kannaland LM has been under S139(5) administration since December 2016.

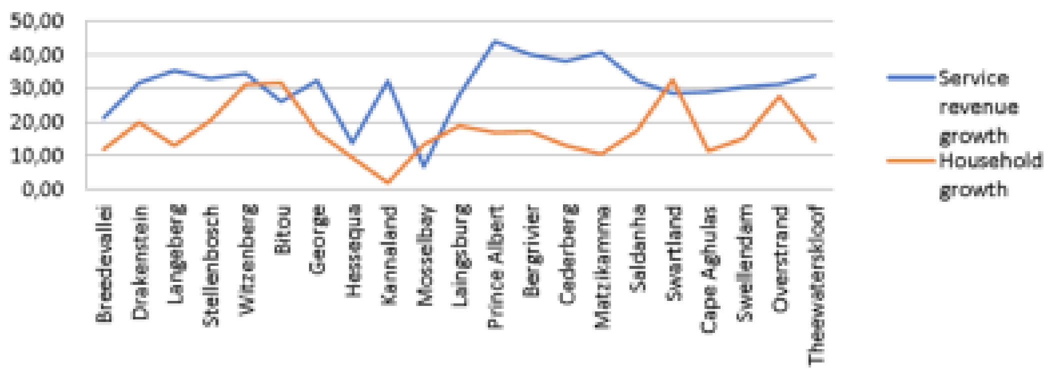
4.1 Local municipality sustainability trends in the Western Cape

Key pre-pandemic sustainability trends in LMs are discussed below, relating to fiscal capacity and operating revenue, operating expenditure, governance expenditure, liquidity, debtors management and potential new revenue sources.

4.1.1 Fiscal capacity and operating revenue trends

Growth of households impacts both on the demand for municipal service, and – to the extent they are willing and able to pay for these services – also on service revenue.

FIGURE 4: ANALYSIS OF THE GROWTH OF SERVICE REVENUE RELATIVE TO HOUSEHOLD GROWTH, 2017/18

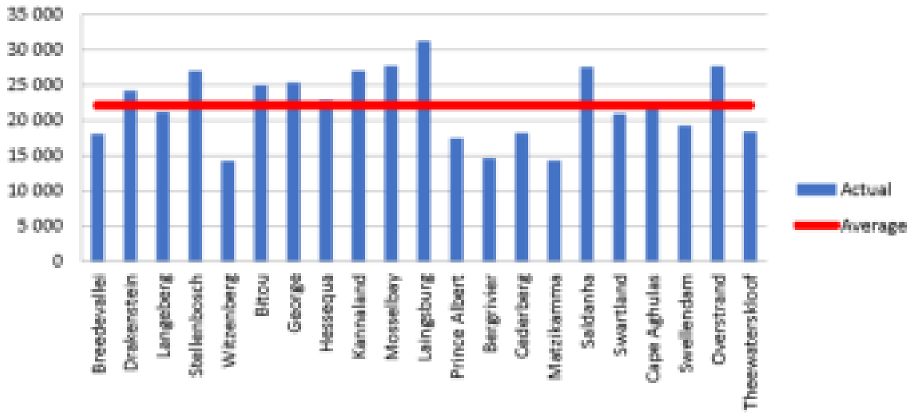


Source: Schwella, Brand, Van der Westhuizen, & Faurie, 2018: 31

The larger municipalities with more economic opportunities tended to exhibit the fastest growth in households: Witzenberg, Bitou, Swartland and Overstrand, and to a lesser extent, Drakenstein and Stellenbosch. In general, service revenue growth is expected to increase with the number of households in a municipality. However, in Kannaland, Bergrivier and Cederberg, service revenue has exceed household growth. In the case of Kannaland and Cederberg, this is due to intergovernmental grants, whereas in Bergrivier it is driven by effective implementation of credit control policies (Schwella et al, 2018).

Considering municipal operating income per households (see Figure 5), the wide variation across LM's is clearly apparent.

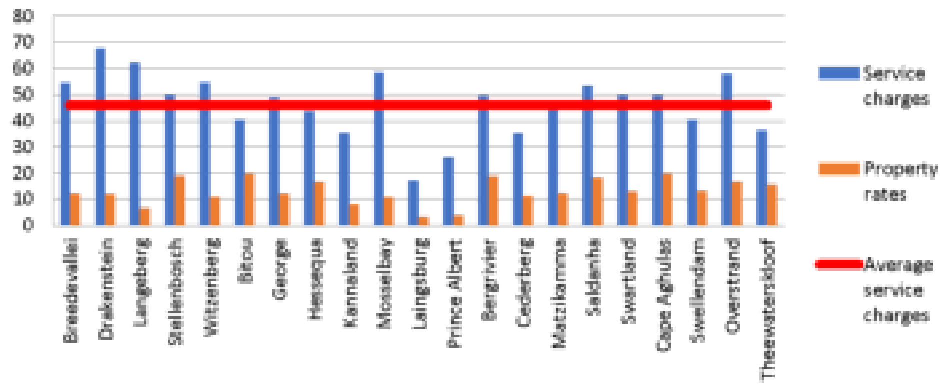
FIGURE 5: MUNICIPAL INCOME PER HOUSEHOLD, 2017/18



Source: Schwella, Brand, Van der Westhuizen, & Faurie, 2018: 31

For some LMs, income per household is largely driven by strong fiscal capacity and own revenue bases for service charges and property rates (e.g. Drakenstein, Stellenbosch, Mosselbay, Saldanha and Overstrand). Other LM's (such as Kannaland and Laingsburg) have income per households greater than the average, which are not driven by own revenues, which are below average (see Figure 6 below).

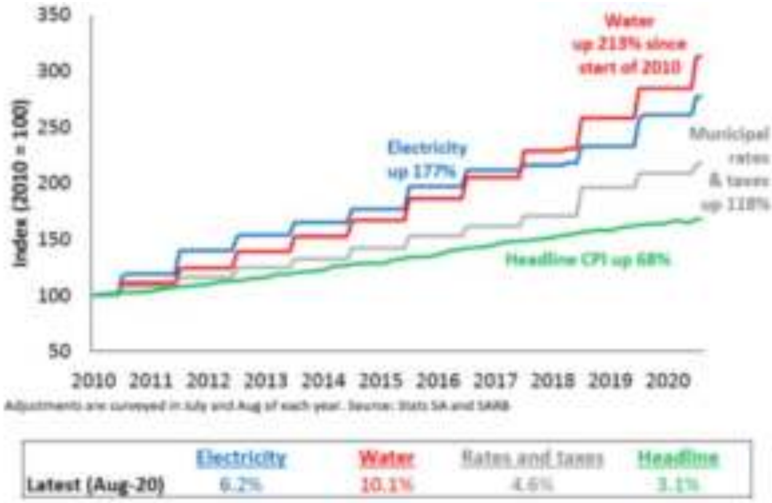
FIGURE 6: MUNICIPAL OWN REVENUE AS A PROPORTION OF TOTAL INCOME, 2017/18



Source: Schwella, Brand, Van der Westhuizen, & Faurie, 2018: 30

While tariffs are required by law to be cost-reflective (as mentioned earlier), this must be balanced against decreasing affordability of municipal services. Electricity, water tariffs and municipal rates and taxes have escalated by 177%, 213% and 188% respectively since 2010, far in excess of headline CPI inflation, which only increased by 68% over the period.

FIGURE 7: INCREASES IN MUNICIPAL ELECTRICITY AND WATER TARIFFS



Source: South African Reserve Bank 2020 Monetary Policy Review

Not only do WC municipalities have greater fiscal capacity than many of their counterparts in most of the other provinces, they also typically exert greater fiscal effort. Revenue collection rates in the Western Cape (and Gauteng) ranged between 80–90%, vis-à-vis 70–80% average in other provinces. In 2014/15, roughly a quarter of households in the WC were receiving free basic services (Schwella et al, 2018).

4.1.2 LM operating expenditure trends

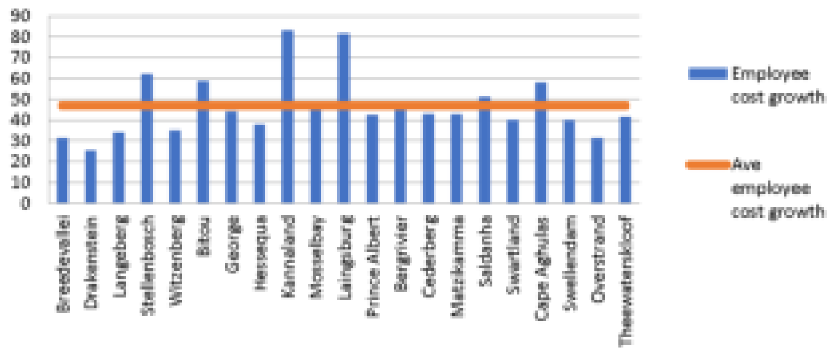
Schwella et al (2018) point out that while there is data on expenditure, data on costs of services is much more sparse and unreliable, even in audited financial statements. For instance electricity spending less bulk services has been reported as negative in some municipalities. This is concerning since realistic, cost-recovering baseline tariffs cannot be set without accurate fixed and variable costs.

Operating surpluses from electricity and water were used for cross-subsidisation, but these have been placed under pressure by increases in bulk service cost and personnel increases. Previously around 1998, South Africa had some of the lowest bulk electricity prices in the world, and municipalities earned significant margins on the sale of electricity (PARI, 2020). In recent years, loadshedding (which reduced municipal revenue), sharp increases in Eskom tariffs and the cap on prices municipalities may charge the final consumer imposed by the National Energy Regulator of South Africa (NERSA), and reduced electricity demand as consumers move off the grid, have all steadily eroded that surplus. NERSA have approved tariff increases of 9.4% in 2019/20, 8.1% in 2020/21 and 5.2% in 2021/22. Changes to South Africa's Electricity Regulations on New Generation Capacity legislation gazetted in October 2020 will allow municipalities in good financial standing to produce their own power and and purchase power directly from independent power providers, bypassing Eskom. This would be a breakthrough for municipalities over the medium to long term, but there is still some uncertainty around the implementation details. Except for Rand Water Board's proposed tariff of increase 6%, SALGA rejected 8 water boards' proposed increases[2], suggesting that an independent water regulator might be called for (ESI-Africa, 2020). The City of Cape Town is in the fortunate position of being a producer of bulk water, rather than being served by a water board.

Cost of employment is one of the largest components of LM budgets. While municipalities have control over staff numbers, management of overtime and salary levels, increases in conditions of service are centrally bargained. Except for Stellenbosch, the municipalities which performed the poorest (such as Kannaland and Laingsburg) tend to have the biggest increases in personnel costs between 2011 and 2016 (see Figure 9). The South African Local Government Bargaining Council concluded a three year wage collective agreement for the period from 1 July 2018 to 30 June 2021 which awarded increases of 7%, 6,5% and 6.25% in 2018/19, 2019/20 and 2020/21 (SALGA, 2018).

For most LMs, personnel related spending is one of their major cost drivers. While they retain some control over personnel headcount (subject to labour legislation), wage rates full largely outside the control of an individual LM or DM, with cost of employment determined centrally at the Local Government Bargaining Council and gazetted norms for senior management and councillors. Cost of employment increases have generally exceeded increases in intergovernmental grants and other sources of revenue.

FIGURE 8: EMPLOYEE EXPENDITURE GROWTH, 2011--2016



Source: Schella et al. (2018)

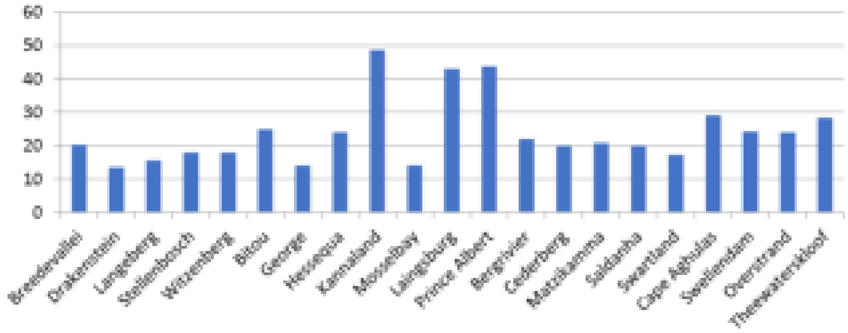
SALGA has pointed out that the health sector has recognised that attracting well qualified and experienced doctors to rural areas requires additional financial incentives, but the municipal compensation framework has not. The current regulatory framework puts an upper limit on the salary scale of municipal managers based on the grading and category of a municipality which has had "the unintended consequence of depriving small, rural and poor municipalities of the high calibre skills necessary to turn them around" (Nkadimeng, 2020).

[2] Amatola Water — 8.28%, Bloem Water — 9%, Lepelle Northern Water — 8.5%, Magalies Water — 12%, Mhlathuze Water — 9.37%, Overberg Water — 8%, Sedibeng Water — 7.5%, Umgeni Water — 9.6%

4.1.3 Spending on Governance mandated responsibilities

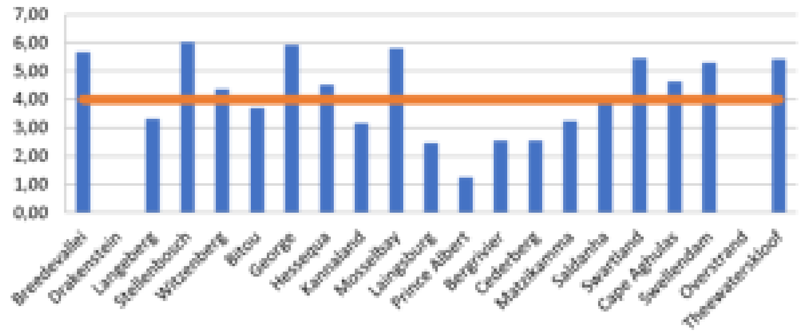
Governance costs encompass spending on the political structure such Councillor remuneration and support and are driven by number of councillors, portfolio committees, support staff etc. Administration costs senior management costs, finance, IT, HR and other corporate expenditure. This category varies markedly across municipalities (as illustrated in Figure 9 below), with Kannaland, Laingsburg and Prince Albert particularly high.

FIGURE 9: GOVERNANCE AND ADMINISTRATION COST AS A PROPORTION OF TOTAL OPERATING EXPENDITURE



Maintenance as a percent total spending in Laingsburg, Bergrivier, Cedarberg and Prince Albert were low in 2017/18 relative to the 4% recommended by National Treasury (see Figure 10 below).

FIGURE 10: MAINTENANCE AS A PROPORTION OF TOTAL OPERATING EXPENDITURE



Note: data for Drakenstein not reported.
Source: Schwella et al, 2018

Audit fees are determined by the Auditor-General based on the time to complete the volume of audit work required to express an opinion. Table 2 illustrates that, with few exceptions, audit fees are much higher than 1% of the budget,

TABLE 2: AUDIT FEES PER HOUSEHOLD, 2013/14

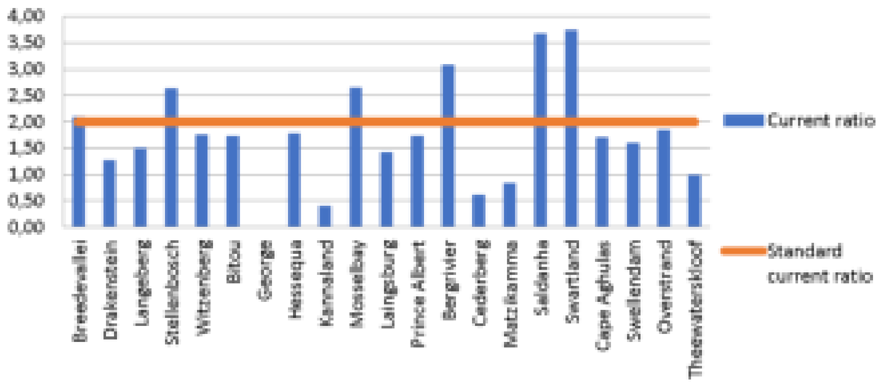
Test Data	Province	Cat	Number of Households (2014/15)	Actual Audit Fees (2013/2014)	Audit Fee per Household	Calculated Audit Fee @ 1%	Difference (1% vs. Actual)
Buffalo City	EC	A	227 315	11 692 400	51	54 700 136	79%
Drakenstein	WC	B1	61 378	5 447 663	89	18 084 091	70%
Stellenbosch	WC	B1	45 059	4 753 380	105	13 018 536	63%
City of Matlosana	NW	B1	122 662	2 021 883	16	21 257 742	90%
Mogale City	GAU	B1	122 115	215 530	2	26 593 117	99%
Polokwane	LIM	B1	185 357	4 897 935	26	28 383 354	83%
Knysna	WC	B2	22 676	5 415 766	239	6 342 014	15%
Midvaal	GAU	B2	31 507	2 140 825	68	7 573 737	72%
Hessequa	WC	B3	16 201	2 098 988	130	3 923 703	47%
Mnquma	EC	B4	70 184	2 964 222	42	2 650 490	-12%
Moses Kotane	NW	B4	76 134	2 445 503	32	6 227 551	61%
Nkangala	MPU	C1	371 694	2 946 563	8	4 517 461	35%
Xhariep	FS	C1	45 874	2 269 611	49	617 899	-267%
Joe Gqabi	FS	C2	99 323	4 770 494	48	6 362 241	25%

Source: i @ Consulting (Pty) Ltd, 2015

4.1.4 LM liquidity

The current ratio (defined as current assets divided by current liabilities) is a measure of a municipalities ability to meet its short term financial commitments to debt-holders, suppliers and other creditors. While Bergriver, Saldanha and Swartland have liquidity positions significantly better than the norm of 2, Kannaland, Cedarberg and Matzikama have significantly lower coverages, indicating financial stress.

FIGURE 11: CURRENT RATIO

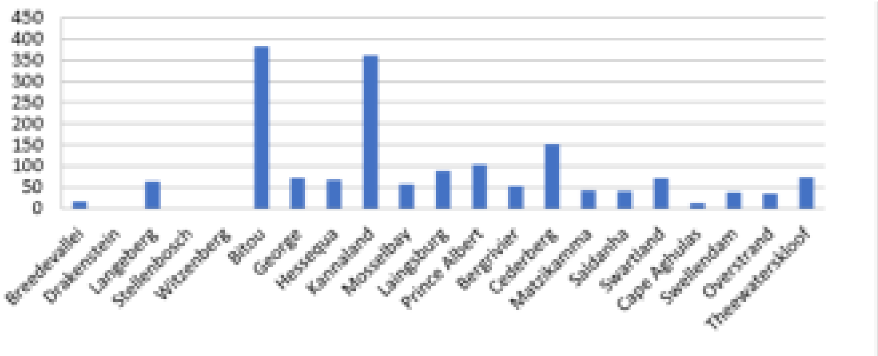


Note: data for George not reported.

Source: Schwella et al, 2018

The MFMA requires that creditors be paid within 30 days. Bitou, Kannaland – and to a lesser extent – Cederberg were all greatly in excess of this guideline.

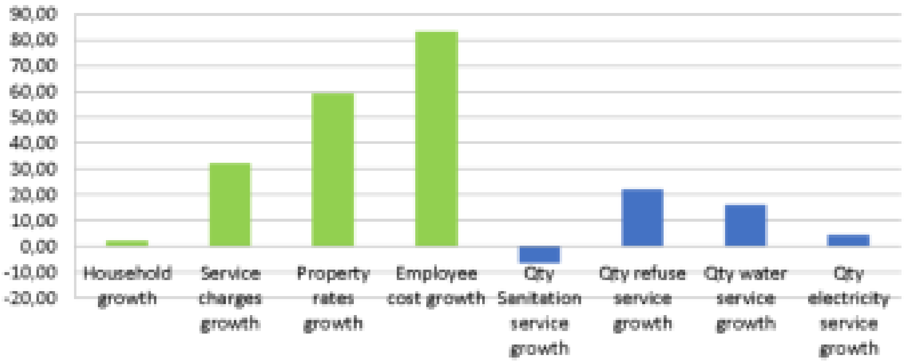
FIGURE 12: CREDITOR PAYMENT IN DAYS



Note: data for Drakenstein, Stellenbosch and Witzenberg not reported.
Source: Schwella et al, 2018

In Kannaland, employee growth exceeded both property rates and services charges growth, while household growth was marginal and increases in service growth was much smaller. A top heavy personnel establishment was placing pressure on property rates and service charges, despite significant intergovernmental transfers.

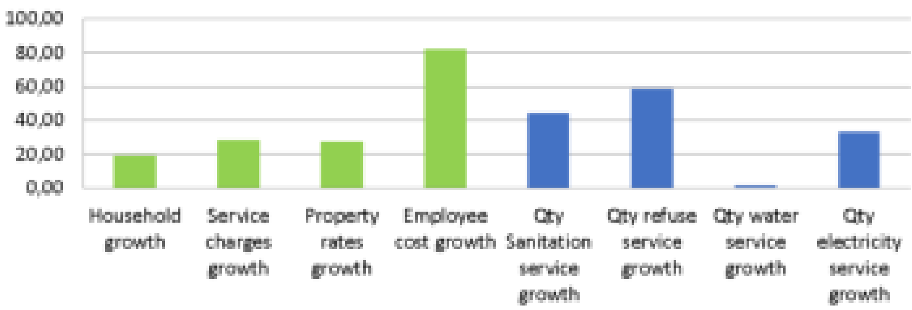
FIGURE 13: KEY DRIVERS FOR SERVICE DELIVERY IN KANNALAND



Source: Schwella et al, 2018

A similar pattern is evident in Laingsburg (see Figure 14), but the rate of property rates and service charge growth has been less, and improvements in service delivery more pronounced.

FIGURE 14: KEY DRIVERS FOR SERVICE DELIVERY IN LAINGSBURG



Source: Schwella et al, 2018

4.1.5 Existing revenue sources: debtor management and credit control

Average revenue collection rates in the Western Cape reported in s71 reports as at June 2020 was at 99.4%, much higher than the national average of 82%. However there is considerable variation, with municipalities such as Cedarberg, Swartland and Langeberg having recovery rates of 100% or more, other have considerably lower collection rates: Matzikama 81.1%, Kannaland 74% and Beaufort West 61.7%

Revenue collection performance is influenced by a host of factors, some of which relate to fiscal capacity (which are largely outside the control of municipalities) and others to fiscal effort (which municipalities can influence). Economic downturns, increasing unemployment, natural disasters such as drought, in-migration of poor households, a culture of non-payment, construction of state subsidised RDP housing for indigent households can all influence fiscal capacity. Other operational factors relate to fiscal effort include unsatisfactory metering operations and management (e.g. servicing), disruptions in the continuity or quality of water and electricity supply, as well as tampering with electricity and water meters and other forms of illegal connection.

For instance, the Financial and Fiscal Commission found that water service payments had decreased from 61.9% of the billed amount in 2005 to 43.9 per cent in 2015 due to factors beyond the control of the municipality (such as droughts exacerbated by climate change, reduced demand due to water conservation awareness and behaviour change by companies and household and a culture of non-payment), as well as internal financial and operational challenges such as ineffective invoicing systems and technical water losses due to dilapidated infrastructure (South Africa. Financial and Fiscal Commission, 2019).

Fiscal effort is also compromised by the poorly designed revenue management, debtor and indigent policies, weak implementation of debt collection and credit control policies, imprecise consumption estimates(leading to invoice queries and late payment or bad debt), inaccurate billing from dysfunctional invoicing systems, weak credit control measures, ineffective customer service mechanisms, inaccurate, incomplete and outdated customer databases, lack of visible political support for revenue enhancement programmes by mayors and councillors (who are often themselves also in arrears), and insufficient skills/capacity in the revenue section. Billing systems which do not reconcile with the deeds registry or valuation rolls can undermine the verification of the completeness of revenue. Processes for identifying, registering and maintaining an up to date database are often bedevilled by fraudulent applications. Poor coordination among departments and business units may undermine the effectiveness of the revenue collection process. Systems for exception reporting and triggering investigations are not always in place, Processes for managing refunds may not be efficient and unallocated payments are placed in suspense accounts, which in turn lead to apparent non-payment. To promote a payment culture, consumer debt write-offs should not be arbitrary but only in terms of policy and be largely confined to prescribed debt, uncollectable debts and indigent debt (with a move to prepaid meters) (Western Cape Department of Economic Development and Tourism, 2015).

Between 2011/12 and 2017/18, non-payment of municipalities by other organs of state has increased steadily R50 billion, with municipalities in turn owing creditors more than R150 billion. (South Africa. Financial and Fiscal Commission, 2019)

Key elements of the revenue management process include consumption monitoring daily with monthly invoicing, levying of interest for invoices not paid by due date, warning letters, disconnection orders, hand over to debt collectors or attorneys, final demand letters, adverse credit rating, summonses and judgement warrants if the debt still has not been settled. Some municipalities have been able to use the process for issuing clearance certificates before the transfer of properties as a means to leverage debt collection. Other special debt collection initiatives include collection of staff and councillor arrears (via salary deduction, debit order and/or normal debt collection), collection of government department debt, electricity pre-paid as collection mechanism, restriction of consumption (disconnection, restriction and/or blocking), indigent categories and process (investigation, re-apply and blocking), sales in execution,, collection in terms of business rescue principles, door to door collection principle, debt payment incentives (interest rebates) and "naming and shaming" publication of outstanding debt amounts (Tesselaar, 2017).

Eskom sometimes supplies areas within a municipality. While municipalities have a constitutional mandate to distribute electricity, they have no levers to compel payment in Eskom supplied areas within their jurisdictions. The Financial and Fiscal Commission has recommended that Eskom and municipalities should align their credit control systems and that Eskom should assist municipalities with credit control via electricity disconnections within the municipality's area supplied by Eskom (South Africa. Financial and Fiscal Commission, 2019). SALGA has suggested the following proposals to enhance revenue collection:

1. Measures to write-off the ever increasing household debts to municipalities, including the introduction of a national Bill for the writing off of these household debts in exchange for the installation of prepaid water and electricity meters;
2. Amendment the Tax Administration Act so that before SARS pays tax refunds, they first check is the particular tax payer does not have monies due to his/her municipality. If the tax payer owes, the amount due to the municipality will be paid first before a refund is deposited to the tax pay account.
3. Amendment of schedule 2 section 10 of the Municipal System Act so that all state employees and elected and appointed representatives in other spheres – not just municipal councillors and employees – who may not be in arrears with their municipal bills for a period more than three months.
4. Establishment of a District Revenue Collection Agency to achieve better collection efficiencies and will free up municipal personnel to focus on service delivery. SARS systems and processes would be considered in putting this together after due diligence is done.
5. Amendment of the Procurement Regulations to make it compulsory for any potential service provider to produce a Municipal Services Rates compliance certificate, prior to being awarded a government contract. (Nkadimeng, 2020).

TABLE 3: AN ASSESSMENT OF MECHANISMS FOR INCREASING PROPERTY RATES IN SOUTH AFRICA

	MECHANISM FOR INCREASE	REVENUE GENERATION	COST IMPLICATIONS	COMPLEXITY	POLITICAL/ PUBLIC ACCEPTABILITY
Undergo a rates base determination	All properties in the city will be covered, so full value is captured through rates	Limited to those properties not captured in current rates base	Assessing all properties will be very costly	Assessing all properties will be laborious and lengthy	Unlikely to face undue resistance
Increase the cent in the rand charged	Rates charged per property will increase	Unlimited	Negligible costs associated with legislative processes	Lengthy legislative process and bureaucracy	Guaranteed widespread public resistance
Re-evaluate all properties in the city	More frequent re-evaluations will reduce the lag-time between value growth and growth in rates received	Limited by number of properties and growth in property values	Regular evaluation of all properties will be very costly	Regular evaluation of all properties will be very time-consuming.	Likely to be moderate resistance from the public to regular rates increases
Reduce/ remove thresholds	Reduction in or removal of rebates will broaden base of taxable properties	Limited to number of properties receiving rebates	Negligible costs associated with legislative processes	Requires overhaul of MPRA, so lengthy legislative processes	Likely resistance from poor/ indigent households. Contrary to policy/ progressive taxation regime
Improve collection rates	Higher rates of collection will increase value captured	Limited to current properties for which rates are not collected	Negligible costs associated with increased labour	Increased personnel and responsibilities	Unlikely to face undue resistance
Rezone	Property mix will include a greater proportion of properties with higher cent-in-the-rand rates	Limited only by how much non-urban land exists within municipal boundaries	Costs of rezoning predominantly for applicants or developers	Administrative burden borne largely by applicants or developers	Demand-driven process but open to public comment[4]

● favourable ● neutral ● unfavourable

[4]Rezoning applications are open to public comment and grounds for resistance. In greenfield developments, public comment and resistance are far less likely because these relatively large agricultural properties usually have few neighbouring properties and are sometimes surrounded by vacant land.

Source: South African Cities Network (2019, p. 73)

The State of City Finances Report 2018 provides a useful assessment of the mechanisms for increasing property rates, in terms of revenue generation potential, cost implications, complexity and political/public acceptability. These are summarised in the table above.

4.1.6 New sources of revenue for local municipalities

As seen in Table 4, development charges, tourism levies, fire levies, and amusement and advertisement (billboard) taxes have been identified as possible new revenue options for LMs (South Africa. Financial and Fiscal Commission, 2019), as well as dumping site usage fees.

TABLE 4: ALTERNATIVE REVENUE SOURCES

	Metropolitan Municipalities	Secondary Cities	Other Urban Municipalities	District Municipalities	Rural Municipalities
Revenue Instruments					
Development Charges	✓	✓	✓		
Fire levy				✓	✓
Advertisement Tax	✓	✓	✓		
Tourism Levies/Occupancy Tax	✓	✓	✓		✓
Amusement Tax	✓	✓	✓		
Weigh in Bridges in Mining Areas				✓	✓
Financing Arrangements					
Impact Fees	✓	✓			
Tax Increment Financing				✓	
Public-Private Partnerships	✓	✓	✓	✓	✓

Source: FFC, 2019:53

They have also suggested that the extensive land holdings of municipalities could be used to generate income. National Treasury has published the Municipal Fiscal Powers and Functions Amendment Bills, which deals with development charges for public comments (Gazette Notice number 3 of 2020) until the 31 March 2020, provides for a uniform regulation of development charges. Development charges are a once off charge levied by a municipality on the landowner as a condition for approving land development application and are intended to cover the costs incurred by the municipality when installing new infrastructure or upgrading existing infrastructure required to service the proposed development.

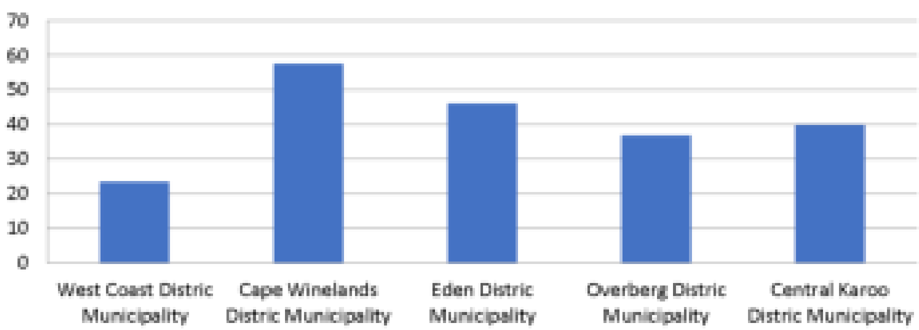
4.2 District municipality sustainability trends

Key sustainability trends relating to DM operating revenues and expenditures are explored below as well as existing research on identifying new revenue sources.

4.2.1 District municipality operating revenue trends

As can be seen in Figure 15 below, DMs are more dependent on the local government Equitable Share grants than LMs.

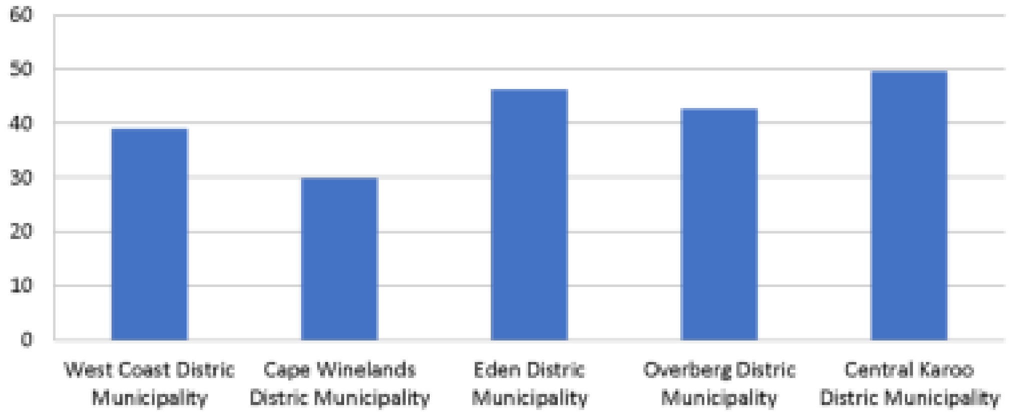
FIGURE 15: DISTRICT MUNICIPALITY RELIANCE ON INTERGOVERNMENTAL GRANTS



Source: Schwella et al, 2018

Revenue from road agency functions is also an important source of revenue. DM's may also perform agency functions for the Department of Environmental Affairs Working for Water programme. This is funded through the Municipal Extended Public Works Programme incentive grant in the annual division of revenue, which covers these costs.

FIGURE 16: ROAD AGENCY FEES AS A PROPORTION OF TOTAL REVENUE



Source: Schwella et al, 2018

DMs which have been able to build up historic reserves also receive interest income.

Over time, regulation by national and provincial departments have also eroded the few own revenue sources of DMs, for example national regulation of fees for air quality licence applications and renewals reduced this source of income for DM and boat levies (which were previously levied by West Coast DM) can no longer be levied (PDG, 2017)

Modelling by the Palmer Development Group (which separated out core functions – which include governance and overheads – from non-core spending) suggested that West Coast, Overberg and Central Karoo DMs were experiencing under-funding of core services, while Eden derived income slightly more than their core expenditure requirement. By contrast Cape Winelands DM received income significantly in excess of their core which appeared to be directed at non-core functions such as social and rural development in particular (PDG, 2017).

4.2.2 District municipality operating expenditure trends

Since DMs typically do not deliver infrastructure or purchase bulk services, their main cost driver is personnel spending. Over the last 10 years, personnel costs have grown at a much faster rate than the intergovernmental grants on which DMs are reliant (PDG, 2017).

A study conducted in 2017 noted that the high cost of financial compliance, coupled with the inability to raise own revenues, has resulted in a diversion of funds from services which meet the needs of the public towards meeting the reporting and auditing demands of national government (PDG, 2017). Cape Winelands and Eden spent more than expected on Governance and Administration, whereas Central Karoo and Overberg spend less, This study identified the following cost saving opportunities: corporate and councillor support (as opposed to remuneration), ICT costs, and printing costs for the vast number of meetings required each year. A key finding was that Cape Winelands and Eden DMs appearing to have spent more on core functions than currently required, while West Coast, Overberg and

Central Karoo do not. The availability of revenue seems to me the main reason for this (PDG, 2017)

A 2017 study found that fire services were underfunded fell short of the SANS 10090 minimum standards which was particularly concerning in the case of West Coast and Overstrand which provide a structural fire service to LMs without a service of their own.

4.2.3 Possible new revenue sources for district municipalities.

The following revenue sources have been proposed but these are likely to be marginal at best (PDG, 2017):

1. *Municipal health* user fees for items such as export certificates. Public health concerns however constrain the ability to levy fees,
2. *Air quality*: Petition the Minister who regulates fees for licences and renewals to raise the permitted fees chargeable.
3. *District fire services*: Membership of fire associations suggested as an alternative to payment for landowners who volunteer their labour: non- member, have to pay costs of fire service. The primary intention would be to incentivise participation in fire associations, rather than maximising revenue.
4. *MIG funding for rural roads*: are funded by the WC provincial government only and there are no other funds to provide rural transport infrastructure, as envisaged in the 2015 National Transport Strategic Framework.
5. *Fuel levy*: A portion of the fuel levy is currently paid to Metro's, in lieu of their former RSC levies and this may be a significant potential source of unconditional revenue, but once again would lie outside the control of the DM.
6. *Tourism or bed tax*: 1% Tourism Marketing levy is already levied on certain hotels, and is payable to the Tourism Business Council of South Africa (TBCSA) for the international marketing of South Africa. The TBCSA is struggling to collect these levies which suggests high administrative costs for DM, and the proceeds may have to be shared with LMs.
7. Environmental management revenues: new leases and concessions on coastal public property, re-evaluation and/or renewal of existing leases and concessions on coastal public property; off-road vehicle permits; dumping permits; coastal discharge permits and fines and penalties for regulatory violations.

As seen in Table 4, the Financial and Fiscal Commission has also considered fire levies, weigh in bridges (which would help municipalities recover some of the infrastructure damage cause by heavy haulage trucks), public-private partnerships and tax increment financing (which aims to capture increased tax revenue from increased property values as a result of public investment (South Africa. Financial and Fiscal Commission, 2019).

4.3 Metropolitan municipality: City of Cape Town

Three consecutive years of the driest wet seasons and persistently declining dam levels culminated in the drought being declared a disaster in May 2017, with the City becoming the first city in the world faced running out of water an "Day Zero" scenario. By end of 2018, good winter rains and the City's success in cooperating with residents to achieve dramatically reduced water consumption levels. This section will focus on the operational and financial strategies in response to this disaster, and how these would later increase the City's resilience relative to the pandemic.

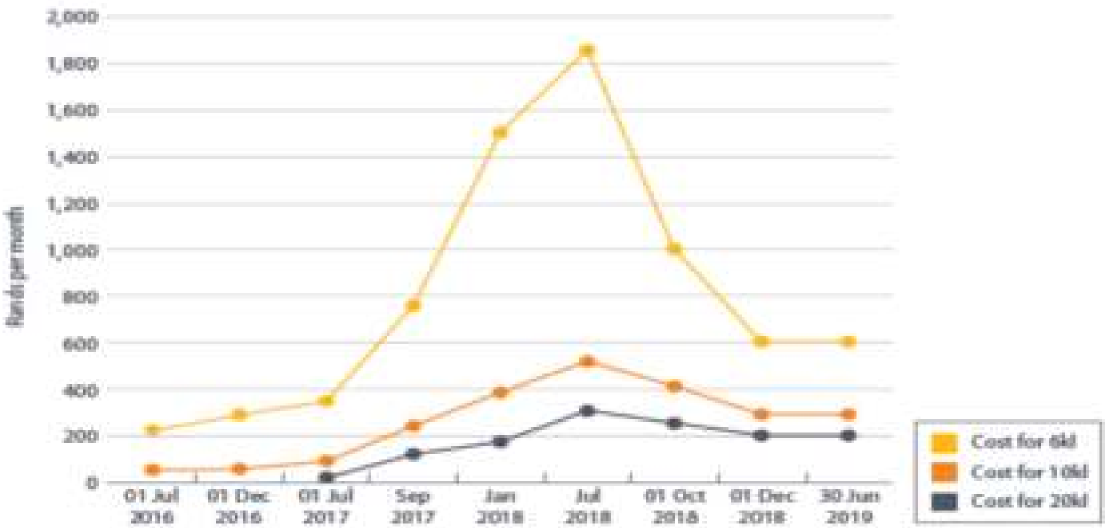
While the City relied extensively on public education and awareness raising to encourage behaviour change, directly rationing water supply, sharply increased drought water and sanitation tariffs and changes to the tariff structure were key elements in successfully restricting water consumption, as well as reduction in water leakages (which would reduce bulk water costs as well as revenue forgone). As explored below, the longer term response for water security includes investment in infrastructural programmes which then impacted the City's MTREF planned capital expenditure and capital funding mix (which are considered in greater detail later in the financial analysis this report in Section 5).

In response to dam levels which had sunk perilously low to 24.5% of capacity by February 2018, the City introduced level 6B water restrictions which limited individuals to 50kl of water a day. This resulted in a drop of water sales by 50%, incurring losses estimated at R1.6 billion for 2017/18. Water restrictions also created losses in the agricultural sector which contributes roughly 23% to the Western Cape's GDP. Moreover, the drought also discouraged tourists from visiting the province, with negative impacts on the hospitality, tourism and related industries. Water restrictions were eventually lifted by the national Department of Water and Sanitation in September 2018, after dam levels were restored to 88% of capacity. In 2020/21 the City's 5 level block tariff was de-linked from the restriction levels promulgated. Projecting water demand has become more uncertain given that some of the drop in water demand could be permanent as users adopt water saving technologies. Falling water demand also erodes water surpluses in the higher usage tariff blocks which could be use for cross subsidization.

As can be seen from the diagram below, domestic full tariff water bills for 6kl, 20kl and 40kl at the height of restrictions on 1 July 2018 were 10.4, 4.3 and 4.2 times higher than on 1 July 2017. This was not only as a result of increased charges for the higher tariff blocks (the City uses a block tariff structure with a stepwise increasing structure in which consumers in higher consumption blocks pay higher prices), but also as a result of changes in the tariff structure. The City implemented a fixed basic charge for access in 2018/19, payable at all consumption levels, and introduced a charge for the first 6KL of water and 4.2 kl sanitation (which had been provided to all households until then). This charge was then subsequently increased. The charge, however, only applied to non-indigent households. Under a different lifeline tariff, indigent customers retained their 6kl free basic service allocation, and this was increased from 6kl to 10.5kl in 2018/19. These fixed basic charges are important for the City's sustainability (as seen during pandemic where service revenues would have fallen a lot faster in their absence and because they help to ensure that the fixed costs of water provision (which can be as much as 60% of total costs) are covered. The fixed costs of electricity provision are also high (about 40% of total costs) and basic fixed charges can ensure that fixed costs are covered even if electricity sales decline as electricity users migrate to small scale embedded generation. These users do not completely exit from the grid which means that the City still needs to cover the fixed costs of operating and maintaining the grid (South African Cities Network, 2020, p. 45).

Many municipalities use household income below a threshold determined by their indigent policies as the prime indicator for indigency, but this is difficult to determine when people are earning their livelihoods in cash (e.g., in the informal sector). The City therefore focusses on property and property values (which are easier to identify) as the main criterion for indigency status in awarding service rebates. As only homeowners can open up accounts with the City, the property then becomes security for payment of the services accounts and non-payment could lead to legal process which could result in sales in execution. This also dispenses with the need for consumer deposits, lowering administrative costs and hence unit service costs (South African Cities Network, 2019).

FIGURE 17: DOMESTIC FULL TARIFF BILLS FOR 6KL, 20KL AND 40KL OF WATER FOR CITY OF CAPE TOWN (1 JULY 2016 TO 1 MAY 2019)



Source: South African Cities Network (2021, p. 14)

While there are sustainability advantages for fixed charges, they compromise the affordability of tariffs and are regressive in nature (i.e. the greatest incidence falls on those with lower incomes). Because there is such variation in tariff structures across municipalities, the *State of City Finances* 2020 report defines 4 standard service packages for different types of households, the rand values of which are compared over time. The packages are described below:

National Treasury advises that the total user tariff and property rates bill for each of the service packages should not 10% of household income. For the City, the municipal bill as a percentage of benchmark income for the poorest paying households was greater than that 10% norm: household A's municipal bill was 13.4% of benchmark income in 2019 (up from 11.8% in 2018) and for household B was 10.1% of benchmark income in 2019 (up from 8.3% in the previous year). The municipal bill of household A was, however, greater than 10% in other cities, bar Johannesburg and Nelson Mandela Bay, ranging from 11.4% of benchmark household income in eThekwini to 14.5% in Msunduzi. In Johannesburg and Nelson Mandela Bay, municipal household bills for household A were 9.9% and 10% of benchmarh household income in 2019. The City however was the only one for which household B's municipal bill as a proportion of household income of 10.1% marginally exceeded the 10% guideline, with the other cities ranging from 5.5% in Ekhurleni to 9.2% in Buffalo City Municipality (South African Cities Network, 2020).

FIGURE 18: STANDARD SERVICE PACKAGES TO COMPARE TARIFF INCREASES

SERVICE PACKAGES	PROPERTY VALUE	ELECTRICITY CONSUMPTION (KWH/MONTH)	WATER CONSUMPTION (KL/MONTH)	SOLID WASTE (WEEKLY REMOVAL OF A 240L BIN)
Type A	100,00	400	20	1
Type B	250,000	500	25	1
Type C	500,000	800	30	1
Type D	1,000,000	1500	40	1

Source: South African Cities Network, 2021 (p. 41)

In order to contain water losses, the City fixes water leaks of all indigent properties free of charge, and writes off all debt and interest charges if the indigent household agrees to the free installation of water management devices. A similar process obtains in respect of debt and interest on unpaid electricity bills subject to installation of a prepaid electricity meter free of charge.

Towards the end of the drought period, the City was criticized for over-recovering water and sanitation revenues when the much higher tariffs still did not deter water consumption as much as the City had anticipated when setting its budget. However, continued high consumption by non-paying customers resulted in provisions for bad debt exceeding budget, so that these revenue over-recoveries were not cash backed (South African Cities Network, 2020). Another factor impinging on the decision to lower tariffs was the need to additional capital reserves need for roll out and renewal of infrastructure required by the City's water strategy to build resilience against climate change by diversifying water sources, which would require surpluses on the City's operating budget as well as judicious borrowing. These include investment in the Cape Flats Managed Aquifer Recharge Scheme, upgrading of the Atlantis Managed Aquifer Recharge Scheme, upgrading of the Table Mountain Group Aquifer Scheme and permanent sea water desalination plants to meet water demand.

Despite the pressures the drought put on the City's credit rating, to finance its green water and public transport projects, the City succeeded in issuing an innovative 10 year green bond in July 2017, underwritten by Rand Merchant Bank. External verification is a requirement of most stock exchanges, and the Climate Bond's initiative certified the City's green bond. It had a 10.7% yield, was awarded a "GB1" rating from Moody's and garnered significant market interest, with 29 investors offering the equivalent of R4.3 billion (South African Cities Network, 2019) .

Desalination plants are energy intensive with very high stand by costs. The city had invested in temporary desalination plants for 24 months after which the infrastructure would be dismantled, thereby preempting high costs in future once water supply had normalized. Short term water needs compelled the investment but the investment case was uncertain since – while severe droughts are expected to become more frequent, there exact timing (and thus when desalination might again be required) is difficult to predict. If the drought had been prolonged beyond 2018, then temporary desalination plants would have helped to foster water security. However, if winter rainfall normalizes or increases, then the initial investment in the construction of the plant would be wasted. If a new, severe drought occurs soon after the desalination plants had been removed, then the initial investment would also have been wasted. The City's investment in temporary desalination plants has been seen as a "last resort adaptation investment" under immense public pressure and uncertainty, whereas more cost-effective alternatives would have been feasible had they been more proactively applied e.g. earlier demand management, rainwater harvesting, expansion of bulk water storage capacity (South African Cities Network, 2020, p. 33).

4.4 Leadership, governance and capacity

Successive Auditor-General reports over the last few decades have emphasised the role of the stability of the political-administrative interface, institutional stability, the tone set by leadership and the cohesiveness of the management team as indispensable conditions for good financial administration, and by extension, financial sustainability.

For the 2018/19 financial year, the Auditor-General in his *MFMA Consolidated Report* has grouped Western Cape municipalities into 3 categories: those with control environments that are institutionalised and received clean audits (Witzenberg LM, West Coast DM, Cape Winelands DM, Drakenstein, Langeberg, Prince Albert, Saldanha and Theewaterskloof), those that are reactive and susceptible to change where they had clean audits but regressed (City of Cape Town and Swartland) and those with dysfunctional control environments (Beauford West, Laingsburg and Kannaland).

The first high performing groups is characterised by strong leadership tone at the top, cohesive management teams, low vacancies, effective internal audit, audit committees and functional municipal public accounts committees and councils, responsiveness to audit findings and institutionalised systems (South Africa. Auditor-General, 2020).

The second group of reactive municipalities which had regressed were characterised by political instability resulting in instability in key positions such as those of the municipal manager and chief financial officer, as well as a change in the tone at the top (City of Cape Town) and a deterioration of preventative controls and systems (e.g. the City of Cape Town's financial system was not configured to prevent payments being made after the expiry date of contracts or in excess of the contract amounts, and Swartland's systems failed to correct material misstatements).

Swellendam and Cedarberg had unqualified audit reports with findings. Both have strong spending discipline but experience revenue collection challenges.

The third group of municipalities with dysfunctional control environments exhibit leadership apathy characterised by the Auditor-General as a "maak nie saak nie" attitude. The Auditor-General found that "an overall lack of accountability" in Beaufort West, with no actions are being taken by the council, the executive mayor and the municipal manager to ensure that controls are implemented", with the Council not providing oversight or consequence management. There was council leadership instability and council members were "appointed to positions in the administration of the municipality". The AG noted that the municipal manager was ""seldom present at the municipality, which contributes to the poor control

environment and employees not fulfilling their roles and responsibilities" and did not drive the implementation of the municipality's action plan, leaving the compilation of financial statements and audit queries to consultants (South Africa. Auditor-General, 2020, pp. 126-127).

The AG noted that Laingsburg was also characterised by "poor tone" at the top and ineffective audit and municipal public accounts committees due the rural location of the municipality which undermines its ability to attract the necessary skills, capacity constraints in the finance department and over-reliance on consultants (South Africa. Auditor-General, 2020, pp. 126-127).

Kannaland was also characterised by instability in political and administrative positions with vacancies in key positions such as the CFO and supply chain and officials in acting positions for protracted periods resulting in audit action plans not being developed or implemented, constrained finance department capacity and therefore a dependence on consultants and ineffectual internal and audit committees (South Africa. Auditor-General, 2020, pp. 126-127).

Part of the reason for WC's superior financial management performance relative to other provinces is the qualifications of staff managing the finances. For instance, out of 24 CFOs in the WC, 20 met minimum competence requirements in 2018, in comparison to 37% nationally. However, as noted above, smaller and more rural municipalities struggle to attract and retain the requisite skills.

FIGURE 19: MINIMUM COMPETENCE LEVELS AMONG SENIOR MUNICIPAL OFFICIALS, 2018

Province	Number of Municipalities	Accounting Officer	Meet Minimum Competency	Chief Financial Officer	Meet Minimum Competency	Senior Manager	Meet Minimum Competency	Head of Supply Chain Management unit	Meet Minimum Competency	Supply Chain Management Manager	Meet Minimum Competency	Middle Manager	Meet Minimum Competency	Other Official	Meet Minimum Competency	Total Officials who Meet Minimum Competency
EC	39	30	14	29	13	110	53	15	8	28	18	386	130	340	175	411
FS	23	34	8	23	11	90	8	2	1	12	3	173	37	403	277	345
GT	11	9	6	25	3	263	149	12	11	63	41	628	402	528	359	971
KZN	54	43	23	45	13	125	34	13	3	42	18	461	99	777	344	534
LIM	27	21	6	23	6	85	25	6	2	17	8	225	73	477	216	336
MP	20	13	10	15	6	113	35	6	3	16	6	200	75	524	256	371
NC	31	31	13	28	8	84	24	15	4	14	6	150	35	250	98	188
NW	22	17	9	12	3	62	20	4	0	17	6	183	61	392	118	217
WC	30	25	18	24	20	105	70	21	13	27	30	468	253	401	272	666
TOTAL	257	223	107	224	83	1037	418	94	45	236	128	2854	1165	4092	2095	4039

Source: National Treasury, 2020

4.5 Shared services

There have been a number examples of shared services in the Western Cape, such as

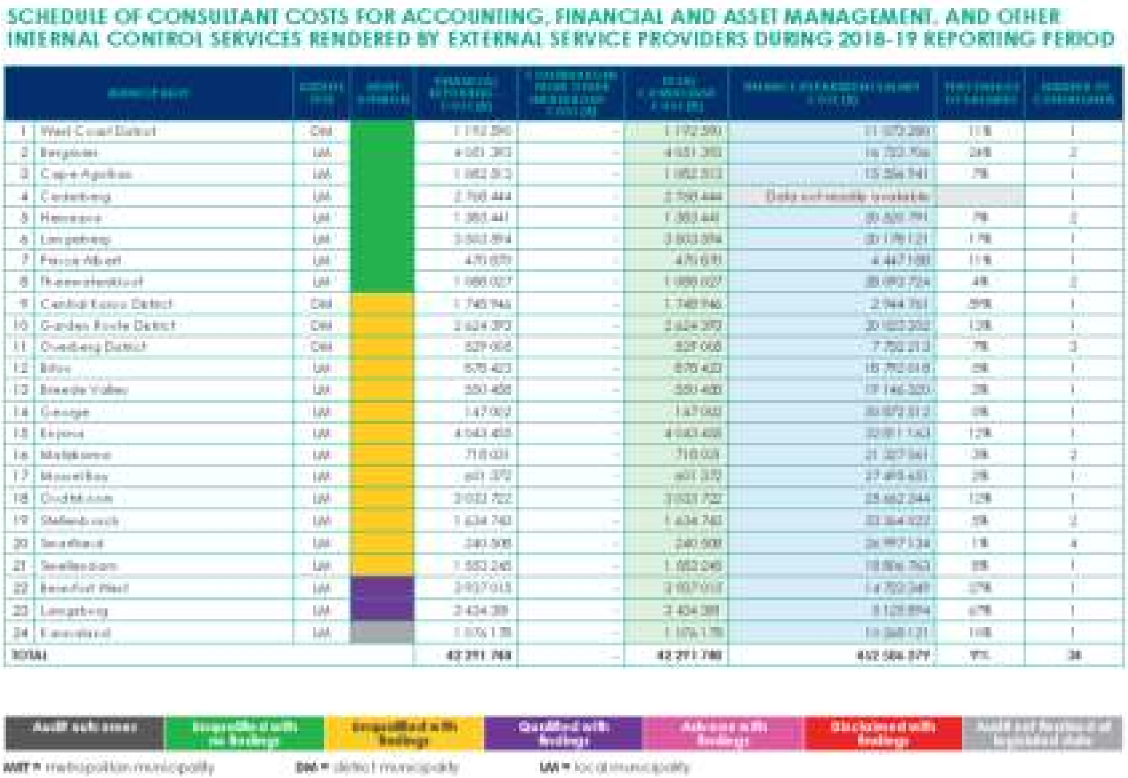
- Information and communication technology (ICT) services in the Overberg region, which includes the Overberg District Municipality, Cape Agulhas Local Municipality, Swellendam Local Municipality, Theewaterskloof Local Municipality and Overstrand Local Municipality.
- Risk management and legal services in the Overberg region, including the Overberg District Municipality and the four local municipalities.
- Fire-fighting and disaster management services in the Central Karoo region.
- A shared services centre in Central Karoo district (Central Karoo District Municipality, Beaufort West Municipality, Laingsburg Municipality and Prince Albert Municipality) in relation to legal services, internal audit and risk management, planning and ICT (Schwella, Brand, Van der Westhuizen, & Faurie, 2018).

The WC Government by supporting local government in terms of sec. 154(1) of the Constitution has promoted the shared services arrangements in which municipalities agree to share an identified service performed within their respective administrations, splitting the associated costs, with an appropriate governance mechanism such as a governance board.

In 2019, the Financial and Fiscal Commission recommended that provincial governments facilitate the process of municipalities in the same district municipality share the costs of the valuation process to attract qualified property valuers and ensure that properties are accurately valued (South Africa. Financial and Fiscal Commission, 2019).

But these shared service agreements are not without their challenges. These relate, inter alia, to apportionment of costs, differing risk cultures and the inefficiencies associated with shared staff travelling between municipalities.

FIGURE 20: CONSULTING COSTS FOR ACCOUNTING, FINANCIAL AND ASSET MANAGEMENT DURING 2018/19



5 Short and medium term impact of the pandemic on the sustainability of WC municipalities

This section first discusses the short term impacts of the corona virus pandemic in LMs. DMs and the metro. An analysis of the 3-year rolling Medium Term Revenue and Expenditure Frameworks (MTREFs) provides a perspective on how municipalities envisage their medium term fiscal futures when they formally tabled their budgets in June 2020 at the beginning of the 2021 financial year.

- The sampled municipalities are classified according to the Municipal Infrastructure Investment Framework model.
- A: metropolitan municipalities.
- B1: local municipalities containing secondary cities.

- B2: local municipalities with a large town as core.
- B3: local municipalities with relatively small populations and a significant proportion of urban population but with no large town as core.
- B4: local municipalities which are mainly rural with, at most, one or two small towns in their area.
- C1: District municipalities which are not water service providers.
- C2: District municipalities which are water service providers.

National Treasury's classification was used to designate the sampled municipalities as high, medium and low capacity.

5.1 Short term pandemic impacts

In the sections below, the short-term impacts of the pandemic are analysed for the first three quarters of the pandemic (from April 2020 to December 2021). Since quarterly data are highly seasonal, the focus is on year-on-year (YoY) changes from the same quarter in the previous year. These are un-audited data downloaded from the Section 71 Quarterly Reports on the National Treasury website. Due to the transition to the Municipal Standard Chart of Accounts (MSCOA) and the challenges experienced by certain municipalities, there are a few anomalies in the data. However. the broad impacts of the short-term impact can still be discerned. Because financial data are largely historic and backward looking, these trends must be supplemented by the findings from the interviews in the next section, which are more prospective.

5.1.1 Short term impact on local municipalities

The impact of the pandemic on LM operating and capital budgets is examined first, and then the impacts on DMs.

5.1.1.1 Operating budget balances in sampled LMs

Table 5 shows quarterly operating revenue, expenditure, capital transfers and subsidies and budget balance for sampled local municipalities arranged from the biggest to the smallest, in terms of operating revenue. It reflects financial performance for 4 quarters prior to the pandemic, and well as the first 3 quarters of the pandemic: 2019/20Q4 (1 April to 30 June 2020) and 2020/21Q1 (1 July 2020 to 30 September 2020). For the 3 quarters during the pandemic, the operating surplus or deficit is given as a percentage of operating revenue.

As can be seen Table 5 below, the larger local municipalities (Stellenbosch LM and Drakenstein LM) ran operating surpluses in the first quarter of the pandemic 2019/20Q4 of 3% and 18% respectively, despite the hard lockdown. Property rates payments are due by the end of the financial year, which would have supported this outcome. Stellenbosch went on to run operating surpluses of 41% of operating revenue in following 2 quarters, while Drakenstein run an operating deficit of 31% of operating revenue in 2020/21Q2. However, this deficit is largely due to non-cash expenditures: depreciation, asset impairment and debt impairment, although cost of employment increased as well (see Appendix 4: Composition of quarterly operating expenditure). As a result, Drakenstein's cashflow would not have been as greatly affected in that quarter. Since these are largely determined by asset management and accounting policies and application of credit control policies in past quarters, they are not attributable to pandemic impacts.

By contrast, Kannaland, Bergrivier, and Swellendam ran operating deficits in the first quarter of the pandemic 2019/20Q4 (of 1%, 2% and 13% of operating revenue respectively), but later reflected operating surpluses in 2020/21Q1 and 2020/21Q2. Swartland, Laingsburg and Hessequa appear harder hit by operating deficits of 22%, 34% and 54% of operating revenues in the first quarter of the pandemic, 2019/20Q4. Similar to Drakenstein, however, the operating deficits in Hessequa and Laingsburg were driven largely by non-cash debt impairment and employee costs, which were not directly pandemic related. In Laingsburg, increased contracted services also contribute to the 20/21 operating deficit.

Table 5: Operating budget balances of sampled local municipalities

CATEGORY	CAPACITY	MUNICIPALITY	R millions	Pre-pandemic actual				Pandemic actual			Surplus/deficit as % operating revenue			
				18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2
B1	High	Stellenbosch	Operating Revenue	328.9	481.3	363.6	368.4	365.4	493.3	388.9	(5%)	3%	41%	5%
			Operating Expenditure	340.7	284.6	341.2	386.6	354.3	289.7	370.2				
			Operating Surplus/(Deficit)	**(11.8)**	**196.6**	**22.4**	**(18.3)**	**11.1**	**203.6**	**18.7**				
			Transfers and subsidies - capital	46.0	2.1	65.6	13.6	26.9	-	21.4				
			Surplus/(Deficit)	**34.1**	**198.7**	**88.0**	**(4.7)**	**38.0**	**203.6**	**40.1**				
B1	High	Drakenstein	Operating Revenue	315.0	584.6	512.0	562.6	504.0	581.9	551.7	21%	18%	19%	(31%)
			Operating Expenditure	409.8	517.9	565.2	443.8	411.7	469.2	724.5				
			Operating Surplus/(Deficit)	**(94.8)**	**66.7**	**(53.2)**	**118.9**	**92.3**	**112.7**	**(172.8)**				
			Transfers and subsidies - capital	20.2	-	16.5	12.9	68.7	26.7	29.5				
			Surplus/(Deficit)	**(74.6)**	**66.7**	**(36.7)**	**131.7**	**161.0**	**139.3**	**(143.3)**				
B3	Medium	Swartland	Operating Revenue	160.9	199.2	173.9	177.6	172.6	210.9	199.4	20%	(22%)	34%	22%
			Operating Expenditure	160.7	128.6	147.2	142.7	210.7	138.2	155.3				
			Operating Surplus/(Deficit)	**0.2**	**70.6**	**26.7**	**34.9**	**(38.1)**	**72.7**	**44.1**				
			Transfers and subsidies - capital	0.2	0.2	0.3	1.1	0.1	0.3	0.7				
			Surplus/(Deficit)	**0.4**	**70.8**	**27.0**	**36.0**	**(38.0)**	**73.0**	**44.8**				
B3	Medium	Hessequa	Operating Revenue	84.0	188.0	104.8	103.0	70.8	208.4	113.3	(10%)	(54%)	55%	(19%)
			Operating Expenditure	99.8	78.2	131.5	112.9	109.2	94.6	135.3				
			Operating Surplus/(Deficit)	**(15.9)**	**109.8**	**(26.7)**	**(9.8)**	**(38.4)**	**113.9**	**(21.2)**				
			Transfers and subsidies - capital	2.7	0.6	1.7	1.8	2.8	0.7	-				
			Surplus/(Deficit)	**(13.2)**	**110.4**	**(25.0)**	**(8.1)**	**(35.6)**	**114.6**	**(21.2)**				
B3	Medium	Bergrivier	Operating Revenue	67.3	135.7	62.0	75.4	79.1	104.9	92.8	5%	(2%)	20%	2%
			Operating Expenditure	84.5	82.0	74.9	71.6	80.7	84.0	90.9				
			Operating Surplus/(Deficit)	**(17.2)**	**53.7**	**(12.9)**	**3.9**	**(1.7)**	**21.0**	**1.8**				
			Transfers and subsidies - capital	3.5	-	1.7	4.0	5.6	1.8	-				
			Surplus/(Deficit)	**(13.7)**	**53.7**	**(11.3)**	**7.8**	**3.9**	**22.8**	**1.8**				
B3	Low	Swellendam	Operating Revenue	45.6	72.0	66.5	64.9	44.0	74.8	77.1	21%	(13%)	39%	9%
			Operating Expenditure	48.7	57.9	66.7	55.8	49.7	57.4	73.2				
			Operating Surplus/(Deficit)	**(3.1)**	**14.1**	**(0.2)**	**9.1**	**(5.7)**	**17.4**	**4.0**				
			Transfers and subsidies - capital	4.7	0.0	4.1	2.3	4.4	0.0	5.2				
			Surplus/(Deficit)	**1.6**	**14.1**	**3.9**	**11.4**	**(1.3)**	**17.4**	**9.1**				
B3	Medium	Kannaland	Operating Revenue	37.5	35.5	35.3	32.6	22.8	43.7	41.5	30%	(1%)	35%	21%
			Operating Expenditure	51.7	14.5	37.9	22.8	23.1	28.3	32.8				
			Operating Surplus/(Deficit)	**(14.2)**	**21.0**	**(2.6)**	**9.8**	**(0.3)**	**15.5**	**8.7**				
			Transfers and subsidies - capital	5.1	0.5	0.4	-	-	-	3.1				
			Surplus/(Deficit)	**(9.1)**	**21.5**	**(2.2)**	**9.8**	**(0.3)**	**15.5**	**11.8**				
B3	Medium	Laingsburg	Operating Revenue	14.1	18.3	36.4	16.7	17.7	25.4	28.3	(28%)	(34%)	33%	(3%)
			Operating Expenditure	25.4	12.7	41.7	21.7	23.7	19.5	28.9				
			Operating Surplus/(Deficit)	**(11.3)**	**5.6**	**(5.3)**	**(5.0)**	**(6.0)**	**5.9**	**(0.6)**				
			Transfers and subsidies - capital	5.5	1.4	2.8	0.8	1.8	0.8	7.3				
			Surplus/(Deficit)	**(5.8)**	**7.0**	**(2.5)**	**(4.2)**	**(4.3)**	**6.7**	**6.7**				

From the table, the resilience of the sampled WC municipalities is evident. All in all, in short term, the WC does not seem to have been as badly compromised by the onset of the coronavirus epidemic as other South African provinces. For the South African local government sphere in aggregate, only 20% of billed revenue was collected in 2019/20Q4, the first quarter of the pandemic (April to June 2020) vis-à-vis 93% in same quarter in the prior year (South Africa. National Treasury, 2021). In the WC revenue outcomes were much better. The reasons for this re explored further below and in the interview reporting, but includes the fiscal capacity of the sampled LMs, the revenue enhancement and cost containment strategies and systems put in place prior to the pandemic, as well as proactive strategies put in place by municipalities to respond agilely to the public health disaster and lockdown response.

Table 6 shows changes in operating revenue in the three quarters of the pandemic (2019/20Q1, 2020/21Q1 and 2020/21Q2) from same quarter in the previous financial year. Municipalities such as Stellenbosch and Swartland have achieve positive revenue growth over the three quarters of the pandemic, whereas Hessequa and Kannaland have seen year on year (YoY) operating revenue contractions in the first quarter of the pandemic, 2019/20Q1, of 16% and 39% respectively. Bergrivier experienced a 23% YoY decline in operating revenues in the second quarter of the pandemic (2020/21Q1) and Laingsburg a decrease of 22% YoY. The succession of operating deficits in municipalities like Hessequa and Laingsburg suggest severe cash flow pressures.

TABLE 6: YEAR-ON-YEAR (YOY) CHANGE IN OPERATING REVENUES IN SAMPLED LOCAL MUNICIPALITY

R miilions	Pre-pandemic actual				Pandemic actual			% Change YOY		
Operating revenue	18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	19/20Q4	20/21Q1	20/21Q2
Stellenbosch	328.9	481.3	363.6	368.4	365.4	493.3	388.9	11%	3%	7%
Drakenstein	315.0	584.6	512.0	562.6	504.0	581.9	551.7	60%	(.5%)	8%
Swartland	160.9	199.2	173.9	177.6	172.6	210.9	199.4	7%	6%	15%
Hessequa	84.0	188.0	104.8	103.0	70.8	208.4	113.3	(16%)	11%	8%
Bergrivier	67.3	135.7	62.0	75.4	79.1	104.9	92.8	17%	(23%)	50%
Swellendam	45.6	72.0	66.5	64.9	44.0	74.8	77.1	(4%)	4%	16%
Kannaland	37.5	35.5	35.3	32.6	22.8	43.7	41.5	(39%)	23%	18%
Laingsburg	14.1	18.3	36.4	16.7	17.7	25.4	28.3	25%	39%	(22%)

Appendix 3 on page 179 reflects YoY changes in operating revenues during the pandemic, and Appendix 4 on page 182 shows the composition of operating revenue over these quarters.

Some of the key trends from these data are summarised below:

Smaller own revenue sources (such as fines and licences, rental of facilities, agency services and other revenues) tended to be most affected by the first 2 quarters of the lockdown, recovering slightly in the third quarter. However, the overall impact on operating revenue is lessened because they only contribute a small part of overall operating revenue. As shown in Appendix 3 for instance, income from fines, penalties, licences and permits in Stellenbosch shrunk sharply YoY from the previous quarter by -60% in 2019/20Q4 and -61% in 2020/21Q1, by -75% and -18% in Drakenstein in the same quarters, by -77% and -35% in Hessequa, and by -98% and -13% in Kannaland. A similar pattern of sharp contraction in income from rental of LM facilities can be discerned. There was a general declining trend in interest income received, as internal reserves and investments were drawn down.

Most sampled LMs saw quarterly revenue from agency services (delivered by municipalities on behalf of provincial departments such as certain housing and vehicle licencing functions) plummet in the first quarter of the pandemic 2019/20Q4, only to revert to positive YoY growth in subsequent quarters, with the smaller municipalities comparatively harder hit. Agency service revenue contracted by -60% and -61% YoY in the first 2 quarters of the pandemic in Stellenbosch LM, to recover to positive 51% YoY growth in 2020/21Q2. Swartland saw an initial decline of -72% in 2019/20Q4, followed by YoY growth of 54% and 25% in the subsequent quarters. Hessequa had a -42% decrease in YoY agency revenues, followed by increases of 17% and 28% in the subsequent 2 quarters of the pandemic. Laingsburg experienced a YoY -77% reduction in agency service revenue, followed by increase of 43% and 162% in the subsequent quarters. In Swellendam and Kannaland, agency payment dwindled to zero in the first quarter, but rebounded in the subsequent quarters. By contrast, Bergrivier only evinced a -6% contraction in agency income in the first and -1% in the third quarter of the pandemic.

The LM municipalities (such Stellenbosch, Drakenstein, Swartland) rely mainly on electricity and - to a much lesser extent – water, sanitation and refuse charges, and property rates for the bulk of their operating revenues. And while the share of water, electricity and other service charges as a proportion of total operating revenue declined in 2019Q4, and more so in the subsequent 2 quarters of the pandemic, they still remain the main revenue drivers, and were less compromised by the lockdown than other own revenue sources described above.

Stellenbosch LM experienced declines in electricity revenue of -9%, -1% and -19% in each of the three quarters of the pandemic, as well as YoY contractions of water revenue in 2020/21Q1 and 2020/21Q2. Drakenstein, Hessequa and Bergrivier experienced YoY decreases in electricity and water charges of the first 3 months course of the pandemic. Swellendam's electricity charges showed positive increases for all three quarters of the pandemic, and water charges only shrank -6% in 2020/21Q2. Kannaland recorded a YoY -12% contraction in electricity revenues in the first quarter of the pandemic but recorded YoY increases in the 2 quarters thereafter. Water charges in Kannaland exhibited YoY increases in all three quarters, driven by increased drought water charges. Swartland recorded positive YoY increases in electricity and water charges in all three quarters of the pandemic, as did Laingsburg.

In Bergrivier, revenues for sanitation declined YoY in all three quarters of the pandemic and refuse revenues decreased in 2 of the three quarters. Drakenstein sustained YoY decreases in sanitation and refuse revenue in the first quarter of the pandemic, but reflected YoY increases thereafter. Swellendam saw YoY increases in sanitation revenue in all 3 pandemic quarters but experienced a -27% contraction in sanitation service revenue in 2019/20Q4, with positive YoY growth in the 2 subsequent quarters. Stellenbosch LM, Hessequa, Kannaland and Laingsburg had YoY increases in sanitation and refuse charges all three quarters of the pandemic.

There appears to be significant differences in impact on the various municipalities, but on the whole, a fair degree of short term resilience in respect of service charges.

Smaller municipalities like Kannaland and Laingsburg saw YoY declines in property rates revenue in 2019/20Q4, with positive growth in the subsequent 2 quarters of the pandemic.

Kannaland experienced a -39% contraction in rates income in 2019/20Q4, increasing by 28% and 22% in the next 2 quarters. By contrast, the larger municipalities (Stellenbosch and Drakenstein) generated positive YoY increases in property rates over all the quarters of the pandemic. Property rates are typically levied on higher income households who would be more able to work from home and less vulnerable to loss of income or livelihood.

As can be expected given the redistributive thrust of the local government equitable share (LES), operating transfers and subsidies are more prominent in municipalities such as Bergrivier, Swellendam, and especially Kannaland and Laingsburg rather than in the bigger municipalities such as Stellenbosch or Drakenstein. National Treasury's *Budget Review 2021* indicates that between March 2020 and February 2021, a budgeted R11 billion was added to the local government equitable share to help finance the Covid-19 response (p69). In general, transfers and subsidies showed YoY increases, which helped to offset decreases in services charges and property rates.

Table 7 shows each municipality from largest to smallest, and spending per category in R millions, for 4 quarters before the start of the pandemic and 2 quarters during the pandemic, starting 2019/20Q4 in April 2020. The table also shows the change in spending from the same quarter in the previous financial year, year-on-year (YoY). The LMs in the sample generally continued and intensified pre-pandemic cost containment measures, to contain operating expenditure YoY increases in line with changes in operating revenue broadly. Increases in expenditure due to the pandemic (e.g. spending on Personal Protective Equipment – PPE – was offset to some extent by decreases in other areas, e.g. transport and subsistence costs for meeting attendance.

TABLE 7: YEAR-ON-YEAR (YOY) CHANGE IN OPERATING EXPENDITURE IN SAMPLED LOCAL MUNICIPALITIES

R miilions	Pre-pandemic actual				Pandemic actual			% Change YOY		
	18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	19/20Q4	20/21Q1	20/21Q2
Stellenbosch	340.7	284.6	341.2	386.6	354.3	289.7	370.2	4%	2%	9%
Drakenstein	409.8	517.9	565.2	443.8	411.7	469.2	724.5	.5%	(9%)	28%
Swartland	160.7	128.6	147.2	142.7	210.7	138.2	155.3	31%	7%	6%
Hessequa	99.8	78.2	131.5	112.9	109.2	94.6	135.3	9%	21%	3%
Bergrivier	84.5	82.0	74.9	71.6	80.7	84.0	90.9	(5%)	2%	21%
Swellendam	48.7	57.9	66.7	55.8	49.7	57.4	73.2	2%	(1%)	10%
Kannaland	51.7	14.5	37.9	22.8	23.1	28.3	32.8	(55%)	95%	(13%)
Laingsburg	25.4	12.7	41.7	21.7	23.7	19.5	28.9	(7%)	53%	(31%)

Appendix 4 shows the YoY changes in quarterly operating expenditure for each of the sample municipalities and Appendix 6 shows the changes in the composition of quarterly operating expenditures. From these, it can be seen that the 31% YoY increase in operating expenditure in Swartland in 2019/20Q4 was largely due to depreciation and asset impairment (non-cash items which are determined by the municipality's asset management policies and hence unrelated to the pandemic). Similarly, the 21% YoY increase in Bergrivier in 2020/21Q2 is largely due to depreciation, asset and debt impairment, non-cash items which would not impact on cash flow. Drakenstein's YoY increase in operating expenditure in 2020/21Q2 is also largely attributable to increased depreciation, asset impairment and debt impairment charges, and finance charges. Hessequa's YoY increase in operating expenditure in 2020/21Q2 was largely due to increases in bulk service costs. In 2019/20Q4, Kannaland saw a -29% YoY decrease in employee costs and a -27% YoY decline in bulk services costs, contributing to a 55% reduction in quarterly operating expenditure in 2019/20Q4. The next quarter, 2020/21Q1, also saw a -10% decrease in employment costs which were more than offset by a large increase in bulk service costs, leading to a net increase in operating expenditure in that quarter. The next quarter saw a 6% increase in employee costs accompanied by a -49% in bulk service costs, leading to a net decline in quarterly operating expenditure by -13%. In Laingsburg, the 53% YoY increase in quarterly operating expenditure in 2020/21Q1 was due mainly to increases in debt impairment and increased employee related costs. The -31% YoY reduction in quarterly operating expenditures were due primarily to decreases in debt impairment, depreciation and asset impairment, partially offset by increasing employee costs.

In conclusion, it appears that, as at May 2021, operating costs are being driven largely by systemic factors other than the pandemic per se. The more protracted the pandemic, the greater the likelihood of this changing.

5.1.1.2 Capital budgets in sampled LMs

By contrast to the operating budgets, the impact of the coronavirus pandemic can clearly be seen in the capital budgets of both large and small LMs, especially in the first quarter of the pandemic, 2019/20Q4. Stellenbosch saw YoY reductions in quarterly capital expenditure of -56% in 2019/20Q4, 2020/21Q1 and 2020/21Q2. Drakenstein's capital expenditure contracted by 52% YoY in 2019/20Q4 and -38% in 2020/21Q2.

TABLE 8: YEAR-ON-YEAR (YOY) CHANGES IN QUARTERLY CAPITAL EXPENDITURE IN SAMPLED LOCAL MUNICIPALITIES

R miilions	Pre-pandemic actual				Pandemic actual			% Change YoY		
	18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	19/20Q4	20/21Q1	20/21Q2
Stellenbosch	182.2	94.1	108.9	70.7	79.7	63.6	83.4	(56%)	(32%)	(23%)
Drakenstein	205.8	26.9	66.6	63.9	99.2	34.4	41.3	(52%)	28%	(38%)
Swartland	36.3	10.8	36.5	19.4	50.2	21.3	45.5	38%	98%	25%
Hessequa	16.2	1.3	14.0	9.8	30.5	6.9	9.7	88%	432%	(31%)
Bergrivier	-	3.3	9.5	12.4	18.1	5.2	10.3	-	58%	9%
Swellendam	6.3	0.5	4.7	3.4	5.1	2.1	4.9	(18%)	330%	5%
Kannaland	14.0	3.6	3.5	1.3	6.4	4.8	3.5	(54%)	36%	(.5%)
Laingsburg	4.7	1.4	3.1	1.5	1.1	41.8	7.3	(77%)	2 836%	139%

Capital spending fell YOY for 5 of the 8 sampled LMs in the first quarter of the pandemic, but generally rebounded in the second quarter, once lockdown levels eased. In Hessequa, capital expenditure declined by -31% in 2020/21Q2, and in Swellendam it decreased by -18% in 2019/20Q4. Kannaland and Laingsburg capital budgets contracted by -54% and -77% in 2019/20Q4 respectively, but appear to have improved in subsequent quarters, especially in Laingsburg. Remarkably, the capital programmes in Swartland and Bergrivier appear to have sustained minimal disruption, attesting to the resilience of these medium sized LMs.

The smaller municipalities such as Laingsburg and Kannaland devote the bulk of their capital spending on trading services (water, electricity, and to a lesser extent waste-water and waste management). Medium sized municipalities (Hessequa, Bergrivier and Swellendam), in addition to trading services, also spending on road transport (as an agency function) and other community services (community services, sports and recreation and public safety). The largest municipalities (Stellenbosch and Drakenstein) also spend on their agency housing function. Governance and administration capital expenditure is driven largely by finance and administration spending, rather than Council and Exco or internal audit.

TABLE 9: YEAR-ON-YEAR (YOY) CHANGE IN QUARTERLY CAPITAL REVENUES IN SAMPLED LOCAL MUNICIPALITIES

CATEGORY	CAPACITY	Municipality	R miilions	Pre-pandemic actual				Pandemic actual			% Change YOY		
			Revenue source	18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	19/20Q4	20/21Q1	20/21Q2
B1	High	Stellenbosch	Transfers: National	21.2	2.1	30.3	9.1	18.2	0.9	15.1	(14%)	(57%)	(50%)
			Transfers: Provincial	15.3	1.4	48.9	6.0	3.2	2.5	5.1	(79%)	79%	(90%)
			Transfers: Other	-	-	-	-	-	1.5	7.3	-	-	-
			Borrowing	38.8	3.0	19.0	31.7	20.7	2.9	6.7	(47%)	(4%)	(65%)
			Internal funds	106.4	87.6	10.7	23.8	37.6	55.9	49.2	(65%)	(36%)	360%
			Total capital revenue	**181.8**	**94.1**	**108.9**	**70.7**	**79.7**	**63.6**	**83.4**	**(56%)**	**(32%)**	**(23%)**
B1	High	Drakenstein	Transfers: National	17.9	2.1	11.2	25.6	48.8	19.1	15.1	173%	801%	35%
			Transfers: Provincial	19.6	0.4	25.6	7.4	17.9	10.0	11.9	(9%)	2 122%	(53%)
			Transfers: Other	10.5	-	0.0	0.7	0.5	-	0.9	(95%)	-	1 689%
			Borrowing	130.1	24.0	14.9	18.8	22.0	-	-	(83%)	(100%)	(100%)
			Internal funds	27.7	0.4	14.9	11.4	10.1	5.3	13.4	(64%)	1 219%	(10%)
			Total capital revenue	**205.8**	**26.9**	**66.6**	**63.9**	**99.2**	**34.4**	**41.3**	**(52%)**	**28%**	**(38%)**
B3	Medium	Swartland	Transfers: National	10.5	3.3	11.3	4.6	11.0	2.4	20.1	5%	(27%)	77%
			Transfers: Provincial	6.6	-	11.4	7.1	19.3	9.0	6.4	193%	-	(43%)
			Transfers: Other	0.3	-	-	-	1.9	-	-	644%	-	-
			Internal funds	19.0	7.4	13.8	7.7	17.9	9.9	19.0	(6%)	33%	38%
			Total capital revenue	**36.3**	**10.8**	**36.5**	**19.4**	**50.2**	**21.3**	**45.5**	**38%**	**98%**	**25%**
B3	Medium	Hessequa	Transfers: National	6.2	0.1	1.5	0.6	10.4	0.5	2.3	66%	299%	52%
			Transfers: Provincial	2.6	0.0	1.0	0.3	0.2	-		(91%)	(100%)	(100%)
			Transfers: Other	0.0	-	-	-	0.0	-		(27%)	-	-
			Borrowing	6.1	0.5	9.8	6.9	12.5	3.6	3.2	106%	574%	(67%)
			Internal funds	1.3	0.6	1.7	2.0	7.4	2.9	4.1	477%	355%	147%
			Total capital revenue	**16.2**	**1.3**	**14.0**	**9.8**	**30.5**	**6.9**	**9.7**	**88%**	**432%**	**(31%)**
B3	Medium	Bergrivier	Transfers: National	-	0.8	3.3	2.9	9.7	2.2	2.5	-	178%	(25%)
			Transfers: Provincial	-	0.5	0.6	2.5	2.0	0.4	0.3	-	(25%)	(48%)
			Borrowing	-	0.8	1.9	1.6	1.7	0.2	4.0	-	(73%)	111%
			Internal funds	-	0.8	3.6	5.7	4.6	0.6	3.0	-	(25%)	(17%)
			Total capital revenue	**-**	**2.9**	**9.5**	**12.7**	**17.9**	**3.5**	**9.8**	**-**	**18%**	**4%**
B3	Low	Swellendam	Transfers: National	4.3	-	4.1	2.2	3.1	0.0	4.6	(28%)	-	12%
			Transfers: Provincial	0.3	-	-	0.1	0.4	-	0.5	40%	-	-
			Internal funds	1.8	0.5	0.6	1.1	1.7	0.1	1.8	(7%)	(81%)	206%
			Total capital revenue	**6.3**	**0.5**	**4.7**	**3.4**	**5.1**	**0.1**	**6.9**	**(20%)**	**(72%)**	**47%**
B3	Medium	Kannaland	Transfers: National	9.9	3.6	3.0	0.3	6.0	4.5	3.3	(40%)	28%	10%
			Transfers: Provincial	3.0	-	0.5	1.0	0.4	0.3	0.2	(85%)	-	(55%)
			Borrowing	-	-	-	-	-	-	-	-	-	-
			Internal funds	1.0	-	0.1	0.0	-	-	-	(100%)	-	(100%)
			Total capital revenue	**14.0**	**3.6**	**3.5**	**1.3**	**6.4**	**4.8**	**3.5**	**(54%)**	**36%**	**(%)**
B3	Medium	Laingsburg	Transfers: National	4.6	1.4	3.1	1.5	1.1	35.0	5.7	(77%)	2 356%	86%
			Transfers: Provincial	-	-	-	-	-	0.7	1.6	-	-	-
			Internal funds	0.0	-	-	-	-	0.3	-	(100%)	-	-
			Total capital revenue	**4.6**	**1.4**	**3.1**	**1.5**	**1.1**	**36.0**	**7.3**	**(77%)**	**2 427%**	**139%**

Smaller municipalities also tend to be largely dependent on national and, to a lesser extent, provincial conditional grants to finance their capital projects. Laingsburg saw a YoY increase in capital grant financed spending in 2020/21Q1 to R35 million. The medium sized municipalities rely less on conditional grants and more on internally generated revenue (Swartland, Hessequa, Bergrivier and Swellendam). Hessequa and Bergrivier also borrow to finance capital spending. The larger municipalities (Stellenbosch and Drakenstein) have the least reliance on capital grants and rely mainly on internal sources and borrowing.

While use of internal funds for financing capital projects decreased in all the LM's except Hessequa, changes in grant use is mixed, with some LMs seeing decreased application of grant funds (e.g. Stellenbosch, Hessequa and Kannaland) and others seeing increases (e.g. Drakenstein and Bergrivier). Reduction in accumulated trading surpluses and investments will place pressure on internally generated funds in future, since municipalities may not borrow to replenish their capital reserves.

The pandemic has prompted a review of borrowing strategies with municipalities reducing their exposure to borrowing risk due to the uncertainty of the situation they find themselves in and the high costs of borrowing, and greater reliance on internal funds and transfers.

In sum, there were no major aggregate changes in spending during the pandemic period, with savings in some areas probably offsetting cost increases in others. This may be because sampled municipalities found ways to return to operational status fairly soon, and alternative working arrangements to accommodate pandemic conditions.

5.1.2 Short term impact on District Municipalities

This section reviews the short-term impact of the lockdown on the sampled district municipalities' operating and capital budgets

5.1.2.1 Operating budgets

The three District municipalities also exhibit the pattern of being hardest hit at the beginning of lockdown in 19/20Q1 but running operating surpluses thereafter. West Coast DM however runs an operating deficit of 1.3% of operating revenue in 20/21Q2, driven largely by costa of employment, increases in contracted services and bulk services and, to a much lesser extent, by non-cash items such as depreciation and impairment. Cape Winelands exhibited the largest deficit as a percentage of operating revenue in 2019/20Q4 (75%) with West Coast DM and Central Karoo DM reporting operating deficits of 12% and 11% of operating revenue respectively.

In the sampled DMs, the main revenue drivers are operating transfers (the RSC Levy replacement grants and other operating grants), agency services (e.g. for roads). Central Karoo DM depends largely on those sources, whereas West Coast DM and to a lesser extent, Cape Winelands DM, have more diversified revenue sources. West Coast DM also derives income from bulk water service charges as a result of its water concession. Cape Winelands and West Coast also rely on interest income from reserves and investments as a source of operating revenue, whereas Central Karoo does not.

Table 10: Operating budget balances of sampled district municipalities

CATEGORY	CAPACITY	MUNICIPALITY	R millions	Pre-pandemic actual				Pandemic actual			Surplus/deficit as % operating revenue			
				18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2
C1	Medium	Cape Winelands	Operating Revenue	75.4	126.3	104.5	124.0	50.6	118.8	113.2				
			Operating Expenditure	62.8	70.1	99.7	105.7	88.4	72.7	100.6				
			Operating Surplus/(Deficit)	**12.6**	**56.3**	**4.8**	**18.3**	**(37.9)**	**46.1**	**12.5**	15%	(75%)	39%	11%
			Transfers and subsidies - capital	-	1.0	-	-	0.1	-	0.0				
			Surplus/(Deficit)	**12.6**	**57.3**	**4.8**	**18.3**	**(37.8)**	**46.1**	**12.5**				
C1	Medium	West Coast	Operating Revenue	81.6	93.8	119.3	108.9	71.8	105.7	106.6				
			Operating Expenditure	81.6	70.2	111.2	92.8	80.2	75.3	108.0				
			Operating Surplus/(Deficit)	**0.1**	**23.6**	**8.1**	**16.0**	**(8.3)**	**30.4**	**(1.4)**	15%	(12%)	29%	(1%)
			Transfers and subsidies - capital	0.4	0.1	0.0	-	-	-	0.5				
			Surplus/(Deficit)	**0.4**	**23.7**	**8.2**	**16.0**	**(8.3)**	**30.4**	**(0.9)**				
C1	Medium	Central Karoo	Operating Revenue	20.6	4.1	20.3	22.2	18.6	30.1	24.1				
			Operating Expenditure	30.8	11.3	22.1	19.8	20.6	12.1	16.6				
			Operating Surplus/(Deficit)	**(10.2)**	**(7.2)**	**(1.8)**	**2.5**	**(2.1)**	**18.0**	**7.6**	11%	(11%)	60%	31%
			Transfers and subsidies - capital	-	-	-	-	-	-	-				
			Surplus/(Deficit)	**(10.2)**	**(7.2)**	**(1.8)**	**2.5**	**(2.1)**	**18.0**	**7.6**				

As can be seen in Table 11, the DMs generally were hardest hit in 2019/20Q4 across the board (especially agency services, a major revenue driver) and then showed some improvement in the following quarter, 2020/21Q1. Central Karoo's rebound was assisted by an increase in operating transfers and subsidies. With fewer revenue bases, districts are clearly more financial vulnerable than their LM counterparts. Prudent financial in the past resulting in investment reserves and interest income streams such as Cape Winelands and West Coast greatly enhance their resilience. By contrast, Central Karoo DM does not have that advantage. The other two sampled DMs also derive a very small income stream from rental of facilities and equipment, which Central Karoo DM – which is without a property portfolio – does not have.

Cape Winelands had a 33% YoY contraction in operating revenues in 2019/20Q4, the first quarter of the lockdown, driven mainly by a -60% reduction in operating transfers that quarter, a -46% drop in interest earned, a -18% decrease in agency service income and a -17% decrease in rental income. In 2020/21Q2, there was a -73% decline in agency service income and -37% decrease in increase earned, which were partially offset by an increase in operating transfers and subsidies, resulting in a net YoY drop in operating revenue of -6%. In 2020/21Q2, a 70% YoY increase in quarterly agency service income and a 3% increase in interest income were partially offset by a decrease in transfers received, resulting in an overall YoY increase of 8% of quarterly operating revenue.

Table 11: Year-on-Year (YoY) quarterly change in operating revenue in sampled district municipalities

R millions	Pre-pandemic actual				Pandemic actual			% Change YOY		
Revenue Source	18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q3	19/20Q4	20/21Q1	19/20Q4	20/21Q1	20/21Q2
Cape Winelands	75.4	126.3	104.5	124.0	50.6	118.8	113.2	**(33%)**	**(6%)**	**8%**
West Coast	81.6	93.8	119.3	108.9	71.8	105.7	106.6	**(12%)**	**13%**	**(11%)**
Central Karoo	20.6	4.1	20.3	22.2	18.6	30.1	24.1	**(10%)**	**641%**	**19%**

While West Coast DM also experienced a -82% in transfers and subsidies in 2019/20Q4, a –31% drop in agency service income, and a -46% in interest earned, bulk water service charges (which comprises between 25 to 40% of quarterly operating revenue), only declined by -2% YoY. Furthermore, West Coast's rental income and licences, permits and other revenue streams show YoY increases despite the pandemic, with a net result of a -12% decline in quarterly operating revenue in the first quarter of the pandemic 2019/20Q4.

Central Karoo DM has a -10% decrease in quarterly operating revenue in the first quarter of the pandemic 2019/20Q4, driven mainly by a -65% contraction in transfers and subsidies, and a -25% decline in interest earned. In the subsequent 2 quarters of the pandemic, interest income, rental income and licenses, permits and other revenue continued to decline, but increases in operating transfers and subsidies, significantly bolstered quarterly operating revenue.

Please see Table 12 for YoY quarterly growth in revenue sources and Appendix 3 for the changes in the composition of operating revenues. From the above analysis, it is clear that the pandemic did undermine DM own revenue streams, notably agency service fee income, interest income, rental income and fines, penalties, licenses and permits. However, it is reductions to operating transfers and subsidies from national government which posed a greater threat to DMs during the period under study. These reductions are a product of national government's fiscal consolidation strategy per se. Increases in transfers and subsidies provided some relief in the successive 2 quarters, but it is evident that the factors confronting DMs are largely systemic in nature.

While Cape Winelands DM experienced a YoY 41% increase in operating expenditure compared to the same quarter in the previous financial year, West Coast and Central Karoo reported declines in quarterly operating expenditure of -1.7% and -33% YoY in the same quarter (see Table 12).

TABLE 12: YEAR-ON-YEAR INCREASE IN QUARTERLY OPERATING EXPENDITURE FOR SAMPLED DISTRICT MUNICIPALITIES

R millions	Pre-pandemic actual				Pandemic actual			% Change YOY		
Operating expenditure	18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	19/20Q4	20/21Q1	20/21Q2
Cape Winelands	62.8	70.1	99.7	105.7	88.4	72.7	100.6	41%	4%	1%
West Coast	81.6	70.2	111.2	92.8	80.2	75.3	108.0	(1.7%)	7%	(3%)
Central Karoo	30.8	11.3	22.1	19.8	20.6	12.1	16.6	(33%)	7%	(25%)

Cost of employment is the biggest expense at DMs ranging from 28% to 68% of quarterly expenditure in the sampled DMs. Cape Winelands DM's increase operating expenditure in the first quarter of the pandemic 2019/20Q4 had little to do with the pandemic but was driven mainly by 171% YoY increase in employment related costs and a 60% YoY in councillor remuneration. In the same quarter, this was partially offset by a -58% decline in depreciation and asset impairment, and other expenditure grew at a fairly modest 9%. In the two subsequent quarters, YoY increase in employee related costs was more restrained (9% and 5% respectively), as well as councillor remuneration (4% and 5% respectively). Other expenditure bore the brunt of cost containment, with declines of -9% and -8% in 2020/21Q1 and 2020/21Q2 respectively.

Cape Winelands has been less successful than the other 2 DMs sampled in terms of personnel spending restraint. While West Coast and Central Karoo have exhibited quarterly average growth rates in employee costs of 5% and -2% between 2018/14Q4 and 2021/22Q2, Cape Winelands has reported a 22% quarterly average growth rate over these 7 quarters. Remuneration of councillors at Cape Winelands increased at an average quarterly growth rate of 6% over the same period, which was on par with Central Karoo (also 6%) but exceeded that West Coast (2%). Central Karoo quarterly employment costs increased YoY by 12% in 2019/20Q4, then contracted by -29% in 2020/21Q1 and -31% in 2020/21Q2. Appendix 6 shows the composition of quarterly operating expenditures and Appendix 5 reflects the YoY changes in operating expenditure from the same quarter in the prior year.

All three DMs showed decreases in contracted services and in other expenditures. For Cape Winelands, there may be very little scope for further cuts without compromising services, and cuts in employment costs may be its only remain option. West Coast DM is the only one of the 3 sampled DMs which had finance charges which was negligible. Cape Winelands and West Coast have small depreciation and asset impairment charges, whereas Central Karoo to all intents and purposes has none.

5.1.2.2 Capital budgets

The resilience of DMs is evident and in the short term they seem to have weathered the storm fairly well in terms of the operating budget balance. However, the greatest short-term impacts have been on capital budgets, which would have operational consequences for municipalities in future. Appendix 7 and Appendix 8 provide more detailed information on capital spending performance during the 3 quarters of the pandemic under study.

TABLE 13: YEAR-ON-YEAR (YOY) CHANGE IN QUARTERLY CAPITAL EXPENDITURE FOR SAMPLED DISTRICT MUNICIPALITIES

R miilions	Pre-pandemic actual				Pandemic actual			% Change YOY		
	18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	19/20Q4	20/21Q1	20/21Q2
Cape Winelands	4.0	0.0	5.6	0.9	0.9	0.0	0.7	(78%)	5%	(87%)
West Coast	6.4	0.5	1.2	3.2	1.9	0.3	2.4	(70%)	(28%)	106%
Central Karoo	0.2	0.0	0.0	0.1	0.0	-	0.0	(88%)	(100%)	9%

DM capital projects are mainly in the areas of health, other community services and governance and administration. Cape Winelands has a road agency function and West Coast DM also spends on bulk water and waste management capital projects. DMs generally saw a decrease in capital projects during the pandemic, except governance and administration. This is perhaps because of existing contractual obligations and the need for financial compliance.

DMs tend to have relatively small capital projects since they do not have to establish or maintain service infrastructure. As can be seen in Table 14, DMs do not receive national capital grants (such as the Municipal Infrastructure Grant) and are therefore heavily reliant on internal funding sources and, to a much lesser extent, provincial conditional grants for funding capital projects. Even more so than the LM's, depletion of investments will make capital funding for DM's extremely difficult, given their lack of own revenue sources and limited scope for accumulating surpluses.

Table 14: Year-on-Year (YoY) change in capital revenue in sampled district municipalities

CATEGORY	CAPACITY	Municipality	R miilions / Revenue source	Pre-pandemic actual 18/19Q4	19/20Q1	19/20Q2	19/20Q3	Pandemic actual 19/20Q4	20/21Q1	20/21Q2	% Change YOY 19/20Q4	20/21Q1	20/21Q2
C1	Medium	Cape Winelands	Transfers: National	-	-	-	-	-	-	-	-	-	-
			Transfers: Provincial	(0.3)	0.0	(0.0)	0.1	0.1	-	0.1	(120%)	(100%)	(1 894%)
			Internal funds	4.3	0.0	5.6	0.8	0.8	0.0	0.7	(81%)	25%	(88%)
			Total capital revenue	**4.0**	**0.0**	**5.6**	**0.9**	**0.9**	**0.0**	**0.7**	**(78%)**	**5%**	**(87%)**
C1	Medium	West Coast	Transfers: National	-	-	-	-	-	-		-	-	-
			Transfers: Provincial	0.1	0.1	0.0	0.2	(0.2)	-	0.5	(256%)	(100%)	1 095%
			Internal funds	6.3	0.4	1.1	3.0	2.1	0.3	1.9	(66%)	(13%)	69%
			Total capital revenue	**6.4**	**0.5**	**1.2**	**3.2**	**1.9**	**0.3**	**2.4**	**(70%)**	**(28%)**	**106%**
C1	Medium	Central Karoo	Transfers: National	-	-	-	-	-	-		-	-	-
			Internal funds	0.2	0.0	0.0	0.1	0.0	-	0.01	(85%)	(100%)	9%
			Total capital revenue	**0.2**	**0.0**	**0.0**	**0.1**	**0.0**	**-**	**0.01**	**(85%)**	**(100%)**	**9%**

See Appendix 7 for change in composition of quarterly capital expenditures.

5.1.3 Shorter term impact on the metro: City of Cape Town

The quarter in which the pandemic struck 2019/20Q4 saw an operating deficit of about R2.4 billion, nearly 25% of operating revenue, and down from a roughly R1.7 billion surplus the previous quarter. The next quarter. 2020/21Q1, saw a rebound to an operating surplus of roughly R3.7 billion.

Table 15: Operating balance as a percentage of operating revenue, City of Cape Town

CATEGORY	CAPACITY	MUNICIPALITY	R millions	Pre-pandemic actual 18/19Q4	19/20Q1	19/20Q2	19/20Q3	Pandemic actual 19/20Q4	20/21Q1	20/21Q2	Surplus/deficit as % 19/20Q3	19/20Q4	20/21Q1	20/21Q2
A	High	City of Cape Town	Operating Revenue	8 661.5	11 272.6	10 991.9	11 047.4	8 601.3	11 339.6	11 159.0				
			Operating Expenditure	8 976.0	8 834.7	10 068.9	9 350.4	11 019.6	9 362.9	11 030.8				
			Operating Surplus/(Deficit)	**(314.5)**	**2 437.9**	**923.1**	**1 697.1**	**(2 418.4)**	**1 976.7**	**128.2**	15.4%	(28.1%)	17.4%	1.1%
			Transfers and subsidies - capital	555.2	168.1	537.7	678.8	241.2	283.1	354.7				
			Taxation	-	-	-	-	(6.4)	(5.4)	(15.7)				
			Attibutable to minorities	-	-	-	-	-	(7.6)	(7.9)				
			Surplus/Deficit	**240.7**	**2 606.1**	**1 460.8**	**2 375.9**	**(2 170.7)**	**2 257.6**	**490.7**				

The quarterly deficit in 2021/22Q1was driven not so much by a shortfall in operating revenue, which increased 2.2% YoY (see the table below), but largely because of accelerating operating expenses which increased by 23% YoY.

As can be seen in the diagram below, service charges for water, electricity, refuse, and sanitation constituted the biggest share of annual operating revenues in the City of Cape Town (47%), followed by property rates (24%) and operating transfers and subsidies (12%), and an assortment of smaller own revenue sources which collectively comprise 17% of operating revenue.

FIGURE 21: COMPOSITION OF OPERATING REVENUES, CITY OF CAPE TOWN, 2019/20 UNAUDITED ACTUAL

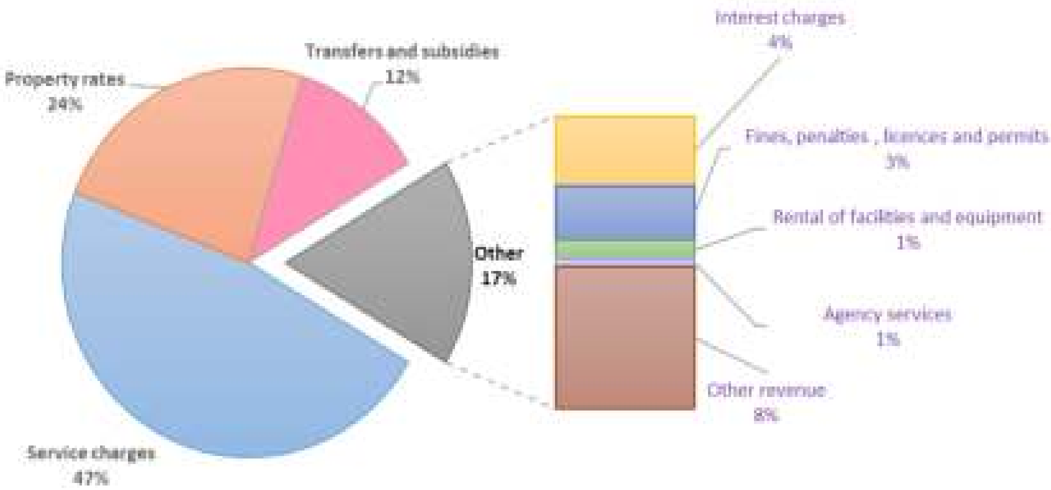


Table 16 illustrates that YoY electricity sales were reduced in compared to the same quarter in the previous year by -3% in 2019/20Q4 (the first quarter of the pandemic), -1% in 2020/21Q1 and 2% in 2020/21Q2. YoY decreases in refuse charges of -7% and -8% can be discerned in 2020/21Q1 and 2020/21Q2. By contrast, water service charges held up fairly well in 2019/20Q4 and the subsequent 2 quarters of the pandemic, possibly because of the drought restrictive water charges. The same applies to sanitation which is linked to water billing.

TABLE 16: YEAR-ON-YEAR (YOY) CHANGES IN QUARTERLY OPERATING REVENUE, CITY OF CAPE TOWN

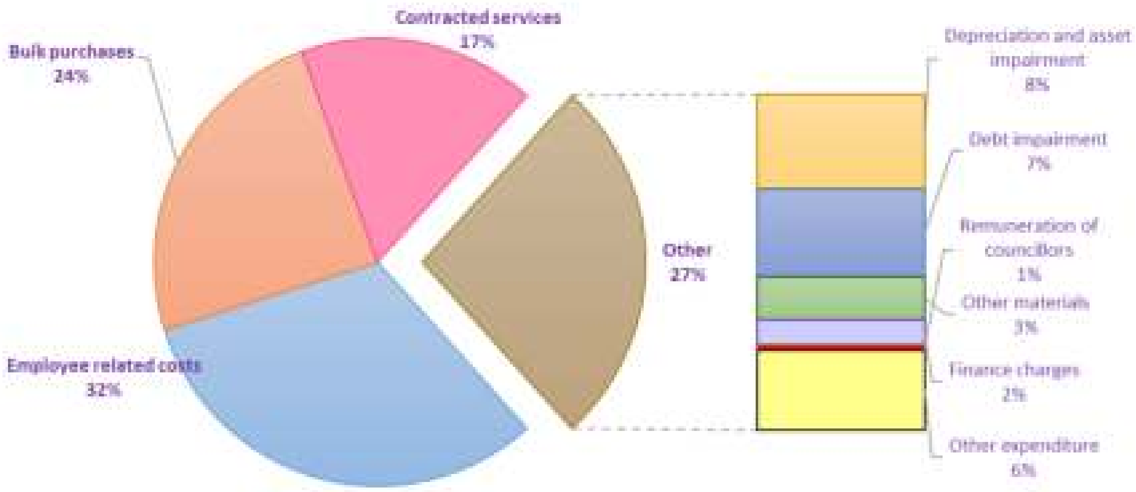
CAPACITY	Municipality	R miilions Revenue source	Pre-pandemic actual				Pandemic actual			% Change YOY		
			18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q3	19/20Q4	20/21Q1	19/20Q4	20/21Q1	20/21Q2
High	City of Cape Town	Property rates	2 395.6	2 480.6	2 542.4	2 474.3	2 507.5	2 570.9	2 596.6	5%	4%	2%
		Electricity charges	3 222.6	3 907.2	3 532.7	3 539.0	3 212.2	3 857.1	3 259.6	(.3%)	(1%)	(8%)
		Water charges	251.3	666.8	732.3	867.4	795.1	711.2	778.0	216%	7%	6%
		Sanitation charges	253.0	340.6	377.5	442.1	408.8	346.1	392.2	62%	2%	4%
		Refuse charges	304.9	321.9	322.0	321.7	307.2	297.9	296.2	1%	(7%)	(8%)
		Transfer and subsidies	999.9	1 483.2	1 417.1	1 251.2	327.2	1 706.4	1 979.6	(67%)	15%	40%
		Interest earned	289.5	415.1	374.0	468.0	453.0	417.7	278.9	56%	1%	(25%)
		Fines, penalties, licences & permits	619.8	384.5	501.1	471.6	260.5	277.9	390.3	(58%)	(28%)	(22%)
		Rental of facilities and equipment	51.9	113.9	94.0	110.9	96.1	114.9	86.9	85%	1%	(7%)
		Agency services	63.2	56.6	62.2	64.4	15.7	72.0	74.7	(75%)	27%	20%
		Other revenues	209.7	1 102.3	1 036.7	1 036.9	218.0	967.5	1 025.9	4%	(12%)	(1%)
		Total operating revenue	**8 661.5**	**11 272.6**	**10 991.9**	**11 047.4**	**8 601.3**	**11 339.6**	**11 159.0**	**(1%)**	**1%**	**2%**

Property rates exhibited YoY increases of 5%, 4% and 2% in 2019/20Q4,2020/21Q1, and 2020/21Q2 respectively. It is clear that the City's two largest operating revenue sources, though negatively impacted by the pandemic, remained fairly stable. Operating transfers contracted sharply by 67% YoY in 2019/20Q4 but recover and increase at 15% and 40% YoY in the subsequent quarters. Hardest hit by the lockdown were the smaller revenue sources: fines, penalties, licences and permits which have sharply contracted by -58%, -28% and -22%

in 2019/20Q4, 2020/21Q1 and 2020/21Q2 respectively. To a lesser degree, this also applied to rental income and other revenues. Agency services declined precipitously YoY by -17% during the hard lockdown in the first quarter of the pandemic 2019/20Q4 and then recover in the 2 subsequent quarters.

As regards operating costs, the largest cost drivers were employee related costs (32% of operating expenditure), Bulk purchases of water and electricity (24%) and contracted services (17%), as can be seen in the diagram below.

FIGURE 22: COMPOSITION OF OPERATING EXPENDITURE, CITY OF CAPE TOWN, 2019/20 UNAUDITED ACTUAL



As can be seen from the table below, total operating expenditure increased by 23% YoY in 2019/20Q4, 6% YoY in 2020/21Q1 and 10% in 2020/21Q2. The 50% increase in transfers and subsidies paid could have been driven by the need for humanitarian aid in the face of the pandemic. City of Cape Town also directed increased resources to support the City's health response and support cleansing and sanitation services.

TABLE 17: YEAR-ON-YEAR (YOY) CHANGES IN QUARTERLY OPERATING EXPENDITURE, CITY OF CAPE TOWN

CATEGORY	CAPACITY	Municipality	R miilions	Pre-pandemic actual				Pandemic actual			% Change YOY		
			Expenditure category	18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	19/20Q4	20/21Q1	20/21Q2
B1	High	City of Cape Town	Employee related costs	2 889.2	2 893.0	3 602.2	3 189.8	3 218.4	3 249.8	3 956.8	11%	12%	10%
			Bulk purchases	1 872.2	2 525.8	2 191.7	2 074.3	3 027.2	2 456.9	2 229.0	62%	(3%)	2%
			Contracted services	1 981.8	970.6	1 745.9	1 725.4	1 912.6	1 014.6	1 932.3	(3%)	5%	11%
			Depreciation and asset impairment	484.1	740.1	745.0	748.9	770.8	701.7	708.1	59%	(5%)	(5%)
			Debt impairment	492.5	577.0	598.9	473.9	850.7	913.7	921.5	73%	58%	54%
			Other materials	384.9	281.3	398.3	346.5	304.0	202.4	435.9	(21%)	(28%)	9%
			Finance charges	175.8	190.5	193.0	190.3	192.0	193.1	193.5	9%	1%	.3%
			Transfers and subsidies	81.3	96.6	87.8	70.7	121.7	79.7	83.5	50%	(18%)	(5%)
			Remuneration of councillors	40.1	40.4	40.9	40.3	46.0	41.6	41.6	15%	3%	2%
			Other expenditure	574.1	519.4	465.3	490.3	576.2	509.4	528.6	.4%	(2%)	14%
			Total operating expenditure	**8 976.0**	**8 834.7**	**10 068.9**	**9 350.4**	**11 019.6**	**9 362.9**	**11 030.8**	**23%**	**6%**	**10%**

Bulk purchases increased in 2019/20Q4 by 62% YoY in 2019/20Q4 and then moderated in the following 2 quarters. Employee costs (which account for roughly 1/3 of operating expenditure in the City) increased YoY by 11%, 12% and 10% in the first 2 quarters of the pandemic. There were also substantial increases in non-cash items in 2019/20Q4 such as depreciation and asset impairment (which is largely determined by the City's asset management policy) and debt impairment (which would have reflected credit control implementation in quarters prior to the pandemic. It is clear that the increase in expenditure costs were affected by pressures from the pandemic but were largely systemic in nature.

5.1.3.1 Capital budget

In terms of capital expenditure, the City has done extremely well under the circumstances, with substantial YoY increase in capital expenditure in all three quarters of the pandemic.

TABLE 18: YEAR-ON-YEAR (YOY) CHANGE IN QUARTERLY CAPITAL EXPENDITURE, CITY OF CAPE TOWN

CATEGORY	CAPACITY	Municipality	R millions / Expenditure category	Pre-pandemic actual 18/19Q4	Pre-pandemic actual 19/20Q1	Pre-pandemic actual 19/20Q2	Pre-pandemic actual 19/20Q3	Pandemic actual 19/20Q4	Pandemic actual 20/21Q1	Pandemic actual 20/21Q2	% Change YOY 19/20Q4	% Change YOY 20/21Q1	% Change YOY 20/21Q2
B1	H	City of Cape Town	Electricity	22.2	0.6	1.8	3.1	93.7	124.6	136.7	321%	20 395%	7 682%
			Water management	29.4	0.5	33.3	33.9	8.0	214.1	207.7	(73%)	42 058%	524%
			Waste water management	2.6	-	10.0	0.7	4.6	219.1	168.8	82%	-	-
			Waste management	7.8	0.3	0.4	0.9	9.5	57.6	49.0	22%	19 569%	13 539%
			Road transport	20.0	0.4	5.9	38.3	268.7	56.4	152.3	1 243%	14 406%	2 500%
			Other community services & public safety	20.3	15.8	25.4	106.1	115.9	159.9	97.1	471%	913%	282%
			Housing	3.0	0.3	4.8	1.4	9.8	90.6	120.7	222%	-	-
			Health	1.6	0.7	3.7	4.1	10.7	1.5	6.2	582%	104%	65%
			Planning, development & Environmental protection	7.2	2.3	2.6	2.3	18.8	38.4	7.0	161%	1 542%	173%
			Governance & administration	138.7	12.5	53.4	158.3	223.5	164.1	123.0	61%	1 209%	130%
			Other	19.7	-	15.6	11.0	17.5	9.2	8.5	(11%)	-	(45%)
			Total capital expenditure	**272.5**	**33.5**	**156.7**	**360.0**	**780.7**	**1 135.4**	**1 077.0**	**187%**	**3 287%**	**587%**

As can be seen in the table below, the City not only increased borrowing for its capital programme, but also received increase in national and provincial capital grants.

TABLE 19: YEAR-ON-YEAR CHANGE IN QUARTERLY CAPITAL REVENUE, CITY OF CAPE TOWN

CATEGORY	CAPACITY	Municipality	R millions / Revenue source	Pre-pandemic actual 18/19Q4	Pre-pandemic actual 19/20Q1	Pre-pandemic actual 19/20Q2	Pre-pandemic actual 19/20Q3	Pandemic actual 19/20Q4	Pandemic actual 20/21Q1	Pandemic actual 20/21Q2	% Change YOY 19/20Q4	% Change YOY 20/21Q1	% Change YOY 20/21Q2
A	H	City of Cape Town	Transfers: National	6.9	(0.01)	3.4	28.7	152.0	198.2	292.0	2 107%	(1 893 548%)	8 548%
			Transfers: Provincial	1.8	0.1	0.8	2.7	11.8	0.4	2.6	571%	217%	219%
			Transfers: Other	1.3	(0.02)	(0.1)	0.0	0.1	-	0.6	-	-	(889%)
			Borrowing	201.7	33.0	128.2	282.6	469.3	299.9	440.5	133%	808%	243%
			Internal funds	-	-	-	-	-	-	926.6	-	-	-
			Total capital revenue	**211.7**	**33.1**	**132.4**	**314.0**	**634.5**	**1 109.9**	**1 662.3**	**200%**	**3 251%**	**1 156%**

5.2 Medium term pandemic impacts

To get a perspective of the impact of the pandemic on sampled municipalities in the medium term, this section examines the 2020/21 budgets of municipalities which began in July 2020 and the 2 outer years projections in the Medium Term Expenditure and Revenue Framework (MTREF) budgets table by Councils.

5.2.1 Regional GDP growth rates and employment in sampled municipalities

Table 20 shows the narrow defined official unemployment rate for persons 15 to 64 years old each of the sampled LMs and the City of Cape Town, ranging from 5.1% and 6% in 2018 in Bergrivier and Swellendam respectively, to 16.4% and 21.4% in Laingsburg and City of Cape

Town in the same year. This narrow definition excludes discouraged workers who had not actively sought work in the previous 4 weeks, and therefore under-estimates unemployment more broadly defined. The table also shows a related measure, the employment-to-population ratio (or labour absorption rate) in 2018 for each municipality, which is the proportion of the working-age population that is employed. The table also shows the regional Gross Domestic Product (GDP-R) of each municipality in 2018, with Drakenstein and Stellenbosch having the largest GDP-R's outside the City of Cape Town, and Kannaland and Laingsburg having the smallest GDP-R. The GDP-R is the aggregate of gross value added (GVA) of all resident producer units in the municipality, and therefore captures the size of the local economy of a municipality, and – by extension – its revenue base. The table below shows the GDP-R of the sampled municipalities in descending order, as a proxy for local economic activity within each municipal jurisdiction. The Cape Metro dominates the other sampled municipalities in terms of GDP-R.

TABLE 20: PROJECTED GDP-R GROWTH RATES IN SAMPLED MUNICIPALITIES 2019-2021

Municipality	Unemployment rate (narrowly defined) (2018)	Labour absorption rate (2018)	Value of GDP-R R million (2018)	GDP-R % average growth (2014-2018)	Estimated real GDP-R growth (2019)	Projected growth rate (2020)	Projected growth rate (2021)	No of jobs (2018)	% average annual change in jobs (2014-2018)	Estimated net change (2019)
Drakenstein LM	13.1	59.5	R22 022	1.4%	0.0%	-6.7%	3.6%	112 778	2 355	117
Stellenbosch LM	10.3	62.5	R16 176	1.4%	0.1%	7.6%	4.3%	78 701	78 701	-107
Swartland LM	10.1	56.8	R8 324	1.8%	-1.2%	-5.7%	4.1%	46 694	1 147	143
Hessequa LM	6.6	68.7	R3 933	1.4%	-0.2%	-6.3%	3.7%	25 484	362	-262
Swellendam LM	6.0	69.3	R2 659	2.5%	0.4%	-4.1%	4.3%	17 804	458	61
Bergrivier LM	5.1	63.9	R4 487	1.4%	-2.30%	-2.1%	1.7%	29 923	546	-59
Hessequa LM	6.6	68.7	R3 933	1.4%	-0.2%	-6.3%	3.7%	25 484	362	-262
Kannaland LM	8.4	57.8	R1 281	1.6%	-1.1%	-4.4%	3.7%	10 230	145	-114
Laingsburg LM	16.4	55.3	R436	0.9%	-1.2%	-1.8%	0.8%	2 928	79	39
Cape Metro	21.4	53.2	R423 210	1.3%	0.5%	-7.3%	3.8%	1 622 989	27 273	-3 564
Western Cape	**18.0**	**56.2**	**R589 444**	**1.4%**	**0.3%**	**-6.9%**	**3.8%**	**2 589 080**	**46 746**	**-4 421**

Source: Data drawn from Western Cape Provincial Treasury (2020)

The Western Cape Treasury's 2020 Municipal Economic Review and Outlook (MERO) shows the slowdown in growth in 2019, prior to the pandemic, to 0.3% for the Western Cape as a whole. As a result, of the pandemic, the WC province's GDP-R was projected to have contracted by 6.9% in 2020 and is expected to increase to 3.8% in 2021. As can be seen in Table 20, the City of Cape Town (with its reliance on tourism, hospitality and related industries, was particularly badly affected, as was Drakenstein and Hessequa with contractions in GDP-R of -7.3%, -6.7% and -6.3% anticipated in 2020 respectively. For 2021, GDP-R growth in Laingsburg (0.8%) and Bergrivier (1.8%) is expected to be slow, Stellenbosch (4.3%), Swellendam (4.3%) and the City (3.8%) are expected to rebound much faster. The table also reveals that, despite positive job growth between 2014 and 2018, Bergrivier, Kannaland, Stellenbosch and the City were projected to have job losses, potentially increasing the number of indigents and undermining their user tariff and rates bases. Agriculture and agro-processing (e.g. citrus) are projected to be fast growing sectors as they recover from the contraction caused by the drought in the Western Cape. The Central Karoo (Laingsburg) has been particularly hard-hit by persistent drought conditions in recent years which has impacted negatively on growth and employment.

The GDP-R growth rates are a good proxy indicator of the growth of a municipality's rates base, its ability to borrow and trends in relation to bad debt, increased indigence and demand for free basic services.

5.2.2 Local municipalities' medium term fiscal forecasts

The analysis in this section focusses on annual audited data 2016/17 to 2018/19, unaudited estimates for 2019/20 (a period which included the first 3 months of the pandemic in the last quarter of that financial year) and medium term projections for 2020/21–2022/23, in contrast to the analysis in the section which focused on quarterly actuals. A medium term perspective can be gained on how municipalities view their sustainability, contingent on the assumptions that they make about the future (e.g. growth rates of tax bases, expenditures and inflation. As explored further below, the sustainability issues which appear to be not that pressing in the short term, are more clearly visible over the medium term.

The balance on the operating budget (i.e. surplus or deficit) is one of the most fundamental measures of financial performance. The ability of municipalities to generate cash based operating surpluses is critical to accumulate internal reserves to fund capital expenditure, as well as to insulate the municipality against shocks like droughts and pandemics. Accumulated surpluses can also be used to finance long term debt, and therefore the operating budget balance is a crucial indicator for assessing a municipality's creditworthiness, which in turn impacts its cost of borrowing.

As can be seen from Table 21, in the original budget tabled in council at the start of the 2019/20 financial year, Laingsburg had budgeted for an operating deficit of R11.5 million. Capital transfers to the tune of 12.1 billion would have resulted in a positive overall balance of R0.6 million. The unaudited projected outcome for 2019/20 (which incorporates the first quarter of the pandemic) is estimated to have resulted in a larger operating deficit of R11.5 million at year end, due to operating expenditure being 6% more than originally budgeted for, and operating revenue 8% higher than budgeted. With actual capital transfers only amounting to R 6.7 million, the overall balance in 2019/20 is estimate at deficit of R6 million. As will be explored further later, the larger than budgeted increase was driven mainly by non-cash items (depreciation, asset impairment and debt impairment) and therefore would not compromise liquidity as much. Hessequa also had initially budgeted for an operating deficit of R16.5 million but ended the year with an operating deficit R16.8 million, with revenues 7% higher than the previous year and operating expenses 20% higher. This was driven mainly by depreciation and asset impairment being 25% higher than budgeted for, finance charges being 27% higher and contracted services 59% higher. It is difficult to compare contracted services during the MTREF with prior year actuals since after the implementation of the municipal standard chart of accounts (MSCOA), some of the services under general expenses were re-classified as contracted services, resulted in higher reported amounts.

With capital transfers of R17.5 million, Hessequa attains an overall positive balance of R0.6 million. What is interesting is that these operating deficits are largely not as a result of the pandemic: depreciation and asset impairment is a function of the municipality's asset management policy and debt impairment the outcome of credit control implementation in previous periods. In Kannaland, an operating deficit of R31.2 million had been budgeted for, but an estimated operating deficit -R0.9 million was achieved. While actual operating revenue fell —4% short of budgeted targets, but costs were constrained to -28% below budgeted. While operating revenue was -6% less than the prior year, operating expenditure was -30% lower.

TABLE 21: 2020/21 MTREF OPERATING BALANCES FOR SAMPLED LOCAL MUNICIPALITIES

CATEGORY	CAPACITY	Municipality	R millions	Audited Outcome			Original Budget	Pre-audit Actual Outcome	Medium Term Revenue & Expenditure Framework			% change YoY	Actual vs budget variance	Avg annual growth over MTREF period	
				16/17	17/18	18/19	19/20		20/21	21/22	22/23	19/20		2016/17-2019/20	2020/21-2022/23
B1	High	Stellenbosch	Operating Revenue	1 429.2	1 532.4	1 524.0	1 778.6	1 578.6	1 899.7	2 025.1	2 172.5	4%	-11%	3%	7%
			Operating Expenditure	1 316.4	1 346.3	1 487.6	1 808.2	1 366.8	1 887.5	2 002.4	2 141.7	-8%	-24%	1%	7%
			Operating Surplus/(Deficit)	**112.8**	**186.1**	**36.4**	**(29.6)**	**211.8**	**12.3**	**22.6**	**30.8**	**482%**	**816%**	**23%**	**59%**
			Capital transfers and subsidies	105.2	77.5	88.2	141.1	108.2	113.4	89.3	100.7	23%	-23%	1%	-6%
			Surplus/(Deficit)	**218.0**	**263.6**	**124.6**	**111.5**	**320.0**	**125.7**	**111.9**	**131.5**	**157%**	**187%**	**14%**	**2%**
	High	Drakenstein	Operating Revenue	1 783.4	1 886.8	1 979.3	2 331.8	2 163.2	2 431.2	2 604.7	2 795.0	9%	-7%	7%	7%
			Operating Expenditure	1 822.6	2 035.2	2 200.1	2 399.6	1 938.5	2 515.2	2 653.7	2 787.7	-12%	-19%	2%	5%
			Operating Surplus/(Deficit)	**(39.2)**	**(148.4)**	**(220.9)**	**(67.8)**	**224.6**	**(84.0)**	**(49.0)**	**7.3**	**202%**	**431%**		
			Capital transfers and subsidies	74.6	156.0	177.1	120.9	98.1	168.1	65.0	62.7	-45%	-19%	10%	-39%
			Surplus/(Deficit)	**35.4**	**7.6**	**(43.8)**	**53.1**	**322.7**	**84.2**	**16.0**	**70.0**	**-837%**	**508%**	**109%**	**-9%**
B3	Medium	Swartland	Operating Revenue	601.1	682.7	754.6	751.7	810.8	783.2	886.2	917.1	7%	8%	10%	8%
			Operating Expenditure	545.6	615.5	686.9	737.9	746.1	797.9	876.1	909.9	9%	1%	11%	7%
			Operating Surplus/(Deficit)	**55.5**	**67.2**	**67.7**	**13.8**	**64.7**	**(14.7)**	**10.1**	**7.2**	-4%	368%	5%	
			Capital transfers and subsidies	35.4	56.7	47.1	67.2	63.8	86.9	28.9	66.7	36%	-5%	22%	-12%
			Surplus/(Deficit)	**90.9**	**123.9**	**114.8**	**81.0**	**128.5**	**72.1**	**39.0**	**73.9**	**12%**	**59%**	**12%**	**1%**
B3	Medium	Hessequa	Operating Revenue	435.1	422.2	467.5	480.9	499.0	537.8	602.6	632.7	7%	4%	5%	8%
			Operating Expenditure	391.0	405.4	430.6	497.4	515.9	572.7	622.1	652.3	20%	4%	10%	7%
			Operating Surplus/(Deficit)	**44.0**	**16.8**	**36.8**	**(16.5)**	**(16.8)**	**(34.9)**	**(19.5)**	**(19.6)**	-146%	2%	-173%	-25%
			Capital transfers and subsidies	95.8	35.6	29.6	17.1	20.7	22.2	16.7	14.3	-30%	21%	-40%	-20%
			Surplus/(Deficit)	**139.8**	**52.5**	**66.4**	**0.6**	**3.9**	**(12.7)**	**(2.8)**	**(5.3)**	**-94%**	**522%**	**-70%**	**-35%**
B3	Medium	Bergrivier	Operating Revenue	286.3	288.2	321.2	368.2	352.2	364.5	418.8	440.9	10%	-4%	7%	10%
			Operating Expenditure	276.6	285.5	315.3	376.5	309.2	378.6	422.4	436.3	-2%	-18%	4%	7%
			Operating Surplus/(Deficit)	**9.7**	**2.7**	**5.9**	**(8.3)**	**43.0**	**(14.1)**	**(3.6)**	**4.6**	627%	-616%	64%	
			Capital transfers and subsidies	12.3	16.7	20.6	24.3	11.2	15.9	14.9	18.0	-46%	-54%	-3%	6%
			Surplus/(Deficit)	**22.0**	**19.4**	**26.5**	**16.0**	**54.2**	**1.7**	**11.3**	**22.6**	**104%**	**239%**	**35%**	**260%**
B3	Low	Swellendam	Operating Revenue	213.8	230.2	247.7	281.8	270.5	297.6	308.3	347.1	9%	-4%	8%	8%
			Operating Expenditure	213.3	238.3	246.8	299.1	261.2	322.9	331.6	369.8	6%	-13%	7%	7%
			Operating Surplus/(Deficit)	**0.5**	**(8.2)**	**0.9**	**(17.2)**	**9.3**	**(25.3)**	**(23.4)**	**(22.7)**	941%	154%	171%	-5%
			Capital transfers and subsidies	14.2	17.5	11.9	15.3	38.2	16.2	14.8	13.5	220%	150%	39%	-9%
			Surplus/(Deficit)	**14.7**	**9.3**	**12.8**	**(1.9)**	**47.5**	**(9.1)**	**(8.6)**	**(9.2)**	**270%**	**2595%**	**48%**	**1%**
B3	Medium	Kannaland	Operating Revenue		145.6	137.2	162.1	171.2	163.7	177.7	194.3	25%	6%	8%	9%
			Operating Expenditure		63.4	169.1	163.0	165.3	163.2	175.8	193.7	-2%	1%	61%	9%
			Operating Surplus/(Deficit)	**-**	**82.3**	**(31.9)**	**(0.9)**	**6.0**	**0.5**	**1.9**	**0.6**	119%	787%	-73%	9%
			Capital transfers and subsidies		11.7	11.2	52.2	35.3	65.4	40.2	36.9	216%	-32%	74%	-25%
			Surplus/(Deficit)		**93.9**	**(20.3)**	**51.4**	**41.3**	**65.9**	**42.0**	**37.5**	**-304%**	**-20%**	**-34%**	**-25%**
B3	Medium	Laingsburg	Operating Revenue	65.1	74.8	77.4	82.6	89.1	93.6	95.6	99.5	15%	8%	11%	3%
			Operating Expenditure	80.6	74.1	87.9	94.1	99.8	98.9	100.0	103.7	14%	6%	7%	2%
			Operating Surplus/(Deficit)	**(15.5)**	**0.7**	**(10.5)**	**(11.5)**	**(10.7)**	**(5.3)**	**(4.4)**	**(4.2)**	3%	-6%	-12%	-11%
			Capital transfers and subsidies	9.5	7.5	13.2	12.1	6.7	10.0	8.4	8.5	-49%	-44%	-11%	-8%
			Surplus/(Deficit)	**(6.1)**	**8.1**	**2.7**	**0.6**	**(4.0)**	**4.7**	**4.0**	**4.3**	**-246%**	**-792%**	**-13%**	**-4%**

Note: There are no data for Kannaland for 2016/17 and 2018/19, which is current under administration in a section 139(5) intervention. Kannaland's annual average growth rates are calculated from 2017/8-2019/20 due to unavailable data for 2016/17

Source: National Treasury website MTREF database, own calculation

Surprisingly, Stellenbosch, Drakenstein, Bergrivier, and Swellendam had all budgeted for operating deficits in their original 2019/20 budgets at the beginning of the financial year, but are estimated to have operating surpluses in 2019/20, despite the pandemic, mainly by ensuring that, despite revenue falling short of budgeted in 2019/20, expenditures fell faster. Swartland had budgeted for an operating surplus of R13.8 million in 2019/20, and achieved a greater actual operating surplus of R64.7 million due to operating revenues 8% in excess of budgeted targets, while operating expenditure was only 1% over budget.

Swellendam has forecasted both an operating and overall deficit over each of the three years of the MTREF period (-R25.3 million, -R23.4 million and -R22.7 million in 2020/21, 2021/22 and 2022/23 respectively), suggesting a significant deterioration in fiscal sustainability, driven by operating expenditures envisaged to escalate at an annual average growth rate of 7% over the MTREF period, while revenues are only projected to increase at an annual average growth rate of 8%. It should be noted that Swellendam's MTREF remains "funded" in terms of cash backed reserves/accumulated services as per MFMA Circular 42, with projected cash and investments sufficient to cover the projected liabilities/commitments that would exist. Laingsburg and Hessequa similarly also project operating deficits over each of the 3 MTREF years, but achieve positive overall balances due to capital transfers. Bergrivier project operating deficits in 2020/21 and 2021/22 but envisage operating surpluses in 2022/23, as does Drakenstein. Swartland has projected a R14.7 million operating deficit in 2020/21, thereafter swinging into operating surpluses of R10.1 million and R7.2 million in 2021/22 and 2022/23 respectively. Kannaland has budgeted for modest surpluses of R0.5 million, R1.9 million and R0.6 million over the MTREF. Stellenbosch has budgeted for operating surpluses of R12.3 million. R22.6 million and R30 million in 2020/21, 2021/22 and 2022/23 respectively, but these operating surpluses are modest compared to the operating surpluses ran in 2017/18 (R186.1 million) and 2019/20 (R211.8 million). These operating surpluses will be crucial for replenishing capital replacement reserves in these municipalities. Drakenstein, in its 2020/21 MTREF Budget Report indicated that cash surpluses at year end would be dedicated to this purpose.

Analysis of the medium term outlook of sampled municipalities reveals more fundamental, negative fiscal sustainability trends, not only related to the pace of the post-pandemic economic recovery but also due to systemic factors explored further below. Running operating deficits depletes internal funds and reduces investment income. Since municipalities are not allowed to borrow to replenish their capital reserves, this has serious ramifications for capital programmes in municipalities which rely on internal funds.

That the short term revenue impact on the sample from 2019/20Q4, the first quarter of the pandemic was not as bad as could have been expected (given the magnitude of the disaster) is evidenced by the fact that total operating revenue only fell short of budgeted targets by more than 10% only in 2 municipalities: Kannaland and Stellenbosch. As reflected in Table 22, Kannaland undershot its annual revenue target by 20% in 2019/20, and saw a YoY decrease in revenue of -6% in total operating revenue from the previous year. Services charges, which comprised 70% of the municipality's operating revenue in 2019/20, marginally exceeded the budgeted amount by 2%. However, there was an across-the-board decline in other revenue sources, including transfers and subsidies, which comprised 24% of operating revenue in the same year and fell short of the budgeted target by 18%. Property rates, which constituted 11% of Kannaland's budget undershot budgeted targets by 14% in 2019/20 (which encompassed the first quarter of the pandemic). Road agency services and other revenues (fines, penalities, licences, permits etc) had budget shortfalls of -28% and -48% in 2019/20 (and shrank by -12% and -64% from the previous year. Fortunately road agency services and other revenues collectively contribute only 6% of Kannaland's revenue.

Stellenbosch undershot its revenue target by 11% in 2019/20 (as can be seen in Table 22), but still achieved a 4% increase over the previous financial year. Here again transfers and subsidies, interest earned and other revenues experienced the greatest shortfalls, but only comprise a small proportion (6%) of operating revenues in 2019/20. By contrast, service revenue which constitutes 60% of the municipality's operating revenue, only fell short of the revenue target in 2019/20 by 7% and still exhibited a 16% increase from the prior year. Interestingly, property rates outcomes exceeded budgeted targets by 3%, a 16% increase from the prior year. This reflects the more skilled and affluent nature of the municipalities rates base, which could more easily transition to working from home and were less vulnerable to loss of livelihood.

Table 22 reflects that four municipalities saw operating revenue decline less than 10% below budgeted targets in 2019/20, but still recorded an increase in revenue from the prior year (Drakenstein, Stellenbosch, Bergrivier and Swellendam). Three municipalities in the sample not only increased revenues from the previous year, but also surprisingly exceeded their 2019/20 revenue targets (Swartland, Hessequa, Laingsburg). The coronavirus pandemic and lockdown did constrain municipality's ability to increase tariffs. Bergrivier, in its 2019/20 MTREF Budget report notes that "Covid-19 has forced us to temporarily abandon certain normal tariff setting principles to ensure that the impact that the pandemic has had on municipal customers is mitigated to some extent" (p16) and provided 1KL of water free to all households during lockdown (p18). Similarly, Swartlands 2020/21 MTREF Budget Report notes that after "a detailed analysis of financial position and current risks, the Executive Mayor made it clear that the tariffs and taxes be revised downwards to assist the struggling consumers and business during this time, having regard for the impact on cash flows and the municipality's reserves" (p10).

In relation to water tariffs, the drought had been declared a national disaster in terms of the National Disaster Management Act by the Minister of Cooperative Government in March 2020 (2 years after the previous drought disaster declaration in 2018 which brought the City of Cape Town and other Western Cape municipalities perilously close to a Day Zero scenario). Munipalities such as Kannaland would have therefore approved water restriction and higher drought tariff guidelines from 1 July 2020. This could also account for stronger than anticipated water revenues.

In general, while property rates and service charge revenue remained relatively stable or increased, this was offset by drops in other own revenue. These sources include rental of municipal facilities, fines and penalties, licences etc, all of which would have been curtailed by the lockdown in the last quarter of 2019/20.

The average annual growth in operating revenue for the sampled LMs over the MTEF period is 7.6%. Kannaland (9%) and Bergrivier (10%) saw operating revenue increases higher than that, and Lainsburg (3%) significantly lower than that. Kannaland's revenue continues to be placed under pressure by the continuing drought. Kannaland's 2020/21 MTREF Budget reports that while the municipality sets tariff increases above inflation, its increased inability to collect has meant that this is not translated into additional revenue (p11).

The larger municipalities had higher rates of property rates and service charge increases over the MTREF. While medium size municipalities may have seen property rates income increase due to the third supplementary valuation roll, the property market is expected to be much more subdued in the wake of the pandemic, undermining the growth of the rates base. In its 2020/21 MTREF Budget Report, Bergrivier LM notes that the “current rates base can no longer support the costs of services" (p14) and emphasised the importance of securing additional revenue sources.

Some medium and smaller LMs also saw quite large nominal increases in transfers over the MTREF (Hessequa 24%, Bergriver 16%, Kannaland 16%) which allowed them to have smaller increases in property rates and service charges. Laingsburg projected the lowest increase in transfers and subsidies over the MTREF (3% annual average growth rate) and the lowest total operating revenue growth over the same period. In the past, government had sought to protect the equitable share transfers from fiscal consolidation in order to foster a stable fiscal framework. Recently, however, the need for fiscal consolidation (exacerbated by a national tax collapse) and the need to bail out state own entities has resulted in cuts to the local government Equitable Share and conditional grants. Reductions to intergovernmental operating and capital grants are a material risk over the MTREF. This is likey to affect the most grant dependent municipalities the greatest (Bergrivier, Swellendam, Kannaland and Laingsburg).

The sampled LM’s also revised their annual collection rates downwards due to the Covid-19 pandemic, with a slow recovery towards the end of the MTREF period. Hessequa, for instance, adjusted its collection rate downwards from 98% to 95%. Due to the outbreak of the COVID-19 virus and its negative impact on the economy, Drakenstein lowered its projected revenue collection rate from 97.8% to 94% of the billed revenue and made provision for bad debt impairment for the shortfall.

Most of the municipalities sampled intend embarking on new revenue enhancement programmes or intend intensifying their credit control initiatives. For instance, Bergrivier – in its 2021/22 MTREF budget document indicated that a revenue enhancement plan had been drafted and to ensure all revenue is correctly billed in accordance with the category, user type and applicable tariffs and number of service units. Many sampled LM’s also used the lockdown to intensify data cleansing of service user and rate payer accounts, and are seeking to reduce illegal connections and theft. Swellendam’s 2020/21 MTREF Budget Report hlighlights the need for an “aggressve revenue anagement framework” with a focus not only concurrent billings but also the recovery of payments from debtors with arrears in exceess of 90 days (p57).

Kannaland’s 2020/21 MTREF Budget Report also indicated its intension to engage in data cleansing, door to door audits and a GPS exercise to attain the revenue enhancement goals in its Financial Recovery Plan (p11) and noted that the prevention of water losses due to by-passed and faulty water meters has already resulted in revenue increases (p4). Laingsburg has a satisfactory average collection rate of 95.7% but envisages that thise will weaken during 2020/21 due to the pandemic but recover in the MTREF outer years. Consequently, the municipality’s 2020/21 Budget Statement notes that more serious efforts will have to be applied to collecting debt from consumers who can afford to pay for service (p11). It will also promote the installation of new prepaid water meters to ensure that those customers who can afford to pay but are currently consuming free water, do so.

TABLE 22: 2020/21 MTREF OPERATING REVENUE FOR LOCAL MUNICIPALITIES

CATEGORY	CAPACITY	Municipality	R millions	Audited Outcome 16/17	Audited Outcome 17/18	Audited Outcome 18/19	Original Budget 19/20	Pre-audit Actual Outcome 19/20	MTREF projections 20/21	MTREF projections 21/22	MTREF projections 22/23	% YoY change 19/20	Actual vs budget variance 19/20	Avg annual growth over MTREF period 2016/17-2019/20	Avg annual growth over MTREF period 2020/21-2022/23
B1	High	Drakenstein	Property rates	224.8	245.5	271.1	305.3	314.5	331.5	356.4	383.1	16%	3%	12%	8%
			Service charges	1 232.9	1 296.1	1 357.2	1 605.0	1 569.2	1 676.4	1 807.5	1 948.8	16%	-2%	8%	8%
			Transfer and subsidies	144.6	178.1	182.5	250.7	197.2	265.1	282.3	301.4	8%	-21%	11%	7%
			Interest earned	36.7	40.2	25.1	24.6	13.4	16.3	17.1	17.8	-47%	-45%	-28%	4%
			Other revenues	144.4	127.0	143.3	146.2	68.9	141.9	141.5	143.9	-52%	-53%	-22%	1%
			Total operating revenue	**1 783.4**	**1 886.8**	**1 979.3**	**2 331.8**	**2 163.2**	**2 431.2**	**2 604.7**	**2 795.0**	**9%**	**-7%**	**7%**	**7%**
B1	High	Stellenbosch	Property rates	290.0	310.0	333.0	356.1	365.7	392.2	417.7	444.9	10%	3%	8%	7%
			Service charges	795.2	862.0	817.8	1 024.6	950.9	1 072.8	1 159.7	1 254.2	16%	-7%	6%	8%
			Transfer and subsidies	122.6	133.1	146.0	172.3	163.2	178.5	181.2	197.6	12%	-5%	10%	5%
			Interest earned	62.7	62.0	52.3	55.5	48.7	51.2	48.7	44.6	-7%	-12%	-8%	-7%
			Agency services	6.4	2.4	2.8	2.9	2.5	2.9	3.1	3.3	-11%	-11%	-27%	6%
			Other revenues	152.3	163.1	172.2	167.3	47.6	202.1	214.6	227.9	-72%	-72%	-32%	6%
			Total operating revenue	**1 429.2**	**1 532.4**	**1 524.0**	**1 778.6**	**1 578.6**	**1 899.7**	**2 025.1**	**2 172.5**	**4%**	**-11%**	**3%**	**7%**
B3	Medium	Swartland	Property rates	89.5	102.7	115.7	121.3	125.0	128.9	141.1	150.4	8%	3%	12%	8%
			Service charges	342.1	358.6	406.2	419.7	454.7	444.4	473.5	503.1	12%	8%	10%	6%
			Transfer and subsidies	86.8	110.0	130.6	112.7	126.2	120.5	176.4	162.6	-3%	12%	13%	16%
			Interest earned	28.7	33.9	42.8	43.7	47.6	35.3	38.2	42.5	11%	9%	18%	10%
			Agency services	3.8	4.1	4.4	4.3	3.9	4.9	5.2	5.5	-10%	-8%	1%	6%
			Other revenues	50.2	73.4	54.9	50.1	53.3	49.2	51.8	53.0	-3%	6%	2%	4%
			Total operating revenue	**601.1**	**682.7**	**754.6**	**751.7**	**810.8**	**783.2**	**886.2**	**917.1**	**7%**	**8%**	**10%**	**8%**
B3	Medium	Hessequa	Property rates	71.0	78.1	86.7	94.7	94.7	100.9	106.7	113.0	9%	0%	10%	6%
			Service charges	189.0	201.5	218.9	245.1	245.4	261.3	278.6	297.9	12%	0%	9%	7%
			Transfer and subsidies	62.6	60.3	56.6	59.1	65.2	73.4	110.6	112.9	15%	10%	1%	24%
			Interest earned	19.6	19.9	20.6	10.4	10.4	10.5	13.7	13.7	-49%	0%	-19%	14%
			Agency services	2.0	2.2	2.4	2.2	2.2	2.5	2.6	2.8	-9%	0%	4%	6%
			Other revenues	90.9	60.1	82.4	69.4	81.2	89.1	90.5	92.4	-1%	17%	-4%	2%
			Total operating revenue	**435.1**	**422.2**	**467.5**	**480.9**	**499.0**	**537.8**	**602.6**	**632.7**	**7%**	**4%**	**5%**	**8%**
B3	Medium	Bergrivier	Property rates	56.4	62.6	67.8	71.7	74.1	77.8	81.5	85.4	9%	3%	9%	5%
			Service charges	149.3	145.6	160.6	188.1	189.9	193.0	202.3	212.0	18%	1%	8%	5%
			Transfer and subsidies	42.6	49.0	56.5	67.1	54.9	68.9	86.2	93.4	-3%	-18%	9%	16%
			Interest earned	10.1	12.0	13.6	10.0	13.8	12.6	13.2	13.8	2%	38%	11%	5%
			Agency services	3.8	4.0	4.3	4.4	3.6	4.7	5.0	5.2	-17%	-19%	-2%	5%
			Other revenues	24.1	14.9	18.4	26.9	15.9	7.5	30.7	31.1	-14%	-41%	-13%	104%
			Total operating revenue	**286.3**	**288.2**	**321.2**	**368.2**	**352.2**	**364.5**	**418.8**	**440.9**	**10%**	**-4%**	**7%**	**10%**
B3	Low	Swellendam	Property rates	32.6	35.1	37.5	40.5	39.9	42.1	45.4	48.6	6%	-2%	7%	7%
			Service charges	100.7	104.7	113.1	126.3	127.0	138.3	149.2	160.8	12%	1%	8%	8%
			Transfer and subsidies	35.1	40.3	41.3	52.4	56.7	55.3	49.9	71.9	37%	8%	17%	14%
			Interest earned	5.3	5.4	6.0	5.3	6.7	6.0	6.8	7.1	11%	27%	8%	9%
			Agency services	1.7	1.9	2.1	1.9	1.9	2.2	2.3	2.4	-8%	1%	5%	5%
			Other revenues	38.4	42.8	47.6	55.5	38.3	53.7	54.7	56.2	-20%	-31%	0%	2%
			Total operating revenue	**213.8**	**230.2**	**247.7**	**281.8**	**270.5**	**297.6**	**308.3**	**347.1**	**9%**	**-4%**	**8%**	**8%**
B3	Medium	Kannaland	Property rates		17.2	15.5	17.1	17.1	19.5	21.3	23.1	10%	0%	0%	9%
			Service charges		68.7	69.7	89.0	90.4	90.4	76.1	92.0	30%	2%	15%	1%
			Transfer and subsidies		47.1	33.8	37.1	46.3	37.8	43.4	51.1	37%	25%	-1%	16%
			Interest earned		3.9	0.7	6.1	6.4	5.6	5.9	6.3	791%	4%	28%	7%
			Agency services		-	0.8	1.0	1.0	1.0	1.1	1.1	22%	0%		5%
			Other revenues		8.6	16.6	11.7	10.0	7.8	8.3	8.7	-40%	-15%	7%	6%
			Total operating revenue		**145.6**	**137.2**	**162.1**	**171.2**	**163.7**	**177.7**	**194.3**	**25%**	**6%**	**8%**	**9%**
B3	Medium	Laingsburg	Property rates	3.3	3.5	3.9	4.3	4.2	4.7	4.9	5.2	7%	-2%	9%	5%
			Service charges	16.8	17.3	17.3	20.9	21.4	25.1	26.3	27.6	24%	2%	8%	5%
			Transfer and subsidies	17.1	21.6	18.9	22.3	17.9	27.6	27.5	29.1	-6%	-20%	1%	3%
			Interest earned	0.9	0.8	1.4	1.2	1.3	1.4	1.3	1.3	-8%	7%	15%	-6%
			Agency services	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2	-19%	-11%	-5%	6%
			Other revenues	27.0	31.5	35.7	33.7	44.2	34.6	35.4	36.2	24%	31%	18%	2%
			Total operating revenue	**65.1**	**74.8**	**77.4**	**82.6**	**89.1**	**93.6**	**95.6**	**99.5**	**15%**	**8%**	**11%**	**3%**

Note: There are no data for Kannaland for 2016/17 and 2018/19, which is current under administration in a section 139(5) intervention. Kannaland's annual average growth rates are calculated from 2017/8-2019/20 due to unavailable data for 2016/17

Source: National Treasury website MTREF database, own calculation

LMs also stressed the importance of exploring new revenue sources. Hessequa's 2021/22 MTREF budget report notes that the Municipal Fiscal Powers and Functions Act already allows municipalities to apply to the Minister of Finance to levy additional taxes such as the tourism levies and fire levies recommended by the FFC (p 16). It goes on to stress the importnce of applying to the Minister of Finance to pilot the introduction of new revenue sources.

Employee costs and bulk services are the largest cost drivers for LMs. As can be seen from Table 23, in 2019/20, only 3 of the 7 sampled LMs had pre-audit total operating expenditure outcomes which exceeded their original budgets: Swartland (1%), Hessequa (4%) and Laingsburg (6%). In Swartland, this is attributable to employee related costs exceeding the original budget by 1% (and increasing 14% from the previous year) and by bulk services 1% in excess of the original budget, a YoY increase of 18%, while debt impairment unaudited actual exceeded the original budget by 37%. In Hessequa, cost of employment rose by 24% from the previous year, but still fell short of the original budgeted amount by 1%, and there was no variance between actual and budgeted bulk purchases (which increased 12% YoY). In this municipality, debt impairment and contracted services exceeded the original budgeted amount by 24% and 28% respectively. Contracted services are expected to increase by an annual average rate of 33% over the MTREF period. In the case of Laingsburg, employee related costs, bulk services and contracted services expenditure outcomes for 2019/20 were tightly controlled, well within the budgeted allocations, but finance charges, depreciation and asset impairment and debt impairment exceeded original budget amounts by 24%, 30% and 33% respectively. While finance charges comprise less than 1% of Laingsburg's operating spending, depreciation and debt impairment, and debt impairment were more significant cost drivers in 2019/20, amounting to 13% and 18% of operating expenditures in that year. In Swellendam, total operating expenditure in 2019/20 increased by 6% compared to the previous year, but was still -13% smaller than the originally budgeted amount. Although employee costs, bulk purchases and contracted services increased by 14%, 16% and 25% from the prior year, these were partially offset by YoY declines in finance charges (-34%), debt impairment (-10%) and other expenditures (-10%). The three LMs with most stringent cost containment measures not only remained within their operating expenditure budgets but even exhibited decreases compared to the previous year: Stellenbosch has an -8% YoY decrease in total operating expenditure, Drakenstein had a -12% YoY decrease, and Kannaland had a -30% decrease. In Stellenbosch, this outcome was largely driven by significant decreases in depreciation and asset impairment, finance charges, debt impairment and other expenditures. Drakenstein and Kannaland not only decreased these expenditure items, but also decreased cost of employment by -5% and -8% respectively.

The impact of COVID-19 also resulted in unforeseen and unfunded expenditure requirements for municipalities. For Drakenstein, for instance, according to its 2020/21 MTREF budget report, indicated that these included humanitarian aid of R1.8 million, of which R800 000 came from own funding, personal protective equipment (PPE); overtime and standby allowance and the costs of sanitising and health precautions for municipal buildings and employees. Hessequa's 2020/21 MTREF Budget Report notes that R700 000 was used by the municipality for PPE and sanitization of public facilities. Even though food security is not the mandate of LMs, Drakenstein municipality, in terms of the Disaster Management Act and MFMA, concluded an agreement with a nonprofit organization, Valcare, to send electronic food vouchers directly to the phone of the beneficiary which were redeemable at a number of local Drakenstein stores. This is an excellent example of innovation and collaboration with NPOs and the communities.

The e-food voucher, sent directly to the phone of the beneficiary, is redeemable at a number of local Drakenstein stores. Also, additional water tanks and sanitation was provided to informal settlements On the other hand, there were offsetting factors such as lower costs of travel and subsistence to attend meeting which partially offset this, as well as increased national operating grants. Bergrivier also increased its humanitarian relief efforts as a result of the pandemic from R625 000 initially budgeted in 2020/21 to R 1.355 million

Table 23 illustrates that the annual average increase in operating expenditure in the sample of LMs over the MTREF period was 6.4%, roughly in line with the Consumer Price Index and higher than the average annual increase of 6.1% between 2016/17 and 2019/20.

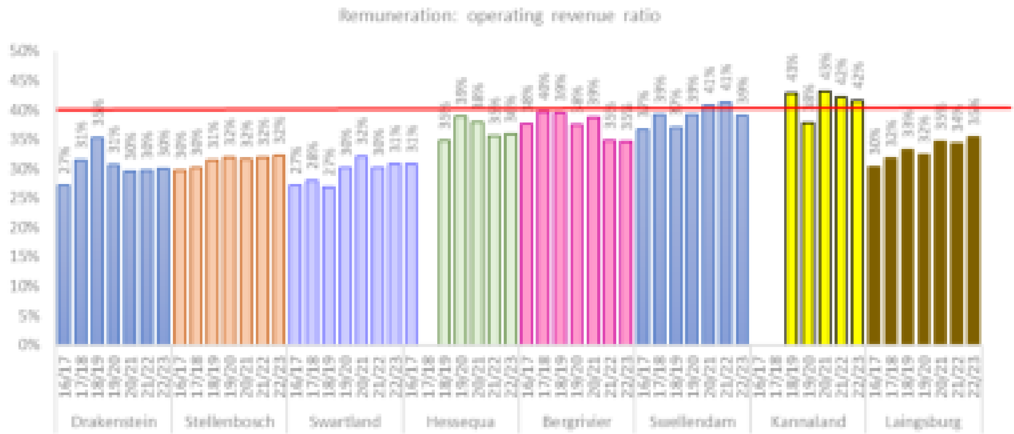
The larger LM's (Drakenstein and Stellenbosch) have made the largest provisions (8%). for increases in employee costs over the MTREF. Swartland, Swellendam and Kannaland are projecting an average annual personnel cost increase of about 6% over the MTREF, and Bergrivier, Hessequa and Laingsburg have estimate personnel cost increases of less than that, suggesting more stringent control of employment costs. (Given that conditions of service are centrally bargained, this suggests reduced headcount through freezing vacancies etc). P6: Most municipalities aligned to the Salary and Wage Collective Agreement for the period 01 July 2018 to 30 June 2021 is was still in operation, resulting in an increase of 6.25% for 2020/21, 6% for 2021/22 and 6% for 2022/23, excluding the increase in other benefits that are applicable and the annual 2.5% notch increase where applicable. In Swartland, section 56 managers received no increase. Drakenstein's 2020/21 MTREF Budget Report discloses that the same applied to their section 56 managers and stated the municipality's intention toan apply to the South African Local Government Bargaining Council for a waiver relating to matters of remuneration.

As noted in Kannaland's 2020/21 MTREF Budget Document, the municipality's ability to effect personnel savings was contingent on adoption of a new organisational structure. A recent High Court judgment (Western Cape Provincial Executive, the Administrator of Kannaland and others vs Kannaland Municipality and Others) handed down on 19 March 2021 highlighted the lack of political support for the new organisational structure, with court granting the Western Cape Provincial Government an interdict against Kannaland's intention to nearly double the political structure in the Office of the Speaker by adding 5 additional personnel.

The remuneration to total operating revenue ratio includes both employee personnel costs as well as remuneration of councillors. The National Treasury norm is 25% to 40%. The ratio exceeding the norm could indicate inefficiencies and overstaffing as well as rapid increases in conditions of services which are nationally bargained. In addition to the salary increases which were agreed upon in 2018 for the next three years at the South African Local Government Bargaining Council, annual notch increases and rapidly escalating costs of medical aid also need to be taken into account.

From the diagram below, it is clear that the large municipalities (Drakenstein, Stellenbosch and Swartland fall comfortably within the norm. Hessequa and Bergrivier are also within the norms but have signalled the intention to reduce the remuneration to operating revenue ratio over the MTREF. No new posts were approved in Hessequa in the 2020/21 MTREF Budget Report. Laingsburg also falls within the norm, but sees the ratio rising over the MTREF from 30% in 2016/17 to 35% in 2022/23. Swellendam and Kannaland project remuneration in excess of the norm in 2020/21 and 2021/22 suggesting pressures that may squeeze out other forms of service delivery spending, such as capital spending. Kannaland had already in its 2020/21 MTREF budget indicated that its cost of employment budget would be in excess of the National Treasury norm, as reflected in the graph below. Expansion of its political support structure under conditions of shrinking operational grants from national government over the MTREF is extremely troubling and the high court's award of an interdict on further employment is therefore understandable.

Figure 23: Remuneration to operating revenue ratio in sampled municipalities, 2016/17–2022/23



Most of the sampled LMs have budgeted for a 6 or 7% increase in bulk services over the MTEF period. Bergrivier and Laingsburg have budgeted slightly lower than that at 5%. This is largely outside the control of LMs, and the court case between ESKOM and the energy regulator, NERSA, had introduced an element of uncertainty regarding bulk electricity prices. National Treasury's advice to municipalities was to prepare scenarios for electricity bulk price increases in 2020/21 of between about 7 per cent and 15 per cent. At the time of finalising the budget for 2020/21, NERSA has indicated a 6.9% Eskom electricity tariff and a 6.23% average electricity tariffs for municipalities, which inhibits municipalities from passing on the full increase in ESKOM bulk charges to their service users.

Swartland's 2020/21 MTREF Budget Statement raises some concerning issues in relation to the NERSA consultation paper on 20 March 2020 with the guideline electricity tariff adjustments for municipalities, which were based on an Eskom tariff increase of 6.9% for electricity purchases and a nominal increase of 6.23% as well as Eskom based tariff structures and tariffs for municipal customers:

Swartland Municipality identified inconsistencies with respect to the calculation methodology adopted by NERSA and lodged compelling objections against the application of Eskom related tariffs for reselling. *The application of the Eskom related tariffs would have resulted in almost the complete elimination of the net surplus derived from electricity sales and would severely impact the* *financial viability of all municipalities*. NERSA subsequently conceded and reverted to the typical municipal tariff structures as applied in previous years. NERSA issued a guideline tariff determination on 30 April 2020 based on a 6.23% nominal increase, albeit the tariff determination was still designated as a draft version. On 15 May 2020 NERSA issued the final tariff benchmark determination at a nominal increase of 6.22% for 2020/21" (p27, own emphasis).

This resonated with the perception shared by senior management respondents at other sampled municipalities that NERSA did not fully understand the ramifications of their decisions on municipalities' financial viability. Because NERSA decisions have prevented the municipalities from passing on all Eskom bulk tariff increases from Eskom onto end users, gross profit margins for electricity have been declining, and existing surpluses eroded, which undermines municipalities' ability to fund new infrastructure as well as upgrades and rehabilitation, or to cross-subsidise other services. Swellendam, in its 2020/21 MTREF Budget Report, indicated that its revenue base is heavily dependent on electricity sales and any external decision on revenues immediately impacts the whole budget: "This electricity sensitivity is not healthy for the municipality and could have a severe impact of this important revenue source is threatened by external factors and/or if it is withdrawn as a critical function from municipalities" (p11). Stellenbosch in its 2020/21 MTREF Budget Report has also reported the negative impact of a "declining electricity surplus, year-on year, putting more pressure on the level and quality of services provided" (p16).

Drakenstein and Stellenbosch have only budgeted 3% and 2% increases in contracted services spending (off fairly high baselines). Similarly Laingsburg has budgeted for only a 4% increase in contracted services. By contrast, Swartland (20%), Bergrivier (34%), Swellendam (20%) and Kannaland (33%) are significantly higher.

Bergrivier has budgeted the greatest increase in debt impairment over the MTREF horizon (17%). By contrast, Swellendam has projected debt impairment to remain stable (0% increase over the medium term), and Laingsburg and Hessequa have projected declining debt impairment over the MTEF period (-2% and -10% respectively). Deteriorating revenue collection and increases in debt impairment reduce electricity and water surpluses, already under pressure from bulk service increases.

Increases in finance charges over the MTEF period were generally modest, except in the case of Stellenbosch where it is expected to increase at an annual average growth rate of 29% over the MTEF period. In its 2020/21 MTREF Budget Report, Stellenbosch noted the upwaard pressure increased finance charges (interest payments on borrowing) would have on the affordability of future tariffs.

As noted earlier, capital expenditures and capital revenues in the sampled LMs municipalities, were much more disrupted by the pandemic in 2019/20 than operating budgets over the same period. Fairly large contractions in capital spending and revenues over the MTREF period in some municipalities raise operational sustainability concerns, especially in the smaller, more rural municipalities with significant backlogs. There were also significant realignments of the funding mix, with more risk averse borrowing strategies being pursued. At the same time, decreasin national transfers and depleted internal capital reserves results in large and worrisome declines in projected capital spending over the MTREF.

Table 23: 2020/21 MTREF operating expenditure for local municipalities

CATEGORY	CAPACITY	Municipality	R millions	Audited Outcome 16/17	Audited Outcome 17/18	Audited Outcome 18/19	Original Budget 19/20	Pre-audit Actual Outcome 19/20	Medium Term Revenue & Expenditure Framework 20/21	Medium Term Revenue & Expenditure Framework 21/22	Medium Term Revenue & Expenditure Framework 22/23	% YoY change 19/20	Actual vs budget variance 19/20	Avg annual growth 2016/17-2019/20	Avg annual growth over MTREF period 2020/21-2022/23
B1	High	Drakenstein	Employee related costs	462.5	564.9	669.0	678.5	638.9	688.2	741.1	803.0	-5%	-6%	11%	8%
			Bulk purchases	658.8	634.7	678.0	793.9	690.4	847.9	905.6	967.2	2%	-13%	2%	7%
			Contracted services	175.6	177.5	143.9	232.5	158.8	211.5	220.9	223.4	10%	-32%	-3%	3%
			Depreciation & asset impairment	175.3	214.5	211.6	215.9	106.9	240.4	244.7	248.1	-49%	-50%	-15%	2%
			Finance charges	94.0	132.4	158.4	162.8	108.4	182.3	180.7	176.8	-32%	-33%	5%	-2%
			Debt impairment	105.4	127.8	105.6	125.0	65.4	157.1	169.9	176.9	-38%	-48%	-15%	6%
			Other expenditure	151.1	183.3	233.6	191.0	169.7	187.9	190.9	192.3	-27%	-11%	4%	1%
			Total operating expenditure	**1 822.6**	**2 035.2**	**2 200.1**	**2 399.6**	**1 938.5**	**2 515.2**	**2 653.7**	**2 787.7**	**-12%**	**-19%**	**2%**	**5%**
B1	High	Stellenbosch	Employee related costs	407.8	444.6	461.1	603.3	505.7	579.4	623.5	676.7	10%	-16%	7%	8%
			Bulk purchases	347.8	329.7	380.7	406.5	400.0	482.2	516.2	552.5	5%	-2%	5%	7%
			Contracted services	149.2	123.0	151.8	238.0	159.5	245.5	244.7	255.8	5%	-33%	2%	2%
			Depreciation & asset impairment	149.6	157.5	176.7	207.0	96.3	205.6	214.9	224.6	-45%	-53%	-14%	4%
			Finance charges	19.6	18.8	23.2	39.9	31.1	39.3	52.7	65.2	34%	-22%	17%	29%
			Debt impairment	82.2	48.0	105.2	72.1	28.4	74.0	76.0	78.1	-73%	-61%	-30%	3%
			Other expenditure	160.2	224.8	188.9	241.7	145.8	261.4	274.4	288.9	-23%	-40%	-3%	5%
			Total operating expenditure	**1 316.4**	**1 346.3**	**1 487.6**	**1 808.2**	**1 366.8**	**1 887.5**	**2 002.4**	**2 141.7**	**-8%**	**-24%**	**1%**	**7%**
B3	Medium	Swartland	Employee related costs	162.7	181.2	193.0	217.5	219.5	239.4	254.9	270.5	14%	1%	10%	6%
			Bulk purchases	176.0	178.6	194.3	227.7	229.1	251.0	268.3	286.8	18%	1%	9%	7%
			Contracted services	57.3	66.9	86.1	62.2	66.9	57.5	102.9	82.3	-22%	8%	5%	20%
			Depreciation & asset impairment	59.4	83.1	85.9	88.3	88.5	92.8	94.5	102.1	3%	0%	14%	5%
			Finance charges	16.8	15.5	14.5	18.6	14.5	11.9	11.1	10.2	0%	-22%	-5%	-8%
			Debt impairment	20.3	28.3	40.6	35.3	48.2	43.9	39.4	48.8	19%	37%	33%	5%
			Other expenditure	53.2	62.0	72.5	88.3	79.4	101.4	105.0	109.2	10%	-10%	14%	4%
			Total operating expenditure	**545.6**	**615.5**	**686.9**	**737.9**	**746.1**	**797.9**	**876.1**	**909.9**	**9%**	**1%**	**11%**	**7%**
	Medium	Hessequa	Employee related costs	127.8	150.5	149.1	186.2	184.7	194.3	204.1	216.2	24%	-1%	13%	5%
			Bulk purchases	87.9	89.4	97.2	108.9	108.9	120.4	127.6	135.2	12%	0%	7%	6%
			Contracted services	38.7	32.2	26.3	32.7	41.7	48.1	84.7	84.9	59%	28%	3%	33%
			Depreciation & asset impairment	25.6	30.0	27.8	34.7	34.7	39.0	41.0	42.9	25%	0%	11%	5%
			Finance charges	17.7	18.8	16.9	21.5	21.5	21.4	23.9	26.7	27%	0%	7%	12%
			Debt impairment	47.5	34.3	57.8	41.6	51.6	71.6	57.0	58.0	-11%	24%	3%	-10%
			Other expenditure	45.9	50.1	55.5	71.7	72.6	78.0	83.8	88.5	31%	1%	17%	7%
			Total operating expenditure	**391.0**	**405.4**	**430.6**	**497.4**	**515.9**	**572.7**	**622.1**	**652.3**	**20%**	**4%**	**10%**	**7%**
	Medium	Bergrivier	Employee related costs	102.2	105.7	117.3	134.0	119.1	134.0	138.1	144.7	2%	-11%	5%	4%
			Bulk purchases	78.8	77.8	83.7	96.5	98.3	102.2	107.1	112.2	18%	2%	8%	5%
			Contracted services	-	16.1	16.3	27.0	15.5	22.7	38.4	40.9	-5%	-43%	-	34%
			Depreciation & asset impairment	19.6	20.6	20.2	23.3	15.1	23.6	24.8	25.9	-25%	-35%	-8%	5%
			Finance charges	12.7	12.8	15.3	14.0	8.4	16.7	18.1	17.6	-45%	-40%	-13%	3%
			Debt impairment	12.3	12.2	16.1	21.5	5.4	26.9	41.7	36.5	-67%	-75%	-24%	17%
			Other expenditure	51.0	40.2	46.4	60.2	47.3	52.5	54.2	58.5	2%	-21%	-2%	6%
			Total operating expenditure	**276.6**	**285.5**	**315.3**	**376.5**	**309.2**	**378.6**	**422.4**	**436.3**	**-2%**	**-18%**	**4%**	**7%**
	Low	Swellendam	Employee related costs	76.3	80.9	85.6	108.3	97.6	115.6	121.1	129.3	14%	-10%	9%	6%
			Bulk purchases	50.4	51.6	55.7	67.3	64.6	72.7	77.6	83.7	16%	-4%	9%	7%
			Contracted services	18.8	13.7	13.2	24.1	16.5	35.8	30.5	51.1	25%	-32%	-4%	20%
			Depreciation & asset impairment	9.4	7.5	9.8	9.3	9.9	11.4	11.6	12.0	1%	6%	2%	2%
			Finance charges	6.2	6.6	6.9	6.5	4.6	6.1	5.9	5.8	-34%	-30%	-10%	-3%
			Debt impairment	22.6	34.8	35.3	34.2	31.9	36.9	36.9	36.9	-10%	-7%	12%	0%
			Other expenditure	29.6	43.2	40.3	49.2	36.2	44.3	48.0	51.0	-10%	-26%	7%	7%
			Total operating expenditure	**213.3**	**238.3**	**246.8**	**299.1**	**261.2**	**322.9**	**331.6**	**369.8**	**6%**	**-13%**	**7%**	**7%**
	Medium	Kannaland	Employee related costs		35.2	55.5	59.4	61.4	58.3	61.8	65.5	11%	3%	32%	6%
			Bulk purchases		40.9	35.5	40.2	40.2	42.7	45.3	48.2	13%	0%	-1%	6%
			Contracted services		16.6	7.8	15.5	22.8	15.7	19.2	27.6	190%	47%	17%	33%
			Depreciation & asset impairment		0.7	26.7	11.2	9.3	12.2	12.8	13.5	-65%	-17%	264%	5%
			Finance charges		3.5	2.9	0.7	0.7	0.2	0.2	0.2	-77%	-7%	-56%	1%
			Debt impairment		20.2	25.9	14.1	11.6	11.9	12.8	13.7	-55%	-18%	-24%	7%
			Other expenditure		16.8	14.7	21.8	19.3	22.1	23.6	25.0	31%	-12%	7%	6%
			Total operating expenditure		**133.8**	**169.1**	**163.0**	**165.3**	**163.2**	**175.8**	**193.7**	**-2%**	**1%**	**11%**	**9%**
	Medium	Laingsburg	Employee related costs	19.0	20.6	23.2	26.9	24.0	29.0	29.4	31.6	3%	-11%	8%	4%
			Bulk purchases	7.5	7.3	7.4	7.9	7.6	9.1	9.6	10.0	2%	-4%	1%	5%
			Contracted services	-	4.7	7.5	6.3	2.8	7.1	7.4	7.8	-62%	-55%	-	4%
			Depreciation & asset impairment	7.9	7.1	8.3	9.7	13.0	5.7	5.6	5.5	56%	33%	18%	-2%
			Finance charges	0.2	0.5	0.0	0.01	0.01	0.8	0.8	0.8	-37%	24%	-66%	3%
			Debt impairment	21.3	21.9	25.2	26.4	34.3	27.3	26.5	26.3	36%	30%	17%	-2%
			Other expenditure	24.7	12.1	16.2	16.8	18.1	19.8	20.7	21.7	12%	8%	-10%	5%
			Total operating expenditure	**80.6**	**74.1**	**87.9**	**94.1**	**99.8**	**98.9**	**100.0**	**103.7**	**14%**	**6%**	**7%**	**2%**

Note: There are no data for Kannaland for 2016/17 and 2018/19, which is current under administration in a section 139(5) intervention. Kannaland's annual average growth rates are calculated from 2017/8-2019/20 due to unavailable data for 2016/17

Source: National Treasury website MTREF database, own calculation

In 2019/20, the impact of the pandemic was manifested in six LMs significantly underspending relative to their original capital budgets (Swartland -16%, Drakenstein -18% Stellenbosch -37%, Laingsburg -43%, Hessequa -50% and Kannaland -61%). By contrast Swellendam exceeded their capital budget by 175%, but this was as a result of a financial and administration project, not services infrastructure. With capital expenditure only -4% under budget and 18% higher than the previous year, Bergrivier did well under the circumstances. The municipality was able to reprioritise its capital projects: while water management and waste water management and housing significantly underperformed relative to budgeted capital expenditure, road transport, waste management, governance and administration, public safety and other community services exceeded the original budget. These changes would have been effected via an adjustment budget. The timing of capital rollout plans is important (whether infrastructure delivery included the last quarter 2019-20 which was disrupted by the lockdown, or scheduled earlier in the year). Capital projects are generally completed towards the final quarter of the financial year.

TABLE 24: 2020/21 MTREF CAPITAL EXPENDITURE FOR LOCAL MUNICIPALITIES

R millions	Audited Outcomes			Original Budget	Pre-audit Actual Outcome	MTREF projections			% YoY change	Actual vs budget variance	Avg annual growth over MTREF period	
	16/17	17/18	18/19	19/20		20/21	21/22	22/23	19/20		2016/17-2019/20	2020/21-2022/23
Stellenbosch	410.2	72.6	482.0	558.3	353.4	375.8	436.3	458.1	-27%	-37%	-5%	10%
Drakenstein	544.0	653.0	572.5	378.0	308.4	308.4	256.6	217.0	-46%	-18%	-17%	-16%
Swartland	109.0	100.4	88.2	143.9	121.3	212.4	137.6	137.7	38%	-16%	4%	-19%
Hessequa	123.1	62.3	68.1	110.4	55.6	105.1	69.6	63.5	-18%	-50%	-23%	-22%
Bergrivier	28.8	31.4	41.6	51.2	49.1	43.3	40.3	45.7	18%	-4%	19%	3%
Swellendam	14.9	20.9	17.0	20.6	56.5	22.1	19.2	17.9	232%	175%	56%	-10%
Kannaland	24.6	22.2	18.8	52.6	20.8	63.3	36.9	33.5	11%	-61%	-5%	-27%
Laingsburg	8.0	16.6	27.8	12.2	7.0	10.0	8.4	8.5	-75%	-43%	-4%	-8%

Municipalities such as Swartland and Drakenstein have long term financial plans and capital expentiture framework in which they locate their borrowing strategies.

From an operational sustainability perspective it is of some concern that 5 municipalities are shrinking their capital budgets over the MTREF period: Swellendam (an annual average decline of -10%), Drakenstein (-16%), Swartland (-19%), Hessequa (-22%) and Kannaland (-27%). Once the decline in purchasing power due to inflation is taken into account, these cuts translate into greater real drops, which is worrisome in the light of service backlogs and ageing infrastructure in some of these municipalities.

In Bergrivier and Stellenbosch, by contrast, capital budgets are set to increase over the MTREF period by 3% (which is less than the CPI inflation rate over the period and is still therefore a decreases in real terms) and 10% respectively.

After considering the uncertainty induced by the pandemic and the costs of borrowing sampled municipalities decided not to borrow externally but rely on internal funding. Internal funding has implications for the operational budget (e.g. tariff setting) and – given the cashflow challenges – resulted in much smaller capital programmes. There is substantial variation in capital mix. The larger and some medium sized municipalities are able to access capital markets, whereas smaller municipalities such as Swellendam, Kannaland and Laingsburg did not borrow in 2019/21. For instance, 15% of Bergrivier's capital revenues are derived from borrowing in 2019/20, 21% of Stellenbosch's, 31% of Drakenstein's and 54% of Hessequa's. In Bergrivier, Stellenbosch, Drakenstein and Hessequa internal funds also comprise a significant proportion of capital revenue in 2019/20: 35%, 45%, 14% and 11.7% respectively. Hessequa and Stellenbosch were the least dependent on conditional grants, with national and provincial capital transfers comprising 25% and 34% of capital revenues in 2019/20. In Drakenstein, Swartland and Bergrivier, intergovernmental capital transfers constitutes just over half of capital revenues in 2019/20. Swellendam is highly dependent on national and provincial grants, with capital transfers amount to 80% of capital revenues in 2019/20, with internal funds comprising the remainder. Finally Kannaland and Laingsburg, the smallest municipalities, are totally dependent on national and provincial capital grants.

Table 25 reveals that 5 of the 7 sampled LMs generated less capital revenue than budgeted in 2019/20: Swartland (-16%), Laingsburg (-18%), Drakenstein, (-32%) and Stellenbosch (-37%), Laingsburg (-43%) and Hessequa (-50%). Swartland did not borrow as anticipated in its 2019/20 budget and also received lower provincial transfers than anticipated, but was able to redirect 9% more internal funds than budgeted for initially, and whole capital revenues fell -16% below budget, it was still a 40% increase from the prior year.. Both Drakenstein and Stellenbosch also substantially reduced their borrowings in 2019/20 (-47% and -64% less than originally budgeted), Drakenstein was able to draw on more of its internal reserves (R36.8 million vis-à-vis R8.9 million originally budgeted for). Stellenbosch, however, applied less internal reserves than budgeted for, with a -52% deviation from the budget. Capital revenues were -24% less than the prior year in Stellenbosch, -55% less in Drakenstein.

Hessequa not only had to scale back on borrowing in 2019/20 (-55% less than budget) and reduced internal funding (-58%), but also experienced -16% shortfall in national capital transfers due to fiscal consolidation within the national sphere. This reduction in capital transfers in 2019/20 was smaller than those experienced Drakenstein (-1% less than the original budget), Bergrivier (-2% less than budgeted), Stellenbosh (-5% less than budgeted). Hessequa's capital revenue in 2019/20 was -18% less than the previous year, and -75% for Laingsburg. The reason for the unusual in-year cuts in municipal capital grants in 2019/20 was to reprioritisation to fund urgent pandemic response. In the 2020/21 financial year, Hessequa included a provision for R9.517 million finance charges for landfill sites.

Laingsburg is wholly dependent on capital grants and received 20% less in national capital transfers, and provincial capital transfers which were budgeted for at the 2019/20 financial year did not materialise. While Kannaland received 35% greater capital transfers from provincial government than budgeted for, its national capital grants were decreased by -70% and the municipality also had to reduce the application of internal funds by-75%. This was however an increase of 21% over the prior year.

Bergrivier only experienced a capital revenue shortfall of -4% in relation to the budgeted amount in 2019/20. Bergrivier borrowed 9% more than originally budgeted at beginning of the year, and receieved 19% higher provincial capital transfers, but also reduced the amount of internal funds which amounted to -17% less than budgeted for. Despite ths, capital revenues had increased in Bergrivier by 18% from the previous year.

Swellendam exceeded its budgeted capital revenue in 2019/20 by 28%. Swellendam received provincial capital transfers in 2019/20 which were twice the quantum originally budgeted for.

Of deep concern is that 6 of the 8 sampled LM's envisage capital revenues declining over the medium term at annual average rates of -8% in Laingsburg, -10% in Swellendam, -28% in Drakenstein, -19% in Swartland, -22% in Hessequa and -27% in Kannaland. This will seriously impact operationally on the ability of these municipalities to renew their infrastructural assets, deliver services efficiently without undue technical water and electricity losses, and eliminate service backlogs. After taking inflation into acount over the MTREF, the real decline in purchasing power would be even larger.

By contrast, the capital revenues of Bergrivier and Stellenbosch are expected to grow by 3% and 10% respectively. Stellenbosch's anticipated capital revenue performance is predicated on increased borrowing and internal funds over the MTREF period as its GDP-R rebounds, and national capital transfers decline at an average annual rate of -15%.

Table 25 also illustrates a more conservative capital funding mix for most of the sampled municipalities. Drakenstein and Swartland intend to refrain from borrowing at all. Hessequa envisages reduction in its yearly borrowing, from R63.4 million in 2020/21, to R45.3 million in 2021/22 aand R41.3 million in 2022/23. Bergrivier intends keeping borrowing more or less constant at about R15.2 million over the MTREF period. Only Stellenbosch intends to increase borrowings at an average annual growth rate of 28% over the MTREF, albeit at a slower pace than the average annual growth of 31% which had prevailed between 2016/17 and 2019/20.

Fiscal consolidation at national level has resulted in capital transfers shrinking over the MTREF, and – depending on the duration of the pandemic – may decline further. Swartland Hessequa and Kannaland have projected a -6%, -13%, and -25% annual average decline in national capital transfers over the MTREF respectively. Laingsburg expects no increases in national capital transfers over the MTREF, which translate into a real decline in purchasing power, given the inflation rate. Swellendam and Bergrivier are the only sampled LMs expecting increases in national capital transfers, of 7% and 10% respectively.

Similar to Stellenbosch, capital transfers in Drakenstein decline at an annual average rate of 15% over the MTREF. In Drakenstein's 2020/21 MTREF Budget Report, the municipality claimed that the amount of capital grants received from national government was "far less than what other secondary cities with similar demographics are receiving" and that it was not receiving its "fair share" from the national fiscus (p 17)

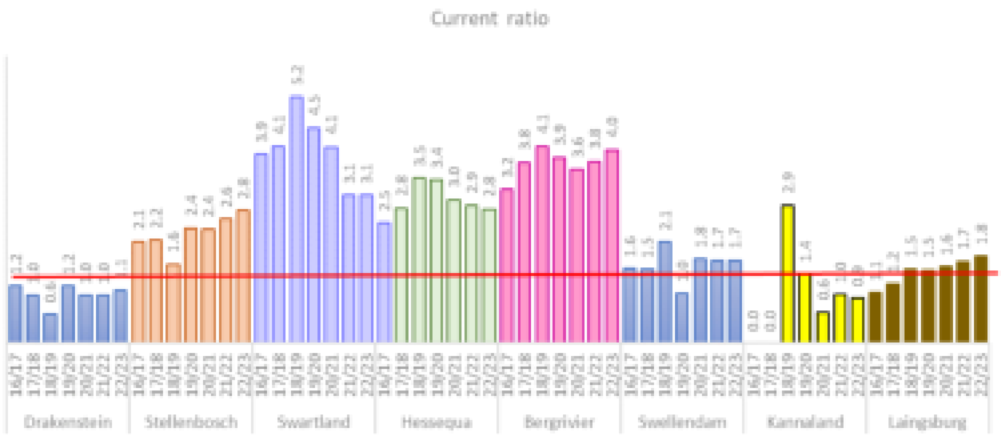
TABLE 25: 2020/21 MTREF CAPITAL REVENUE FOR LOCAL MUNICIPALITIES

CATEGORY	CAPACITY	Municipality	R miilions / Revenue source	Audited Outcome 16/17	Audited Outcome 17/18	Audited Outcome 18/19	Original Budget 19/20	Pre-audit Actual 19/20	MTREF projections 20/21	MTREF projections 21/22	MTREF projections 22/23	% YoY change 19/20	Actual vs budget variance 19/20	Avg annual growth over MTREF period 2016/17-2019/20	Avg annual growth over MTREF period 2020/21-2022/23
B1	H	Stellenbosch	Transfers: National	41.4	40.2	40.8	62.5	59.7	63.7	43.7	46.1	46%	-5%	13%	-15%
			Transfers: Provincial	1.3	(3.7)	42.4	26.1	59.5	49.7	45.6	54.6	40%	128%	259%	5%
			Transfers: Other	0.5	0.2	-	-	-	31.9	13.0	1.7			-100%	-77%
			Borrowing	33.4	(98.7)	120.6	140.0	74.5	102.8	103.8	169.0	-38%	-47%	31%	28%
			Internal funds	333.7	150.6	262.6	329.7	159.7	127.6	230.2	186.7	-39%	-52%	-22%	21%
			Total capital revenue	**410.2**	**88.8**	**466.4**	**558.3**	**353.4**	**375.8**	**436.3**	**458.1**	**-24%**	**-37%**	**-5%**	**10%**
B1	H	Drakenstein	Transfers: National	42.4	50.7	35.0	88.4	87.6	86.1	63.5	61.8	151%	-1%	27%	-15%
			Transfers: Provincial	23.1	71.0	91.9	55.5	51.3	64.9	1.5	0.9	-44%	-8%	30%	-88%
			Transfers: Other	-	-	9.4	2.6	1.3	2.6	-	-	-86%	-51%		-100%
			Borrowing	452.9	476.2	357.1	222.6	79.6	-	-	-	-78%	-64%	-44%	
			Internal funds	25.6	-	79.1	8.9	36.8	63.3	50.0	50.0	-53%	314%	13%	-11%
			Total capital revenue	**544.0**	**597.9**	**572.5**	**378.0**	**256.6**	**217.0**	**115.0**	**112.7**	**-55%**	**-32%**	**-22%**	**-28%**
B3	M	Swartland	Transfers: National	24.0	27.6	32.0	30.3	30.3	32.8	27.7	28.8	-5%	0%	8%	-6%
			Transfers: Provincial	8.8	29.0	13.9	36.9	29.9	52.9	0.1	36.8	116%	-19%	51%	-17%
			Transfers: Other	33.0	-	0.3	-	1.9	-	-	-	647%		-62%	
			Borrowing	-	-	-	22.6	-	-	-	-		-100%		
			Internal funds	43.2	43.8	40.6	54.1	58.8	126.7	109.9	72.1	45%	9%	11%	-25%
			Total capital revenue	**109.0**	**100.4**	**86.7**	**143.9**	**120.9**	**212.4**	**137.6**	**137.7**	**40%**	**-16%**	**4%**	**-19%**
B3	M	Hessequa	Transfers: National	87.6	23.8	14.3	15.0	12.6	18.9	16.7	14.2	-12%	-16%	-48%	-13%
			Transfers: Provincial	1.2	2.3	8.0	1.3	1.6	-	0.1	0.1	-80%	22%	8%	
			Transfers: Other	0.1	0.2	4.8	-	0.02	3.3	-	-	-100%		-34%	-100%
			Borrowing	29.5	27.4	34.6	66.4	29.8	63.5	45.3	41.3	-14%	-55%	0%	-19%
			Internal funds	4.7	-	6.5	27.8	11.7	19.4	7.5	7.9	80%	-58%	35%	-36%
			Total capital revenue	**123.1**	**53.8**	**68.1**	**110.4**	**55.6**	**105.1**	**69.6**	**63.5**	**-18%**	**-50%**	**-23%**	**-22%**
B3	M	Bergrivier	Transfers: National	10.3	13.4	20.0	17.9	17.5	14.6	14.4	17.6	-13%	-2%	19%	10%
			Transfers: Provincial	0.8	1.5	1.6	6.2	7.3	1.2	0.4	0.8	357%	19%	106%	-18%
			Transfers: Other	0.2	1.9	-	-	0.1	-	-	-				
			Borrowing	6.6	4.5	6.4	6.6	7.2	15.2	15.1	15.1	12%	9%	3%	0%
			Internal funds	11.0	10.1	13.5	20.6	17.1	12.4	10.4	12.2	26%	-17%	16%	-1%
			Total capital revenue	**28.9**	**31.4**	**41.6**	**51.2**	**49.1**	**43.3**	**40.3**	**45.7**	**18%**	**-4%**	**19%**	**3%**
B3	L	Swellendam	Transfers: National	8.5	12.7	11.5	12.5	12.5	11.6	14.7	13.4	8%	0%	14%	7%
			Transfers: Provincial	1.0	4.4	-	2.8	8.5	4.6	-	-		208%	101%	-100%
			Internal funds	5.3	3.8	5.4	5.3	5.3	6.0	4.5	4.5	-2%	0%	0%	-13%
			Total capital revenue	**14.9**	**-**	**17.0**	**20.6**	**26.3**	**22.1**	**19.2**	**17.9**	**55%**	**28%**	**21%**	**-10%**
B3	M	Kannaland	Transfers: National	23.0	13.0	14.1	47.7	14.5	59.7	36.9	33.5	3%	-70%	-14%	-25%
			Transfers: Provincial	1.4	3.3	2.0	4.6	6.2	3.6	-	-	205%	35%	64%	-100%
			Transfers: Other	0.1	-	-	-	-	-	-	-			-100%	
			Internal funds	0.2	-	1.0	0.4	0.1	-	-	-	-90%	-75%	-18%	
			Total capital revenue	**24.6**	**16.3**	**17.1**	**52.6**	**20.8**	**63.3**	**36.9**	**33.5**	**21%**	**-61%**	**-5%**	**-27%**
B3	M	Laingsburg	Transfers: National	7.0	16.6	27.8	8.7	7.0	6.3	8.4	6.3	-75%	-20%	0%	0%
			Transfers: Provincial	1.0	-	-	3.5	-	3.7	-	2.2		-100%	-100%	-23%
			Total capital revenue	**8.0**	**16.6**	**27.8**	**12.2**	**7.0**	**10.0**	**8.4**	**8.5**	**-75%**	**-43%**	**-4%**	**-8%**

The current ratio is commonly used to assess a municipality's ability to pay back its short-term liabilities (debt and accounts payable) with its short-term assets (cash, inventory, and accounts receivable). The higher the current ratio, the better is a municipality positioned to pay its current or short-term obligations and provide for a risk cover to enable it to continue operations at desired levels. A financial ratio less than 1 suggests that the municipality would be unable to pay all its current or short-term obligations if they fall due at any specific point. The norm range is between 1.5 to 2. The lower bound of this range is illustrated by the red line in Figure 24 below.

While the cashflows of Stellenbosch, Swartland, Hessequa and Bergrivier appear satisfactory over the MTREF period, Swellendam and Laingsburg appear to be more cashflow constrained, just exceeding the 1.5 current ratio norm. Drakenstein and Kannaland fall below the norm, raising concerns that these municipalities may be unable to meet their short term financial obligations or would need to liquidate long term assets to do so.

FIGURE 24: CURRENT RATIO OF SAMPLED LOCAL MUNICIPALITIES, 2016/17–2022/23

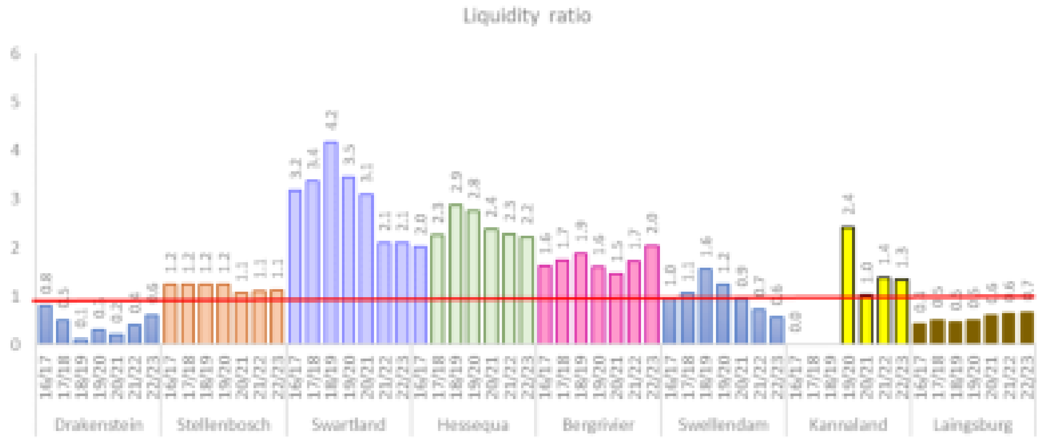


Source: MTREF budget submissions, National Treasury database

The liquidity ratio assesses the extent to which the municipality has cash or monetary assets to meet its current short-term liabilities. This ratio takes into account the composition of current assets - some assets such as accounts receivable over 90 days old, for instance, may be less easily recoverable and convertible into cash. Ideally the municipality should have the equivalent cash and cash equivalents on hand to meet at least the current liabilities, which should translate into a liquidity ratio of 1. Anything below 1 indicates a shortage in cash to meet creditor obligations. For Laingsburg and Drakenstein, the liquidity ratio analysis confirms their cash constraints over the medium term and the need for ongoing cost containment and revenue enhancement.

Laingsburg's 2021 MTREF Budget Report, approved by Council on 27 May 2020 during the first quarter of the pandemic reported that the "municipality's cash flow is currently in a very distressed state. Unspent grants keep the bank account in a favourable balance. If the funds were to be spent according to the programs, this would mean that the municipality would have to make use of overdraft facilities" (p 12).

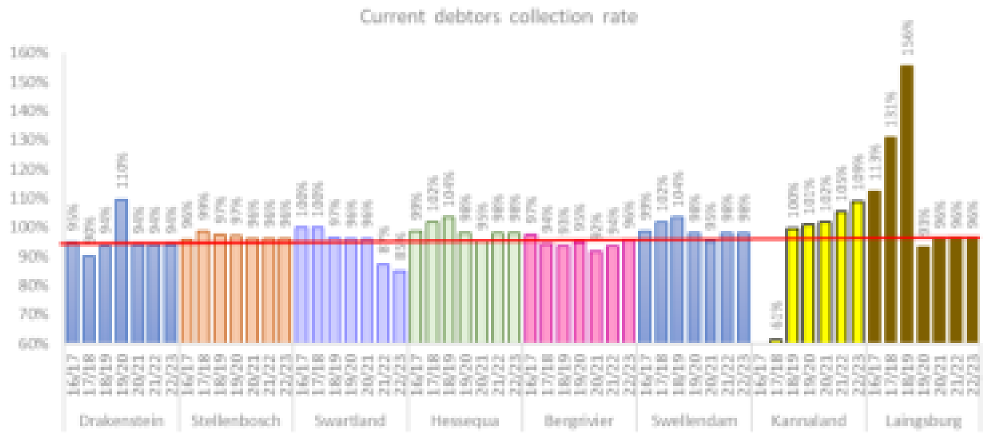
FIGURE 25: LIQUIDITY RATIO OF SAMPLED MUNICIPALITIES, 2016/17–22/23



Source: MTREF budget submissions, National Treasury database

The current debtors collection rate shows cash receipts from property rates and service charges as a percentage of total annual ratepayer and user charge revenues. The collection ratio provides an indication of the cumulative revenue management performance (the effectiveness of credit control i.e. ensuring that what is billed is collected; and effectiveness of revenue management - the ability to set affordable tariffs and bill correctly). The norm is 95%. If the ratio is below the norm this is an indication that revenue collection of the municipality requires urgent attention and corrective measures should be implemented. A municipality with outstanding debtors should aim at achieving a collection rate of more than 100%. The collection rate will impact on the cash position of the municipality and inform the level of cash and cash equivalents at year end, and hence liquidity and solvency.

FIGURE 26: CURRENT DEBTORS COLLECTION RATE FOR SAMPLED LOCAL MUNICIPALITIES 2016/17– 2022/23

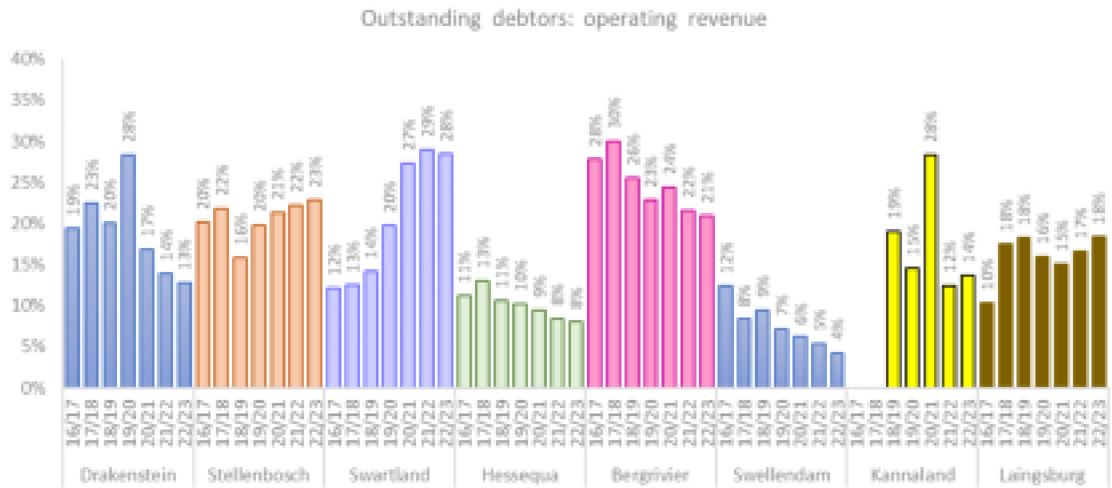


Source: MTREF budget submissions, National Treasury database

While the bigger LMs, Drakenstein and Stellenbosch anticipate that the revenue collection rate will remain relatively steady over the medium term, in Hessequa, Bergrivier, Swellendam and Laingsburg, the collection rate is expected to decline in 2021 due to the pandemic's impact on local economies, and then to recover in the 2 subsequent outer year of the MTREF. This pattern is most pronounced in Swartland, which has projected the collection rate plummeting from 96% in 2020/21 to 87% in 2021/22, and 85% in 2022/23. Kannaland is the only exception projecting collection rates of more than 100% over the MTREF period, but this is because of its exceptionally low revenue collection rates in prior years, and the prospects of recovering some of the outstanding consumer debt.

Unlike the current collection rate which focuses exclusively on consumer debt from rates and tariffs, this outstanding debt figure also includes other debtors (e.g. in respect of agency service fees) and the current portion of long term liabilities. As indicated in the diagram below, Stellenbosch, Swartland, and Laingsburg expect outstanding debt as a proportion of annual operating revenue to rise over the MTREF. Drakenstein, Hessequa, Bergrivier and Swellendam are projecting that total outstanding debt as a percentage of annual operating revenue will decline.

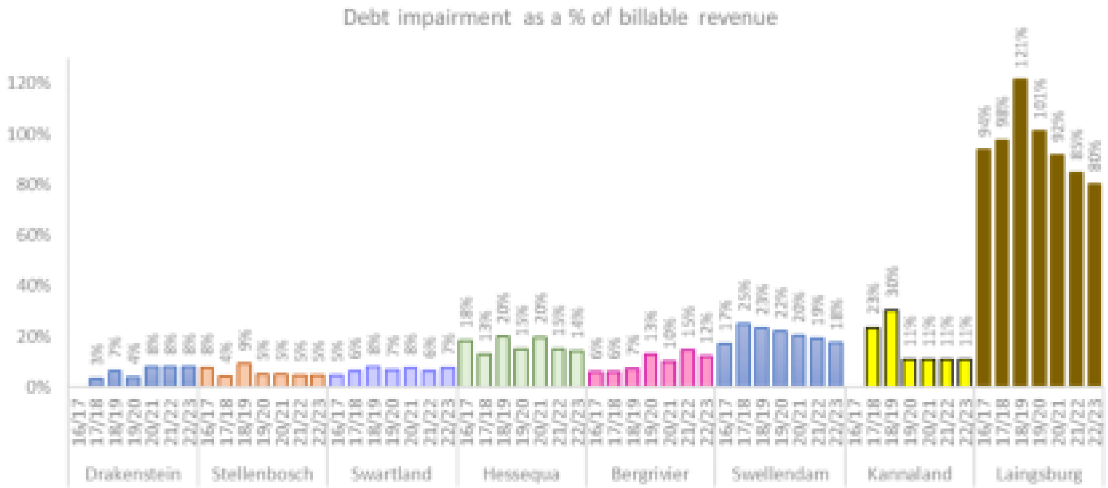
FIGURE 27: OUTSTANDING DEBTORS TO OPERATING REVENUE RATIO IN SAMPLED LOCAL MUNICIPALITIES, 2016/7–2022/23



Source: MTREF budget submissions, National Treasury database

As can be seen in the graph below, the larger municipalities (Drakenstein, Stellenbosch and Swartland) have maintained low levels of debt impairment before the pandemic (below 8% of billable revenue) and expect this trend to continue over the MTREF. Hessequa, Bergrivier, Swellendam and Kannaland are projecting higher levels of debt impairment, ranging between 10 and 20% of billable revenue. Laingsburg has projected the highest levels of debt impairment. Laingsburg has the largest provisions for doubtful debt, which amounted to 34% of operating expenditure in 2019/20.

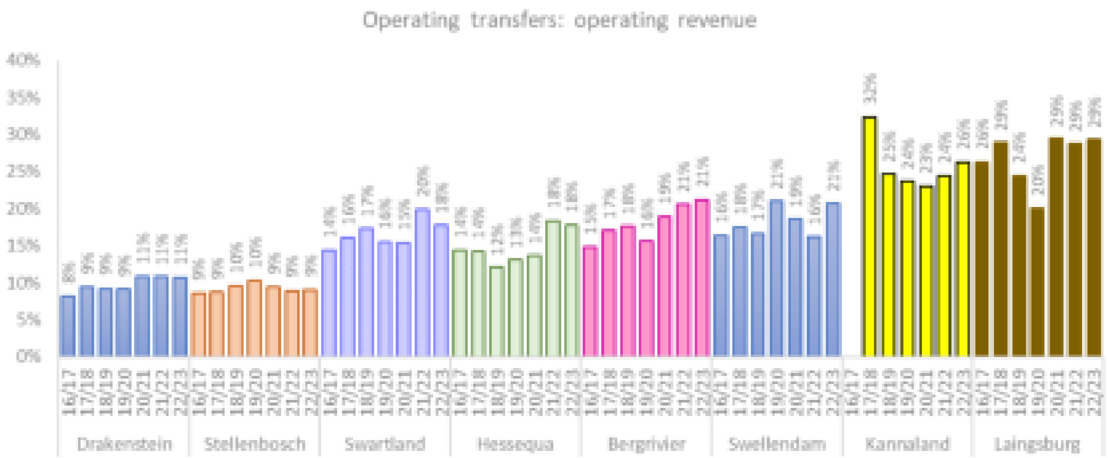
FIGURE 28: DEBT IMPAIRMENT AS A PERCENTAGE OF BILLABLE REVENUE, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

As can be seen in the diagram below, operating grants such as the local government equitable share only constitute a relatively small proportion of Drakenstein and Stellenbosch's operating revenues (less than 11%). Swartland, Hessequa, Bergrivier and Swellendam depend on grants for between 14% and 20% of their operating revenues and this is likely to increase slightly over the MTREF horizon. Kannaland and Laingsburg are heavily grant dependent for 25% to 30% of operating revenue and are likely to become more so over the MTREF.

FIGURE 29: OPERATING TRANSFERS TO OPERATING REVENUE IN SAMPLED LOCAL MUNICIPALITIES, 2016/17–2022/23



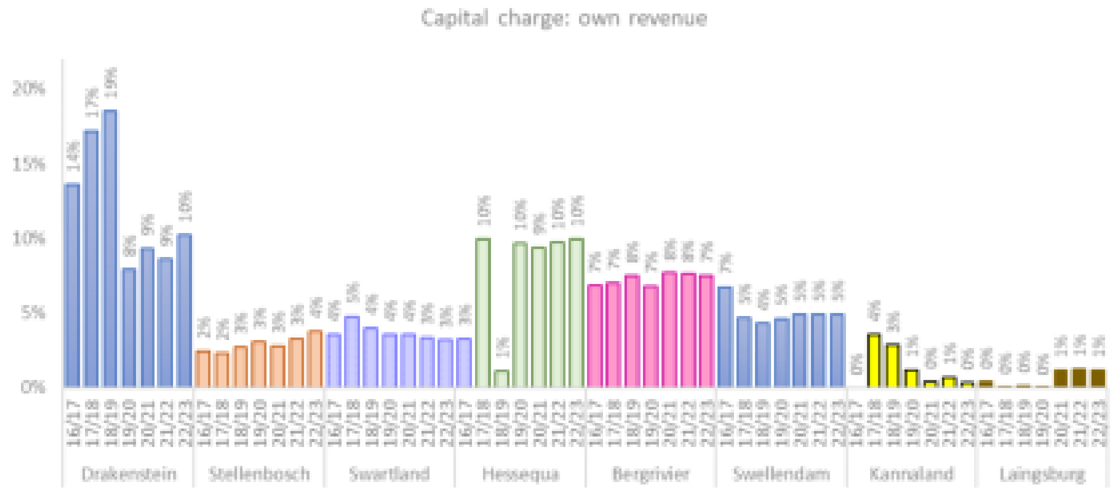
Source: MTREF budget submissions, National Treasury database

The capital charge to own revenue ratio is a measure of the municipality's ability to service and repay its debt through own revenues. In general, the higher this ratio, the greater the financial risk exposure of the municipality. Capital charges are measured by interest finance charges and debt repayment. Own revenue is captured by operating revenues before capital transfers less operating transfers and grants such as the Local Equitable Share.

From the diagram below, it is clear that municipalities' borrowing strategies over the medium term (2020/21 to 2022/23) is to keep their debt financing stable (Stellenbosch, Swellendam, Hessequa, Bergrivier) or decrease their borrowing (most notably Drakenstein, but also Swartland and Kannaland). This was mainly due to the uncertainty about interest rates during the pandemic, as the high cost of capital and the pressure on affordability of future tariffs in order the service the debt.

In the recent past, Drakenstein had invested in infrastructure in anticipation of local growth (and hence an increased revenue base) which unfortunately has not materialised (partly due to the pandemic). While past borrowing decisions impact heavily on Drakenstein's current cash flows, the infrastructure will position the municipality well after the pandemic when growth takes off. According to Drakenstein's Budget Report 2021, its external loans of the Development Bank of Southern Africa, Standard Bank and Nedbank had to undergo a restructuring process and no further external loans will be taken up over the next five financial years. Bergrivier's 2021 MTREF budget report also signals the intention to rely more on internal funds such as Capital Reserve Funds and grant funding, rather than borrowing in order to mitigate financial risk. Kannaland's 2020/21 MTREF Budget Report indicates that the municipality has not been able to establish a Capital Reserve Fund.

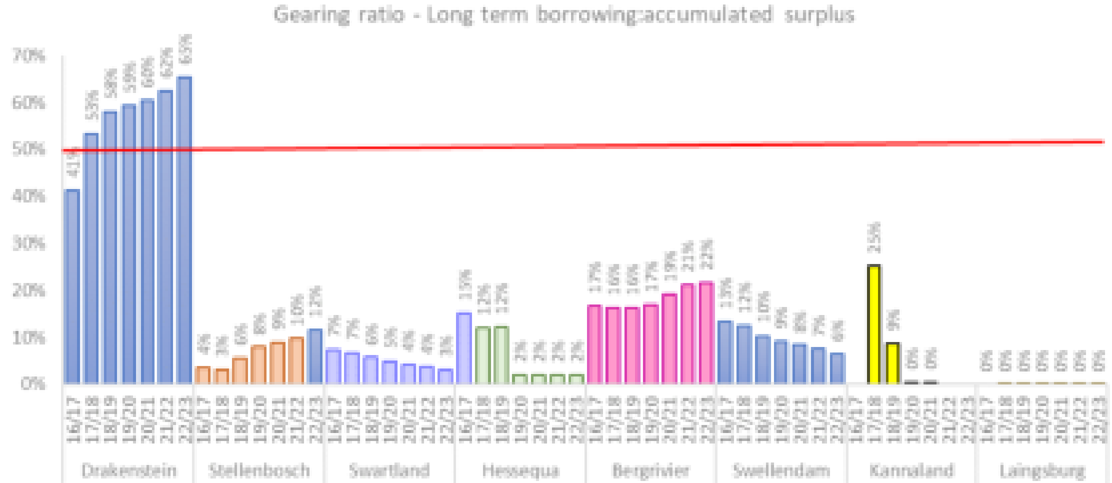
Figure 30: Capital charges to own revenue in sampled local municipalities, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

Another way to view the borrowing strategy of municipalities is through their gearing ratio which reflects the municipality's ability to repay its long term borrowing from its accumulated surpluses and other reserves. The lower the ratio, the greater the municipality's ability to repay is debt. Drakenstein's ratio greatly exceeds the 50% maximum norm prescribed by National Treasury. Drakenstein's 2020/21 MTREF budget envisages no further external borrowing in order to improve that ratio.

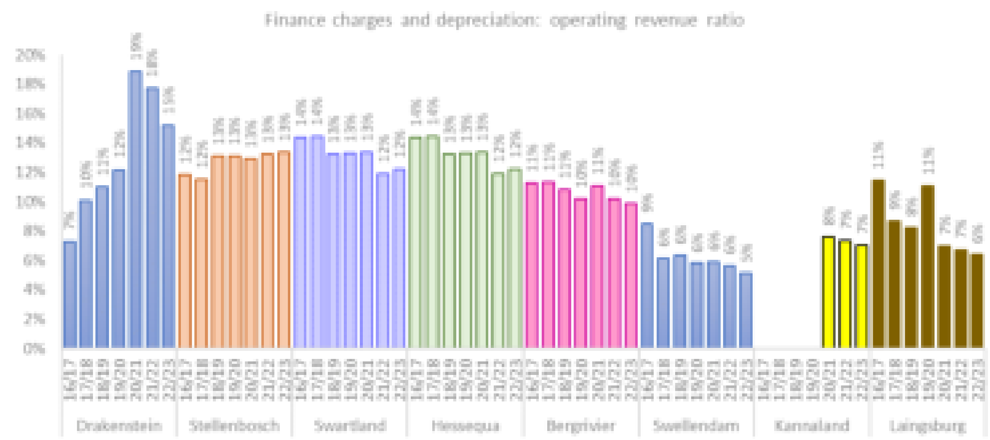
FIGURE 31: GEARING RATIO: LONG TERM BORROWING TO ACCUMULATED SURPLUS IN SAMPLED LOCAL MUNICIPALITIES



Source: MTREF budget submissions, National Treasury database

As can be seen in the graph below, all sampled local municipalities indicated decreasing finance charges and depreciation over the MTREF period. The decreased interest charges are due primarily to the more conservative borrowing strategies discussed earlier. Depreciation is widely considered a proxy for the measurement of the rate at which assets are consumed Depreciation charges are largely determined by the municipality's asset management plan, and therefore could not be significantly impacted by the pandemic

FIGURE 32: FINANCE CHARGES AND DEPRECIATION TO OPERATING REVENUE IN SAMPLED LOCAL MUNICIPALITIES, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

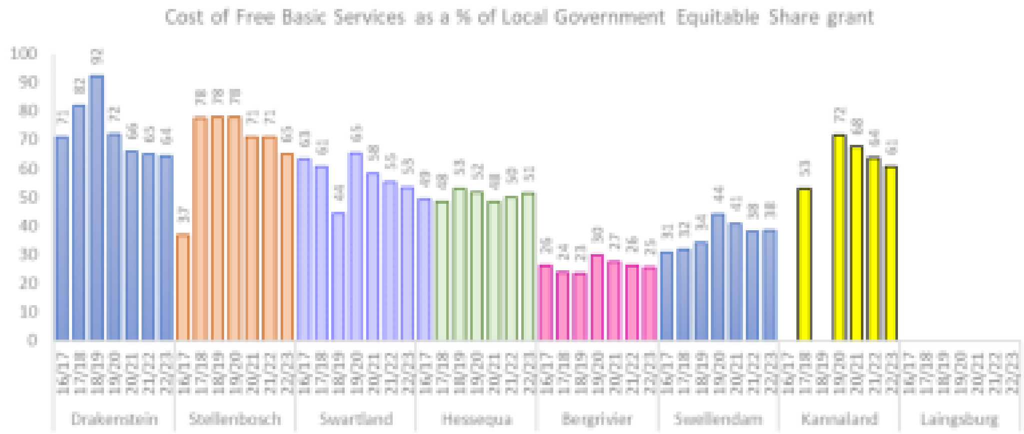
The pandemic is likely to increase the number of indigent households applying for free basic services. Bergrivier's 2020/21 MTREF Budget Report estimates that about 2300 households would receive the indigent subsidy in the 2020/2021 financial year, an increase of approximately 27% from the number initially budgeted. It is therefore important to consider the extent to which the local government equitable share covers the costs of free basic services.

Municipalities are obliged to render a minimum basket of service to indigent households (6kl of water per household per month, 50kwh per household per month of electricity, a minimum level of sanitation and refuse removed at least once a week). This cost of free basic service excludes other community services which municipalities provide to indigent households.

If municipalities provide services in excess of the minimum basket (e.g. 100kwh of electricity or more water), then this is regarded as revenue forgone by the municipality (i.e. the municipality could have charged for it, but didn't). Some municipalities also offer more generous exemptions, reduction and rebates on property rates which would also constitute revenue forgone. The same would apply to housing rental rebates and top structure subsidies. Bergrivier used to have a generous threshold for the provision of subsidies to indigent households (twice the old age pension plus 40%). However, in its 2020/21 MTREF Budget Report, the municipality observed that this level of subsidy had regrettably become unaffordable in the long term and that the threshold had been capped at a combined household income of R5000 per month, which is still nearly 40% more than the threshold determined by the National Treasury.

The diagram below suggests that while the cost of Free Basic Services for all sampled municipalities are currently being covered by the unconditional Local Government Equitable Share Grant (LGES) in terms of section 214 of the Constitution, Kannaland, Stellenbosh and Drakenstein intend devoting more than 60% of the LGES to covering the costs of FBS.

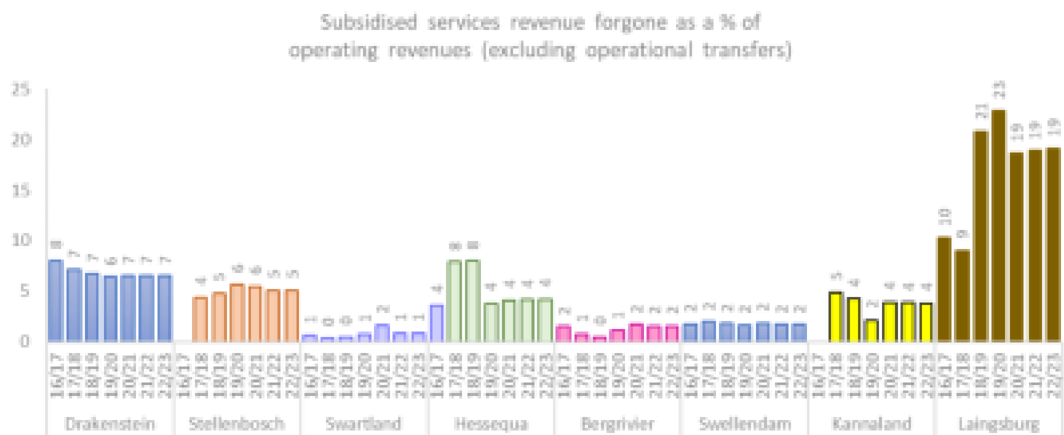
FIGURE 33: COST OF FREE BASIC SERVICES AS A PERCENTAGE OF THE LOCAL GOVERNMENT EQUITABLE SHARE GRANT IN SAMPLED LOCAL MUNICIPALITIES, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

To get a sense of whether the revenue forgone on providing subsidised services is sustainable, this amount can be expressed a proportion of own revenues (i.e. total operating revenues less operational transfers like the LGES). As can be seen in the diagram below, revenue forgone does not constitute a prohibitive proportion of own revenues, except perhaps in Laingsburg. Laingsburg however receives quite a large LGES and can easily cover subsidies services revenue expenditure.

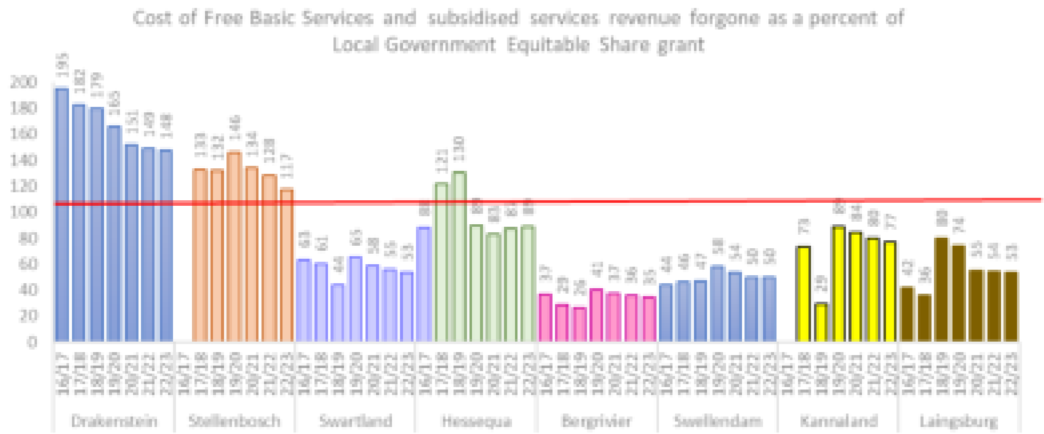
FIGURE 34: SUBSIDISED SERVICES REVENUE FORGONE AS A PERCENTAGE OF OPERATING REVENUE FORGONE (EXCLUDING OPERATIONAL TRANSFERS) FOR SAMPLED LOCAL MUNICIPALITIES, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

To get a rough indicator of the sum of FBS costs and subsidised revenue forgone as a proportion of the LGES. The diagram below suggests that all municipalities (including Laingsburg) cost of subsidised services (the "social package") is covered by the LGES, with the exceptions of Stellenbosch and Drakenstein, which are less grant dependent and can rely on own revenues.

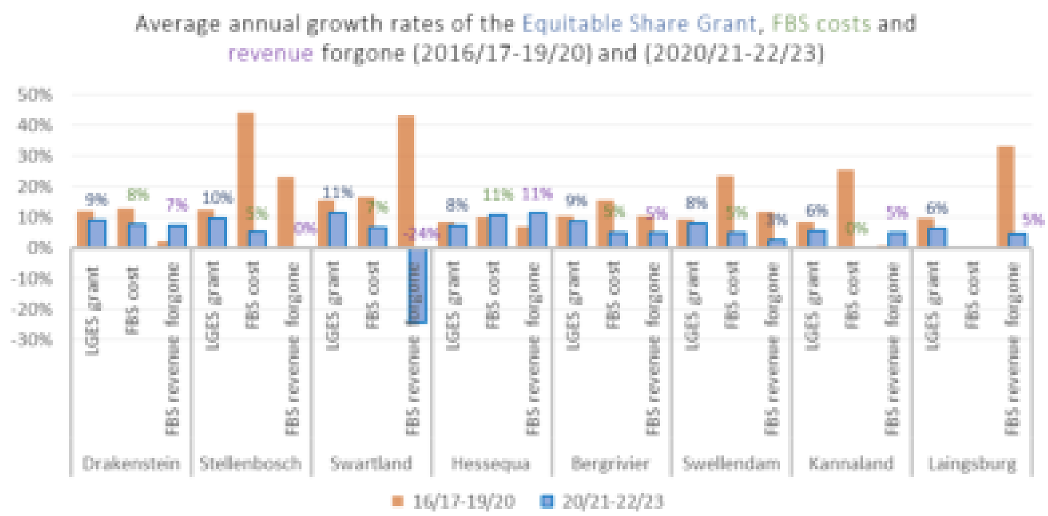
FIGURE 35: COST OF FREE BASIC AND SUBSIDISED SERVICES REVENUE FORGONE AS A PERCENTAGE OF THE LOCAL GOVERNMENT EQUITABLE SHARE, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

The chart below compares the growth rates of the LGES, FBS costs and subsidised services revenue forgone for the sampled municipalities for the periods 2016/17 to 2019/20 (orange bars) and over the MTREF period 2020/21-22/31 (blue bars). Over the MTREF period, most sampled LMs anticipate that average annual increases in their FBS costs and revenue forgone will be less than LGES growth over the MTREF (Drakenstein, Stellenbosch, Swartland, Bergrivier, Swellendam and Laingsburg. The one exception is Hessequa, which anticipates above CPI increases in FBS costs and in revenues forgone. However, as shown in the first graph above, Hessequa is only utilising a relatively small proportion of its LGES grant for this purpose and can most probably sustain it.

FIGURE 36: AVERAGE ANNUAL GROWTH RATES OF THE EQUITABLE SHARE GRANT, FREE BASIC SERVICES COSTS AND REVENUE FORGONE IN SAMPLED MUNICIPALITIES, 2016/17–2019/20 AND 2020/21–2022/23



Source: Own calculations based on MTREF budget submissions, National Treasury database

The table below, based on basic service delivery measures reported to the National Treasury in 2020/21 budget documentation shows numbers of households receiving free basic water and electricity.

TABLE 26: ACTUAL AND PROJECTED NUMBER OF INDIGENT HOUSEHOLDS IN SELECTED LOCAL MUNICIPALITIES (2016/17 – 2022/23)

		Actual			Estimate	MTREF projection			Avg annual growth rate	
		16/17	17/18	18/19	19/20	20/21	21/22	22/23	16/17-19/20	20/21-22/23
Drakenstein	Households with free water	18 373	18 000	18 000	18 500	19 000	19 500	19 500	0%	1%
	Households with free electricity	17 653	18 000	18 000	18 500	19 000	19 500	19 500	2%	1%
Stellenbosch	Households with free water		6 182	6 482	6 000	6 000	6 000	6 000	-1%	0%
	Households with free electricity		6 182	6 482	6 000	6 000	6 000	6 000	-1%	0%
Swartland	Households with free water	5 495	8 738	8 724	9 073	9 247	9 524	9 810	18%	3%
	Households with free electricity	5 266	7 752	7 759	8 468	8 745	9 007	9 277	17%	3%
Hessequa	Households with free water	4 961	3 547	5 385	5 111	5 162	5 575	6 021	1%	8%
	Households with free electricity	5 395	5 150	5 493	5 932	6 407	5 932	6 407	3%	0%
Swellendam	Households with free water	1 562	1 975		2 259	2 260	2 261	2 262	13%	0%
	Households with free electricity	1 562	1 594		2 259	2 260	2 261	2 262	13%	0%
City of Cape Town	Households with free water	222 098	231 793	267 325	270 025	253 851	253 851	253 851	7%	0%
	Households with free electricity	236 941	195 564	183 070	183 070	183 070	183 070	183 070	-8%	0%

Source: National Treasury database MTREF 2020/21 budget submissions, Table A-10 Basic Service Delivery Measurement. Own growth rate calculations

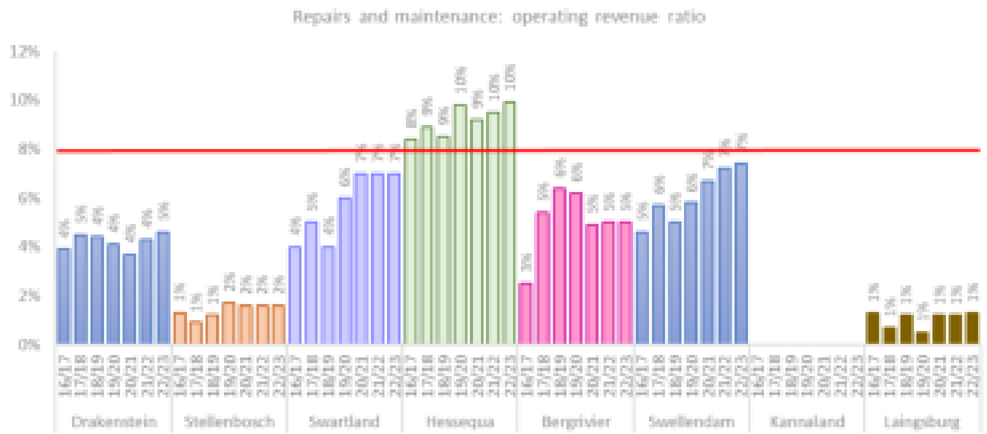
What is notable is that – except for Hessequa – most the other municipalities are projecting the number of indigent households to grow at modest annual average growth rates of 3% or less. It is not certain how credible these projections are given the slow post pandemic recovery projected for some of these municipalities, unless there are significant numbers of households receiving free services which can indeed afford to pay. Alternatively, it could mean that municipalities intend moving further away from broad based targeting of free basic services to both low income and indigent households (as envisaged in the 1998 White Paper for Local Government, to targets at indigent households only, when indigent registers are often not updated, tend to have low registration rates and hence high levels of exclusion (South African Cities Network, 2020).

The ratio of repairs and maintenance as a percentage of the carrying value of Property, Plants and Equipment and Investment Property (PPE) captures the level of routine repairs and maintenance to prolong the useful life of assets, ensure continued service provision, prevent breakdowns and interruptions to service delivery. Repairs and maintenance is required to ensure the continued provision of services.

As depicted by the red line in the diagram below, the National Treasury the norm is 8%. A ratio below the norm suggests that insufficient resources are being devoted to repairs and maintenance to the extent that it could increase impairment of useful assets.

An increasing expenditure trend may be indicative of high asset-usage levels, which can prematurely require advanced levels of repairs and maintenance, or a need for asset renewal or replacements. Also, should an increasing expenditure trend suddenly drop to lower levels without an increase in the fixed asset value, this may be indicative of challenges in spending patterns. This may also indicate that the municipality is experiencing cash flow problems and therefore unable to spend at appropriate levels on its repairs to existing assets or purchase of new assets thus impacting negatively on service delivery.

FIGURE 37: REPAIRS AND MAINTENANCE TO OPERATING REVENUE IN SELECTED LOCAL MUNICIPALITIES, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

As can be seen in the graph below, Hessequa meets the National Treasury repairs and maintenance guidelines over the MTREF period, while Swartland and Swellendam are fairly close to compliance. However, Stellenbosch and Laingsburg - and to a lesser extent Drakenstein and Bergrivier fall far short of the requisite level of repairs and maintenance spend. Figures for Kannaland were not available. This ratio is made more difficult to interpret because the implementation of the new SCOA accounts, where the costs of employees working in the maintenance teams are directly linked to repairs and maintenance, with the result that reported repairs and maintenance might rise, without any real actual increase in resources devoted to this purpose.

While it is understandable that the immense cash flow pressures of the pandemic might result in the postponement of repairs and maintenance spending, if routine preventative maintenance is deferred indefinitely, the integrity and functionality of the asset might be so compromised that maintenance costs escalate exponentially, or replacement is required. Moreover, ageing and neglected infrastructure can result in higher electricity and water losses, for which provisions will have to be made, resulting in loss of income.

5.2.3 District municipalities medium term fiscal forecasts

The financial viability of DM's was more uncertain than LMs before the pandemic, and they have become even more so during the pandemic. Unlike LM's, the impact of the pandemic and lockdown was not directly via falls in rates and user charges payments as in the case of LM's but via intergovernmental transfers which were curtailed as a result of the R230 billion tax collapse at national level in 2019/20 due to the pandemic, and the imperative for deeper fiscal consolidation as debt at national level accelerated to unsustainable levels..

As noted earlier, the balance on the operating budget (i.e. surplus or deficit) is one of the most fundamental measures of financial performance. The ability of municipalities to generate cash based operating surpluses is critical to accumulate internal reserves to fund capital expenditure, as well as to insulate the municipality against shocks like droughts and pandemics. Accumulated surpluses can also be used to finance long term debt, and therefore the operating budget balance is a crucial indicator for assessing a municipality's creditworthiness, which in turn impacts its cost of borrowing.

The three sampled DMs rely heavily on intergovernmental transfers and subsidies (the RSC Levy replacement grant primarily, to a much lesser extent the local government Equitable Share grant which funds the environmental health function and other smaller operating transfers) and roads agency income. In Cape Winelands in 2019/20, unaudited outcomes suggest that 55% of Cape Winelands DM's operating income was derived from intergovernmental transfers and subsidies, and a further 28% was derived from agency services (predominantly roads). Central Karoo was even more dependent on operating transfers. They constituted 45% of the municipality's operating revenue, while road agency services comprise a further 50% (jointly 95% of total revenue). Interest from investments and own revenues are very small revenue sources, except in West Coast District Municipality which due to water concession arrangements derives bulk water service charges (30%), as well as agency service income (32%) and significant own revenue income from sources such as permits and licenses, building plans, connection fees and rental of municipal assets (26%).

As a risk mitigation strategy, all three sampled DM's ran greater operating surpluses than originally budgeted in 2019 to help offset planned deficits over the MTREF.

Table 27 illustrates that Cape Winelands DM had budgeted for an deficit of R3 million initially at the start of the 2019/20financial year, but ended with an estimated surplus of R42 million (10% of its operating revenue in that year). While operating revenue fell -8% short of budgeted revenue targets and was -2% less than the prior year, the DM was able to constrain its expenditure to -18% less than budgeted. West Coast had budgeted for a modest surplus R0.6 million in 2019/20 but ended the year with an estimated surplus of R39.4 million (or 10% of its operating revenue in that year). Operating revenue was 5% more than originally budgeted (and an increase of 5% over the prior year) while cost containment measures reduced expenditures to -6% less than budgeted. Central Karoo DM had anticipated a small operating surplus in 2019/20 of R1 million but ended the year with a slightly larger surplus of R1.5 million (amounting to 1% of operating revenue in that year. Operating revenues exceeded budgeted targets in 2019/20 by 8% (but were still -2% less than the prior year), but Central Karoo was less successful than the other two sampled DMs, with operating expenditure exceeding the budgeted amount by 7%.

As can be seen from the table below, DMs appear to be harder hit, with all three of them budgeting for operating and overall deficits over the MTREF, which will place their cashflows under strain. Cape Winelands is projected operational deficits of -R3.4 million in 2020/21, –R6.5 million in 2021/22 and -R7.8 million in 2022/23, and the overall balance after capital transfers remains in deficit over all three years of the MTREF. The same situation applies to West Coast DM which envisages operating deficits of -R5.7 million in 2020/21, -R10.9 million in 2021/22 and -R18.8 million in 2022/23. Central Karoo has projected a modest operating surplus of R0.8 million in 2021/22, but operating deficits of -R0.9 million in 2022/23 and -R2.3 million in 2023/24. In its 2020/21 MTREF Budget Report, Central Karoo disclosed that these outer year deficits relate "purely to the roads budget and the muni will remain in discussion with the WC Dept of Transport and Public Works to ensure that the deficits are fully addressed" (p113). The municipality asserts that the roads budget was prepared based on the allocation received from the WC Dept of Transport and Public Works and that the "total expenditure for the roads depts for the outer years will be scrutinised further and discussed with the WC Dept of Transport and Public Works to ensure that the final figures provide better guidance regarding the outer years". (P12). This suggests that agency contractual arrangements are not providing adequate certainty to either the recipients or the disbursing department, and is a cause for concern.

TABLE 27: 2020/21 MTREF OPERATING BALANCE OF SAMPLED DISTRICT MUNICIPALITIES

CATEGORY	CAPACITY	Municipality	R millions	Audited Outcome			Original Budget	Pre-audit Outcome	Medium Term Revenue & Expenditure Framework			% change YoY	Actual vs budget variance	Avg annual growth over MTREF period	
				16/17	17/18	18/19	19/20		20/21	21/22	22/23	19/20		16/17-19/20	20/21-22/23
C1	Medium	Cape Winelands	Operating Revenue	388.5	380.3	412.4	440.8	405.4	434.2	442.3	454.8	-2%	-8%	1%	2%
			Operating Expenditure	363.6	361.2	361.5	443.8	363.9	437.6	448.8	462.6	1%	-18%	0%	3%
			Operating Surplus/(Deficit)	**24.9**	**19.0**	**50.9**	**(3.0)**	**41.5**	**(3.4)**	**(6.5)**	**(7.8)**	**-18%**	**1483%**	**19%**	**51%**
			Capital transfers and subsidies	-	-	-	6.4	1.1	1.7	1.8	0.6		-82%		-40%
			Surplus/(Deficit)	**24.9**	**19.0**	**50.9**	**3.4**	**42.6**	**(1.7)**	**(4.7)**	**(7.2)**	**-16%**	**1144%**	**20%**	
C1	Medium	West Coast	Operating Revenue	362.2	344.4	363.6	376.6	393.9	427.0	430.1	442.1	8%	5%	3%	2%
			Operating Expenditure	313.5	334.1	349.1	376.0	354.4	432.7	441.0	460.9	2%	-6%	4%	3%
			Operating Surplus/(Deficit)	**48.8**	**10.3**	**14.5**	**0.6**	**39.4**	**(5.7)**	**(10.9)**	**(18.8)**	**172%**	**6572%**	**-7%**	
			Capital transfers and subsidies	-	1.5	2.7	-	0.1	0.6	0.6	-	-96%			-100%
			Surplus/(Deficit)	**48.8**	**11.8**	**17.2**	**0.6**	**39.6**	**(5.0)**	**(10.3)**	**(18.8)**	**130%**	**6593%**	**-7%**	**93%**
C1	Medium	Central Karoo	Operating Revenue	69.0	81.8	106.6	97.2	104.6	101.0	102.7	106.7	-2%	8%	15%	3%
			Operating Expenditure	69.1	42.5	100.7	96.3	103.1	100.2	103.6	109.0	2%	7%	14%	4%
			Operating Surplus/(Deficit)	**(0.01)**	**39.3**	**5.8**	**1.0**	**1.5**	**0.8**	**(0.9)**	**(2.3)**	**-75%**	**50%**	**-586%**	
			Capital transfers and subsidies	0.9	-	0.1	-	-	-	-	-	-100%		-100%	
			Surplus/(Deficit)	**0.9**	**39.3**	**5.9**	**1.0**	**1.5**	**0.8**	**(0.9)**	**(2.3)**	**-75%**	**50%**	**19%**	

The vulnerable position of DMs is illustrated in the table below by their limited revenue growth over the MTEF of 2 to 3% in the sample – below the anticipated CPI inflation rate – despite facing significant cost pressures, especially in relation to cost of employment. In all three DM's growth of operating expenditures exceeds that of operating revenues.

Cape Winelands and West Coast anticipate small annual average increases in operating transfers (on which they are largely reliant) of 2% and 1% respectively over the MTREF, while Central Karoo DM projects no increase at all. These increases are the prerogative of national revenue sharing process, outside the control of municipalities. Given that transfers comprise more than 40% of Central Karoo's income and about 57% of Cape Wineland's income, the impact is very constraining.

Agency service fees are projected by Cape Winelands, West Coast and Central Karoo to grow by 3%, 1% and 5% respectively over the MTREF period.

As noted earlier, the West Coast is not as reliant on transfers and agency services as the other 2 DMs because it derives revenue from bulk water sales which comprise about 27% of its revenues. These are projected to increase by 1% over the MTREF period. The DM's 2020/21 MTREF Budget Report notes that infrastructure assets and liabilities or borrowings related to the water services Department had been transferred to the respective local municipalities as at 30 June 2018, and that this net transfer will have a negative effect on the financial position, especially within non-current assets as well as equity (accumulated surplus).

TABLE 28: 2020/21 MTREF OPERATING REVENUE OF SAMPLED DISTRICT MUNICIPALITIES

CATEGORY	CAPACITY		R millions	Audited Outcome			Original Budget	Pre-audit Actual	MTREF projections			% YoY change	Actual vs budget variance	Avg annual growth	
				16/17	17/18	18/19	19/20		20/21	21/22	22/23	19/20		2016/17-2019/20	2020/21-2022/23
C1	Medium	Cape Winelands	Transfer and subsidies	230.7	230.7	237.7	244.8	244.1	248.4	253.7	260.1	3%	0%	2%	2%
			Interest earned	51.0	51.9	54.3	56.0	56.5	56.0	56.0	56.0	4%	1%	3%	0%
			Agency services	103.4	97.5	110.3	128.2	125.3	117.5	119.5	125.1	14%	-2%	7%	3%
			Other revenues	3.3	0.1	10.0	11.8	16.3	12.3	13.0	13.6	63%	39%	70%	5%
			Total operating revenue	**388.5**	**380.3**	**412.4**	**440.8**	**442.3**	**434.2**	**442.3**	**454.8**	**7%**	**0%**	**4%**	**2%**
C1	Medium	West Coast	Service charges	112.8	93.7	73.8	101.3	119.3	117.5	118.4	119.4	62%	18%	2%	1%
			Transfer and subsidies	88.9	22.1	21.9	24.9	23.5	27.0	28.2	29.5	7%	-6%	-36%	5%
			Interest earned	20.7	21.9	24.1	21.9	23.8	21.6	22.8	23.2	-2%	9%	5%	4%
			Agency services	120.6	128.5	139.8	131.1	124.3	152.0	149.0	156.1	-11%	-5%	1%	1%
			Other revenues	19.2	78.3	103.9	97.4	103.0	109.0	111.7	113.9	-1%	6%	75%	2%
			Total operating revenue	**362.2**	**344.4**	**363.6**	**376.6**	**393.9**	**427.0**	**430.1**	**442.1**	**8%**	**5%**	**3%**	**2%**
C1	Medium	Central Karoo	Transfer and subsidies	27.8	31.8	37.6	44.0	47.0	43.3	42.4	43.5	25%	7%	19%	0%
			Interest earned	0.5	0.5	0.7	0.6	0.9	1.1	0.9	0.9	25%	48%	23%	-10%
			Agency services	37.3	45.8	61.9	48.4	52.4	51.6	54.1	56.8	-15%	8%	12%	5%
			Other revenues	3.4	3.7	6.4	4.3	4.3	5.1	5.2	5.5	-33%	1%	8%	4%
			Total operating revenue	**69.0**	**81.8**	**106.6**	**97.2**	**104.6**	**101.0**	**102.7**	**106.7**	**-2%**	**8%**	**15%**	**3%**

In 2019/20, all 3 DMs saw increases in overall operating cost of only 1% to 2% from the prior year, which is well below CPI projections for the period and reflects application of stringent cost control measures.

Personnel costs is the single largest expenditure item at DM level. Personnel costs escalated by 4%, 8% and 6% in Cape Winelands, West Coast and Central Karoo respectively Contracted services generally did not grow, or shrink over the MTREF period, as did depreciation and asset impairment. The Other Spending category are set to increase by 5% in Central Karoos. In Cape Winelands and West Coast Other Spending increases are projected at 1% and -2% over the MREF period, suggesting that complementary inputs are being squeezed out by personnel spending.

TABLE 29: 2020/21 MTREF OPERATING EXPENDITURE OF SAMPLED DISTRICT MUNICIPALITIES

	R millions		R millions	Audited Outcome			Original Budget	Pre-audit Outcome	Medium Term Revenue & Expenditure Framework			% YoY change	Actual vs budget variance	Avg annual growth over MTREF period	
				16/17	17/18	18/19	19/20		20/21	21/22	22/23	2019/20		2016/17-2019/20	2020/21-2022/23
	Medium	Cape Winelands	Employee related costs	173.8	182.9	178.2	225.7	199.2	233.4	246.6	258.6	12%	-12%	5%	5%
			Contracted services	58.2	50.3	43.5	62.1	35.9	58.0	57.3	55.5	-17%	-42%	-15%	-2%
			Depreciation & asset impairment	8.4	10.0	11.8	10.0	9.9	12.0	12.0	12.0	-16%	-1%	6%	0%
			Finance charges	0.0009	-	-	-	-	-	-	-	-	-	-	-
			Debt impairment	**1.3**	**0.1**	**0.1**	**1.1**	**-**	**0.8**	**0.8**	**0.8**	-100%	-100%	-100%	1%
			Other expenditure	121.9	117.9	128.1	144.8	118.8	133.5	132.2	135.9	-7%	-18%	-1%	1%
			Total operating expenditure	**363.6**	**361.2**	**361.5**	**443.8**	**363.9**	**437.6**	**448.8**	**462.6**	**1%**	**-18%**	**0%**	**3%**
C1	Medium	West Coast	Employee related costs	155.6	160.8	174.3	193.8	174.1	208.2	225.1	241.8	0%	-10%	4%	8%
			Bulk purchases	8.7	24.1	8.4	13.5	10.9	14.8	15.6	16.4	30%	-20%	8%	5%
			Contracted services	-	26.6	26.1	28.9	20.0	26.2	26.4	26.0	-23%	-31%	-	0%
			Depreciation & asset impairment	7.7	8.2	8.7	9.3	7.0	9.0	9.8	9.8	-20%	-25%	-3%	4%
			Finance charges	7.3	5.7	3.7	0.2	2.7	0.1	0.1	0.1	-27%	1448%	-28%	5%
			Debt impairment	-	0.8	0.6	0.9	0.4	0.8	0.8	0.8	-40%	-58%	-	3%
			Other expenditure	134.2	107.8	127.4	129.5	139.4	173.6	163.3	166.0	9%	8%	1%	-2%
			Total operating expenditure	**313.5**	**334.1**	**349.1**	**376.0**	**354.4**	**432.7**	**441.0**	**460.9**	**2%**	**-6%**	**4%**	**3%**
	Medium	Central Karoo	Employee related costs	35.0	-	47.0	50.4	54.6	55.5	57.9	62.0	16%	8%	16%	6%
			Contracted services	3.5	4.7	14.1	4.3	5.8	9.6	9.3	8.4	-59%	35%	19%	-7%
			Depreciation & asset impairment	0.8	0.5	0.5	0.3	0.7	0.7	0.5	0.5	36%	142%	-5%	-9%
			Finance charges	0.9	0.9	0.0	-	-	-	-	-	-100%		-100%	-
			Other expenditure	29.0	36.3	39.1	41.3	42.1	34.4	35.9	38.1	8%	2%	13%	5%
			Total operating expenditure	**69.1**	**42.5**	**100.7**	**96.3**	**103.1**	**100.2**	**103.6**	**109.0**	**2%**	**7%**	**14%**	**4%**

Table 30 reflects that Cape Winelands and Central Karoo significantly underspent their capital budgets in 2019/20 by 30% and 42% respectively. While West Coast exceeded budgeted capital expenditure marginally by 1%, this was still 28% lower than the prior year.

Of significant operational sustainability concerns are the average annual declines in planned capital expenditure of -12%, -22% and -24% in Cape Winelands, Central Karoo and West Coast DM respectively. These nominal decreases translate into greater real capital spending declines, with consequences for community services, health services and other district infrastructure.

TABLE 30: 2020/21 MTREF CAPITAL EXPENDITURE OF SAMPLED DISTRICT MUNICIPALITIES

	Audited Outcomes			Original Budget	Pre-audit Actual Outcome	MTREF projections			% YoY change	Actual vs budget variance	Avg annual growth over MTREF period	
R millions	16/17	17/18	18/19	19/20		20/21	21/22	22/23	19/20		2016/17-2019/20	2020/21-2022/23
Cape Winelands	11.4	18.3	14.2	42.7	7.4	29.9	23.8	23.0	-48%	-30%	**-13%**	**-12%**
West Coast	10.9	13.7	9.4	9.4	6.8	9.5	10.2	5.4	-28%	1%	**-15%**	**-24%**
Central Karoo	1.1	0.6	0.1	0.7	0.1	0.4	0.3	0.3	141%	-42%	**-51%**	**-22%**

Cape Winelands and Central Karoo fell substantially short of their original capital budget revenues (-30% and -42% respectively) in 2019/20, while West Coast was marginally above budgeted revenue (1%). This was driven mainly by declines in internally generated funds

DM's do not receive capital grants such as the Municipal Infrastructure Grant from national government, since they typically do not have to rollout or maintain service infrastructure. They therefore tend to mainly reliant on internal funds, and – to a much lesser extent – provincial capital transfers.

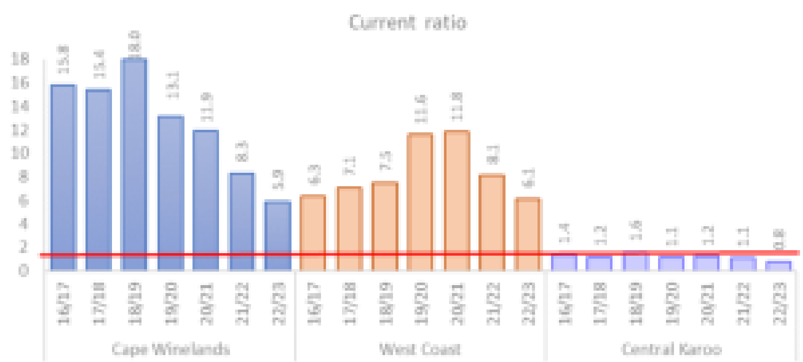
Cape Winelands (-12%), Central Karoo (-22%) and West Coast (-24%) all budgeted for decreases in their capital revenue budgets over the MTREF.

Table 31: 2020/21 MTREF capital revenue of sampled district municipalities

CATEGORY	CAPACITY	Municipality	R miilions / Revenue source	Audited Outcome 16/17	Audited Outcome 17/18	Audited Outcome 18/19	Original Budget 19/20	Pre-audit Actual 19/20	MTREF projections 20/21	MTREF projections 21/22	MTREF projections 22/23	% YoY change 19/20	Actual vs budget variance 19/20	Avg annual growth over MTREF period 2016/17-2019/20	Avg annual growth over MTREF period 2020/21-2022/23
CI	Medium	Cape Winelands	Transfers: Provincial	0.7	1.9	1.7	6.4	0.1	1.7	1.8	0.6	-92%	-73%	-42%	-40%
			Internal funds	10.6	16.4	12.6	36.2	7.2	28.2	22.0	22.4	-43%	-22%	-12%	-11%
			Total capital revenue	**11.4**	**18.3**	**14.2**	**42.7**	**7.4**	**29.9**	**23.8**	**23.0**	**-48%**	**-30%**	**-13%**	**-12%**
CI	Medium	West Coast	Transfers: Provincial	-	(0.7)	0.5	-	0.1	0.6	0.6	-	-74%			-100%
			Transfers: Other	0.0	-	-	-	-	-	-	-			-100%	
			Internal funds	10.9	7.9	8.6	9.4	6.6	8.9	9.6	5.4	-23%	-6%	-15%	-22%
			Total capital revenue	**10.9**	**7.2**	**9.1**	**9.4**	**6.8**	**9.5**	**10.2**	**5.4**	**-26%**	**1%**	**-15%**	**-24%**
CI	Medium	Central Karoo	Transfers: Provincial	0.9	-	-	-	-	-	-	-			-100%	
			Transfers: Other	0.2	-	-	-	-	-	-	-			-100%	
			Internal funds	-	-	-	0.7	0.1	0.4	0.3	0.3		-42%		-22%
			Total capital revenue	**1.1**	**-**	**-**	**0.7**	**0.1**	**0.4**	**0.3**	**0.3**		**-42%**	**-51%**	**-22%**

As can be seen in Figure 38, the decrease in the current ratio in Cape Winelands between 2016/17 and 2019/20 is significant and is set to deteriorate further during the MTREF period. This suggests that the municipalities to pay back its short-term liabilities (debt and accounts payable) with its short-term assets (cash, inventory, and accounts receivable) has diminished and that it has less risk cover to enable it to continue operations at desired levels. This also applies to West Coast DM where the current ratio improves markedly between 2016/17 and 2021/22 but is set to deteriorate in the 2 outer years of the MTREF. Both Cape Winelands DM and West Coast have current ratios easily in excess of the 1.5 National Treasury minimum norm over the MTRF, while Central Karoo does not meet this norm, suggesting more severe cashflow pressures over the MTREF.

Figure 38: Current ratio in sampled district municipalities, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

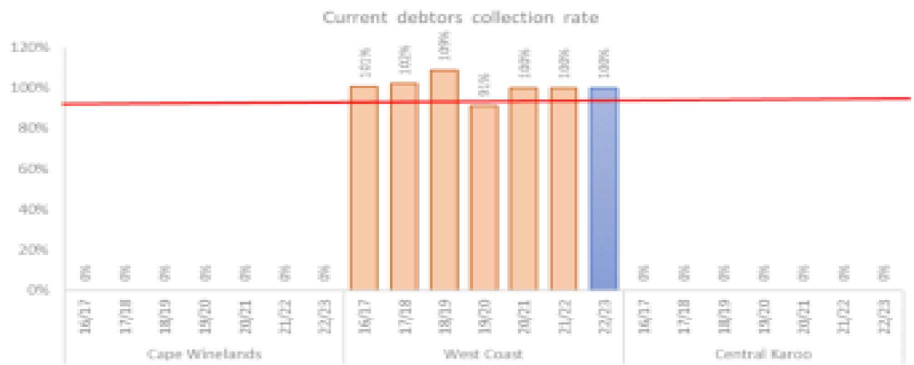
Like the current ratio, the liquidity ratio also captures the extent to which the municipality has cash or monetary assets to meet its current short term liabilities, but takes into account the composition of current assets - some assets such as accounts receivable over 90 days old, for instance, may be less easily recoverable and convertible into cash. Ideally the municipality should have the equivalent cash and cash equivalents on hand to meet at least the current liabilities, which should translate into a liquidity ratio of 1. Anything below 1 indicates a shortage in cash to meet creditor obligations. When the liquidity ratio is considered, trends similar to that of the current ratio emerge as DMs typically do not sell services and therefore their accounts receivable and consumer debt tend to be small.

FIGURE 39: LIQUIDITY RATIO IN SELECTED DISTRICT MUNICIPALITIES, 2016/17–2022/23

Source: MTREF budget submissions, National Treasury database

As noted earlier, the current debtors collection rate shows cash receipts from property rates and service charges as a percentage of total annual ratepayer and user charge revenues. The collection ratio provides an indication of the cumulative revenue management performance (the effectiveness of credit control i.e. ensuring that what is billed is collected; and effectiveness of revenue management - the ability to set affordable tariffs and bill correctly). The norm is 95%. If the ratio is below the norm this is an indication that revenue collection of the municipality requires urgent attention and corrective measures should be implemented. A municipality with outstanding debtors should aim at achieving a collection rate of more than 100%. The collection rate will impact on the cash position of the municipality and inform the level of cash and cash equivalents at year end, and hence liquidity and solvency. Because DM's don't levy property rates or deliver services, the current collection ratio is not really applicable to Cape Winelands and Central Karoo. It is applicable to the bulk water sales revenue accruing to the West Coast DM. West Coast is comfortably in excess of the National Treasury norm.

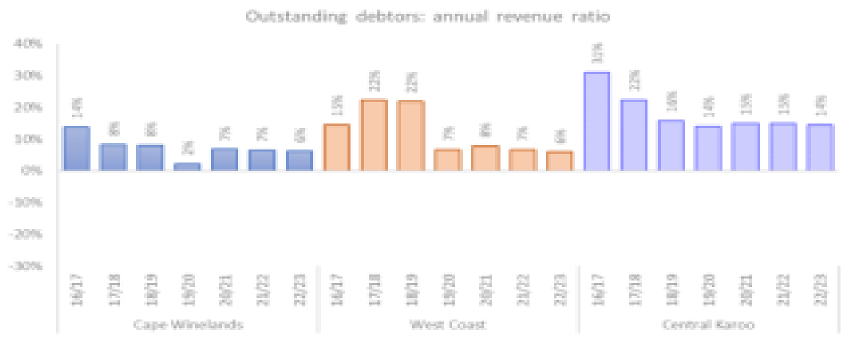
FIGURE 40: CURRENT DEBTORS COLLECTION RATE IN SAMPLED DISTRICT MUNICIPALITIES, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

Unlike the current collection rate which focuses exclusively on consumer debt from rates and tariffs, the outstanding debt as a proportion of annual operating revenue is a more comprehensive measure which includes other debtors (e.g. in respect of agency service fees) and the current portion of long term liabilities. Applying the more broadly defined outstanding debtors to annual revenue ratio, it is clear that Central Karoo has a much higher level of outstanding debtors than the other two sampled DMs.

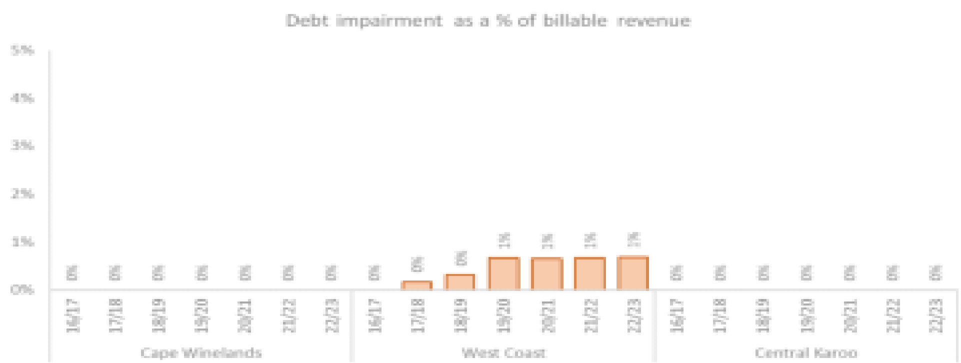
Figure 41: Outstanding debtors to annual revenue ration



Source: MTREF budget submissions, National Treasury database

The District DM, being largely intergovernmental grant reliant, do not provide services and therefore have no consumer debt. West Coast, because of its bulk water services has very low levels of debt impairment.

Figure 42: Debt impairment as a percentage of billable revenue, 2016/17–2022/23



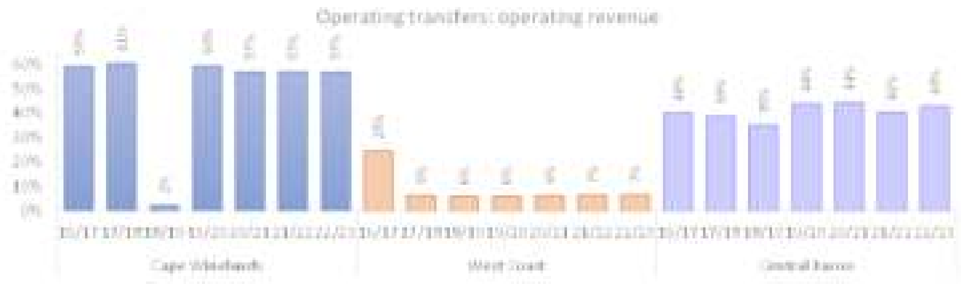
Source: MTREF budget submissions, National Treasury database

It is concerning that compensation of employees amounts to more than half of operating revenue in district municipalities in 2020/21 and that this is set to increase over the MTREF period to 57% in Cape Winelands DM and West Coast, and 63% in Central Karoo

District municipalities are largely reliant on the RSC replacement grant to fund their operational needs. West Coast DM derives revenue from bulk water sales in terms of its water concession arrangement and is consequently less dependent on intergovernmental transfers. The RSC replacement grant for Cape Winelands is projected to only increase by

2.7%, 2.8% and 2.4% over the MTREF period, while employment costs are expected to escalate at an annual average rate of 5% over the same period.

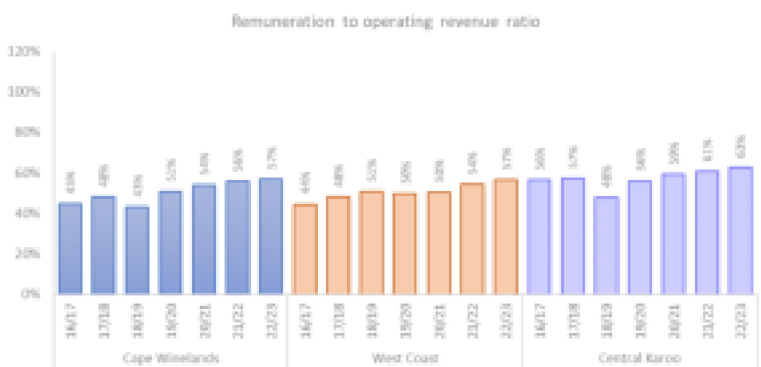
FIGURE 43: OPERATING TRANSFERS TO OPERATING REVENUE RATIO IN SELECTED DISTRICT MUNICIPALITIES, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

It is concerning that compensation of employees amounts to more than half of operating revenue in district municipalities in 2020/21 and that this is set to increase over the MTREF period to 57% in Cape Winelands DM and West Coast, and 63% in Central Karoo. In 2020/21 employee related costs in Cape Winelands only increased by 3.82% opposed to the budgeted increase of 6.25% due to certain vacant posts not being budgeted for the whole financial year. Similarly, in West Cost DM 's vacancies have been significantly rationalised as part of a cost reprioritisation and cash management strategy and provisions for overtime are restricted to emergency services and other critical function. Central Karoo's 2020/21 MTREF Budget Report notes that the "5% increase in the proposed Equitable Share allocation does not make an adequate provision for the impact of the SALGBC agreement relating to wate increases that was entered into in 2018 for the next 3 years. The real effect of the increases in the wage amounts to 9.5% when the annual notch increases of staff are taken into account. Should the final Division of Revenue Act lower the proposed Equitable Share, the impact on the municipality will be catastrophic" (p4). Remuneration of Councillors is budgeted for in terms of the Public Office Bearers Act.

FIGURE 44: REMUNERATION TO OPERATING REVENUE RATIO IN SELECTED DISTRICT MUNICIPALITIES, 2016/17–2022/23



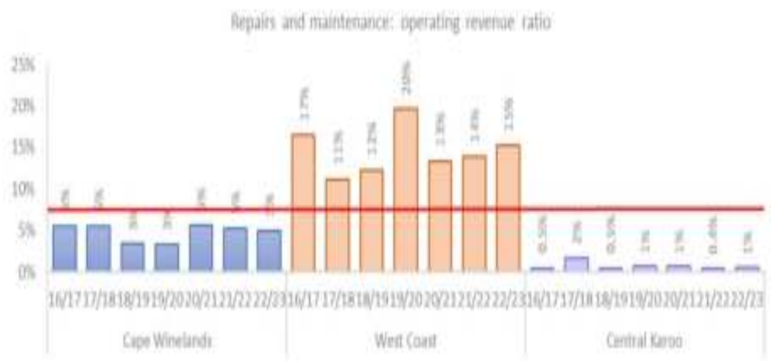
Source: MTREF budget submissions, National Treasury database

The ratio of repairs and Maintenance as a percentage of the carrying value of Property, Plants and Equipment and Investment Property (PPE) captures the level of routine repairs and maintenance to prolong the useful life of assets, ensure continued service provision, prevent breakdowns and interruptions to service delivery. Repairs and maintenance is required to ensure the continued provision of services. As depicted by the red line in the diagram below, the National Treasury the norm is 8%. A ratio below the norm suggests that insufficient resources are being devoted to repairs and maintenance to the extent that it could increase impairment of useful assets.

An increasing expenditure trend may be indicative of high asset-usage levels, which can prematurely require advanced levels of repairs and maintenance, or a need for asset renewal or replacements. Also, should an increasing expenditure trend suddenly drop to lower levels without an increase in the fixed asset value, this may be indicative of challenges in spending patterns. This may also indicate that the municipality is experiencing cash flow problems and therefore unable to spend at appropriate levels on its repairs to existing assets or purchase of new assets thus impacting negatively on service delivery.

As district municipalities are typically not involved in the delivery of tradeable services, their asset bases tend to be smaller, and repairs and maintenance is mainly in respect of the buildings/property the DMs own. West Coast records a high proportion of repairs due to its bulk water delivery in terms of a water concession arrangement. West Coast therefore is aligned with National Treasury norms, whereas Central Karoo - and to a much lesser extent Cape Winelands - fall short of the norm. The low levels of repairs and maintenance in Central Karoo is of concern since it is likely to have operational sustainability consequences in subsequent years.

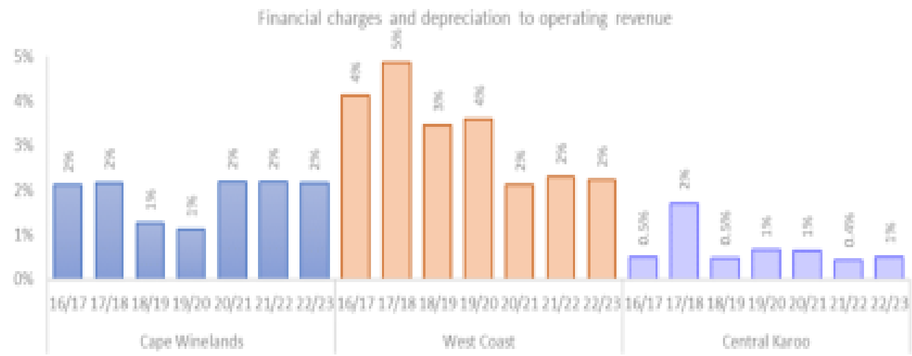
FIGURE 45: REPAIRS AND MAINTENANCE TO OPERATING REVENUE RATIO IN SAMPLED DISTRICT MUNICIPALITIES, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

Depreciation charges are largely determined by the municipality's asset management plan, and finance charges relate to the interest costs of borrowing and loan redemption. Except for West Coast, which borrows to finance its water concession, the other 2 sampled municipalities are reliant on the RSC Replacement grant and do not borrow. Finance charges are therefore small.

FIGURE 46: FINANCE CHARGES AND DEPRECIATION TO OPERATING REVENUE RATIO IN DISTRICT MUNICIPALITIES, 2016/17–2022/23



Source: MTREF budget submissions, National Treasury database

5.2.4 City of Cape Town medium term fiscal forecasts

As noted earlier, the balance on the operating budget (i.e. surplus or deficit) is one of the most fundamental measures of financial performance. The ability of cities to generate cash based operating surpluses is critical to accumulate internal reserves to fund capital expenditure, as well as to insulate the city against shocks like droughts and pandemics. Accumulated surpluses can also be used to finance long term debt, and therefore the operating budget balance is a crucial indicator for assessing a city's creditworthiness, which in turn impacts its cost of borrowing.

As can be seen in the table below, after three consecutive years of operating surpluses of about 10% of operating revenues between 2016/17 and 2018/19, the City had budgeted for an operating deficit at the beginning of the 2019/20 financial year. Unaudited estimates of actual outcomes at the end of 2019/20 suggests that instead the City had an operating surplus in 2019/20, with operating revenues exceeding budget by 3% despite the hard lockdown in 2019/20Q4, and operating expenditures 4% less than budgeted for. Over the MTREF period, the City intends to continue to run operating deficits of -6%, -1% and -1% of operating revenues. Capital transfers are expected to increase by 9% over the MTREF and the overall balance for the municipality after capital transfers and subsidies, taxation and revenue attributable to minorities, is positive. Despite these operating deficits, the City envisages it will remain in a surplus net cash flow position and that that budgets over the MTREF would be fully funded.

TABLE 32: MTREF OPERATING BALANCE, CITY OF CAPE TOWN

CATEGORY	CAPACITY	Municipality	R millions	Audited Outcome 16/17	Audited Outcome 17/18	Audited Outcome 18/19	Original Budget 19/20	Pre-audit Outcome 19/20	Medium Term Revenue & Expenditure Framework 20/21	Medium Term Revenue & Expenditure Framework 21/22	Medium Term Revenue & Expenditure Framework 22/23	% change YoY 19/20	Actual vs budget variance 19/20	Avg annual growth 16/17-19/20	Avg annual growth 20/21-22/23
A	High	City of Cape Town	Operating Revenue	36 383	36 898	40 276	41 095	42 402	42 443	46 563	50 238	5%	3%	5%	9%
			Operating Expenditure	33 024	33 390	36 164	42 099	40 440	45 145	47 123	50 644	12%	-4%	7%	6%
			Operating Surplus/(Deficit)	**3 359**	**3 509**	**4 111**	**(1 005)**	**1 961**	**(2 701)**	**(561)**	**(406)**	**-52%**	**95%**	**-16%**	**-61%**
			Capital transfers and subsidies	2 022	1 942	2 304	2 379	2 106	3 005	3 440	3 559	-9%	-11%	1%	9%
			Taxation	14	-	-	-	(27)	(26)	(21)	(21)				
			Attibutable to minorities	(13)	-	-	-	-	(20)	(14)	(14)				
			Surplus/Deficit	**5 354**	**5 451**	**6 415**	**1 374**	**4 095**	**309**	**2 886**	**3 159**	**-36%**	**198%**	**-9%**	**220%**

Operating expenditure is expected to exhibit an annual average increase at 6% over the MTREF, while operating revenue is expected to increase more rapidly at 9%. According to its 2020/21 MTREF Budget Report, the City had introduced a cost containment strategy aimed at strictly controlling spending and reducing reliance on consultants. Some of the responses to the 2018 drought to reduce water losses also reduced operating cost. As part of its proactive water demand management strategy, the City focused on water pressure management, leak repairs and demand management. In its 2020/21 MTREF Budget Report, the City of Cape Town reports that pressure management achieved savings of more than 60 Mℓ/day, leak repair programmes an estimated 4,75 Mℓ/day, and additional large demand reductions were achieved by logging and focusing on the top 200 users. To redirect funds to meet the additional requirements of the pandemic and mitigate revenue losses, an adjustment budget reduced budgets for filling vacancies by R250 million.

Table 33 illustrated that quite remarkably, despite the lockdown in 2019/20Q4, operational revenues were 3% in excess of the budget in that year. Property rates (which comprised 24% of operating revenue in 2019/20) and service charges (which constitute 47% of operating income for the City, both exceeded budgeted revenue targets by 2% and increased 6% from the prior year. Only agency income had a shortfall of -8% in relation to revenue targets and declined -13% from the previous year. According to its 2020/21 MTREF Budget Report, debtor who are in a position to pay but opt not to, the City has focused on the top 1000 debtors, especially high value business and residential accounts and government accounts, as well as staff and councillor arrears. Credit control measures include issuing of warning letters, restriction or disconnection of water and electricity, adverse credit listing, and legal action which could lead to a sale in execution of the property. The City has been offering affordable payment plans to individual households in arrears, where debt management actions and interest are suspended until the arrears are paid in full. With the coronavirus pandemic, the City – according to the 2020/21 MTREF Budget Report – is also extending these arrangements to parts of the commercial sector hardest hit by the lockdown (e.g. hotels), in compliance with the City's credit control policy and section 164(1)(c)(iii) of the Municipal Finance Management Act which prohibits a municipality from making loans to members of the public.

TABLE 33: MTREF OPERATING REVENUES, CITY OF CAPE TOWN

CAPACITY		R millions	Audited Outcome			Original Budget	Pre-audit Actual	MTREF			% YoY change	Actual vs budget variance	Avg annual growth over MTREF period	
			16/17	17/18	18/19	19/20		20/21	21/22	22/23	19/20		16/17-19/20	20/21-22/23
High	City of Cape Town	Property rates	8 100	8 674	9 542	9 917	10 081	10 512	11 556	12 624	6%	2%	8%	10%
		Service charges	17 878	17 055	18 929	19 690	20 099	19 886	22 554	24 407	6%	2%	4%	11%
		Transfer and subsidies	5 864	4 038	4 487	4 806	4 983	5 609	5 574	6 021	11%	4%	-5%	4%
		Interest earned	1 078	1 204	1 498	1 313	1 707	1 245	1 298	1 365	14%	30%	17%	5%
		Agency services	188	214	230	218	201	242	267	287	-13%	-8%	2%	9%
		Other revenues	3 273	5 713	5 589	5 151	5 330	4 950	5 315	5 534	-5%	3%	18%	6%
		Total operating revenue	**36 383**	**36 898**	**40 276**	**41 095**	**42 402**	**42 443**	**46 563**	**50 238**	**5%**	**3%**	**5%**	**9%**

Aggregate operating revenue is expected to grow at an average annual rate of 9% over the MTREF, with the 2 major revenue drivers, property rates and service charges expected to grow at an average annual rate of 10% and 11% respectively. Property rates were supported by the General Valuation of 2018.

Transfers and subsidies, which had declined an annual average rate of -5% 2016/17 to 2019/20, are projected to grow at 4%, broadly in line with inflation. Agency service revenue is expected to recover at a 9% annual average rate over the MTREF.

In 2019/20, not only did operating revenue exceed budget, but cost containment held operating costs -4% below budget. There was a significant increase in debt impairment of 77% from the prior year and 20% in excess of the budget, which would have been influenced by the pandemic. As can be seen in Table 34, except for that non-cash item and finance charges which exceeded budget, costs were below budget, especially in relation to cost of employment, bulk purchases and other expenditure. Unlike other metropolitan municipalities which are served by water boards, the City produces its own bulk water, which results in lower bulk service expenditure as a proportion of operating expenditure than in other metropolitan municipalities (South African Cities Network, 2020)

Table 34: MTREF operating expenditure, City of Cape Town

CATEGORY	CAPACITY	Municipality	R millions	Audited Outcome			Original Budget	Pre-audit Outcome	Medium Term Revenue & Expenditure Framework			% YoY change	Actual vs budget variance	Avg annual growth	
				16/17	17/18	18/19	19/20		20/21	21/22	22/23	2019/20		16/17-19/20	20/21-22/23
A	High	City of Cape Twon	Employee related costs	9 729	10 984	12 414	13 909	12 853	15 296	16 695	18 074	4%	-8%	10%	9%
			Bulk purchases	8 438	8 122	8 632	10 093	9 858	9 991	11 092	12 044	14%	-2%	5%	10%
			Contracted services	4 300	5 505	6 093	7 274	6 948	7 322	7 409	7 816	14%	-4%	17%	3%
			Depreciation & asset impairment	2 341	3 085	2 886	3 065	3 059	3 355	3 432	3 610	6%	0%	9%	4%
			Finance charges	733	852	789	791	814	828	1 239	1 446	3%	3%	4%	32%
			Debt impairment	2 324	1 362	1 583	2 342	2 804	3 641	2 252	2 361	77%	20%	6%	-19%
			Other expenditure	5 159	3 479	3 767	4 626	4 105	4 712	5 004	5 294	9%	-11%	-7%	6%
			Total operating expenditure	**33 024**	**33 390**	**36 164**	**42 099**	**40 440**	**45 145**	**47 123**	**50 644**	**12%**	**-4%**	**7%**	**6%**

While total operating expenditure is expected to increase at 6% over the MTREF, it is disconcerting that employee cost and bulk services are increasing at 9% and 10%, while other expenditure is only growing at 6%, which is only increasing in line with inflation. While debt impairment is expected to decrease by an annual average rate of -19% over the MTREF once the economy recovers, finance charges are expected to increase by an annual average rate of 32%.

As can be seen in Table 35, the City's capital budget was hardest hit during the 2019/20Q4 hard lockdown, with actual capital expenditure falling short of budgeted by 20%. However the capital budget is set to grow at a health average annual growth of 20% over the MTREF period.

Table 35: MTREF capital expenditure, City of Cape Town

CATEGORY	CAPACITY	Municipality	R miilions	Audited Outcome			Original Budget	Pre-audit Actual Outcome	MTREF projections			% YoY change	Actual vs budget variance	Avg annual growth	
			Revenue source	2016/17	2017/18	2018/19	2019/20		2020/21	2021/22	2022/23	19/20		16/17-19/20	20/21-22/23
A	H	City of Cape Town	Electricity	11 809	8 415	6 571	8 052	6 639	6 639	5 712	10 277	23%	-18%	-17%	24%
			Water management	9 148	936	6 981	15 179	10 026	10 026	8 903	12 879	117%	-34%	3%	13%
			Waste water management	6 591	821	1 657	13 811	9 511	9 511	2 177	14 652	733%	-31%	13%	24%
			Waste management	1 725	219	1 171	4 725	2 229	2 229	(123)	5 582	304%	-53%	9%	58%
			Road transport	13 788	6 398	5 829	13 521	13 056	13 056	6 457	18 792	132%	-3%	-2%	20%
			Other community services & public safety	4 017	2 531	2 507	5 903	4 512	4 512	4 514	7 581	135%	-24%	4%	30%
			Housing	4 769	1 011	1 008	8 691	8 992	8 992	2 274	8 949	762%	3%	24%	0%
			Governance & administration	6 163	13 359	7 590	11 200	10 006	10 006	6 628	13 963	48%	-11%	18%	18%
			Other	4 717	1 681	1 622	3 228	2 712	2 712	1 596	4 139	99%	-16%	-17%	24%
			Total capital expenditure	**62 726**	**35 372**	**34 937**	**84 309**	**67 684**	**67 684**	**38 138**	**96 814**	**94%**	**-20%**	**3%**	**20%**

There was also a shortfall in capital revenues which were 21% below budget in the 2019/20 financial year. There was a more conservative capital mix with borrowing -34% less than originally budgeted and 47% greater reliance on internal funds than originally budgeted.

National and especially provincial capital transfers exceeded budgeted amounts by 6% and 70% respectively.

A municipality's creditworthiness impacts on the costs of capital. When Moody's downgrated the sovereign rating for the South African government on 6 April 2020, the City of Cape Town's global rating was also downgraded from Baa3/P-3 to Ba1/NP. Its national scale rating of Aaa.za/P-1.za.

FIGURE 47: MTREF CAPITAL REVENUES, CITY OF CAPE TOWN

CATEGORY	CAPACITY	Municipality	R miilions / Revenue source	Audited Outcome 16/17	Audited Outcome 17/18	Audited Outcome 18/19	Original Budget 19/20	Pre-audit Actual 19/20	MTREF projections 20/21	MTREF projections 21/22	MTREF projections 22/23	% YoY change 19/20	Actual vs budget variance 19/20	Avg annual growth rate 16/17-19/20	Avg annual growth rate 20/21-22/23
A	H	City of Cape Town	Transfers: National	20 094	6 664	8 862	21 893	23 190	23 190	8 047	28 034	162%	6%	5%	10%
			Transfers: Provincial	461	34	124	220	374	374	332	124	203%	70%	-7%	-42%
			Transfers: Other	719	59	1 504	537	421	421	402	680	-72%	-22%	-16%	27%
			Borrowing	27 392	17 242	18 675	49 175	32 632	32 632	19 796	25 000	75%	-34%	6%	-12%
			Internal funds	14 060	-	-	425	626	626	14	42 826		47%	-65%	727%
			Total capital revenue	**62 726**	**23 999**	**29 164**	**72 251**	**57 243**	**57 243**	**28 591**	**96 664**	**96%**	**-21%**	**-3%**	**30%**

Table 36 contains trends in key financial ratios over the MTREF period for the City of Cape Town. The current ratio is commonly used to assess a municipality's ability to pay back its short-term liabilities (debt and accounts payable) with its short-term assets (cash, inventory, and accounts receivable). The higher the current ratio, the better is a municipality positioned to pay its current or short-term obligations and provide for a risk cover to enable it to continue operations at desired levels. A financial ratio less than 1 suggests that the municipality would be unable to pay all its current or short-term obligations if they fall due at any specific point. The norm range is between 1.5 to 2. As can be discerned from the table, the City ended 2020/21 with a surprisingly health current ratio of 2 due to the operational surplus in that year. With the projected operational deficits over the MTREF, the current ratio declines but remains within acceptable range in 2020/21 and 2021/22. In 2022/23, the current ratio at 1.4 begins to skirt the lower bounds of what National Treasury deems acceptable.

The liquidity ratio assesses the extent to which the municipality has cash or monetary assets to meet its current short-term liabilities. This ratio takes into account the composition of current assets - some assets such as accounts receivable over 90 days old, for instance, may be less easily recoverable and convertible into cash. Ideally the municipality should have the equivalent cash and cash equivalents on hand to meet at least the current liabilities, which should translate into a liquidity ratio of 1. Anything below 1 indicates a shortage in cash to meet creditor obligations. Liquidity ratios of 0.7 in 2020/21 and 2021/22 and 0.6 in 2022/23 suggests increased cashflow pressures for the City, intensifying in the final year of the MTREF. However, the City – in its 2020/21 MTREF Budget Report – has indicated that it does not concur with the methodology applied by National Treasury: "The preferred calculation is current assets less inventory, divided by current liabilities. This ratio averages 1.5% over the MTREF" (p78).

Increased outstanding debtors and lower collection rate contribute to this deterioration in liquidity of the City of Cape Town. The current debtors collection rate shows cash receipts from property rates and service charges as a percentage of total annual ratepayer and user charge revenues. The collection ratio provides an indication of the cumulative revenue management performance (the effectiveness of credit control i.e. ensuring that what is billed is collected; and effectiveness of revenue management - the ability to set affordable tariffs and bill correctly). The norm is 95%. If the ratio is below the norm this is an indication that revenue collection of the municipality requires urgent attention and corrective measures should be implemented. A municipality with outstanding debtors should aim at achieving a collection rate of more than 100%. The collection rate will impact on the cash position of the municipality and inform the level of cash and cash equivalents at year end, and hence liquidity and solvency. The collection rate which stood at 103.8% in 2018/19, fell substantially to 92.9% in 2019/20 and is only expected to recover to 96.8% in 2022/23. This drop in the collection rate is in contrast to the over-collection in the three previous years which were underpinned by a conservative approach to revenue forecasting and rigorous credit control and debt management.

Unlike the current collection rate which focuses exclusively on consumer debt from rates and tariffs, this outstanding debt figure also includes other debtors (e.g. in respect of agency service fees, fines, penalties, licenses etc) and the current portion of long term liabilities. The outstanding debt to revenue ratio is expected to decrease to 20.1% in 2020/21 before rebounding to 19.5% in 2022/23.

To assess the City's borrowing strategy, the capital charge to own revenue ratio is a measure of the municipality's ability to service and repay its debt through own revenues. In general, the higher this ratio, the greater the financial risk exposure of the municipality. Capital charges are measured by interest finance charges and debt repayment. Own revenue is captured by operating revenues before capital transfers less operating transfers and grants such as the Local Equitable Share. To finance expansion in its capital programme, the City's borrowing increases over the MTREF, reflected in the borrowing funded by "own" capital revenue, which increases markedly from an estimated 25% in 2019/20 to 68.7% in 2022/23. Consequently, interest charges and redemption of capital also doubles from 3.5% of own revenue in 2019/20 to 7.1% in 2022/23. Also, the debt coverage ratio declines: whereas the City's own operating revenues (less operating transfers) was expected to cover debt service payments during the financial year 25.8 times in 2019/20, this decreases to 16.8 times in 2022/23. This is consistent with the higher gearing ratio. Another way to view the borrowing strategy of municipalities is through their gearing ratio which reflects the municipality's ability to repay its long-term borrowing from its accumulated surpluses and other reserves. The lower the ratio, the greater the municipality's ability to repay is debt. long term borrowing was roughly equal to funds and reserves in 2019/20 (115%). This position deteriorates as long-term borrowing increases to more than double the City's funds and reserves (246%).

In its 2020/21 MTREF Budget Report, the City has indicated that it does not agree with the way National Treasury calculates the gearing ratio: "The preferred calculation is borrowing less cash and bank balances divided by community wealth/equity, of which the City's outcome over the 2020/21 MTREF averages 9%. The low gearing ratio shows that the City as a small proportion of debt versus equity" (p 77).

TABLE 36: FINANCIAL PERFORMANCE INDICATORS OVER MTREF PERIOD: CITY OF CAPE TOWN

Financial performance indicator	Basis of calculation	Audited outcome			Full Year Forecast	MTREF projections		
		2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Liquidity: current ratio	Current assets/current liabilities	1.3	1.7	2.0	2.2	1.7	1.6	1.4
Liquidity ratio	Monetary Assets/Current Liabilities	0.6	0.9	1.2	1.2	0.7	0.7	0.6
Liquidity: cost coverage	(Available cash + Investments)/monthly fixed operational expenditure	1.7	2.5	3.4	2.6	1.4	1.9	1.7
Revenue management: annual debtors collection rate	Last 12 Mths Receipts/Last 12 Mths Billing		105.8%	103.8%	92.9%		92.4%	96.8%
Revenue management: current debtors collection rate	Cash receipts % of Ratepayer & Other revenue	105.7%	103.7%	104.9%	92.9%	92.4%	96.8%	96.9%
Revenue management: outstanding debtors to revenue	Total Outstanding Debtors to Annual Revenue	17.8%	19.1%	18.5%	19.3%	20.1%	19.6%	19.5%
Borrowing management: Capital charges to own revenue	Finance charges & Repayment of borrowing /Own Revenue	4.3%	3.8%	3.6%	3.5%	3.3%	4.8%	7.1%
Borrowing management: borrowed funding of 'own' capital expenditure	Borrowing/Capital expenditure excl. transfers and grants and contributions	0.7%	25.6%	6.0%	25.0%	36.8%	78.5%	68.7%
Borrowing management: debt coverage	(Total Operating Revenue - Operating Grants)/Debt service payments due within financial year)	19.5	16.8	25.6	25.8	22.9	15.6	16.8
Safety of capital: gearing	Long Term Borrowing/ Funds & Reserves	153.7%	187.6%	130.7%	115.0%	167.4%	213.8%	245.7%
Creditor management: Creditors System Efficiency	% of Creditors Paid Within Terms (within MFMA s 65(e))	96.5%	97.3%	96.0%	97.0%	97.0%	97.0%	97.0%
Creditor management: creditors to cash and investments		159.5%	102.9%	51.2%	44.1%	75.8%	58.0%	65.1%
Remuneration	Total remuneration/(Total Revenue - capital revenue)	28.4%	30.0%	31.1%	34.3%	36.5%	36.3%	36.5%
Repairs and maintenance	R&M/(Total Revenue excluding capital revenue)	10.8%	10.3%	9.4%	9.5%	10.9%	11.0%	10.7%
Finance charges and depreciation	FC&D/(Total Revenue - capital revenue)	9.1%	10.7%	9.2%	9.7%	9.9%	10.0%	10.1%

The ratio of creditors to cash and investments is also expected to rise substantially from 44.1% in 2019/22 to 65.1%, which is a sign of depleting cash reserves as the City runs operating deficits over the MTREF.

Remuneration as a proportion of operating revenue escalates from 31.1% in 2018/19 to 36.5% in 2021/22 and is expected to remain at that level for the outer years of the MTREF. This is below National Treasury's guideline of 40%. The personnel budget was based on a 2020/21 cost of living increase as per the SALGBC wage agreement of CPI plus 1.25% 5% plus 1.25%).

Finance charges and depreciation also increase marginally over the MTREF from 9.9% to 10.1%. Depreciation is widely considered a proxy for the measurement of the rate at which assets are consumed Depreciation charges are largely determined by the municipality's asset management plan.

Repairs and maintenance as a percentage of operating revenue at around 11% over the MTREF comfortably exceeds National Treasury's 8% norm.

Municipalities are obliged to render a minimum basket of service to indigent households (6kl of water per household per month, 50kwh per household per month of electricity, a minimum level of sanitation and refuse removed at least once a week). This cost of free basic service excludes other community services which municipalities provide to indigent households.

If municipalities provide services in excess of the minimum basket (e.g. 100kwh of electricity or more water), then this is regarded as revenue forgone by the municipality (i.e. the municipality could have charged for it, but didn't). Some municipalities also offer more generous exemptions, reduction and rebates on property rates which would also constitute revenue forgone. The same would apply to housing rental rebates and top structure subsidies.

The graph below depicts the costs of free basic services for the City, the revenue costs of subsidized services and the local government Equitable Share Grant (LGES) between 2016/17 and 2022/23.

FIGURE 48: COST OF FREE BASIC SERVICES, REVENUE COST OF SUBSIDISED SERVICES AND THE LOCAL GOVERNMENT EQUITABLE SHARE GRANT FOR THE CITY OF CAPE TOWN

It is clear that the LGES has exceeded the costs of providing FBS over the entire period. However, between 2016/17 and 2019/20, the combined value of FBS costs and revenue forgone exceed the LGES, which indicates that some of the City's own revenues have supported FBS provision. Between 2016/17 and 2019/20, FBS costs, and subsidized services revenue forgone grew at annual average rates of 14% and 2% respectively, while the LGES grew at an annual average rate of 12% per annum. In 2019/20, the costs of FBS is estimated to be R1.7 billion, and the cost of revenue forgone R1.3 billion, totalling R3 billion, which exceeds the R2.8 billion of the LGES. Between 2020/21 and 2022/23, the LGES is expected to increase at a lower rate annual average rate of 9% over the MTREF, while FBS also grows at 9% and subsidized service revenue forgone increases by 4%. The LGES exceeds the sum of FBS costs and subsidized services revenues forgone over the MTREF period.

The table below compares the City of Cape Town's cost of FBS per household (R318) with other cities and reveals that it in the sample, only eThekwini has a lower cost of FBS provision of R214, while Johannesburg reports R610 and eKhurleni R1307 per household.

TABLE 37: COST PER HOUSEHOLD FOR PROVIDING FREE BASIC SERVICES IN SELECTED CITIES, 2018/19

RANDS	JHB	CPT	EKU	ETH	TSH	NMB	BCM	MSU
Water	60	115	89	65	147		351	319
Sanitation	120	73	78	54	40	162	126	24
Electricity	380	53	942	60	147		49	47
Solid waste	50	77	199	36	99	92	205	82
Total	610	317	1 307	214	434		732	471

Note: NMB did not report cost per household for providing water and electricity services

Source: South African Cities Network (2020, p. 64)

5.3 Key themes emerging from the financial analysis

Some of the salient trends which emerged from the financial analysis of quarterly Section 71 quarterly reports and MTREF projections are captured below.

5.3.1 Key themes for local municipalities

While the pandemic has exerted short term financial and operational sustainability pressures, sampled WC municipalities on the whole have been more resilient under the circumstances than would have been expected. Their resilience is largely a function of the resilience of their tax bases and the agility of their pandemic responses.

Size and diversity of the revenue base is an important factor for resilience: larger municipalities with more buoyant and diversified rates and service user charge bases fared better than their smaller counter parts. The composition of the local economy also played a major role: those dependent on agriculture where the drought had broken fared better than those reliant on the tourism and hospitality sector. Similarly, those municipalities with a higher proportion of industries designated as essential (such as financial services) and with more skilled residents who could take advantage of working from home arrangements. Smaller municipalities, such as Laingsburg, were placed under severe cashflow pressure with unspent conditional grants virtually the only funds in their bank accounts.

If there were challenges prior to the pandemic, these were magnified during the pandemic. But municipalities with the systems maturity, governance stability, business continuity risk management and financial management capacity in place prior to the pandemic were better placed to respond agilely during the pandemic. Proactive strategies included: working from home, opening revenue offices early in the lockdown, intensifying pre-pandemic revenue enhancement strategies (e.g prepaid meters, e-billing, changes to tariff structures to include flat rate connection fees) and existing cost containment measures.

Hardest hit were the capital budgets of LMs. The uncertainty occasioned by the pandemic cause LM's to adopt more conservative borrowing strategies with increased reliance on internal funds and capital transfers, some ceasing long-term borrowing altogether. Drawing down of internal funds will have operational consequences in future, as well as additional pressure to raise tariffs to engender future operating surpluses to replenish capital reserves since borrowing for that purpose is not permitted.

Rates and user charges were not as strongly undermined as they could have been, but smaller own revenue sources were hard hit by the lockdown: fines, penalties, licences, rental of municipal properties etc. The pandemic has made it more difficult to balance sustainability and affordability of tradeable services in the face of large-scale loss of jobs and livelihoods. Debt impairment is expected to increase.

Long term sustainability factors appear to be more important than COVID-19 in the near term, although this could change, should the pandemic drag on. These include LGES increases, employment increases and bulk service increase, eroding electricity surpluses. *Most significant expenditure pressures largely driven by systemic factors, not pandemic costs primarily*, including unaffordable national minimum norms and standards, increased costs of landfill services, increase incidence of land invasion.

Cost containment strategies have been stringently applied, and there is decreasing scope for savings as expenditure is pared to the bone. Personnel budgets have the most significant scope for savings.

For most LM's the growth of *FBS costs* and subsidised revenue costs over the MTEF is projected at below the growth rate of the LG Equitable share grant, but the assumptions about increases in indigent households might be under-estimates.

There has been an increased *reporting compliance* during the pandemic, due to the special reporting requirements by National Treasury as well as

The transition to MSCOA remains a challenge as evidenced, for example, by the number of negative balances in the Section 71 quarterly reports where correcting journal entries have been processed. The interviews reflect that MSCOA is not seen as a value add by high capacity municipalities and there are perceptions of insufficient support by the lower capacity municipalities.

The pandemic has also seen innovation from sampled LM's such as Drakenstein's small scale yet rapid and flexible emergency food security programme through partnering with an NGO, where e-vouchers were sent to recipient's mobile phones for redemption at local shops. This was a safer and more creative response than the Department of Social Development's slower food parcel response which exposed recipients to infection by the virus in long queues.

5.3.2 Key themes for district municipalities

The sampled DMs were harder hit than LMs in the first quarter of the pandemic 2019/20Q4 in terms of the operating balances, but then showed somewhat of recovery as they intensified expenditure control measures and road agency functions picked up. DM's are highly dependent on the RSC replacement grant, especially those DM's without property portfolios. West Coast's water concession and resort income places it in a more favorable position than the other two DMs. In the past, DM's income from intergovernmental transfers were limited but stable, as SARS's performance backstopped the fiscal framework and created predictability. With fiscal consolidation at national level resulting in declines or slow growth of intergovernmental transfers, the tax collapse as a result pandemic and an imminent national debt consolidation crisis, the fiscal framework is far less stable. For the first 15 years after democracy, subnational grants (especially the Equitable Share) were protected over the MTREF period, which no longer seems the case. The DM's prime income source is therefore likely to be both smaller over the medium term, and more uncertain.

Similar to LM's the largest negative repercussion of the pandemic relates to constrained capital budgets with repairs and maintenance falling below the norm (except in West Coast DM).

Despite this, due to the responses of DM's, short term liquidity and solvency impaired slightly but still satisfactory. The depletion of DM internal reserves and consequently lower interest income will impact on own revenues over the medium term.

There are huge short-term pressures from cost of employment budgets and longer term pressures from drivers such as national minimum standards in functions such as environmental health, fire-fighting etc. Agency service agreements appear to be ad hoc and do not create funding certainty over the MTREF but create pressures for expansion of roads function employment (e.g. Central Karoo).

The pandemic also highlighted the social development role of DMs in rural areas, which are at the coalface of community needs and in a better position to respond to community needs – as the COVID-19 pandemic clearly illustrates, despite this not formally being in their mandate.

5.3.3 Key themes for the City of Cape Town

Despite the sharp contraction in the GDP-R of Cape Town's economy (estimated at -7.3% in 2020), it is expected to rebound to a positive growth rate of 3.8% in 2021. While the financial performance of the City has been negatively impacted by the lockdown, many of the measures taken to manage the risks of "Day Zero" and the fall-out of load-shedding as a seemingly permanent and disruptive feature of the South African economic landscape, have enhanced its short term resilience in the face of the pandemic e.g. the transition to fixed access charges, constant updating of customer contact details such as mobile numbers and email addresses permitted extension of e-billing, introduction of prepaid water and electricity meters, etc. Similarly work-from-home policies developed in response to traffic congestion and carbon footprint challenges were also appropriate for the pandemic.

Over the MTREF period, the City intends to continue to run operating deficits of -6%, -1% and -1% of operating revenues in 2020/21, 2021/22 and 2022/23. As the City's overhead and external payments increase (remuneration, finance charges, bulk service charges, creditors), and revenue collection falls with reduced liquidity and depleted internal reserves, the City's financial position is set to deteriorate over the medium term. While some of these trends can be attributed to the impact of the aftermath of the pandemic (e.g increased debt impairment), these are not as prominent causal factors as longer term systemic factors (e.g. the failure to constrain growth in personnel budgets, fiscal consolidation at the national government sphere which results in cutting of local government capital grants to fund, for example, national state owned entities and higher education). Much, however, depends on the duration of the lockdown (and its impact on solvency of businesses in the tourism, hospitality and related industries, for instance), how quickly the urban metropole's economy will rebound and how growth enhancing the City's capital investment will be.

6 Themes from interviews with sampled municipalities

To get a richer understanding of the dynamics behind the short and medium term pandemic impacts presented in the financial analysis, the qualitative insights emerging from the interview processes are presented below.

6.1 First-round interviews to mark out overall municipal financial and operational sustainability in the Western Cape.

As was indicated in the Introduction, these interviews focused on three overarching questions, firstly on overall municipal financial and operational sustainability and its main drivers before and since Covid-19; secondly on cost minimisation efforts and the factors impeding and challenging achievement of a Minimum Efficient Cost for each responding municipality; and thirdly on maximising revenue and factors impeding and challenging achievement of the Maximum Fiscal Capacity by each responding municipality.

The responding municipalities have been identified during a meeting of the Municipal Managers Forum on 27 August 2020 and were selected to represent small, medium and large size municipalities as well as local and district municipalities. The municipalities, in chronological order of interviews, were West Coast District Municipality; Bergrivier Local Municipality (medium); Laingsburg Local Municipality (small); Swellendam Local Municipality (small); Kannaland Local Municipality (small); Garden Route District Municipality; Central Karoo District Municipality; Drakenstein Local Municipality (large); Stellenbosch Local Municipality (large); City of Cape Town (metro).

The interviews took place between 14 and 30 September 2020 and on 11 and 15 February (City of Cape Town) by means of Microsoft Teams video-conference calls and the interview panel consisted of Prof Johan Burger (lead interviewer); Prof Tania Ajam (research project leader); Ms Deyana Isaacs and Ms Melissa Botha. Respondents were municipal managers and / or chief financial officers and / or managers delegated for the interview due to their context-specific knowledge and experience. Although the interview schedule provided a list of specific questions, as is typical with such expert interviews, each interview resulted in responses leading to follow-up questions and discussions that provided a wealth of information that were used to inform the content of the in-depth interviews. Respondents were introduced to each overarching question as well as its sub-questions, and could move around in their responses between sub-questions as further questioning reminded them of further relevant information relating to previous questions as well. Herewith an integrated summary of responses to each of the three overarching questions. The interviews were conducted in typical case study semi-structured format with data analysis done through analytic induction, and corresponding responses from different case interviews are clustered together to create a composite view, rather than to provide summaries per respondent. A specific municipality is only acknowledged where an important aspect is mentioned, and we considered that it can only be appreciated in the unique context of the particular municipality.

6.1.1 Overall municipal financial and operational sustainability in the Western Cape

Overall municipal financial and operational sustainability refers to the ability of a municipality to sustain its current spending and revenue policies while delivering on its mandate and meeting its financial obligations, without threatening solvency or default. Respondents were asked to rate themselves on a scale between -3, through 0 to +3, with -3 reflecting very poor prospects, 0 keeping heads above water and +3 very positive prospects. They were asked to rate themselves just before and then during the Covid-19 pandemic and its concomitant restrictions and also do explain the main drivers of their rating.

None of the medium and large local municipalities rated themselves below zero. Amidst the constraints on the sources of revenue and increased expenditure due to Covid-19 restrictions, the respondents indicated a decline in financial sustainability as rated on the scale, but not to the extent that it could not be managed. The drivers of the relatively positive situation include a stable and symbiotic relationship between communities, council, the political executive and senior management as well as good teamwork amongst senior management to find the right balance between service excellence and financial restraint, based on reliable systems and long-term planning. City of Cape Town also attributed their +3 rating to having cleaned up their tax base data and migrating to extended e-services prior to the pandemic. However, their positive rating came qualified: The pandemic may have triggered or accelerated the necessity to take difficult decisions regarding strategic positioning and structural arrangements.

Obviously, the biggest impact of the pandemic on all municipalities may be delayed due to continued economic decline and increased unemployment. It would be wrong to conclude at the time of writing the report that the sustainability effects of the pandemic have been limited.

In spite of a relatively optimistic outlook, in all instances respondents cautioned against increasing demands to service externally induced expectations such as unfunded mandates, regulated prices and compliance and governance regulations. The bigger the municipality, the better the ability to absorb more of these, but obviously, it still detracts from using resources for basic service delivery. This warning, flagged here, served to inform the themes of the in-depth interviews and will not be further discussed in this section.

This same positive outlook referred to above is not present amongst small local municipalities. Two of the three interviewed already rated themselves negative before the pandemic and financial and operational sustainability ratings went down as result of the pandemic. The one small municipality still rating themselves above 0, was rather negative about the prospect that declining sustainability trends could be reversed. The drivers of this negative outlook are not only that these municipalities have a small revenue base, but they share the common characteristics of being rural, which impose various constraints to be considered in the next subsections. The combination of the drought and the pandemic, rather than only the pandemic, increased indigence levels due to reliance on agriculture as main economic activity. Even bigger municipalities recognised that the drought and pandemic lockdown resulted in a blow due to reduced economic activities and tourism (and the absence of students as significant spenders in the case of Stellenbosch) and concomitant increased indigence, but they had a bigger range of options to absorb the shocks. In addition, for small municipalities, the burden of externally induced expectations, the inability to invest in large infrastructure capital projects that could unlock future revenue opportunities and the inability to attract and afford professional staff who would enhance their capacity, limit prospects and serve to create a bleak outlook for financial and operational sustainability.

District municipalities provided fewer clear-cut commonalities that could be linked to overall financial and operational sustainability. Of the three interviewed, one rated its financial and operational sustainability as extremely positive, one as 0 and one negative, at -1! Some of the factors contributing to these diverse outcomes include prudent financial decisions in the past which resulted accumulated savings, whether the district performs agency functions and the property portfolio of the district, and how well they have contained personnel as a percentage of total spending to increase their disposable income. The positive rating came from the district municipality that fulfilled the function of managing the water concession for its local municipalities. Clearly, the extent to which district municipalities are cash-back, grant dependent, make them vulnerable under current circumstances characterised by increasing demands to service externally induced expectations. All three municipalities expressed concern that grant allocations do not keep up with these growing demands.

6.1.2 Achieving Minimum Efficient Cost (MEC)

The Minimum Efficient Cost for a municipality is the least possible cost incurred for the current basket of services and business model, below which service delivery will be compromised. Actual expenditure in a municipality may firstly be higher than its MEC due to inefficient, unproductive, fruitless or wasteful expenditures, for example technical losses of water and electricity and unsound decisions such as overstaffing which are within the control of the municipality.

Secondly, costs may be higher than the MEC due to externally induced costs not fully within the control of the municipality, but still resulting from decisions by the municipality, for example cost of personnel. Employment is a decision of the municipality taken to ensure productivity, but centrally bargained salaries, benefits and other conditions of service are protected and controlled by stakeholders and systems outside of the control of the municipality. All municipalities are subject to these externally induced costs, but not all municipalities have the same levels of productivity. Respondents were therefore specifically prompted to comment on costs relating to political structures, administrative overheads, and municipal debt servicing as such externally induced factors.

Thirdly, municipalities will have different MEC's due to factors such as varying prices (which may differ between coastal and inland municipalities, urban and rural CPI) and other cost disabilities outside the municipality's control, for example distances, population density and geography. In addition, although all municipalities may be subject to externally induced costs such as costs of compliance (for example audit costs) and agency services as potential un(der)funded mandates, the regressive impact of such costs hurts smaller municipalities more than larger municipalities.

The second set of questions therefore endeavoured to determine whether the responding municipalities apply deliberate tactics or tools to achieve Minimum Efficient Cost and to identify (1) which internal and (2) externally induced factors impede achievement of MEC or cause emerging risks for maintaining MEC, or (3) serve to increase the MEC.

Respondents of all municipalities indicated that they do follow cost containment guidelines, directives and tactics. However, the small rural municipalities are at a huge disadvantage. Cost containment for them includes replacing dysfunctional equipment with second hand equipment procured cheaply from other municipalities and reducing the use of consultants that were appointed to fulfil functions of professional staff which the municipalities failed to attract and attain as mentioned before. Clearly, both examples illustrate that capacity to deliver is compromised with such cost containment responses. National norms and standards (for firefighting, municipal health, containing noise pollution and law enforcement, for example) increase MEC, but compliance or meeting the set norms is beyond the means of these municipalities. In addition, they have very long service delivery distances and spread out settlements that require multiple service generation plants that are inefficient due to lack of economies of scale. The COVID-19 pandemic and lockdown increased costs. Sanitizer, masks and personal protection equipment, deep cleaning when staff became infected, food and water to homeless communities (Laingsburg) are costs only partly offset by the national grant to municipalities. Reporting costs on the accountable use of these grants became an added burden.

However, one positive outcome of the pandemic, which have helped to offset additional costs occasioned by the pandemic is that all municipalities confirmed substantive cost savings due to replacing subsistence and travel costs for attending time consuming face-to-face meetings with online synchronous meetings. The pandemic has also opened the eyes of managers to the possibility of reduced accommodation costs with work-from-home possibilities and even reduced personnel costs with smarter work methods born out of necessity. Working from home may also make use of shared services (e.g. a town planner) feasible for small municipalities, by eliminating the need for resettlement and reducing transport costs.

Medium and large municipalities and the metro not only benefit from a bigger revenue base that makes more sophisticated capacity, life-cycle efficiency decisions and economy of scale possible, but they can also afford to engage in more sophisticated cost containment exercises, supported by information and communication technologies and in-depth data analytics as well as long-term modelling exercises.

None of the local municipalities are in favour of any forms of network governance, even though theoretically, they offer enhanced economy, efficiency and effectiveness in the international experience. Without reverting to an in-depth and comprehensive definition of network governance, or rather "networked community governance", it is sufficient to explain that it is a model of public governance embedded in public value theory. It recognises that circumstances are complex, diverse, continuously changing, volatile and prone to risk. Therefore, in order to achieve the desired public value, managers must amongst others create an "authorising environment" by, "building and sustaining a coalition of stakeholders from the public, private and third sectors (including but not restricted to elected politicians and appointed overseers) whose support is required to sustain the necessary strategic action". But, more daunting still in the South African municipal context, build operational capacity by, "harnessing and mobilizing the operational resources (finance, staff, skills technology), both inside **<u>and outside</u>** [own emphasis] the organization, which are necessary to achieve the desired public value outcomes" (Benington and Moore, 2011: 4)[3]

Public-private partnerships, shared services and joint service delivery are particular examples of networked governance. They were not rejected because respondents do not understand their benefits, but because cumbersome legal processes outlined in the legislation and externally induced controls make them cumbersome to implement and sustain. The strong negative opinions expressed by all local municipal respondents served to flag this as matter to be further explored in the in-depth interviews.

Where joint services are necessitated by externally induced prescripts such as is the case with landfill management, once again the small rural municipalities suffer the consequences of increased service distance costs. However, not only the small municipalities, but all expressed concerns about the sharp increase in waste removal costs due to environmental realities. Increased cost due to regional waste management, will result in increased waste tariffs which will limit space for increasing other service tariffs.

Costs relating to political structures, administrative overheads, compliance to prescripts (for example auditing and procurement processes) and agency services as potential un(der)funded mandates are burdensome and respondents from small, rural municipalities claim that prescripts are insensitive to their constraints. Two examples were given in the interviews: With the decision to appoint two additional councillors in a small municipality, came unaffordable additional costs. The cost of councillors, together with their office support staff came an increased wage bill and increased operating costs. The cost of developing and also operating MSCOA has been highlighted by all respondents. Small municipalities felt that they did not receive adequate MSCOA implementation support from provincial and national treasuries. A particular developmental responsibility highlighted by all respondents as seriously compromising MEC, is low-income housing. Even though the grant allocations may cover capital development costs, such grants do not cover administrative costs and costs related to servicing the inevitable increase in indigent households. This suggests a disjoint between indigent housing capital grants and the operational funding in the equitable share which is dependent in infrequently updated census data. This pressure to spend more on social services tend to increase in the period just before local elections. We also flagged the involvement of municipalities in social development as matter to be further explored in the in-depth interviews.

District municipalities are also compelled to apply cost containment measures as increases in grant allocations do not keep up with cost increases. Due to limited options, maintenance of capital assets and infrastructure is compromised, as reported by two of the three district municipalities interviewed. One district municipality reported that their attempt at using a public-private partnership for developing a regional landfill site was thwarted when the private partner could not fulfil its commitments. The initiative has first been delayed, and eventually cancelled due to the private partner's inability to continue as a victim of the Covid-19 disaster.

[3] Benington, J and Moore, MH. 2011. "Public Value in Complex and Changing Times" in Benington, J and Moore, MH (eds). **Public Value. Theory and practice**. London: Palgrave Macmillan.

The personnel costs as proportion of total expenditure are high and increasingly challenging to afford as externally induced annual increases are not sensitive to local conditions. It is also difficult to attract and retain professional staff.

6.1.3 Achieving Maximum Fiscal Capacity

Maximum Fiscal Capacity (MFC) refers to the maximum potential revenue a municipality can derive from its revenue bases. These bases may change over time and are influenced by factors outside a municipality's control, for example the level, nature, spatial distribution of economic activity, property markets and land tenure as well as the concentration of indigence, migration and other socio-economic factors. The actual revenue of a municipality may fall significantly short of the MFC if a municipality does not exert the requisite fiscal effort to fully exploit its revenue collection potential.

The third set of questions therefore endeavoured to determine whether the responding municipalities apply deliberate tactics or tools to achieve MFC from its existing revenue bases, but also to grow these existing bases and establish new revenue bases. We also wished to determine what external factors impede or emerging factors threaten achieving and increasing MFC.

Revenue enhancement, as is the case with cost containment, is a frequently communicated and well received concept, but not necessarily as clearly operationalised under all local conditions as communicated. Revenue enhancement relating to achieving and maintaining MFC from existing revenue bases includes preventing losses, a tariff structure that would maximise revenue, maintaining data integrity on accounts receivable, timeous billing, short turnover times for accounts receivable, and a high debtors collection rate. Local municipalities in the Western Cape are quite aware of this and engaged in ongoing initiatives in this regard. In many Western Cape municipalities revenue collection rates were therefore high before the pandemic and despite decreases of approximately five percent during lockdown, remained surprisingly high, especially for those municipalities which opened revenue offices early in the lockdown. However, the pandemic has resulted in an increase in indigence and at the time of the interviews, it was too early to project the longer-term impact on the annual debtors' collection rate of medium and large municipalities and to determine to what extent the tax bases me have been adversely affected. The City of Cape Town surprisingly did not experience a reduction of revenue as was expected as a result of the pandemic. They ascribed this to the comprehensive exercise prior to the pandemic to clean up data on properties, only billing property owners and not their tenants and holding property owners liable for the payment of municipal accounts, improving data on consumption, the move to greater service automation, reducing waste and an appropriate indigent policy and indigent management practices. Small rural municipalities are at a particular disadvantage. They report high levels of indigence and substantive increases in indigence due to the pandemic. In addition, the advance in small-scale embedded generators (SSEGs) inevitably heading towards feeding electricity back into the grid (buy-back) is considered a threat to these municipalities. Their clients with SSEGs typically do not get entirely off the grid but revert when they are unable to generate. Therefore, municipalities have to retain the capacity to meet their demand, while forgoing much of their revenue. Furthermore, affluent residential clients get off the grid, leaving only the indigent behind.

District municipalities with their dependence on grant funding, are not as directly subjected to revenue enhancement relating to achieving and maintaining MFC from existing revenue bases. Unlike the rest of the country where the districts have more capacity than the locals and supply electricity on their behalf, this does not take place in the Western Cape. All district municipalities have a roads agency function and West Coast District Municipality uniquely has a water concession. None of these may have been adversely affected by the pandemic, but Garden Route District Municipality indicated that expected revenue from camping sites and big sporting events were not realised due to the pandemic.

Prospects to grow existing revenue bases through deliberate local economic development initiatives vary among municipalities. The Western Cape is blessed with conditions conducive for agriculture and tourism, which forms strong bases for revenue enhancement. However these are also sectors adversely affected by disasters and combinations of disasters such as the drought and pandemic. Municipalities experiencing in-migration of more affluent households are investing in expansion of residential and business infrastructure. The small rural municipalities each have their own unique opportunities but lack the financial ability to invest in big capital projects to unlock these opportunities. District municipalities do not have the same scope as local municipalities to grow the revenue base, especially as obligations such as environmental health and fire services are quasi-collective and subject to many externalities that compromise full cost recovery.

Prospects to develop new revenue bases are limited and we found little evidence amongst local municipalities that they actively pursue initiatives, apart from some consideration to cash in on data as sought-after product. One respondent suggested that fibre data provision needs to be designated as a municipal service. Apart from the City of Cape Town, even bigger municipalities have limited scope to invest in infrastructure that would unlock future growth and one respondent has indicated that in their case the capital investment in infrastructure for expected growth did create short to medium term challenges impacting on financial sustainability when the expected growth was delayed. Two of the three district municipalities indicated that they have ideas for establishing new revenue bases regarding provision of services to neighbouring districts, activating currently dormant services such as fresh produce markets, hosting regional sporting events, engaging in alternative energy generation and using a property portfolio to leverage revenue generation.

As has been mentioned in the previous subsection, the interviews revealed very little appetite for joint new initiatives between district and local municipalities, with strong resistance from local municipalities. They appear to be more receptive to changing the boundaries of jurisdiction to make local municipalities more financially and operationally sustainable, rather than to work across these boundaries in joint initiatives for enhanced sustainability. These views were conditioned by unsuccessful past attempts at shared services. Nevertheless, district municipalities did suggest that certain economic development initiatives, such as tourism may benefit from increased centralisation (or regionalisation) to comprehensively develop its potential for increased impact, while high-tech and capital intensive solutions such as construction of incinerators for solid waste management could also only be feasible at district level.

Questions about grant allocations as source of revenue did not reveal particular patterns of opinion, although small rural and district municipalities expressed views that the formula for allocation of the equitable share needs to be reviewed. One local municipality also felt that there is no policy predictability in the allocation of the various Provincial grants.

6.1.4 Conclusions drawn from first round interviews

Municipal financial and operational sustainability cannot be confused with short term liquidity. One way of maintaining short-term liquidity is to postpone investment in infrastructure that would ensure longer-term operational sustainability, especially to be able to continue sustainably amidst crises such as droughts and pandemics. This requires both resilience and agility. The Western Cape is not the ideal province to select cases for research to discover the depth and causes of the widely published distress in South African municipalities. Our interviews revealed that Western Cape municipalities so far have shown remarkable resilience, even after the devastating drought and amidst the most devastating pandemic and concomitant lockdown restrictions. This is partly attributable to strong and resilient financial and service delivery positions prior to the pandemic, and the competence, cohesion, continuity and experience of their management teams. In addition, the most resilient municipalities also ascribed their favourable financial and operational sustainability to executive maturity and stability and good working relationships between the officials and politicians.

There are nevertheless serious concerns about longer term operational and financial sustainability, mostly as a result of factors outside the control of the municipalities. The interview panel realised that more in-depth investigations are required to unpack these concerns. The interviews did not reveal widespread optimism for changing either the basket of services or the business models for providing these services and it raises questions about systems agility to face the increasing uncertainties. This matter was therefore flagged for more in-depth investigation.

The envisaged in-depth reviews, however, should not only take a closer look at constraining factors, but given that the various sustainability ratings and findings always have Western Cape municipalities at the top end of the national rankings, we also wanted to determine what is the recipe of success of these most financially and operationally sustainable municipalities in the country, and how they deal with the same constraints.

6.2 In-depth interviews to determine how specific constraining factors impact on municipal financial and operational sustainability

It is quite evident from the first round of interviews that small rural municipalities are flailing to keep head above water and where they still succeed, respondents were not too optimistic about their longer term future. They have been especially vocal about externally induced constraints and the fact that the formulae for grant allocations do not adequately take the impediments of being small and rural into consideration. Nevertheless, none of the local municipal respondents believed that changing either the basket of services or the business models for providing these services can work, again due to externally induced constraints. Even district municipalities felt that they could expand maximum fiscal capacity if circumstances would permit.

As indicated in Section 1, the objective of the in-depth interviews was to determine how court judgements, prescripts and compliance, labour regulation, external role players in municipal service delivery, intergovernmental grants and agency services, municipal structures and systems as well as the current basket of services impact on municipal financial and operational sustainability and how municipalities deal with it. Three municipalities, widely acknowledged for their financial and operational sustainability, volunteered for the in-depth interviews, namely, Cape Winelands District Municipality, Swartland Local Municipality and Hessequa Local Municipality. In addition, the interviews with two respondents representing the City of Cape Town covered both the first round interview questions and the in-depth questions. The fact that we could interview these municipalities, assisted in not only understanding the impact of externally induced constraints, but also how to navigate them – which would help to get pointers towards not only resilience, but also agility. In addition to the interview panel members of the first round interviews, Prof. Geo Quinot, amongst other a local government law and governance and supply-chain management researcher, strengthened our ability to engage rigorously with respondents about these issues. Interviews were conducted through quite lengthy Microsoft Teams sessions on 20 October (Cape Winelands District Municipality and Swartland Local Municipality); 2 November (Hessequa Local Municipality) and 11 and 15 February (City of Cape Town).

As with the first round interviews, respondents were introduced to each overarching question per factor as well as its sub-questions as set out in Annexure A and could move around in their responses between sub-questions as further questioning reminded them of further relevant information relating to previous questions as well. Again, the interviews were conducted in typical case study semi-structured format. Although where possible data analysis was done through analytic induction, and corresponding responses from different case interviews are clustered together to create a composite view, the in-depth interview questions elicited specific responses from each municipality and the unique context of each did play a bigger role. Both the creation of a composite view and of mentioning a specific municipality for unique views, necessitated that participants had to concur with our summaries before it could be released.

6.2.1 The impact of court judgements

The role of a judiciary separated from legislature and executive governments in terms of the "trias politica" doctrine to uphold the rule of law and maintain civil liberty is an undisputed democratic value. It guards just administrative action and combats irregularities. The reason for engaging with this factor first, is because several respondents in the first round of interviews indicated that recent judgements regarding land invasion and evictions as well as supply-chain management disenchanted them. From sustainability of finance and operations point of view it makes sense that these two issues came to the fore. Land invasions and evictions require spending of money not budgeted for and unforeseen management responses, similar to, for example dealing with the sudden lockdown regulations. It may also be (such as is the case in urban areas) that land invasions increased due to lockdown and the crippling drought. The three crises together could potentially be devastating for financial and operational sustainability.

Challenges regarding deemed irregularities in supply-chain management may impact as well: Whereas the Municipal Supply Chain Management Regulations (RSA 2005) calls for a policy framework providing for systems of demand management, acquisition management, logistics, disposal, risk and performance management, the intention is clearly to enhance and support financial and operations management. However, if court judgements would reveal circumstances where municipalities may have misinterpreted the Regulations, it could have the effect of discouraging them from considering changes in the current basket of services or alternative business models towards more agility, but rather to strengthen their own resilience. The overarching interview question was therefore, "To what extend are court judgements constraining municipal operational and financial sustainability?" and the discussion explored answers around the following sub-questions: "To what extent are you attuned to court judgements; To what extent are court judgements attuned to local government context?; How do judgements on land invasion affect you?; How do judgements on evictions affect you?; How do judgements on supply chain management affect you?; Any other specific judgements affecting you?"

One local municipality (Swartland, which is closer to the urban pull of a metropole) has indicated that court judgements do impact on their work, and from the experience of one of the two, judgements that are insensitive to local government context are challenging. Although the municipality did not have any specific recent court judgements against them, to ensure that they have good controls and systems in place to prevent adverse findings, cost money. Land invasion and housing backlogs as bigger problem are affecting financial sustainability and maintaining expected levels of service. Land invasion on private land and eviction orders have a ripple effect. For the municipality to provide space for settlement of the homeless and eventually housing opportunities not only require housing grants, but also rezoning of agricultural land. As action must be taken swiftly, it means that expenditures must be incurred for which no budget allocations are made. In the example quoted, expensive provision of new bulk services outside the urban edge which disrupts existing plans and capital budgeting had to be provided. Swartland also noted that while emergency housing was a local function, housing itself was a national and provincial function, and as such the additional costs should have been carried by the relevant departments rather than the municipality.

Generally, especially magistrates (local courts), give very little consideration to the wider financial implications of their judgements. The second local municipality (Hessequa, which is further away from urban pull) argues that by following the narrow legislative mandate of a municipality no adverse court judgements will occur. They do not have specific land invasion problems and have procedures in place to accommodate the homeless. None of the two municipalities have adverse judgements regarding supply chain management. In order to prevent adverse court judgements, very solid and tight internal systems are maintained, which are expensive to do, and by implication a conservative approach excludes options such as joint services. Although Regulation 32 of the Municipal Supply Chain Management Regulations (RSA 2005) provides for procurement of goods and services under contracts secured by other organs of state, the adverse findings regarding the use of Regulation 32 have been discouraging (Kwadukuza Municipality versus Skillful 1169 CC and Technologies Acceptances (Pty) Limited, 2017). Without exception, the sentiment expressed in both the first round and in-depth interviews was that Regulation 32 should rather be scrapped.

The City of Cape Town is different by virtue of size. Not only do they have the capacity to contest adverse challenges, but they also have the resources to absorb cost implications of adverse findings mid-stream. They can adopt particular positions and take a robust stand on it due to their knowledge base and sophisticated systems. This is the benefit of being a R54Bn organisation!

From a district municipal point of view (Cape Winelands), land invasion is not a problem, as the district has limited land for own use only and does not have to deal with evicted people. As is the case with the local municipalities, supply-chain management actions are strictly controlled to prevent irregularities. However, as stated, "Our job is not supply-chain, it is service delivery"! Strictly controlled supply-chain activities come at the price of reduced efficiency, with delays or non-acceptance of tenders resulting from Bid Adjudication Committee referring tenders back. Where the previous SLA (e.g. security services) lapses but bidders are non-compliant, assets are exposed to theft. The red tape and delays make doing business with municipalities very expensive, and this results in higher prices paid. Demand management may delay acquisition by up to two years, in which case prices have risen. SCM prescripts are more geared to urban markets and the Framework for Infrastructure Development Procurement Management (FIDPM) doesn't adequately take the local government operational context into account.

In rural areas, there may only be a single supplier in town, which makes obtaining more quotations difficult, and purchasing in Cape Town increased travel and personnel cost time for maintenance and operating the procured items – this issue has also been raised by rural local municipalities. Municipalities sometimes face a choice between incurring irregular expenditure and hence audit queries or compromising service delivery. For example, Cape Winelands suspended bid committee operations when they only employed three senior managers and therefore could not comply with the prescribed four senior managers on the bid committee. Now NT has changed the regulations to permit managers from other municipalities to participate. But if there are issues, accountability is unclear.

Cape Winelands pointed out that SCM Regulations are constantly evolving and National Treasury's guidance is often not clear, resulting in trial and error by the municipalities, which may differ from the interpretation of the Auditor General. Regulation 32 mentioned above was changed after established practices of 20 years, resulting in irregular expenditure. The municipality realises that specification writing and contract management and consequence management requires more sophisticated and expensive capacity, which they do not have.

The bottom line in this sub-section is that for all but the biggest municipalities, the care that should be taken to prevent irregular action that can be challenged in court and playing it safe in a dynamic environment not only requires more sophisticated capacity, but also lead to a strong tendency to follow the narrowest confines of the municipal legal mandate, which may not be conducive for longer term operational sustainability. This is likely to be exacerbated by the Public Audit Amendment Act which holds accounting officers personally liable.

6.2.2 The impact of prescripts and compliance

In spite of the autonomy of municipalities as sphere and units of government, they function under a comprehensively defined set of laws, regulations, policies, and are further directed by numerous norms, standards and directives and controlled through conditions attached to grant allocations. In this sub-section we refer to these collectively as prescripts. Although these prescripts progressively came about for good reason, namely to strengthen accountability, the cumulative burden of compliance may challenge municipal sustainability. It is accepted that the cost of non-compliance – including waste through irregular as well as fruitless and wasteful expenditure – also compromises financial sustainability, the question under investigation here is whether the cumulative burden of compliance to the prescripts may have reached a point where it too has become unsustainable. Prescripts are designed for worse-case scenarios, just like security control at airports, but can it be that prescripts are too heavy-handed to allow for good localised strategic and tactical management and stifle the innovations necessary for the kind of agility that all contemporary organisations require to survive?

In this subsection, we therefore report on the following questions: Which prescripts cause network governance options (shared services, joint services, PPP's) not to be viable even though it is widely promoted as alternative business model? How do prescripts impact on prioritization? Are prescripts by Statutory Authorities such as NERSA sensitive enough for sustainability? Are there specific laws that you want to highlight as constraining sustainability? Are prescripts on auditing constraining? It may be that prescripts are not sensitive enough to diverse localized contexts. We therefore also asked which prescripts are not formulated with sensitivity for local context. We also wanted to know whether it could be that it is not the prescripts that bring unsustainability, but how they are applied. Could the nature of oversight, rather than prescripts be a problem for sustainability? Should legislation separating responsibilities of political oversight, political executives and management be strengthened?

Both local municipalities interviewed indicated that they have established reliable systems designed to comply with prescripts. Although they actively participate in the dialogue around the burden of compliance, the pragmatic attitude is not to spend too much time on matters that cannot be changed. In responding to prescripts, good governance principles are applied. Both local municipalities therefore endeavour to achieve clean audits annually, which, together with following the correct steps for new initiatives, including engaging with communities, result in maintaining indisputably correct behaviour.

With regards to the role of prescripts in preventing alternative business models, again both local municipalities are willing to engage in such initiatives (for example Hessequa's public-private partnership for building a solar-powered desalination plant), but both are unequivocally against following a joint services option with other municipalities, as they consider it to bring no financial or operational benefit, and in fact may be more expensive, and add operational and financial risks that they cannot mitigate. It also add a bigger distance between local communities and planning processes. With public-private partnerships, the more sophisticated approach calls for well-informed transaction advisors and funding to package the project in addition to navigating through the complicated and protracted legal process and getting politicians on board. The establishment of rural Category A municipalities is considered by both to be preferable to joint services or the district development model.

In spite of the positive attitude reflected above, both municipalities acknowledge that prescripts reduce their freedom to provide what communities deem priority. Money, for example spent to pay audit fees and SALGA membership, cannot be used for addressing service delivery needs. Similarly, money spent on ensuring clean audits is lost for direct spending on service delivery. Such as vehicle replacement. Small municipalities are compelled to spend more on audit fees annually than on vehicle and equipment replacement. Prescripts by Statutory Authorities such as NERSA are not sensitive enough for sustainability, nor for specific local contexts. During the first round of interviews Swellendam respondents have indicated that tariff increases from ESKOM is increasing faster than municipalities are allowed by NERSA to recoup, which is eroding historic surpluses used for cross subsidisation. This is further exacerbated by load shedding. Prescripts such as relating to liquor control and expropriation assign functions to municipalities without consideration of the operational implications.

Prescripts that constrain financial and operational sustainability are indeed doing so due to interpretation as well as implementation practices directed by external authorities. The monitoring reports required by provincial departments are time-consuming and costly to complete. None of these contribute to delivering on strategic priorities and they do not support internal performance management. For this, own performance instruments are used and the data required generated from internal systems not aligned with the prescripts for external monitoring processes. In order to remain financially and operationally sustainable, especially amidst crises such as the Covid-19 pandemic and lockdown, require day-to-day responses based on dynamically changing circumstances and the externally induced reporting prescripts do not support this need.

The City of Cape Town, in spite of the ability to bring robust bargaining power as well as implementation capacity to the table when whatever now prescripts emerge, provided a view quite similar to that presented by the two local municipalities regarding prescripts that constrain financial and operational sustainability. The perspective provided is that Statutory Authorities have a silo view, each only focusing on their particular sector or resource, while the City must consider the total municipal account (TMA) and its impact on households. They do modelling, considering household consumption over the past year and historic trends, cutting across the suite (basket) of hard engineering and social services to obtain a 360 degree view of each consumer. Inevitably, the silo view and TMA modelling are not always reconcilable.

In the responses so far, it is evident that the burden of the magnitude, nature, interpretation and enforcement of prescripts is indeed challenging. However, we also wanted to know if specific prescripts relating to the separation of responsibilities of political oversight, political executives and management should be strengthened. In other words, whether there room for even more comprehensive prescripts in certain areas. Clearly from the responses provided in this regard, the clarity of understanding of separation of responsibilities and the stable, considerate and productive working relationships between members of council, the mayoral committee members and senior management is one of the most important contributing factors to the success of the municipalities interviewed here. Respondents acknowledged that should this good working relationships be absent, and each group pursues own interests, success will no longer be possible. The impact on financial and operational sustainability is a gradual decline over time which is accelerated by crises such as the drought and the Covid-19 pandemic. The focused use of available resources where it matters most for communities is only attainable when these three stakeholder groups work together. Both local municipalities reported that realistic longer term financial and operational planning with buy-in by these stakeholders, resulting from open and honest communication, has been critical in their sustainability. It can be deduced that leadership and experience are extremely important, regardless of whether prescripts are strengthened or not, but there may be room for strengthening or at least consolidating prescripts in this regard.

The team of respondents from the district municipality echoed sentiments similar to these reflected by the two local municipalities. However, they sense deteriorating relationships between municipalities which have had clean audits and good governance ratings. Instead of "reasonable assurance", there is the perception that over the last two years, there is a "concerted attempt to catch you out". If the focus is on reasonable assurance and deficiencies, it adds value, but with the current approach, the municipal response is "not to admit anything and fight to death". Joint initiatives are considered unviable due to restricting prescripts and even though they are more positive about the district development model (naturally), they too argued that such a model will require even more sophisticated capacity. They too consider reporting requirements of provincial and national treasuries to be excessive and the MSCOA prescripts as unattainable, with both the development cost and cost of populating it challenging. In general therefore, capacity for compliance is falling short.

6.2.3 The impact of labour regulation

Although nationally-imposed labour-related prescripts serve the purpose of ensuring equity and preventing abuse, we have explored its impact on financial and operational stability of municipalities. The importance of the HR functioning as executed by managers and the HR division in a municipality cannot be over-emphasised. They must ensure that service delivery capacity is maintained and enhanced by appropriate appointments and staff development. However, as remuneration is directed by national initiatives, there is potential that the wage bill can increase faster than municipal revenue, especially when revenue growth is subdued by crises such as the drought and the Covid-19 pandemic. This then results in declining labour productivity. We therefore wanted to determine to what extend labour prescripts that must be adhered to, constrain municipal operational and financial sustainability. The discussions revolved around three questions: What employee-related impediments to sustainability do externally-induced prescripts cause? Should a municipal norm be created for productivity ratios? Will a single public service and Public Administrative Management Act, controlling remuneration, be a solution?

Both local municipalities report that they deliberately and actively manage labour relations. They are not concerned about the cost of labour and they do not experience a decline in productivity. Although a uniform productivity norm may be difficult to prescribe, given the varying circumstances amongst municipalities, the idea of monitoring productivity is supported and practiced by both. Neither agree that a single public service with remuneration controlled nationally is a solution, given the unique capacity demands for local government in general and the diverse capacity challenges faced by each individual municipality and given the acknowledged unproductivity of the public sector.

The stability between stakeholders as discussed in the previous subsection also extends into the realm of employees. Where top management is willing to engage constructively and systematically with organised labour as well as with employees, desirable productivity levels will be maintained. If organised labour representatives and employees are involved in resource allocation decision making and are given responsibility for the resources they use, a greater sense of ownership develops. The cost of labour as component of operational and to a certain extent capital expenditure is apportioned to service costs, which brings greater internal awareness of productivity. In the final instance, the philosophy reflected is that of, "train them well enough so that they can leave, but treat them well enough so that they want to stay"!

City of Cape Town respondents held a similar view. They also gave testimony to the stability of the workforce and added that they were engaged in exercises to imagine "the future of work" even before the pandemic, but the pandemic accelerated the process. Many employees will carry on working from home after the pandemic, because of productivity gains and cost of employment reductions. Nevertheless, that envisaged future of work will also require bold and unpopular decisions. Employee-related costs currently contributes between 32 and 36 percent of the budget and it is considered to be too high.

From a district municipality perspective, there is some confirmation that the wage bill is getting out of hand. It was mentioned that productivity reviews are met with resistance and suggested that national legislation should require it. Although there is understanding for the rationale behind a single public service to promote employee movement between spheres of government, differentiation of the nature of work done and the need to remunerate accordingly calls for greater flexibility. Nationally-determined remuneration prescripts are to the detriment of smaller municipalities.

6.2.4 The impact of external role players in municipal service delivery

The Constitution, MFMA and the Municipal Systems Act require the maintenance of a close, cooperative relationship within, and between, the different spheres of government, especially in terms of planning, budgeting and financial management, as well as in areas of service delivery operations. Legislation provides a role for national and provincial government to support, to build capacity and to monitor municipalities and prescribes mechanisms for sector-specific regulators such as the National Energy Regulator of South Africa (NERSA) and parastatals such as ESKOM and other public entities to engage with municipalities. In addition, the South African Local Government Association (SALGA) is constitutionally mandated for local government oversight to ensure that local government realises/achieves spatial justice and social cohesion.

National Treasury prescribes regulations, frameworks, budget formats, inflation limits, and other information to ensure uniform norms and standards for implementation. Other national government departments also have a key role to play in policy development and in the execution of programmes in municipalities. The Department of Cooperative Governance have an overarching responsibility for strengthening cooperative governance, while departments of Water and Sanitation, Mineral Resources, Energy, Transport and Human Settlements play direct roles in monitoring sector-specific outcomes and service delivery.

Provincial treasuries must, among other duties, promote the object of the MFMA within the framework of cooperative government, and they must assist the National Treasury in enforcing and monitoring and to assist in preparing the budget. Similarly, the provincial department of local government has a role to play in promoting and strengthening cooperative and local governance, while each of the other provincial departments play roles in monitoring sector-specific outcomes and service delivery, with a view to ensure province-wide service enhancement.

Although all of these external relationships serve to promote the interests of society and maximise public value and promote the development of local government capacity, it is possible that the cumulative engagements from each external role player with one single municipality can become time-consuming, onerous and costly. This possibility is further increased in times of crises, such as the drought and the Covid-19 pandemic and it is also affected by dynamic policy issues occurring within the realms of each of these role players. This sub-section therefore reports on the question whether services and support by external role players are effective for municipal operational and financial sustainability. Discussions were guided by four questions: Are the current roles of national and provincial departments in supporting municipal sustainability efficient and how should it be enhanced? How do regulators such as NERSA and Water Boards impact on municipal operational and financial sustainability? How will restructuring of Eskom and the electricity industry impact on municipal financial sustainability? How does SALGA impact on municipal financial sustainability?

The responding municipalities indicated that the engagement and support by external role players are indeed cumbersome and demanding, as a result of the silo-nature of the engagements, causing endless repetition of questionnaires to be completed. They do experience "questionnaire fatigue". The suggestion is that provincial department support is hampered by inadequate local government experience. The two local municipalities indicated that "they do their own thing". "We are not over eager to attend seminars and talk shows for days on end. We make use where we can, but we do our own thing". The district municipality feels that in some instances engagement directly with national departments would be more effective than working through provincial departments as intermediaries. The discussions in general do suggest that the departmental oversight model should be reconsidered to ensure a more integrated approach and smoother transfer of available grants, and better alignment between integrated local and integrated (as opposed to fragmented) provincial development planning.

The City of Cape Town's response relating to the silo perspectives of external role players has already been captured in Section 3.2 and the reality is that the silo view of external role players to the extent that they provide support and total municipal account modelling by the municipality are not always reconcilable. In addition, examples of breakdown of intergovernmental cooperation and integration of services occur. Two very specific publicly detrimental examples were mentioned: The first example mentioned related to the long queues where people were literally waiting for hours to renew motor vehicle licenses during the pandemic drew much criticism against the municipality from the public, but the municipality who is not the owner of the National Traffic Information System, has too little discretion over the that system and resources to introduce much needed systems improvement, or for that matter, to introduce a totally different licensing system not reliant on issuing of a paper licence disc. The second example mentioned relates to the registration of property. Whereas the City has already successfully automated their processes and strongly advised the Deeds Office in their much later initiatives to ensure that when they procure a new Deeds System that the Deeds System is properly integrated with those of the municipalities. This was not done, resulting in systems and processes that remain fragmented. It was also mentioned that the City did not receive any allocation from Provincial Government relating to the pandemic, but did allocate R900m for pandemic-related expenditure, mostly allocated to primary health services.

None of the responding municipalities answered the second question about regulators or the third question about restructuring of Eskom directly (partly because the particular issues have also been discussed in Section 3.2), but from the ensuing discussion, one local municipality (Hessequa) indicated that they work towards being carbon neutral and independent from Eskom and self-sufficient as water provision is concerned (amongst others by installation of a solar-powered desalination plant). The restructuring of Eskom provides opportunity to pursue options that can deliver on sustainability beyond only financial and operational sustainability. With regards to SALGA, no animosities were expressed, but reservations about the value added, given the membership fees payable, were raised.

6.2.5 The impact of intergovernmental grants and agency services

The transfer of centrally generated revenue to municipalities in the form of an equitable share and conditional grants, and the assignment of mandates by other spheres of government for municipalities to perform services on their behalf, are part of cooperative government. However, given responses during the first round interviews, we were interested to extract more information on how the arrangements around these impact on finance and operations in a municipality. We wanted to know whether grants, agency services and support are effective for municipal operational and financial sustainability. We explored this topic by way of the following questions: If not so, how should grant allocation criteria be altered to be more equitable? How should grant allocation for mandates be structured to prevent underfunded mandates? Can unfunded or unfunded mandates be challenged? How does low income housing impact on municipal operational and financial sustainability? What social development functions do you perform and how are these affecting sustainability? Specifically for the district municipality: How do roads agency services impact on municipal operational and financial sustainability?

Both responding local municipalities indicated that the equitable share allocations are adequate to finance implementation of their indigence policies, even though, in the case of Hessequa, a third of households are indigent. However, both indicated that MIG allocations are inadequate, which can be ascribed to using incorrect data for apportionment, and too restrictive. It should be extended to include infrastructure maintenance as well. Both municipalities also indicated that various mandates are indeed underfunded. They viewed the proportion of income from motor vehicle-related services to be inadequate and not supported by a service level agreement. The servicing of low income housing beneficiaries and household support and early childhood development are not funded. The provision and administration of food parcels, although it was a function of the Department of Social Development, but only a small portion of the needy that applied were helped, so definitely the aid provided by the municipality is another example where the survival of communities depended on the unfunded aid by the municipality.

The City of Cape Town respondents also confirmed that underfunded mandates are contributing substantively (R1.5bn) to the operating account. Primary health services staff budget (R800m), libraries staff budget (R400m), maintenance of provincial metropolitan roads and law enforcement (Leap Programme) that are only subsidized in the first three years are such services mentioned. These services cannot be handed back, as there will be "downstream" negative externalities.

To the extent applicable, the respondents from Cape Winelands District Municipality echoed the responses given by the local municipalities. Grant allocations did not keep track with cost increases. The municipality provides a wide range of rural social development services, which make up a substantive proportion of the budget. It includes infrastructural services such as ablution facilities, upgrading, lighting, bus shelters and sidewalks, sports field, vanity kits to school girls linking with social development, aged and youth. They also provide assistance to small businesses – funding, skills and support for local economic development. Awareness programmes, sport, recreational and early childhood development are also provided.

With regards to the newly allocated roads function rendered on agency basis on behalf of provincial government, the pressure is on to increase the staff component to provide a satisfactory level of service, but already it takes up 60 percent of the salaries component of the budget. As agency fee agreements are not gazetted and can be chopped and changed, it intensifies municipal risk. When the function was transferred, resources did not follow the function. It will require substantive additional funds to appoint the necessary staff for adequate capacity, which will definitely affect sustainability. There is a pressing need to consider this issue not only from technical point of view, but a "whole-of-business" point of view. Currently, the municipality does not foresee that this agency function offers prospects to become an important revenue generation function for district municipalities in future.

6.2.6 The impact of municipal structures and systems

Municipal structures and systems are subject to well-delimited prescripts, as was partly explored in sub-section 3.2. Whereas the focus in sub-section 3.2 was on the impact of the prescripts, here we consider whether the municipal structures and systems are effective for municipal operational and financial sustainability? We specifically focused on the relationship between local and district municipalities and the ongoing processes of renewal. The particular questions that guided the discussion, were: How are district service systems impacting on municipal operational and financial sustainability? (e.g. regional waste); What are the unintended operational and financial consequences of proposed amendments to Municipal Systems, Municipal Demarcation, Municipal Structures and the District Development Model? Should district municipalities rather than local municipalities do IDPs? Should agency services for socio-economic development be transferred to District Municipalities? Should District Municipalities be given more regional economic development responsibilities in order to take on bigger and more profitable capital projects that cannot be done by Local Municipalities?

The intention behind these questions was to explore, in the spirit of the proposed District Development Model, whether that model should be used as vehicle for comprehensive district development, thereby causing de facto rural metros through networks of municipalities all working towards integrated and shared spatial, economic and social development objectives. Both local municipalities rejected the idea, although both were in favour of the establishment of rural Category A Municipalities. Both argued that they are in the "people business" whereby close and continued interaction with communities is a vital ingredient for success. They argued that the District Development Model would create greater space between local residents and the mechanisms ensuring integrated service delivery and development. There is room for regional initiatives such as waste management, but a "one plan fits all" is not desirable for social development. One response indicating the skepticism was to suggest that the housing function should be given to district municipalities and then see how they cope. The point made is that housing is not a function in isolation, but can only result in socio-economic development if it forms part of integrated with all other services.

The responses from the District Municipality partly echoed that of the local municipalities. The difference between a Category A Municipality and the District Development Model is that Category A Municipality has one executive authority and one legislature and one set of systems, while in a district there are many - that are potentially irreconcilable. The high level of politicization of socio-economic development exacerbates the problem. However, there is room for bigger district-wide economic development initiatives and shared systems development (ICT included for better management of big data) if all municipalities can come to an agreement about these.

6.2.7 The impact of the current basket of services

It is inevitable that the discussion in this sub-section overlaps with the previous, as judgements as form of law-making, prescripts, the national labour regime, external role players, intergovernmental relations and municipal structures and systems all relate to the basket of services typically offered by a municipality. The question explored here, namely, how the current basket of services can be sustained operationally and financially, was derived from the responses from the first round interview questions relating to minimising costs and maximise revenue. The intention was to determine whether further "fine-tuning" is possible, and where practices, whether it enhances financial and operational sustainability. The discussions revolved around the following: How can ring-fencing, zero-based budgeting, more equitable overhead and indirect cost apportionment impact on municipal operational and financial sustainability? These are techniques that highlight and reveal more accurately the cost structure of a service at different levels. What are the limitations and negative externalities of cross-subsidization? Cross subsidization may be a convenient way to transfer some costs of services with less price elasticity, but simultaneously cause reduced cost awareness in decision making. What societal (external) and basket of service (internal) factors determine a minimum threshold size below which a municipality cannot be sustainable? Any service plant has a minimum number of units below which fixed costs cannot be sustained. How can smaller local municipalities finance big infrastructure projects that will grow revenue base? This serves to explore how a municipality with limited revenue can invest into assets that can grow its revenue base. How can technology further reduce costs and grow revenue base? This serves to explore whether the explosion of new technologies have the potential or are already enabling municipalities to enhance financial and operational sustainability.

Both local municipalities indicated that they apply techniques to reveal real costs of services, and contrary to the feedback during the first round interviews, they consider MSCOA to assist in this regard. The district municipal respondents indicate that there is room for more sophisticated costing and more equitable overhead cost allocation. All respondents do, however, confirm that external prescripts in the various forms discussed in previous sub-sections do serve to restrain the use of more innovative techniques. Nevertheless, the meticulous management of costs keeps them sustainable. This ability to retain sustainability through meticulous management raises the question whether there is even more room to reduce costs, should the current pressure be increased. We need to flag the possibility that the level of pressure on financial and operational sustainability correlates with the meticulousness of management in a successful municipality, meaning the bigger the crunch, the leaner and fitter for purpose the municipality becomes! It is evident that municipalities with greater responsibility to live within their means by balancing revenue and expenditure and not being bailed out by grants keep on doing that even when disasters such as the pandemic strike. The balancing act as continuous process involving both short term adaptation and long term financial planning is an important contributor to financial and operational sustainability.

However, Swartland indicated that they have reached that point beyond which the above will not hold true unless they can come up with new solutions should financial and operational sustainability be threatened in further. Costs that are discretionary have already been pared to the bone by years of cost containment, but where cost drivers outside the control of the municipality are driving cost increases, it becomes a serious challenge to sustainability.

Currently, cross-subsidization is essential, but one should continuously strive to ensure that tariffs do cover all costs. Maintaining the balance between the need for cross-subsidization and the need for appropriate cost structures is making a big contribution towards sustainability, but it cannot be done without mature political oversight.

The City of Cape Town responses also strongly indicated that continuous "fine-tuning" of systems remains a necessity, whether there is a crisis such as the drought or pandemic or not. The crises nevertheless handed them a very particular "deck of cards" and challenged them to review the structure of the long-term financial plan. This resulted in updates of operational plans, business plans and sector plans. Contracts and programme and project management systems were amended as a result. These are certainly manifestations of agility. They also emphasised that full cost recovery remains the premise for tariff setting, which depends on credible data and in-depth understanding of cost (and revenue) behaviour. This then not only enables them to maintain the most productive tariff structure, but also to create space for building up some reserves towards greater resilience. Cross-subsidization is therefore not a technical decision where it occurs, but rather a political (value) decision taken with consideration for maximising positive outcomes.

There are still options, even for small municipalities, to engage in projects that will expand its revenue base or create new revenue-generating opportunities. Hessequa is currently involved in a project to develop an Information Centre for the Blombos Heritage Site. A trust has been established, and the project is done in partnership with the Provincial Government and also offers opportunity for further partnerships. This development is not costing the municipality much, but has great potential for creating archaeological tourism. In addition, with relatively small infrastructure investment, Stilbaai has become a sought-after retirement destination. Investment in establishing optical fibre networks, which make a town even more attractive as "Zoom Town", does not have to cost the municipality anything. It is important though, added respondents from Swartland, that the municipality should also rethink its own systems. Accelerated approval of building plans or development applications and generally reducing red tape, for example, makes it more attractive for businesses to invest in a town.

6.2.8 How to survive financially and sustain operations

As was already observed during first round interviews, only the small municipalities consider themselves already to be financially and operationally unsustainable over the medium term and the pandemic and lockdown may have served to accelerate their demise. District municipalities with their extensive reliance on grant-funding and cash-back funding also indicated increasing challenges to make ends meet. These realities are concerning and clearly needs to be addressed. However, more surprising is how many municipalities in both rounds of interviews still considered themselves as sustainable while the reality in other provinces is that most municipalities are not sustainable any more. The discussions during both rounds of interviews therefore continuously turned towards the positive question of "what makes you sustainable in spite of all the challenges as revealed in the report so far?" In this subsection, we provide a short list of the answers:

- An irreproachable attitude against corruption. It speaks for itself – corruption reduces efficiency. More resource input is required to retain the same quantity and level of service output. There will always be loopholes providing opportunity for self-enrichment in the complex business of local government, but whenever revealed, it must be acted upon decisively.
- Grant-dependence and/or cash-back based financing does not provide an incentive to become more efficient in the continuous offensive to maintain sustainability. Municipalities that rely on remaining sustainable through selling their products and services engage in long-term financial planning, sophisticated data-collection and financial modelling, creative searches for making the right capital investments to remain sustainable, continuously improve service delivery and support systems and reduce waste, continuously search for ways to increase productivity and adapt to changing circumstances.
- A "mature" council and political executive understanding the bigger picture and providing the leadership necessary to take decisions that may be unpopular in the short term, but deliver better results for all in the medium to long term.
- Continuous and meaningful engagement with communities. Individual residents, households, community-based organisations and local businesses must not be allowed to experience the municipality as impenetrable fortress.
- Positive working relationships between council, political executives and senior management, built around long-term plans enjoying the buy-in of all.
- Effective, efficient, reliable and responsive financial and operational policies and management systems that are resilient enough not to fail when under pressure, but also agile enough to adapt when crises strike.
- Experienced senior managers that know the business of a municipality through-and-through and are working together as a team to prevent a silo management culture from developing.

- Investing time, resources and innovation and building partnerships to ensure the success of strategic initiatives that will make the municipality attractive for living and working in.
- Competent staff enjoying market related remunerations and satisfactory working conditions, with HR Recruitment systems successfully resisting jobs for pals.

6.3 Conclusion: Interpretation of interview results

The results from the interviews with several municipal experts dealing with the realities of keeping municipalities afloat on a day-to-day basis, provided some valuable insights. Many of the responses captured here can be viewed as "the same old story" repeated by the same people that have also responded to many other initiatives and dialogues about sustaining municipalities. It is also possible to interpret the positive financial and operational sustainable position of most responding municipalities as indication that they will always cope (and complain) and therefore the status quo can be maintained.

Such interpretation can be fatal. The feedback captured in this report indicates that most local municipalities, with the exception of the smallest, have so far succeeded to remain sustainable through their resilience and agility. However, there is a sense from the majority of respondents that the status quo will not be enough going into the future. The pandemic may have just accelerated the inevitable, namely that externally induced constraints, the current basket of services for local and district municipalities and arrangements between them, the current business model by which these baskets are operated, the current grant allocation models, the current arrangements around agency services and even the current demarcation of boundaries, especially in the case of small municipalities, need drastic revision.

This interviews report represents but one part of the research, and in subsequent reports, will be integrated with the information generated from the other methods of data collected for this research project.

7 Regulatory analysis

7.1 Introduction

During the interviews conducted in both the first phase and the follow-up in-depth interviews, it emerged that the regulatory environment plays an important role in the strategies adopted by municipalities in respect of their financial and operational sustainability.

It emerged, for example, that particular forms of networked governance were not pursued because of cumbersome legal processes imposed on municipalities through legislation and external controls such as court orders and Auditor-General findings. The sheer cost and operational implications of seemingly increasing compliance demands brought about by regulatory frameworks also emerged as a noteworthy consideration.

In this analysis, we consider the regulatory framework within which municipalities operate with a particular focus on public finance regulation. The aim is to analyse this framework in light of the data that emerged from the interviews and to draw conclusions regarding the implications of the regulatory framework for operational and financial sustainability of municipalities.

7.2 Financial management regulation

7.2.1 MFMA

The financial management of municipalities is primarily governed by the Local Government: Municipal Finance Management Act 56 of 2003 (MFMA). The MFMA must of course be read in conjunction with a number of other statutory instruments, such as chapters 7 and 13 of the Constitution of the Republic of South Africa, 1996 (the Constitution), the Local Government: Municipal Structures Act 117 of 1998, Local Government: Municipal Systems Act 32 of 2000 as well as a significant range of regulations and other secondary legislation issued under these enactments.

The MFMA imposes a fairly rigid financial management regime on municipalities with very limited differentiation between different types of municipalities. The basic public finance management framework applicable at local government level is thus largely the same for metros as for small local municipalities.

The MFMA also imposes strict parameters on local government finances in limiting the powers of municipalities in respect of a range of financial matters both in substance and procedure. The following examples are pertinent:

- A municipality may not sell capital assets needed to provide minimum levels of municipal services (MFMA section 14(1));
- Limitations on budgeting and spending funds on capital projects, such as
  - the 20% limitation on moving appropriated funds between different budget years (MFMA section 31);
  - the requirement to solicit views from all levels of government before entering into contracts that impose financial obligations on the municipality beyond three years (MFMA section 33);
- Limitations on short-term and long-term debt, both in substance and procedure, such as the obligation to pay off short-term debt within the financial year, the prohibition against refinancing short-term debt beyond a financial year and the prohibition against foreign currency debt (MFMA sections 45, 46 and 47 read with the Municipal Regulations on Debt Disclosure, 2007);
- Limitations on the types of investments that municipalities may make, including a prohibition against investment in foreign currency instruments (Municipal Investment Regulations, 2005, regulations 6 and 7);
- Public participation processes before certain contracts may be amended (MFMA section 116);
- Strict and onerous regulatory requirements for concluding public-private partnerships (MFMA section 120 read with the Municipal Public-Private Partnership Regulations, 2005).

7.2.2 Reporting obligations

In addition to the regulatory limitations imposed on municipalities in respect of their financial management, the strict regulatory framework also imposes considerable reporting burdens on municipalities. The MFMA and the regulations promulgated under it impose extensive reporting obligations on municipalities towards provincial and national government across a very wide range of financial management matters. From the interviews it emerged that these obligations may impact adversely on municipalities' capacity to pursue their service delivery mandate given that limited capacity is consumed by reporting obligations. It furthermore emerged that these reports are not always perceived as contributing to the financial health of the municipality or assisting the municipality in its own financial management and planning. These findings confirm similar conclusions drawn in previous investigations and currently informing a law reform project of the SALRC (SALRC 2019).

An analysis of the interview data suggests that the regulatory burden imposed by enactments such as the MFMA may impact disproportionately on smaller municipalities compared to larger ones, such as metros, but also larger local municipalities. It seems that larger municipalities are able to maintain sufficient capacity to deal with high reporting burdens without having to sacrifice that capacity elsewhere. However, smaller municipalities do not seem to be able to do the same and are consequently forced into capacity trade-offs between reporting and other functions, such as financial planning. Given the normative character of the reporting obligations, by virtue of being imposed via the regulatory framework, such smaller municipalities have little choice but to prioritise reporting above other functions. It is, however, not clear that such prioritisation contributes to greater financial health and sustainability.

This differentiated impact of the regulatory reporting obligations may also undermine the very purpose of the municipal public finance management regulatory regime, viz. to address weak financial management at local government level that inhibit service delivery. The larger municipalities that seem to be able to absorb the reporting burden without sacrificing capacity elsewhere also seem to be the ones that are less in need of strict financial controls. In contrast, the smaller municipalities that seem to struggle with the reporting burden and are forced into detrimental capacity trade-offs may indeed be the very municipalities most at risk in terms of financial management and thus most in need of strict financial controls.

7.2.3 Supply chain management

Supply chain management (SCM) emerged as an area of particular concern during the first round of interviews and explored in more detail in the second round of in-depth interviews. This observation from the interviews aligns with findings of the Auditor-General, who has at least for the last ten years consistently noted supply chain management as one of the key risk areas not receiving the required attention and hence posing significant risk to municipal finances (Auditor-General, 2013; Auditor-General, 2020).[4]

A number of particular areas of concern in relation to municipal SCM regulation emerged in this project.

[4] Auditor-General of South Africa, 2013. Consolidated general report on the audit outcomes of local government 2011-12. Pretoria: AGSA; Auditor-General of South Africa, 2020. Consolidated general report on the local government audits MFMA 2018-19. Pretoria: AGSA.

7.2.3.1 Capacity constraints

Capacity to implement and manage the prescribed SCM system is a challenge. Not all municipalities are able to maintain the kind of capacity in an SCM unit that the regulatory regime ostensibly necessitates. In smaller municipalities, the available capacity for SCM is extremely limited with the result that only the most basic compliance work can be done. This leaves very little, if any, capacity for any form of strategic procurement, including thorough demand management and contract management practices. Again, as noted in respect of the reporting burden above, this issue impacts smaller municipalities disproportionately compared to larger municipalities. If one considers that these smaller municipalities operate with much more constrained budgets it follows that they are the ones that can benefit most from more strategic approaches to procurement to pursue optimal leveraging of their procurement spent. However, under current conditions, they are the ones less likely to be able to pursue strategic procurement.

The same applies to risk in SCM. The smaller municipalities are more exposed to the risk of procurement failures in respect of their key commodities, given their financial inability to cover such risks, which makes the use of strategic sourcing approaches more important in these municipalities. Larger municipalities, in contrast, can more easily afford to mitigate any risk in the procurement of their key commodities. They are thus less vulnerable to such risks. This reduces the urgency of adopting strategic sourcing approaches as a risk-mitigating strategy.

Capacity constraints furthermore adversely affect the operation of the SCM system. For example, the complexity of the SCM regulatory regime and the high risk of compliance errors that may lead to decisions being invalidated in judicial review applications or found as irregular by the Auditor-General, lead to overly cautious approaches by decision-makers in the face of any uncertainty in any procurement. The result is that procurement processes are often grossly delayed. When a bid adjudication committee (BAC) considers a tender and compliance questions emerge, the matter will most likely be stood over to the next meeting for further clarification. This inevitably results in month-long delays in finalising procurement processes with inevitable cost implications. These delays also impact on a municipality's ability to effectively spend its allocated budget within the financial year. Another example of capacity constraints undermining the operation of the SCM system is the requirement in the Municipal Supply Chain Management Regulations, 2005 that a BAC must consist of at least four senior managers of the municipality. However, some municipalities do not have such four senior managers that may imply that it cannot constitute a BAC. The effect would be that the municipality cannot award any bids. In order to avoid this problem, the Minister of Finance issued a general exemption to municipalities in 2020 from compliance with the BAC composition requirements where the municipality does not have four senior managers approved in their organogram and allowing such municipalities to "utilise" senior managers from neighbouring municipalities to serve on its BAC. This arrangement raises as many questions as it solves. It is, for example, not clear how the "visiting" managers will be held accountable for their decisions on the BAC given that they are not employed by that municipality.

7.2.4 Procurement methods

Prescribed procurement methods or procedures also create challenges at local government level. The thresholds for using different procurement procedures were set in the Municipal Supply Chain Management Regulations in 2005. They have not been adjusted since. These thresholds prescribe the use of the open bidding procedure for all procurements above the value of R200 000 (including VAT). This means that for all procurements above R200 000, a full bid invitation must be prepared, advertised and a full tender evaluation process be run before the contract can be concluded and the goods or services procured. In contrast, the threshold for the use of the open bidding procedure by provincial and national organs of state (under the Public Finance Management Act 1 of 1999 (PFMA)) is currently set at R500 000. The R200 000 threshold at local government level is very low and has evidently not kept pace with inflation over the last 15 years. It is highly likely that the transaction costs attendant on an open bidding procedure will be more than the contract value for procurements just above the threshold. In October 2020, a draft proposal was gazetted to amend the thresholds for local government procurement. Under this proposal, a differentiated approach is proposed for different types of municipalities and the threshold for the use of the open bidding procedure proposed as:

- R300 000 (VAT included) for local municipalities
- R200 000 (VAT included) for district municipalities
- R750 000 (VAT included) for metropolitan municipalities.

Incidentally, National Treasury also put forward a proposal to amend the threshold for the use of the open bidding procedure under the PFMA, i.e. for national and provincial organs of state, to R1 000 000.

The proposed differentiated thresholds for municipalities are interesting. It is not entirely clear why smaller municipalities, with smaller budgets and less capacity, should be forced to adopt more expensive procedures requiring more capacity for their procurement compared to metropolitan municipalities that can much more easily afford the costs, both financial and in human resources, of more comprehensive procedures. This uneven regulatory burden seems questionable from a sustainability perspective.

For procurements below R200 000, but above R10 000, municipalities are obliged to follow the formal written price quotation method of procurement. One of the requirements for this procedure is that at least three written quotations must be obtained. If it is not possible to obtain three quotations, the reasons for the impossibility must be recorded and approved by the chief financial officer of the municipality. This requirement may create problems for municipalities in rural areas where there may not be three service providers to supply a particular good or service. In such an instance, the municipality may be obliged to source quotes from suppliers based at some geographical distance from the municipality. If the municipality can source such quotations from suppliers based outside its jurisdiction, e.g. in the nearest metropolitan area, it would not be able to claim that it is impossible to obtain three quotes and it will thus be obliged to source such quotes. However, when the quotes are adjudicated, price is mostly the most significant award criterion. This means that the municipality will have to award the contract to the supplier that quoted at the lowest price.

If such a supplier is not based in the municipal area, additional costs may not be factored into the contract such as the cost of municipal employees having to travel to the supplier.

The final procurement method worth noting is that of joining another organ of state's contract. This method is provided for in regulation 32 of the Municipal SCM Regulations. In essence this method allows a municipality to procure goods or services under a contract concluded competitively by another organ of state without the municipality having to conduct a competitive bidding process itself. The potential cost savings of this approach is self-evident and it has been used by municipalities for a considerable period of time. It also provides one method of networked governance in the context of SCM. However, this avenue has been significantly narrowed down by recent interpretations in court cases, by the Auditor-General and by National Treasury. In judgments such as *Blue Nightingale Trading 397(Pty) Ltd t/a Siyenza Group v Amathole District Municipality* 2017 (1) SA 172 (ECG) and *Kwadukuza Municipality versus Skillful 1169 CC and Technologies Acceptances (Pty) Limited* [2018] ZAKZDHC 35 (6 July 2018), the High Court interpreted regulation 32 restrictively so that this method of procurement has become largely ineffective. Under this interpretation, a municipality may only join the existing contract on the exact same terms, including price and time period of the existing contract. The arrangement between the municipality and service provider cannot extend beyond the period of the original contract. National Treasury endorsed this interpretation in MFMA Circular Nr 96 of 2019. This Circular thus advises municipalities making use of regulation 32 that the "goods or services required by the participating municipality or municipal entity must be exactly the same as advertised and adjudicated by the other organ of state and may not be increased from the originally contracted quantity." According to this interpretation of the regulation, by agreeing to the municipality's request to join the contract, the original organ of state that secured the contract through competitive methods "is willing to forfeit a portion of its contract that has not already been utilised to the accounting officer who is requesting to procure under that contract". The Circular furthermore states that "[m]unicipalities or municipal entities may only participate on framework agreements arranged by organs of state, for example, State Information Technology Agency (SITA), the relevant treasury; that are empowered by legislation to arrange such on behalf of other organs of state." This statement is legally questionable since it conflates the distinct concepts of transversal contracts and framework agreements. It is correct that the power to conclude transversal contracts is statutorily limited to certain organs of state, primarily treasuries. However, there is no similar limitation in South African law pertaining to framework agreements. Any organ of state may procure goods or services for itself by means of framework agreements. Accordingly, any municipality, by means of regulation 32, may seek to join a framework agreement concluded by another organ of state. The narrow (and arguably incorrect) interpretation adopted by National Treasury in this respect closes down one of the potentially most advantageous uses of regulation 32.

7.2.5 Multi-year contracts

The interaction between the SCM system, particular in the form of the open bidding procedure, and the procedural requirement for multi-year contracts creates significant bottlenecks.

In terms of section 33 of the MFMA, a municipality may only enter into a contract which will impose financial obligations on the municipality beyond the three years covered in the annual budget if certain strict conditions are met. These conditions include soliciting the views of the local community, the National Treasury, provincial treasury, national department responsible for local government and, if the contract relates to water, sanitation or electricity, also the relevant national department in those areas. The municipality may only proceed to conclude the contract once it has considered these views. This implies that a municipality cannot proceed with the contract until it has received the relevant views.

Where the relevant multi-year contract amounts to a procurement, the usual SCM rules will also apply. These would inevitably be the rules governing the open bidding procedure given the low threshold for the use of this procedure at local government level. The municipality will thus have to go through the extensive process of formulating the specifications for the contract, including the terms of the contract, advertise it, evaluate and finally adjudicate all bids received before it can take a decision to conclude the contract.

These two procedures do not, however, readily co-exist at a practical level. To comply with both sets of rules, the municipality will have to seek input on the draft contract it wishes to conclude *before* it advertises the bid since it cannot change those terms *after* it has published the advertisement. At the same time, the municipality would not know the price it will pay under the contract at this point since that will only be determined once the preferred bidder had been identified following the adjudication phase of the procurement process. At this stage, and before actually awarding the bid and concluding the agreement, the municipality may ostensibly again be obliged to seek the views of all the listed parties in order to meet the conditions in section 33.

This is quite evidently not a feasible way of concluding agreements. The significant delays caused by the multiple regulatory requirements will most likely make this type of arrangement unworkable. However, entering into longer-term contracts that would allow for stable supply and the establishment of effective working relationships between suppliers and municipalities may in many instances be a superior way of acquiring goods and services.

7.2.6 Compliance

A theme that emerged from the interviews was the interaction between municipalities and various regulatory controls over public finance management. The most salient controls here are the courts and the Auditor-General.

The statutory nature of the regulation of public finance in South Africa has two very important implications for compliance. Firstly, it means that general administrative law applies to most public finance management decisions taken by municipalities. This further means that the right to administrative justice in section 33 of the Constitution along with the Promotion of Administrative Justice Act 3 of 2000 are applicable to such decisions. One of the core legal mechanisms under these enactments is that of judicial review. This mechanism allows any affected party to approach the High Court to review and potentially set aside (i.e. invalidate) the impugned municipal decision.

Secondly, municipal finance decisions are obviously also subject to audit by the Auditor-General. One of the key findings that the Auditor-General must make is that of irregular expenditure. Irregular expenditure is defined as expenditure incurred in contravention of or not in accordance with *inter alia* the prescripts of the MFMA, the Municipal Systems Act and the municipality's SCM policy (which in itself must comply with the Municipal SCM Regulations). The statutory nature of municipal finance rules thus activates the possibility of a finding of irregular expenditure. Findings of irregular expenditure can have a range of consequences, which may include disciplinary steps against the implicated officials, recovering the expenditure from that official and in serious cases even criminal prosecution.

These far-reaching compliance mechanisms may impact on decision-making within municipalities and encourage narrow, highly-risk averse approaches. This may lead to a culture that does not embrace innovation in financial management. The interview data, however, suggests that relative power seems to play a notable role in this regard. It seems that more powerful municipalities, in the sense of municipalities with significant resources and high profile, are able to adopt more robust approaches to its financial management compared to less powerful municipalities. It seems that the former municipalities are more readily able to form strong views on a particular approach and to robustly engage with the various control mechanisms, such as the Auditor-General and the courts, when they are questioned in order to impose their views. In contrast, smaller, less powerful municipalities are not able to adopt similar approaches. They thus interact with the control mechanisms on a different level with the result that the dampening effect is more pronounced in such municipalities.

7.3 Mandates in terms of schedules 4 and 5 of the Constitution

A regulatory theme that emerged from the interviews is that of unfunded mandates. It emerged, for example, that municipalities are carrying significant financial burdens in relation to the provision of housing and a host of social services which do not fall within the constitutional mandate of local government.

The core competencies of local government within South Africa's constitutional framework of co-operative government are set out in schedules 4B and 5B of the Constitution. These competencies provide the basis for determining the equitable share and allocation of revenue to municipalities under section 214 of the Constitution. It follows that the fulfilment of a function by a municipality outside of these competencies and that is not provided for in a particular statutory delegation of functions with dedicated funding attached, may involve significant expenditure by municipalities that are not accounted for revenue allocations.

Housing and social services are good examples of such unfunded functions that pose financial challenges to municipalities. Housing and welfare services are both listed in Schedule 4A of the Constitution as concurrent national and provincial competencies. To the extent that these services are provided by municipalities, such as where municipalities are obliged to install bulk services to an area to address a housing challenge, e.g. because it is ordered by a court to assist residents in need of emergency housing, they are not adequately reflected in revenue allocation.

Another dimension to the financial challenges brought about by the allocation of municipal mandates in Schedules 4 and 5 of the Constitution is the limited opportunities for municipalities to generate additional income. Since municipalities may not engage in functions that are not listed in the schedules (or have been statutorily assigned to municipalities),

municipalities are significantly constrained in exploring opportunities for generating additional income. This is especially true in relation to emerging services, i.e. services that emerged only after the adoption of the Constitution in 1996. Given the nature of the allocation of competencies between the levels of government by means of a fixed list of competencies that provincial and local government may exercise while all others are by default national competencies, all emerging services will necessarily be national competencies. These could only be allocated to another level of government, such as local government, at the discretion of national government. A good example is the provision of internet fiber services. It is not evident that this function can be included within any of the competencies listed in either Schedules 4 or 5 with the result that it is by default a national competence. However, this is arguably a service from which municipalities could meaningfully generate income and could thus be a good candidate as a municipal competence.

7.4 Eskom and municipal debt

Throughout this report, the key role of the delivery of electricity and the attendant financial implications for municipalities are noted. It is accordingly of particular relevance in this regulatory analysis to also note recent legal developments in respect of the relationship between ESKOM and municipalities.

During the last few years and with increasing frequency since 2019, municipalities and Eskom have resorted to litigation to resolve payment disputes. As the judge stated in one of the most recent such cases, namely *Nketoana Local Municipality v Eskom Holdings (SOC) Limited* [2021] ZAFSHC 1 (7 January 2021) at para 1: "In recent years our courts have constantly been confronted with the endemic problem of municipalities failing to pay Eskom for the bulk supply of electricity to their areas of jurisdiction, and of Eskom wanting to implement stringent measures against those municipalities in order to enforce immediate payment of what is due to it. This matter is no exception." In the Supreme Court of Appeal judgment in *Eskom Holdings SOC Ltd v Resilient Properties (Pty) Ltd and Others; Eskom Holdings SOC Ltd v Sabie Chamber of Commerce and Tourism and Others; Chweu Local Municipality and Others v Sabie Chamber of Commerce and Tourism and Others* [2020] ZASCA 185 (29 December 2020), it is noted at para 17 that the total municipal debt owing to Eskom stood at approximately R30 billion by April 2020.

The typical form of these cases is that Eskom threatened a municipality with electricity supply restrictions, including complete discontinuation of bulk supply, if the relevant municipality failed to pay its outstanding debt to Eskom by a certain date. The municipality (or, in some instances, affected parties such as ratepayers' associations or local chambers of commerce) then approached the High Court for an order interdicting Eskom from implementing any such restrictions in supply. In quite a few cases, it is affected parties other than the municipality itself, such as ratepayers' associations or local chambers of commerce that launch the application, such as for example in the *Resilient Properties* matter, *Vaal River Development Association (Pty) Ltd v Eskom Holdings SOC Ltd and Others; Lekwa Rate Payers Association NPC v Eskom Holdings SOC Ltd and Others* [2020] ZAGPPHC 429 (28 August 2020). Eskom typically responded by filing a counter application in which it sought to enforce the repayment of the debt on particular terms via a court order. The municipality typically acknowledges that it is indebted to Eskom, but raises a number of arguments as to why supply should not be discontinued. These range from disputes about the actual amount of indebtedness to the inability to pay the full amount outstanding by the date of demand.

In the *Nketoana Local Municipality* matter, the judge summarized this typical state of affairs as follows in para 29: "By now it should be clear that this court is again confronted by the classic problem of a municipality that is unable to pay the spiralling debts it owes to Eskom, while Eskom finds itself in a position where it has to take extraordinary measures to ensure that payment of these debts will be forthcoming. In the present case, this problem is further complicated by the lapse of time since the municipality fell in arrears with the payment of its account in 2013, but more particularly, since the filing of the urgent application on 9 March 2018."

Invariably, the applicants in these cases (whether the relevant municipality or some affected party such as a ratepayers' association) succeeded in their application to interdict Eskom from introducing restrictions or termination of supply and Eskom failed to obtain relief by way of its counter application to judicially enforce the debt owed to it. The reason for the courts' view that Eskom cannot succeed in terminating supply hinges on the rationality or reasonableness of such a decision. In the *Nketoana Local Municipality* case, the judge set out this reasoning as follows:

"The next inquiry is then whether the Eskom decision complies with the requirement of rationality or even reasonableness. The decision was obviously taken to compel payment of the arrear amount, and to compel regular payment of the current account. Viewed objectively, the decision certainly cannot ensure payment of the arrear debt as it now stands, and perhaps not even payment of the current account. In this respect, the decision cannot pass the test of rationality, even if it encourages the Municipality to make every effort to pay the current account. This is so, because the municipality does not have the means to pay the arrears. On the other hand, if the interruption or termination is to be implemented, it would cause nothing but disaster to the residents of the municipal area. In this sense, the decision does not even pass the test of reasonableness."

The courts have furthermore shied away from granting any relief in terms of the payment dispute between Eskom and municipalities in these types of cases on the basis that such disputes amount to intergovernmental disputes that should be addressed via the mechanisms created under chapter 3 of the Constitution before resorting to litigation. In *Nketoana Local Municipality,* the court outlined at paras 47 to 48 the following mechanisms and procedures that may have to be followed:

"The mechanisms and procedures are, inter alia, the following: Section 139(1) of the Constitution provides that when a municipality cannot fulfil an executive obligation, the relevant provincial executive may intervene by taking any appropriate steps to ensure fulfilment of their obligation. Section 44 of the Municipal Finance Management Act 56 of 2003 demands that whenever a dispute of a financial nature arises between organs of state, the parties concerned must as promptly as possible take all reasonable steps that may be necessary to resolve the matter out of court. If the National Treasury is not a party to the dispute, the parties must report the matter to the National Treasury, and may request it to mediate between the parties or to designate a person to mediate between them. Section 139 of the same Act provides that where a municipality is in serious or persistent material breach of its obligations to meet its financial commitments, or admits that it is unable to meet its obligations or financial commitments, the provincial executive must promptly request the Municipal Financial Recovery Service, amongst others, to determine the reasons for the crisis and to prepare an appropriate recovery plan for the municipality.

Furthermore, Section 30 of the ERA [Electricity Regulation Act 4 of 2006] provides that if there is a dispute between licensees, the National Energy Regulator must act as a mediator if so requested by both parties to the dispute. Section 45 of the IRFA [Intergovernmental Relations Framework Act 13 of 2005] provides that no organ of state may institute judicial proceedings in order to settle an intergovernmental dispute unless the dispute has been declared a formal intergovernmental dispute in terms of Section 41 of the Act, and all efforts to settle the dispute were unsuccessful. Once a formal intergovernmental dispute has been declared, the parties must promptly convene a meeting between themselves in terms of Section 42 of the Act, and if they fail to do so, the Minister or the MEC may convene such a meeting or may designate a facilitator on behalf of the parties. The facilitator must, inter alia assist the parties to settle the dispute in any manner necessary."

These cases and the relationship that they create between municipalities and Eskom hold important potential implications for the financial sustainability of municipalities generally. It is evident that Eskom's inability to expediently collect outstanding municipal debt for bulk electricity supply via judicial processes places significant financial pressure on Eskom. This places pressure on Eskom's ability to effectively deliver electricity services to all municipalities with serious implications for municipalities' own reliance on income from electricity supply. Furthermore, the continuing (and growing) outstanding municipal debt to Eskom forces Eskom to increase its rates for bulk supply, which is not necessarily matched in NERSA's tariff increases to allow municipalities to manage such increased bulk supply rates.

The dynamic between Eskom and municipalities illustrated by these cases point to a larger issue regarding intergovernmental debt. The question is how debt is to be effectively settled between organs of state. These cases illustrate that the usual debt enforcement mechanisms such as termination of performance under a contract by a creditor, an acknowledgement of debt or judicial enforcement of debt may not be effective in the context of intergovernmental debt. As the Supreme Court of Appeal noted in the *Resilient Properties* matter at para 79, the "relationship between Eskom on the one hand and the [municipalities] on the other is more than merely a contractual one regulated purely in terms of the ESAs [electricity supply agreements] that the parties concluded. Eskom supplies bulk electricity to the municipalities which, in turn, have a concomitant duty to supply it to the end-users. The unique feature of this relationship is that Eskom, as an organ of state, supplies electricity to local spheres of government to secure the economic and social well-being of the people". The question thus emerges how effective the alternative mechanisms under the intergovernmental framework are to address outstanding intergovernmental debt. The Eskom cases suggest at least that these mechanisms are not particularly effective. Beyond the Eskom/municipality relationship, the question thus emerges whether municipalities are placed at increased risk when they are forced to fulfil mandates that are not fully funded within their equitable share and must thus rely on "repayments" from other levels of government to cover the shortfall, but seemingly without any effective legal mechanisms to extract repayment.

8 Strategic option analysis: broad themes

The preceding analysis reveals that the pandemic generally amplified pre-existing sustainability challenges, especially for smaller LMs and DMs. Conversely, municipalities which were functional with effective systems, adequate capacity, management continuity and a stable political-administrative interface prior to the pandemic, were more resilient in their responses during the pandemic. However, while WC municipalities have weathered the pandemic better in the short term than would have been expected, they still confront longer term sustainability challenges which are attributable more to systemic factors, than the COVID-19 pandemic per se. Consequently, the analysis below focuses primarily on those systemic factors.

Many of the factors affecting longer term municipal sustainability lie outside the direct control of municipalities themselves, and therefore require joint responses with other spheres of government. Accordingly, the focus of the analysis is systemic, as well as on the steps which municipalities themselves can take in order to foster their own operational and financial sustainability. The COVID-19 pandemic is obviously one such example, but others include the persistent drought and higher probabilities of future adverse climate events due to the climate emergency, the adverse impacts of ESKOM loadshedding, uncertainty for municipal sphere due uncertainties around the restructuring of electricity provision and uncertainty about long term water and energy consumption.

Ultimately the growth of local economies (and by extension municipal revenue bases) is inextricably linked to the vibrancy of the national economy. The South African economy has experienced a decade of sluggish economic growth, due to a host of factors ranging from policy uncertainty and incoherence leading to low investor confidence, deteriorating terms of trade, poor performance of state owned entities resulting in deteriorating public infrastructure and ballooning contingent liabilities, the inability to implement the reforms outlined in 2012 in the National Development Plan, state capture and pervasive corruption, the hollowing out of the South African Revenue Service and the declining legitimacy of government institutions.

Since 2015, South Africa's fiscal policy response has been what Sachs (2021) terms "fiscal austerity without consolidation": instead of adjusting to permanently lower growth rates in the wake of the end of the commodity cycle in 2010, the country has instead created more social entitlements (such as fee free higher education). While National Treasury has been able to cap aggregate expenditure levels for all three spheres of government, rapidly rising personnel costs have resulted in lower headcounts of public services, the crowding out of complementary non-personnel service delivery inputs and capital budgets, with negative impacts on service delivery. While government has been creating new entitlements (and is entertaining the introduction of a basic income grant), instead of progressive realisation of its existing socio-economic entitlements in health, basic education and public security, there has been retrogression over the last decade. Slow economic growth has been accompanied in record unemployment levels, reduction in disposable income of households and increased poverty and indigence, exacerbated by the extended lockdown.

The COVID-19 lockdown response to the pandemic has significantly undermined tax revenues. The South African Revenue Services preliminary (net) collection outcome for the 2020/21 financial year was R1.25 trillion, which exceeded the R1.21 trillion target in the

COVID-19 adjustment budget in June 2020, but constitute a contraction of R105.6 billion (-7.8%) relative to the 2019/20 financial year. This has rendered a national fiscal crisis which was unsustainable even before the pandemic even more precarious:

In the aftermath of Covid-19, the fiscal position is profoundly unsustainable. Growth rates are below interest rates and (in these conditions) the primary balance needed to stabilise debt is not feasible… If fiscal imbalances are not resolved, the burden of interest payments will quickly become intolerable, making the future ability and willingness of the state to honour its obligations questionable. South Africa is entering a period of fiscal distress (Sachs, 2021, p. 46).

Given the magnitude of the fiscal adjustment required, it is unlikely that local government as a sphere will receive additional support from the national fiscus. Quite the contrary – this can be expected to decrease in the medium term. This means that municipalities will have to intensify efforts to raise own revenues and enforce the user pays principle, while making fundamental cuts to their expenditures in order to remain sustainable. While some of these hard revenue enhancement and expenditure control actions lie within the purview of municipalities themselves, others are the prerogative of role players at national and provincial level.

While there are serious challenges with fiscal effort and the allocative and operational efficiency of municipal spending, it is also glaringly apparent that some of the fiscal stress experienced is also attributable to structural deficiencies in the local government fiscal and functional framework. In the WC, where fiscal effort and operational efficiency is greater than in many of municipalities in rest of the country and less obscured by challenges of capacity, maladministration, fraud and financial misconduct, these are starkly apparent. WC municipalities do surprisingly well *despite* the dysfunctionality of the intergovernmental system, rather than because of the system. After 20 years of incremental evolution of the system of municipal finances, the current financial crises – exacerbated by the pandemic – has made a fundamental re-think of existing arrangements a matter of urgency.

The strategic option analysis below considers the problem statements relating to the thematic areas identified in the financial analysis and the two rounds of interviews in the following categories:

- The process to action this report's recommendations;
- Financial drivers of financial and operational sustainability
- Institutional factors conditioning municipal sustainability
- Regulatory factors impacting municipal sustainability

8.1 Process to action the recommendations in this report

Problem statement:

No report has self-implementing recommendations. The strategic options put forward in this report will have to be assessed for feasibility, prioritised, sequenced and translated into an action plan with appropriate roles, responsibilities and timelines.

Recommendation:

- A technical working group should be assigned the task of assessing and prioritizing recommendations over the short and medium term, and assigning appropriate roles, responsibilities and timelines.

8.2 Financial drivers of financial and operational sustainability

The following financial drivers are explored in greater detail below: the local government fiscal framework, funding of capital programmes, optimising existing revenue sources (property rates and tradable services), possible new revenue sources, managing the costs of employment and Free Basic Services.

8.2.1 The local government fiscal framework and operational intergovernmental transfers

Problem statement

The challenges with the local government Equitable Share grant (LGES) relate to adequacy and stability. In recent years, the LGES grant has not kept pace with escalating costs of employment or increasing bulk services costs. The local government share of nationally collected revenue (arising from the vertical division of revenue) had risen from 3% in 2000 (R6 billion) to 8.9% in 2018/19, but fell to 8.3% in 2018/19. This share is projected to increase again to 9% in 2021/22, and anticipated to rise further to 9.7% in 2023/24 (South Africa. National Treasury, 2021). While this aggregate allocation to local government takes into consideration the own revenue raising capacity of municipalities, "the fairness of this vertical division of revenue has remained a bone of contention, especially considering that the demands for local government services have expanded in the past two decades" (South Africa. Financial and Fiscal Commission, 2019, p. 23). As a result of the need for fiscal consolidation and pandemic induced fiscal constraints, Budget 2021 reduced the amounts flowing to municipalities via the LGES by R14.7 billion and from general fuel levy sharing with metropolitan municipalities by R2.7 billion (South Africa. National Treasury, 2021).

During the interviews, officials from rural municipalities expressed concern that cost disabilities of rural municipalities (which are largely outside their control) were not adequately taken into consideration in LGES. They also raised the concern that the LGES appears to be overly focused on Free Basic Services and not the other services municipalities provide. The vertical division of revenue determines the aggregate amount of the nationally collected revenue and the LGES formula ensures that this is distributed among individual municipalities, based three components:

- a *Basic Services (BS) component* which covers the cost of providing free basic services based on the number of eligible households and the estimated cost of providing these services),
- an *Institutional and Community Services (I&CS) Component* (modified by a revenue adjustment factor) which contributes towards administrative costs of a municipality (proxied by the number of councillors) as well as collective services such as municipal health, fire, roads, cemeteries, planning, stormwater management streetlighting and parks (proxied by the total number of households in the municipality). In order to prioritise municipalities which are least able to raise own revenues, municipalities are

ranked in terms of an index which aims to capture their own revenue raising capability. The top 10% of municipalities receive zero I&CS component while the bottom 25% receive the full I&CS component and those in between receive a pro rated amount based on a sliding scale. Because some WC municipalities have significant own revenue resources, their I%C allocations tend to be vastly reduced by the revenue adjustment factor

- A Correction and Stabilisation (C) factor to ensure a degree of stability in each municipality's allocation over the MTREF period.

The BS component is "kept fixed and the per councillor and per household allocations for the I and CS components are adjusted up or down. In other words, higher BS allocations will result in lower I and Cs allocations" (South African Cities Network, 2020, p. 59). This means that while the BS component is related to expected costs of provision, the I&CS and C components are merely a balancing residual to ensure that the total local government share is fully allocated, and that the total local government share determined by the vertical division is not exceeded. The link between costs of these collective services and formula is therefore tenuous at best. Moreover, the administrative component does not directly factor in the cost of increases in the administrative compliance burden such as the complicated and often duplicated reporting requirements, implementation of the municipal Standard Chart of Accounts and the proliferation of other administrative requirements from other spheres of government. The gap between the "reasonable" efficient cost of delivering collective services to low income and indigent households and the grant revenue actually received would contribute a "transfer gap" referred to earlier.

The structure of the LGES formula has not change much since its introduction in 1999/2000, two decades ago. The formula is based on extrapolations from outdated datasets, whereas there have been considerable movements of people across municipal jurisdictions as well as changes in the financial status of households. For example, when the current LGES formula was introduced in 2013/14 it was based on updated Census 2011 data, with a phase in between 2013/14 and 2017/18 of changes to allocations as a result of the formula. The formula was then updated based on Community Survey 2016 data, with the associated phase-in between 2017/18 to 2019/20. Finally, while the LGES had been protected in the first two decades of the revenue sharing arrangements after the transition to democracy (for example, through stable outer year baseline forecasts and phasing in of changes to the formula and data updates), increasingly fiscal consolidation and uncertainty around revenue collection at national government level – exacerbated by the pandemic – is undermining predictability and intensifying funding uncertainty at municipal level.

Crafting a coherent local government fiscal framework is contingent on a coherent local government functional framework so that "finance can follow function". However issues relating to powers and functions and the role of the three categories of municipalities have languished unresolved, for more than a decade. This situation cannot be resolved in a piecemeal fashion without also considering the role of provincial governments. In 2008, the former Department of Provincial and Local Government had initiated a policy process on the system of provincial and local government, which would then update the 1998 White Paper. More than a decade later, these issues have never been dealt with. For example, the FFC has raised "serious questions about the effectiveness of district municipalities, especially with regard to their ability to carry out their respective mandates and indeed their relevant in the intergovernmental make-up of the country at present" (South Africa. Financial and Fiscal Commission, 2019, p. 10). Decisions on the shifting of functions across spheres have largely occurred on an incremental sectoral basis, without sufficient consideration on their collective impact on the local government functional framework as a whole.

Some of the key premises underpinning the 1998 White Paper no longer obtain, such as the assumption that local government in aggregate could raise 73% of its own revenue, and new policy challenges have become foregrounded since then including the climate emergency and the imperative of a just transition from centralised carbon-based energy production to decentralised renewable energy production. In 1998, South Africa had one of the cheapest bulk electricity prices globally, but Eskom's operational and governance dysfunctions since have lead to a marked escalation of bulk electricity tariffs well in excess of inflation, with the result that it is now mid-priced. Municipal electricity surpluses have been significantly eroded, compounded by more affluent users opting to leave the grid in the face of rising consumer tariffs (Ledger & Rampedi, 2020). Recent policy reforms aim to increase private sector investment in embedded generation, and permit municipalities to source from them rather than Eskom. Also, the long proposed unbundling of Eskom into separate generation, transmission and distribution entities, is gathering momentum. With the longer term transition into green energy, it is clear that business models and cost structures will change. In the medium term, load-shedding will continue to be a brake on economic growth and detract from municipal revenue bases, while Eskom tariffs are likely to increase substantially. On the other hand, the price of renewable energy is likely to be on a downward trend as technologies improve and the scale of decentralised production increases. In the long term, there will be little place for municipal electricity surpluses to cross-subsidise low income households which do not qualify as indigent, as well as other services. Furthermore, as businesses and more affluent consumers gradually defect from the electricity grid to alternative energy sources, only poorer consumers will remain, further eroding surpluses and room for cross-subsidisation. Municipalities will have to adjust their strategies to create an incentive for energy users to stay on the grid (including tariff setting or possibly corporatisation of electricity functions).

This situation is compounded by the perception among sampled municipalities that NERSA does not fully comprehend the impact of their determinations on municipal sustainability. A case in point is reflected in Swartland Municipality's *2020/21 MTREF Budget Report*, that notes that NERSA's consultation paper with proposed guideline electricity tariff adjustments for municipalities on 20 March 2020 contained inconsistencies in the calculation methodology that would have lead to the "almost the complete elimination of the net surplus derived from electricity sales and would severely impact the financial viability of all municipalities" (p27). NERSA conceded after Swartland Municipality lodged an objection against the application of Eskom related tariffs for reselling and reverted to the typical municipal tariff structures as applied in previous years in the subsequent guideline tariff determination. This aptly illustrates the need for more local government voices in national decision-making and reform processes which affect them. NERSA's approval of a 6.90% increase in electricity bulk purchases in 2020/21 but restriction of the average tariff municipalities may charge users to 6.43% means that LMs could not pass the full increase on to their customers, thus reducing their surpluses.

This places additional pressure on the levels and quality of services delivered municipalities are able to deliver, as well as reduced internal funding for new infrastructure development, rehabilitation and upgrade.

Long term water consumption patterns are changing markedly, driven by the intensified need for water demand management as drought like conditions and other adverse weather events become more frequent, resulting in permanent drops in consumption. Similar to the electricity industry, far reaching reforms have been proposed in the water industry with the creation of an independent economic regulator, thus separating regulation from the roles of policymaker, planner, investor and operators of water resources infrastructure. This would also entail reviewing pricing (including raw water pricing) and service standards as well as investigating the feasibility of a national water resources infrastructure agency which was proposed by the National Development Plan 2030 (South Africa. National Treasury, 2019). As decentralised energy production eliminates monopoly rents on electricity sales, this will place additional pressure on water prices to rise, not only for demand management purposes, but to generate operating surpluses.

In the same vein, the additional transport costs entailed by regionalisation of landfill sites (as per national policy) also materially affect municipal cost structures, with the implication of higher tariffs, which would reduce their affordability for households. Simultaneously, certain national policies are undermining municipal revenue sources. For example, the Administrative Adjudication of Road Traffic Offences (AARTO) Act (No 46 of 1998) which is due to come into full effect July 2021, will undermine municipal revenue from fines, a small but significant revenue source for many WC municipalities.

In December 2020, a special lekgotla of the Budget Forum (the intergovernmental structure established to facilitate formal consultation on local government finances) resolved that National Treasury, the Department of Cooperative Governance and SALGA should review the local government fiscal framework. In the past, incremental reviews have been done predicated largely on the current functional framework configuration, but a more thorough review based on a streamlined, differentiated and clearly defined long term functional framework and an associated change management plan is called for. Past reviews typically focus on the technical details of the LGES formula and capital grant frameworks, whereas the vertical division of revenues across national, provincial and local spheres is also crucial, but it is regarded as a political decision. Yet it would be critical to align the vertical division of revenue with the local government functional framework.

Unlike the 1998 White Paper which relied on assumptions in lieu of credible empirical data, this review should be based on twenty years of evidence relating to the fiscal effort gap, the expenditure inefficiency gap, the transfer gap and the unfunded/underfunded mandate gaps.

Recommendations

- The local government functional framework should be reviewed in the light of 25 years of local government experience and the implementation of far-reaching reforms in electricity and water industries. The revised functional framework should inform a fundamental review of the local government fiscal framework.
- A process of this magnitude should not just involve SALGA, provincial departments of local government and provincial treasuries but also consultation with individual

municipalities, so that the differentiated impacts can be understood, and diverse municipal voices can be heard.

8.2.2 Funding of capital programmes

Problem statement

Even prior to the pandemic, WC municipalities experienced funding gaps in respect of their capital budgets. For instance, the City of Cape Town's capital funding gap between 2017 and 2026 was estimated at 70% of its capital expenditure needs, compared to 73%, 50% and 45% in the Cities of Johannesburg, eThekwini and Tshwane respectively over the same period (South African Cities Network, 2019). Drakenstein's Long Term Revenue and Expenditure Framework reflects an average funding gap of 53.2% between 2021 and 2030.

The preceding financial analysis and interview results demonstrate that the biggest impact of the pandemic has been on reductions in capital spending in the sampled Western Cape municipalities. Inadequate capital investment not only undermines the eradication of service delivery backlogs, but also put operational pressure on existing infrastructure networks, with implications for their maintenance and renewal costs.

Due to the fiscal capacity, good governance, financial management capacity and creditworthiness of WC municipalities, they have been able to engage in long term borrowing. The proportion of local municipalities (21 out of 24) accessing long term debt markets in the Western Cape is higher than in all the other provinces. WC secondary cities comprised 40% of the R5.8 billion long term belonging to secondary cities in 2020. Of the R2.6 billion in long term debt owed by municipalities other than secondary cities, 61% is attributable to the WC (South Africa. National Treasury, 2020). More conservative borrowing strategies are however being followed by WC municipalities, given the uncertainty occasioned by the pandemic, creating more reliance on internal reserves and greater dependence on intergovernmental capital grants. At the same time, due to fiscal consolidation prior to the pandemic, and competing funding priorities within the national sphere, conditional capital grants across all spheres of government were already being cut prior to the pandemic. The need to reprioritise funds to respond to the pandemic intensified this trend, with further cuts to direct conditional grants of R2 billion announced in the 2021 budget (South Africa. National Treasury, 2021).

Given the greater funding gap and lower fiscal capacity in aggregate elsewhere in the country, even if more grant funds were to be made available, WC municipalities would not be well positioned to receive them, given the redistributive nature of grant instruments. However, in March 2020, National Treasury stopped grants to 47 municipalities because of their inability to spend them effectively, and it can be asserted with a fair degree of certainty that this is likely to continue. WC municipalities which have a track record in spending their capital allocations effectively should therefore develop a pipeline of feasible "shovel ready" projects which they can fast track should such funds become available, and plan their capital delivery completion earlier in the financial year than the last quarter in order to avail themselves of opportunities which present themselves.

There are differing views on the fairness of the capital grants received. Some of the sampled municipalities raised no issues in this regard. On the other hand, Drakenstein Municipality in its *2020/21 MTREF Budget Report* expressed the view that its allocations were "far less than what other secondary cities with similar demographics are receiving" and that "Drakenstein does not receive their fair share from the National Fiscus as a secondary city" (p17). In terms of the Financial and Fiscal Commission Act (FFC) 99 of 1997 (as amended in 2003), organs of state may request the FFC to provide advice on financial and fiscal matters. Drakenstein DM could therefore request an independent, impartial opinion on this matter from the FFC, a body specifically created by the Constitution to deal with the equitable distribution of nationally collected revenue.

The FFC has noted that the current revenue sharing arrangements encourage development of new infrastructure assets rather than the rehabilitation and upgrade of existing infrastructure and that the number of capital grants has proliferated, increasing the administrative and reporting burden (South Africa. Financial and Fiscal Commission, 2011). Increased grant dependence by municipalities creates a tension between the preferences of the community identified in IDP processes and the need to meet national conditional grant requirements. The FFC notes that: "Infrastructure grants are supposed to fund projects identified and approved through IDP processes…Yet national grant administrators often seen to dictate the investment priorities of municipalities, thus compromising the delivery management framework laid out in legislation and existing guidelines (South Africa. Financial and Fiscal Commission, 2019, p. 83).

By drawing on increased internal funding, municipalities deplete their capital reserves and should replenish them. Failure to do so would impair the municipalities' ability to fund their capital budgets and undermine their liquidity and creditworthiness. Generating addition internal funding requires surpluses on the operating budget, which are limited by affordability constraints.

Recommendations

1. In the face of tightening capital budget constraints, Municipalities should review their systems of capital project prioritisation to ensure that they balance social infrastructure (e.g. informal settlement backlogs) with economic infrastructure that can generate revenues and grow the tax base, and balance new infrastructure with rehabilitation and upgrades.
2. Municipalities should establish a pipeline of shovel ready projects in a pipeline and aim to deliver early in the financial year to order to take advantage of additional unplanned capital funding grant opportunities.
3. Municipalities should build up their internal reserves to help finance their capital expenditure and facilitate borrowing once the pandemic has ended. This has implications for tariff setting in order to generate operating surpluses.
4. Municipalities should explore project finance and other forms of off-balance sheet lending where bankable projects can be identified. Cooperation among municipalities with provincial government support to help identify and package bankable projects may be required for projects which transcend the boundaries of any single municipalities like dams, and renewable natural gas projects from municipal solid waste landfills and wastewater treatment facilities.
5. Innovative lending arrangements should be explored e.g. green bonds and concessionary financing from the World Bank's Climate Investment Fund. The City of Cape Town, for instance, has already issued green bonds, and its current small scale embedded generation

programme could be scaled up as a basis for a tradeable renewable certification scheme. This would establish markets for both renewable energy and tradeable green energy certificates. If other municipalities were to generate their own renewable energy, these sales and revenue from selling green certificates could ensure the sustainability of this form of borrowing.

6. Drakenstein Municipality should request from the FFC an independent assessment of the fairness of its capital grant allocation relative to similar secondary cities, in terms of the FFC Act.
7. The Western Cape Provincial should support the case for streamlining capital grants to reduce their administrative burden, in a differentiated, risk-based approach that recognises municipalities' track record in delivery and good financial management.

8.2.3 Property rates: balancing affordability and sustainability

Problem statement

Property rates as form of wealth taxation traditionally covers the cost of collective services as well as the fixed cost element of quasi-collective services (such as combating fires and health services and public transport). In theory, both the benefit-received principle and the ability-to-pay principle should be applied, in the former by differentiating rates between category of property (e.g., residential vis-à-vis commercial) and the latter by making allowance for rebates to the indigent while also potentially differentiating rates in the same category (e.g. higher rates in high-value property neighbourhoods). Generally, the convention is that the capital value of a property indicates ability-to-pay and benefit-received, provided that valuations are done regularly. However, crises such as the drought and the COVID-19 pandemic skew the assumptions based on these theories and conventions. The interviews indicated that generally, the ability-to-pay principle is applied to residential property. For example, the City of Cape Town deem all properties below R300 000 to belong to the indigent unless proven otherwise, with 100 percent rebate on rates. In addition, if total household income is below R4 500, such households can register as indigent and therefore also qualify for a 100 percent rate rebate. This shows that residential property is indeed treated sensitively regarding ability-to-pay, and individual households are therefore covered when disasters such as Covid-19 strike, which render them indigent.

This however is not the case with commercial property. Many such properties closed down as a result of the lockdown, and work-from-home arrangements effectively shifted many commercial activities to residences. Although the full economic impact of COVID-19 pandemic is not yet known at the time of writing this report, it is clear that a significant proportion of the decline in demand for certain types of commercial spaces will be permanent. This will therefore also result in lower income from such property and lower ability-to-pay on the side of such property owners. In addition, certain sectors, such as agriculture-related industries (during the drought and lockdown) and the tourism, hospitality and higher education-related industries (during lockdown), suffered massive losses due to declining economic activity. The City of Cape Town has indicated that there is no provision in legislation (the Municipal Property Rates Act - MPRA), allowing rebates for businesses in the hospitality sector, which form part of the business and commercial category of properties, and they only allow deferred payments options to such affected property owners. Obviously, any lasting impact requiring more widespread application of the ability-to-pay principle will impact on revenue collected from rates and will inevitably lead to an increase in the rate applied to the remaining properties, unless external controls limit that possibility. That will further compromise the ability of municipalities to fund and maintain infrastructure. As halting infrastructure maintenance and improvement through capital projects has indeed been the emergency response resulting from Covid-19, it has a medium to long term operational sustainability implication.

Recommendations

The interviews revealed a number of initiatives that are already achieving positive results and deserve further consideration. First, by following deliberate strategies to make it attractive for households that can afford rates to resettle, thereby growing the tax base (e.g. as work-from-home arrangements and online learning make rural municipalities more attractive to more affluent households), service delivery capacity can be better utilised and better economy of scale achieved. Second, the successes that municipalities have achieved in optimising existing revenue streams through up-to-date valuations, cleansing of customer and account databases, using cutting edge information and communication technology and financial modelling in the interest of minimising the total municipal account for households, demonstrates that capacity for optimising existing revenue streams exist. As summarised in Section 4.1.5, *The State of City Finances Report 2018* identifies various mechanisms for further increasing property rates in South African cities that deserve consideration South African Cities Network, 2018).

Third, applying the principles of managing constraints may bring further optimisation. In terms of these principles, any service delivery system's capacity is determined by binding constraints causing bottlenecks. Therefore, higher capacity in the rest of the system is under-utilised. Managing constraints would entail either subordinating the capacity of the rest of the system to the capacity of the constraint, thereby saving costs, or removing the constraint, whereby capacity is increased. If municipal plant, equipment and expertise are constrained, the sharing of plant, equipment and expertise between municipalities could in principlr increase capacity. Fourth, the potential of reducing indirect and overhead costs by amalgamating small rural municipalities, deserve further investigation.

In summary, therefore, enhancing the ability to optimise existing revenue streams from rates, revolve around the following possibilities:

1. Enhancing the attractiveness for targeted categories of households to relocate (Municipal strategic planning, but district-wide initiatives may require District Development Model-type planning by all role players).
2. Enhancing further advances in optimising existing revenue streams through expanding capacity for data management and considering the mechanisms for increasing revenue from property rates proposed by the South African Cities Network 2018 State of City Finances Report.
3. Better utilisation of dormant capacity in service systems or reducing costs through constraint management combined with alternative delivery models (Municipal tactical planning, but district-wide initiatives may require DDM-type planning by all role players).

4. Investigating the feasibility of municipal re-demarcation with a view to amalgamate small rural municipalities (Provincial Department of Local Government and National Department of Cooperative Government).
5. Review the Municipal Property Rates Act and related legislation with a view to make allowance for affordable repayment arrangements for businesses.

8.2.4 Tradable services: balancing affordability and sustainability

Problem statement

The sale of basic municipal services, it is often argued, should be based on business principles as they are particular or specific services to which the benefit-received principle should be applied in full. However, no business will willingly engage in market-related initiatives where there are so many demand limitations, negative externalities, controls, restrictions and other interferences and risks to factor in, to the extent that they narrow profit margins to below generally accepted margins for sustaining liquidity. None of the basic services - electricity, water, sanitation and solid waste - are without ecological and social consequences, due to extraction and disposal limitations and harsh socio-economic realties. Although municipalities may not have competition like businesses, only the most competitively structured and managed institutions can remain financially and operationally sustainable. Understandably, even with the ability to provide such services competitively, the smaller the demand, the smaller the contribution margin to finance fixed and indirect costs when negative externalities, controls, restrictions and other interferences and risks put a lid on tariff increases. Smaller municipalities need a different solution. Alternative delivery models as discussed above have the potential to reduce fixed and indirect costs through achieving economy of scale between municipalities, but due to the costs related to externally determined political structures, remunerations, quality specifications, service standards, accounting systems, membership and audit fees, the fixed and indirect cost elements are still a heavy burden. In addition, unit costs are high due to longer service delivery distances and may even become higher with alternative models.

Recommendations

Recommendations are similar to that prosed for property rates: The interviews revealed a number of solutions that are already achieving positive results and deserve further consideration: First, by following deliberate strategies to make it attractive for households that can afford to pay for services to resettle, service delivery capacity can be better utilised and better economy of scale achieved. Second, the successes that municipalities have achieved in optimising existing revenue streams through cleaning up data; using cutting edge information and communication technology; financial modelling as well as a controlled degree of cross-subsidization between services in the interest of minimising the total municipal account for households, show that capacity for treading the fine line between affordability for households and financial and operational sustainable delivery by municipalities. The "Differentiated Service Affordability Model for the Basket of Services Provided by Western Cape Municipalities" (HS Business Solutions, 2019) provides for differentiating enabling baskets of services to groups of households and enabling basic baskets of services for informal settlements and indigent households as further step in this regard. Third, applying the principles of managing constraints may bring further optimisation. In terms of these principles, any service delivery system's capacity is determined by the constraints causing bottlenecks. Therefore, higher capacity in the rest of the system is under-utilised. Managing constraints would entail either to subordinate the capacity of the rest of the system to the capacity of the constraint, whereby costs are saved, or by removing the constraint, whereby capacity is increased. If, municipal plant, equipment and expertise are constrained, the sharing of plant, equipment and expertise between municipalities can increase capacity. If available input, e.g. raw water, is constrained during times of drought it may be a viable solution to reduce the whole water purification system to that constraint and allow a market to develop to permanently (not only during droughts) service further demand at market prices, using water extracted from different sources. Fourth, the potential of reducing indirect and overhead costs by amalgamating small rural municipalities, deserve further investigation. In summary, therefore, enhancing the ability to optimise existing revenue streams, revolve around the following possibilities:

1. Enhancing the attractiveness for targeted categories of households to relocate (Municipal strategic planning, but district-wide initiatives may require DDM-type planning by all role players);
2. Promoting further advances in optimising existing revenue streams through expanding capacity for data management and implementing the "Differentiated Service Affordability Model for the Basket of Services Provided by Western Cape Municipalities" (HS Business Solutions, 2019) (Provincial support);
3. Better utilisation of dormant capacity in service systems or reducing costs through constraint management combined with alternative delivery models (Municipal tactical planning, but district-wide initiatives may require DDM-type planning by all role players);
4. Investigating the feasibility of municipal re-demarcation with a view to amalgamate small rural municipalities (Provincial Department of Local Government and National Department of Cooperative Government).

8.2.5 New revenue sources

With the abolition of the Regional Services Council Levy in 2006/7, the RSC Levy Replacement Grant was introduced as an interim measure but – more than a decade since – DM's still have not been allocated an own revenue source. The RSC Levy Replacement Levy, according to the FFC, "defies all principles of a good grant instrument" (South Africa. Financial and Fiscal Commission, 2019, p. 51), but the Commission notes that the potential of any new revenue sources for DM's can only be completely tested and implemented once their assigned functions are clarified – currently there is substantial variation in the functions districts perform.

Changes to long term water and electricity consumption as well as proposed restructuring of those industries will erode current water and electricity surpluses, necessitating alternative revenue sources for LMs and metros as well. Without own revenue sources, municipalities have little agency in relation to their financial destinies, with funding decisions in the hands of other spheres of government. Moreover, breaking the link between revenue and expenditure dilutes accountability at the margin. But increasing levels of existing revenue sources or introducing new sources also requires a fair deal of political will and a longer term vision rather than a myopic focus on short term objectives and short term electoral outcomes. This is extremely difficult when there is political governance instability and poor working relationships between politicians and senior officials in a municipality. When new revenue instruments are introduced, it is also important that they aim to target new revenue bases, rather than creating a new instrument (with additional associated compliance and administrative costs) for what is essentially the same tax base. This would, for instance, be the case when a local business tax on payroll is suggested which is substantively identical to an existing instrument such as the skills development levy. There are already high costs of doing business in South Africa and excessive red tape, so the costs of adding to this should be borne in mind, especially for fragile businesses still reeling from the impact of the pandemic.

The FFC has advocated a differentiated approach to new revenue sources based on fiscal capacity. Metros and intermediate cities with their more vibrant economies have the greatest revenue potential, followed by smaller urban municipalities and district municipalities. Small rural municipalities, however, have much narrower and less diversified revenue bases, and high levels of poverty and unemployment which make reliance on intergovernmental transfers unavoidable. They also tend to lack the scope and sometimes the capacity to administer their existing own revenue sources much less new ones, and sometimes the incentive to raise own revenue when they can simply rely on grants. The ability to raise additional revenue is also contingent on the quality of services which a municipality renders. Attempts to raise additional revenue when service quality falls below standard will elicit fierce resistance from communities, as illustrated by ratepayers' associations withholding rates payments in protest at poor service delivery in other parts of the country.

Research studies have been conducted which have explored the policy, administrative and regulatory dimensions of either sharing existing revenue sources/reassigning them to local government or introducing new revenue sources. In respect of existing revenue sources, the South African Cities Network and the City of Tshwane have suggested property transfer duties (linked to local property markets), the fuel levy for municipal roads, vehicle licence fees and public transport permits. The new revenue sources proposed include a local business tax through a payroll tax or a tax on local turnover, city congestion charges and a tourism levy/occupancy tax. Their preferred options were a tourism tax/hotel occupancy tax in the short term and a local business tax in the longer term (South African Cities Network, 2019).

The FFC has also proposed tourism levies, in addition to development charges, fire levies for district and rural municipalities and land value capture mechanisms. Land value capture mechanisms include:

- The acquisition of land next to a public investment by a municipality which is then sold later when its value increases because of the public investment.
- Betterment levies: typically, once-off levies/taxes to capture the additional value of land resulting from investment in public infrastructure.
- Developer exactions: requiring property developers to install public infrastructure on-site at their own cost.
- Development impact fees: a once off levy charged on approval of a building permit.
- Sale or leasing of municipal land near new infrastructure and invest the proceeds in more infrastructure (South Africa. Financial and Fiscal Commission, 2019).

They have also considered street advertisement taxes (billboards), amusement taxes, and weigh-in bridges in mining areas, lease of fibre optic cables and sales of bandwidth, parking lot takes, air pollution, harbour taxes, licensing of mortuaries, dumping site usage fees. The lease of fibre optic cables and access fees could create an opportunity for rural municipalities where the private sector is reluctant to provide the service due to lower population densities and hence profitability, since the cost-plus surpluses they pursue might be lower than the returns required by the private sector.

The Municipal Finance Powers and Functions Act of 2007 (MFPFA) outlines a process for a new municipal tax to be proposed to the Minister of Finance which is quite rigorous and therefore onerous. Proposals should include the base, rate, incidence of liability for the tax, proposed exceptions, methods and costs of administration, estimates of anticipated revenues over the 3-year MTREF period, consultation processes and the impacts on individuals, businesses and economic development, amongst other requirements.

Previous attempts to propose a local business tax for metros via the MFPFA process had been rejected by the National Treasury on the grounds that the slow growth rendered the introduction of new taxes or increasing existing taxes inadvisable. Moreover, they argued that metros had not yet fully exploited their existing revenue sources, improved their consumer debt management or fully eliminated non-core expenditures. National Treasury's argument therefore rests on the case that there is no structural transfer funding gap, rather there is a fiscal effort and inefficiency gap. This line of argument is becoming increasingly difficult to sustain, as the systemic disjoints in the local government fiscal framework become increasingly clear.

National Treasury's response relating to the current fragile state of the economy is certainly a cogent one, because even after the lockdown ends, recovery may be protracted in hard hit sectors like tourism and hospitality. Nonetheless, as note in Section 5.2.1, the regional GDPs (GDP-R) varies markedly across the nine provinces and across municipalities in those provinces, with the Western Cape expected to recover much faster than most of the rest of the country. A computable general equilibrium modelling exercise could provide an assess the validity of this claim, and an evidence basis for the anticipated benefits and costs.

Depending on the nature and design of the proposed revenue instrument, a case can be made that the potential negative impact of the introduction of new revenue sources would be less for municipalities in the Western Cape where the GDP-R is expected to rebound rapidly, than for the rest of the country, and that negative spillover effects may therefore be constrained. Moreover, some Western Cape municipalities have the institutional maturity and capability to administer new revenue sources fairly and efficiently, and there is also opportunities for municipal cooperation in this area to achieve economies of scale in collection. While fiscal consolidation at national level results in material reductions in operating and capital grants as expenditure pressures to a large extent outside of individual municipalities, the rationality for blanket withholding of permission for additional tax sources by National Treasury becomes increasingly questionable. This is amplified by the long-term changes in the water and electricity industry and their impact on the local government fiscal framework outlined previously, which will entrench a structure transfer deficit.

Bearing this in mind, it is proposed that the Western Cape government requests the permission to pilot various revenue source options in the next 2 years so that their feasibility and collection outcomes relative to administrative costs can be assessed, with the intention to scale up the successful ones via the MFPFA process in the third year of the MTREF.

Recommendation

1. Western Cape municipalities should apply to National Treasury via the MFPFA to pilot revenue instruments which have been proposed (congestion charges etc) to more accurately gauge their feasibility in terms of impacts, potential revenue and administrative costs.
2. Municipalities (especially those with property portfolios) should investigate the feasibility of implementing land value capture mechanisms.
3. A "virtual municipalities" simulation based on actual data could be set up to enable sensitivity analyses to test the viability and impact of new sources of revenue.

8.2.6 Managing costs of employment pressures

All of the sampled municipalities are engaged in cost containment programmes. The scope for further cost reduction in non-personnel related spending categories is increasing as many municipalities already cut spending "to the bone", creating imbalances between personnel spending and the other complementary resource inputs required to delivery services. Therefore, more attention will have to paid to internal efficiencies and savings in respect of personnel costs. Sampled municipalities therefore have controlled overtime and froze the filling of vacancies, either entirely or with few exceptions for critical posts. Some of them are also re-evaluating the need for vacant posts entirely before filling them. Since skilled technical and professional staff are generally more mobile than their administrative counterparts, this form of personnel cost containment by attrition can result in imbalances between core delivery staff and back off administrative staff, as well as between the more skilled professional staff (e.g., engineers) and lower skilled core delivery staff.

As noted earlier, municipal personnel costs are largely a function of staff numbers, levels of wages/salaries and associated benefits (e.g. pensions, medical aid, housing allowances), increases in wages/salaries and associated benefits), notch increases, overtime, and performance bonuses. These are currently more generous than in public service on the national and provincial spheres and have been increasing well in excess of CPI inflation and the growth of revenue sources, such as the local government equitable share grant. In general, the increase in municipal cost of employment bill has been driven by increased average cost of employment per employee, while employee headcount tends to have stagnated or dropped.

The bulk of municipal employees' conditions of service are bargained centrally in the South African Local Government Bargaining Council (SALGBC). The 2020/21 financial year saw the implementation of the final leg of a three-year agreement resulting in an increase of 6.25%, CPI plus 1.25% (which is closer to 9% once benefit costs are included. The profound tension between centrally bargained terms and conditions of employment and decentralised budgets is one of the most fundamental and intractable contradictions inherent in South Africa's constitutional dispensation arising from the negotiated transition to democracy in 1994. The collective bargaining system is labour relations oriented, large geared at individual employers, whereas government, the single largest employer in the country, is not analogous to an other employers in that it also has a responsibility to consider the macroeconomic impact on the entire country from a public finance perspective. Yet there is no formal role for the National Treasury, the custodian of macroeconomic policy in this process. This point was emphasised in a SALGBC circular on 30 July 2020 which stressed that the National Treasury is neither a party nor a signatory to the salary and wage collective agreement, in response to the Treasury's unsuccessful attempt to request that SALGBC parties review and moderate the negotiated increase for 2021 in the light of the catastrophic impact of the lockdown on the fiscus, and SALGA's subsequent attempt to re-open negotiations (SALGBC, 2020).

Given that individual municipalities have very little influence in this process, the only option to municipalities that are unable to afford such increases without compromising repairs and maintenance, capital expenditure and other forms of service delivery, is to apply for exemption. Despite a deterioration in municipal finances in 2020/21 due to the pandemic, only 12 municipalities applied for exemption, most of them from the WC (SALGBC, 2020).

Upper limits for the remuneration of municipal managers and the senior managers reporting to them were regulated for the first time in 2018 (in terms of the Municipal Systems Act), in a bid to create some uniformity across the sphere. However, there may be unintended consequences from this regulation. For example, in the past, mid-level staff in cities would assume more senior positions in rural municipalities, creating a talent pipeline. But some of the interviewed municipalities have indicated that now there is frequently little incentive for mid-level managers in urban areas to assume greater responsibilities in more senior positions in rural municipalities for less remuneration. It is important that an impact evaluation of this regulatory instrument be conducted.

Another option which has been mooted is greater standardisation of municipal organisational structures to promote greater rationalisation through regulation. Regulation is however a blunt instrument which is insensitive to the huge variation in municipal contexts (e.g. delivery models, socio-economic profile, size, settlement patterns, demographics and asset bases) and may be resisted as unwarranted incursion into municipalities' constitutional right to govern the local government affairs of their community on their own initiative. A principle of public financial management (which also underpins the Municipal Finance Management Act) is municipalities can only be held accountable for output delivery if they are given sufficient managerial discretion over inputs. Given that municipalities have little control over increases in compensation of employees, further constraining their action space might be counter-productive and just add another layer of regulation onto an already burdensome load. This approach also implicitly assumes that national and/or provincial governments are more efficient at organisational design than municipalities, and that regulation is capable of being enforced. If existing regulation such as minimum competence standards for employment cannot be enforced effectively, it is unlikely that new regulation will fare any better. Moreover, IDP and other sector plans of the municipality should inform the organisational design, so that "form follows function". Forcing municipalities into more uniform, symmetrical categorisations undermines this principle and could mean that functional WC municipalities which are handling their own personnel budgets responsibly, are deprived of flexibility to deal with a few cases of poor management. Addressing the root causes in these instances might prove more fruitful: the lack of political will to make hard trade-offs in support of longer-term sustainability and strengthening consequence management at political and administrative levels for creating bloated, unfunded establishments.

While the Municipal Systems Act requires that municipal managers review staff establishments regularly, there is very little information linking costs of employment with productivity and performance. Productivity studies therefore should become mandatory at least once in five years, to inform staff establishment and delegations reviews. These could also be used to develop productivity benchmarks (e.g the balance between administrative and core delivery spending in the municipality as a whole and across individual services) and disseminate the good practices of the most efficient municipalities in the Province and further afield.

Recommendations

1. Where municipalities cannot fund nationally negotiated agreements on costs of employment, they should apply for exemption.
2. The WC provincial government should propose to the national Minister of Cooperative Government and Traditional Affairs that at least once every five years, municipalities should conduct productivity studies resulting in recommendations to inform the review of staff establishments, organizational design and delegations. These should be tabled at Council which should be required to explain how they intend to respond to the recommendations.
3. Good practice productivity benchmarks for municipality as a whole and individual services should be developed e.g. to balance administrative and core delivery spending. This could not only improve internal efficiency but promote civil society oversight.
4. An impact evaluation of the 2018 upper limits on the remuneration for senior management should be done, with a view to improving the effectiveness of these regulations and minimising unintended consequences.
5. Where practical, work-from-home and online meeting practices developed during the pandemic should be maintained, in order to attract and retain staff with scarce skills and reduce travel and subsistence costs (especially for the more distant, rural municipalities). These can also facilitate the sharing of human resources among municipalities, since travel time between municipalities could be vastly reduced.

8.2.7 Free Basic Services and indigency

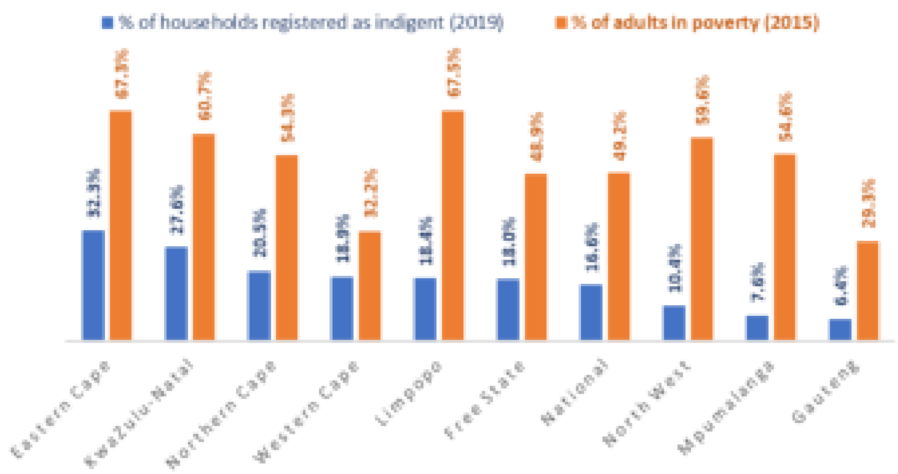
Problem statement

A number of factors have led to increases in the number of low income and indigent households across the country, and in the WC. These include a sluggish, fragile economy with record level unemployment and poverty, even prior to the pandemic. While the analysis of the sampled municipalities in this report suggests that the LGES grant adequately covers free basic services, increased developments of low-cost housing and growing informal settlements not only add to current and future operating costs but also fail to develop the future revenue base of municipalities.

The non-financial census of municipalities across South Africa indicates that the number of registered indigents is declining, despite increased poverty and actual indigence levels, caused largely by municipalities changing the targeting mechanisms of their indigent policies. The 2019 Non-financial Census of Municipalities shows that the number of indigent households registered with South African municipalities nationwide decreased from 3.6 million in 2017 and 2018, to 2.9 million in 2019 (Statistics South Africa, 2020). Of these, 12.9% (or 372 545) reside in the WC. The graph below compares the percentage of households which registered as indigent in each province as a proportion of the provincial population, with the percentage of the adults living in poverty in that province, according to the Living Conditions Survey 2014/15

It is clear that the municipalities in the WC have fared better than their counterparts in other provinces in terms of coverage. In the WC, 18.9% of the households are registered as indigent, while 32.2% of its adults are living poverty. By contrast, Gauteng has a lower poverty rate among adults of 29.3%, but only 6.4% of its households are registered as indigents. Limpopo and the Free State have roughly the same proportion of indigent households registered (around 18%), but much higher poverty rates of 67.5% and 48.9% respectively, which suggests higher levels of exclusion. The Eastern Cape, KwaZulu-Natal and the Northern cape have higher levels of indigent registration, but they also have much higher poverty rates, suggesting greater exclusion.

FIGURE 49: COMPARISON OF PERCENTAGE OF HOUSEHOLDS REGISTERED AS INDIGENT AS A PROPORTION OF TOTAL PROVINCIAL HOUSEHOLDS (2019) AND THE PERCENTAGE OF ADULTS LIVING IN POVERTY BY PROVINCE (2015)



Sources: Statistics South Africa (2020) Non-financial census of municipalities; Stats SA (2015) Men, Women, Children: Findings of the Living Conditions Survey 2014/15

The decreasing fiscal space available to WC municipalities means that it may be harder to extend the indigent support so desperately needed by poor communities. As concluded earlier in this report, the estimates of sampled municipalities for increases in the numbers of indigent seem to increase slowly over the MTREF while poverty is set to increase. The credibility of these assumptions needs to be further interrogated.

Recommendations

- Municipalities should ensure that their projected increases in indigent households are realistic.

- A consolidated provincial data set on households receiving FBS should be created to assist in identifying vulnerable households in the event of a national disaster such as a pandemic, and to track the impact of the free basic services policy with a view to impact evaluation.

8.3 Institutional sustainability factors

The following institutional factors are discussed below: affordability political structures, revenue uncertainty in agency services agreements, shared services, public-private partnerships, municipal cooperation, the social development focus of district municipalities and audit fees.

8.3.1 Affordability of political structures

Problem statement

Maintaining and supporting the political structures of a municipality contribute to the indirect costs of a municipality. The related costs include cost of employment of dedicated, permanent administrative support staff. The demands for the extent of support for political structures vary across municipalities. However, where politicians prefer to select their own support staff, and when employment contracts are permanent or not aligned to the electoral cycles, staff redundancy develops. For the smaller municipalities and district municipalities, these costs incurred are proportionally bigger and less affordable due to the limited revenue realised from service delivery and shrinking intergovernmental transfers.

Recommendations: The size of councils for different size municipalities has been a topic for consideration from representation and oversight point of view, but the full cost of maintaining and supporting political structures and controls to prevent excessive demands for support deserve further consideration. The costs of maintaining and supporting political structures also contribute to indirect costs that determine at which point a municipality cannot maintain its financial and operational sustainability because it generates inadequate revenue. If it is endeavoured to improve financial and operational sustainability, all such costs need careful reconsideration. In summary:

- The cost of political structures and control support costs can be enhanced by issuing guidelines and norms and, as a last resort, by means of prescripts where excessive compared to own revenue, population size and other guideline benchmarks (Provincial Department of Local Government and national Department of Cooperative Government).
- The feasibility of municipal re-demarcation should be investigated, with a view to amalgamate small rural municipalities (Provincial Department of Local Government and national Department of Cooperative Government), or create single tier rural municipalities.

8.3.2 Revenue certainty of agency funding arrangements

Problem statement

Municipalities engage in the delivery of agency services on behalf of the provincial government (e.g. DMs provide road agency services). Some of these agreements appear to be ad hoc, annually renegotiated, not formally gazette and therefore subject to change and therefore not creating funding certainty for municipalities in the MTREF outer years. However, delivering those services engender expenditure commitments for municipalities, such as personnel and may also require investment expensive or specialised equipment with extended payback periods which would take time to recoup. Furthermore, this situation may lead to audit issues if not resolved.

Recommendation

All agency agreements should be formalized and duly gazetted with the aim of providing at least a minimum degree of funding certainty for municipalities over the MTREF period and avoid audit queries.

8.3.3 Alternative delivery models: shared services

Problem statement

Shared services, for the purpose of summarising the issue, refers to the sharing of resources and internal processes amongst municipalities, while joint service delivery refers to combining efforts to deliver services. Shared and joint services represent in particular examples of networked governance that theoretically, and from international best practices, offer enhanced economy, efficiency and effectiveness in service delivery, as well as enhanced positive societal outcomes that tend to transgress boundaries of jurisdiction.

The first-round interviews revealed that this alternative model is not rejected because respondents do not understand the benefits, but because currently, cumbersome legal processes outlined in the legislation and externally induced controls make them unattractive to implement and sustain. The strong negative opinions expressed by all local municipal respondents served to flag this as matter to be further explored in the in-depth interviews.

The in-depth interviews again did not reveal strong aversion against either shared/joint services or the legal processes derived from prescripts, externally induced controls or court judgements, but a very pragmatic response to these – namely not to do shared/joint services! This response suggests that the perceived transaction costs due the regulatory environment so far exceed the potential benefits that it is not even worthwhile to attempt overcome these regulatory impediments. This may be a perception due to the overwhelming emphasis on the regulatory, control environment and clean audits in judging – and holding municipalities accountable for – inputs, process compliance and outputs (financial and operational sustainability), rather than evaluating societally beneficial outcomes (financial, social and ecological sustainability). As was indicated in the interviews report, the financially and operationally sustainable municipalities are doing well by strengthening their own resilience in traditional service delivery models at the cost of opening opportunities for longer-term comprehensive sustainability through more agile arrangements. Shared/joint services also have an institutional behaviour implication: that different institutions with different institutional cultures, must work together.

Where joint services are necessitated by externally induced prescripts such as is the case with landfill management, these come at a higher price for individual local municipalities and invariably higher tariffs.

None of the findings from both first-round and in-depth interviews on how to survive financially and sustain operations indicate the need for engaging in shared services. In fact, given that relationships between political executives and senior management, and amongst senior managers and communication with communities - as well as in-depth and very sophisticated planning approaches - enhance financial and operational sustainability, the alternative of shared/joint services is just not attractive, as complexity, increased transaction costs and conflicting priorities are increased by widening the circle of role-players. It also becomes commensurately harder to enforce service level agreement standards.

Recommendations

It is safe to state that there are circumstances where shared or joint services are more cost-effective than traditional service delivery. However, the decision to depart from the traditional and embrace shared/joint service delivery as model, cannot be a decision enforced through further prescription and more controls emanating from national or provincial decision making and applied as context-insensitive blueprint to all municipalities. The space for expanding the potential for shared/joint services must be enlarged by streamlining the regulatory and oversight environment and eliminating the impediments, strengthening the consequences of service delivery failure, place greater emphasis on societal outcomes and enhancing the capacity for delivery by shared services. Currently, the more sustainable municipalities have the capacity to use analytical techniques such as cost-effectiveness analyses and feasibility studies, and engage in institutional change management initiatives that will make shared/joint services a viable option, but they do not need it. The less-sustainable municipalities do not have the capacity even though they have the need. In summary therefore, to the extent that shared/joint service delivery may be a more sustainable option, it requires the following reforms:

1. Removing or reducing regulatory impediments to shared services (national reform);
2. Strengthening consequences for council, the political executive and senior management of service delivery failure (national reform);
3. Introducing outcomes evaluation: The 2019 National Evaluation Policy Framework (NEPF) has set the objective of ensuring local government successfully institutionalises the practice of evaluation and this should be encouraged. Evaluation must go beyond compliance-oriented audits of performance for accountability purposes to provide for learning and critical self-reflection;
4. Enhancing capability for shared services by way of seconded personnel, capacity building, risk management and good practice initiatives for successfully introducing shared/joint services as a viable option (provincial responsibility);
5. Creating a community of practice and safe space for small-scale “sandbox”-type controlled experiments on shared/joint services, which bring together highly experienced local government practitioners, sector professionals and researchers to jointly develop innovative solutions (Local and provincial government, regional offices of national departments and research institutions).

8.3.4 Public-private partnerships (an operational perspective)

Problem statement: Similar to shared services, public-private partnerships, theoretically, and from international best practices, offer enhanced economy, efficiency and effectiveness in service delivery, as well as enhanced positive societal outcomes that tend to transcend boundaries of jurisdiction. Although PPPs have received some expressions of preference in South African policy practices, they are not free of controversy or contestation. This is due to the fact that PPPs constitute a phenomenon with a variety of meanings and applications, i.e. for a specific project, for example a delivery model of specific infrastructure; for a policy preference; or as a governing mechanism. Another reason is that a PPP is not a single delivery model, but provides a massive range of options. While procurement policies tend to refer to PPPs as a very particular type of long-term infrastructure contract type, there are actually many possible different contractual arrangements. There is no such thing as '*the*' PPP model. It is therefore more challenging to argue that PPPs as alternative delivery model would be inherently more financially sustainable than traditional service delivery models, but what is needed is rather to determine when a particular PPP configuration is a better option than conventional delivery. On the upside, capital funding and risk-taking by the private partner rather than the public institution make it attractive in principle, but on the downside one of the issues is the loss of flexibility that comes with the long-lived contractual obligations governments must respect in a PPP. This is especially salient in local government where decisions by one council would bind future councils for 20 to 30 years, and once the municipality has lost the capacity to fulfil the function, it is very difficult to reverse.

An example of a PPP that did not deliver on the expectations is the public-private partnership for developing the Gouriqua regional landfill site in the Garden Route District, which was thwarted when the private partner could not fulfil its commitments. The initiative has first been delayed, and eventually cancelled when the private partner could not continue. Therefore, an example where a PPP rather than enhancing resilience against disasters, became a victim of the disaster!

Another failed attempt at a PPP is currently (March 2020) unfolding in the Western Cape, namely the proposed Kannaland PPP. In *Executive Council of the Western Cape Province and Others v Kannaland Local Municipality and Others* [2021] ZAWCHC 51 (19 March 2021), the Western Cape High Court interdicted the Kannaland Municipality from proceeding with a proposed PPP for the provision of energy, water and information technology for a 25-year period. The court found that a range of regulatory requirements had not been met by the municipality and that there were serious doubts about the affordability of the project, especially given the financial challenges facing the municipality.

Further analysis of these and other PPP examples could provide valuable lessons for future PPP contracting. Minnie (2011) did a PhD on critical success factors for public-private partnerships in South Africa, which provides a useful framework for analysing the three cases. But, the fact of the matter is, we also need compelling PPP success stories.

These two failures nevertheless illustrate what was also learned from the interviews, namely that public-private partnerships represent a much more complicated alternative service delivery model that calls for well-informed transaction advisors and funding to package the project (e.g. feasibility studies) in addition to navigating through the complicated and protracted legal process and getting politicians on board. The respondents did not reject PPPs because they did not see the benefits, but because cumbersome legal processes outlined in the legislation and externally induced controls make them cumbersome to implement and sustain. According to the Budget Review (National Treasury, 2021), there has been a review of the regulatory framework for PPPs: "The regulatory framework review includes PPPs regulated by the Public Finance Management Act (1999) and the Municipal Finance Management Act (2003). The public and private sectors have contributed important suggestions, which, alongside lessons learnt, have been incorporated into the draft final recommendations report. The National Treasury will present the recommendations at a validation workshop in March 2021 to stakeholders and PPP practitioners before formally adopting the recommendations. After the workshop, the approved recommendations will be published on the National Treasury website. These recommendations will be implemented in 2021/22".

Recommendations

As in the case of shared services as an alternative delivery model, it is safe to claim that there are circumstances where the range of PPP configurations provide more cost-effective solutions than traditional service delivery models. However, the decision to depart from the traditional and adopt a particular PPP model, can also not be a decision enforced through further prescription and more controls emanating from national or provincial decision making and applied as context-insensitive blueprint to all municipalities. The space for exploring the potential of a customised PPP must be enlarged by streamlining the regulatory and oversight environment and eliminating the impediments (i.e. implementing the recommendations of the National Treasury Report), by strengthening consequences of service delivery failure, by evaluating societal outcomes and by enhancing capacity for delivery by PPPs, which could include public-community partnerships for creating greater positive externalities. Currently, the more sustainable municipalities may have the capacity and even the strategic-tactical thinking to use analytical techniques such as cost-effectiveness analyses, feasibility studies, modelling and design special contracting options for PPPs, and engage in institutional capacity development and change management initiatives to create workplace acceptance and protocols for such co-production, but the incentives for adopting it are mostly still not low hanging fruits ripe for the picking. The less-sustainable municipalities do not have the capacity even though they have the need. In summary therefore, to the extent that PPPs as range of alternative service delivery models may be more sustainable, the following reforms are required:

1. Removing or reducing regulatory impediments (national reform, implementing National Treasury recommendations);
2. Strengthening consequences for council, the political executive and senior management of service delivery failure (national reform);
3. Introducing outcomes evaluation;
4. Providing capacity (including grant funding for feasibility studies) for successfully configuring a PPP as a viable option (provincial responsibility)

5. Creating a community of practice and safe space for small-scope "sandbox"-type controlled experiments on PPPs which bring together highly experienced local government practitioners, sector professionals, legal experts and researchers to jointly develop innovative solutions (Local and provincial government, regional offices of national departments and research institutions).

8.3.5 Alternative service delivery models: co-production and the District Development Model

Problem statement

In the State of the Nation Address 2019 (SONA 2019) the President indicated that the practice of operating in silos has led to a lack of coherence in planning and implementation, and has made monitoring and oversight of government's programme difficult. The consequence has been non-optimal delivery of services and lack of success in combating triple challenge of poverty, inequality, and unemployment.

As remedy, President Ramaphosa launched the District Development Model (DDM), which entails an, "integrated district-based approach to addressing service delivery challenges through, among others, localised procurement and job creation that promotes and supports local businesses, and involves local communities. It calls for One District, One Plan, and One Budget" (Parliament of the Republic of South Africa, 2019: 1)[5]

The DDM, according to Parliament's Research Unit, "aims to accelerate, align and integrate service delivery under a single development plan per district or metro that is developed jointly by national, provincial, and local government, as well as business, labour, and community in each district. It further ensures that national priorities, such as economic growth and employment; improvements to living conditions; the fight against crime and corruption, and better education outcomes are attended to in the locality concerned" (Parliament of the Republic of South Africa, 2019: 2). Planning and spending across the three spheres of government would be integrated and aligned, with each district or metro plan developed taking the interests and input of communities into account upfront. The DDM is a clear expression of networked governance and its concomitant notion of coproduction. It links output (municipal service delivery) to desirable outcome (successfully combating poverty, inequality, and unemployment), with alignment of resources and plans of all role players to ensure that the outcomes will be achieved.

The interviews revealed lack of enthusiasm for the DDM amongst respondents. Whereas in other provinces districts may be more capacitated than their associated local municipalities, the Western Cape generally has very strong local municipalities. Furthermore, Section 156(4)(4) of the Constitution, 1996 determines that "the national government and provincial governments must assign to a municipality, by agreement and subject to any conditions, the

[5] Parliament of the Republic of South Africa. 2019. "Overview of the District Development Model – A Framework for Co-Operative Service Delivery". Research Paper. Cape Town: Research Unit.

administration of a matter listed in Part A of Schedule 4 or Part A of Schedule 5 which necessarily relates to local government, if -

(a) that matter would most effectively be administered locally; and

(b) the municipality has the capacity to administer it."

This suggests a constitutional element of subsidiarity favouring the lowest level of delivery where the requisite capacity to deliver exists.

Further reasons for lack of enthusiasm include: the predominance of output-driven formal accountability systems; the power of restrictive prescripts; output-driven performance competitiveness; conflicting institutional cultures; the danger of shifting planning further away from the grassroots; the implied power-authority relationships and the blueprint characteristics of the model:

- *The predominance of output-driven formal accountability systems*: The Auditor General (emphasising compliance-driven clean audits and performance to mandate) and National Treasury (regulating financial, accounting and reporting systems, setting annual budget frameworks and conditions for "unconditional" grant allocations) are regulators of local government and the systems of accountability they apply dominate the actions of municipalities. These are generally input-process-output and jurisdiction-oriented systems that direct the energy to compliance and conformance. In addition, accountability to local councils with their various oversight committees and the fostering of positive working relationships with them takes up time and effort of senior management. Working with multiple oversight structures in a district understandably may be too much to get anything done. This is why a number of respondents indicated that the establishment of rural metros, each with one council, would work better.
- *The power of restrictive prescripts*: This topic has been explained under the heading of shared / joint services. An alternative model that requires working across geographical and functional areas of jurisdiction is not rejected because respondents do not understand the benefits, but because currently, cumbersome legal processes outlined in the legislation and externally induced controls make them unattractive to implement and sustain.
- Output-driven performance competition: Public regulators and private analysts analyse municipal data such as financial ratios and the publicity from their findings has created a competitiveness for being at the top of the ratings. Being competitive is commendable, but the alignment of effort towards this competitiveness may inadvertently cause neglect of that which is not measured.
- Conflicting institutional cultures: Competitiveness as mentioned above instils a high-performance institutional culture. From the analyses, it is clear that most Western Cape local municipalities are high-performing under circumstances. Like any competitive high-performance team, success comes from the concerted effort of all involved and there is no room for under-performers. This was very evident from the interviews. The dilemma is that such teams find it difficult to merge with other teams, because of differing ways of achieving success, especially if the other team is not so high performing and does not go to the same lengths to align efforts. The lack of high-performance local municipalities in other provinces (as measured by the analysts, not by the research team responsible for this report), may create circumstances that are more conducive for developing stronger

district municipalities, and may therefore be more conducive for the introduction of the DDM, but it does not automatically imply better outcomes as the debris of cultures creating low-performance, such as resource waste, incapacity, poor work discipline and unethical conduct may still be present.

- The danger of shifting planning further away from the grassroots: Both the processes to be followed in adherence to prescripts for integrated development planning (IDP) and the summary of findings on how to survive financially and sustain operations in the interviews report emphasise continuous and meaningful engagement with communities. Individual residents, households, community-based organisations and local businesses must not be allowed to experience the municipality as impenetrable fortress. The DDM may have the unintended consequence of pooling the customised needs of individual communities with that of too many other communities and other role-players, resulting in less sensitivity for such needs.
- The implied power-authority relationships and direction of enforcements: Although the Constitution carefully recognise the authority of each sphere of government rather than each level of government, the *de facto* situation is still that local government is subordinate to other spheres of government. Although the IDP process was intended to integrate all development needs in one geographical area, its credibility depends on the buy-in of all provincial and national departments and entities, which were so far often absent due to different priorities resulting from different priority-setting processes. By shifting the direction of enforcement even more towards being top-down, local priority-setting may be further compromised.
- The blueprint characteristics of the model: One size fits all does not work, but the DDM may unintentionally follow uniform procedures and adopt policies and practices that are not well-aligned with local circumstances and may actually result in poorer service delivery, i.e. compromising the output expected of municipalities.

Recommendations

The need to achieve desirable outcomes such as reduced poverty, inequality and unemployment is incontestable. Any "Theory of Change" also recognises that planning starts from intended outcomes, and then do reverse alignment of the outputs, internal processes and inputs of all role-players that can be related to the outcomes. That aim and objectives of the DDM are commendable. New models such as the DDM cannot however be enforced, but should come from the conviction and need to change or expand on what is delivered. Then the space for a model to achieve that should be created before embarking on processes that may lose momentum due to an inability to successfully navigate the combined impediments of the previous systems together with that of the new systems, and the debris of past failures (such as resource waste, incapacity, poor work discipline and unethical conduct). Institutional maturity is a prerequisite. Just like an individual cannot enter into a meaningful relationship with another (especially with a view to achieve outcomes not typically achievable as individual, e.g. raise a family) without first being able to self-manage, organisations need that same quality to meet the challenges of sophisticated multiple relationships as equal partners For DDM's to deliver better on outputs and achieve desirable outcomes, the following need to be in place:

1. Removing or reducing regulatory impediments (national reform);

2. Strengthening consequences for council, the political executive and senior management for service delivery failure (national reform);
3. Cleaning up causes of poor output delivery, such as resource waste, incapacity, poor work discipline, unethical conduct and politicking – the latter is especially vital as can be expected that councils with different majority parties must work together (Department of Cooperative Governance and Provincial Department of Local Government);
4. Strengthening outcomes-based planning, configuration, monitoring and evaluation to be on par with output-driven accountability (Department of Cooperative Governance and Provincial Department of Local Government);
5. Providing capacity for successfully configuring a DDM as a viable option (Department of Cooperative Governance and Provincial Department of Local Government);
6. Creating a community of practice and safe space for small-scope "sandbox"-type controlled experiments on shared/joint services which bring together highly experienced local government practitioners, sector professionals and researchers to jointly develop innovative solutions (Local and provincial government, regional offices of national departments and research institutions).

8.3.6 The social and economic development focus of district municipalities

Problem statement

This research project has once again shown that the allocation of functions and funding to District Municipalities remain subject to much uncertainty and asymmetry. Clearly, the current funding model for DMs is flawed, and given the government's financial crisis, grant allocations do not keep up with cost increases. The District Development Model implies a much bigger district coordination role, making them ideally positioned as intermediary between national and provincial departments, businesses and agriculture, and with regards to especially social development and environmental protection where local municipalities' reach fall short. They however require capacity to fulfil such a role, and the buy-in from local municipalities. All four the DM's interviewed have found themselves roles in this intermediary space: West Coast in water concessions, Cape Winelands and Central Karoo in rural social relief and social development and Garden Route in housing provision as agent for the Provincial Department of Human Settlements. All are involved in fulfilling road maintenance functions for the Provincial Department of Transport and Public Works as well as environmental health and fire services. These are done on a reimbursement for costs basis, and therefore do not in the current financing arrangement, point at an emerging model that could lead to more predictable and manageable revenue flows. All four the DM's interviewed also demonstrated an appetite for exploring district-specific and district-wide innovative possibilities for revenue generation and economic development.

Recommendations

The extent to which District Municipalities will be given a more financially sustainable niche in the emerging DDM, through supporting and widening their scope of options for exploring unique district-specific and district-wide innovations that would enhance their own revenue-generation capacity, deserve further consideration. In addition, the role of district municipalities in coordinating initiatives to better utilise local dormant capacity in existing service systems or doing constraint management by discarding dormant local capacities and adopting alternative delivery models, especially in deep rural areas should be explored. The establishment of fully integrated rural metropolitan municipalities with a single council, is a matter for serious consideration between affected local municipalities, the district municipalities, the Provincial Department of Local Government and the Department of Cooperative Government. The options can be summarised as follows:

1. Supporting and widening the scope of options for unique district-specific and district-wide innovations that would enhance the revenue-generation capacity of district municipalities and support district-wide local economic development (Provincial Department of Local Government);

2. Better utilisation of dormant capacity in service systems or reducing costs through constraint management combined with alternative delivery models (District-wide initiatives may require DDM-type planning by all role players);

3. Investigating the feasibility of municipal re-demarcation with a view to amalgamate small rural municipalities (Provincial Department of Local Government and National Department of Cooperative Government), or create single tier rural municipalities.

4. Assessing the feasibility of formalising the social development role of district municipalities.

8.3.7 Audit costs

Problem statement

Interviews with sampled municipalities indicate that the cost of compliance with financial compliance requirements (such the municipal Standard Chart of Accounts, and annual audit fees) is high, and diverts resources from other critical service delivery. In one of the interviewed municipalities, the cost of audit fees exceeded the limited budget available for vehicle replacement. On the other hand, audits are crucial for accountability, transparency and good governance, and so an appropriate balance must be struck.

Recommendation

- The provincial government should propose to the National Treasury and Auditor-General a reform whereby municipalities with clean audits for the last three years, are audited every two years instead of annually. This approach is risk based, grounded in objective criteria, and rewards municipalities which have demonstrated their institutional maturity and the soundness of their control environments.

8.4 Regulatory factors impacting municipal operational and financial sustainability

8.4.1 General observations on regulatory impacts

At a general level, local government is a highly regulated area, which implies that all activities are subject to specific and fairly detailed regulatory prescripts. There are too many regulatory instruments that are not adequately aligned resulting in regulatory overload (SALRC 2019). Linked to very strict compliance systems, e.g. via Auditor-General audits, the result is a high compliance culture, which is extremely risk averse and not agile. The focus in local government operations becomes increasingly on compliance only as opposed to development and responsiveness.

In respect of local government finances more specifically, it must be noted that the key regulatory framework, namely the MFMA, has been on the statute books since 2003 and there has been no notable review of this framework. The question must thus be asked whether the regulatory framework is still fit for purpose nearly two decades later. The general sense of increasing focus on compliance to the detriment of service delivery and development suggests that the original intent of the public finance framework namely, to allow local government managers to effectively manage, is not being achieved. Instead, the focus of the municipal finance framework seems to increasingly be on micro-level controls.

The expanding regulatory regime is also characterised by a lack of regulatory co-ordination. There seems to be very little attention to coordination of various regulatory regimes as they impact at local government level. Nobody seems to be focusing on the system-wide impacts of distinct pieces of regulation and regulatory decisions e.g. the impact of NERSA's decisions regarding Eskom rates and municipal tariffs or the impact of the regulation of the upper salary limits for senior management on rural municipalities. Little attention seems to be given to engaging with the operational and financial sustainability consequences of individual regulatory prescripts at local government level prior to implementation. Increasingly, regulatory instruments seem to reflect hierarchical national priorities with less local input and less funding going down to meet the implementation demands of those national priorities at local government level. The implementation of regulatory prescripts at local government level suggests a mismatch between the constitutional design of local government as an equal and fully-fledged sphere of government and reality in terms of which local government is largely still viewed as a secondary implementation agent of other levels of government, much like under the previous constitutional design.

Closely linked to the problem of ineffective coordination and planning in the design of regulatory interventions is the absence of reliable and comprehensive data of local government operations. In the absence of reliable, accessible, comprehensive and consistent data about local government operations is becomes extremely difficult, if not impossible, to do adequate analysis of the implementation implications of any proposed regulatory intervention. While it is widely recognised that proposed legislative instruments, at least in the form of primary legislation, must be accompanied by regulatory impact analyses, including cost analyses, such analyses become meaningless in the absence of appropriate data. Furthermore, there is no general practice of secondary forms of legislation, such as new regulations or regulatory decisions, being subjected to impact analyses.

One of the main problems in this respect is the reality that while regulatory instruments are routinely designed within a particular (national) sectoral framework, with narrow, sectoral considerations in mind, they must eventually be implemented within the integrated reality of a local government. At the municipal level, many different sectoral instruments are simultaneously brought to bear in a single context and municipalities are faced with the challenging task of reconciling disparate regulatory instruments that were not designed from this integrated perspective. These challenges do not only emerge from the potential incompatibility of, or tension among, various regulatory prescripts, but simply from the cumulative effect of their simultaneous implementation. Within current regulatory design practices, very little coordinated attention, premised on reliable, appropriate data, is given to this cumulative and integrated implementation reality.

The problems regarding inadequate impact assessments are exacerbated by a tendency to pursue unaffordable (national) norms and standards, e.g. in the context of environmental health, fire services or environmental protection. While these norms and standards are undoubtedly important, the question must be asked whether they represent *minimum* norms and standards or gold standards. The question is accordingly to what extent these standards can be implemented within the reality of South African local government. It seems of little use to put gold standards on paper, but they cannot realistically be implemented. Questions emerge in this regard about the involvement of entities meant to represent local government views, such as SALGA and COGTA, in the adoption of these standards.

Recommendations

The approach to regulatory design should be reformed to allow for more coordinated methodologies and ongoing review of the adequacy of existing regulatory frameworks. It is noted that the South African Law Reform Commission is currently engaged in a project on the *Review of Regulatory, Compliance and Reporting Burdens Imposed on Local Government by Legislation, Project 146* (SALRC 2019). It has published one issue paper on the project, calling for public comment in 2019. The reforms proposed here could logically contribute to that larger process. The following reforms are proposed:

1. Rationalise the regulatory environment.
2. Pay closer attention to differentiation between different local government contexts in regulatory regimes.
3. Consider more collaborative operational models and determine the extent to which the regulatory environment facilitate or prohibit such collaborative approaches.
4. Institutionalise meticulous impact assessments of all new regulatory prescripts from an implementation perspective, based on comprehensive, reliable data.
5. Scrutinise all new norms and standards closely to determine whether they in fact represent minimum norms and standards or gold standards.
6. Ensure that findings of impact assessments are adequately internalised across the regulatory framework, including in funding decisions.
7. Move away from a paradigm of national agenda-setting that informs regulatory prescripts that are forced down on local governments to simply implement in favour of a model where local governments drive the regulatory agendas from the bottom up, both in terms of setting the agenda and priorities and in terms of the content of regulatory instruments.

8. Further research on the formulation of regulatory prescripts, including norms and standards, in particular areas is required in order to identify the presence or absence of local government perspectives, and by implication implementation perspectives, in such formation processes. The results of such research will be important to formulate appropriate reforms.

8.4.2 Supply chain management: a regulatory perspective

Problem statement

Supply chain management is probably the prime example of the regulatory overburdening discussed in general terms above. Instead of facilitating agile and innovative acquisition practices that can strengthen strategic objectives, SCM has become a compliance minefield.

The local government SCM regulatory regime pays lip service to the MFMA's intention of enabling municipalities and their managers to manage their own affairs in ways that are appropriate to their context. Instead, it prescribes a rigid one-size-fits all approach. For the highly developed, resourced and capacitated municipalities, this framework only serves to slow them down and prohibit them from engaging in more strategic SCM practices. For the less developed, resourced and capacitated municipalities, the SCM framework presents an unachievable standard. In none of these contexts, the SCM framework achieves the objectives of the system of acquisition envisaged in section 217 of the Constitution. These realities are for example illustrated in the strict rules governing composition of bid committees where some municipalities do not have enough senior managers in place to constitute a committee. Another inappropriate one-size-fits all example is the rule that at least three quotations must be obtained, which could generate unintended and adverse results in rural contexts.

As with the MFMA regime generally, the SCM regulatory framework has been ossified SCM practices and has not kept up with developments. For example, the threshold for use of competitive bidding at local government level set in 2005 under the Municipal SCM Regulations at R200 000 is too low. The cost of running a full competitive bidding process for contracts just over this threshold probably exceeds the cost benefits to be achieved by the method and may even exceed contract value. The recently proposed adjustments to these thresholds are still inadequate and the differentiation between DM and LM does not make sense in all contexts.

The SCM regulatory regime is largely focused on the paradigm of individualized and transactional acquisition as opposed to collaborative, relational approaches. The potential mechanisms that do exist that can enable collaborative approaches, such as inter-organ of state contracting, PPPs and joining another entity's contract, have been increasingly narrowed down in the increasing compliance focus. These mechanisms have, as a result, become less attractive, thus undermining collaboration. Likewise, longer-term contracting is too burdensome, which, when read with the short municipal budgeting cycles, undermine long-term planning through which long-term, stable supply relationships can be developed.

Recommendations

A thorough overhaul of the SCM regulatory regime is urgent. The current proposals for such an overhaul, as represented in the draft Public Procurement Bill published for public comment in February 2020, are completely inadequate in addressing any of the SCM concerns at local government level. The following reforms are proposed:

1. Adopt a regulatory regime that is more flexible in the way that it should be applied in different municipal contexts. This must include rules that are suitable to the context of rural SCM.
2. Rethink SCM regulatory approaches that are currently focused on individual municipalities rather than any form of collaborative approaches.
3. Design and experiment with mechanisms that encourage greater collaboration, for example by providing for SCM as a shared service or streamlined PPP processes or other mechanisms to collaborate such as through joint municipal entities.
4. Engage in more dedicated capacity development for SCM units at local government level.
5. Develop and implement minimum competency levels for SCM officials, linked to a drive towards greater professionalization of SCM in South Africa in general and in local government as a sub-specialisation more specifically.
6. Encourage greater collaboration between municipalities in SCM, e.g. SCM as a shared service.
7. Adjust the thresholds for the use of competitive bidding procedures upwards (at least to R500 000 if not more), taking into account real figures of contract values and transaction costs. Risk management approach could rather be adopted to thresholds, including maturity levels of individual entities, e.g. clean audits over time as way of determining maturity as opposed to stark contract values.
8. Allow more flexibility in entering into long-term contracts. Reduce the regulatory burden regarding such contracts, e.g. mandatory input from various levels of government.

8.4.3 Regulatory reporting

Problem statement

Regulatory reporting places a high burden on all municipalities (SALRC 2019), but larger municipalities can simply absorb it without much impact, while smaller municipalities cannot. At the same time, larger municipalities are less in need of oversight by way of such reporting given their higher levels of capacity and more mature systems compared to smaller municipalities where there is more significant need for more stringent oversight. The result is that those who can comply do not really need to, while those who cannot are exactly those that must. The value of this reporting regime across a vast range of different regulatory instruments is doubtful in light of the uneven ability of different municipalities to comply.

Recommendation

1. Improved systems should be considered that would enable data to be captured in a manner accessible to all, which would not only enable continuous oversight, but also provide ongoing management data.
2. There should be greater use of technology, such as cloud-based solutions, in this regard. Municipalities should ideally only be responsible for capturing the base data in a system that is generally accessible to other levels of government and organs of state that play an oversight role (such as the Auditor-General) in order for those entities to analyse the data for their own purposes.

3. The attention to capturing data in appropriate systems should also serve to make the data available to the municipalities themselves for management purposes, such as, for example, informing business intelligence solutions.
4. Careful attention should be given to what type of data is really required and in what format in order to remove redundancies.
5. Attention should be given to differentiated reporting approaches depending on a municipality's own performance. That is, a system of self-regulation based on own performance. Thus, municipalities with a record of good governance over a set period of time could be granted greater leeway in respect of reporting and oversight and effectively be granted greater self-regulation powers. Such a system should be premised on clear, objective criteria that determine a municipality's movement within the system and thus enable municipalities to manage their own affairs in pursuit of a particular self-regulation status. The system should also be dynamic in that any municipality could move in any direction depending on its continued performance in terms of the set metrics. The cost implications of a particular status within this system, i.e. of being more or less self-regulating, should be clearly set out. Generally, having greater self-regulation would be more costly since oversight would be done locally and a municipality should thus be able to afford such self-regulation.

8.4.4 Mandates of municipalities

Problem statement

The static nature of local government mandates as set out in schedules 4 and 5 of the Constitution and the precarious nature of any expansion thereof by way of legislation (i.e. at the will of national or provincial government) unduly limit the ability of local government to keep up with developing needs and opportunities. There also seems to be a significant disconnect between *de jure* mandates and *de facto* mandates, with many municipalities performing many functions that are not wholly within their prescribed mandates. This adversely affects their financial position since funding for these functions remain equally precarious.

Recommendation

1. Consider adjusting the approach to municipal mandates, either by way of a constitutional amendment to bring more agility to the system or by way of overarching legislation.
2. Align actual mandates with legal mandates.
3. Explore ways in which newer functions, such as the provision of data services, could be incorporated at appropriate levels within the mandate scheme.

8.4.5 Intergovernmental debt (Eskom, etc)

Problem statement

The challenging reality of intergovernmental debt, which is currently most vividly illustrated by the relationship between defaulting municipalities and Eskom, requires urgent attention. The issue is not simply one of municipalities owing other organs of state, such as Eskom, money, but also of other organs of state owing municipalities money. At a general level, it seems that there is an inadequate legal framework to deal with intergovernmental debt.

Courts seem reluctant to become involved in disputes involving intergovernmental debt despite the seeming increase in lawfare between different levels of government.

More specifically, the dysfunctional relationship between Eskom and many municipalities present real threats to financial sustainability of all municipalities. The seeming inability of Eskom to secure the settlement of vast amounts of municipal debt through any legal means puts significant further financial pressure on Eskom and increases the risk of electricity supply failure for all municipalities.

Part of this problem relates to the absence of effective consequence management mechanisms, especially in relation to political accountability of councils for decisions they take with financial implications. Disputes such as the current litigation between the Western Cape Government and the Kannaland Municipality suggest that the existing legal mechanisms aimed at enforcing accountability, such as provincial or national intervention, are not generating adequate results in terms of political accountability.

Recommendations

1. Urgent attention must be given to resolve Eskom's municipal debt problem. This will seemingly only be possible by way of intergovernmental collaboration between all three levels of government.
2. A more reliable and efficient system of resolving intergovernmental debt must be established.
3. In creating intergovernmental mechanisms to deal with problems at local government level, care should be taken not to adopt an approach that routinely results in local powers and capacities being absorbed into higher levels of government, but rather to work with the problem at the local level and with the local capacities.

8.4.6 Financial impact of court orders

Problem statement

Problems caused by the lack of regulatory coordination and unfunded mandates are intensified by court orders placing heavy burdens on municipalities outside of their planning and budgeting processes. For example, when a municipality is ordered to provide emergency housing or make land available for housing, the order may have very significant cost implications outside of the municipality's budgetary planning for the relevant period. While individuals are entitled to a range of services and courts are empowered to grant orders for such services to be provided where necessary, the immediate implications for municipalities must also be borne in mind. Without the careful balancing of these considerations that are often in tension, the financial sustainability of municipalities will be seriously undermined.

Recommendations

1. When service delivery orders are granted, all levels of government should be joined so as to ensure that the burden of implementation can be appropriately shared between the different levels of government.
2. In instances where court orders routinely result in disruption to municipal planning, a process of review should be initiated to establish the underlying reasons for such

disruptions, e.g. whether the demands made on municipalities in such cases are inappropriate and thus requiring an adjustment to the entitlements enforced in such cases or whether planning processes and budgeting are inadequate to cater for legitimate claims made on municipalities and thus requiring appropriate adjustments in municipal planning and budgeting. Such a review process could be initiated as part of ongoing local government oversight by bodies such as COGTA or SALGA.

9 Summary of recommendations

Four categories of recommendations have been made. These relate to the process for actioning the recommendations of this report, financial sustainability recommendations, institutional recommendations and regulatory recommendations.

Process recommendations

Process to action the recommendations in this report

1. A technical working group should be assigned the task of assessing and prioritizing recommendations over the short and medium term, and assigning appropriate roles, responsibilities and timelines.

Financial sustainability recommendations

The local government fiscal framework and operational intergovernmental transfers

2. The local government functional framework should be reviewed in the light of 25 years of local government experience and the implementation of far-reaching reforms in electricity and water industries. The revised functional framework should inform a fundamental review of the local government fiscal framework.
3. A process of this magnitude should not just involve SALGA, provincial departments of local government and provincial treasuries but also consultation with individual municipalities, so that the differentiated impacts can be understood, and diverse municipal voices can be heard.

Funding of capital programmes

4. In the face of tightening capital budget constraints, Municipalities should review their systems of capital project prioritisation to ensure that they balance social infrastructure (e.g. informal settlement backlogs) with economic infrastructure that can generate revenues and grow the tax base, and balance new infrastructure with rehabilitation and upgrades.
5. Municipalities should establish a pipeline of shovel ready projects in a pipeline and aim to deliver early in the financial year to order to take advantage of additional unplanned capital funding grant opportunities.
6. Municipalities should build up their internal reserves to help finance their capital expenditure and facilitate borrowing once the pandemic has ended. This has implications for tariff setting in order to generate operating surpluses.
7. Municipalities should explore project finance and other forms of off-balance sheet lending where bankable projects can be identified. Cooperation among municipalities with provincial government support to help identify and package bankable projects may be required for projects which transcend the boundaries of any single municipalities like dams, and renewable natural gas projects from municipal solid waste landfills and wastewater treatment facilities.
8. Innovative lending arrangements should be explored e.g. green bonds and concessionary financing from the World Bank's Climate Investment Fund. The City of Cape Town, for instance, has already issued green bonds, and its current small scale embedded generation programme could be scaled up as a basis for a tradeable renewable certification scheme.

This would establish markets for both renewable energy and tradeable green energy certificates. If other municipalities were to generate their own renewable energy, these sales and revenue from selling green certificates could ensure the sustainability of this form of borrowing.

9. Drakenstein Municipality should request from the FFC an independent assessment of the fairness of its capital grant allocation relative to similar secondary cities, in terms of the FFC Act.
10. The Western Cape Provincial should support the case for streamlining capital grants to reduce their administrative burden, in a differentiated, risk-based approach which recognises municipalities' track record in delivery and good financial management.

Existing revenue sources: balancing affordability and sustainability

Enhancing the ability to optimise existing revenue streams from rates and tradeable services, revolve around the following possibilities:

11. Enhancing the attractiveness for targeted categories of households to relocate (Municipal strategic planning, but district-wide initiatives may require District Development Model-type planning by all role players).
12. Promoting further advances in optimising existing revenue streams through expanding capacity for data management and considering the mechanisms for increasing revenue from property rates proposed by the South African Cities Network 2018 State of City Finances Report.
13. Better utilisation of dormant capacity in service systems or reducing costs through constraint management combined with alternative delivery models (Municipal tactical planning, but district-wide initiatives may require District Development Model-type planning by all role players).
14. Investigating the feasibility of municipal re-demarcation with a view to amalgamate small rural municipalities (Provincial Department of Local Government and national Department of Cooperative Government), or create single tier rural municipalities.
15. Reviewing the Municipal Property Rates Act and related legislation with a view to make allowance for affordable repayment arrangements for businesses affected by the pandemic
16. Promoting further advances in optimising existing revenue streams of tradeable services through expanding capacity for data management and implementing the "Differentiated Service Affordability Model for the Basket of Services Provided by Western Cape Municipalities" (HS Business Solutions, 2019), with provincial support.

New revenue sources

17. Western Cape municipalities should apply to National Treasury via the Municipal Fiscal Powers and Functions Act to pilot revenue instruments which have been proposed (congestion charges etc) to more accurately gauge their feasibility in terms of impacts, potential revenue and administrative costs.
18. Municipalities (especially those with property portfolios) should investigate the feasibility of implementing land value capture mechanisms.
19. A "virtual municipalities" simulation based on actual data could be set up to enable sensitivity analyses to test the viability and impact of new sources of revenue.

Managing costs of employment pressures

20. Where municipalities cannot fund nationally negotiated agreements on costs of employment, they should apply for exemption.
21. The WC provincial government should propose to the national Minister of Cooperative Government and Traditional Affairs that at least once every five years, municipalities should conduct productivity studies resulting in recommendations to inform the review of staff establishments, organizational design and delegations. These should be tabled at Council which should be required to explain how they intend to respond to the recommendations.
22. Good practice productivity benchmarks for municipality as a whole and individual services should be developed e.g. to balance administrative and core delivery spending. This could not only improve internal efficiency but promote civil society oversight.
23. An impact evaluation of the 2018 upper limits on the remuneration for senior management should be done, with a view to improving the effectiveness of these regulations and minimising unintended consequences.
24. Where practical, work-from-home and online meeting practices developed during the pandemic should be maintained, in order to attract and retain staff with scarce skills and reduce travel and subsistence costs (especially for the more distant, rural municipalities). These can also facilitate the sharing of human resources among municipalities, since travel time between municipalities and travel costs could be vastly reduced.

Free Basic Services

25. Municipalities should ensure that their projected increases in indigent households are realistic.
26. A consolidated provincial data set on households receiving FBS should be created to assist in identifying vulnerable households in the event of a national disaster such as a pandemic, and to track the impact of the free basic services policy with a view to impact evaluation.

Institutional recommendations

Affordability of political support structures

27. The cost of political structures and control support costs can be enhanced by issuing guidelines and norms and, as a last resort, by means of prescripts where excessive compared to own revenue, population size and other guideline benchmarks (Provincial Department of Local Government and national Department of Cooperative Government).
28. The feasibility of municipal re-demarcation should be investigated, with a view to amalgamate small rural municipalities (Provincial Department of Local Government and national Department of Cooperative Government), or create single tier rural municipalities.

Revenue certainty of agency funding arrangements

29. All agency agreements should be formalized and duly gazetted with the aim of providing at least a minimum degree of funding certainty for municipalities over the MTREF period and avoid audit queries.

Alternative delivery models: shared services and co-production

To the extent that shared/joint service delivery may be a more sustainable option, it requires the following reforms:

30. Removing or reducing regulatory impediments to shared services (national reform);
31. Strengthening consequences for council, the political executive and senior management of service delivery failure (national reform);
32. Introducing outcomes evaluation: The 2019 National Evaluation Policy Framework (NEPF) has set the objective of ensuring local government successfully institutionalises the practice of evaluation and this should be encouraged. Evaluation must go beyond compliance-oriented audits of performance for accountability purposes to provide for learning and critical self-reflection;
33. Enhancing capability for shared services by way of seconded personnel, capacity building, risk management and good practice initiatives for successfully introducing shared/joint services as a viable option (provincial responsibility);
34. Creating a community of practice and safe space for small-scale "sandbox"-type controlled experiments on shared/joint services, which bring together highly experienced local government practitioners, sector professionals and researchers to jointly develop innovative solutions (Local and provincial government, regional offices of national departments and research institutions).

Public-private partnerships (an operational perspective)

To the extent that PPPs as range of alternative service delivery models may be more sustainable, the following reforms are required:

35. Removing or reducing regulatory impediments (national reform, implementing National Treasury recommendations);
36. Strengthening consequences for council, the political executive and senior management of service delivery failure (national reform);
37. Institutionalising outcomes evaluation;
38. Providing capacity (including grant funding for feasibility studies) for successfully configuring a PPP as a viable option (provincial responsibility)
39. Creating a community of practice and safe space for small-scope "sandbox"-type controlled experiments on PPPs which bring together highly experienced local government practitioners, sector professionals, legal experts and researchers to jointly develop innovative solutions (Local and provincial government, regional offices of national departments and research institutions).

The social and economic development focus of district municipalities

The options can be summarised as follows:

40. Supporting and widening the scope of options for unique district-specific and district-wide innovations that would enhance the revenue-generation capacity of district municipalities and support district-wide local economic development (Provincial Department of Local Government).
41. Better utilisation of dormant capacity in service systems or reducing costs through constraint management combined with alternative delivery models (District-wide initiatives may require DDM-type planning by all role players).

42. Investigating the feasibility of municipal re-demarcation with a view to amalgamate small rural municipalities (Provincial Department of Local Government and National Department of Cooperative Government), or create single tier rural municipalities.
43. Assessing the feasibility of formalising the social development role of district municipalities in rural areas.

Audit costs

44. The provincial government should propose to the National Treasury and Auditor-General a reform whereby municipalities with clean audits for the last three years, are audited every two years instead of annually. This approach is risk based, based on objective criteria, and rewards municipalities which have demonstrated their institutional maturity and the soundness of their control environments.

Regulatory recommendations

General regulatory recommendations

The following reforms are proposed:

45. Rationalise the regulatory environment.
46. Pay closer attention to differentiation between different local government contexts in regulatory regimes.
47. Consider more collaborative operational models and determine the extent to which the regulatory environment facilitate or prohibit such collaborative approaches.
48. Institutionalise meticulous impact assessments of all new regulatory prescripts from an implementation perspective, based on comprehensive, reliable data.
49. Scrutinise all new norms and standards closely to determine whether they in fact represent minimum norms and standards or gold standards.
50. Ensure that findings of impact assessments are adequately internalised across the regulatory framework, including in funding decisions.
51. Move away from a paradigm of national agenda-setting that informs regulatory prescripts that are forced down on local governments to simply implement in favour of a model where local governments drive the regulatory agendas from the bottom up, both in terms of setting the agenda and priorities and in terms of the content of regulatory instruments.
52. Further research on the formulation of regulatory prescripts, including norms and standards, in particular areas is required in order to identify the presence or absence of local government perspectives, and by implication implementation perspectives, in such formation processes. The results of such research will be important to formulate appropriate reforms.

Supply chain management: a regulatory approach

53. Adopt a regulatory regime that is more flexible in the way that it should be applied in different municipal contexts. This must include rules that are suitable to the context of rural SCM.
54. Rethink SCM regulatory approaches that are currently focused on individual municipalities rather than any form of collaborative approaches.

55. Design and experiment with mechanisms that encourage greater collaboration, for example by providing for SCM as a shared service or streamlined PPP processes or other mechanisms to collaborate such as through joint municipal entities.
56. Engage in more dedicated capacity development for SCM units at local government level.
57. Develop and implement minimum competency levels for SCM officials, linked to a drive towards greater professionalization of SCM in South Africa in general and in local government as a sub-specialisation more specifically.
58. Encourage greater collaboration between municipalities in SCM, e.g. SCM as a shared service.
59. Adjust the thresholds for the use of competitive bidding procedures upwards (at least to R500 000 if not more), taking into account real figures of contract values and transaction costs. Risk management approach could rather be adopted to thresholds, including maturity levels of individual entities, e.g. clean audits over time as way of determining maturity as opposed to stark contract values.
60. Allow more flexibility in entering into long-term contracts. Reduce the regulatory burden regarding such contracts, e.g. mandatory input from various levels of government.

Regulatory reporting

61. Improved systems should be considered that would enable data to be captured in a manner accessible to all, which would not only enable continuous oversight, but also provide ongoing management data.
62. There should be greater use of technology, such as cloud-based solutions, in this regard. Municipalities should ideally only be responsible for capturing the base data in a system that is generally accessible to other levels of government and organs of state that play an oversight role (such as the Auditor-General) in order for those entities to analyse the data for their own purposes.
63. The attention to capturing data in appropriate systems should also serve to make the data available to the municipalities themselves for management purposes, such as, for example, informing business intelligence solutions.
64. Careful attention should be given to what type of data is really required and in what format to remove redundancies.
65. Attention should be given to differentiated reporting approaches depending on a municipality's own performance. That is, a system of self-regulation based on own performance. Thus, municipalities with a record of good governance over a set period of time could be granted greater leeway in respect of reporting and oversight and effectively be granted greater self-regulation powers. Such a system should be premised on clear, objective criteria that determine a municipality's movement within the system and thus enable municipalities to manage their own affairs in pursuit of a particular self-regulation status. The system should also be dynamic in that any municipality could move in any direction depending on its continued performance in terms of the set metrics. The cost implications of a particular status within this system, i.e. of being more or less self-regulating, should be clearly set out. Generally, having greater self-regulation would be more costly since oversight would be done locally and a municipality should thus be able to afford such self-regulation.

Mandates of municipalities

66. Consider adjusting the approach to municipal mandates, either by way of a constitutional amendment to bring more agility to the system or by way of overarching legislation.
67. Align actual mandates with legal mandates.
68. Explore ways in which newer functions, such as the provision of data services, could be incorporated at appropriate levels within the mandate scheme.

Intergovernmental debt (Eskom, etc)

69. Urgent attention must be given to resolve Eskom's municipal debt problem. This will seemingly only be possible by way of intergovernmental collaboration between all three levels of government.
70. A more reliable and efficient system of resolving intergovernmental debt must be established.
71. In creating intergovernmental mechanisms to deal with problems at local government level, care should be taken not to adopt an approach that routinely results in local powers and capacities being absorbed into higher levels of government, but rather to work with the problem at the local level and with the local capacities.

Financial impact of court orders

72. When service delivery orders are granted, all levels of government should be joined so as to ensure that the burden of implementation can be appropriately shared between the different levels of government.
73. In instances where court orders routinely result in disruption to municipal planning, a process of review should be initiated to establish the underlying reasons for such disruptions, e.g. whether the demands made on municipalities in such cases are inappropriate and thus requiring an adjustment to the entitlements enforced in such cases or whether planning processes and budgeting are inadequate to cater for legitimate claims made on municipalities and thus requiring appropriate adjustments in municipal planning and budgeting. Such a review process could be initiated as part of ongoing local government oversight by bodies such as COGTA or SALGA.

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Appendix 1: Minimum service standards

The minimum service standards per service are set down beloe

Refuse Removal

- The most appropriate level of waste removal service provided based on site specific circumstances.
- **Quality (The same for all baskets of services):** A basic level of service, be it in an urban or rural set-up, is attained when a municipality provides or facilitates waste removal through:
  - a) On-site appropriate and regularly supervised disposal in areas designated by the municipality (applicable mainly to remote rural areas with low density settlements and farms supervised by a waste management officer);
  - b) Community transfer to central collection point (medium density settlements);
  - c) Organised transfer to central collection points and/or kerbside collection (high density settlements); and
  - d) Mixture of 'b' and 'c' above for the medium to high density settlements

Communal (informal settlements)

- **Quantity**: The collection frequency is dependent on the composition and the volumes of waste generated. The most appropriate collection frequency in medium and high-density settlements is set out as:
- At least once a week for purely biodegradable domestic waste, but on-site composting should be promoted.
- At least once a month for recyclable materials in rural areas.
- **Charge:** Free

Indigent Households

- **Quantity**: At least once a week for purely biodegradable domestic waste, but on-site composting should be promoted.
- At least once a month for recyclable materials in rural areas.
- **Charge:** Free

Standard

- **Quantity**: At least once a week for purely biodegradable domestic waste, but on-site composting should be promoted.
- At least once a month for recyclable materials in rural areas.
- **Charge:** Charged as part of municipal account

Electricity

- The responsibility to distribute electricity to consumers is shared between municipalities and Eskom

Informal Settlements

- **Quality:** Communal connection points in certain municipal areas
- **Quantity**: Mostly not metered, especially illegal connections
- **Charge:** Free

Indigent Households

- **Quality:** Individual connection (prepaid meter)
- **Quantity**: According to demand
- **Charge:** 50 kWh per month free; charged for additional consumption
- Unit charge increases as consumption increases

Standard

- **Quality:** Individual connection (in some cases prepaid)
- **Quantity**: According to demand
- **Charge:** Charged from first unit (kWh) of consumption.
- Unit charge increases in steps as consumption increases

Appendix 2: Profiles of sampled municipalities

The data below are drawn from https://municipalities.co.za which aggregates data from Statistics South Africa and other official data sources.

As at 2016 unless otherwise stated		Municipalities							
		Stellenbosch	Drakenstein	Swartland	Hessequa	Bergriver	Swellendam	Kannaland	Laingsburg
Demographics	Population	173 197	280 195	133 765	54 237	67 474	40 211	24 168	8 895
	Dependancy Ratio - means or indigence	38.7	45	44.7	54.3	48.7	52	54	42.3
	Population Growth per annum	2.4%	2.5%	3.7%	0.7%	2.0%	2.57%	-0.56%	1.60%
Labour Market	Unemployment rate	n/a	17.6% (2011)	12.7% (2011)	14.1% (2011)	6.8% (2011)	11.4% (2011)	17.3% (2011)	17,9 (2011)
	Youth unemployment rate	n/a	24.6% (2011)	17.9% (2011)	18.9% (2011)	9.6% (2011)	15.0% (2011)	22.7% (2011)	22% (2011)
Household Dynamics	Households	52 274	71 686	39 139	17 371	19072	11 678	6333	2 862
	Average household size	3.3	3.9	3.4	3.1	3.5	3.4	3.8	3.1
	Formal Dwellings	65%	90%	95%	96%	92%	96%	97%	98%
	Housing owned	50%	55%	65%	73%	61%	66%	71%	61%
Household Services	Flush toilet connected to sewerge	97%	97%	86%	91%	83%	94%	65%	83%
	Weekly refuse removal	71%	91%	84%	74%	84%	87%	79%	80%
	Piped water inside dwelling	67%	85%	84%	85%	85%	86%	87%	57%
	Electricity for lighting	93%	96%	99%	98%	98%	97%	92%	89%

As at 2016 unless otherwise stated		District Municipalities			Metro
		Cape Winelands	West Coast	Central Karoo	City of Cape Town
Demographic Information	Population	866 001	436 403	74 247	4 005 016
	Dependancy Ratio - means or indigence	45.1	46.5	48.3	47.6
	Population Growth per annum	2.2%	2.5%	1.0%	1.6%
Labour Market	Unemployment rate	Nothing for 2016 or 2011	14.6% (2011)	23.1% (2011)	23.9% (2011)
	Youth unemployement rate	Nothing for 2016 or 2012	19.9% (2011)	30.9% (2011)	31.9% (2011)
Household Dynamics	Households	235 906	129 862	21 980	1 264 949
	Average household size	3.7	3.4	3.4	3.2
	Formal Dwellings	81%	86%	98%	82%
	Housing owned	49%	63%	68%	69%
Household Services	Flush toilet connected to sewerge	94%	85%	94%	91%
	Weekly refuse removal	82%	83%	91%	88%
	Piped water inside dwelling	77%	80%	74%	77%
	Electricity for lighting	94%	94%	95%	97%

Services delivery indicators		Local municipalities							
		Stellenbosch	Drakenstein	Swartland	Hessequa	Bergriver	Swellendam	Kannaland	Laingsburg
Water	Blue Drop Score	80.12 (2013/14)	72.14 (2013/14)	74.7 (2013/14)	55.18 (2013/14)	63,8 (2013/14)	57.25 - (2013/14)	31.7 (2013/14)	n/a
	Is the municipality responsible to provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Does the municipality have infrastructure to provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Does the municipality actually provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Is the service outsourced/commercialised?	No	No	No	No	No	No	No	No
	Number of households and non-domestic customers to which provided	52 225	45 828	22 104	15 561	9 028	6 451	5 089	1 453
	Number of domestic households/delivery points	51 322	45 166	20 716	15 561	9 028	6 451	4 746	1 342
	Inside the yard	41 623	41 222	20 716	15 207	9 028	6 245	4 646	1 342
	Less than 200m from yard	9699	3944	0	444	0	206	100	0
	More than 200m from yard	0	0	0	0	0	0	0	0
	Domestic households with access to free basic service	6 453	19 030	8 738	5 179	1 746	6 245	2 192	603
Electricity	Is the municipality responsible to provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Does the municipality have infrastructure to provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Does the municipality actually provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Is the service outsourced/commercialised?	No	Yes	No	No	Yes	Yes	No	Yes
	Number of households and non-domestic customers to which provided	52 374	52 653	18 160	15 609	9 572	6 692	4 546	1 296
	Domestic households with access to free basic service	11 670	18 860	7 752	5 179	713	6 692	2 192	606
Sewerage and Sanitation	Green Drop Score	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
	Is the municipality responsible to provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Does the municipality have infrastructure to provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Does the municipality actually provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Is the service outsourced/commercialised?	No	No	No	No	No	No	No	No
	Number of households and non-domestic customers to which provided	41 298	50 004	20 654	15 571	9 534	7 374	4 777	1 402
No of Households using::	Flush toilet - public sewerage	38 027	40 513	18 205	13 351	7 371	5 823	1 542	1 241
	Flush toilet - septic tank	1 079	8 309	824	1 713	2 148	436	189	68
	Ventilated pit latrine	0	142	0	487	0	294	0	0
	Bucket system	0	378	0	0	0	0	0	0
	Other	1267	0	0	0	0	0	2703	0
	Domestic households with access to free basic service	6 453	19 030	8 261	5179	1534	1975	2192	606
Solid Waste Services	Is the municipality responsible to provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Does the municipality have infrastructure to provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Does the municipality actually provide?	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
	Is the service outsourced/commercialised?	No	No	No	No	No	No	No	No
	Number of households and non-domestic customers to which provided	49 072	33 628	20 176	15873	9499	6342	4494	1360
	Domestic households with access to free basic service	6 453	19 030	8 556	5179	1753	1975	2192	613

Services Delivery Statistics		District municipalities		
		Cape Winelands	West Coast	Central Karoo
Water	Blue Drop Score	n/a	n/a	n/a
	Is the municipality responsible to provide?	No	Yes	No
	Does the municipality have infrastructure to provide?	No	Yes	No
	Does the municipality actually provide?	No	Yes	No
	Is the service outsourced/commercialised?	No	No	No
	Number of households and non-domestic customers to which provided	0	1006	0
	Number of domestic households/delivery points	0	1006	0
	Inside the yard	0	1006	0
	Less than 200m from yard	0	0	0
	More than 200m from yard	0	0	0
	Domestic households with access to free basic service	0	17	0
Electricity	Is the municipality responsible to provide?	No	Yes	No
	Does the municipality have infrastructure to provide?	No	Yes	No
	Does the municipality actually provide?	No	Yes	No
	Is the service outsourced/commercialised?	No	No	No
	Number of households and non-domestic customers to which provided	0	99	0
	Domestic households with access to free basic service	0	17	0
Sewerage and Sanitation	Green Drop Score	n/a	n/a	n/a
	Is the municipality responsible to provide?	No	Yes	No
	Does the municipality have infrastructure to provide?	No	Yes	No
	Does the municipality actually provide?	No	Yes	No
	Is the service outsourced/commercialised?	No	No	No
	Number of households and non-domestic customers to which provided	0	99	0
No of Households using::	Flush toilet - public sewerage	0	99	0
	Flush toilet - septic tank	0	0	0
	Ventilated pit latrine	0	0	0
	Bucket system	0	0	0
	Other	0	0	0
	Domestic households with access to free basic service	0	17	0
Solid Waste Services	Is the municipality responsible to provide?	No	Yes	No
	Does the municipality have infrastructure to provide?	No	Yes	No
	Does the municipality actually provide?	No	Yes	No
	Is the service outsourced/commercialised?	No	No	No
	Number of households and non-domestic customers to which provided	0	99	0
	Domestic households with access to free basic service	0	16	0

Employment in 2017/18	Sampled local municipalities							
	Stellenbosch	Drakenstein	Swartland	Hessequa	Bergriver	Swellendam	Kannaland	Laingsburg
Total employee positions	1210	2119	560	487	438	297	388	82
Vacant employee positions	91	293	16	14	55	26	211	13
% vacancies	8%	14%	3%	3%	12%	9%	54%	16%
Total managerial positions by organogram	69	59	23	23	10	16	12	6
Vacant managerial positions	6	6	2	0	1	0	8	1
% managerial vacancies	9%	10%	9%	0%	10%	0%	67%	17%
Community and Social Service positions	128	311	107	66	41	70	164	5
Vacant Community and Social Service positions	5	85	49	5	10	8	52	0
% vacancies: Community and Social Services	4%	27%	46%	8%	24%	11%	32%	0%
Finance and Administration positions	241	521	98	91	107	74	84	23
Vacant Finance and Administration positions	33	98	3	2	9	5	52	2
% vacancies: Finance and Social Service positions	14%	19%	3%	2%	8%	7%	62%	9%
Electricity positions	77	151	38	37	21	16	10	0
Vacant Electricity positions	4	12	1	2	0	0	0	0
% vacancies: Electricity positions	5%	8%		5%	0%	0%	0%	0%
Enviromental Protection positions	40	47	0	7	0	4	0	7
Vacant Enviromental Protection positions	0	1	0	0	0	1	0	0
% vacancies: Environmental Protection positions	0%	2%	0%	0%	0%	25%	0%	0%
Public Safety positions	199	215	37	23	24	13	17	5
Vacant Public Safety positions	2	35	2	0	3	2	9	0
% vacancies: Public Safety positions	1%	16%	5%	0%	13%	15%	53%	0%
Road Transport positions	105	165	98	76	94	31	26	13
Vacant Road Transport positions	7	0	1	2	26	3	21	2
% vacancies: Road Transport positions	7%	0%	1%	3%	28%	10%	81%	15%
Sport and Recreation positions	63	250	15	57	54	1	13	0
Vacant Sport and Recreation positions	15	32	0	0	0	0	12	0
% vacancies: Sport and Recreation positions	24%	13%	0%	0%	0%	0%	92%	0%
Waste Management positions	63	182	66	39	45	15	24	4
Vacant Waste Management positions	6	24	1	1	6	1	24	0
% vacancies: Waste Management positions	10%	13%	2%	3%	13%	7%	100%	0%
Vacant Waste Water Management positions	88	121	30	14	14	20	18	5
Vacant Waste Water Management positions	8	0	1	0	0	3	16	1
% vacancies: Waste Water Management positions	9%	0%	3%	0%	0%	15%	89%	20%
Water positions	130	91	41	21	23	27	16	7
Vacant Water positions	4	0	0	0	0	2	14	3
% vacanices: Water positions	3%	0%	0%	0%	0%	7%	88%	43%
Other positions	0	0	0	28	0	5	0	7
Vacant Other positions	0	0	0	0	0	1	0	4
Vacancies: Other positions	0%	0%	0%	0%	0%	20%	0%	57%

Employment in 2017/18	District municipalities			Metropolitan
	Cape Winelands	West Coast	Central Karoo	City of Cape Town
Total employee positions	467	664	157	30 239
Vacant employee positions	49	52	0	2 648
% vacancies	10%	8%	0%	9%
Total managerial positions by organogram	44	26	7	10
Vacant managerial positions	1	0	0	0
% managerial vacancies	2%	0%	0%	0%
Community and Social Service positions	6	5	1	2 121
Vacant Community and Social Service positions	2	0	0	135
% vacancies: Community and Social Services	33%	0%	0%	6%
Finance and Administration positions	114	72	33	6 665
Vacant Finance and Administration positions	8	2	0	717
% vacancies: Finance and Administration positions	7%	3%	0%	11%
Electricity positions	0	9	0	2 752
Vacant Electricity positions	0	0	0	219
% vacancies: Electricity positions	0%	0%	0%	8%
Enviromental Protection positions	5	42	0	565
Vacant Enviromental Protection positions	5	1	0	42
% vacancies: Environmental Protection positions	100%	2.30%	0%	7%
Health positions	43	26	5	1 818
Vacant Health positions	3	0	0	109
Percentage calculation of vacant health positions	6.9	0%	0%	6%
Public Safety positions	63	74	0	4 376
Vacant Public Safety positions	2	0	0	248
% vacancies: Public Safety positions	3.1	0%	0%	6%
Road Transport positions	178	277	108	1 946
Vacant Road Transport positions	28	26	0	143
% vacancies: Road Transport positions	16%	9%	0%	7%
Sport and Recreation positions	0	15	0	1 742
Vacant Sport and Recreation positions	0	1	0	80
% vacancies: Sport and Recreation positions	0%	7%	0%	5%
Waste Management positions	0	0	0	3450
Vacant Waste Management positions	0	0	0	42
% vacancies: waste management positions	0%	0%	0%	1%
Vacant Waste Water Management positions	0	0	0	386
Vacant Waste Water Management positions	0	0	0	42
% vacancies: Waste Water Management positions	0%	0%	0%	11%
Water positions	0	113	0	4 047
Vacant Water positions	0	22	0	603
% vacancies: Water positions	0%	19%	0%	15%
Other positions	9	0	0	41
Vacant Other positions	0	0	0	6
Vacancies: Other positions	0%	0%	0%	15%

Appendix 3: Year-on-Year change in operating revenues in 2019/20Q4, 2020/21Q1 and 2020/21Q2

CATEGORY	CAPACITY	Municipality	R millions / Revenue source	Pre-pandemic actual 18/19Q4	19/20Q1	19/20Q2	19/20Q3	Pandemic actual 19/20Q4	20/21Q1	20/21Q2	% Change YOY 19/20Q4	20/21Q1	20/21Q2
B1	High	Stellenbosch	Property rates	67.1	144.8	72.9	73.9	74.1	152.3	80.4	10%	5%	10%
			Electricity charges	159.0	173.9	143.1	170.4	145.1	171.8	116.5	(9%)	(1%)	(19%)
			Water charges	38.3	33.1	39.3	49.7	47.0	31.7	27.8	23%	(4%)	(29%)
			Sanitation charges	19.6	26.1	18.4	21.9	19.9	26.3	20.5	1%	1%	11%
			Refuse charges	12.4	23.4	12.3	13.6	13.7	25.5	15.8	11%	9%	28%
			Transfer and subsidies	0.4	59.3	48.8	9.0	46.1	68.8	73.6	10 287%	16%	51%
			Interest earned	13.7	11.0	11.6	15.2	10.9	8.8	6.9	(21%)	(20%)	(41%)
			Fines, penalties, licences & permits	8.9	2.6	8.6	5.8	3.5	1.0	40.8	(60%)	(61%)	371%
			Rental of facilities and equipment	2.2	2.1	2.1	3.8	2.1	2.4	2.2	(7%)	16%	6%
			Agency services	1.2	0.5	0.8	0.5	0.7	0.3	1.2	(46%)	(47%)	51%
			Other revenues	5.8	4.5	5.6	4.6	2.3	4.4	3.2	(61%)	(2%)	(42%)
			Total operating revenue	**328.9**	**481.3**	**363.6**	**368.4**	**365.4**	**493.3**	**388.9**	**11%**	**3%**	**7%**
B1	High	Drakenstein	Property rates	0.7	106.2	74.8	75.3	58.2	112.4	76.7	8 571%	6%	3%
			Electricity charges	261.6	305.6	282.8	296.3	279.0	301.2	279.8	7%	(1%)	(1%)
			Water charges	32.9	33.9	39.0	43.6	42.6	41.5	37.1	29%	23%	(5%)
			Sanitation charges	(5.4)	31.1	27.7	30.3	27.2	33.3	29.9	(600%)	7%	8%
			Refuse charges	(8.6)	32.2	31.1	33.5	33.1	32.6	32.5	(483%)	1%	5%
			Transfer and subsidies	13.3	62.8	22.5	70.4	41.6	45.4	26.7	212%	(28%)	19%
			Interest earned	6.5	3.4	3.6	4.5	1.9	2.9	3.1	(70%)	(17%)	(12%)
			Fines, penalties, licences & permits	1.1	1.0	22.1	1.5	0.3	0.8	55.6	(75%)	(18%)	152%
			Rental of facilities and equipment	(0.7)	0.9	(1.5)	(2.1)	15.5	3.5	0.7	(2 254%)	306%	(145%)
			Agency services	-	-	-	-	-	3.9	4.4	-	-	-
			Other revenues	13.8	7.5	9.9	9.4	4.5	4.3	5.0	(67%)	(43%)	(50%)
			Total operating revenue	**315.0**	**584.6**	**512.0**	**562.6**	**504.0**	**581.9**	**551.7**	**60%**	**(.5%)**	**8%**
B3	Medium	Swartland	Property rates	25.9	39.9	24.8	30.0	29.5	36.3	32.4	14%	(9%)	31%
			Electricity charges	64.6	78.3	72.9	75.1	70.6	85.3	77.8	9%	9%	7%
			Water charges	14.0	14.1	16.4	20.5	14.9	18.4	17.3	6%	30%	5%
			Sanitation charges	9.7	10.4	11.4	11.2	10.9	11.0	11.3	11%	5%	(1%)
			Refuse charges	6.3	6.9	6.9	6.9	6.7	6.9	6.9	7%	%	1%
			Transfer and subsidies	-	38.1	30.5	22.9	-	46.0	44.9	-	21%	47%
			Interest earned	34.7	3.3	3.1	4.9	36.4	1.3	1.6	5%	(61%)	(48%)
			Fines, penalties, licences & permits	1.2	1.1	1.2	1.1	0.3	1.2	1.2	(72%)	5%	(6%)
			Rental of facilities and equipment	0.4	0.4	0.3	0.4	0.3	0.3	0.3	(22%)	(24%)	(3%)
			Agency services	1.1	1.2	1.2	1.1	0.5	1.8	1.5	(60%)	54%	25%
			Other revenues	2.8	5.4	5.2	3.5	2.5	2.4	4.3	(11%)	(55%)	(16%)
			Total operating revenue	**160.9**	**199.2**	**173.9**	**177.6**	**172.6**	**210.9**	**199.4**	**7%**	**6%**	**15%**
B3	Medium	Hessequa	Property rates	0.1	95.5	0.4	(0.3)	(0.2)	102.3	(0.4)	(292%)	7%	(209%)
			Electricity charges	33.5	37.8	37.0	39.7	36.4	45.1	35.0	8%	19%	(5%)
			Water charges	8.2	10.6	9.9	11.2	9.5	11.8	9.0	15%	12%	(9%)
			Sanitation charges	4.8	8.0	5.3	5.4	5.3	8.3	5.6	10%	3%	7%
			Refuse charges	4.8	5.6	5.5	5.6	5.6	8.0	5.9	16%	44%	6%
			Transfer and subsidies	4.0	20.2	17.1	14.4	2.6	21.7	26.8	(36%)	7%	57%
			Interest earned	5.8	0.4	5.6	6.3	6.1	5.0	0.3	6%	1 007%	(94%)
			Fines, penalties, licences & permits	18.8	3.0	16.2	16.3	4.2	2.0	22.3	(77%)	(35%)	38%
			Rental of facilities and equipment	1.0	0.7	0.8	0.6	0.7	0.6	1.0	(30%)	(19%)	13%
			Agency services	0.6	0.5	0.6	0.7	0.4	0.6	0.8	(42%)	17%	28%
			Other revenues	2.3	5.5	6.5	3.3	0.3	3.1	7.0	(85%)	(44%)	8%
			Total operating revenue	**84.0**	**188.0**	**104.8**	**103.0**	**70.8**	**208.4**	**113.3**	**(16%)**	**11%**	**8%**

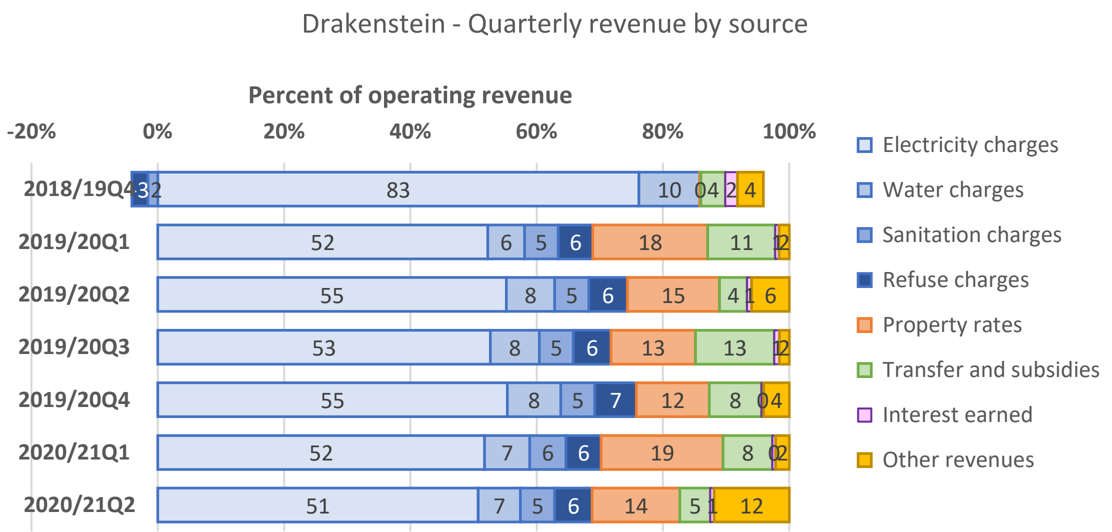
CATEGORY	CAPACITY	Municipality	R miilions Revenue source	Pre-pandemic actual 18/19Q4	19/20Q1	19/20Q2	19/20Q3	Pandemic actual 19/20Q4	20/21Q1	20/21Q2	% Change YOY 19/20Q4	20/21Q1	20/21Q2
B3	Medium	Bergrivier	Property rates	14.9	47.1	(5.9)	16.1	16.7	26.7	17.3	12%	(43%)	(395%)
			Electricity charges	32.5	33.8	33.0	19.0	38.5	31.5	31.2	19%	(7%)	(5%)
			Water charges	6.6	11.5	1.6	9.3	7.5	6.7	7.1	13%	(41%)	355%
			Sanitation charges	4.0	6.8	(0.1)	3.5	3.3	3.7	3.6	(16%)	(46%)	(3 599%)
			Refuse charges	6.4	8.7	2.4	5.6	5.6	6.0	5.9	(12%)	(31%)	151%
			Transfer and subsidies	(4.0)	18.8	17.8	14.7	3.7	23.5	21.1	(193%)	25%	18%
			Interest earned	4.2	5.5	2.7	3.8	1.8	2.6	2.4	(57%)	(52%)	(10%)
			Fines, penalties, licences & permits	0.4	0.7	1.1	0.7	0.6	0.4	1.0	46%	(43%)	(8%)
			Rental of facilities and equipment	(0.2)	0.4	0.7	(0.4)	0.2	1.8	(0.3)	(184%)	342%	(137%)
			Agency services	0.7	0.6	1.3	1.0	0.6	1.0	1.3	(6%)	50%	(1%)
			Other revenues	1.8	1.9	7.5	2.1	0.4	1.1	2.3	(76%)	(43%)	(70%)
			Total operating revenue	**67.3**	**135.7**	**62.0**	**75.4**	**79.1**	**104.9**	**92.8**	**17%**	**(23%)**	**50%**
B3	Low	Swellendam	Property rates	9.0	11.8	9.3	9.4	9.1	12.8	9.8	1%	8%	5%
			Electricity charges	18.4	21.2	21.1	19.8	19.8	21.9	22.7	8%	3%	8%
			Water charges	3.5	4.1	4.7	4.9	3.5	4.3	4.4	1%	7%	(6%)
			Sanitation charges	3.0	3.8	3.9	5.4	3.9	6.3	4.1	29%	65%	6%
			Refuse charges	2.6	2.4	2.4	2.4	1.9	2.8	2.7	(27%)	17%	15%
			Transfer and subsidies	3.5	22.6	18.7	10.5	5.0	17.6	20.7	43%	(22%)	10%
			Interest earned	1.6	1.2	2.0	2.1	0.5	1.1	1.1	(69%)	(10%)	(44%)
			Fines, penalties, licences & permits	2.5	2.8	2.5	9.3	0.3	5.9	9.8	(90%)	114%	287%
			Rental of facilities and equipment	0.1	0.2	0.2	0.2	0.0	0.3	0.1	(81%)	22%	(19%)
			Agency services	0.4	0.5	0.5	0.6	0.0	0.7	0.7	(100%)	42%	26%
			Other revenues	1.1	1.4	1.1	0.4	(0.0)	1.1	0.9	(101%)	(24%)	(17%)
			Total operating revenue	**45.6**	**72.0**	**66.5**	**64.9**	**44.0**	**74.8**	**77.1**	**(4%)**	**4%**	**16%**
B3	Medium	Kannaland	Property rates	5.0	6.4	3.0	2.2	3.1	8.3	3.6	(39%)	28%	22%
			Electricity charges	12.9	10.6	12.6	12.4	11.3	14.8	12.9	(12%)	40%	2%
			Water charges	3.2	2.4	4.2	5.9	4.4	3.7	4.5	40%	54%	9%
			Sanitation charges	1.5	0.7	1.8	1.2	1.7	1.9	1.9	16%	181%	6%
			Refuse charges	1.4	0.6	1.7	1.1	1.7	1.8	1.8	18%	202%	6%
			Transfer and subsidies	11.1	13.4	9.5	7.7	0.0	12.0	15.5	(100%)	(11%)	63%
			Interest earned	0.3	0.3	0.2	0.2	0.2	0.2	0.3	(43%)	(18%)	19%
			Fines, penalties, licences & permits	1.5	0.5	1.6	1.2	0.0	0.5	0.5	(98%)	(13%)	(69%)
			Rental of facilities and equipment	0.1	0.0	0.1	0.1	0.1	0.1	0.1	(7%)	161%	(9%)
			Agency services	0.3	0.2	0.2	0.3	-	0.3	0.3	(100%)	45%	25%
			Other revenues	0.2	0.2	0.4	0.3	0.3	0.2	0.2	15%	(15%)	(56%)
			Total operating revenue	**37.5**	**35.5**	**35.3**	**32.6**	**22.8**	**43.7**	**41.5**	**(39%)**	**23%**	**18%**
B3	Medium	Laingsburg	Property rates	0.1	4.1	0.0	0.0	0.0	4.4	0.0	(64%)	7%	28%
			Electricity charges	3.2	4.0	2.6	3.5	3.3	4.1	3.8	6%	1%	49%
			Water charges	0.5	0.8	0.6	0.8	0.8	0.9	1.0	78%	12%	63%
			Sanitation charges	0.5	0.7	0.5	0.7	0.7	0.8	0.8	58%	5%	59%
			Refuse charges	0.4	0.6	0.4	0.6	0.6	0.7	0.7	66%	11%	65%
			Transfer and subsidies	0.0	6.9	5.0	5.0	1.0	8.4	10.6	6 163%	22%	113%
			Interest earned	0.2	0.3	0.6	0.3	0.2	0.2	0.1	1%	(39%)	(91%)
			Fines, penalties, licences & permits	9.0	0.4	26.5	5.3	10.6	5.5	10.9	18%	1 345%	(59%)
			Rental of facilities and equipment	0.3	0.4	0.2	0.4	0.3	0.4	0.5	9%	2%	95%
			Agency services	0.04	0.05	0.02	0.04	0.01	0.1	0.05	(77%)	43%	162%
			Other revenues	0.05	0.04	0.02	0.04	0.03	0.1	(0.1)	(44%)	28%	(447%)
			Total operating revenue	**14.1**	**18.3**	**36.4**	**16.7**	**17.7**	**25.4**	**28.3**	**25%**	**39%**	**(22%)**

Source: National Treasury website s71 reports. Note negative figures are as reported by the respective municipalities and maybe MSCOA transition anomalies.

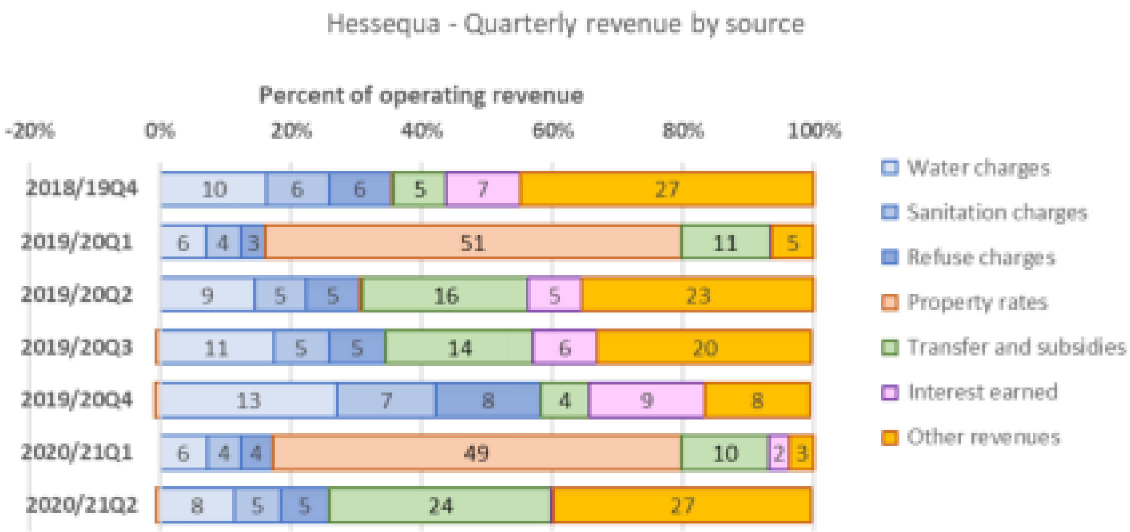
CATEGORY	CAPACITY	Municipality	R millions	Pre-pandemic actual				Pandemic actual			% Change YOY		
			Revenue Source	18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	2019/20Q4	2020/21Q1	2020/21Q2
C1	Medium	Cape Winelands	Interest earned	41.4	2.8	4.4	9.9	22.5	1.8	4.5	(46%)	(37%)	3%
			Agency services	30.0	19.9	18.1	49.4	24.6	5.4	30.7	(18%)	(73%)	70%
			Transfer and subsidies	1.3	3.6	98.0	139.6	0.5	108.8	75.9	(60%)	2 887%	(23%)
			Rental of facilities and equipment	0.1	0.03	0.1	0.1	0.1	0.1	0.1	(17%)	111%	(37%)
			Licence, permits & other revenue	2.5	100.0	(16.0)	(75.1)	2.8	2.8	1.9	11%	(97%)	(112%)
			Total operating revenue	**75.4**	**126.3**	**104.5**	**124.0**	**50.6**	**118.8**	**113.2**	**(33%)**	**(6%)**	**8%**
C1	Medium	West Coast	Interest earned	19.4	2.1	2.1	2.9	16.5	1.1	1.2	(15%)	(46%)	(45%)
			Agency services	24.5	22.0	48.1	37.2	17.0	27.2	37.4	(31%)	24%	(22%)
			Water charges	30.1	23.5	30.4	34.6	29.6	26.6	27.0	(2%)	13%	(11%)
			Electricity	0.2	0.3	0.2	0.2	0.3	0.3	0.3	29%	12%	17%
			Transfer and subsidies	2.4	8.3	12.2	2.6	0.4	9.0	15.8	(82%)	8%	30%
			Rental of facilities and equipment	0.5	0.7	0.7	0.7	0.9	0.7	0.9	61%	11%	23%
			Licence, permits & other revenue	4.4	37.0	25.5	30.5	7.1	40.7	24.0	61%	10%	(6%)
			Total operating revenue	**81.6**	**93.8**	**119.3**	**108.9**	**71.8**	**105.7**	**106.6**	**(12%)**	**13%**	**(11%)**
C1	Medium	Central Karoo	Interest earned	0.3	0.2	0.2	0.3	0.2	-		(25%)	(100%)	(100%)
			Agency services	13.1	3.8	8.4	13.0	15.8	0.4	9.2	20%	(90%)	10%
			Transfer and subsidies	7.4	0.03	11.7	8.9	2.6	30.5	15.5	(65%)	106 978%	33%
			Rental of facilities and equipment	-	0.001	0.01	0.01	(0.01)	-		-	(100%)	(100%)
			Licence, permits & other revenue	(0.2)	0.01	0.02	0.02	0.03	(0.8)	(0.6)	(116%)	(8 778%)	(2 728%)
			Total operating revenue	**20.6**	**4.1**	**20.3**	**22.2**	**18.6**	**30.1**	**24.1**	**(10%)**	**641%**	**19%**

Appendix 4: Composition of quarterly operating revenues during the pandemic

The graphs below show the percentage of each revenue source of total operating revenue for each municipality. User charges for trading services (electricity, water, sanitation and refuse) are shown in shades of blue, property rates in orange and transfers and subsidies in green. Interest earned and other own revenues are shown in yellow. Due to the transition to Municipal Standard Chart of Accounts (MSCOA), there are anomalies in the Section &1 report data drawn from the National Treasury website (such as negative balances due to journal corrections processed). These have been left as reported by the municipalities.



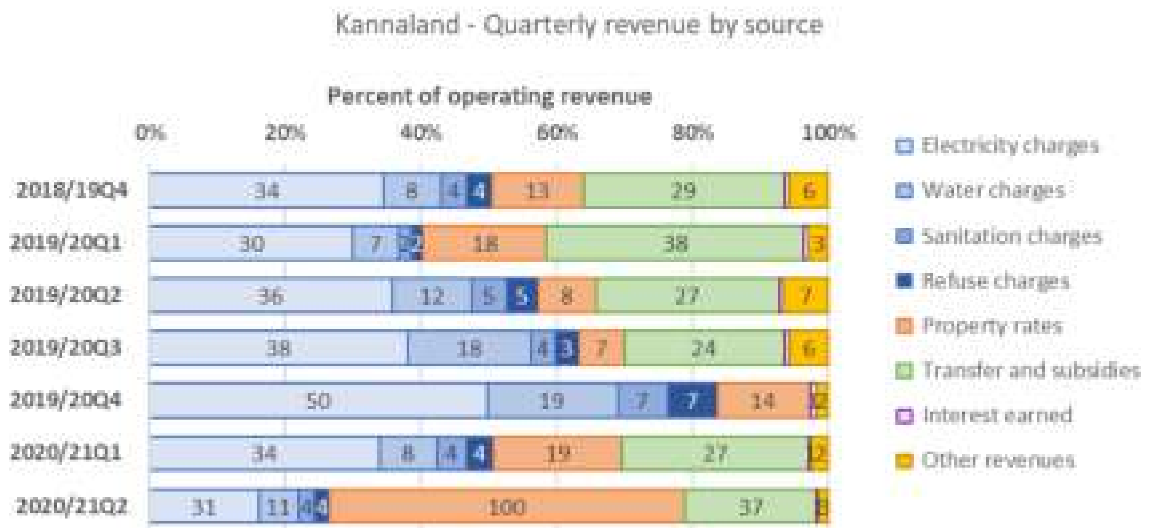

Swartland - Quarterly revenue by source
Percent of operating revenue
0%
20%
40%
60%
80%
100%
2018/19Q4
2019/20Q1
2019/20Q2
2019/20Q3
2019/20Q4
2020/21Q1
2020/21Q2
Electricity charges
Water charges
Sanitation charges
Refuse charges
Property rates
Transfer and subsidies
Interest earned
Other revenues


Hessequa - Quarterly revenue by source
Percent of operating revenue
-20%
0%
20%
40%
60%
80%
100%
2018/19Q4
2019/20Q1
2019/20Q2
2019/20Q3
2019/20Q4
2020/21Q1
2020/21Q2
Water charges
Sanitation charges
Refuse charges
Property rates
Transfer and subsidies
Interest earned
Other revenues

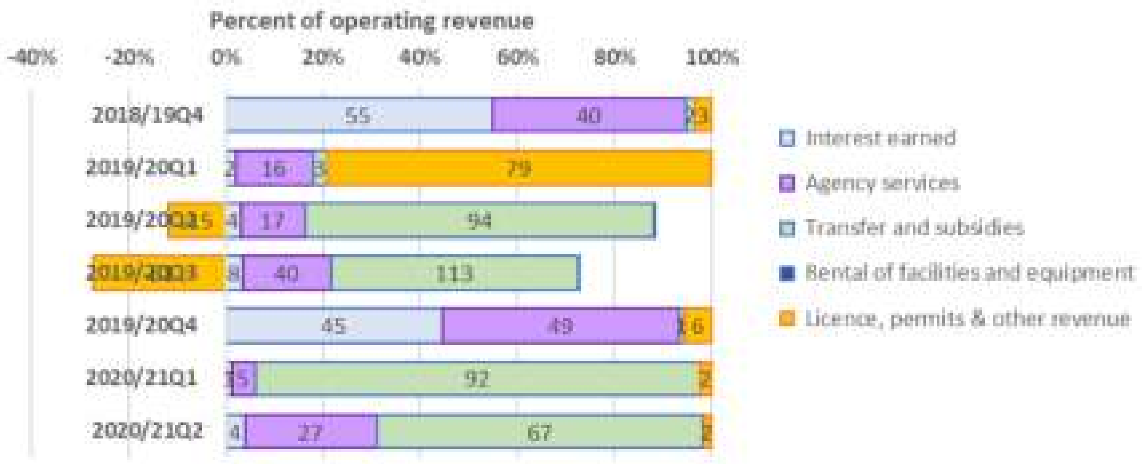
Bergrivier - Quarterly revenue by source

Swellendam - Quarterly revenue by source

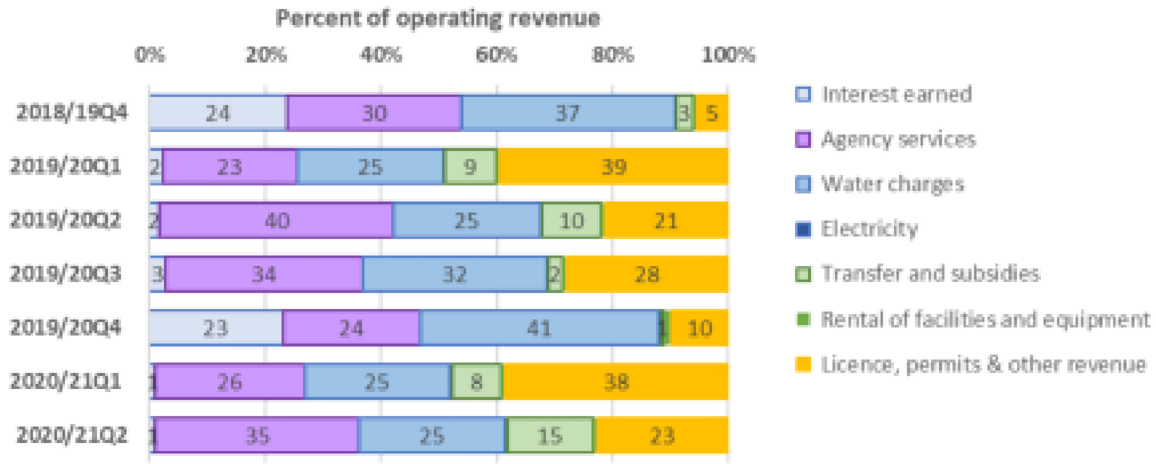

Laingsburg - Quarterly revenue by source
Percent of operating revenue
0%
20%
40%
60%
80%
100%
2018/19Q4
2019/20Q1
2019/20Q2
2019/20Q3
2019/20Q4
2020/21Q1
2020/21Q2
Electricity charges
Water charges
Sanitation charges
Refuse charges
Property rates
Transfer and subsidies
Interest earned
Other revenues


Kannaland - Quarterly revenue by source
Percent of operating revenue
0%
20%
40%
60%
80%
100%
2018/19Q4
2019/20Q1
2019/20Q2
2019/20Q3
2019/20Q4
2020/21Q1
2020/21Q2
Electricity charges
Water charges
Sanitation charges
Refuse charges
Property rates
Transfer and subsidies
Interest earned
Other revenues

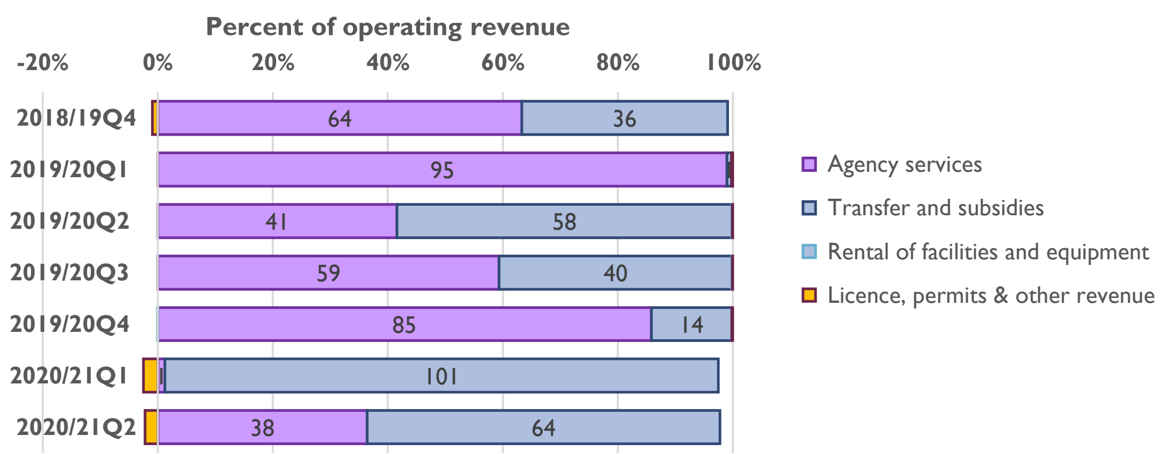
Cape Winelands DM - Quarterly revenue by source



West Coast DM - Quarterly revenue by source



Central Karoo - Quarterly revenue by source



City of Cape Town - Quarterly revenue by source

Appendix 5: Year-on-Year Changes in operating expenditure in 2019/20Q1, 2020/21Q1 and 2020/21Q2

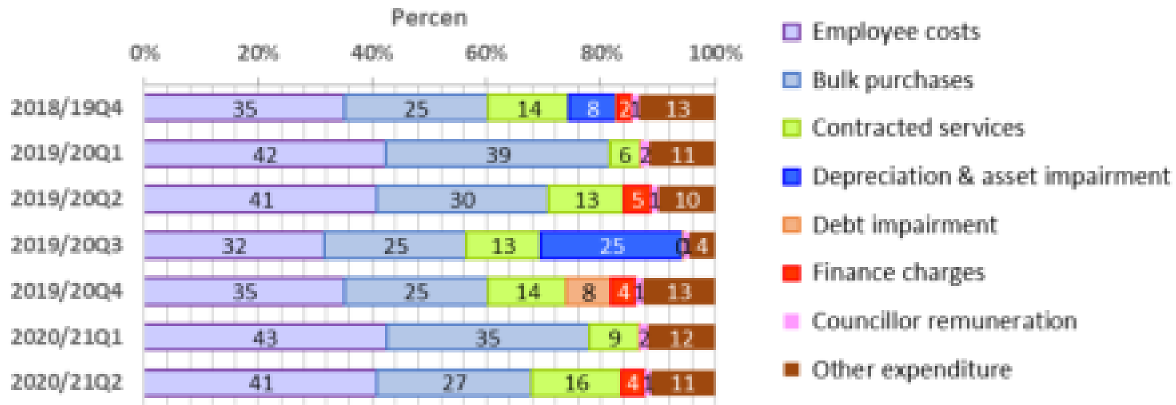
CATEGORY	CAPACITY	Munic	R miilions Expenditure category	Pre-pandemic actual				Pandemic actual			% Change YOY		
				18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	2019/20Q4	2020/21Q1	2020/21Q2
B1	High	Stellenbosch	Employee related costs	119.6	120.3	139.3	121.9	124.2	123.3	151.0	4%	2%	8%
			Bulk purchases	86.1	111.8	102.0	96.7	89.4	102.7	100.4	4%	(8%)	(2%)
			Contracted services	47.8	15.8	45.5	50.0	48.2	25.2	58.0	1%	60%	28%
			Depreciation and asset impairment	28.7	0.0	0.0	96.3	-	-	0.1	(100%)	(100%)	12 746%
			Debt impairment	0.5	0.0	0.1	0.2	28.1	0.2	0.0	6 040%	53 131%	(78%)
			Finance charges	8.3	-	16.0	-	15.2	-	14.6	83%	-	(9%)
			Remuneration of councillors	4.3	4.4	4.4	4.5	4.6	4.6	4.6	8%	5%	4%
			Other expenditure	45.5	32.4	33.8	17.1	44.6	33.8	41.5	(2%)	4%	23%
			Total operating expenditure	**340.7**	**284.6**	**341.2**	**386.6**	**354.3**	**289.7**	**370.2**	**4%**	**2%**	**9%**
B1	High	Drakenstein	Employee related costs	149.1	149.4	182.6	154.5	152.3	146.5	187.0	2%	(2%)	2%
			Bulk purchases	97.2	190.9	165.0	172.5	162.0	245.0	180.6	67%	28%	9%
			Contracted services	52.7	24.7	48.9	37.0	48.3	18.9	34.7	(8%)	(23%)	(29%)
			Depreciation and asset impairment	-	53.5	53.5	-	-	-	119.2	-	(100%)	123%
			Debt impairment	18.1	13.2	31.2	13.2	7.8	20.9	69.4	(57%)	58%	122%
			Finance charges	48.3	40.5	40.5	27.0	0.4	-	91.9	(99%)	(100%)	127%
			Remuneration of councillors	7.5	7.5	7.5	7.4	8.5	7.7	7.8	13%	2%	3%
			Other expenditure	36.9	38.3	35.9	32.1	32.4	30.2	34.0	(12%)	(21%)	(5%)
			Total operating expenditure	**409.8**	**517.9**	**565.2**	**443.8**	**411.7**	**469.2**	**724.5**	**.5%**	**(9%)**	**28%**
B3	Medium	Swartland	Employee related costs	56.0	47.3	59.5	51.1	51.7	50.4	67.0	(8%)	7%	13%
			Bulk purchases	61.1	59.5	47.7	51.2	51.9	63.0	55.5	(15%)	6%	16%
			Contracted services	18.5	8.1	16.1	18.6	16.3	10.0	11.6	(12%)	23%	(28%)
			Depreciation and asset impairment	-	-	-	7.1	69.9	-	-	-	-	-
			Debt impairment	2.1	0.1	-	2.0	1.6	(0.0)	-	(26%)	(105%)	-
			Finance charges	7.2	0.2	6.1	0.5	6.3	0.1	5.9	(13%)	(47%)	(2%)
			Remuneration of councillors	2.6	2.6	2.6	2.5	3.1	2.7	2.7	19%	5%	4%
			Other expenditure	13.1	10.7	15.2	9.6	10.0	11.9	12.6	(24%)	11%	(17%)
			Total operating expenditure	**160.7**	**128.6**	**147.2**	**142.7**	**210.7**	**138.2**	**155.3**	**31%**	**7%**	**6%**
B3	Medium	Hessequa	Employee related costs	36.6	37.2	45.8	39.4	39.1	41.3	49.1	7%	11%	7%
			Bulk purchases	20.9	21.0	26.4	30.8	29.0	35.0	21.8	39%	67%	(18%)
			Contracted services	5.9	3.4	8.0	8.3	7.4	4.0	7.9	26%	19%	(%)
			Depreciation and asset impairment	4.6	-	16.1	8.0	5.4	-	13.2	17%	-	(18%)
			Debt impairment	14.3	1.6	13.0	12.1	8.5	1.2	19.6	(40%)	(24%)	51%
			Finance charges	5.3	-	6.4	-	5.8	-	6.0	10%	-	(6%)
			Remuneration of councillors	1.9	1.9	1.9	1.9	2.2	2.0	2.0	15%	4%	3%
			Other expenditure	10.5	13.2	13.9	12.4	11.8	11.0	15.6	13%	(16%)	12%
			Total operating expenditure	**99.8**	**78.2**	**131.5**	**112.9**	**109.2**	**94.6**	**135.3**	**9%**	**21%**	**3%**

CATEGORY	CAPACITY	Munic	R miilions Expenditure category	Pre-pandemic actual 18/19Q4	19/20Q1	19/20Q2	19/20Q3	Pandemic actual 19/20Q4	20/21Q1	20/21Q2	% Change YOY 2019/20Q4	2020/21Q1	2020/21Q2
B3	Medium	Bergrivier	Employee related costs	29.8	30.3	36.4	23.5	28.9	30.9	37.7	(3%)	2%	4%
			Bulk purchases	26.6	22.9	22.2	21.8	31.5	24.3	24.5	18%	6%	10%
			Contracted services	7.3	3.6	4.2	4.1	3.6	3.6	4.3	(51%)	1%	3%
			Depreciation and asset impairment	3.6	5.8	-	9.3	-	5.8	6.1	(100%)	%	-
			Debt impairment	-	5.4	-	-	-	6.7	6.7	-	25%	-
			Finance charges	4.2	1.8	2.0	-	4.7	2.5	1.6	11%	-	(19%)
			Remuneration of councillors	1.6	1.6	1.6	1.6	1.8	1.7	1.7	14%	3%	4%
			Other expenditure	11.3	10.6	8.5	11.3	10.3	8.5	8.2	(9%)	(20%)	(3%)
			Total operating expenditure	**84.5**	**82.0**	**74.9**	**71.6**	**80.7**	**84.0**	**90.9**	**(5%)**	**2%**	**21%**
B3	Low	Swellendam	Employee related costs	21.2	22.8	26.9	23.6	22.8	23.8	28.7	7%	4%	7%
			Bulk purchases	11.8	15.7	15.0	13.4	12.6	15.4	15.8	7%	(2%)	6%
			Contracted services	4.1	10.1	7.9	5.1	4.0	3.3	6.3	(2%)	(67%)	(21%)
			Depreciation and asset impairment	0.0001	-	4.7	3.1	2.6	2.9	2.9	2 885 856%	-	-
			Debt impairment	0.9	-	-	2.7	-	3.7	6.2	(100%)	-	-
			Finance charges	0.3	1.4	0.5	1.2	0.5	1.3	0.2	99%	-	(53%)
			Remuneration of councillors	1.2	1.2	1.3	1.3	1.5	1.3	1.3	19%	7%	4%
			Other expenditure	9.2	6.7	10.5	5.5	5.6	5.7	11.7	(39%)	(15%)	12%
			Total operating expenditure	**48.7**	**57.9**	**66.7**	**55.8**	**49.7**	**57.4**	**73.2**	**2%**	**(1%)**	**10%**
B3	Medium	Kannaland	Employee related costs	18.9	11.2	16.7	14.5	13.4	10.1	17.7	(29%)	(10%)	6%
			Bulk purchases	9.0	0.4	16.0	1.7	6.5	13.6	8.1	(27%)	3 127%	(49%)
			Contracted services	5.6	0.7	2.1	3.9	1.5	1.1	2.6	(73%)	54%	25%
			Depreciation and asset impairment	-	-	-	-	-	-	0.001	-	-	-
			Debt impairment	8.1	0.03	0.02	(0.00)	0.01	-	0.05	(100%)	(100%)	-
			Finance charges	0.4	0.1	0.1	0.1	0.0	0.0	0.1	(97%)	-	(48%)
			Remuneration of councillors	2.8	0.4	0.7	0.5	0.6	0.5	0.6	(80%)	15%	(18%)
			Other expenditure	6.9	1.5	2.3	2.1	1.1	2.9	3.7	(84%)	88%	62%
			Total operating expenditure	**51.7**	**14.5**	**37.9**	**22.8**	**23.1**	**28.3**	**32.8**	**(55%)**	**95%**	**(13%)**
B3	Medium	Laingsburg	Employee related costs	7.3	5.8	5.7	6.1	6.4	6.8	8.0	(12%)	18%	40%
			Bulk purchases	2.0	2.2	0.7	2.8	2.0	1.6	2.5	1%	(25%)	268%
			Contracted services	2.2	0.5	0.7	0.6	1.0	1.2	2.5	(57%)	123%	257%
			Depreciation and asset impairment	2.4	-	7.3	3.2	2.4	1.0	1.9	2%	-	(74%)
			Debt impairment	6.3	-	21.4	4.3	8.6	4.3	8.6	36%	-	(60%)
			Finance charges	0.001	0.001	0.001	0.001	0.005	0.004	0.0003	761%	710%	(76%)
			Remuneration of councillors	1.0	0.8	0.5	0.8	0.9	0.6	0.8	(15%)	(27%)	55%
			Other expenditure	4.2	3.5	5.3	3.9	2.4	4.0	4.6	(42%)	15%	(14%)
			Total operating expenditure	**25.4**	**12.7**	**41.7**	**21.7**	**23.7**	**19.5**	**28.9**	**(7%)**	**53%**	**(31%)**

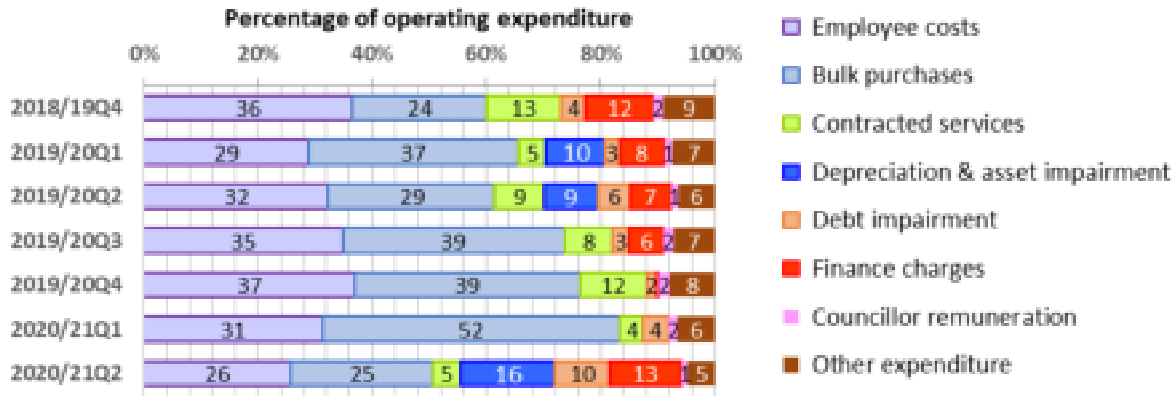
CATEGORY	CAPACITY	Municipality	R millions Expenditure category	Pre-pandemic actual				Pandemic actual			% Change YOY		
				18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	19/20Q4	20/21Q1	20/21Q2
C1	Medium	Cape Winelands	Employee related costs	17.6	45.1	54.9	51.5	47.6	49.3	57.6	171%	9%	5%
			Contracted services	12.7	2.4	9.0	16.2	8.4	2.4	9.5	(34%)	1%	7%
			Depreciation and asset impairment	6.2	-	4.6	2.6	2.6	-	4.3	(58%)		(7%)
			Remuneration of councillors	2.2	3.0	3.0	3.0	3.5	3.2	3.2	60%	4%	5%
			Other expenditure	24.1	19.5	28.1	32.3	26.3	17.8	26.0	9%	(9%)	(8%)
			Total operating expenditure	**62.8**	**70.1**	**99.7**	**105.7**	**88.4**	**72.7**	**100.6**	**41%**	**4%**	**1%**
C1	Medium	West Coast	Employee related costs	38.8	39.8	51.3	41.6	41.4	44.3	53.1	7%	11%	3%
			Contracted services	7.9	2.2	7.9	4.7	5.2	2.1	7.3	(34%)	(5%)	(7%)
			Bulk purchases	3.2	3.1	3.0	2.4	2.4	1.4	5.1	(26%)	(55%)	72%
			Depreciation and asset impairment	1.2	-	3.2	1.8	2.0	0.0	3.5	71%	-	11%
			Debt impairment	0.6	-	-	-	0.4	-	-	(35%)	-	-
			Finance charges	0.0	0.0	0.9	0.9	0.9	0.0	0.4	15 175%	149%	(59%)
			Remuneration of councillors	1.5	1.6	1.6	1.6	1.8	1.7	1.7	15%	8%	10%
			Other expenditure	28.3	23.5	43.4	39.9	26.2	25.8	36.8	(8%)	10%	(15%)
			Total operating expenditure	**81.6**	**70.2**	**111.2**	**92.8**	**80.2**	**75.3**	**108.0**	**(2%)**	**7%**	**(3%)**
C1	Medium	Central Karoo	Employee related costs	10.1	6.5	13.4	10.9	11.3	4.6	9.2	12%	(29%)	(31%)
			Contracted services	11.1	0.8	1.1	0.8	3.4	0.1	0.3	(69%)	(88%)	(76%)
			Depreciation and asset impairment	(0.0)	-	-	-	-	-	-	(100%)	-	-
			Remuneration of councillors	0.6	0.3	1.0	1.0	1.1	0.8	0.9	85%	130%	(11%)
			Other expenditure	9.0	3.6	6.6	7.1	4.8	6.6	6.2	(47%)	84%	(6%)
			Total operating expenditure	**30.8**	**11.3**	**22.1**	**19.8**	**20.6**	**12.1**	**16.6**	**(33%)**	**7%**	**(25%)**

Appendix 6: Composition of quarterly operating expenditures

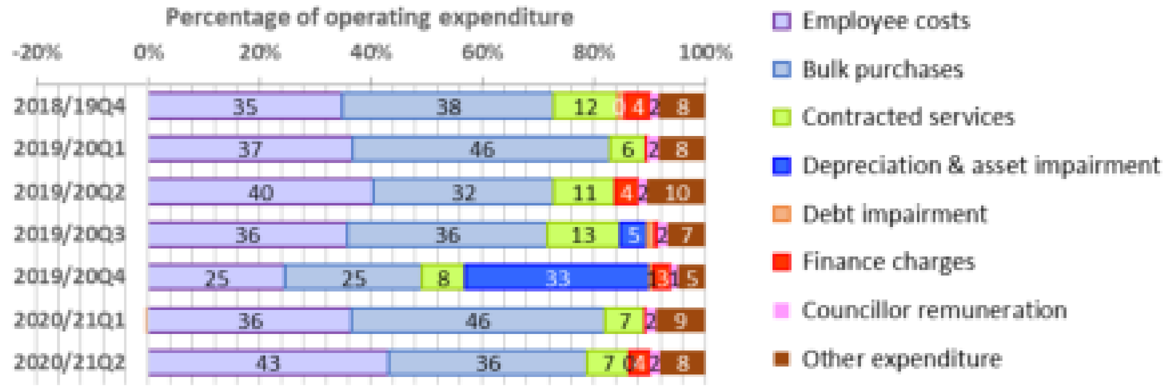
Stellenbosch - Quarterly operating expenditure by item



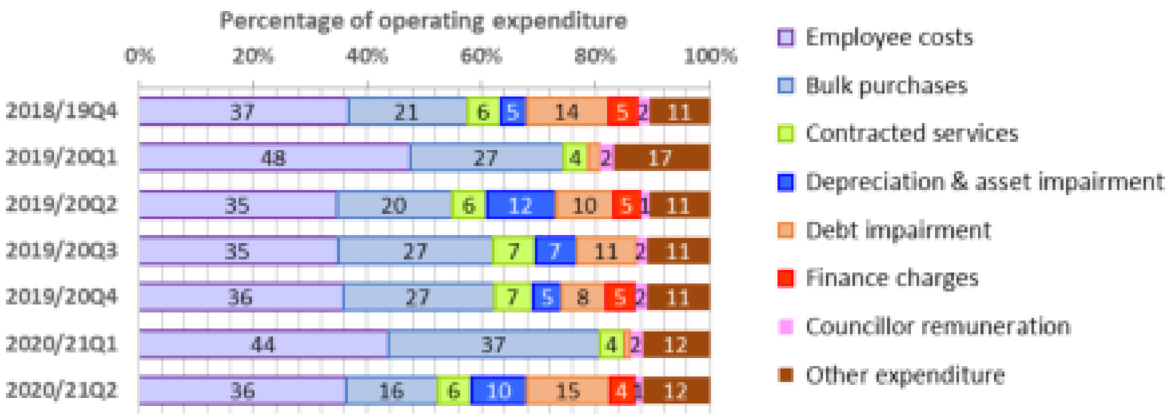
Drakenstein - Quarterly operating expenditure by item



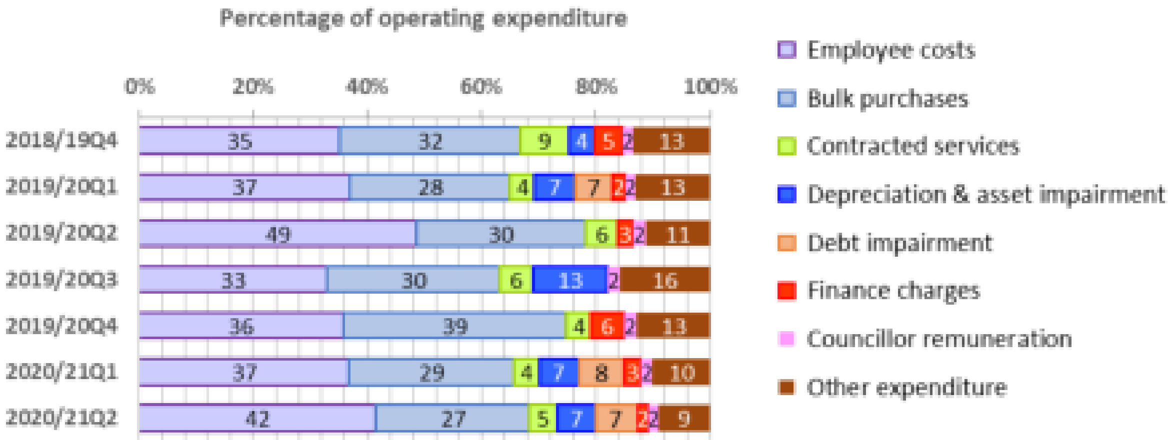
Swartland - Quarterly operating expenditure



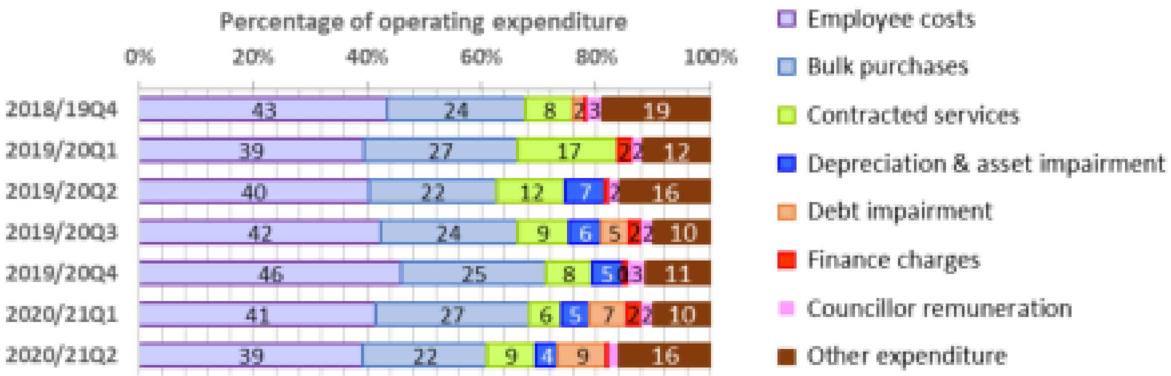
Hessaqua - Quarterly Operating Expenditure

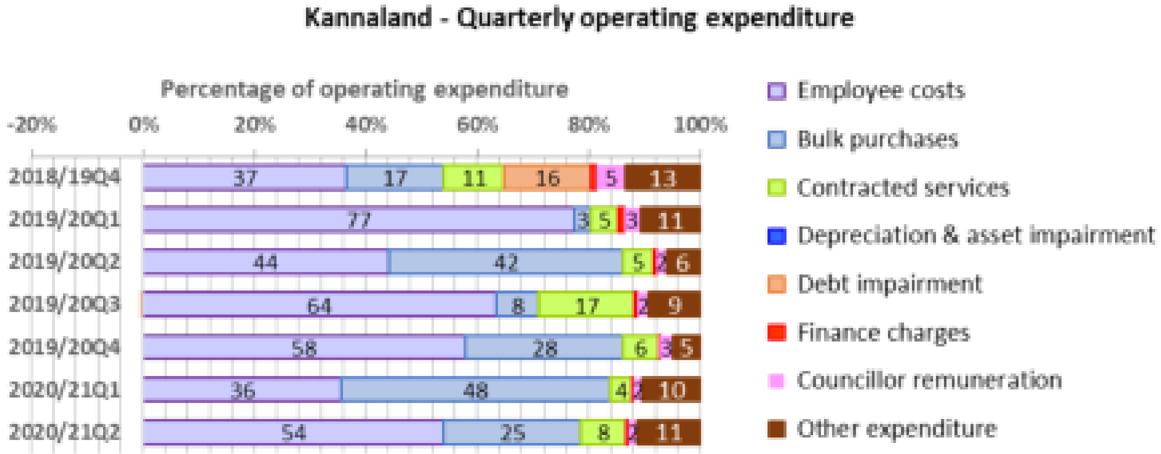


Bergrivier - Quarterly Operating Expenditure

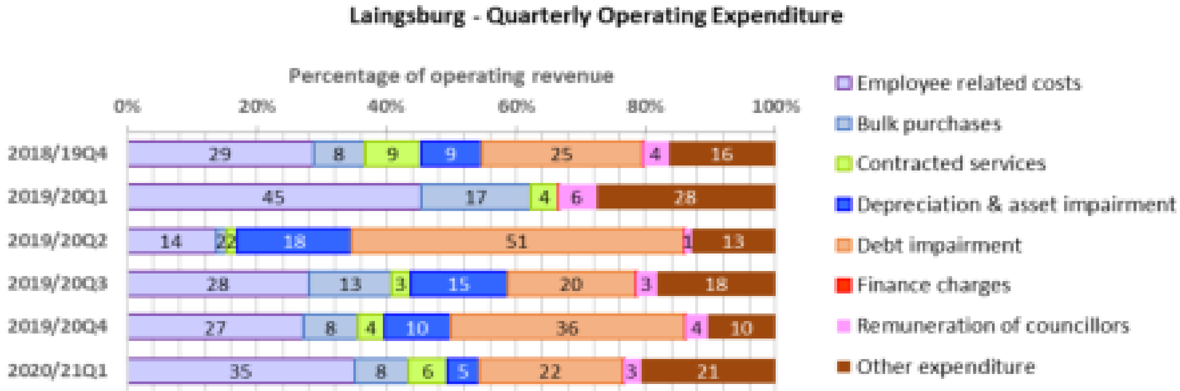


Swellendam - Quarterly operating expenditure

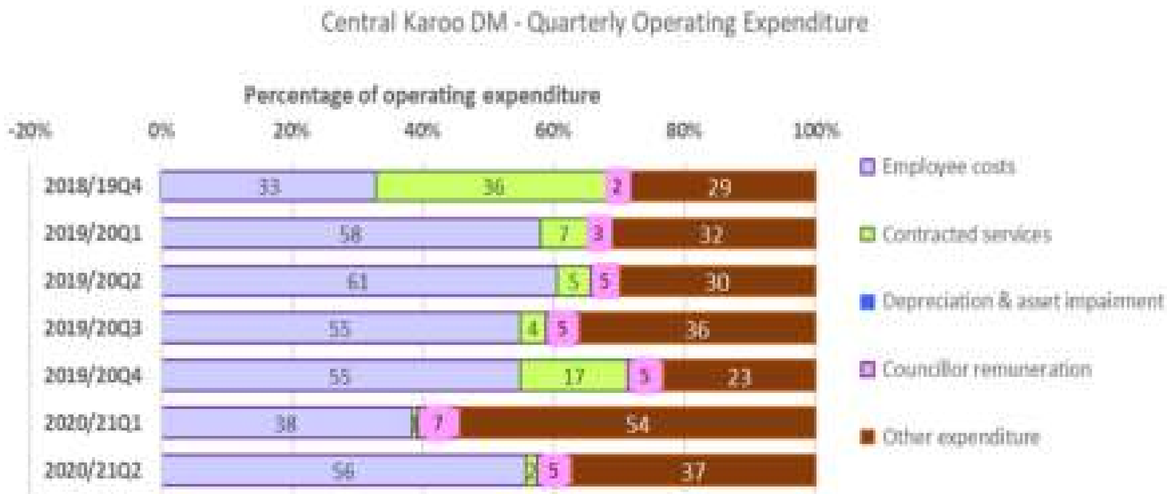




Kannaland - Quarterly operating expenditure
Percentage of operating expenditure
-20% 0% 20% 40% 60% 80% 100%
2018/19Q4 37 17 11 16 5 13
2019/20Q1 77 3 5 3 11
2019/20Q2 44 42 5 2 6
2019/20Q3 64 8 17 2 9
2019/20Q4 58 28 6 3 5
2020/21Q1 36 48 4 2 10
2020/21Q2 54 25 8 2 11
Employee costs
Bulk purchases
Contracted services
Depreciation & asset impairment
Debt impairment
Finance charges
Councillor remuneration
Other expenditure

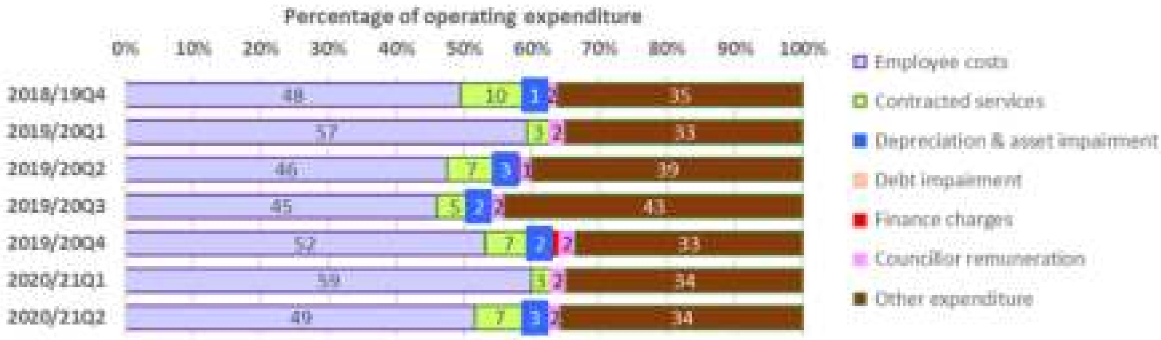


Laingsburg - Quarterly Operating Expenditure
Percentage of operating revenue
0% 20% 40% 60% 80% 100%
2018/19Q4 29 8 9 9 25 4 16
2019/20Q1 45 17 4 6 28
2019/20Q2 14 2 2 18 51 1 13
2019/20Q3 28 13 3 15 20 3 18
2019/20Q4 27 8 4 10 36 4 10
2020/21Q1 35 8 6 5 22 3 21
Employee related costs
Bulk purchases
Contracted services
Depreciation & asset impairment
Debt impairment
Finance charges
Remuneration of councillors
Other expenditure

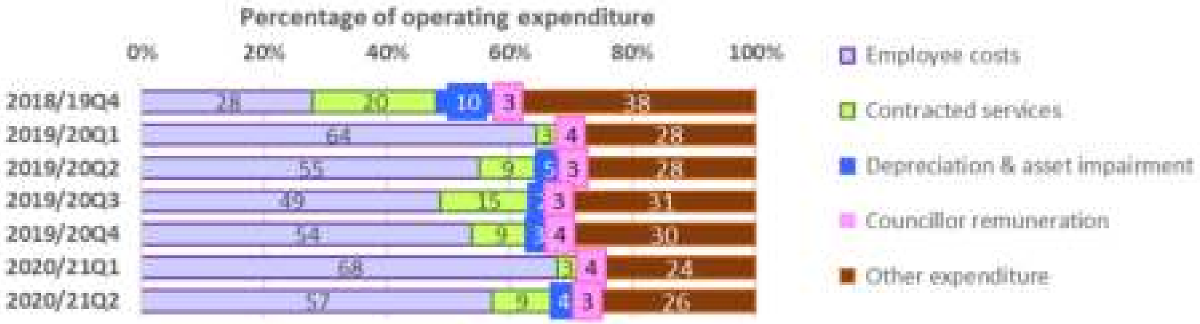


Central Karoo DM - Quarterly Operating Expenditure
Percentage of operating expenditure
-20% 0% 20% 40% 60% 80% 100%
2018/19Q4 33 36 2 29
2019/20Q1 58 7 3 32
2019/20Q2 61 5 5 30
2019/20Q3 55 4 5 36
2019/20Q4 55 17 5 23
2020/21Q1 38 7 54
2020/21Q2 56 2 5 37
Employee costs
Contracted services
Depreciation & asset impairment
Councillor remuneration
Other expenditure

West Coast DM - Quarterly Operating Expenditure

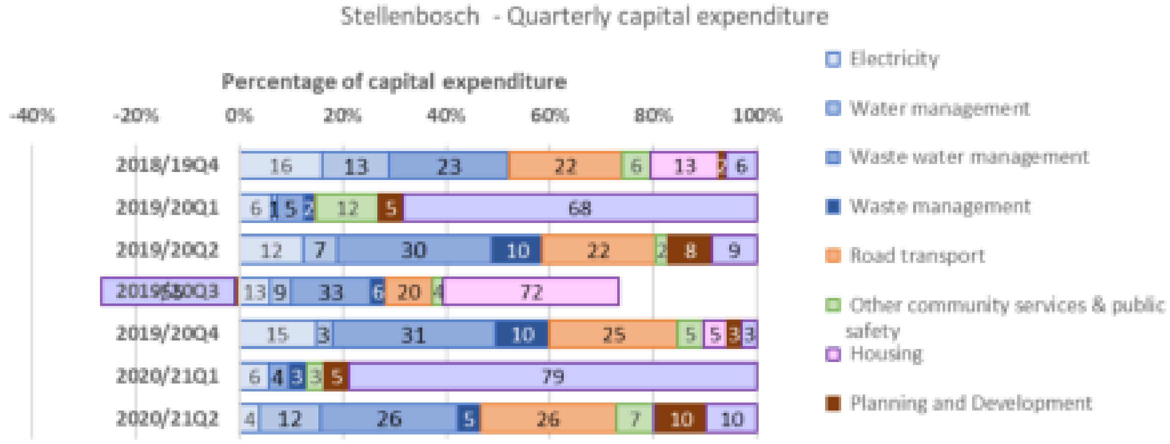


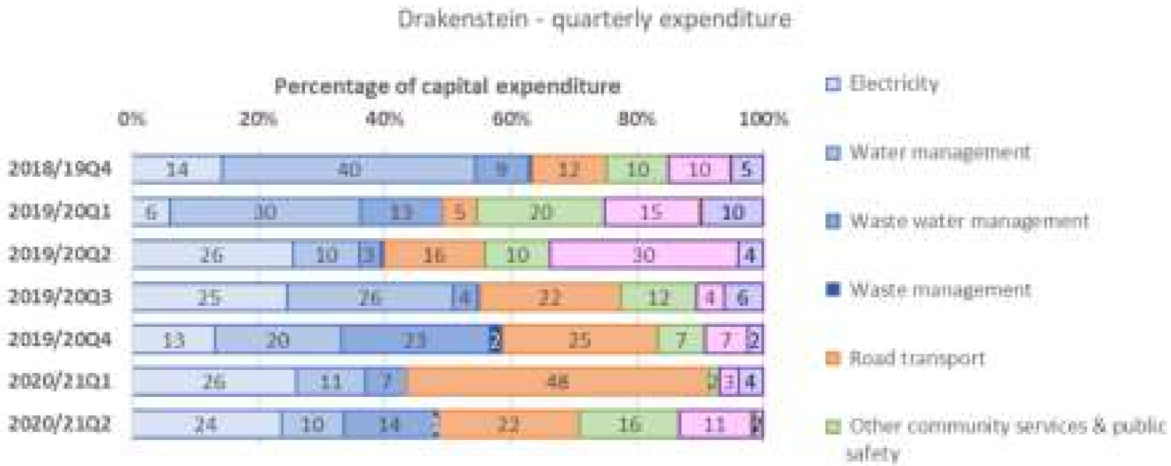
Cape Winelands - Quarterly Operating Expenditure

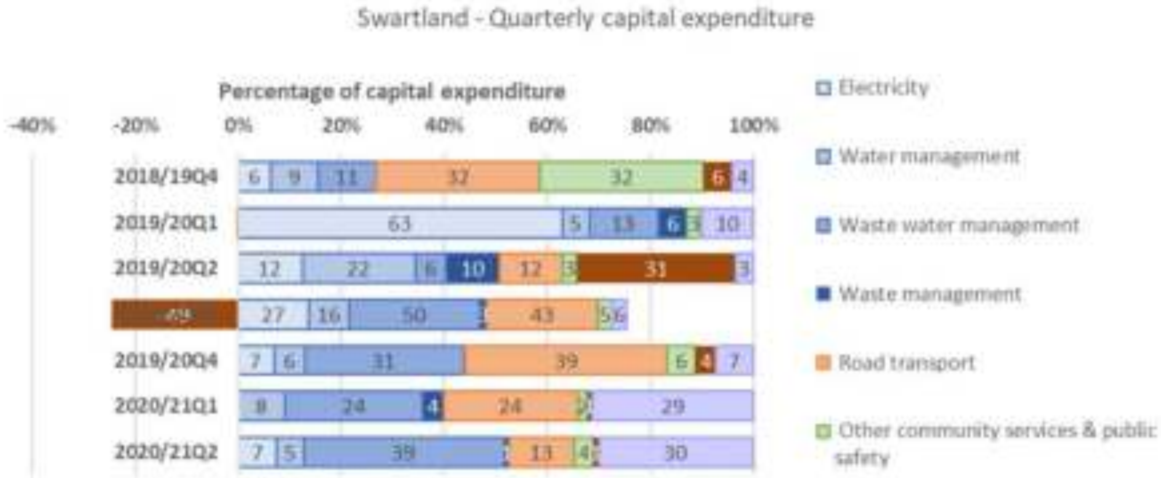


City of Cape Town - Quarterly operating expenditure

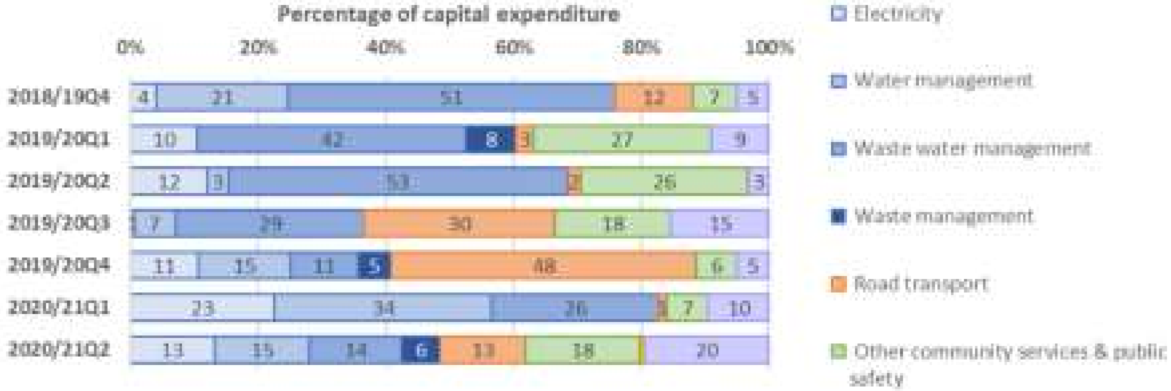
Appendix 7: Composition of quarterly capital expenditures





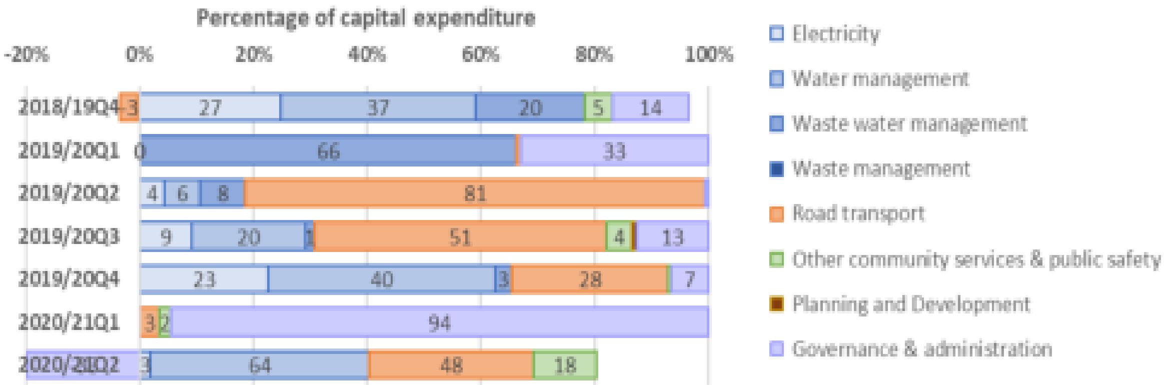


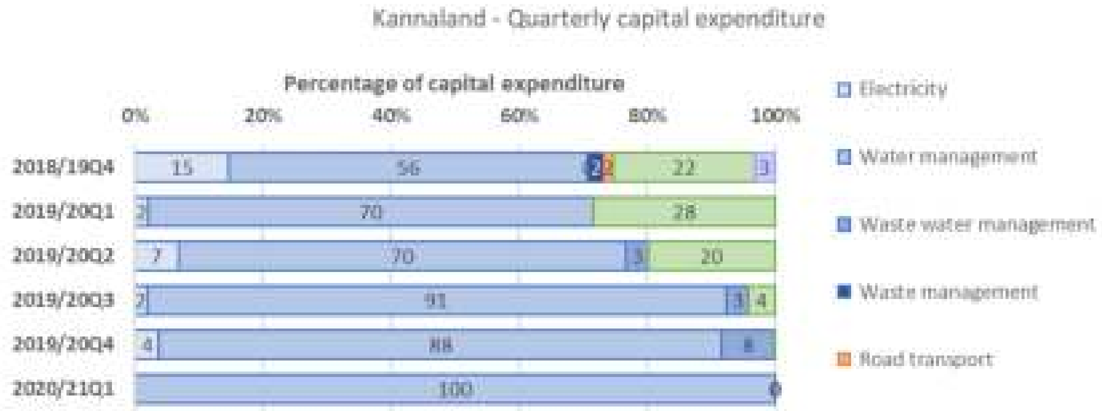
Hessequa - Quarterly capital expenditure

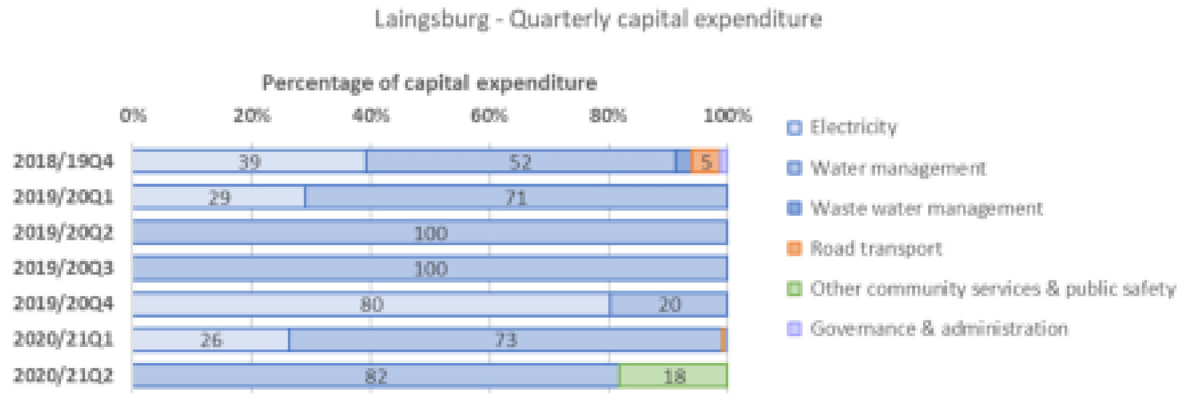


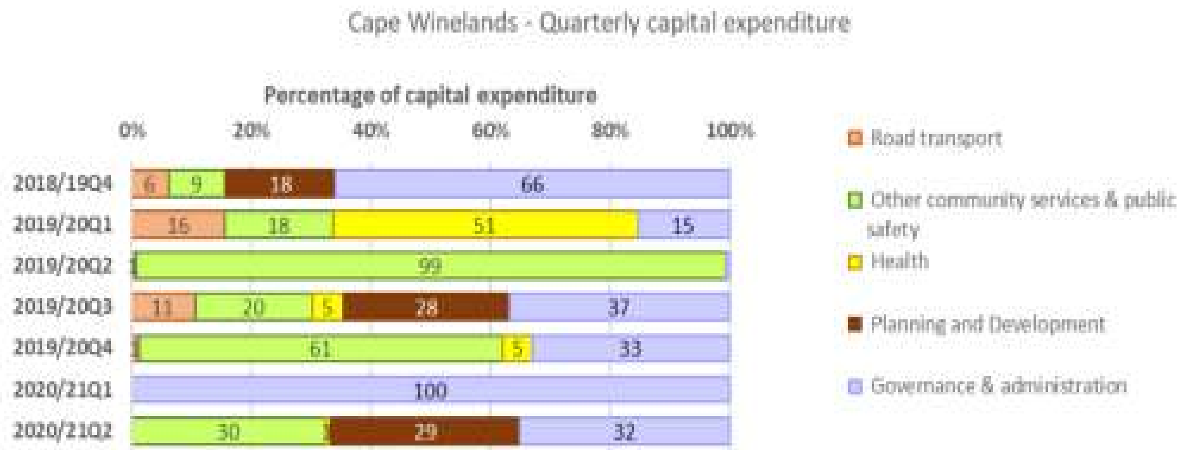
Bergrivier - Quarterly capital expenditure

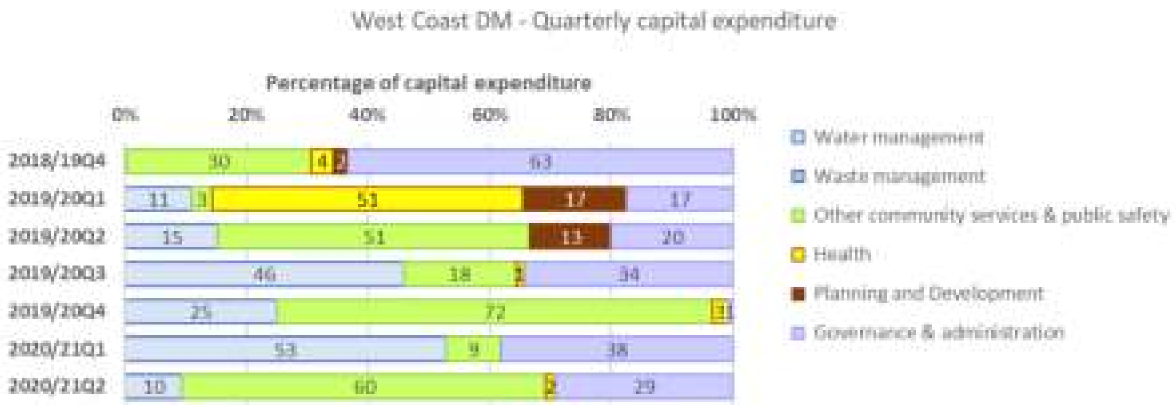
Swellendam - Quarterly capital expenditure

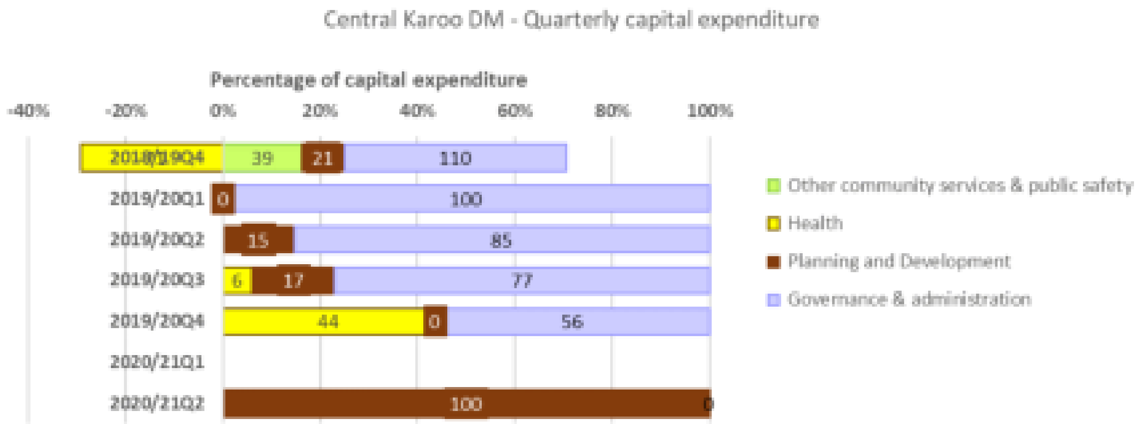


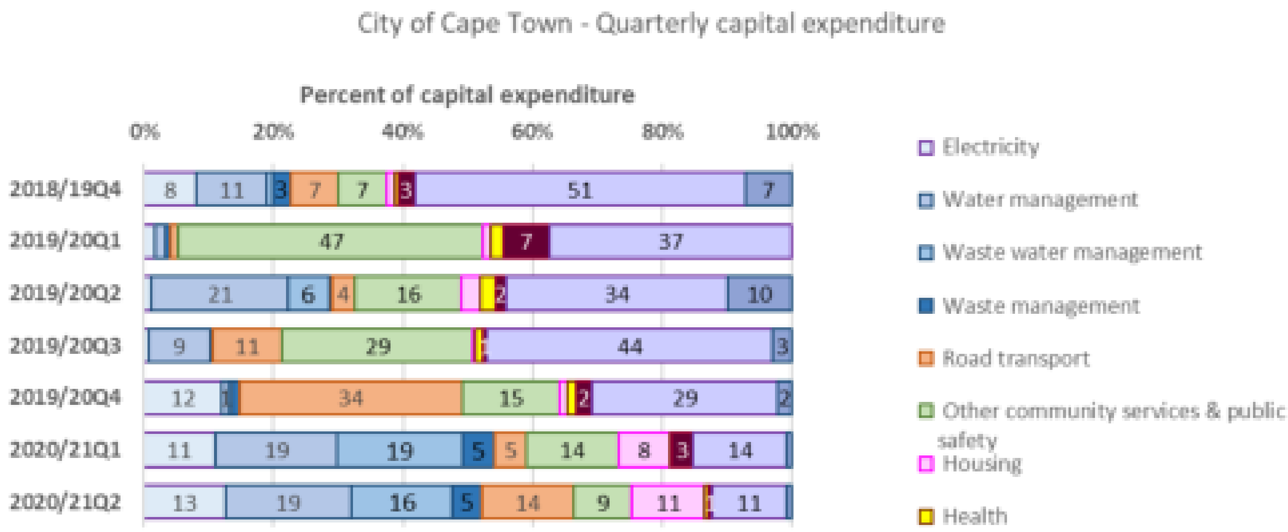

Kannaland - Quarterly capital expenditure
Percentage of capital expenditure
0%
20%
40%
60%
80%
100%
2018/19Q4
2019/20Q1
2019/20Q2
2019/20Q3
2019/20Q4
2020/21Q1
15
56
22
3
70
28
7
70
3
20
91
3
4
4
88
8
100
Electricity
Water management
Waste water management
Waste management
Road transport


Laingsburg - Quarterly capital expenditure
Percentage of capital expenditure
0%
20%
40%
60%
80%
100%
2018/19Q4
2019/20Q1
2019/20Q2
2019/20Q3
2019/20Q4
2020/21Q1
2020/21Q2
39
52
5
29
71
100
100
80
20
26
73
82
18
Electricity
Water management
Waste water management
Road transport
Other community services & public safety
Governance & administration


Cape Winelands - Quarterly capital expenditure
Percentage of capital expenditure
0%
20%
40%
60%
80%
100%
2018/19Q4
2019/20Q1
2019/20Q2
2019/20Q3
2019/20Q4
2020/21Q1
2020/21Q2
6
9
18
66
16
18
51
15
99
11
20
5
28
37
61
5
33
100
30
29
32
Road transport
Other community services & public safety
Health
Planning and Development
Governance & administration


West Coast DM - Quarterly capital expenditure
Percentage of capital expenditure
0%
20%
40%
60%
80%
100%
2018/19Q4
2019/20Q1
2019/20Q2
2019/20Q3
2019/20Q4
2020/21Q1
2020/21Q2
Water management
Waste management
Other community services & public safety
Health
Planning and Development
Governance & administration


Central Karoo DM - Quarterly capital expenditure
Percentage of capital expenditure
-40%
-20%
0%
20%
40%
60%
80%
100%
2018/19Q4
2019/20Q1
2019/20Q2
2019/20Q3
2019/20Q4
2020/21Q1
2020/21Q2
Other community services & public safety
Health
Planning and Development
Governance & administration


City of Cape Town - Quarterly capital expenditure
Percent of capital expenditure
0%
20%
40%
60%
80%
100%
2018/19Q4
2019/20Q1
2019/20Q2
2019/20Q3
2019/20Q4
2020/21Q1
2020/21Q2
Electricity
Water management
Waste water management
Waste management
Road transport
Other community services & public safety
Housing
Health

Appendix 8: Year-on-Year change in quarterly capital expenditure

CATEGORY	CAPACITY	Municip	R miilions	Pre-pandemic actual				Pandemic actual			% Change YOY		
			Expenditure category	18/19Q4	19/20Q1	19/20Q2	19/20Q3	19/20Q4	20/21Q1	20/21Q2	19/20Q4	20/21Q1	20/21Q2
B1	H	Stellenbosch	Electricity	29.0	5.9	13.4	8.9	11.7	3.6	3.3	(60%)	(38%)	(75%)
			Water management	23.9	1.1	7.3	6.3	2.7	-	9.7	(89%)	(100%)	34%
			Waste water management	41.8	4.8	32.4	23.1	25.1	2.4	22.0	(40%)	(50%)	(32%)
			Waste management	0.4	2.0	10.8	4.3	8.4	2.1	3.9	1 972%	7%	(64%)
			Road transport	39.7	0.2	23.9	13.9	19.7	0.1	21.8	(50%)	(52%)	(9%)
			Other community services & public safety	10.3	11.4	2.7	3.2	4.0	2.1	6.2	(61%)	(81%)	129%
			Housing	23.7	-	0.0	51.2	3.6	0.0	0.2	(85%)	-	-
			Planning, Development & Environment	2.8	4.5	9.0	(1.4)	2.2	3.1	8.0	(23%)	(30%)	(10%)
			Governance & administration	10.7	64.2	9.5	(38.7)	2.4	50.1	8.2	(77%)	(22%)	(14%)
			Total capital expenditure	**182.2**	**94.1**	**108.9**	**70.7**	**79.7**	**63.6**	**83.4**	**(56%)**	**(32%)**	**(23%)**
B1	H	Drakenstein	Electricity	29.4	1.6	17.0	15.7	13.1	9.0	9.7	(56%)	451%	(43%)
			Water management	82.4	8.1	7.0	16.7	19.9	3.7	4.2	(76%)	(54%)	(40%)
			Waste water management	17.6	3.6	2.2	2.5	23.2	2.3	5.9	32%	(37%)	165%
			Waste management	1.2	-	0.4	0.2	2.0	-	0.3	64%	-	-
			Road transport	24.2	1.4	10.7	14.3	24.4	16.4	9.3	1%	1 054%	(13%)
			Other community services & public safety	20.0	5.5	6.9	7.7	7.4	0.6	6.5	(63%)	(89%)	(6%)
			Housing	20.3	4.0	19.7	2.8	6.7	1.0	4.7	(67%)	(74%)	(76%)
			Planning, Development & Environment	0.1	0.1	-	-	-	-	0.1	(100%)	(100%)	
			Governance & administration	10.6	2.6	2.7	4.0	2.4	1.4	0.7	(77%)	(48%)	(75%)
			Total capital expenditure	**205.8**	**26.9**	**66.6**	**63.9**	**99.2**	**34.4**	**41.3**	**(52%)**	**28%**	**(38%)**
B3	M	Swartland	Electricity	2.3	6.8	4.6	5.2	3.5	1.9	3.4	51%	(72%)	(25%)
			Water management	3.3	0.6	8.0	3.1	3.0	1.8	2.4	(10%)	217%	(70%)
			Waste water management	4.0	1.4	2.2	9.7	15.5	5.2	17.7	284%	259%	705%
			Waste management	-	0.6	3.7	0.5	0.1	0.8	0.5	-	36%	(88%)
			Road transport	11.6	(0.0001)	4.5	8.3	19.7	5.0	5.8	70%	(8 683 312%)	28%
			Other community services & public safety	11.5	0.3	0.9	1.0	2.8	0.4	1.7	(76%)	30%	80%
			Housing	-	-	-	-	-	-		-	-	-
			Planning, Development & Environment	2.0	0.0	11.3	(9.4)	2.0	0.2	0.5	(2%)	1 228%	(96%)
			Governance & administration	1.5	1.1	1.2	1.1	3.6	6.1	13.7	143%	460%	1 021%
			Total capital expenditure	**36.3**	**10.8**	**36.5**	**19.4**	**50.2**	**21.3**	**45.5**	**38%**	**98%**	**25%**
B3	M	Hessequa	Electricity	0.7	0.1	1.7	0.1	3.2	1.6	1.3	391%	1 060%	(25%)
			Water management	3.3	-	0.5	0.6	4.4	2.4	1.4	32%	-	-
			Waste water management	8.3	0.5	7.4	2.9	3.2	1.8	1.4	(61%)	232%	(81%)
			Waste management	-	0.1	0.0	0.0	1.6	-	0.6	-	(100%)	3 929%
			Road transport	2.0	0.0	0.3	2.9	14.5	0.1	1.3	644%	131%	400%
			Other community services & public safety	1.1	0.4	3.7	1.8	2.0	0.5	1.7	75%	27%	(53%)
			Housing	-	-	-	-	0.0	-		-	-	-
			Planning, Development & Environment	0.0	-	0.0	-	-	-	0.1	-	-	-
			Governance & administration	0.8	0.1	0.4	1.5	1.5	0.7	1.9	86%	460%	332%
			Total capital expenditure	**16.2**	**1.3**	**14.0**	**9.8**	**30.5**	**6.9**	**9.7**	**88%**	**432%**	**(31%)**

CATEGORY	CAPACITY	Municip	R miilions Expenditure category	Pre-pandemic actual 18/19Q4	19/20Q1	19/20Q2	19/20Q3	Pandemic actual 19/20Q4	20/21Q1	20/21Q2	% Change YOY 19/20Q4	20/21Q1	20/21Q2
B3	M	Bergrivier	Electricity	-	0.0	2.7	1.1	5.1	0.0	0.4	-	13%	(84%)
			Water management	-	0.1	0.3	0.6	0.8	0.1	0.6	-	55%	76%
			Waste water management	-	1.2	2.9	1.4	3.7	0.0	0.3	-	(100%)	(90%)
			Waste management	-	0.2	0.4	0.1	0.1	0.1	0.3	-	(32%)	(41%)
			Road transport	-	0.7	0.8	4.2	5.5	2.4	6.2	-	267%	660%
			Other community services & public safety	-	0.1	1.1	3.7	0.6	0.3	1.1	-	132%	2%
			Housing	-	0.0	0.0	-	-	-		-	(100%)	(100%)
			Planning, Development & Environment	-	0.6	0.5	1.2	1.7	0.4	0.3	-	(23%)	(39%)
			Governance & administration	-	0.5	0.7	0.0	0.8	1.8	1.1	-	290%	64%
			Total capital expenditure	**-**	**3.3**	**9.5**	**12.4**	**18.1**	**5.2**	**10.3**	**-**	**58%**	**9%**
B3	L	Swellendam	Electricity	1.7	-	0.2	0.3	1.2	-	0.1	(31%)	-	-
			Water management	2.3	-	0.3	0.7	2.0	-	3.1	(11%)	-	-
			Waste water management	1.3	0.3	0.4	0.1	0.1	-		(89%)	(100%)	(100%)
			Waste management	(0.0)	-	-	-	-	-		(100%)	-	-
			Road transport	(0.2)	0.0	3.8	1.7	1.4	0.1	2.4	(795%)	1 806%	(38%)
			Other community services & public safety	0.3	-	-	0.1	0.0	0.0	0.9	(92%)	-	-
			Housing	-	-	-	-	-	-		-	-	-
			Planning, Development & Environment	-	-	-	0.0	-	-		-	-	-
			Governance & administration	0.9	0.2	0.0	0.4	0.3	2.0	(1.6)	(63%)	1 134%	(6 656%)
			Total capital expenditure	**6.3**	**0.5**	**4.7**	**3.4**	**5.1**	**2.1**	**4.9**	**(18%)**	**330%**	**5%**
B3	M	Kannaland	Electricity	2.1	0.1	0.2	0.0	0.2	-		(88%)	(100%)	(100%)
			Water management	7.8	2.5	2.5	1.2	5.6	4.8	3.1	(28%)	96%	26%
			Waste water management	-	-	0.1	0.0	0.5	-		-	-	-
			Waste management	0.3	-	-	-	-	-		(100%)	-	-
			Road transport	0.2	-	-	-	-	-		(100%)	-	-
			Other community services & public safety	3.1	1.0	0.7	0.1	0.0	-	0.4	(100%)	(100%)	(43%)
			Housing	-	-	-	-	-	-		-	-	-
			Planning, Development & Environment	-	-	-	-	-	-		-	-	-
			Governance & administration	0.4	-	-	-	-	-		(100%)	-	-
			Total capital expenditure	**14.0**	**3.6**	**3.5**	**1.3**	**6.4**	**4.8**	**3.5**	**(54%)**	**36%**	**(.5%)**
B3	M	Laingsburg	Electricity	1.8	0.4	-	-	0.9	11.0		(53%)	2 560%	
			Water management	2.5	1.0	3.1	1.5	0.2	30.5	6.0	(91%)	2 914%	96%
			Waste water management	0.1	-	-	-	-	-		(100%)	-	
			Waste management	-	-	-	-	-	-		-	-	
			Road transport	0.2	-	-	-	-	0.2		(100%)	-	
			Other community services & public safety	0.0	-	-	-	-	0.1	1.3	(100%)	-	
			Housing	-	-	-	-	-	-		-	-	
			Planning, Development & Environment	-	-	-	-	-	-		-	-	
			Governance & administration	0.1	-	-	-	-	0.0		(100%)	-	
			Total capital expenditure	**4.7**	**1.4**	**3.1**	**1.5**	**1.1**	**41.8**	**7.3**	**(77%)**	**2 836%**	**139%**