



Submission to the National Ports Regulator

SUBJECTS:

THE NATIONAL PORT AUTHORITY'S TARIFF APPLICATION FOR THE 2022 / 2023 FINANCIAL YEAR

PREAMBLE:

The South African Association of Freight Forwarders (the Association) makes this submission on behalf of its members and its member's clients.

This is the 11th annual submission by the Association to the Regulator on the National Port Authority's tariff applications. On that basis, previous information submitted on SAAFF's position as the sole voice of the industry in South Africa has been omitted from this submission but is available on request.

SUBMISSION:

Tariff Methodology:

In this Association's previous submission covering financial year 2021/22 attention was drawn to the Authority's executive summary in that year's application where certain inherent limitations of the current tariff methodology were discussed.

The Association believes that these limitations are once again exposed in the current application. Where previous year's volume and revenue growth do not reach expectations and volume growth assumptions are relatively low, then the structure of the methodology dictates that increases well beyond what would be appropriate in a low growth economic environment are demanded. This helps to create an environment which facilitates and accentuates the low volumes and revenue growth currently experienced.

The consequences of this in previous years and again in this application are that the Authority has to resort to the use of the ETIMC to cushion port customers from excessive increases. The inevitable result of this approach is that this tariff application, if successful, will exhaust all remaining funds in the ETIMC. Since those funds are clearly intended to be used for the benefit of the customers, it is arguable that protecting them from an increase which probably should not be levied in the first place, is not an appropriate use of the funds.



Without the buffer of the ETIMC the Authority will in future be forced to apply for tariff increases well above what can be afforded by port customers and the broader economy.

The ETIMC has provided cash reserves which have enabled the Authority and Regulator to smooth out tariff increases over recent years and keep rates at or below inflation. Port users will be concerned that without a substantial transfer of cash resources from the Transnet Group to the “corporatised” Authority’s reserves then future increases will be excessive, imposing a real constraint on trade and economic development.

Cargo Volume & Revenue Forecast:

In preparing submissions on the Authority’s tariff applications port users are constrained by a lack of financial and volume data on which to base their assessment of current levels and forecasts going forward. Actual revenue figures will not be available until Transnet’s annual financial report is released after the submission deadline.

With the exception of a marginal increase in liquid bulk and healthy growth in automotive volumes, financial 2020 saw material drops in all commodities and cargo types. Volumes and revenue were impacted by the COVID19 pandemic over the entire 12 months. Revenue from freight, (cargo dues) dropped by 8,79% and from “other”, Marine and Real Estate by 5,46% *
(source: Transnet Annual Report 2020)

Volumes during calendar 2021, are showing a different and much improved situation. An example of this is the increase in the high revenue full container imports through the port of Durban. During the first five months of this financial year full 6m. import containers increased year on year by 20392; (15.5%) and 12m Full imports by 41503; (37.5%). Increased revenue from cargo dues will amount to >R193m on this traffic alone. Calendar year volumes of most other commodities through Durban are running well ahead of the same period 2020.

This assessment contradicts the Authority’s opinion expressed in section 7.4.1. of the application where container growth forecast was in the region of 5%. It reflects the global surge in demand subsequent to countries exiting various levels of Covid-induced lockdowns.

The application estimates marine revenue for the year ending March 2021/22 at R8163m. this is marginally higher than the relevant ROD which allowed for revenue of R8109m. The Association believes that a final revenue figure for 2021/22 will be at least 5% higher resulting in



revenue of R8400m. The improvement in volumes is forecast to continue into 2022/23 where growth will reach 7.5%.

Half year volume data will be available to the Regulator prior to announcing the ROD as will Transnet's annual report for 2021.

The Association trusts that the Regulator will be in a position to arrive at a more accurate estimate of revenue for the current year using the Transnet annual report for 2021 and half year volume data from the 2022 interim report.

Weighted Average Cost of Debt.

In past submissions the Association has raised the high level of cost of debt. Once again weighted average debt (WACD) is at 10.75% (real 6.14%) whilst global interest rates continue at far lower levels, (US Treasury 10-year yield is currently 1.61%, real -89%) Though fully understanding forex risks the Association continues to question whether there is sufficient effort to reduce interest cost on both long and short-term borrowings. Corporatisation must provide an opportunity for the Authority to review borrowing and the cost of debt. With R9545m capex investment planned through 2025 the use of ring-fenced project finance would appear to be one opportunity to address high debt costs. Future applications should include granular data on debt costs and action taken to reduce borrowing and interest liabilities.

Tax Calculation.

The application utilises a corporate tax rate of 28% for financial 2022/23, The Regulator will no doubt take into consideration the actual corporate tax rate for 2023 which is 27%.

Port users will take note of the substantial year on year increase in corporate tax liability as a result of the corporatisation of the Authority, should it occur in 2023. The application forecasts taxation for 2022/23 at R1211m. whereas the most recent ROD utilised an equitable tax rate of 14.03% amounting to R471m. in 2021 / 22. This huge increase in tax liability (R740m) largely due to the corporatisation of the Authority, is responsible for the bulk of the increase in revenue requirement. Had the authority had been able to retain its surplus cash generated over the years, then the taxation issue would not really present a problem



Regulatory Asset Base (RAB):

Table 19, Page 46, of the application indicates an opening Nett Book Value (NBV) for 2022/23 of R78447m. The ROD for the previous year 2021/22 Table 3 Page 10 required a closing NBV balance of R76831m. There is no apparent explanation for the increase of R1616m.

The Association's concerns around the Regulatory Asset Base calculation have been raised in previous submissions. On March the 28th 2018 the Regulator articulated the methodology to be used in arriving at an accurate RAB. Those changes to the methodology would have considerably reduced the RAB and consequently had a material impact on the Authority's tariff applications, revenue stream and business model. Agreement was reached to retain the TOC calculation model which reduced RAB value only marginally in following years. The Association looks forward to a review of the RAB valuation as and when the Authority is corporatised. Here again we can refer to our repeated comments over the years around the unilateral revaluation of assets which underlies the RAB.

Operating Expenditure:

The amount of negative R547.4m appearing under 2021/22 sundry costs is not supported in the narrative.

Group cost (actual) for 2021/22 at R374m is substantially below previous and future years without explanation.

The corporatisation of the Authority should have an impact on group cost allocation, this is not reflected in 2022/23 or following year forecasts, despite the fact that corporatisation has been mandated to take place within a definite time frame.

The application would have been prepared prior to the announcement of voluntary retrenchment packages, which we understand have been accepted by a substantial number of Transnet employees. This will impact on labour costs, most likely negatively in 2021/22 but positively in future.

Submission Conclusion:

As the owner and landlord of all the country's commercial ports, as the only supplier of marine services, and as a division of Transnet that has monopoly or near monopoly on a range of port services it is incumbent upon the Authority to ensure that it provides port



services of a standard that compare with similar facilities elsewhere, at a cost that does not negatively impact on the country's economy. During the recent past it has become increasingly clear that this has not happened and that service levels have persistently declined across many port operations.

In the application's executive summary, the Authority indicates that above inflation adjustments will be required to "*deliver on Transnet's segment strategy and (incur) significant capital expenditure*". The Association does not dispute the need for urgent capital investment in our ports, the fact that such investment is now urgent underlines the extremely poor performance of the Authority in addressing capex needs over recent years, and its failure to undertake planned maintenance of equipment.

The application does not address these shortcomings or how this consistently poor performance will be corrected.

The National Port Act No 12 of 2005 provided the Authority with a clear mandate to ensure "*that adequate, affordable and efficient port services and facilities are provided*"

Since its inception the Ports Regulator has consistently understood this to mean that the Authority's responsibility was, inter-alia, to ensure that port tariffs remain competitive, are in line with global port costs and stay within the bounds of the targeted inflation bands of 3% - 6%. The Association has in past submissions made clear that it fully supports the Regulator's position on this.

Based on the Association's volume/revenue estimates above we forecast revenue as follows:

Prior Year Revenue R8500m.

Estimated Volume Growth 7.5%.

Revenue after volume growth R9137m.

This brings revenue close to the Required Revenue of R9397m which will change with adjustments to tax calculation on high income and a lower rate and possible reduction on operational expenses around group costs and labour.

Should these revenue estimates be anywhere close to accurate, it would allow for an across-the-board increase in the region of 6% whilst requiring a draw down from the ETIMC of less than R1000m.



This South African Association of Freight Forwarders Association believes that without the Regulator's positive interventions since its inception the Authority's tariff would be substantially higher. We trust that this will continue to be the case when assessing the current application.

A handwritten signature in black ink, appearing to read "D.H. Watts". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

D.H.Watts.

South African Association of Freight Forwarders

13th October 2021