GEORGE LOCAL MUNICIPALITY

Long Term Financial Plan

2022/23 – 2031/32

INCA
Portfolio Managers

Contact:

Attie van Zyl
Chief Executive

INCA Portfolio Managers (Pty) Ltd
Pinewood Square
33 Riley Road
Woodmead
Johannesburg

t: 011 202 2211
e: attie.vanzyl@inca.co.za

TABLE OF CONTENTS

LIST OF FIGURES

LIST OF GRAPHS

LIST OF TABLES

ABBREVIATIONS USED

AFS	Annual Financial Statements
ARC	Asset Replacement Cost
CPI	Consumer Price Index
CRC	Current Replacement Cost
CRR	Capital Replacement Reserve
EAP	Economically Active Population
FY	Financial Year
FYE	Financial Year End
GVA	Gross Value Added
GLM	George Local Municipality
IDP	Integrated Development Plan
INCA	Infrastructure Finance Corporation
IPM	INCA Portfolio Managers
LM	Local Municipality
LTFM	Long Term Financial Model
LTFP	Long Term Financial Plan
MRRI	Municipal Revenue Risk Indicator
MSCOA	Municipal Standard Chart of Accounts
MTREF	Medium Term Revenue and Expenditure Framework
NERSA	National Energy Regulator of South Africa
PPE	Property, Plant and Equipment
PPP	Public Private Partnership
Rm	Rand x 1 000 000
Rb	Rand x 1 000 000 000
SDF	Spatial Development Framework

EXECUTIVE SUMMARY

Introduction to the Report

1. This report contains the proposed long-term financial plan of the George Local Municipality ("George", "George LM" or "GLM"). It is submitted to the municipality for its consideration and adoption.

2. The proposed plan was preceded by an Independent Financial Assessment of George LM prepared by INCA Portfolio Managers in January 2023, drawing on the audited financial statements for the past 8 years up to FYE2021/22. This assessment is attached as Annexure 1. The report in Annexure 1 includes a summary of the latest available information on the demography, economy and household infrastructure of the GLM. Based on the findings of the Independent Financial Assessment, George LM finds itself in a healthy financial position with strong performance on key financial metrics. The strong performance is underpinned by a healthy liquidity position (liquidity ratio of 2.06:1 as at FYE2022), a collection rate in line with the NT recommended norm of 95% and substantial cash surpluses over the minimum liquidity requirements. George has, however, realised operating deficits in 6 of the 8 years under review. The municipality performed well in the provision of infrastructure services over the review period, with the levels of infrastructure backlogs being reduced in the provision of all infrastructure services.

3. George LM achieved a shadow credit rating of 7.0 on the INCA Shadow Credit Rating Model. This is "Investment Grade" and equates to a rating of A on a comparable national credit ratings scale. The municipality should have no trouble accessing competitive lending rates should it decide to approach the external market for borrowing.

4. The municipality's cash needs compared to the operating cash flows it can expect to generate, based on the economy and population of the sub-region, was modelled. This forms the basis to determine the future financial sustainability of the municipality.

5. A number of potential outcomes or scenarios were modelled. The "MTREF Case" forecasts sustained operational deficits driven by high increases of electricity bulk purchases due to NERSA tariff increases for the next two financial periods which may not be fully passed on to the consumer. The MTREF Case forecasts an overdraft position towards the end of the forecast period, mainly driven by extensive use of own cash to fund capital expenditure, resulting in cash shortfalls from FY2029/30 onwards.

6. The drivers or variables causing some of the negative impacts on the MTREF case, were addressed and presented as the **Base Case Model**. The collection rate is assumed to remain at 95% throughout the entirety of the forecast period. The MTREF capital investment programme remains unaltered, while the MTREF funding mix was altered to incorporate an accelerated borrowings programme. The NERSA tariff increases were incorporated into the Base Case Model, and consequently the corresponding tariffs that will be passed onto

the consumer were increased accordingly. Finally, a loadshedding impact scenario was incorporated into the Base Case. These assumptions will be discussed in more detail in Section 6 of this report.

7. As alluded to above, this LTFP report includes the effects of the ongoing energy crisis and how it may impact the financial position of the municipality. Our recommendations are aimed at guiding the municipality towards long-term financial sustainability and resilience, while navigating the financial and operational challenges presented by the lack of electricity supply and consequent loadshedding. The model continues to assess the potential impact of unexpected events and a range of operational and policy responses to help mitigate these impacts.

Key Findings

8. The following summary observations, pursuant to the Independent Financial Assessment for the historic period FYE2014/15 to FYE2021/22 and the interpretation of the socio-economic and infrastructure data published by the IHS Global Insight Rex database, were made:

    8.1. George has a total population of approximately 231 575 (2021) with average annual growth of 1.66% over the last 5 years. 53.6% of the population are of working age (25-64 years), while 36.7% of the population are regarded as economically active, this figure has declined by 7.8% since 2017.

    8.2. Annual per capita income amounted to R98 795 in 2021, the fourth highest in the Garden Route District. Approximately 19.6% of all households have an annual income of less than R54 000 and, in theory, should qualify for free basic services.

    8.3. The local economic output (GVA) amounted to R22.68 billion in 2021, constituting 34.08% of the Garden Route District GVA. George's 5-year economic movement has been stagnant, with a 5-year average GVA growth rate of just 0.4%. This is particularly sluggish when compared to the 5-year average population growth rate mentioned above. This is reflected in a reduced GVA per capita in 2021 of R73 425.53 as compared to R77 868.42 in 2017.

    8.4. The local economy is underpinned by the Financial, Community Services and Trade Sectors, which together comprised 66.7% of total GVA in 2021. These three sectors are the predominant providers of employment in GLM, with a combined total of 35 403 jobs in 2021. The total number of formally employed people declined by 6 535 jobs in 2021.

    8.5. The Official Unemployment Rate saw an increase of 7.2% in 2021, to a total of 25.0%. This increasing trend has been in place since 2018 and is of concern. This remains below the Garden Route District figure of 26.0% and slightly above the Western Cape

Provincial rate of 24.8%. It must be noted that the Official Unemployment Rate employs a narrow definition which excludes discouraged workers and those not actively searching for work, thus in actuality this rate is considerably higher.

8.6. Total tourism spend saw a significant increase in 2021, to a total of R2.41 billion, despite the total number of trips declining for the second consecutive year. The tourism sector plays a significant role in the local economy, the total GVA contribution of 9.67% in 2021 reflects this.

8.7. The municipality's service delivery improved significantly during the review period, with reduced backlogs in the provision of all infrastructure services.

8.8. The municipality has maintained a healthy liquidity position during the review period, exceeding the NT recommended norm of 1.5:1 throughout the entirety of the review period. The 8-year average liquidity ratio of 2.08:1 (2.06:1 as at FYE2022) is indicative of sound financial management and provides a healthy buffer in the event of unforeseen financial shocks.

8.9. The municipality has successfully deleveraged its debt profile throughout the review period, reducing its gearing ratio from 35% to just 10% over the 8-year period. The affordability of the current debt profile provides scope to accelerate the external borrowing programme. The municipality has budgeted to utilise this scope.

8.10. The collection rate was 95% as at FYE2022, maintaining the 8-year average of the same figure. Debtor days came to 41 days at year-end, marginally exceeding the NT norm of 30 days. Creditor payment days totalled 40 days at year-end, slightly exceeding the NT norm of 30 days, however, this is deemed acceptable.

8.11. George LM managed to generate cash from its operations throughout the review period, at an average of R185.8 million p.a. (R408.6 million in FY2021/22) This is reflective of the efficacy of collection procedures.

8.12. Unencumbered cash and cash equivalents fully covered the minimum liquidity requirements all the eight years under review, with a cash surplus of R250.6 million as at FYE2021/22. This is despite significant use of own cash to fund capital investment (average of R92.0 million p.a.), highlighting the high levels of cash generation throughout the review period.

8.13. Financial performance was generally acceptable throughout the review period. However, upon the exclusion of capital grants, operating deficits were realised in six of the eight years under review.

8.14. As the main income contributor, contributing an average of 35% p.a. of revenue, electricity services had an average surplus margin of 31% for the review period. There

has been a declining trend noted since FY2017/18, highlighted by a 9% reduction of the surplus margin to 25% in FY2021/22.

8.15. Expenditure on repairs and maintenance as a percentage of property plant and equipment averaged 4% over the review period. This is well below the NT benchmark of 8%.

8.16. Heavy reliance has been placed on capital grants and own cash to fund capital expenditure, with no external financing undertaken since FY2019/20. Notwithstanding the historically strong cash generation, excessive use of cash reserves to fund capital expenditure is financially unsustainable. The cumulative capital expenditure amounted to R1.91 billion for the 8-years under review.

8.17. George LM underspent on its capital budget throughout the same period, with actual capital expenditure as a percentage of budgeted capital expenditure being consistently below the NT norm range of 95% to 100%.

Conclusions drawn from Financial Model

A long-term financial model was developed, based on the FY2021/22 Audited AFS of the municipality and populated with several assumed variables. A summary of the outcome of the Base Case of the model is presented in **TABLE 1** below.

TABLE 1: SUMMARIZED BASE CASE FINANCIAL OUTCOMES

Outcome	10-Years up to 2032
Average annual % increase in Revenue	7,5%
Average annual % increase in Expenditure	7,8%
Accounting Surplus accumulated during Planning Period (Rm)	R 3 242
`Operating Surplus accumulated during Planning Period (Rm)	R 151
Cash generated by Operations during Planning Period (Rm)	R 3 234
Average annual increase in Gross Consumer Debtors	11,2%
Capital investment programme during Planning Period (Rm)	R 5 861
External Loan Financing during Planning Period (Rm)	R 1 952
Cash and Cash Equivalents at the end of the Planning Period (Rm)	R 1 611

9. In the ***Base Case Scenario,*** the municipality will, over the 10-year planning period from FY2022/23 to FY2031/32 realise an Accumulated Operating surplus of R 151 million, generate Cash from Operations of R 3 234 million and can afford a Capital Investment Programme of R 5 861 million.

Recommendations

10. Chapter 12 of the main report details a comprehensive list of recommendations. These recommendations are based on the historic independent financial assessment and long-term financial model. In summary, a financial plan is recommended with the following focus areas:

    10.1. Maintenance of the historically strong collection rate and liquidity position, through analysis of the efficacy of collection procedures ensuring shortcomings are addressed as they arise.

    10.2. Fostering an optimized capital funding mix that provides a balance between external financing and own cash to supplement capital grants.

    10.3. Ensuring that all applicable consumers are billed, at the correct amounts and that this revenue is collected.

    10.4. Maximising available revenue streams and safeguarding of service charges surplus margins.

    10.5. Develop a cost-reflective tariff model and ensure that the full costs of providing all services are shared by as many households as possible.

    10.6. Develop clear policies for the implementation of the capital budget, ensuring projects that promote economic growth are prioritized.

    10.7. Maintain low distribution losses for water and electricity services, through the safeguarding of infrastructure, employing a proactive approach to maintenance and policing of illegal acts that contribute to these losses.

    10.8. Ensure stringent management of operating expenditure, with a particular focus on expenditure that is efficient, prioritized, and targeted.

1. INTRODUCTION

1.1. This report is the outcome of an assignment undertaken by INCA Portfolio Managers ("IPM") pursuant to an appointment by the municipality, to develop a Long-Term Financial Plan ("LTFP") of George Local Municipality (George LM) for a period of 10 years from 1 July 2023 to 30 June 2032, based on a Long Term Financial Model ("LTFM").

1.2. In this assignment, a historic financial assessment of the municipality with the financial information up to 30 June 2022 has been included.

1.3. The recommendations provided later in this report reflect the outcomes of the analysis and aim to enhance the long-term financial sustainability of George LM.

1.4. The following sources of information have been scrutinised and taken into consideration in the Independent Financial Analysis (IFA) and the development of this LTFP:

a. The audited financial statements for the years ending 30 June 2015 to 30 June 2022
b. George LM Adjusted Budget Report: FY2022/23-FY2024/25.
c. The Medium-Term Revenue & Expenditure Framework FY2022/23 – FY2024/2025.
d. Various other documents of the municipality that are publicly available.
e. Economic, demographic and household infrastructure data extracted from IHS Global Insight's Regional Explorer.

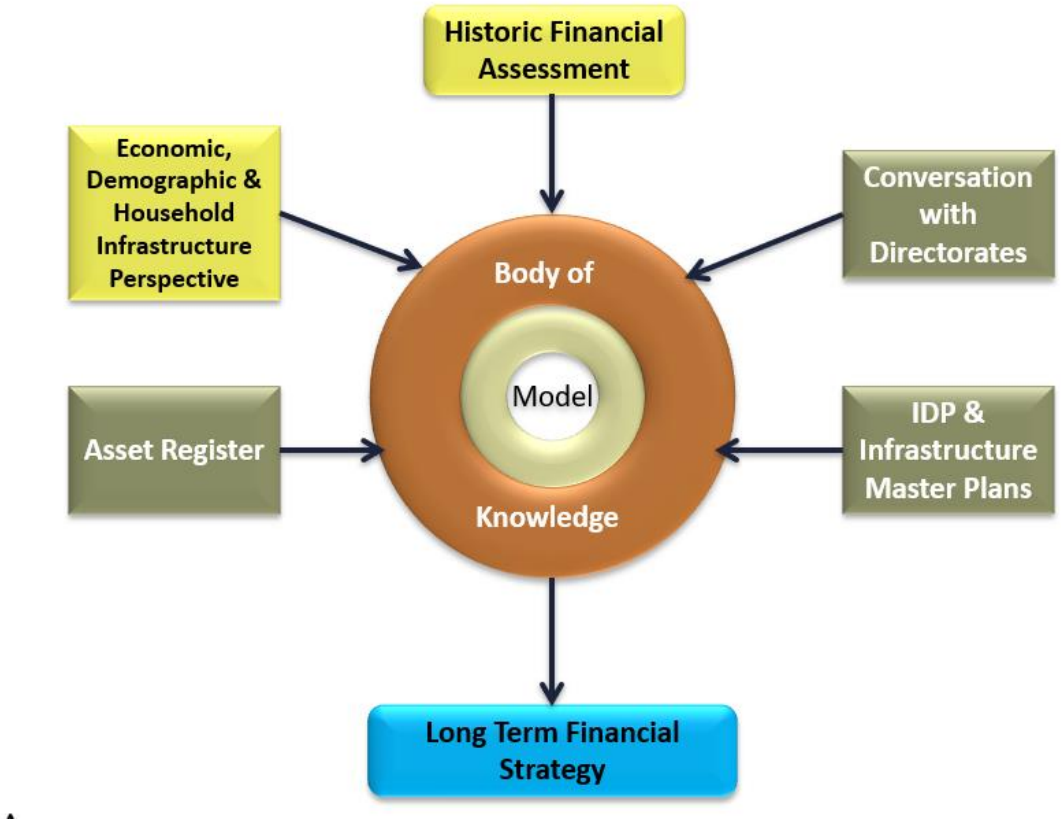
2. OBJECTIVES OF THE LONG-TERM FINANCIAL PLAN

2.1. The purpose of a long-term financial plan is to recommend strategies and policies that will maximise the probability of the municipality's financial sustainability into the future. This is achieved by forecasting future cash flows and affordable capital expenditure based on the municipality's historic performance, future plans and the environment in which it operates.

2.2. The plan provides guidelines, within the context of an uncertain future, of what the municipality can afford.

2.3. The generic process (adapted for each municipality pending availability of data) that was followed in reaching the objective of the Long-Term Financial Plan, is illustrated in the diagram below:

FIGURE 1: PLANNING PROCESS



3. PERSPECTIVE

An assessment of the George LM historic financial performance for the period 2015 to 2022 is presented in more detail in Annexure 1: *George Local Municipality: Independent Financial Assessment against the Background of the Municipality's Demographic, Economic & Household Infrastructure Situation, January 2023.* The GLM is characterized by the following socio-economic and financial indicators:

- ***The total Population*** of 231 575 (iHS 2021), represents 34.0% of people living in the Garden Route District. 5-year average population growth is 1.66%. Approximately 53.6% of the population falls in the working age group of 25 – 64 years with 36.7% of the population being regarded as economically active.
- ***Annual per capita income*** of R 98 795 is low in the district (R 99 133) and provincial (R 100 054) contexts. Approximately 19.6% of all households have an income of less than R 54 000 p.a. and are theoretically considered indigent.
- The Trade, Finance and Community Services are the main drivers of the local economy and contributes approximately 66.7% to the **Gross Value Add** (GVA).
- ***Unemployment Rate*** of 25.0% exceeds the Provincial unemployment rate of 24.8% but is less than the National rate of 33.6%. This is a narrow definition of the unemployment rate, in actuality it is much higher.
- Strong ***liquidity ratio*** of 2.06:1 as at FYE2021/22, which exceeds the NT benchmark range of 1.5:1 to 2:1.
- The ***collection ratio*** as at FYE2022 was 95%, this is in line with the NT benchmark of 95%.
- Analysis of financial performance reveal that on exclusion of capital grants, the municipality realised ***operating deficits*** in 6 of the 8 years under review, while ***cash was generated by operations*** in each year under review.
- ***Cash vs Minimum Liquidity Requirements:*** Unencumbered cash and cash equivalents fully covered the minimum liquidity requirements in each of the 8 years under review, with a cash surplus of R 250.6 million for FY2021/22.
- Overall, the financial indicators reflect a stable, healthy financial position, the municipality is currently in a financially sustainable situation.

3.1. An assessment of George Local Municipality's historic financial performance for the period 2015 to 2022 is presented in more detail in Annexure 1: *George Local Municipality: Independent Financial Assessment against the Background of the Municipality's Demographic, Economic & Household Infrastructure Situation, January 2023.* This is summarised below:

Spatial & Demographic Perspective

3.2. George's Total Population increased from 197 479 in 2012 to 231 575 in 2021.

3.3. 5-year average population growth rate of 1.66% is the third highest of the municipalities within the district and higher than the provincial (1.62%) and national (1.44%) rates.

3.4. 53.6% of the population falls in the working age group of 25 – 64 years with 36.7% of the population being regarded as economically active.

3.5. George's annual average household income of R 352 106 in 2021 is the third highest in the Garden Route District.

3.6. Approximately 19.6% of households in George earn an annual income of below R 54 000 p.a.

3.7. The unemployment rate which increased to 25.0% in 2021, from 17.8% in 2020, is high in the provincial (24.8%) context, but reasonably low in the national (33.6%) context. The increasing trend in unemployment is more pertinent, and of more concern, than the absolute level of unemployment in the municipal area.

Economic Perspective

3.8. George's local economic output, i.e., Gross Value Add (GVA) of R 22.64 billion (current prices) represents approximately 34.0% of the district economy and 2.9% of the provincial economy. GVA annual growth has been stagnant over the most recent five years, with an average rate of 0.4% p.a.

3.9. Concerningly, the 5-year average population growth rate of 1.66% p.a. exceeds the GVA growth rate over the same period.

3.10. The local economy is largely underpinned by the Trade, Finance and Community Services sectors which constitute a combined 66.7% of the GVA.

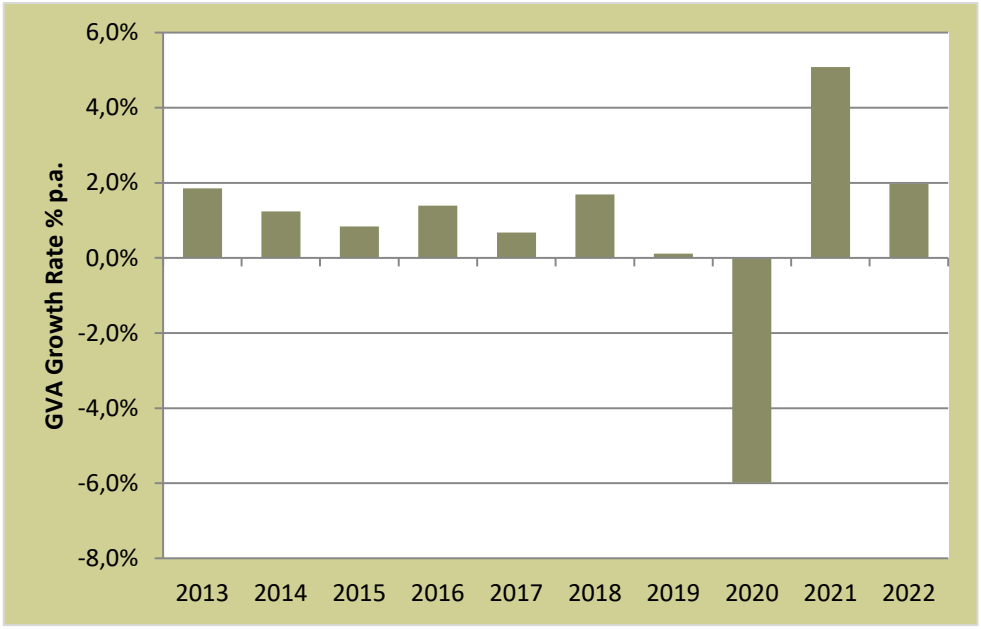
3.11. George LM had a Tress Index, a measure of the degree of economic diversification, of 49.25, indicative of a reasonably concentrated economy.

3.12. Tourism trips declined to 147 761 trips in 2021, with trips for leisure/holiday purposes seeing the biggest decline. Tourism spend saw a significant resurgence after the Covid-19 affected 2020 to a total of R2.41 billion in 2021, representing 9.67% of total GVA in 2021. While this is an increase from 7.17% in 2020, it represents just 52.03% of the pre-pandemic GVA contribution of 18.59% in 2019.

TABLE 2: SECTOR SHARE OF TOTAL GVA

Sub Sector	2012	2021
1 Agriculture	2,7%	3,2%
2 Mining	0,1%	0,1%
3 Manufacturing	15,4%	13,8%
4 Electricity	3,0%	2,4%
5 Construction	6,8%	5,1%
6 Trade	16,8%	15,7%
7 Transport	9,2%	8,8%
8 Finance	24,0%	27,1%
9 Community services	21,9%	23,9%

GRAPH 1: GEORGE: ANNUAL AVERAGE GVA GROWTH RATE % P.A.

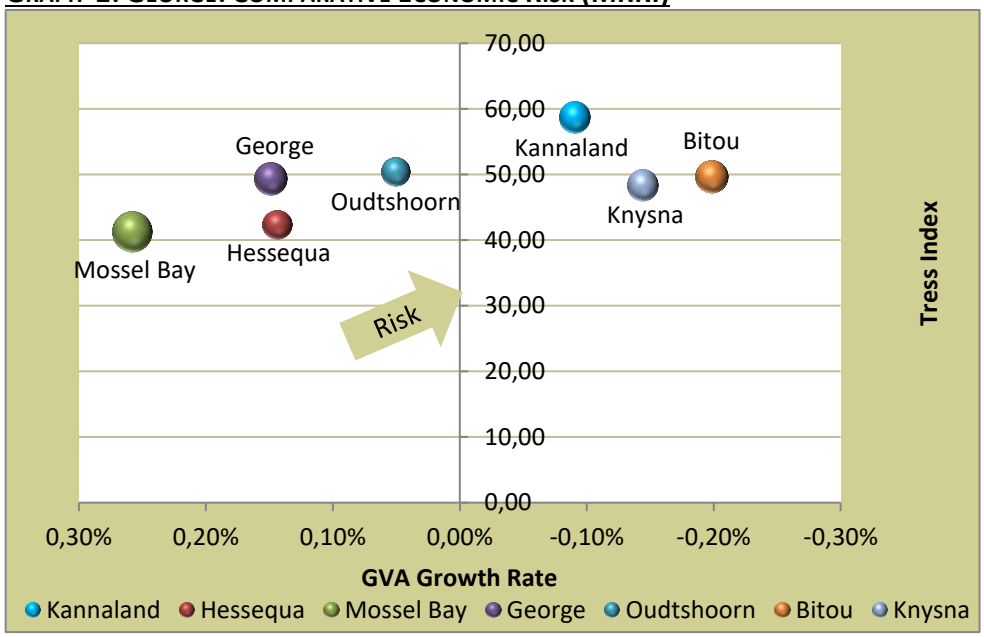


3.13. IPM has developed the Municipal Revenue Risk Indicator ("MRRI"), which measures the risk of a municipality to generate its own revenues. This risk is on the one hand a function of the economy (size of the economy as measured by the GVA per capita, GVA growth rate and Tress Index) and on the other a function of households' ability to pay (measured by the % of households with income below R 54 000 p.a., unemployment rate and Human Development Index).

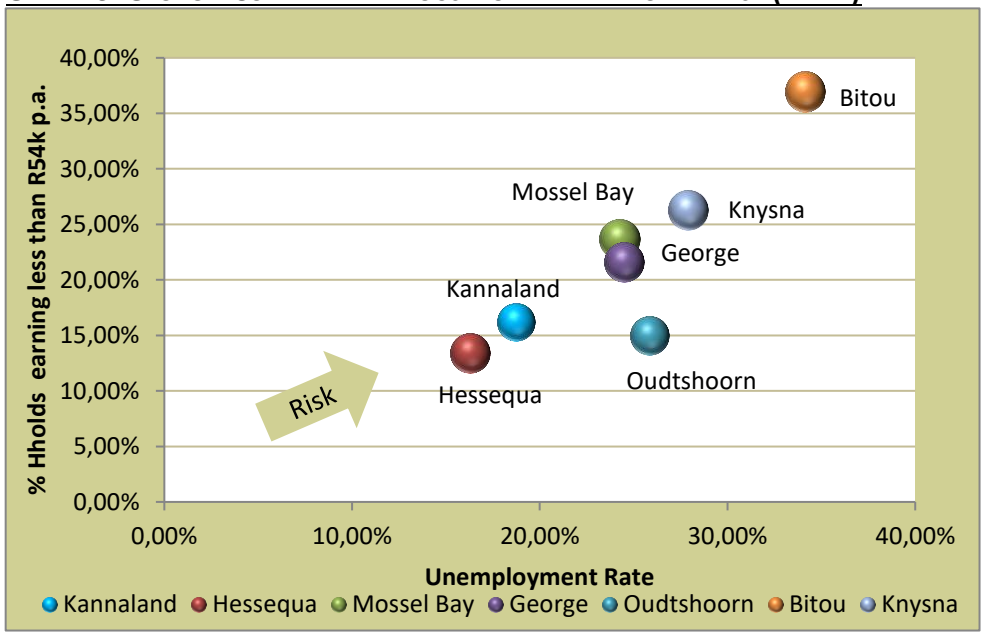
3.14. Sluggish economic growth and the ability of households to pay for services delivered by the municipality, rates George LM as a "High" risk on IPM's Municipal Revenue Risk Indicator scale. There is a high risk that the municipality will not be able to generate enough own revenue in future. Additionally, George's economy is not highly diversified, while unemployment is high. This indicates that the ability-to-pay risk is high.

The following graphs illustrate George's relative position in comparison to the other local municipalities in the Garden Route District.

GRAPH 2: GEORGE: COMPARATIVE ECONOMIC RISK (MRRI)



GRAPH 3: GEORGE: COMPARATIVE HOUSEHOLD ABILITY TO PAY RISK (MRRI)



Household Infrastructure Perspective

3.15. The level of service delivery as expressed by the Infrastructure Index for George LM increased from 0.86 in 2012 to 0.92 in 2021, higher than the district (0.91), provincial (0.90) and national (0.77) indices.

3.16. George LM outperformed the Garden Route District in the provision of all municipal infrastructure services. Additionally, George managed to reduce the level of backlogs in all services over the review period.

3.17. The rate of household formation in George between 2012 and 2021 was 18.5%, the second highest in the district. This equates to an increase of 10 159 households to a total of 64 976 households in 2021. The municipality must be commended for improving its Infrastructure Index over the review period, in light of a significant rate of household formation.

Financial Perspective

Financial Position

3.18. The liquidity ratio fluctuated between a peak of 2.25:1 as at FYE2020/21 and a low of 1.91:1 as at FYE2019/20. This has exceeded the NT norm of 1.5:1 throughout the review period.

3.19. The municipality realised substantial cash surpluses on the minimum liquidity requirements, with a surplus realised in each of the 8 years under review.

3.20. The collection ratio as at FYE2021/22 was 95%, which is on par with the minimum NT benchmark of 95%, whilst Net Debtor days stood at 41 days at year-end, slightly exceeding the NT benchmark of 30 days. Net Creditor days totalled 40 days at year-end, marginally more than the 30-day NT benchmark, but within an acceptable range.

Financial Performance

3.21. On exclusion of capital grants, the municipality realised operating deficits in 6 of the 8 years under review.

3.22. George managed to generate cash from its operations throughout the review period, with a peak of R408.6 million in FY2021/22.

3.23. GLM managed to maintain gross surplus margins on water and electricity services throughout the 8-year period. As the main income contributor, electricity services realised a gross surplus margin averaging 31% over the 8-year period, with a declining trend noted since FY2017/18. Water Services maintained an average gross surplus

margin of 100% over the same period, since the municipality makes use of its own water sources and no water was purchased by the municipality.

3.24. Staff costs as a percentage of total operating expenditure decreased over the review period, with an average contribution of 24% p.a. This figure remained below the NT norm range of between 25% and 40% for the entire review period.

3.25. Expenditure on repairs and maintenance as a percentage of property plant and equipment was 5% during FY2021/22, below the NT benchmark of 8%.

Cash Flow Statement

3.26. Cumulative Capital expenditure of R 1.91 billion over the 8-year period was primarily funded by capital grants (58%), followed by own cash (38%) and financing (4%).

3.27. George LM consistently underspent on its capital budget throughout the same period, with actual capital expenditure as a percentage of budgeted capital expenditure being on average 75%, well below the NT norm range of 95% and 100%.

Cash Forecast

3.28. The municipality has budgeted for an increasing trend in operating profitability, with a budgeted operating deficit of R 111.55 million in FY2022/23 to a surplus of R 23.58 million in FY2024/25. The budgeted operating deficit is driven by a significant reduction in budgeted electricity services income due to an adjustment to account for the energy crisis. Notwithstanding the general positive trend in operating profitability over the review period, the uncertainty regarding the energy crisis on the municipality's electricity services revenue, along with future tariff increase and other factors, the budgeted operating surpluses in the outer MTREF years may be difficult to achieve.

3.29. The MTREF current ratio is budgeted to decline from 2.06:1 in FY2021/22 to 1.31:1 in FY2024/25. This seems to be a reasonably negative outlook considering the historically healthy liquidity position.

3.30. Capital expenditure is budgeted to fluctuate between R 826.1 million and R 943.9 million, based on the FY2022/23 Adjusted Budget. The increase in the budgeted capital investment programme is driven by the receipt of the BFI grant. The budgeted funding mix includes significantly increased levels of borrowing, which allows for reduced usage of own cash to supplement capital grant funding. In light of the affordability of the current debt profile, this is considered an optimal funding mix. The accelerated budgeted capital expenditure programme is feasible and can be achieved without jeopardising the current state of financial sustainability.

4. KEY FOCUS AREAS

The recency and relevance of the previous discussions held during the preparation of the previous LTFP in 2021 deemed fresh discussions not necessary at this stage. Due to travel restrictions to limit the potential spread of the COVID-19 virus, IPM could not meet with the municipality in person. A series of virtual meetings on 11 and 18 August 2021 were however held.

This section highlights key issues raised during the meetings with the George LM directorates. It does not necessarily capture all of the matters raised but focuses on matters which will potentially impact (positively or negatively) on the long-term financial position of the George. The discussions with all Directorates are a key part of the LTFP process and do not only contribute to the body of knowledge but ensures that the desktop analysis and the realities on the ground align.

This section is organised as follows:

- Rapid Expansion and development
- Asset Management and prioritisation process
- Infrastructure and technical services
- Organisational and institutional
- Other matters

4.1 Rapid Expansion and Development

George is a well-run municipality, providing high levels of service to its citizens, with a relatively stable political environment. The town is perceived to be safe, with a high quality of life for families residing within its boundaries. The George Airport is a strategic asset to the town, providing easy access to other economic centres across South Africa. The COVID-19 pandemic brought about change in the working environment and working-from-home has become a norm in many households. This enables families to live in their area of preference, while still being able to work for an employer in another part of the country. These factors all contributed to growth in George, both in terms of population and economy. With the perception of growth, the area now also attracts a significant number of low-income households and people of working age looking for employment opportunities. The municipality has previously been regarded as a destination for retirees to settle, which hasn't necessarily changed.

As a result of this migration of people to George, for various reasons, the municipality currently faces a rising demand in residential properties and an increased need for municipal services. The need for affordable housing (Subsidised housing, Gap housing and FLISP (Finance-linked Individual Subsidy Programme) housing) in the area is expressed by an approximate 17 000 housing backlog. The combined effect of the influx of people and the lack of housing is evidenced in the rapid increase of informal settlements, with increased levels of illegal land occupation, land invasions and land grabs.

4.2 Asset Management and Prioritisation process

The rapid expansion and expected growth of George increases pressure on the municipality to deliver services to a constantly expanding population and consumer base. Currently the lack of bulk infrastructure is inhibiting growth in the municipal area. Of concern is that the growth is mainly centred around households, represented by a high number of indigent households, who will not necessarily contribute to the municipality's income base. It is therefore critical that infrastructure investment is accelerated into productive economic assets that will generate future income to the municipality, which will provide the necessary services to attract investment into the area and stimulate economic growth that provide valuable job opportunities to the growing population.

In this regard, the significant need for capital infrastructure far outweighs the financial capacity of the municipality and budget allocations currently made to the respective directorates. From discussions it appears that master plans are sometimes lacking in that it is either outdated or not aligned to the financial realities of the municipality. There was also an expression of a need for integrated planning within the municipality and a structured investment prioritisation process. Asset management linked to repairs and maintenance are often done on an ad-hoc or reactive basis as opposed to having fully funded proactive maintenance schedules. Our understanding is that project management is performed manually and there is no formal system-driven project reporting in place. The feeling is that George may benefit from a fully integrated system that includes capital prioritisation, project management, asset management and service delivery.

Investment Properties: A need was expressed of identifying "economic" municipal/investment properties. There are concerns that some investment properties are not utilised to its full economic benefit and that current property policies are slanted towards making land available towards social infrastructure. The competitive tender process towards investment properties is complex and often inhibits economic growth. The municipality is in need of a formal investment property policy and a leasing policy (currently being developed) to reduce unnecessary uncertainties and red-tape which will stimulate economic growth – this will also provide additional revenue to George. During a recent land audit concerns were raised about the completeness of the investment property register.

Household bills and cost-reflective tariffs: The municipality's strong financial position is supported by, in addition to sound financial planning and practices, on sustained high levels (above 97%) of revenue collection from a stable ratepayer base willing and able to pay for services. Indications are, however, that (in the absence of economic growth, exacerbated by the Covid-19 pandemic and more recent energy crisis) households are under increasing financial pressure to service their municipal bills. In light of high bulk electricity tariff increase in recent years (passed on to consumers to the extent possible) and the pressure households are experiencing, other service tariff increases have remained low to moderate. This resulted in a less that optimal tariff structure with higher reliance on electricity services income which potentially cross subsidise other services. The municipality has recently embarked on cost-of-supply studies in order to implement cost-reflecive tariffs. There were concerns raised about the level of service provided compared to the tariffs charged. It is imperative that the level of service costed are aligned to the service provided. Higher level of service than costed can potentially result in gross deficits.

4.3 Infrastructure and Technical Services

Bulk Infrastructure: The bulk water structures are affected by the addition of new houses. Recent and expected short-term growth in number of households in George emphasises the need to integrated master plans and human settlement plans. Priorities are driven by growth and development and are changed often. Acknowledging the urgent need for bulk water infrastructure and the limited resources available, it is imperative that realistic and funded integrated master plans are developed to address backlogs and support service delivery initiatives to a rapid growing number of consumers.

Waste Management: George LM collects domestic waste from more than 39 000 households, which is disposed at the PetroSA landfill site and Uniondale landfill site. A dumping fee of approximately R400 000 to R600 000 is paid to Petro SA per month. The municipality also uses its own vehicles for this purpose.

Investment in a compost facility is deemed an appropriate response to the challenge of accommodating garden refuse, while having the ability to save on dumping fees. The new compost facility is under development, but funding remains a big constraint. Our understanding was that approximately R20 million is required to complete this compost facility, while the budget is currently limited to R4 million. It is estimated by the technical department that the completion of the compost facility will result in a cost saving of approximately R200 000 per month of the fee paid to PetroSA. Management also expressed the need for an alternative piece of land for crushing of waste material.

The views were expressed that “waste is costly” and that the municipality should consider time and cost savings by limiting bin bags to 4 per household and separating garden refuse.
The solutions proposed should be explored and assessed. Since George has an Integrated Waste Management Plan in place, an aligned cost benefit analysis to determine the true cost of dumping and potential savings will be beneficial. In addition, the municipality will also benefit from optimised waste recycling approaches, interventions, and strategies to reduce total load on the landfill sites.

Town planning and transport: Go George bus services is focused on its contribution to address spatial challenges of the past, by allowing people, through public transport, access to work opportunities. Revenues from this service are expected to increase with the roll overs into the next phases, however, the municipality agrees in principle that public transport/bus services are not profitable and the financially sustainability of the GIPTN relies on a 12-year agreement with Provincial Government for the funding thereof. Our understanding is that Provincial Government is annually expecting a higher financial contribution from George in rolling out the next phases, which is currently not financially sustainable for the municipality. There is only approximately half of the contract period left and George needs to find solutions urgently as to how the GIPTN will be funded in future or how this service will be delivered in a financially sustainable manner after contract expiration.

4.4 Organisational and institutional

Resource constraints/staff productivity: Most directorates cited limited staff and/or limited financial resources as the main impediment to achieving its objectives. Recruitment policies have, in the past, made it difficult to acquire and retain specialised skills which often led to outsourcing. There is a need to fill critical posts within the municipality. While the municipality requires critical posts to be filled, the municipality needs to remain cognisant of the financial realities it faces. Staff productivity and the rationalisation of non-critical posts therefore need to be considered. IPM supports the view that efficiencies can be gained through the effective use of electronic systems and automation, while the current process of optimisation of municipal systems, the organogram and the effective management of consulting services should be followed through.

To address the limited financial resources concerns, management is advised to consider this long-term financial plan, its outcomes and recommendations to improve George's financial sustainability and increase its access to funding. Management is further encouraged to explore different financing opportunities (such as the utilisation of public-private partnerships, corporate social investments and international funding opportunities).

Performance Management: There is a view that performance management has deteriorated over the years, but we were made aware that GLM is undertaking the rolling out of performance management to include lower staff levels, within a year. The second phase is to develop score cards for managers. This process should be completed to support productivity within the municipality.

Overtime and shift system: Management estimates overtime to account for approximately R25 million to R34 million per annum, which is considered high. Service departments have indicated that they do not have enough staff to maintain the current standard of service delivery into the future and has cited this as one of the main reasons for the high overtime expenses. The suggestion of shift systems has been met with hesitancy due to the lack and shortage of staff to meet current demands and the inability to allocate staff to a number of shifts.

While this may be true for some directorates, it may not be true for all. The reduction of overtime expenses should be considered a priority and the necessary controls need to be put in place to effectively manage overtime and, should the shift system not be a viable solution, find alternative solutions to this challenge.

4.5 Other matters

Non-core functions and shared services: An assessment needs to be made of how the district development model being implemented by the National Government can be best utilised for unfunded mandates, non-core services and other services that can be managed more cost effectively through a shared services approach.

Backyard dwelling: From the discussions it was not clear whether George is facing challenges with regards to backyard dwelling. In our experience backyard dwelling is an urbanisation phenomenon generally experienced by municipalities with universities and/or with a relatively high population growth rate and where there is a perception of job opportunities. Although George is not home to a recognised university, it is a location attracting job seekers

and an economically active population in line with the urbanisation trend, resulting in higher-than-average population growth.

Since the municipality is not clear as to the extent of this challenge and the potential loss in revenue or increased expenditure as a result, it would be prudent to assess and quantify the financial impact. Formalisation of household dwelling and direct connections to the bulk infrastructure would be an opportunity to maximise municipal revenue, although concerns were noted with regards to the capacity of infrastructure and the ability to connect more households to an already constraint and ageing infrastructure network.

Criminality, including illegal dumping, vandalism and theft, clogging of sewer systems and land invasion: A general trend and rising concerns around criminality and illegalities were noted. Although this can be expected in light of the difficult economic environment, rising unemployment and increased levels of population growth, the cost incurred by the municipality in mitigating these risks and/or responding to these matters are enormous. Examples of these incidents include illegal dumping of waste, clogging of sewer systems, vandalism and theft of municipal property and illegal land invasion.

Suggested solutions to address these issues include the distribution of additional bins at an estimated cost of R8 million to R10 million, introduction of CCTV cameras, promotion of educational awareness by the municipal officials and ward councillors, establishment of additional waste transfer sites within informal settlements, stricter enforcement of municipal bylaws and protection of communities. Although there is no easy solution to these matters, the municipality is encouraged to develop an integrated approach in dealing with these issues.

Developmental procurement: In order to develop and grow the local economy a suggestion was made that preference be given in the supply chain processes to big local (George-based) contractors who are able to deliver the services at the expected quality required by the municipality. There must still be provisions for strict regulations in place to ensure that these local contractors adhere to local labour and enterprise commitments. This way the municipality will still receive the required services at the expected quality, but by making use of local contractors the local economy and residents of the municipality will benefit from these contracts.

Post Covid-19 environment: The lockdowns associated with Covid-19 have significantly altered the way municipal business is conducted. There is also an elevated degree of occupational health and safety considerations for staff while working remotely. Notwithstanding the many challenges the pandemic has brought about, the municipality has also observed a certain level of independence of staff. In certain instances, there were significant costs savings realised, for example digital access to documents which reduced printing costs of agendas and other documents. The municipality has also responded in innovative ways to the challenges for example the introduction of an application through which complaints and service delivery can be actioned to devices of employees.

In a Post-Covid-19 environment there is an expectation of improved service delivery and increased productivity, but the positive changes in the last year or two and cost efficiencies gained need to be retained and maximised.

The severe economic impact of Covid-19 felt by George LM, was reflected in a GVA contraction of 5.9% in 2020. There was expected to be a significant economic recovery thereafter, and this

has been somewhat reflected in GVA growth of 5.1% in 2021. However, the recent impact of the ongoing energy crisis and consequent loadshedding, as well as sluggish economic growth driven by factors such as high and rising inflation, exorbitant fuel prices and generally poor economic sentiment, has hampered further economic recovery.

Tourism plays an integral role in George's economy. While the impact of Covid-19 and associated lockdowns on the tourism sector may be dwindling, there are new complications created by the energy crisis and aforementioned economic challenges, that are also impacting the recovery of the tourism sector.

The Manufacturing sector's contribution to the economy is not insignificant, and the energy crisis and lack of energy supply is having a major impact on manufacturing. Loadshedding mitigation costs such as the installation of solar panels, procurement of generators and diesel to run them etc., are severely threatening the bottom line of many companies in this industry. The knock-on effect of this on George's economy is significant.

The current economic climate is a challenging one, and the uncertainty around the duration of these challenges makes planning a difficult exercise. The municipality must continue to factor in all of these challenges into their planning and budgeting processes going forward. The utilisation of the long-term financial model that factors in these challenges, will provide significant assistance in ensuring the long-term sustainability of the municipality.

5. DEMAND FOR FUTURE CAPITAL EXPENDITURE

5.1. The replacement cost at a future replacement date for assets in the asset register was determined. “Replacement” could also imply rehabilitation, enhancement (upgrade) or renewal (refurbishment) of that asset but excludes routine repairs and maintenance.

5.2. The calculation is done mechanistically and does not cater for engineering judgement. The information gained from the municipality’s asset register and the correctness thereof will impact on the accuracy of future replacement- costs and dates. The asset register provided by the municipality included many assets lacking essential data to enable an accurate projection of future replacement cost. For these assets, we had to make calculated assumptions of acquisition dates as well as remaining useful life. The model calculates the Replacement Cost (in nominal terms) of assets for the Planning Period, i.e., up to and including 2031/32. Some asset classes were not reviewed for replacement, viz. “Investment Property”, “Land” and “Heritage Assets”.

5.3. The outcome of this analysis and the Annual Replacement Cost (“ARC”) is presented in Annexure 4: Assets Earmarked for Replacement.

5.4. According to a mechanistic calculation, the nominal replacement cost for the period from 2022/23 (and replacement not done before) to 2031/32 amounts to R 12 869 million. Of this amount an amount of R 1 793 million or 14% consist of assets that should already have been replaced in the past, based on their remaining useful life. The replacement of assets in the Roads Infrastructure category amounts to 26%, followed by Water infrastructure with 20% and Electricity with 19% each. The estimated current replacement cost (“CRC”) of only those assets that were assessed, amounts to R 12 billion compared to the carrying value of PPE assets of approximately R 3.3 billion recorded in the municipality’s annual financial statement for the period ending 30 June 2022.

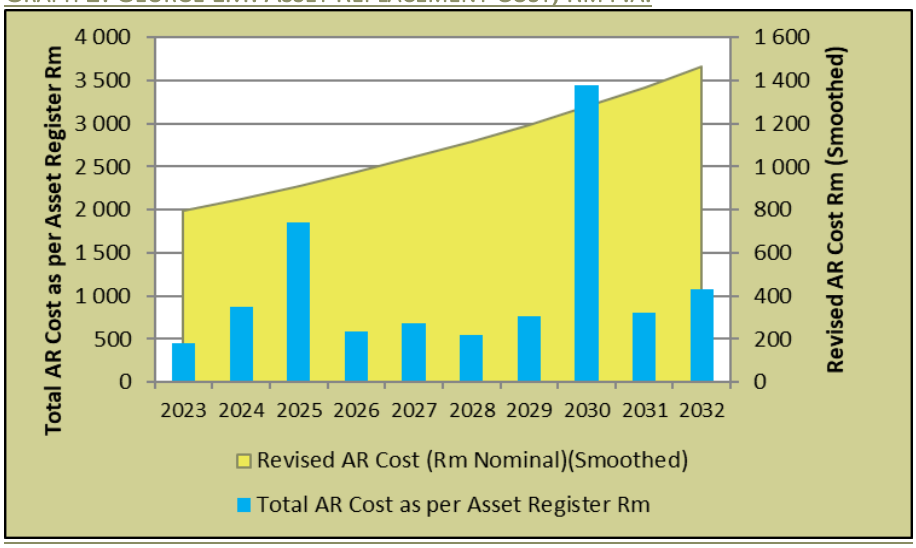
5.5. We have amended the estimated replacement costs. This was achieved by:

- Assuming that the actual remaining life of some assets will exceed the life recorded in the asset register
- Assuming that only a percentage of assets will be replaced when their estimated useful life expires (e.g. in the case of buildings, it is doubtful whether the whole structure will have to be replaced, possibly only certain fittings, roof, finishes, etc.)
- Spreading replacement not done in the past over several future years, and
- Smoothing the constant 2022 value over the Planning Period and reverting these back to nominal values

5.6. Following the above procedure resulted in the total asset replacement cost, for the period 2022/23 to 2031/32 reducing from the original R 12 869 million to R 11 000 million.

5.7. The graph below compares the Replacement Cost as determined from the asset register and the smoothed Replacement cost after adjustment as described above:

GRAPH 2: GEORGE LM: ASSET REPLACEMENT COST, RM P.A.



5.8. The high amounts estimated for 2025 and 2030 are due to an extent, but not exclusively, to the replacement of:

2025
Various civil engineering infrastructure assets
Floodlights Outeniqua Park
George 66 kV Overhead Line - Hare (Wood Pole)
Landfill Site - George

2030
Various asset classes
Heather Park Substation Small Building 01
Glenwood Substation Circuit Breaker02 Transformer2
George Substation Yard Stone
Tamsui Substation Small Building 01

It is worthwhile to assess the condition of the assets as accurately as possible and apply engineering judgment to determine when the asset components need to be replaced.

5.9. The smoothed Annual Replacement Cost ("ARC") curve ranges from R 796 million to R 1 566 million p.a. for the period 2022/23 to 2031/32. A future smoothed asset replacement programme of this nature would be advisable to avoid the spikes as illustrated above. The quantum may however not be affordable considering that the investment in PPE of the municipality in 2021/22 was only R 446 million, which included investment in new as well as replacement assets.

5.10. In addition to asset replacement the municipality has the need to create new capital assets. However, in the light of the need for asset replacement this should not be neglected, and we propose that the municipality identify priority projects and implement a smooth asset replacement budget for future years.

5.11. In the light of the large demand for the replacement of assets that will be reaching the end of its useful life during the 10-year planning period, we propose that the municipality prioritises a cash backed Capital Replacement Reserve ("CRR") for this purpose. It would be prudent to transfer the full depreciation charge to the CRR once the cash balances are available. The CRR can then be used as a funding source for future capital expenditure. Furthermore, once the CRR has built up a significant balance the municipality should avoid depleting its CRR in any given financial year but use a percentage (say 50%) of the prior year balance for assets that require replacement. An asset replacement programme within the levels of available resources in the CRR will go a far way in quantifying the future replacement budget.

6. FINANCIAL MODEL

Future forecasts are based on the outcome of a financial model. Two basic scenarios are presented: First, the MTREF figures from the GLM Adjusted Budget FY2022/23-FY2024/25 were used unaltered. This scenario resulted in an unsustainable outcome, highlighted by sustained operating deficits, a negative bank balance, poor liquidity and cash shortfalls on budgeted capital expenditure. Various adjustments were made to achieve a more sustainable outcome that is reflected in the Base Case. The **Base Case** assumptions of the model are listed in the table below:

ASSUMPTIONS OF BASE CASE VARIABLES

VARIABLE	BASE CASE AVERAGE FOR THE 10 –YEAR PLANNING PERIOD
RSA consumer inflation rate (CPI)	5,3%
Population Growth Rate	1,7%
GVA Growth Rate	2,8%
Short term investment rate (Margin above CPI)	0,0%
Electricity Price Elasticity of Demand	-0,4
Water Price Elasticity of Demand	-0,2
Employee related cost escalation	7,7%
Bulk electricity cost escalation	8,9%
Collection Rate of customer billings	95,2%

The **Base Case** outcomes of the financial model is summarised below:

BASE CASE OUTCOME

Outcome	10-Years up to 2032
Average annual % increase in Revenue	7,5%
Average annual % increase in Expenditure	7,8%
Accounting Surplus accumulated during Planning Period (Rm)	R 3 242
Operating Surplus accumulated during Planning Period (Rm)	R 151
Cash generated by Operations during Planning Period (Rm)	R 3 234
Average annual increase in Gross Consumer Debtors	11,2%
Capital investment programme during Planning Period (Rm)	R 5 861
External Loan Financing during Planning Period (Rm)	R 1 952
Cash and Cash Equivalents at the end of the Planning Period (Rm)	R 1 611
No of Months Cash Cover at the end of the Planning Period (Rm)	4,6
Liquidity Ratio at the end of the Planning Period	2.1 : 1
Gearing at the end of the Planning Period	14,8%
Debt Service to Total Expense Ratio at the end of the Planning Period	6,3%

1.1. The proposals in this financial plan are based on the assumptions in the Base Case Financial Model. We are cognisant of the fact that future cash flows may be influenced by a variety of variables which limits the accuracy with which forecasts can be made.

1.2. The model framework is illustrated in the diagram below:

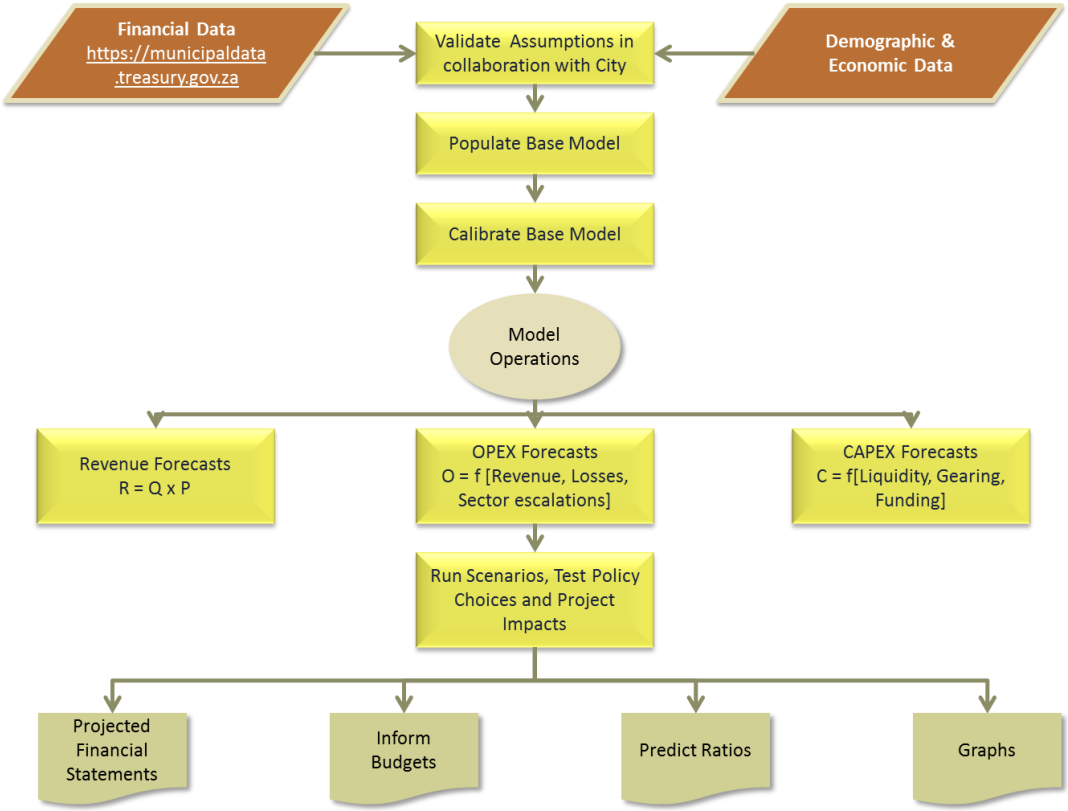


FIGURE 3: LTFM FRAMEWORK

1.3. The output of the Base Case Model, particularly the graphs and tables are used throughout this report. The Projected Financial Statements are presented in Annexure 2, which may also serve as a guide to inform future budgets of the municipality. The Financial ratios are presented in Annexure 3 and summarised in **TABLE 6** below.

1.4. The model forecasts the future revenue and expenditure by applying several independent variables. As an example, the future water services charges will in addition to the tariff charged be affected by future consumption as well as the addition of new users. Generic growth pursuant to the growth in population, households or economic output will be forecast.

1.5. To estimate the future revenue and expenditure, certain assumptions need to be made. These assumptions will serve as input to the model. For example, an assumption of future collection rates (payment ratios) is required to convert billings to actual cash receipts.

The average values for the 10-year planning period of those variables that were also changed for scenario testing are indicated in **TABLE 3** below:

TABLE 3: ASSUMPTIONS OF BASE CASE VARIABLES

VARIABLE	BASE CASE AVERAGE FOR THE 10-YEAR PLANNING PERIOD
RSA consumer inflation rate (CPI)	5,3%
Population Growth Rate (% p.a.)	1,7%
GVA Growth Rate (% p.a.)	2,8%
Short term investment rate (Margin above CPI)	0,0%
Electricity Price Elasticity of Demand	-0,4
Water Price Elasticity of Demand	-0,2
Employee related cost escalation (p.a.)	7,7%
Bulk electricity cost escalation	8,9%
Collection Rate of customer billings	95.2%

1.6. The average economic growth rate, as measured by the percentage GVA p.a. is currently 2.80%. Positive to note is that the forecasted GVA growth rate exceeds the forecasted population growth rate. Employee related expenses are expected to be higher than CPI and increase by 7.7% p.a. The collection rate of customer billings is assumed to remain at approximately 95% throughout the planning period. The model allows for the decline of water consumption pursuant to price increases by applying a Price Elasticity of Demand ratio, estimated to be -0.2.

1.7. The historic financial assessment revealed the stability of George's liquidity position and cash generation, largely driven by a historically stable collection rate. There has been a history of operating deficits, with a less than optimal funding mix that was too reliant on grant funding and own cash. Under-implementation of the capital budget also plagued the municipality. The objective of the assumptions in the model was to incorporate realistic assumptions to ensure future financial sustainability. The following factors represent the most important assumptions that were made in this regard. These assumptions will also have to be incorporated in the formulation of the municipality's long-term financial plan:

1.7.1. The collection rate is assumed to remain at 95% throughout the entirety of the planning period.

1.7.2. The Base Case Model incorporated all the increases in both expenditure and revenue items as announced by the GLM in the Adjusted Budget Report.

1.7.3. Importantly, the Base Case Model incorporates a scenario in which the extent of the impact of the energy crisis and consequent Loadshedding on municipal revenues is modeled. This scenario assumes an average of Stage 4 Loadshedding for FY2023/24, which is expected to result in an annual reduction of 22.6% of electricity consumption. Additionally, a permanent

reduction of 5% of electricity sales was included to account for consumers moving to alternative power sources. Lastly, a reduction of 5% of water sales was included to model the impact of Loadshedding on the water supply.

1.7.4. The NERSA tariff increases of 18.65% and 12.74% were incorporated into both the MTREF Case and Base Case, however the electricity tariffs that are passed onto the consumer were increased to 15.7% in FY2024 and 9.7% in FY2025, in only the **Base Case.**

1.7.5. The MTREF capital funding mix was altered to incorporate significantly increased borrowing over the MTREF period. Specifically, FY2022/23 R312.1 million, FY2023/24 R365.0 million and FY2024/25 R445.0 million. The borrowing for FY2025/26 was reduced to R105.0 million to maintain the affordability and sustainability of the forecasted debt profile. The borrowing in the Base Case consists of 10-year amortising loans at a rate of 4% above CPI per annum. Assumed growth beyond the MTREF period is 4% per annum. The idea behind the increased borrowing is to make use of the affordability provided by the currently under-leveraged debt profile as well as to protect the municipality's cash position.

1.7.6. The Capital Budget included in the Adjusted Budget was not amended over the MTREF period, while the FY2025/26 forecasted capital expenditure was reduced to R400 million. This is assumed to grow at 6% annually beyond the MTREF period.

1.8. These adjustments result in a sustainable case which is referred to as the ***Base Case*** in this report. It must be emphasized that the achievement of this sustainable base case will require a long-term commitment to the parameters of the LTFP, financial discipline and maintenance of strong revenue collection.

1.9. The impact of the Loadshedding Scenario is presented in **TABLE 4** below. The impact of the 22.6% annual reduction in electricity consumption as a result of an average of Stage 4 Loadshedding for FY2023/24 is significant. This is evident in the substantial 23.65% decline in the Base Case forecast electricity revenue for FY2023/24. While the permanent reduction in electricity sales, as well as the forecast tariff increases have an impact, the considerably reduced impact reflected in the 8.38% and 10.42% differences in FY2024/25 & FY2025/26 respectively, highlight the severity of the potential impact of loadshedding on electricity services revenue.

TABLE 4: LOADSHEDDING IMPACT

Electricity Revenue	2023	2024	2025	2026
MTREF Case (Rm)	869 107	986 677	1 127 679	1 245 953
Base Case (Rm)	876 786	753 352	1 033 154	1 116 090
Difference (%)	**0,88%**	**-23,65%**	**-8,38%**	**-10,42%**

1.10. The outcomes of the Base Case are presented in **TABLE 5** below:

TABLE 5: BASE CASE FINANCIAL OUTCOMES

Outcome	10-Years up to 2032
Average annual % increase in Revenue	7,5%
Average annual % increase in Expenditure	7,8%
Accounting Surplus accumulated during Planning Period (Rm)	R 3 242
Operating Surplus accumulated during Planning Period (Rm)	R 151
Cash generated by Operations during Planning Period (Rm)	R 3 234
Average annual increase in Gross Consumer Debtors	11,2%
Capital investment programme during Planning Period (Rm)	R 5 861
External Loan Financing during Planning Period (Rm)	R 1 952
Cash and Cash Equivalents at the end of the Planning Period (Rm)	R 1 611
No of Months Cash Cover at the end of the Planning Period (Rm)	4,6
Liquidity Ratio at the end of the Planning Period	2.1 : 1
Gearing at the end of the Planning Period	14,8%
Debt Service to Total Expense Ratio at the end of the Planning Period	6,3%

1.11. The Base Case reflects Operating Deficits until FY2027/28, after which Operating Surpluses are forecast to be realised for the remainder of the planning period. Cash is forecast to be generated from operations throughout planning period, for a total of R3.23 billion with a forecast period-end (FYE2031/32) cash balance of R1.61 billion. The total capital investment programme is forecast to amount to R5.86 billion. This is primarily funded by capital grants (53%), external financing (33%) and finally own cash reserves (14%). The Base Case funding mix provides a stronger, more sustainable balance between funding sources, reducing reliance on own cash to fund capital investment.

1.12. The aforementioned increase in borrowing remains affordable, as indicated by the forecast period-end gearing and debt service to total expense ratios presented in **TABLE 5** above, that are within the recommended norms of 35% and 7% respectively.

1.13. The summarised projected financial statements for the Base Case are presented in Annexure 2: Base Case Summary Projected Financial Statements.

1.14. George has historically been heavily reliant on electricity services to generate revenue, with an 8-year average contribution of 35%. Loadshedding is expected to have a significant impact on electricity revenue in the short to medium-term and as such, the Long-Term Financial Model caters for this.

1.15. The liquidity ratio is expected to decrease over the MTREF period, after which it is forecast to increase to a healthy 2.1:1 ratio as at FYE2031/32. Improvements in these metrics can be achieved through the fostering of improvements in the municipality's financial performance and operational management. The year-end cash balance remains positive throughout the forecast period, with the minimum liquidity requirement of 1-month's operational expenditure met throughout the planning period. The minimum liquidity requirement of 2-month's Opex will be met in FY2025/26, with the planning period-end bank balance amounting to R1.61 billion. This paints a positive picture of the municipality's future liquidity position, with a healthy buffer provided for in the case of unforeseen financial shocks akin to the pandemic and energy crisis.

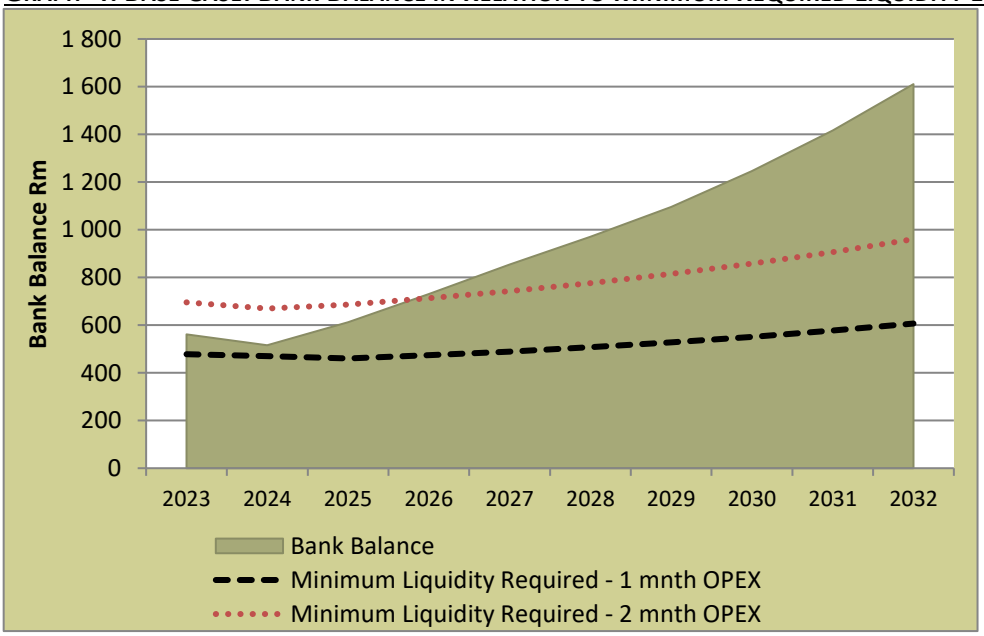
1.16. The affordability and sustainability of George's debt profile is evidenced by the planning period-end gearing and debt service to total expense ratios of 14.8% and 6.3%, respectively. The gearing ratio will remain below the recommended maximum ratio of 35% for George LM. The debt service to total expense ratio will marginally breach the maximum recommended ratio of 7% in FY2024/25 & FY2025/26, however, this will reduce back to an affordable level for the remainder of the planning period. When looked at with a long-term view, the debt profile provides comfort that the municipality will extract maximum value from the use of external financing, whilst remaining financially sustainable.

1.17. A selection of ratios is summarised in **TABLE 6** below. A complete list of ratios is presented in Annexure 3. These ratios are the outcomes of the financial model.

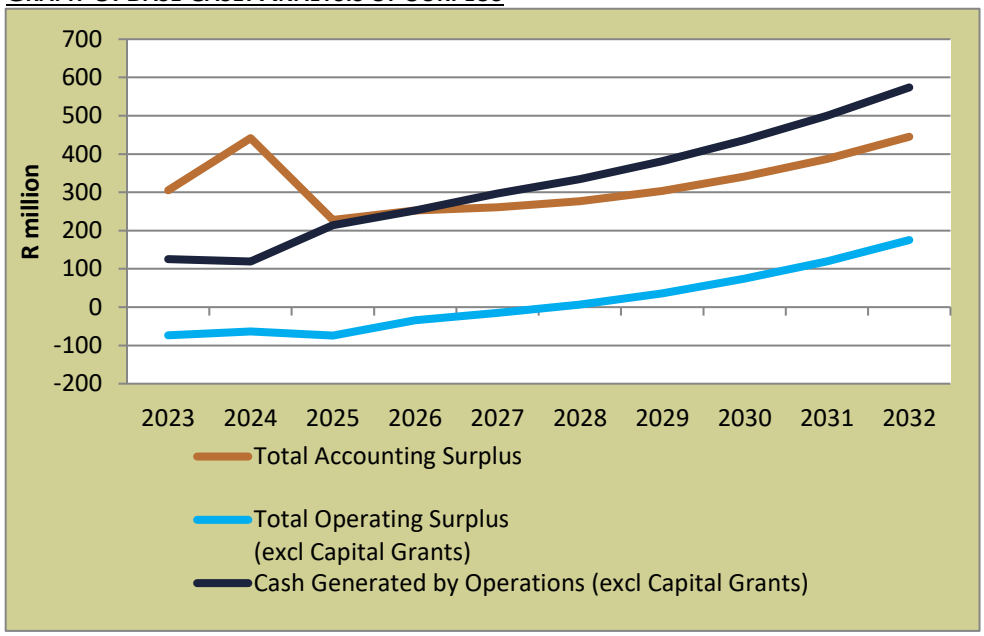
TABLE 6: SELECTION OF RATIOS (SEE ANNEXURE 3 FOR COMPLETE LIST)

YEAR		1	3	5	7	9	10
RATIOS	**Norm**	**2022/23**	**2024/25**	**2026/27**	**2028/29**	**2030/31**	**2031/32**
Cash Generated by Operations / Own Revenue		23,0%	20,6%	19,8%	19,4%	19,7%	19,9%
Liquidity Ratio (Current Assets: Current Liabilities)	1:1.5 - 1:2.0	1.5 : 1	1.4 : 1	1.6 : 1	1.8 : 1	1.9 : 1	2.1 : 1
Cash Surplus / Shortfall on Minimum Liquidity Requirements		R 86 m	R 148 m	R 361 m	R 563 m	R 835 m	R 999 m
Capital Expenditure / Total Expenditure	10% - 20%	21,7%	19,1%	10,7%	10,6%	10,4%	10,3%
Gearing = Total Debt (Borrowings) / Operating Revenue	45%	17%	36%	30%	24%	18%	15%
Debt Service Cover Ratio (Cash Generated by Operations / Debt Service)	Min 1.3:1	4.2 : 1	2.2 : 1	2.3 : 1	2.4 : 1	2.7 : 1	2.7 : 1
Total Grants / Total Revenue		31,6%	26,0%	24,1%	22,9%	21,9%	21,4%

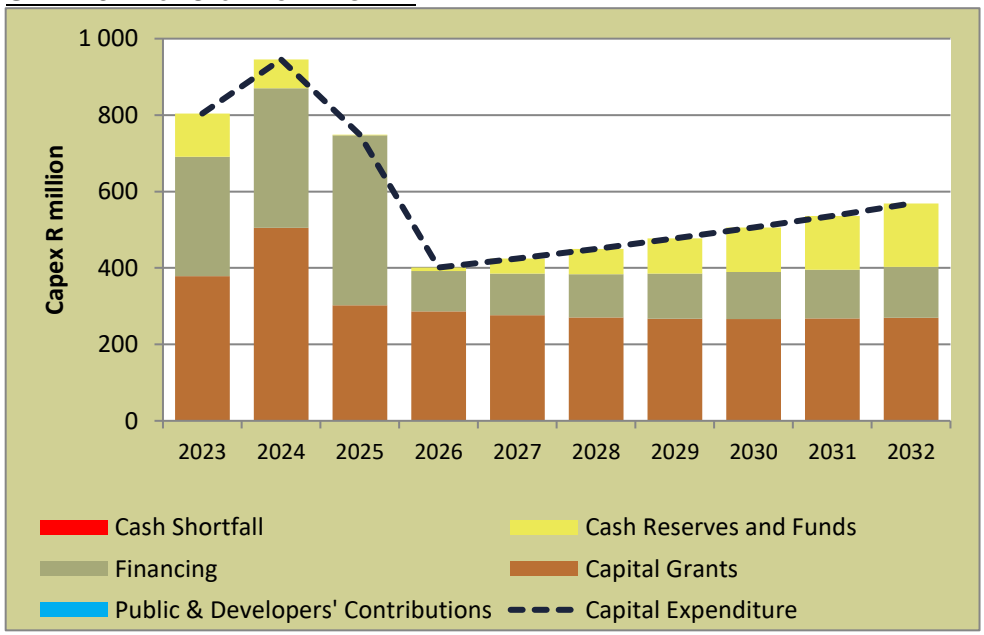
GRAPH 4: BASE CASE: BANK BALANCE IN RELATION TO MINIMUM REQUIRED LIQUIDITY LEVEL



GRAPH 5: BASE CASE: ANALYSIS OF SURPLUS



GRAPH 6: BASE CASE: FUNDING MIX



7. FUTURE MUNICIPAL REVENUE

In constant monetary terms (2015) the municipal revenue per capita in 2032 is estimated to be R 4 989 p.a., this is higher than the R 4 303 p.a. real per capita revenue generated in 2022. This is a key indicator for the municipality's ability to obtain revenue from residents as pointed out in Section 3 above when presenting the MRRI model.

- The estimated future 10-year annual average growth in revenue is 7.5% p.a.

AVERAGE ANNUAL 10-YEAR GROWTH OF MAJOR REVENUE ITEMS

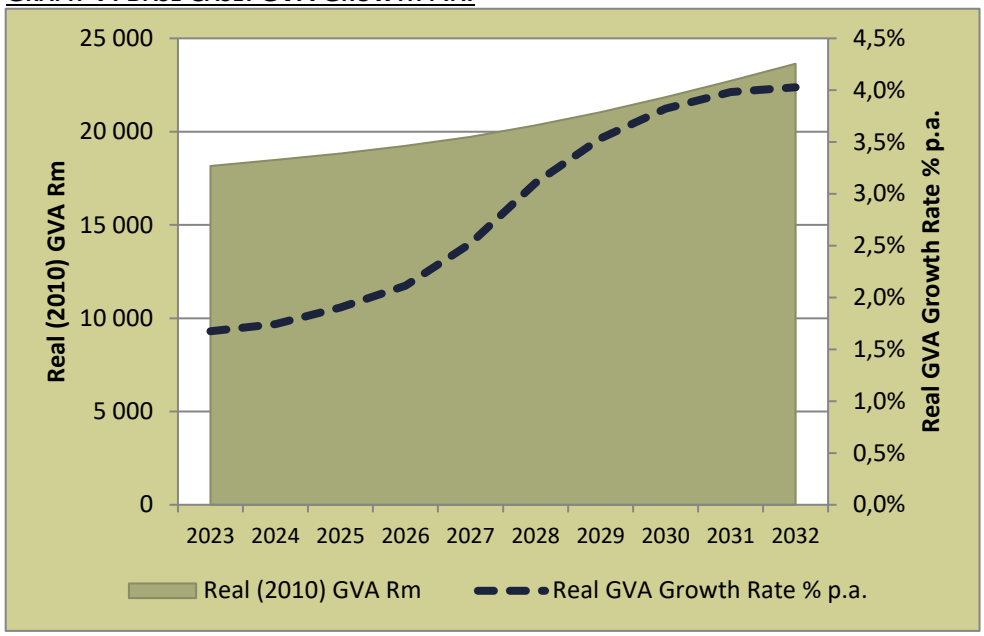
Revenue Item	Average Billings Growth % p.a.
Rates	7.1
Water	5.3
Electricity	7.9
Operating Transfers	6.9
Sanitation	9.3
Refuse	9.3

7.1. The forecast of future revenue in the financial model is based in part on historical trends as well as an estimate of future revenue (Revenue = Quantity x Price), where "Quantity" is a function of independent variables (such households, population and GVA) and "Price" a function of policy choices such as tariff increases.

7.2. The future Gross Value Add ("GVA") of GLM was estimated based on a view of the future economic growth of the region as well as an estimate of future population in the municipal area. **GRAPH 7** below illustrates the Base Case GVA and GVA growth rates used in IPM's model. Notwithstanding the significant economic recovery of 5.1% experienced in 2021, this remains lower than the drastic contraction of -5.9% in 2020 as a consequence of the pandemic. The average annual economic growth rate for the planning period is positive at 2.8% p.a., while there has been sluggish growth over the review period, with average economic growth of 0.9% p.a. since 2011.

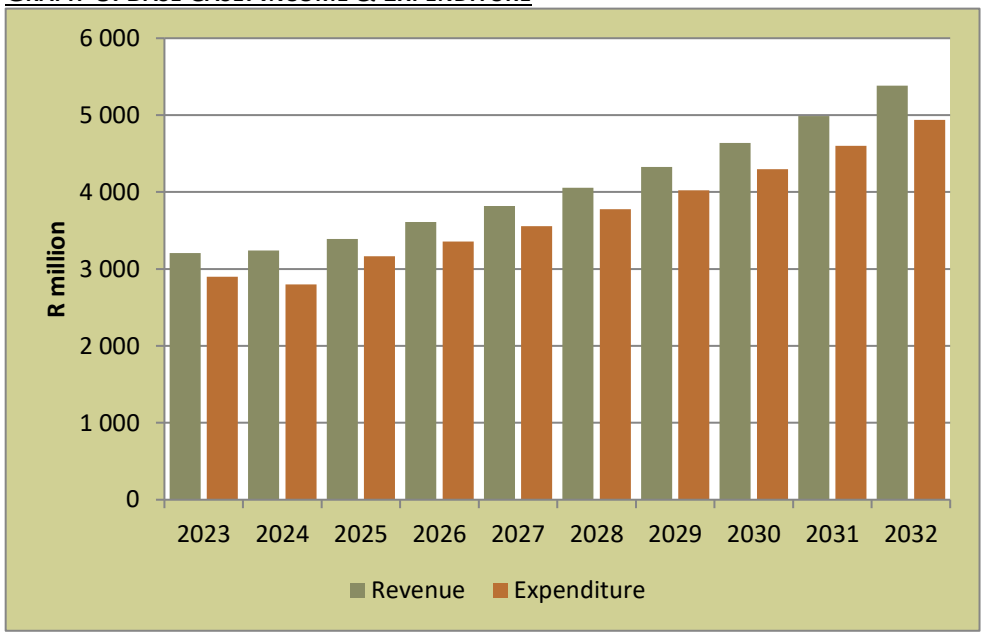
7.3. The expected average population growth rate is 1.7%. when looked at in comparison with the forecast GVA growth rate of 2.8% mentioned above, this bodes well for the municipality's future revenue and growth prospects. The impact of the forecast rate of household formation will be discussed below.

GRAPH 7: BASE CASE: GVA GROWTH P.A.



7.4. The estimated future revenue was informed by the municipality's forecast of future revenue in its MTREF. The estimated Total Income and Expenditure during the planning period for George LM is illustrated in **GRAPH 8**:

GRAPH 8: BASE CASE: INCOME & EXPENDITURE



7.5. The number of households is expected to grow at an average rate of 1.7% p.a., slightly below with the assumed population growth rate of 1.9% p.a. The proportion of indigent households is expected to increase to 40% by the end of the forecast period. Contributing factors to this increase include rising unemployment driven by the harsh economic environment in which the municipality must operate, as well as the increasing trend of urbanisation.

7.6. The 10-year growth in billings of the major revenue items is illustrated in the **TABLE 7** below.

TABLE 7: FORECAST AVERAGE ANNUAL GROWTH OF REVENUE ITEMS

Revenue Item	Average Billings Growth % p.a.
Rates	**7.1**
Water	**5.3**
Electricity	**7.9**
Operating Transfers	**6.9**
Sanitation	**9.3**
Refuse	**9.3**

7.7. **GRAPH 8** above illustrates the increasing trend in profitability throughout the forecast period. While this is positive to note, the municipality will continue to realise Operating Deficits until FY2027/28. The total grants to revenue ratio reflects a decreasing trend (see **TABLE 6** above), however the municipality will remain reasonably reliant on grant funding. It is strongly recommended that the municipality maximises its own revenue and ensures that collection procedures remain strong.

7.8. The increasing number of indigent households provides limited opportunities for higher tariff increases, though according to the percentage of households above the equitable share bracket vs the households receiving RDP level services or higher, there remains scope to increase revenue through billings.

7.9. Electricity services is expected to remain the predominant revenue source, with a forecast average contribution to operating income of 32.4% p.a., below the historical average of 34.9%. The price of electricity is highly regulated. The average electricity gross surplus margin for the forecast period is expected to be 22.8%, again below the historical average surplus margin of 30.5%. The municipality is urged to implement measures to curtail the negative impact of the increasing number of illegal connections, damage to infrastructure, cable theft and resultant repair costs. This will go a long way in safeguarding the municipality's electricity revenue generation efforts.

7.10. IPM's model forecasts that the real GVA per capita in 2032 will be R 85 313, an increase of 12.1% in real terms from the 2022 GVA per capita of R 76 118, a product of forecast economic growth. By comparison, the municipal real revenue per capita (excluding grants) in 2032 is forecast to amount to R 5 006 p.a., an increase of 16.3% from the 2022 total of R 4 303 p.a. We are comfortable that the Real Revenue per Capita for 2032 as forecast by IPM's model is reasonable. Considering the current demographic and socio-economic environment, these projections promote the affordability of the municipal bill.

8. FUTURE OPERATIONAL EXPENDITURE

Employee Related Expenses and Electricity Bulk Purchases are the two largest Operational Expenditure items, followed closely by Contracted Services. To remain sustainable the municipality should maximize its operational productivity by:

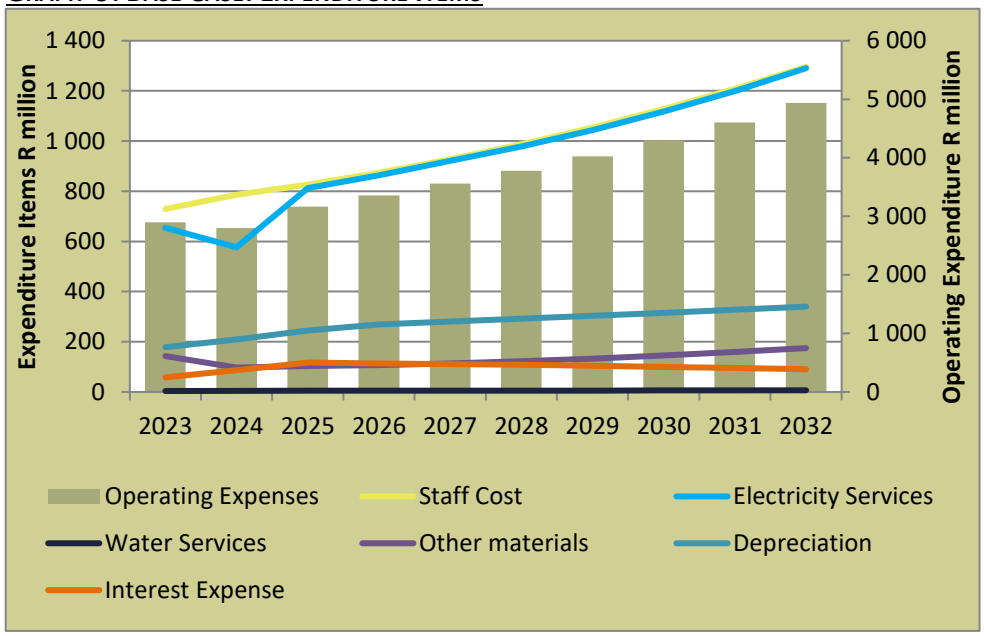
- Optimising the use of employees and contractors.
- Ensuring that operating expenditure is targeted, prioritised and efficient.
- Reviewing debt collection procedures to maintain or improve the collection rate and reduce debt impairment.
- Ensuring that the full cost of service delivery is covered by tariffs.
- Safeguarding of infrastructure and minimising distribution losses for water and electricity.
- Account for the impact of loadshedding on municipal revenues and expenditure.

8.1. Aligning the expenditure budget with the forecast revenues and collections remains a key component of the municipality's budgeting process. It is important for the municipality to ensure that future expenditure is budgeted in accordance with the expected revenues and cash collection to ensure that accounting and operating surpluses are realised.

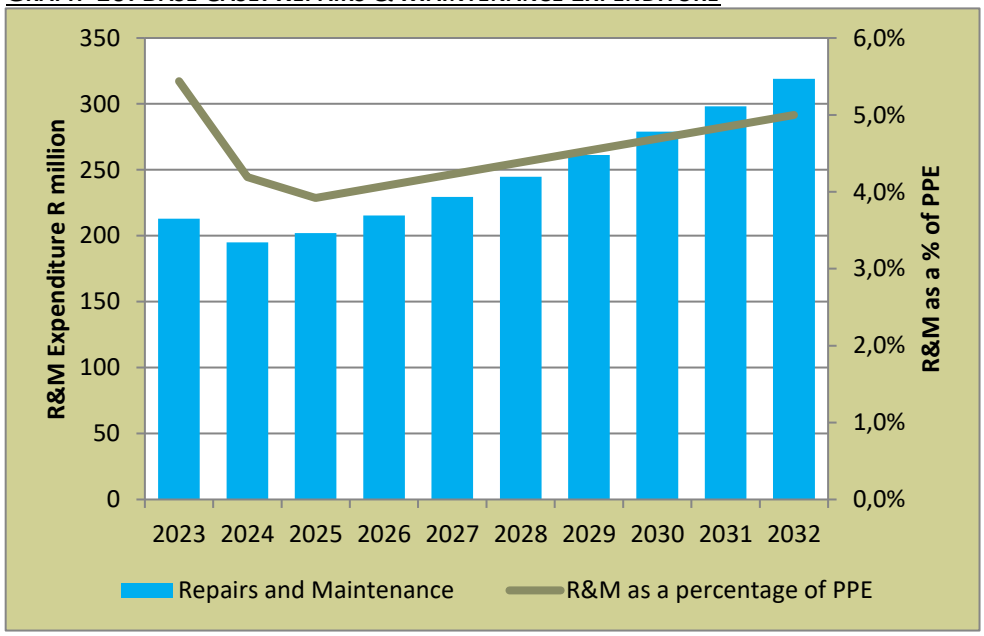
8.2. Significant increases in costs will have a negative impact on the municipality's financial performance, a clear example of this is presented in **TABLE 4**, which presents a comparison of electricity revenue between the MTREF Case and the Base Case Model. While the municipality has taken care to incorporate the impact of loadshedding in year one of the Adjusted Budget, this is not the case for MTREF years two and three. This is clearly reflected in the substantial difference in the MTREF Case and Base Case electricity revenue in FY2023/24. This highlights the vulnerability of the municipality's operational performance to material increases in costs or material reductions of revenue. Careful management and planning of future operational expenditure is therefore required to ensure that expenditure is efficient and that the financial sustainability of the municipality is not compromised.

8.3. The largest expenditure item, employee related expenses, will amount to an average of 22.6% of total expenditure over the forecast period.

GRAPH 9: BASE CASE: EXPENDITURE ITEMS



GRAPH 10: BASE CASE: REPAIRS & MAINTENANCE EXPENDITURE



8.4. Repairs and Maintenance Expenditure amounted to an average of 4% of PPE and Investment Property over the review period, well below the NT recommended norm of 8%. Repairs and Maintenance expenditure is expected to reduce over the MTREF period, before increasing to 5% by the end of the forecast period. It is recommended that going forward this expenditure is increased to closer to the NT norm of 8%, to reduce the likelihood of impairment of assets in future.

8.5. The financial model has assumed cost increases as per the figures contained in the MTREF for the first three years but uses various independent variables to calculate

expenses in future and, where applicable, accounts for losses to calculate bulk purchases and services sold.

9. AFFORDABILITY OF FUTURE CAPITAL EXPENDITURE

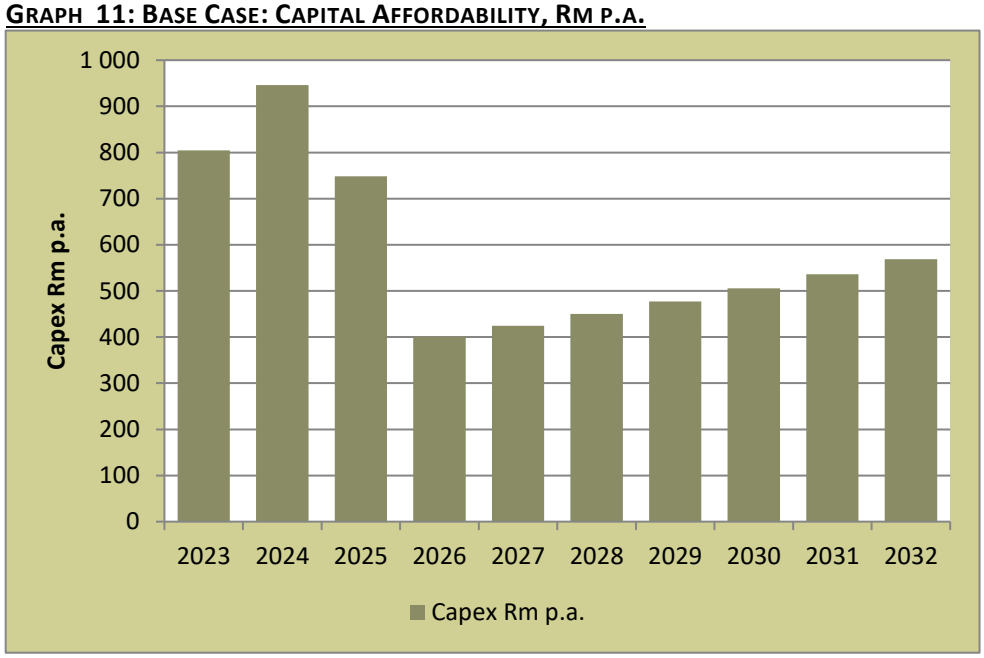
The total affordable capex for the period FY2022/2023 to FY2031/32 amounts to R 5.86 billion. The historic level of annual capital spending was an annual average of R 239.5 million. The model builds on this and accelerates capital expenditure at an annual rate of 6% after the MTREF period. The accelerated capex is primarily funded through increased capital grants (courtesy of the BFI grant) and external financing, with a small percentage funded through own cash.

9.1. It was assumed that the capital expenditure budget presented in the 2022/23 Adjusted Budget will be implemented, while escalating at a rate of 6% per annum beyond the MTREF period. The capital expenditure for FY2025/26 was reduced to R 400 million in the interest of financial sustainability. The long-term financial model calculates the future capital investment that the municipality can afford for the period up to FY2031/32 and increases the expenditure annually within the affordability limits. Over the 10-year forecast period, the annual average capital expenditure amounts to R 586.1 million. This greatly exceeds the historic annual average capital expenditure mentioned above, this is due to the receipt of a BFI grant to the value of R1.10 billion from National Treasury. The receipt of this grant is reflected in the significantly increased capital grant funding in the 2022/23 Adjusted Budget.

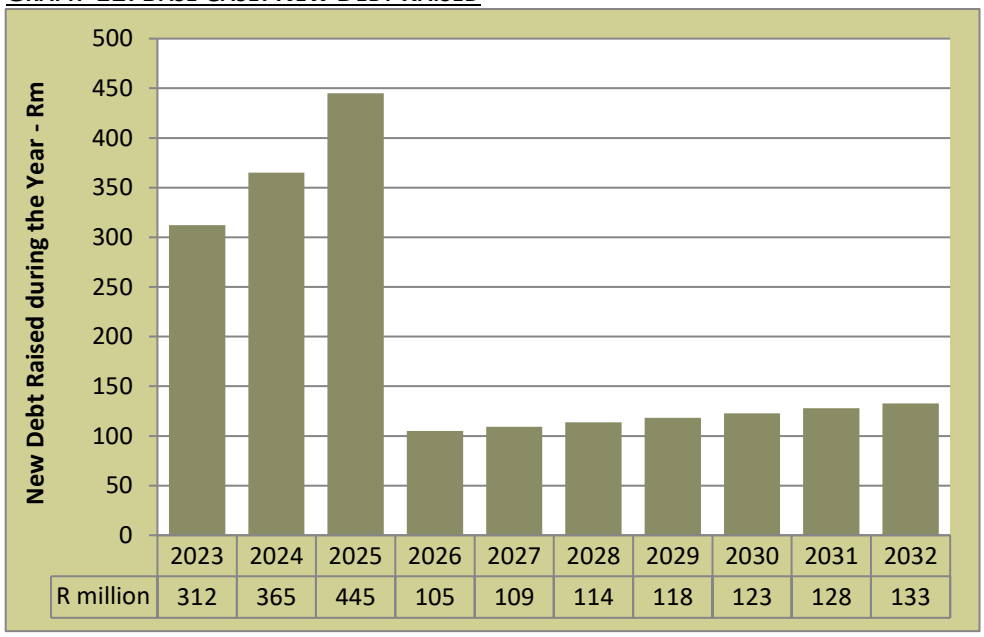
9.2. The MTREF Case capital expenditure forecasts cash shortfalls on budgeted capex from FY2028/29 onwards. As alluded to above, in the interest of ensuring a financially sustainable and affordable capital investment programme, the Base Case capital expenditure was reduced in FY2025/26. In arriving at the Base Case funding mix, borrowing was significantly increased over the MTREF period, before being reduced in FY2025/26. Borrowing is assumed to experience annual growth of 4%. This results in an optimal funding mix, with the increased capital grants remaining the primary funding source, followed by an increased but affordable level of borrowing, with a comparatively smaller amount of own cash required to fund capital investment. The more highly leveraged debt profile remains affordable, as indicated by the debt indicators being within their respective norms by the end of the planning period.

9.3. The affordability of the debt profile, as previously mentioned, will allow the municipality to fund its budgeted capital investment programme through accelerated borrowing, whilst maintaining a financially sustainable position. Improvements in operational performance will, in theory, unlock the acceleration of the capital investment programme, through catering for accelerated affordable borrowing while preserving cash resources and maintaining prudent financial management.

GRAPH 11: BASE CASE: CAPITAL AFFORDABILITY, RM P.A.



GRAPH 12: BASE CASE: NEW DEBT RAISED



10.FUNDING OF FUTURE CAPITAL EXPENSES

The estimated 10-year capex funding is shown in the table below:

FUNDING FUTURE AFFORDABLE CAPITAL EXPENDITURE

Source of Funds	Amount Rm	%
Public & Developers' Contributions	-	-
Capital Grants	3 091	53 %
Financing	1 952	33 %
Cash Reserves and Funds	819	14 %
Cash Shortfall	-	-
TOTAL	**5 861**	**100 %**

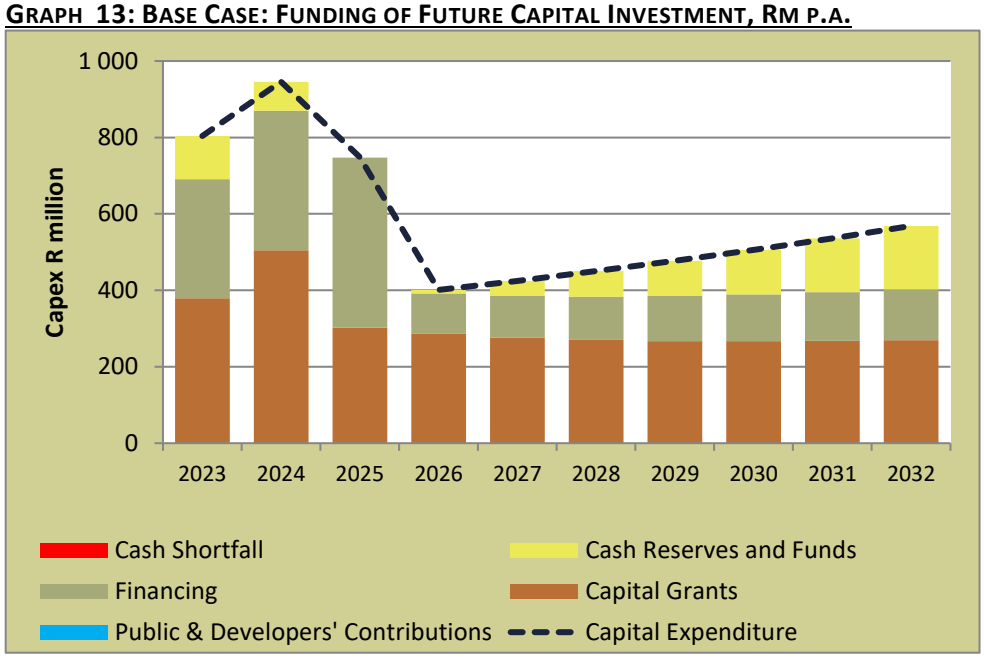
10.1. The funding mix to fund the future affordable capex is determined by the model by ensuring that the available cash is either invested to cover the minimum liquidity requirements and fund a capital replacement reserve or invested in capital assets. In accordance with the model the capex may be funded as follows:

TABLE 8: ESTIMATED 10-YEAR CAPITAL INVESTMENT & FUNDING

Year	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
Public & Developers' Contributions	0	0	0	0	0	0	0	0	0	0
Capital Grants	379	505	302	287	276	270	267	267	268	270
Financing	312	365	445	105	109	114	118	123	128	133
Cash Reserves and Funds	113	75	1	9	39	66	92	116	141	166
Capital Expenditure	**804**	**946**	**748**	**401**	**424**	**450**	**477**	**506**	**536**	**568**

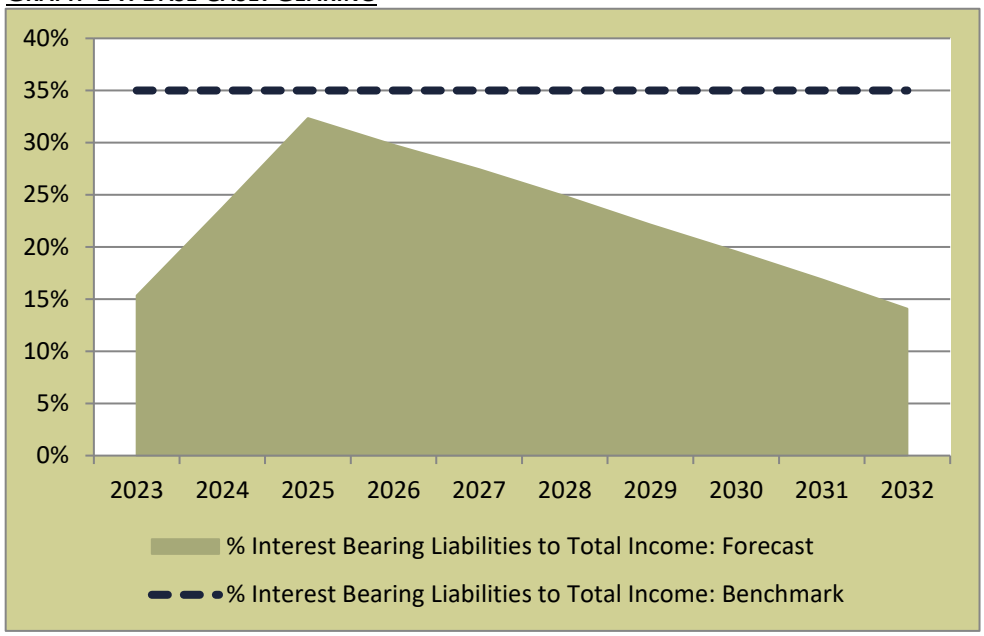
10.2. The BFI grant received by George LM has resulted in substantial increases in capital grant funding over the MTREF period. In light of this, capital grants are forecast to be the primary funding source over the forecast period, with a contribution of approximately 53%. This is followed by the accelerated borrowing programme, that will contribute approximately 33%. This leaves the remaining 14% to be contributed by the municipality's own cash reserves. It is our opinion that the Base Case presents an optimal funding mix, with a fair balance between affordable borrowing and own cash to supplement capital grants.

GRAPH 13: BASE CASE: FUNDING OF FUTURE CAPITAL INVESTMENT, RM P.A.

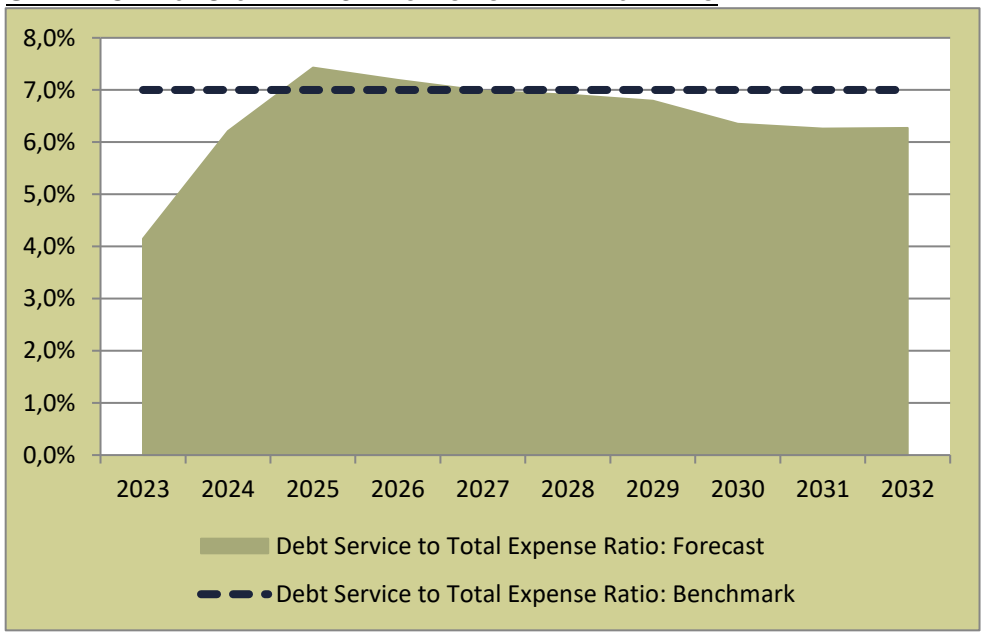


10.3. The amount of Grant funding was informed by historical trends and the Adjusted Budget figures. As illustrated in **GRAPH 13** above, the future amounts of Grant funding are expected to marginally decline beyond the MTREF period. Once the BFI grant funding has been utilised, it is expected that capital grants funding will reduce for the remainder of the forecast period. This will result in the need for alternative funding sources being increased. Consistent accessing of affordable borrowing, along with own cash reserves as a supplement will allow for capital expenditure to remain at a high level. As such, the Base Case incorporates borrowing throughout the forecast period, which will reduce pressure on cash reserves to supplement capital grant funding.

GRAPH 14: BASE CASE: GEARING



GRAPH 15: BASE CASE: DEBT SERVICE TO TOTAL EXPENSE RATIO



10.4. The gearing ratio is forecast to remain below the maximum recommended norm throughout the forecast period. The debt service to total expense ratio is expected to breach the maximum recommended norm in FY2024/25 & FY2025/26, before reducing to affordable levels for the remainder of the forecast period. From a long-term perspective, the marginal nature of the breach and subsequent recovery below the norm deem the Base Case debt profile to be affordable.

10.5. The model proceeds from the premise that the minimum required liquidity must preferably be held in reserve before cash may be spent on capex. The "Liquidity Reserve" is the amount of cash equivalents held to cover the amounts of statutory

reserve requirements, unspent conditional grants, short term provisions and at least one month's operational expenditure. The municipality has historically kept to this principle, realising cash surpluses on minimum required liquidity throughout the review period and is forecast to do the same for the entire planning period.

10.6. As indicated, the Base Case significantly increases the level of external borrowing. The municipality has not undertaken borrowing since FY2019/20 and as such the current debt profile is under-leveraged, meaning there is scope to increase borrowing in an affordable manner. It is positive to note that the municipality has included a significant level of borrowings in the 2022/23 Adjusted Budget. Regular access to the debt market can aid the municipality in obtaining competitive lending rates in future. This requires consistent servicing of debt obligations as scheduled. If this is achieved, the risk view of the municipality will improve and thus lead to a reduction in the overall cost of funding.

10.7. The municipality has developed a targeted and prioritized capital investment programme aimed at improving identified areas such as the Potable Water Security and Remedial Works projects, for which the BFI grant was applied. This approach must be maintained in the long-term. The municipality is further advised to prioritise asset renewal and replacement, with a focus on increasing expenditure on repairs and maintenance, as this will avoid any deterioration in the quality of the asset base.

11. ALTERNATIVE SCENARIOS

Three scenarios were analyzed and compared to the Base Case. The rationale for this section is to identify key variables and demonstrate the impact on the long-term financial position of the municipality by adjusting only one variable at a time. This helps to focus future policy interventions. The scenarios are presented below:

- Scenario 1: Reduced Operating Expenditure: 2% reduction.
- Scenario 2: Extension of average loan tenor.
- Scenario 3: Accelerated borrowing programme.

Environmental factors outside the control of the municipality (e.g. economic growth and regulated prices) as well as policy choices by the municipality (e.g. rates and tariff increases) have a significant impact on future financial viability.

Scenario 1: Improved Financial Performance through reduced Operating Expenditure

11.1. This scenario once again builds on the Base Case Model, by modelling an improvement in financial performance through a 2% reduction of Operating Expenditure.

11.2. The outcomes of this scenario are tabled below.

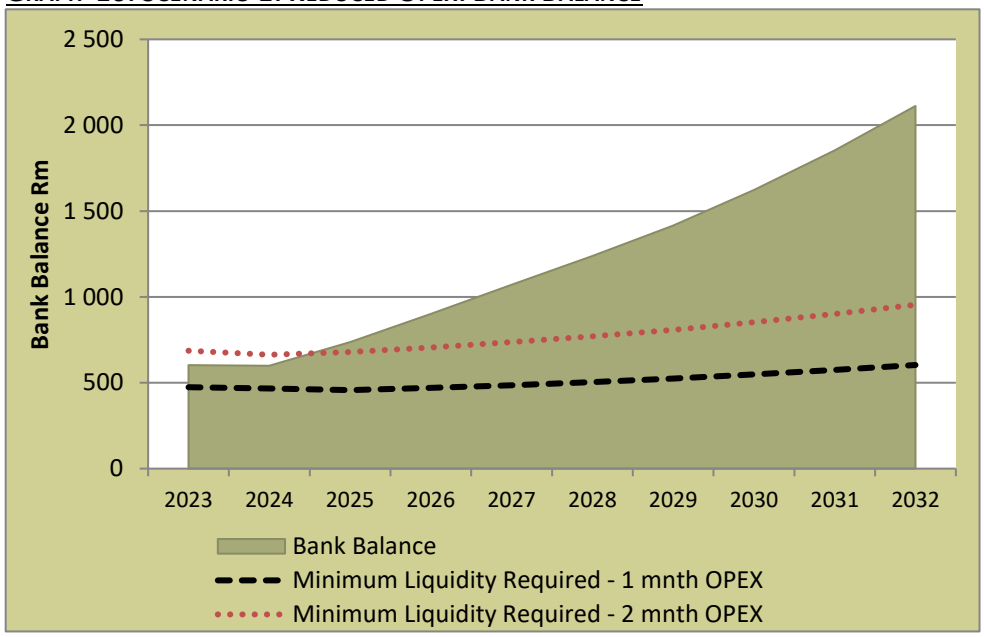
TABLE 9: SCENARIO 1: REDUCED OPEX: OUTCOMES

Outcome	Base Case	Opex -2% Scenario
Average annual % increase in Revenue	7,5%	7,5%
Average annual % increase in Expenditure	7,8%	7,7%
Accounting Surplus accumulated during Planning Period (Rm)	R 3 242	R 3 748
Operating Surplus accumulated during Planning Period (Rm)	R 151	**R 656**
Cash generated by Operations during Planning Period (Rm)	R 3 234	R 3 736
Average annual increase in Gross Consumer Debtors	11,2%	11,2%
Capital investment programme during Planning Period (Rm)	R 5 861	R 5 861
External Loan Financing during Planning Period (Rm)	R 1 952	R 1 952
Cash and Cash Equivalents at the end of the Planning Period (Rm)	R 1 611	**R 2 112**
No of Months Cash Cover at the end of the Planning Period (Rm)	4,6	6,0
Liquidity Ratio at the end of the Planning Period	2.1 : 1	**2.6 : 1**
Gearing at the end of the Planning Period	14,8%	14,7%
Debt Service to Total Expense Ratio at the end of the Planning Period	6,3%	6,3%

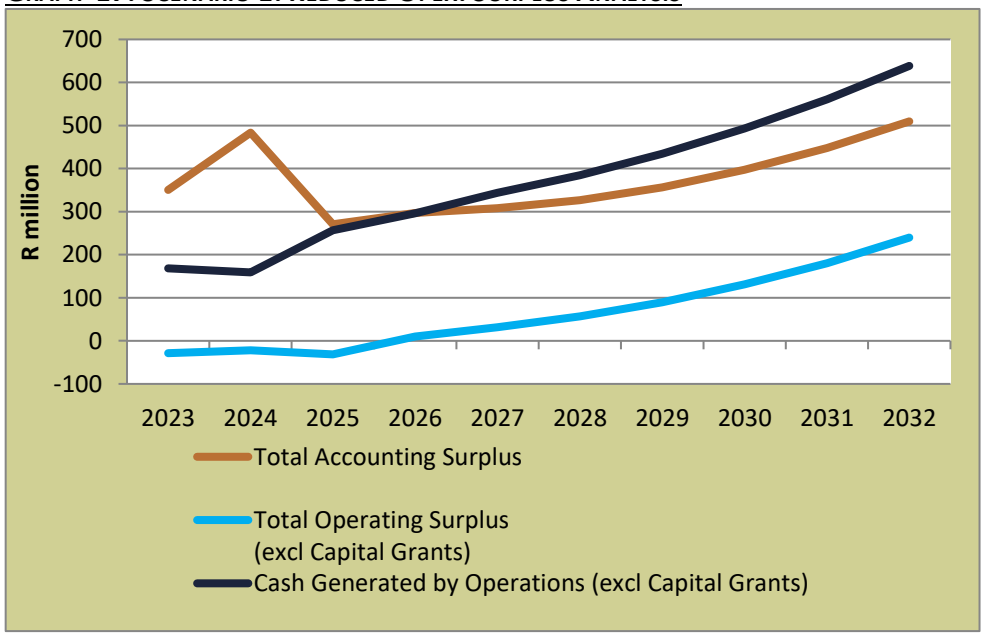
11.3. As presented in **TABLE 9**, GLM's financial performance is significantly improved through improvements in its operational performance. Highlighted by substantially improved profitability and liquidity.

11.4. Considering the limited opportunity for diversification of municipal revenue sources, as well as the fact that the municipality exerts an element of control over its operating expenditure, the importance of operating expenditure management to the sustainability of the municipality cannot be understated.

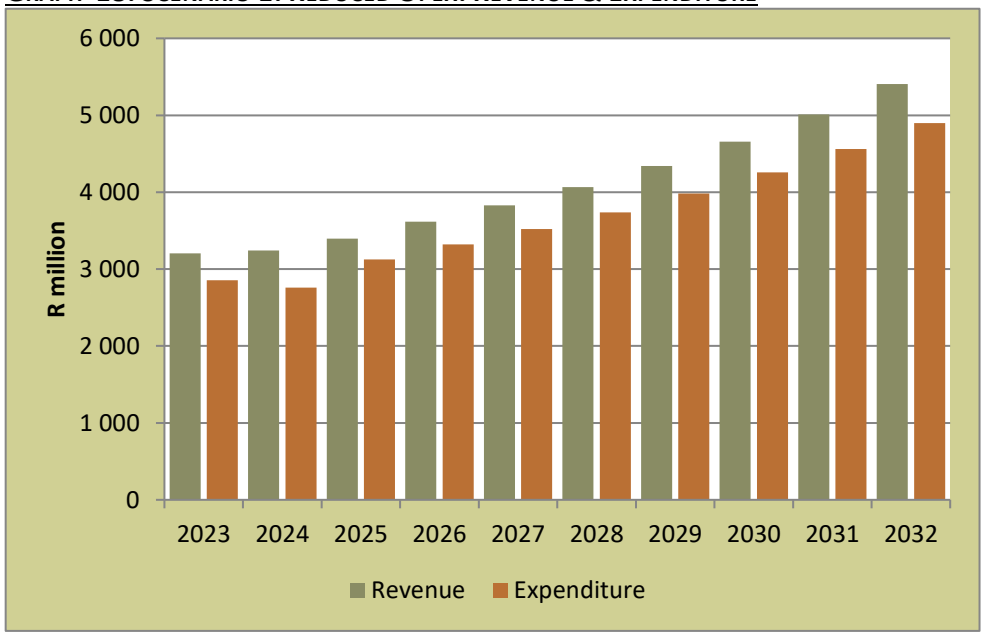
GRAPH 16: SCENARIO 1: REDUCED OPEX: BANK BALANCE



GRAPH 17: SCENARIO 1: REDUCED OPEX: SURPLUS ANALYSIS



GRAPH 18: SCENARIO 1: REDUCED OPEX: REVENUE & EXPENDITURE



11.5. It is imperative that the municipality conducts regular analyses of its operating expenditure, to ensure that expenditure is targeted, efficient and prioritized.

11.6. The improved financial performance as a result of the above will leave the municipality in a sustainable financial position, able to absorb potential financial shocks whilst simultaneously unlocking opportunities for further growth and development.

SCENARIO 2: EXTENDED AVERAGE LOAN TENOR

11.7. This scenario tests the impact of extending the Base Case Model average loan tenor of 10 years, to an average of 13 years.

11.8. The extension of the average loan tenor will have the effect of reducing annual debt servicing charges, while extending the period of time for which the debt will need to be serviced, which may result in increased finance charges.

11.9. As stated, the increased finance charges may negatively impact profitability and this has proven to be the case albeit marginally, with modestly reduced accumulated accounting and operating surpluses over the planning period. A similar effect is had on cash generation due to the cash nature of finance costs payments.

11.10. This scenario will, however, have positive effects on the municipality's liquidity position as evidenced by the outcomes presented in **TABLE 10** below.

11.11. The improved liquidity ratio and increased planning period-end bank balance, leave the municipality in a strong liquidity position, able to absorb potential financial shocks. This is despite the marginally reduced accumulated cash generated by operations over the planning period.

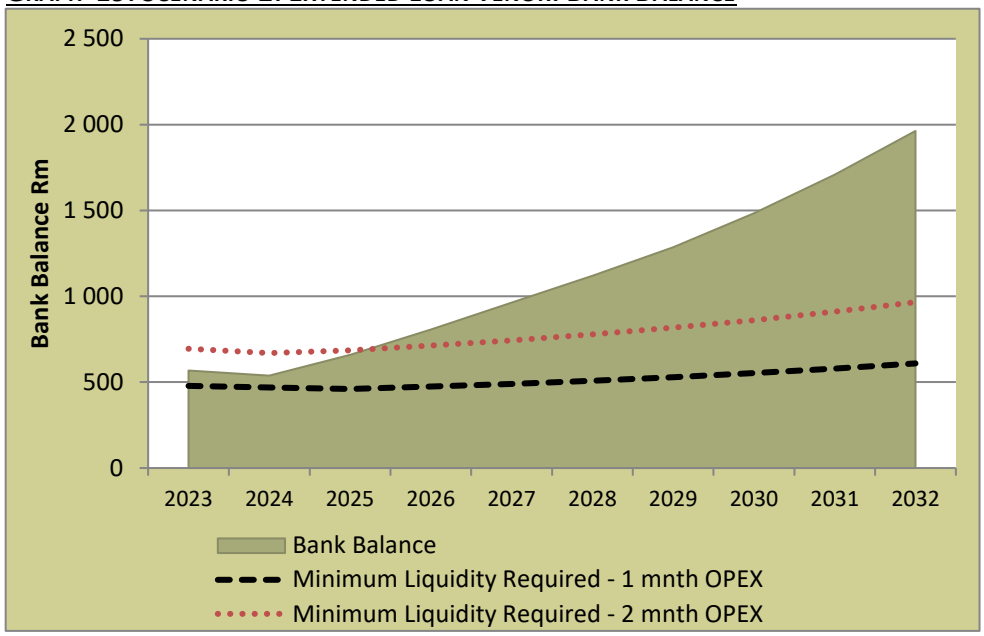
11.12. The impact of the extended loan tenor is evident in the increased gearing ratio and reduced debt service to total expense ratio at the end of the planning period. The gearing ratio is significantly increased as the amount of outstanding debt as at FYE2031/32 will naturally be higher than in the Base Case. A converse effect is had on the debt service to total expense ratio, with it being considerably reduced as compared to the Base Case, a reflection of the reduced annual debt service costs.

TABLE 10: SCENARIO 2: EXTENDED LOAN TENOR: OUTCOMES

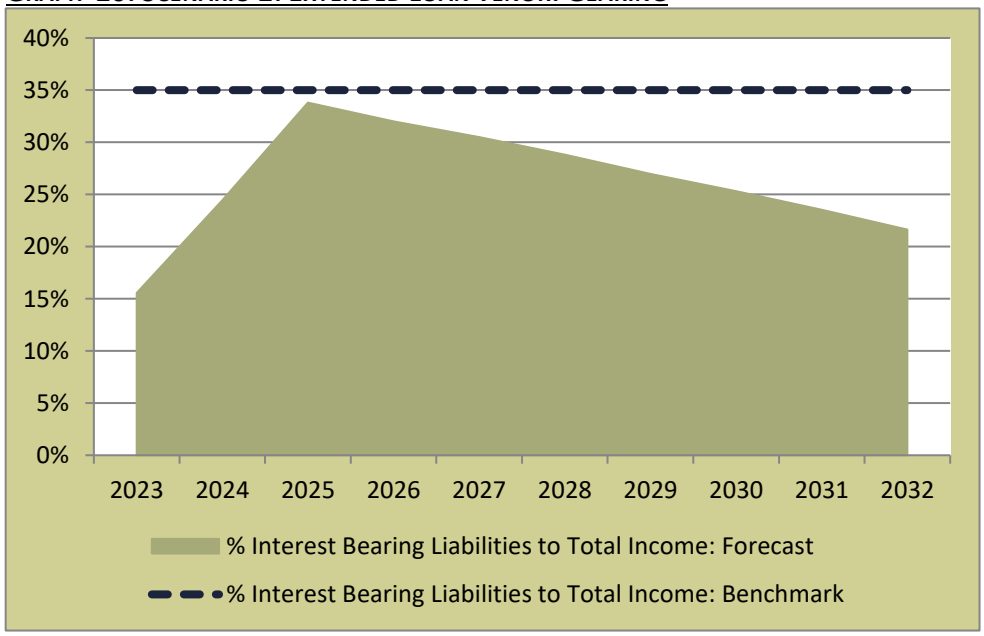
Outcome	Base Case	Extended Loan Tenor
Average annual % increase in Revenue	7,5%	7,5%
Average annual % increase in Expenditure	7,8%	7,9%
Accounting Surplus accumulated during Planning Period (Rm)	R 3 242	R 3 183
Operating Surplus accumulated during Planning Period (Rm)	R 151	**R 92**
Cash generated by Operations during Planning Period (Rm)	R 3 234	R 3 175
Average annual increase in Gross Consumer Debtors	11,2%	11,2%
Capital investment programme during Planning Period (Rm)	R 5 861	R 5 861
External Loan Financing during Planning Period (Rm)	R 1 952	R 1 952
Cash and Cash Equivalents at the end of the Planning Period (Rm)	R 1 611	R 1 963
No of Months Cash Cover at the end of the Planning Period (Rm)	4,6	5,5
Liquidity Ratio at the end of the Planning Period	2.1 : 1	**2.6 : 1**
Gearing at the end of the Planning Period	14,8%	**22,8%**
Debt Service to Total Expense Ratio at the end of the Planning Period	6,3%	**5,4%**

11.13. Notwithstanding the marginally negative impact on long-term profitability, it is recommended that the municipality considers the implementation of an increased loan tenor strategy should it decide to approach the external market for financing. Notwithstanding the historical trend of operating deficits and historically stable liquidity position, it is our view that the marginal reduction in profitability is outweighed by the considerable improvements in the liquidity position. The benefits of such an improvement to the liquidity position are extensive, this will allow the municipality to further accelerate capital investment which in turn will unlock further growth and development within the municipality.

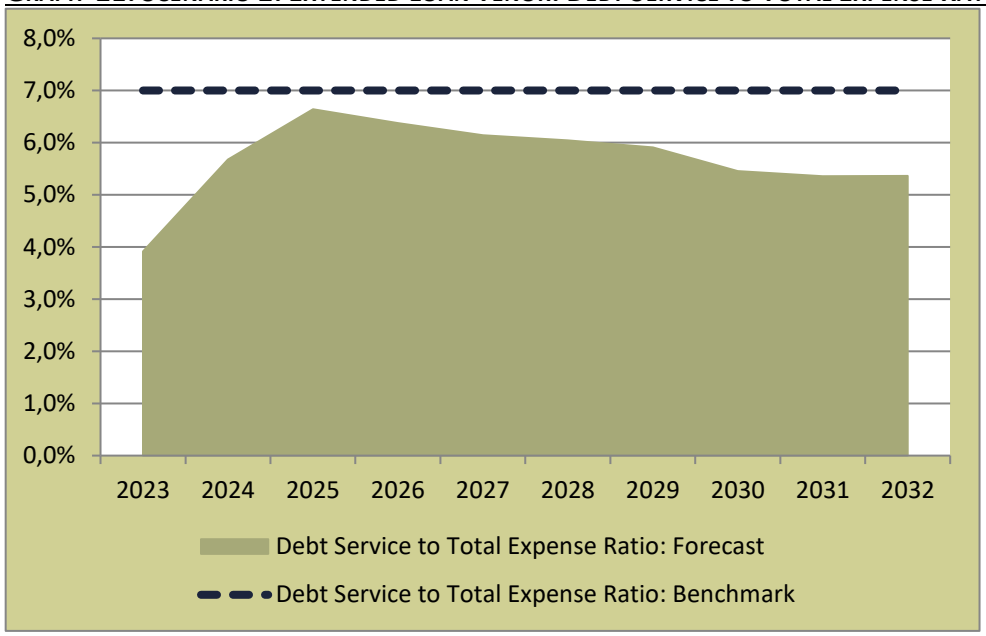
GRAPH 19: SCENARIO 2: EXTENDED LOAN TENOR: BANK BALANCE



GRAPH 20: SCENARIO 2: EXTENDED LOAN TENOR: GEARING



GRAPH 21: SCENARIO 2: EXTENDED LOAN TENOR: DEBT SERVICE TO TOTAL EXPENSE RATIO



SCENARIO 3: ACCELERATED BORROWING PROGRAMME

11.14. This scenario assesses the impact of further acceleration of the borrowing programme. This incorporates significantly increased borrowing as compared to the Base Case, without any amendments to the Base Case capital investment programme.

11.15. Total external financing over the planning period in this scenario is increased by R468 million or 23.9%. The outcomes of this scenario are reflected in the table below.

TABLE 11: SCENARIO 3: ACCELERATED BORROWING: OUTCOMES

Outcome	Base Case	Accelerated Borrowing
Average annual % increase in Revenue	7,5%	7,5%
Average annual % increase in Expenditure	7,8%	7,9%
Accounting Surplus accumulated during Planning Period (Rm)	R 3 242	R 3 122
Operating Surplus accumulated during Planning Period (Rm)	R 151	**R 30**
Cash generated by Operations during Planning Period (Rm)	R 3 234	R 3 114
Average annual increase in Gross Consumer Debtors	11,2%	11,2%
Capital investment programme during Planning Period (Rm)	R 5 861	R 5 861
External Loan Financing during Planning Period (Rm)	R 1 952	R 2 420
Cash and Cash Equivalents at the end of the Planning Period (Rm)	R 1 611	R 1 753
No of Months Cash Cover at the end of the Planning Period (Rm)	4,6	4,9
Liquidity Ratio at the end of the Planning Period	2.1 : 1	2.1 : 1
Gearing at the end of the Planning Period	14,8%	**19,9%**
Debt Service to Total Expense Ratio at the end of the Planning Period	6,3%	**7,7%**

11.16. Accelerating the external borrowing programme will have the impact of improving liquidity and available cash but will naturally further leverage the municipality and

result in increased annual debt service costs. This is reflected in **Table 11** above, wherein the accumulated operating surplus of R151 million is reduced to R30 million.

TABLE 12: SCENARIO 3: BASE CASE VS ACCELERATED BORROWING FUNDING MIX

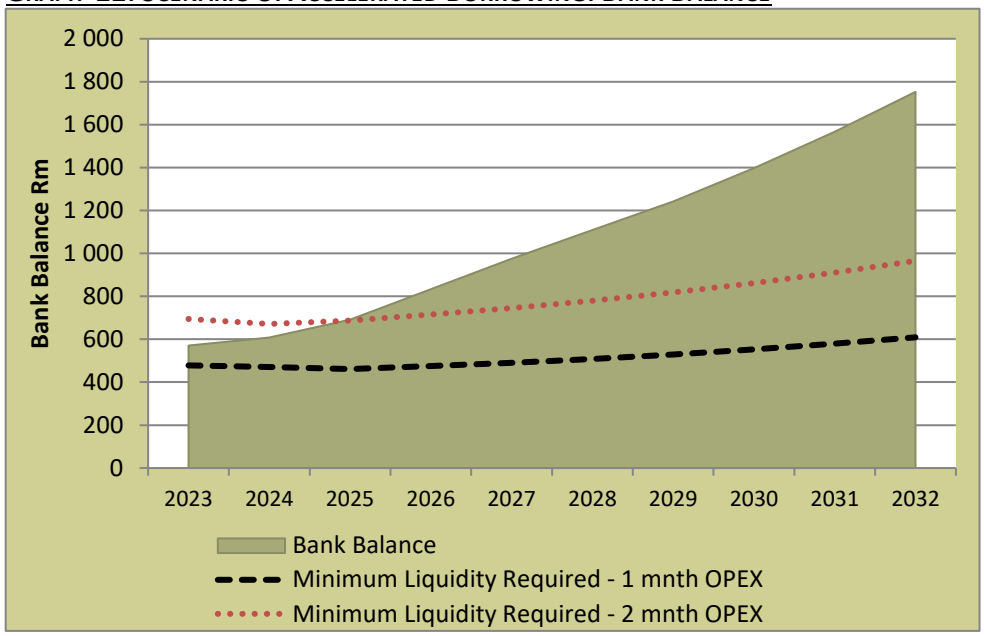
	Base Case		Scenario 3	
Source of Funds	**10-Year Amount Rm**	**%**	**10-Year Amount Rm**	**%**
Public & Developers' Contributions	0	0%	0	0%
Capital Grants	3 091	53%	3 091	53%
Financing	**1 952**	**33%**	**2 420**	**40%**
Cash Reserves and Funds	**819**	**14%**	**419**	**7%**
Cash Shortfall	0	0%	0	0%
TOTAL	**5 861**	**100%**	**5 861**	**100%**

11.17. The above table reflects the differences in the composition of the Base Case funding mix, and the funding mix presented in this scenario. The extent of cash reserves utilised to fund capital investment has been reduced by a considerable R400 million over the planning period, as a result of the 23.9% increase in external financing.

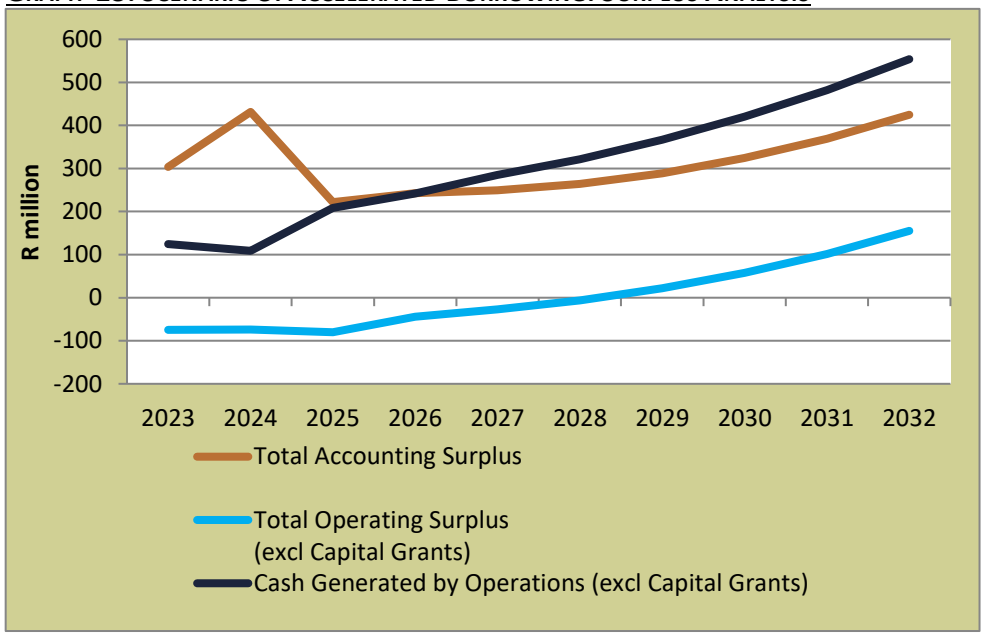
11.18. As mentioned previously in this report, the BFI grant received by the municipality is responsible for the substantial increase in the level of capital investment over the MTREF period. In order for the municipality to continue with an accelerated capital investment programme once the projects for which the BFI grant was earmarked are complete, the municipality will need to explore alternative avenues of funding capital expenditure. Accelerating the external borrowing programme will be the most viable option to achieve this, without putting the municipality's liquidity position at risk.

11.19. Consideration must be given to the impact of the cost of servicing the additional debt on the municipality's financial situation. The gearing ratio remains within the recommended maximum benchmark of 35% throughout the planning period (see **GRAPH 25**), the debt service to total expense ratio will, however, breach the maximum recommended norm of 7% from FY2023/24 for the remainder of the forecast period. This would indicate that the annual debt servicing costs appear high. Should the municipality decide to accelerate its external borrowing programme to such an extent as presented in this scenario, careful management of operating expenditure would be required to ensure that financial sustainability is not threatened by the increased debt service charges. Scrutiny of other financial metrics such as the debt service cover ratio of 2.7, indicates that notwithstanding the breach of the debt service to total expense norm, the municipality remains in a financially sustainable and resilient position. It is thus our view, that the debt profile presented in this scenario, remains affordable.

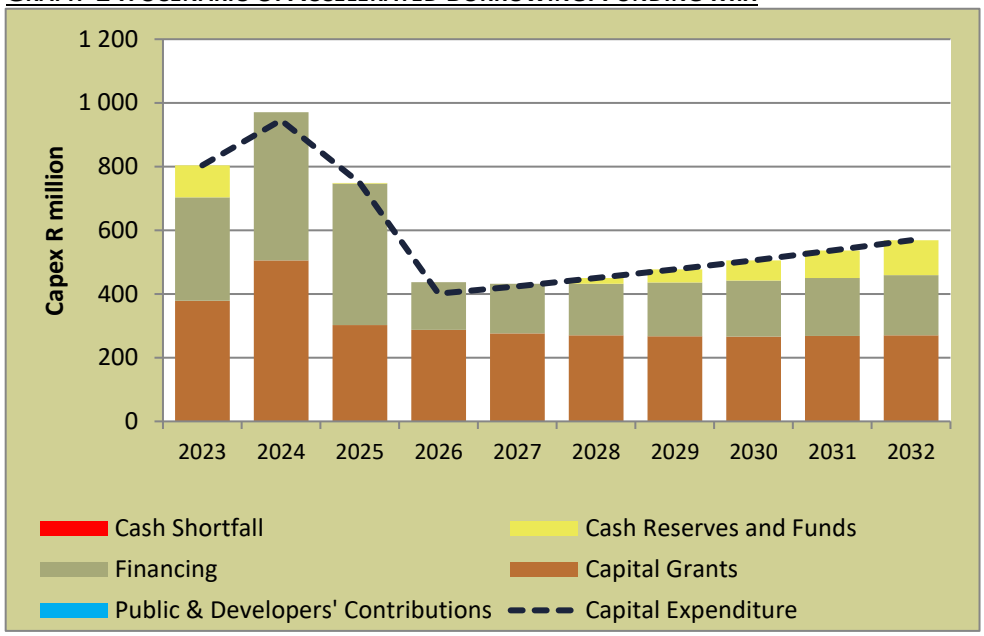
GRAPH 22: SCENARIO 3: ACCELERATED BORROWING: BANK BALANCE



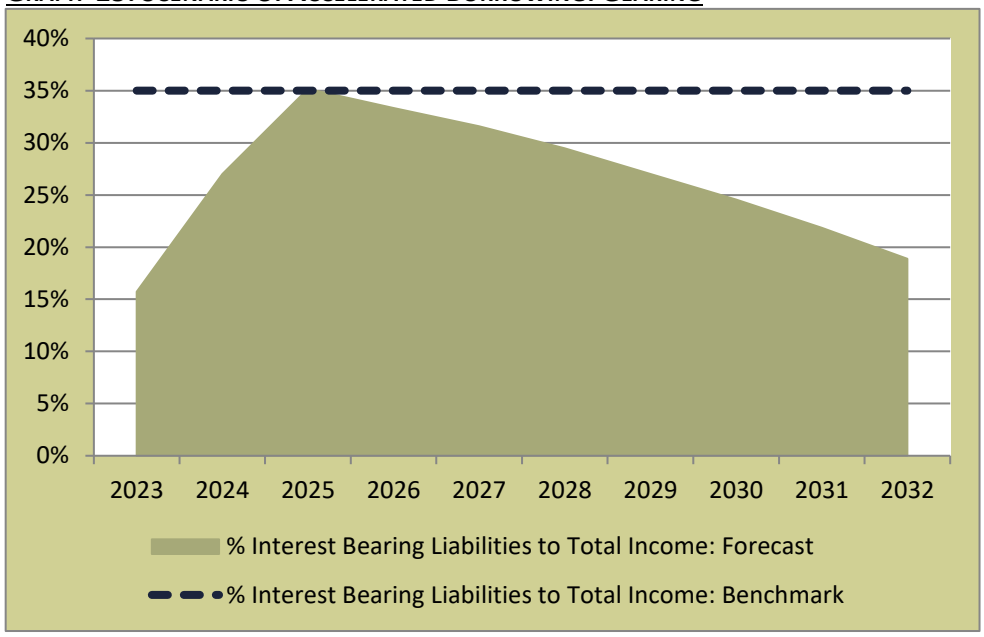
GRAPH 23: SCENARIO 3: ACCELERATED BORROWING: SURPLUS ANALYSIS



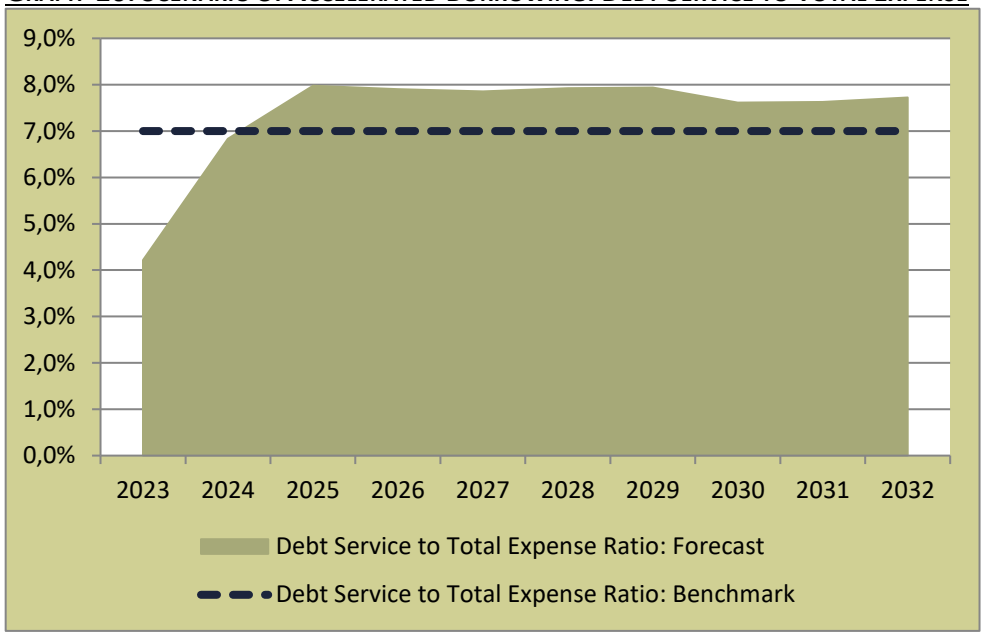
GRAPH 24: SCENARIO 3: ACCELERATED BORROWING: FUNDING MIX



GRAPH 25: SCENARIO 3: ACCELERATED BORROWING: GEARING



GRAPH 26: SCENARIO 3: ACCELERATED BORROWING: DEBT SERVICE TO TOTAL EXPENSE



12.RECOMMENDATIONS

We recommend the following, subject to discussions with Executive Management and Council of the Municipality, to be adopted for inclusion in a long-term financial plan.

The recommendations are based on the findings of the Independent Financial Assessment, which concluded that George LM's financial position is stable, highlighted by strong liquidity and consistent cash generation resulting in substantial cash surpluses on liquidity requirements. There has historically been a trend of operating deficits. The maintenance of the historically strong collection rate is crucial to the future sustainability of the municipality. The recently received BFI grant will allow for the capital investment programme to be significantly accelerated over the MTREF period, as included in the Adjusted Budget. Care must be taken to ensure that cash reserves are not excessively utilised to fund the capital investment programme as, notwithstanding the historically strong cash generation, this may provide a threat to financial sustainability.

12.1. OPERATIONS FRAMEWORK

Whereas some of the Base Case Outcomes do not yet comply with benchmark norms it is essential that the municipality institutionalises a financial plan that aims to achieve the norms of the following parameters (detail and definitions are provided in **ANNEXURE 3: RATIO ANALYSIS** and **ANNEXURE 4: VIABILITY FRAMEWORK**):

TABLE 13: OPERATIONS FRAMEWORK

		MFMA Norm	Minimum	Healthy	Base Case 10-Year Average
FINANCIAL POSITION					
ASSET MANAGEMENT					
	Capital Expenditure / Total Expenditure	10% - 20%	10%	20%	14,0%
	Repairs and Maintenance as % of PPE and Investment Property	8%	n.a.	6%	4.4%
DEBTORS MANAGEMENT					
	Gross Consumer Debtors Growth	n.a.	n.a.	0%	11,2%
	Payment Ratio / Collection Rate	95%	90%	95%+	95%
	Net Debtors Days	30	60	30	31
LIQUIDITY MANAGEMENT					
	Minimum Liquidity Level	1 – 3 months	1 months	3 months	3.5 months
	Liquidity Ratio (Current Assets: Current Liabilities)	1.5:1 – 2.:1	1 : 1	2 : 1	1.7 : 1
LIABILITY MANAGEMENT					
	Debt Service as % of Total Operating Expenditure	6% - 8%	n.a.	8.0%	6,5%
	Total Debt (Borrowings) / Operating Revenue	45%	40%	35%	25%
	Debt Service Cover Ratio (Cash Generated by Operations / Debt Service)	n.a.	1.3	1.5	2,7
SUSTAINABILITY					
	Net Financial Liabilities Ratio	n.a.	n.a.	< 60%	15,2%
	Operating Surplus Ratio	n.a.	n.a.	0% - 10%	0,0%
	Asset Sustainability Ratio	n.a.	n.a.	> 90%	26,7%
FINANCIAL PERFORMANCE					
EFFICIENCY					
	Accounting Surplus R'000	Break even or >0	Break even	> 0	R 3 242
	Cash Operating Surplus R'000	n.a.	Break even	> 0	R 151
	Net Operating Surplus / Total Operating Revenue	>= 0%	Break even	> 0%	0,0%
	Electricity Surplus / Total Electricity Revenue	0% - 15%	> 0%	> 15%	22,8%
	Water Surplus / Total Water Revenue	>= 0%	= 0%	> 0%	97,7%
REVENUE MANAGEMENT					

		MFMA Norm	Minimum	Healthy	Base Case 10-Year Average
	% Increase in Billed Income p.a.	CPI	n.a	n.a	7,6%
	Operating Revenue Growth %	CPI	n.a	n.a	7,9%
	Annual Increase per Income Source: Equitable Share	n.a	n.a	n.a	8,3%
	Annual Increase per Income Source: Property Rates	n.a	n.a	n.a	7,1%
	Annual Increase per Income Source: Electricity Services	n.a	n.a	n.a	7,9%
	Annual Increase per Income Source: Water Services	n.a	n.a	n.a	5,4%
EXPENDITURE MANAGEMENT					
	Creditors Payment Period	30	30	30	51
	Contribution per Expenditure Item: Staff Cost (Salaries, Wages and Allowances)	25% - 40%	25% - 30%	25%	23 %
	Contribution per Expenditure Item: Contracted Services	2% - 5%	2% - 5%	< 5%	17,5%
GRANT DEPENDENCY					
	Total Grants / Total Revenue	n.a.	n.a.	n.a.	25,2%
	Own Source Revenue to Total Operating Revenue	n.a.	n.a.	n.a.	81,3%
	Capital Grants to Total Capital Expenditure	n.a.	n.a.	n.a.	54,4%

12.2. PLANNING STRATEGIES

The municipality must analyse and ensure the viability of its long-term planning processes, with the objective of financial sustainability and resilience at the core of each decision. The institutionalisation of a Long-Term Financial Plan will greatly assist the municipality in this regard.

12.3. ORGANISATIONAL STRATEGIES

We recommend that GLM implement a formalized performance management programme throughout the organization, with clear, consequent management where lapses in outcomes occur. Ensuring accountability must be at the forefront of such a strategy.

12.4. REVENUE RAISING STRATEGIES

The municipality will continue to work on diversifying and ensuring growth of its revenue base. In light of the current energy crisis, revenue from electricity services is expected to be negatively impacted, it is therefore recommended that the following revenue streams are maximised in order to make up for the anticipated shortfall:

- Revenue from service charges
- Agency fees and fines
- Grants
- Donor funding
- Public Benefit Contributions to assist with the rehabilitation and maintenance of infrastructure, particularly where the municipality may lack the expertise to do so effectively itself.

12.4.1. Debtors Collection Action Plan

The municipality has managed to maintain a high collection rate throughout the review period. Analysis must be conducted to assess the efficacy of the current collection procedures to ensure, at a minimum, maintenance of the current collection rate. Any shortcomings must be identified and addressed. The Base Case presents a scenario in which the current collection rate of 95% is maintained throughout the forecast period.

12.4.2. Service Charges Margins

The municipality is advised to safeguard its margins on its service charges from potential decline. The sharp Eskom tariff increases will impact bulk purchases expenditure, while a comparable increase in consumer tariffs is not possible resulting in expected reductions in surplus margins. The Base Case assumes electricity tariffs will increase at a rate of roughly 3% below the associated bulk purchases tariffs throughout the MTREF period.

12.4.3. Enhance Potential Revenue

We recommend that:

- All consumers are captured, data is verified, billing is correct and monies due are collected.
- Large consumers are billed correctly for all services used and payments made are correct.
- GLM ensures payments are made timeously.
- Tariffs are cost reflective.
- Indigent support cases are verified independently.
- Maintain indigent support levels at the minimum levels as funded by fiscal transfers.
- Fines revenue collections are maximised.
- Diversification of revenue streams is limited, thus maximising available revenue streams is critical.

12.5. COST SAVING STRATEGIES

The municipality must compile the expenditure budget in accordance with anticipated revenue growth, as well as to anticipated cash collections to generate cash surpluses. Stringent expenditure management is critical, as is ensuring the expenditure budget is efficient, targeted and prioritised.

12.5.1. Productivity

In light of the history of operating deficits, management of operating expenditure remains critical. The municipality must ensure that expenditure remains efficient and prioritised. Efforts must be made to maintain technical losses for both water and electricity to a minimum. Employee related expenditure must be carefully monitored to ensure it remains efficient; it is thus recommended that the municipality:

- Limits employee related expenditure where possible through reviewing discretionary aspects of salaries and overtime policies.
- Conducts wider organisational review to ensure the municipality is not unnecessarily overstaffed and its organogram is efficiently organized.

12.6. FINANCIAL MANAGEMENT STRATEGIES

The sustainability and financial wellbeing of the municipality is linked directly to sound financial management. In this regard, it is recommended that the municipality continuously:

- Ensures that it complies with GRAP standards.
- Reviews and updates all policies and procedures annually.
- Automates National Treasury reporting templates to ensure proper reporting.
- Maintains an effective system of expenditure control, including procedures for approval authorization, withdrawal and payment of funds.
- Prepares annual financial statements timeously and reviews performance and achievements.
- Prioritises and diversifies its investment portfolio to maximize returns.
- Ensures that multi-year forecasts are sustainable.
- Maintains financial procedures and discipline to achieve and maintain unqualified audit history and addressing the audit findings which were as and when they are raised.

12.7. ASSET MANAGEMENT STRATEGIES

The Municipality must ensure that its assets are properly accounted for and safeguarded. Leveraging on the municipal assets will drive the economic growth and sustainable development of the Municipality. In particular:

12.7.1. Integrated Asset Management

Integrated asset management aims to deliver a required level of service, while being cost-effective through the management of assets for current and future customers. This entails utlising an integrated approach to asset management and performance, through monitoring, operating, maintaining, upgrading and disposing of assets in the most cost-effective manner. The creation and monitoring of a maintenance programme with the philosophy of proactive rather than reactive maintenance is critical and will contribute significantly to the saving of costs in future.

12.7.2. Repairs and Maintenance

The Base Case forecasts repairs and maintenance expenditure to remain at approximately 5% of the carrying value of PPE throughout the forecast period. This is below the recommended benchmark of 8% and ideally must be increased over the forecast period to safeguard against the deterioration of the municipal asset base.

12.7.3. Water and electricity losses

Acceptable electricity losses of 8.9% and water losses of 25.0% in FY2021/22 must be maintained. The Base Case maintains the current level of distribution losses throughout the forecast period.

It is recommended that the municipality, along with the provincial and national law enforcement agencies, coordinate and combine resources to safeguard municipal infrastructure from illegal activity to with a view of maintaining the current acceptable levels of distribution losses.

It is further recommended that the municipality implements a focussed and prioritized approach to ensuring that non-technical losses outside of theft or meter tampering are limited through ensuring that consumers are billed correctly, and these revenues are collected.

12.7.4. Infrastructure planning

It is recommended that this LTFP and a consolidated infrastructure investment plan be used as the basis for annual budgeting and updated when required. Furthermore, and

to ensure political buy-in, that the LTFP be submitted to Council for approval as part of the normal budget cycle.

It is recommended that the GLM implements a formalized system to track and manage the condition and ageing of infrastructure, to serve as input to the development of maintenance schedules as well as rehabilitation / renewal timelines.

12.8. CAPITAL FINANCING STRATEGIES

The municipality received a BFI grant to the value of R1.1 billion in FY2021/22, becoming the first non-metro municipality to receive such a grant. The receipt of this grant will facilitate considerable acceleration of the capital investment programme over the MTREF period. Notwithstanding this fact, the Base Case has adjusted the funding mix to incorporate increased levels of borrowing which as a result will alleviate pressures on cash reserves. It is our view that the funding mix presented in the Base Case is optimized.

Furthermore, it is recommended that the municipality implements an integrated plan which maintains the high collection rate and preserves cash reserves. When this is achieved, the capital investment programme can be accelerated in the medium to long-term through making use of a strategically designed funding mix which aims to strike a balance between external financing and cash reserves to supplement capital grant funding. The municipality is encouraged to explore the option of utilizing longer loan tenors to further assist with the municipality's liquidity position, as well as to consider the further acceleration of the external borrowing programme as presented in Chapter 11 of this report.

12.8.1. Fund a Capital Replacement Reserve ("CRR")

We recommend that the municipality makes use of its strong cash generation and healthy liquidity position to ensure that a CRR is cash backed and that tariffs are progressively increased to include a depreciation charge that can be used to fund a cash backed CRR, which in turn can be applied towards the funding of the replacement of ageing infrastructure.

10.8.2. Tariff Model

George LM has recently undergone a detailed tariff modelling process. The outcomes of the tariff assessment must be implemented as a priority to ensure that tariffs remain cost reflective. This must then be maintained going forward to ensure that cost-reflective tariffs remain the norm over the long-term.

12.9. **OPERATIONAL FINANCING STRATEGIES**

Operational efficiency will be maintained by ensuring the targeted collection rates are achieved and GLM is managing the underlying items of current assets and current liabilities optimally.

ANNEXURE 1: INDEPENDENT FINANCIAL ASSESSMENT AGAINST THE BACKGROUND OF GEORGE LOCAL MUNICIPALITY'S DEMOGRAPHIC, ECONOMIC & HOUSEHOLD INFRASTRUCTURE SITUATION

[SEE SEPARATE DOCUMENT]

ANNEXURE 2: BASE CASE SUMMARY PROJECTED FINANCIAL STATEMENTS

Municipal Financial Model

Statement of Financial Position

Model year	0	1	2	3	4	5	6	7	8	9	10
Financial year (30 June)	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**	**2032**
R thousands											
Non-current assets:	3 490 639	4 100 365	4 841 720	5 346 049	5 476 898	5 621 128	5 779 217	5 952 648	6 142 907	6 351 483	6 579 882
Property, plant and equipment	3 290 606	3 915 401	4 650 477	5 152 956	5 283 409	5 427 163	5 584 673	5 757 422	5 946 892	6 154 571	6 381 967
Intangible assets	1 249	3 369	5 018	6 123	6 519	6 995	7 574	8 256	9 045	9 942	10 945
Investment properties	144 073	141 624	145 601	146 346	146 346	146 346	146 346	146 346	146 346	146 346	146 346
Investments	–	–	–	–	–	–	–	–	–	–	–
Long-term receivables	50 476	36 387	36 387	36 387	36 387	36 387	36 387	36 387	36 387	36 387	36 387
Other non-current assets	4 235	3 584	4 236	4 236	4 236	4 236	4 236	4 236	4 236	4 236	4 236
Current assets:	874 709	839 168	779 726	885 262	1 023 508	1 157 227	1 287 889	1 426 161	1 593 149	1 782 858	1 997 475
Inventories	118 966	155 667	141 434	150 489	170 297	181 144	193 765	208 264	224 724	243 263	263 975
Trade and other receivables	163 210	122 765	122 765	122 765	122 765	122 765	122 765	122 765	122 765	122 765	122 765
Cash & Short term investments	592 533	560 735	515 526	612 007	730 446	853 318	971 359	1 095 132	1 245 660	1 416 830	1 610 735
TOTAL ASSETS	**4 365 348**	**4 939 533**	**5 621 446**	**6 231 311**	**6 500 407**	**6 778 355**	**7 067 105**	**7 378 810**	**7 736 056**	**8 134 341**	**8 577 357**
Municipal Funds:	3 408 698	3 714 017	4 155 813	4 383 642	4 636 083	4 896 986	5 173 844	5 477 396	5 818 321	6 205 871	6 651 016
Housing development fund & Other Cash Backed Reserves	35 873	50 271	42 434	34 940	34 940	34 940	34 940	34 940	34 940	34 940	34 940
Reserves (Not Cash Backed)	85 684	165 805	230 805	295 805	295 805	295 805	295 805	295 805	295 805	295 805	295 805
Accumulated surplus	3 287 141	3 497 942	3 882 574	4 052 897	4 305 339	4 566 241	4 843 099	5 146 651	5 487 577	5 875 127	6 320 271
Non-current liabilities:	189 947	650 657	891 621	1 203 334	1 186 147	1 160 536	1 127 150	1 097 723	1 058 223	1 001 190	975 870
Long-term liabilities (Interest Bearing)	171	405 386	652 534	970 115	937 852	894 108	838 696	783 267	713 713	622 534	559 001
Non-current provisions	189 776	245 271	239 087	233 219	248 295	266 427	288 454	314 456	344 510	378 656	416 869
Current liabilities:	766 703	574 859	574 012	644 335	678 176	720 834	766 111	803 691	859 512	927 280	950 472
Consumer deposits	40 744	42 632	44 628	46 770	49 042	51 540	54 366	57 556	61 136	65 177	69 731
Provisions	153 342	85 121	92 474	100 005	100 005	100 005	100 005	100 005	100 005	100 005	100 005
Trade and other payables	331 080	360 670	319 058	370 140	391 866	416 345	442 760	472 590	505 982	543 171	584 344
Bank overdraft	–	–	–	–	–	–	–	–	–	–	–
Current portion of interest bearing liabilities	241 537	86 437	117 852	127 419	137 263	152 943	168 980	173 540	192 389	218 928	196 391
TOTAL MUNICIPAL FUNDS AND LIABILTIES	**4 365 348**	**4 939 533**	**5 621 446**	**6 231 311**	**6 500 406**	**6 778 355**	**7 067 105**	**7 378 810**	**7 736 056**	**8 134 341**	**8 577 357**

Municipal Financial Model

Statement of Financial Performance

Model year	0	1	2	3	4	5	6	7	8	9	10
Financial year (30 June)	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**	**2032**
R thousands											
Revenue											
Property rates	347 220	370 046	398 423	429 224	462 700	488 777	519 268	554 246	593 758	637 910	686 724
Service Charges	1 221 984	1 304 658	1 213 300	1 547 433	1 679 984	1 789 348	1 902 925	2 031 527	2 175 839	2 336 946	2 515 750
Service charges - electricity	821 001	876 786	753 352	1 033 154	1 116 090	1 189 563	1 264 401	1 349 088	1 444 036	1 549 951	1 667 395
Service charges - water	166 795	168 540	172 840	196 376	211 886	221 744	230 812	241 137	252 718	265 558	279 652
Service charges - sanitation	129 151	143 018	158 335	175 318	194 126	208 483	224 846	243 371	264 207	287 564	313 630
Service charges - refuse	105 037	116 315	128 773	142 585	157 881	169 558	182 865	197 931	214 877	233 873	255 073
Service charges - other	–	0	(0)	(0)	(0)	(0)	(0)	(0)	(0)	(0)	(0)
Rental of facilities and equipment	5 257	4 935	5 025	5 326	5 735	6 159	6 642	7 189	7 805	8 495	9 265
Interest earned - external investments	15 419	38 515	31 962	24 230	26 083	34 063	42 720	51 410	60 495	71 030	82 588
Interest earned - outstanding debtors	9 637	11 061	9 837	10 681	12 603	14 375	16 156	18 010	19 934	21 923	23 967
Dividends received	12 183	–	–	–	–	–	–	–	–	–	–
Fines, penalties and forfeits	86 511	83 896	85 548	87 468	94 186	101 152	109 091	118 078	128 188	139 520	152 167
Licences and permits	1 622	3 863	4 094	4 339	4 697	5 088	5 561	6 120	6 769	7 510	8 346
Agency services	13 429	18 617	17 614	18 671	20 105	21 592	23 287	25 205	27 363	29 782	32 482
Transfers and subsidies (operating)	570 643	635 014	586 635	580 634	610 022	643 557	681 490	723 972	771 136	823 168	880 207
Other revenue	122 412	124 619	147 472	155 705	167 664	180 064	194 196	210 196	228 192	248 365	270 878
Gain on disposal of PPE	–	230 884	234 666	226 111	239 911	258 598	283 171	314 020	351 652	396 626	449 496
Revaluation of assets gain / (loss)	–	–	–	–	–	–	–	–	–	–	–
Total revenue before Capital Grants	2 406 317	2 826 108	2 734 575	3 089 822	3 323 688	3 542 772	3 784 507	4 059 974	4 371 129	4 721 274	5 111 869
Capital Grants	214 688	378 879	505 249	302 110	286 842	276 308	270 172	267 276	266 708	267 771	269 830
Public & developers contributions	–	–	–	–	–	–	–	–	–	–	–
Total Revenue after Capital Grants	2 621 005	3 204 987	3 239 824	3 391 932	3 610 530	3 819 080	4 054 679	4 327 249	4 637 837	4 989 045	5 381 699
Operating expenditure											
Employee related costs	599 156	701 455	758 167	797 823	843 793	895 799	954 083	1 018 890	1 090 457	1 168 994	1 254 670
Remuneration of councillors	23 783	27 930	27 479	28 853	30 083	31 485	33 062	34 812	36 735	38 829	41 093
Debt impairment	31 350	147 966	148 074	167 859	182 316	195 659	210 367	227 044	245 814	266 848	290 297
Depreciation and asset impairment	166 335	178 465	208 906	244 807	269 547	280 246	291 930	303 658	315 521	327 611	340 011
Finance charges	36 701	58 105	87 262	117 217	114 056	111 279	108 180	104 316	99 412	95 651	90 576
Bulk purchases	612 348	654 344	576 573	812 647	863 773	920 655	978 596	1 044 162	1 117 674	1 199 676	1 290 606
Inventory Consumed	88 752	143 224	96 999	103 041	106 683	113 695	122 332	132 689	144 827	158 826	174 741
Repairs and maintenance	–	–	–	–	–	–	–	–	–	–	–
Contracted services	534 461	726 430	640 830	631 068	646 819	688 440	735 176	787 374	845 360	909 600	980 500
Transfers and subsidies	87 691	45 265	19 800	17 833	18 888	20 092	21 465	23 015	24 751	26 686	28 833
Other expenditure	150 500	170 095	187 907	200 355	236 932	252 107	269 280	288 576	310 108	334 048	360 541
Loss on disposal of PPE	–	46 389	46 031	42 600	45 200	48 721	53 350	59 162	66 252	74 726	84 686
Total Expenditure	2 331 077	2 899 668	2 798 028	3 164 103	3 358 089	3 558 178	3 777 820	4 023 697	4 296 912	4 601 495	4 936 554
Suplus/ (Shortfall) for the year	**289 928**	**305 319**	**441 796**	**227 829**	**252 442**	**260 902**	**276 858**	**303 552**	**340 925**	**387 550**	**445 144**

Municipal Financial Model
Cash Flow Statement

Model year	0	1	2	3	4	5	6	7	8	9	10
Financial year (30 June)	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**	**2032**
R thousands											
Cash flows from Operating Activities											
Suplus/Deficit for the year including Capital Grants	289 928	305 319	441 796	227 829	252 442	260 902	276 858	303 552	340 925	387 550	445 144
Suplus/Deficit for the year excluding Capital Grants & Contributions		(73 560)	(63 453)	(74 281)	(34 400)	(15 406)	6 686	36 276	74 217	119 779	175 314
Capital Grants & Contributions		378 879	505 249	302 110	286 842	276 308	270 172	267 276	266 708	267 771	269 830
Adjustments for non-cash items:											
Depreciation, amortisation and impairment loss	166 335	178 465	208 906	244 807	269 547	280 246	291 930	303 658	315 521	327 611	340 011
Revaluation on investment property (gain) / loss	–	–	–	–	–	–	–	–	–	–	–
Increase / (Release from) current provisions & non-interest bearing liabilities	–	(68 221)	7 353	7 531	–	–	–	–	–	–	–
Increase / (Release from) other non-current provisions & non-interest bearing liabilities	–	55 495	(6 184)	(5 868)	15 077	18 132	22 027	26 002	30 054	34 146	38 213
(Increase) / Release from non-current interest bearing assets	–	–	–	–	–	–	–	–	–	–	–
Capitalised interest	–	–	–	–	(0)	(0)	(0)	(0)	(0)	(0)	(0)
Operating surplus before working capital changes:	456 263	471 058	651 871	474 299	537 065	559 280	590 815	633 212	686 501	749 307	823 369
Change in W/C Investment	–	33 334	(27 379)	42 028	1 916	13 634	13 794	15 331	16 932	18 650	20 461
(Increase)/decrease in inventories	–	(36 701)	14 233	(9 055)	(19 809)	(10 846)	(12 621)	(14 499)	(16 460)	(18 539)	(20 712)
(Increase)/decrease accounts receivable	–	40 445	(0)	(0)	(0)	0	0	(0)	0	(0)	(0)
Increase/(decrease) in trade payables	–	29 590	(41 612)	51 082	21 725	24 480	26 415	29 830	33 392	37 189	41 173
Net cash flow from Operating activities	456 263	504 392	624 492	516 327	538 981	572 914	604 609	648 543	703 432	767 956	843 830
Cash flows from Investing Activities											
Capital expenditure	–	(804 226)	(945 742)	(748 391)	(401 105)	(424 476)	(450 018)	(477 089)	(505 780)	(536 187)	(568 411)
Decrease/(Increase) in non-current receivables	–	14 740	(652)	–	–	–	–	–	–	–	–
(Additions) / Disposals of investment property	–	1 295	(3 866)	(745)	709	–	–	–	–	–	–
Net cash flow from Investing activities	–	(788 191)	(950 261)	(749 136)	(400 396)	(424 476)	(450 018)	(477 089)	(505 780)	(536 187)	(568 411)
Cash flows from Financing Activities											
New loans raised	–	312 312	365 000	445 000	105 000	109 200	113 568	118 111	122 835	127 749	132 858
Loans repaid	–	(62 198)	(86 437)	(117 852)	(127 419)	(137 263)	(152 943)	(168 980)	(173 540)	(192 389)	(218 928)
(Decrease) / Increase in consumer deposits	–	1 888	1 996	2 142	2 272	2 498	2 826	3 189	3 580	4 041	4 555
Net cash flow from Financing activities	–	252 002	280 560	329 291	(20 148)	(25 565)	(36 549)	(47 680)	(47 124)	(60 600)	(81 514)
Change in Cash	456 263	(31 797)	(45 209)	96 481	118 438	122 872	118 041	123 773	150 528	171 170	193 905
Cash/(Overdraft), Beginning		592 533	560 735	515 526	612 007	730 446	853 318	971 359	1 095 132	1 245 660	1 416 830
Cash/(Overdraft), Ending	**592 533**	**560 735**	**515 526**	**612 007**	**730 446**	**853 318**	**971 359**	**1 095 132**	**1 245 660**	**1 416 830**	**1 610 735**

ANNEXURE 3: RATIO ANALYSIS

YEAR			2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
FINANCIAL POSITION												
ASSET MANAGEMENT												
R29	Capital Expenditure / Total Expenditure	10% - 20%	21,7%	25,3%	19,1%	10,7%	10,7%	10,6%	10,6%	10,5%	10,4%	10,3%
R27	Repairs and Maintenance as % of PPE and Investment Property	8%	5,2%	4,1%	3,8%	4,0%	4,1%	4,3%	4,4%	4,6%	4,7%	4,9%
DEBTORS MANAGEMENT												
R4	Gross Consumer Debtors Growth		13,7%	10,9%	12,8%	12,2%	11,5%	10,9%	10,4%	10,1%	9,8%	9,7%
R5	Payment Ratio / Collection Rate	95%	95,4%	95,3%	95,3%	95,3%	95,2%	95,2%	95,1%	95,1%	95,1%	95,0%
	Net Debtors Days	30	41	39	40	33	30	28	27	25	23	22
LIQUIDITY MANAGEMENT												
R49	Cash Coverage Ratio (excl. Working Capital)		2,2 : 1	1,9 : 1	2,6 : 1	3,1 : 1	3,6 : 1	4,1 : 1	4,6 : 1	5,1 : 1	5,7 : 1	6,4 : 1
R50	Cash Coverage Ratio (incl. Working Capital)		1,2 : 1	1,1 : 1	1,3 : 1	1,5 : 1	1,7 : 1	1,9 : 1	2,1 : 1	2,2 : 1	2,4 : 1	2,6 : 1
R51	Cash Surplus / Shortfall on Minimum Liquidity Requirements		R 86,2 m	R 43,2 m	R 147,9 m	R 253,5 m	R 360,7 m	R 460,6 m	R 563,4 m	R 690,3 m	R 834,7 m	R 999,2 m
R1	Liquidity Ratio (Current Assets : Current Liabilities)	1:1.5 - 1:2.1	1,5 : 1	1,4 : 1	1,4 : 1	1,5 : 1	1,6 : 1	1,7 : 1	1,8 : 1	1,9 : 1	1,9 : 1	2,1 : 1
LIABILITY MANAGEMENT												
R45	Debt Service as % of Total Operating Expenditure	6% - 8%	4,1%	6,2%	7,4%	7,2%	7,0%	6,9%	6,8%	6,4%	6,3%	6,3%

YEAR			2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
R6	Total Debt (Borrowings) / Operating Revenue	45%	17,4%	28,2%	35,5%	32,3%	29,6%	26,6%	23,6%	20,7%	17,8%	14,8%
R7	Repayment Capacity Ratio		1,10	1,43	2,75	2,53	2,27	2,03	1,76	1,50	1,25	1,00
R46	Debt Service Cover Ratio (Cash Generated by Operations / Debt Service)		4,2 : 1	3,6 : 1	2,2 : 1	2,2 : 1	2,3 : 1	2,3 : 1	2,4 : 1	2,6 : 1	2,7 : 1	2,7 : 1
SUSTAINABILITY												
	Net Financial Liabilities Ratio	< 60%	13,7%	25,1%	31,1%	25,3%	20,4%	16,0%	11,7%	7,4%	3,1%	-1,4%
	Operating Surplus Ratio	0% - 10%	-2,6%	-2,3%	-2,4%	-1,0%	-0,4%	0,2%	0,9%	1,7%	2,5%	3,4%
	Asset Sustainability Ratio	> 90%	54,3%	37,0%	21,6%	20,7%	21,2%	21,5%	21,9%	22,4%	22,8%	23,3%
FINANCIAL PERFORMANCE												
EFFICIENCY												
R42	Net Operating Surplus / Total Operating Revenue	>= 0%	-2,6%	-2,3%	-2,4%	-1,0%	-0,4%	0,2%	0,9%	1,7%	2,5%	3,4%
R43	Electricity Surplus / Total Electricity Revenue	0% - 15%	25,4%	23,5%	21,3%	22,6%	22,6%	22,6%	22,6%	22,6%	22,6%	22,6%
R44	Water Surplus / Total Water Revenue	>= 0%	97,5%	97,6%	97,7%	97,7%	97,7%	97,7%	97,7%	97,7%	97,7%	97,7%
REVENUE MANAGEMENT												
R8	Increase in Billed Income p.a. (R'm)		R 105,2 m	-R 62,9 m	R 365,2 m	R 166,4 m	R 135,9 m	R 144,6 m	R 164,1 m	R 184,4 m	R 205,9 m	R 228,4 m
R9	% Increase in Billed Income p.a.	CPI	6,7%	-3,7%	22,6%	8,4%	6,3%	6,3%	6,8%	7,1%	7,4%	7,7%
R12	Operating Revenue Growth %	CPI	17,4%	-3,2%	13,0%	7,6%	6,6%	6,8%	7,3%	7,7%	8,0%	8,3%
R14	Contribution per Income Source: Equitable Share		6,8%	7,7%	7,4%	7,3%	7,3%	7,4%	7,4%	7,4%	7,4%	7,4%

YEAR			2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
R15	Contribution per Income Source: Conditional Operating Grants		15,6%	13,7%	11,4%	11,0%	10,8%	10,6%	10,5%	10,2%	10,0%	9,8%
R16	Contribution per Income Source: Property Rates		13,1%	14,6%	13,9%	13,9%	13,8%	13,7%	13,7%	13,6%	13,5%	13,4%
R17	Contribution per Income Source: Electricity Services		31,0%	27,5%	33,4%	33,6%	33,6%	33,4%	33,2%	33,0%	32,8%	32,6%
R18	Contribution per Income Source: Water Services		6,0%	6,3%	6,4%	6,4%	6,3%	6,1%	5,9%	5,8%	5,6%	5,5%
R19	Contribution per Income Source: Interest on Investments		1,4%	1,2%	0,8%	0,8%	1,0%	1,1%	1,3%	1,4%	1,5%	1,6%
R20	Annual Increase per Income Source: Equitable Share		13,5%	8,9%	8,6%	6,3%	6,8%	7,2%	7,6%	7,9%	8,2%	8,4%
R21	Annual Increase per Income Source: Property Rates		6,6%	7,7%	7,7%	7,8%	5,6%	6,2%	6,7%	7,1%	7,4%	7,7%
R22	Annual Increase per Income Source: Electricity Services		6,8%	-14,1%	37,1%	8,0%	6,6%	6,3%	6,7%	7,0%	7,3%	7,6%
R23	Annual Increase per Income Source: Water Services		1,0%	2,6%	13,6%	7,9%	4,7%	4,1%	4,5%	4,8%	5,1%	5,3%
R24	Annual Increase per Income Source: Interest on Investments		149,8%	-17,0%	-24,2%	7,7%	30,6%	25,4%	20,3%	17,7%	17,4%	16,3%
R47	Cash Generated by Operations / Own Revenue		23,0%	29,1%	20,6%	19,9%	19,8%	19,5%	19,4%	19,5%	19,7%	19,9%
R48	Cash Generated by Operations / Total Operating Revenue		17,8%	22,8%	16,7%	16,2%	16,2%	16,0%	16,0%	16,1%	16,3%	16,5%
EXPENDITURE MANAGEMENT												
	Creditors Payment Period	30	35	29	43	53	55	56	58	59	61	62
R30	Contribution per Expenditure Item: Staff Cost (Salaries, Wages and Allowances)	25% - 40%	19,7%	21,0%	21,1%	23,2%	23,3%	23,3%	23,4%	23,5%	23,5%	23,5%
	Contribution per Expenditure Item: Contracted Services	2% - 5%	19,6%	17,1%	16,1%	17,2%	17,3%	17,4%	17,5%	17,6%	17,7%	17,8%
R31	Contribution per Expenditure Item: Electricity Services		17,7%	15,4%	20,8%	23,0%	23,1%	23,1%	23,2%	23,3%	23,4%	23,4%

YEAR			2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
R32	Contribution per Expenditure Item: Water Services		0,1%	0,1%	0,1%	0,1%	0,1%	0,1%	0,1%	0,1%	0,1%	0,1%
R33	Contribution per Expenditure Item: Repairs & Maintenance		5,7%	5,2%	5,2%	5,7%	5,8%	5,8%	5,8%	5,8%	5,8%	5,8%
R34	Contribution per Expenditure Item: Depreciation and Asset Impairment		4,8%	5,6%	6,3%	7,2%	7,0%	6,9%	6,7%	6,6%	6,4%	6,2%
R35	Contribution per Expenditure Item: External Interest Charged		1,6%	2,3%	3,0%	3,0%	2,8%	2,6%	2,3%	2,1%	1,9%	1,6%
R36	Annual Increase per Expenditure Item: Staff Cost (Salaries, Wages and Allowances)		17,1%	7,7%	5,2%	5,7%	6,1%	6,5%	6,7%	7,0%	7,2%	7,3%
R37	Annual Increase per Expenditure Item: Electricity Services		6,9%	-11,9%	40,9%	6,3%	6,6%	6,3%	6,7%	7,0%	7,3%	7,6%
R38	Annual Increase per Expenditure Item: Water Services		-1,1%	-0,1%	9,7%	3,7%	5,1%	4,6%	5,0%	5,3%	5,6%	5,8%
R39	Annual Increase per Expenditure Item: Repairs & Maintenance		22,9%	-8,4%	3,6%	6,6%	6,6%	6,7%	6,7%	6,8%	6,9%	7,0%
R40	Annual Increase per Expenditure Item: Depreciation		7,3%	17,1%	17,2%	10,1%	4,0%	4,2%	4,0%	3,9%	3,8%	3,8%
R41	Annual Increase per Expenditure Item: External Interest Charged		58,3%	50,2%	34,3%	-2,7%	-2,4%	-2,8%	-3,6%	-4,7%	-3,8%	-5,3%
GRANT DEPENDENCY												
R10	Total Grants / Total Revenue		31,6%	33,7%	26,0%	24,8%	24,1%	23,5%	22,9%	22,4%	21,9%	21,4%
R11	Own Source Revenue to Total Operating Revenue		77,5%	78,5%	81,2%	81,6%	81,8%	82,0%	82,2%	82,4%	82,6%	82,8%
	Capital Grants to Total Capital Expenditure		47,1%	53,4%	40,4%	71,5%	65,1%	60,0%	56,0%	52,7%	49,9%	47,5%

These ratios are calculated from the output of the model and can at best only approximate the calculation based on actual accounts.

DEFINITIONS	
Liquidity Ratios	
Current Ratio	*Current Assets / Current Liabilities*
Quick Liquidity Ratio	*(Current Assets - Debtors > 30 days) / Current Liabilities*
Minimum Liquidity Level (or Cost Coverage)	*((Cash and Cash Equivalents - Unspent Conditional Grants - Overdraft) + Short Term Investment) / Monthly Fixed Operational Expenditure excluding (Depreciation, Amortisation, Provision for Bad Debts, Impairment and Gain and Loss on Disposal of Assets)*
Overdraft to Total Income	*Overdraft / Total Operating Revenue*
Operational Ratios	
Accounting Surplus	*Total Operating Revenue + Conditional Grants - Total Operating Expenditure*
Cash Operating Surplus	*Total Operating Revenue - Total Operating Expenditure + Working Capital*
Cash from Operations as a % of own Revenue	*Operating Cash / Operating Revenue*
Repairs and Maintenance to PPE	*Total Repairs and Maintenance Expenditure / Carrying Value of PPE x 100*
Debtors Payment Ratio	*(Gross Debtors Closing Balance + Billed Revenue - Gross Debtors Opening Balance + Bad Debts Written Off) / Billed Revenue x 100*
Staff Costs	*Remuneration (Employee Related Costs and Councillors' Remuneration) / Total Operating Expenditure x 100*
External Gearing Ratios	
External Loan Liability Paid Coverage Ratio	*(Total Operating Revenue - Total Operating Expenditure (excluding non-cash items)) / Capital Cost (Interest Paid and Redemption)*
External Interest and Capital Paid to Total Expenditure	*Capital Cost (Interest Paid and Redemption) / Total Operating Expenditure x 100*
External Gearing Ratio (or Debt as a % of Own Revenue)	*(Overdraft + Current Finance Lease Obligation + Non-Finance Lease Obligation + Short Term Borrowings + Long Term Borrowings) / Total Operating Revenue*
Other Ratios	
Level of Grant Dependency	*(Total Grants) / (Total Operating Revenue)*
Operating Surplus Ratio	*(Operating Revenue - Operating Expenditure) / Operating Revenue*
Net Financial Liabilities Ratio	*(Total Liabilities - Current Assets) / Operating Revenue (excl Capital Grants)*
Asset Sustainability Ratio	*Capex for Replacement / Depreciation*

ANNEXURE 4: VIABILITY FRAMEWORK

1. A proposed framework is provided below, within which to manage liquidity, operational performance and external gearing and is aligned to MFMA Circular No. 71.

2. The municipality is advised to include these ratios in the relevant revised financial policies:

Liquidity Ratios

3. Standard Liquidity Ratio (The ability to fully provide for current liabilities with current assets.)

   Minimum norm: 1:1
   Healthy norm: 2:1
   MFMA norm: 1.5 – 2:1

4. Quick Liquidity Ratio (The ability to provide for current liabilities with liquid current assets therefore current assets including only 30-day debtors.)

   Minimum norm: 1:1
   Healthy norm: 2:1
   MFMA norm: None

5. Minimum Liquidity Level (Holding sufficient cash and investments to fully provide for the sum of unspent conditional grants, short term provisions, ceded investments, cash backed reserves and provisions and at least one month of operating expenditure (excluding non-cash expenses).

   Minimum norm: 1:1
   Healthy norm: 1:1 plus an additional month's operational expenditure
   MFMA norm: 1 – 3 months

   MFMA calculation excludes cash backed reserves and short-term provisions; however, an additional ratio is stipulated in Circular 71 regarding the Level of Cash Backed Reserves.

6. Overdraft to Total Income (Preferably a municipality should not have an overdraft facility at all at year end, however, should an overdraft facility be used it should not exceed 5% of Total Income.)

   Maximum norm: 5%
   Healthy norm: 0%
   MFMA: None

7. Other ratios as stipulated below are to be managed at levels applicable to the Municipality and although industry benchmarks exist it is more prudent to set objectives given the current financial context of the Municipality. The following ratios are recommended for consideration, and it would be prudent to report hereon on a quarterly basis to the Finance Committee:

Operational Ratios

8. Total Accounting Surplus (The ability to post an accounting operational surplus where Total Income exceeds Total Expenditure with a positive margin.)

   Minimum norm: Break-even of the above calculation
   Healthy norm: Positive margin that is maintained
   MFMA norm: Break-even or >0

9. Cash Operating Surplus (The ability to generate surplus cash from operational performance therefore Total Income less conditional transfers less total expenditure excluding non-cash items adjusted for changes in working capital should be positive.)

   Minimum norm: Break-even of the above calculation
   Healthy norm: Positive margin that is maintained
   MFMA norm: None

10. Repairs and maintenance to Total Expenditure (The ability of the municipality to effectively maintain the infrastructure assets from which it derives its primary income.)

    Minimum norm: 5%
    Healthy norm: 7%
    MFMA norm: 8%

    MFMA calculation differs in using the Property, Plant and Equipment (carrying value) as the base of the ratio instead of Total Expenditure.

11. Consumer Collection Levels (For a municipality to maintain its viability it should maintain its collection levels at least above 90%. Growth in gross consumer debtors including debts written off in the financial year as a percentage of billed income including equitable share, will provide the non-collection level therefore the difference will indicate the consumer collection level.)

    Minimum norm: 90%
    Healthy norm: 95%+
    MFMA norm: 95%

12. Staff Costs, Allowances and Wages (The level of staff costs, allowances and wages to total operational expenditure needs to be effectively managed to ensure that costs aren't considered too high, but also that the municipality is not under capacitated and employment levels are too low.)

    Minimum norm: 25%
    Healthy norm: 25% to 30%
    MFMA norm: 25% to 40%

External Gearing Ratios

13. Proposed External Gearing ratios are subject to Liquidity ratios being within recommended levels.

14. External Loan Liability Paid Coverage Ratio (The ability to at least cover the External Interest and Capital Payable with the cash generated from operations before interest.)

    Minimum norm: 1:1
    Healthy norm: 2:1
    MFMA norm: None

15. External Interest and Capital Paid to Total Expenditure (The percentage of Total Expenditure Utilized to service external loan repayments.)

    Maximum norm: 10%
    Healthy norm: 7.5%
    MFMA norm: 6% - 8%

16. External Gearing Ratio (The level to which the municipality has geared itself is calculated as Total External Interest-Bearing Debt as a percentage of Total Income less conditional grant funding.)

    Maximum: 40%
    Healthy norm: 35%
    MFMA norm: 45%

ANNEXURE 5: ASSETS EARMARKED FOR REPLACEMENT

The asset register of the municipality was analysed mechanistically (without engineering judgement) and a replacement schedule of the Annual Replacement Cost ("ARC") of different asset classes was determined. This was done with reference to the information in the municipality's asset register. Asset categories such as "Investment Property", "Land" and "Heritage Assets" were excluded from the assessment. The values in the Tables below are in nominal Rand values, escalated to the date of replacement.

TABLE 5.1: GEORGE LM: ESTIMATED ANNUAL REPLACEMENT COST AS EXTRACTED FROM THE ASSET REGISTERS (RM NOMINAL)

#	DESCRIPTION	TOTAL	2021/22 and before	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30	2030/31	2031/32
1	Heritage assets	**0.0**	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
2	Intangible assets	**14.9**	0.00	0.35	1.61	1.77	1.41	3.96	2.14	1.20	2.34	0.00	0.10
3	Investment property	**0.0**	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
4	PPE - Community assets	**474.1**	39.92	8.92	22.78	63.96	33.30	66.59	19.31	31.65	162.47	18.62	6.59
5	PPE - Computer equipment	**142.5**	2.78	3.91	12.38	17.44	16.66	12.39	5.35	16.96	14.95	22.69	16.98
6	PPE - Furniture and office equipment	**76.9**	0.01	2.21	6.53	15.82	11.20	4.25	4.46	6.54	7.96	3.71	14.21
7	PPE - Infrastructure: Electricity	**2 465.7**	237.35	24.23	86.42	238.66	106.61	52.51	64.08	61.11	1 531.25	31.46	31.98
8	PPE - Infrastructure: Roads, pavements, bridges	**3 301.2**	246.40	44.35	418.40	1 013.94	217.51	105.41	92.43	143.58	111.98	126.67	780.53
9	PPE - Infrastructure: Storm water	**476.2**	163.22	0.00	30.58	47.69	14.42	32.24	11.95	47.88	27.86	89.83	10.51
10	PPE - Infrastructure: Waste management	**112.5**	42.41	0.00	0.42	28.62	3.21	2.61	0.00	2.84	29.76	0.00	2.60
11	PPE - Infrastructure: Waste Water management	**1 712.1**	409.31	24.27	45.37	97.24	40.70	130.42	117.85	157.47	591.01	79.19	19.23
12	PPE - Infrastructure: Water	**2 587.3**	515.92	23.04	52.54	124.71	52.06	192.12	201.25	206.68	871.93	330.36	16.71
13	PPE - Land	**0.0**	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
14	PPE - Machinery and equipment	**492.9**	81.35	8.40	31.18	85.62	22.72	44.12	12.89	45.70	61.72	20.46	78.74
15	PPE - Other assets	**343.7**	47.62	3.40	90.51	73.19	63.66	15.10	7.05	17.32	13.38	4.50	8.02
16	PPE - Transport assets	**669.1**	7.15	309.05	71.87	38.97	7.21	20.74	1.60	23.95	15.57	78.36	94.63
	TOTAL	**12 869.0**	**1 793.4**	**452.1**	**870.6**	**1 847.6**	**590.7**	**682.5**	**540.4**	**762.9**	**3 442.2**	**805.8**	**1 080.8**

We have amended the estimated replacement costs. This was achieved by:

- Assuming that the actual remaining life of assets will exceed the life recorded for some of the assets in the asset register,
- Assuming that only a percentage of assets will be replaced when their estimated useful life expires,
- Spreading replacement not done in the past over several future years, and
- Smoothing the constant 2022 value over the Planning Period and reverting these backs to nominal values.

The outcome of this analysis is presented in the Table below:

TABLE 5.2: GEORGE LM: SPREAD, REVISED, REDUCED AND SMOOTHED ESTIMATED ASSET REPLACEMENT COST (RM NOMINAL)

			1	2	3	4	5	6	7	8	9	10
	TOTAL	***2022 and before***	***2023***	***2024***	***2025***	***2026***	***2027***	***2028***	***2029***	***2030***	***2031***	***2032***
ARC (Rm Nominal) Original	**12 869.0**	1 793.4	452.1	870.6	1 847.6	590.7	682.5	540.4	762.9	3 442.2	805.8	1 080.8
ARC (Rm Nominal) Revised & Spread	**10 829.9**		628.9	971.0	1 766.5	744.8	827.1	509.8	688.9	3 049.6	729.8	913.4
ARC (Rm Constant 2022)	**7 440.7**		587.8	848.1	1 442.0	568.2	589.7	339.7	429.0	1 774.9	397.0	464.3
ARC (Rm Constant)(Smoothed)	**7 440.7**		744.1	744.1	744.1	744.1	744.1	744.1	744.1	744.1	744.1	744.1
ARC (Rm Nominal)(Smoothed)	**11 000.0**		796.2	851.9	911.5	975.3	1 043.6	1 116.6	1 194.8	1 278.5	1 367.9	1 463.7

Long Term Financial Plan

This Policy is effective from the date of approval by the Council, as per the approved system of Delegations of the George Municipality.

Signed at GEORGE on the **day** of 12 **June 2023.**

DR MR GRATZ
MUNICIPAL MANAGER