Cape Agulhas Municipality

Long Term Financial Plan – ***Update 2020***

Prepared by
INCA Portfolio Managers
November 2020

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Report Overview – Introduction and Background

The Cape Agulhas Municipality appointed INCA Portfolio Managers in 2014 to prepare a Long-Term Financial Plan. The report entitled Cape Agulhas Local Municipality Long Term Financial Plan: 2015 – 2024; was prepared in June 2014. Since then the report has been updated annually with the latest available information. This 2020 Update aims to review the conclusions reached between 2015 - 2019 based on the most recent information and report on the findings.

The objective 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 and the environment in which it operates.

A summary of the demographic-, economic- and household infrastructure perspective was updated with the latest available information as published by iHS Global Insight. The historic financial analysis was updated with the information captured in the municipality's financial statements of 30 June 2020 along with the adopted MTREF budget for 2020/21. IPM adapted its Long-Term Financial Model to include and project some effects of the Covid-19 pandemic. This adapted model was populated and run with this latest information, and the outcome thereof is reported herein. The model was re-calibrated against the municipality's MTREF for the 3 years from 2020/21 to 2022/23.

As with all the Update Reports we did not renew the analysis of the Asset Register, nor review municipal documents (viz. IDP, Master Plans, etc.) and no conversations with management were undertaken. The conclusions reached in this report are complimentary to the recommendations made previously.

KEY FINDINGS AND CONCLUSIONS DRAWN FROM THE 2020 LTFP 1ST PHASE UPDATE

Cape Agulhas LM's financial position remained sound despite Covid-19 related challenges. The LTFM, however includes proposals to be implemented to safeguard the financial sustainability of the municipality.

The historical financial analysis of Cape Agulhas LM shows:

- A liquidity ratio of 1.89 (above the norm of 1.5)
- A gearing ratio of 8%
- A positive cash coverage ratio of 1.36 including 1 month's working capital
- A lower collection ratio of 94% that is below the norm of 95%
- A decrease in cash and cash equivalents.
- Staff costs that represent more than 40% of total operating expenditure
- Insufficient coverage for debtors older than 90+ days.
- A minimum liquidity shortfall of R 7.4 million i.e. Cape Agulhas cannot cover its minimum liquidity requirements which include unspent conditional grants, short term provisions, funds, reserves and trust funds (cash backed) and working capital provision (one month's operating expenditure). This highlights the need to provide for between 1 and 3 months' operating expenses.

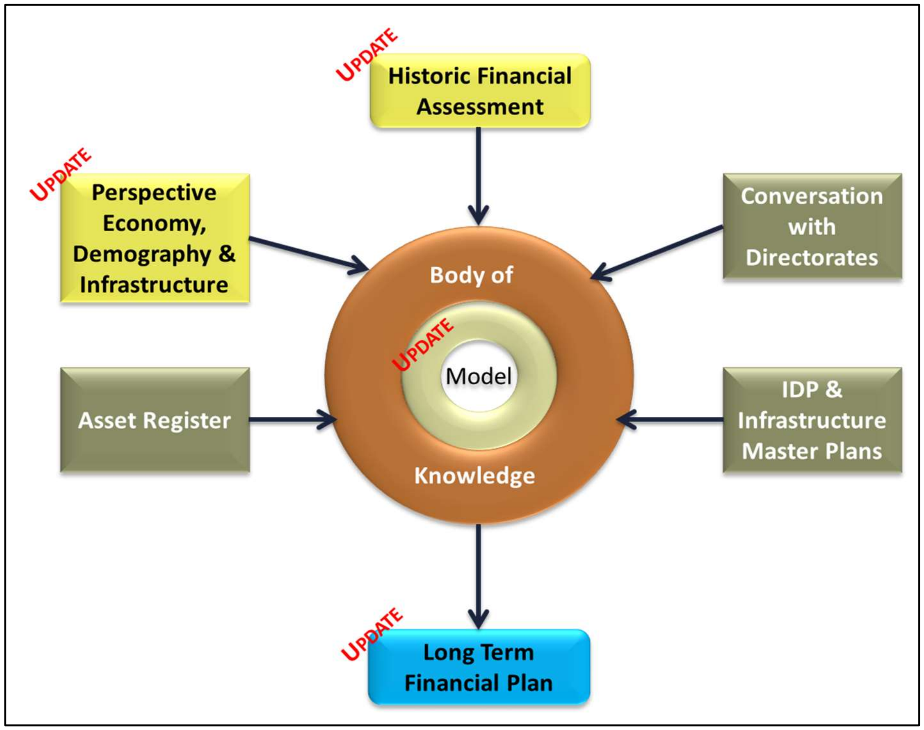
Long term financial planning:

- The MTREF reflects the view of declining profitability, lower levels of cash generated by operations and a deterioration of the cash balances due to the low collection rate and the negative impact of Covid-19 on the households' ability to pay for municipal services.
- The LTFM builds an optimal financial scenario by implementing certain recommendations which among others include a reduction of the operational budget by R4 million per year between 2021 and 2024, adjusting the capital funding mix by borrowing more, and extending the loan tenure from an average of 10 years to 13 years. Under the optimal financial scenario, Cape Agulhas can afford to accelerate the reduced 10-year capital programme of R 503 million (compared to R617 million on the previous update). Maintaining healthy liquidity levels and bank balances sufficient to cover statutory requirements and 1 month's working capital for the duration of the planning period.
- The positive outlook reflected in this report remains subject to prudent financial management and discipline by Cape Agulhas

PLANNING PROCESS

The diagram below illustrates the steps in the process that were followed during the original drafting of the LTFP in 2015 and the steps during the subsequent "Updates":

FIGURE 1: PLANNING PROCESS

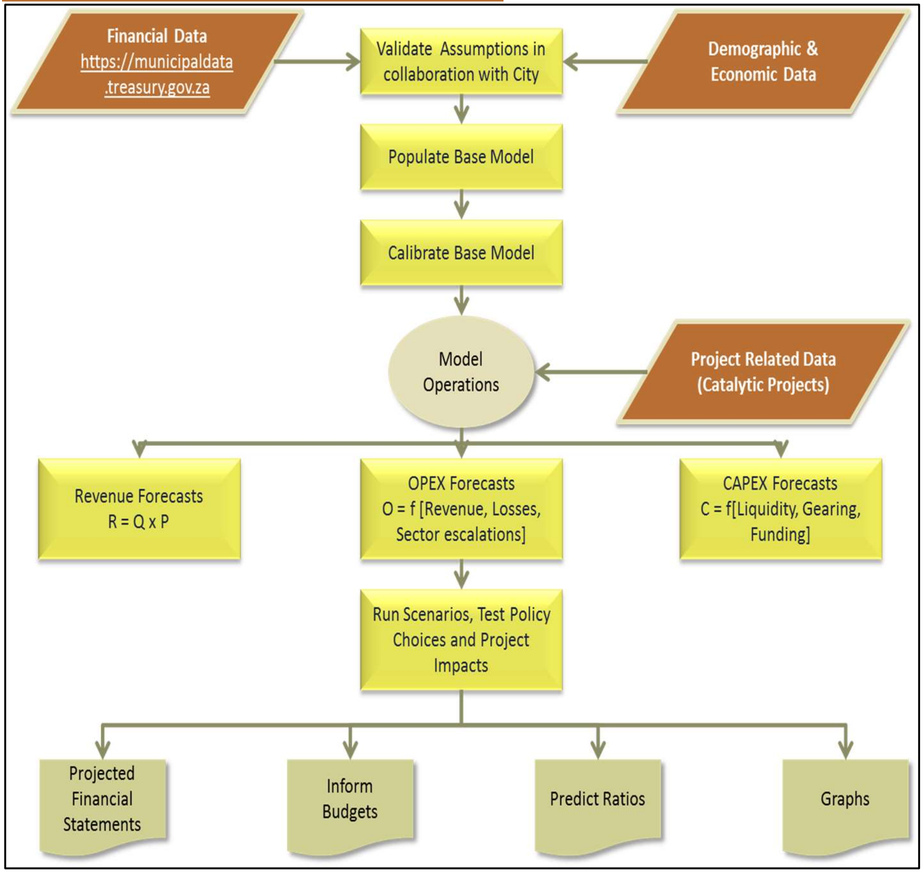


IPM's Long Term Financial Model was populated with the latest information to provide us with a base model on which this update is based.

The diagram below illustrates the outline of the model

The model methodology remains the same and the capital budget as presented in the MTREF was utilised and forecasts of an affordable future capex were made.

FIGURE 2: FINANCIAL MODEL FRAMEWORK



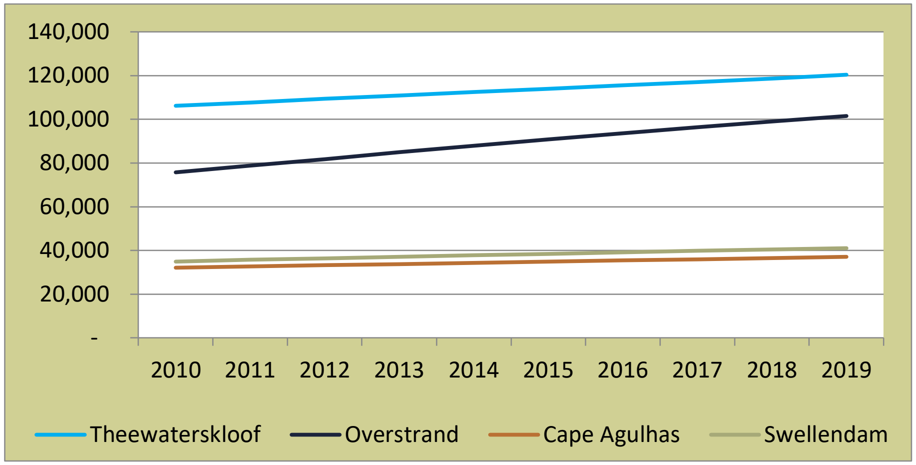
UPDATED PERSPECTIVES – DEMOGRAPHIC, ECONOMIC, HOUSEHOLD INFRASTRUCTURE

DEMOGRAPHY

Cape Agulhas has a ***total population*** of 37 082 (iHS 2019), which represents 12.4% of people living in the Overberg district and is the least densely populated municipality in the district. The population is growing at 1.41%. Compared to the district and province, this is quite low, with growth rates of 1.79% and 1.88% respectively. This relatively low population growth rate may have negative impact on revenue growth, but it supports the municipality in its backlog eradication efforts by limiting the growth in demand for services

The population growth in Cape Agulhas should, however, be considered against the backdrop of a well-functioning local economy, but it has to be noted that a marginal decline was observed annually over the last four years.

GRAPH 1: POPULATION

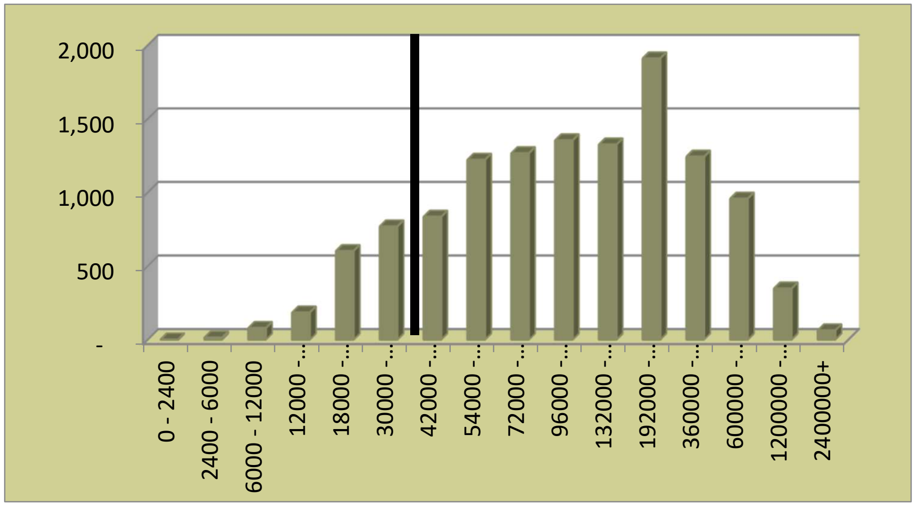


One can reasonably expect that, under normal circumstances, this could lead to a reduction of GVA (Gross Value Add or local GDP) per capita in Cape Agulhas which in turn could negatively impact on household income over the longer term.

However, the population growth rate is partially attributable to an influx of higher income earners to the Struisbaai area. This should have an inverse effect of the expectation under normal circumstances, and an increase in over-all GVA in the area might be observed over the medium-term.

The ***average household income*** came to R 290 348.58, which remains the highest in the district from 2016 and is considerably higher than the national average of R 210 514.06.

GRAPH 2: DISTRIBUTION OF HOUSEHOLD INCOME

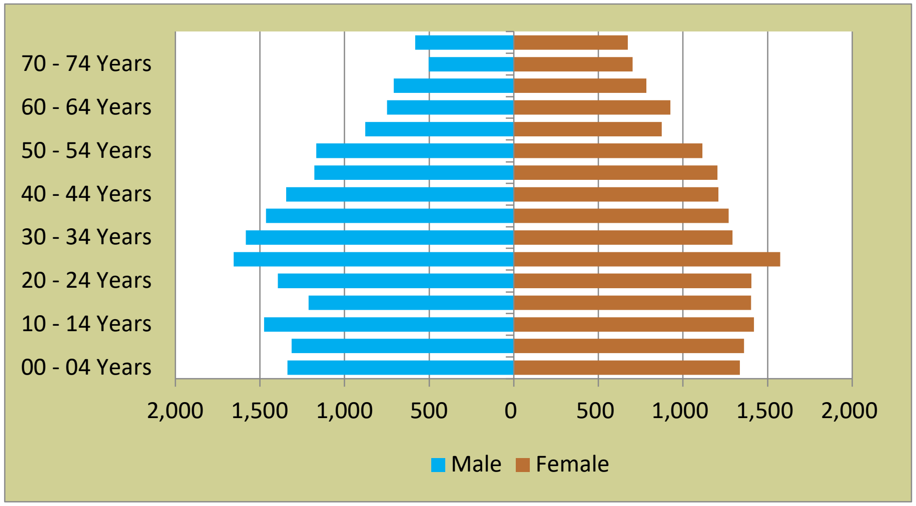


The ***household income distribution*** illustrates that only 13.9% of households earn less than R 42 000 p.a.

Households earning less than R42 000 p.a. is indicative of the number of indigent household in the municipal area and reflect those who qualify for and/or are largely reliant on government grants as source of income.

The provision of RDP level of basic services to these households are theoretically covered by the equitable share, that should compensate the municipality for providing free basic services.

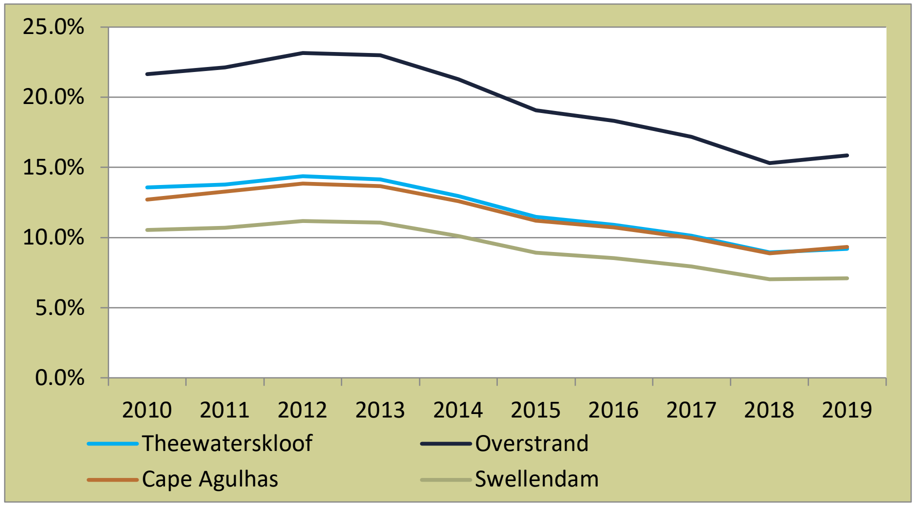
GRAPH 3: AGE PROFILE



Unlike a typical "pine tree" population pyramid associated with developing societies, the ***age profile*** of Cape Agulhas illustrates proportionally fewer people in the category of people younger than 20 years of age. This may be as a result of a decline in the population rate of growth vs the proportionally high number of retirees the area attracts.

The majority of the population (52.5%) are between the ages of 25-64 years. The percentage of economically active population in Cape Agulhas is the highest in the district with 48.77% compared to Theewaterskloof (47.5%) Overstrand (44.03%) and Swellendam (43.5%). This suggests that people perceive the area to be economically progressive and to provide job opportunities.

GRAPH 4: UNEMPLOYMENT RATE



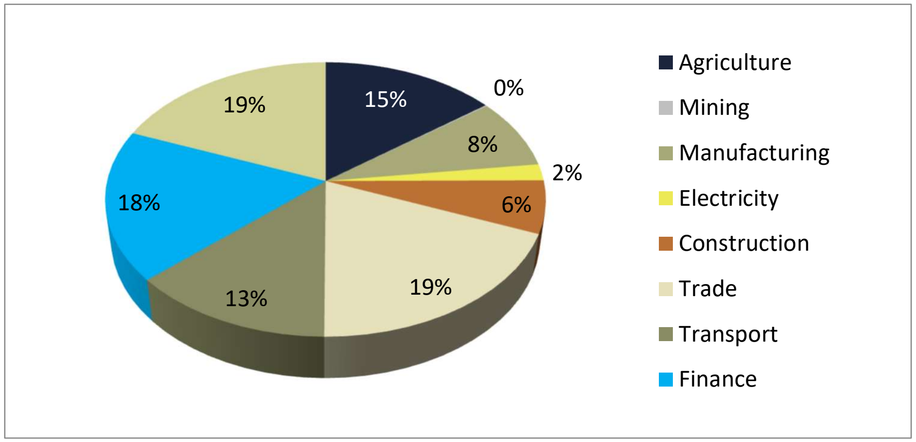
The 2019 ***Unemployment Rate*** is estimated to be around 9.3%, that is substantially lower than the unemployment rate in the Western Cape of 20.5%, as well as the official national unemployment rate of 28.2%.

These key demographic characteristics reflected on indicate towards a stable, lower risk society residing in Cape Agulhas, which in turn might lead to a more stable collection base and contribute to the financial stability and sustainability of the municipality.

ECONOMY

The economy experienced a second consecutive contraction and was the lowest since 2015. Cape Agulhas had a total GVA of R 2.15 billion, down 1.3% from 2019.

GRAPH 5: ECONOMIC SECTORS



The economy of the municipality is relatively diversified. Trade and Community services remain the dominant ***economic sectors*** both with 19% of the output in 2019, followed by Finance (18%) Agriculture (15%) and Transport (13%). Together these five subsectors comprise more than 83% of economic output.

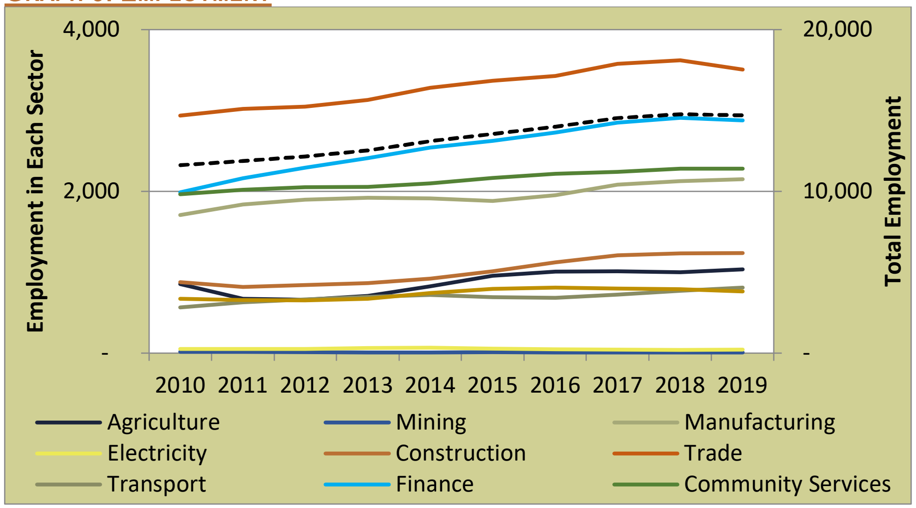
TABLE 1: PROPORTIONAL GROWTH OF ECONOMIC SECTORS

Subsector	2010	2019
Agriculture	16.8%	14.6%
Mining	0.1%	0.1%
Manufacturing	8.9%	8.3%
Electricity	2.5%	1.9%
Construction	6.5%	6.2%
Trade	18.7%	19.0%
Transport	12.6%	13.2%
Finance	15.8%	17.7%
Community Services	18.0%	18.9%

The stable nature and function of the area is reflected in the proportional growth figures of the key economic sectors over the past 10 years. Agriculture experienced a decline of 2.2% in the contribution to total GVA, whilst Trade, Transport, Finance and Community services all increased their contribution to GVA, with Finance having the largest increase in GVA contribution of nearly 2%

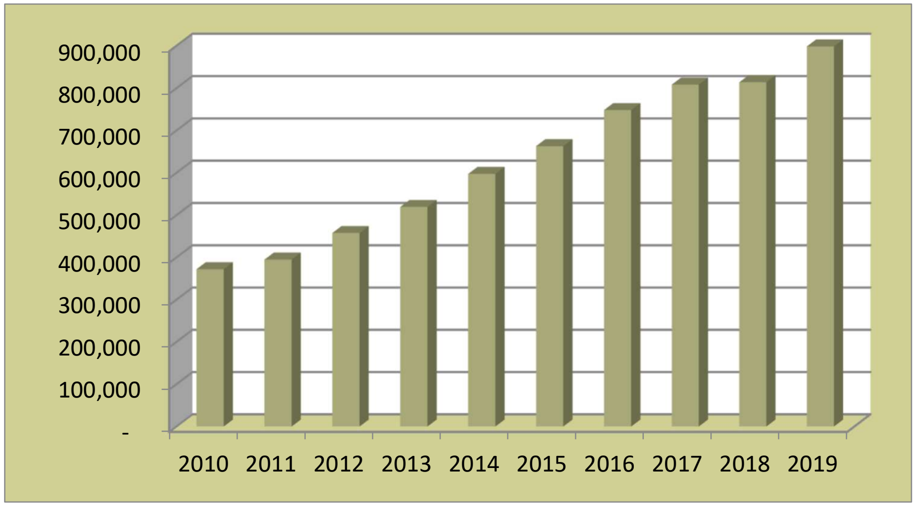
An analysis of the employment figures reveals that Trade, Finance, Community Services and Manufacturing remain the biggest contributors to employment.

GRAPH 6: EMPLOYMENT



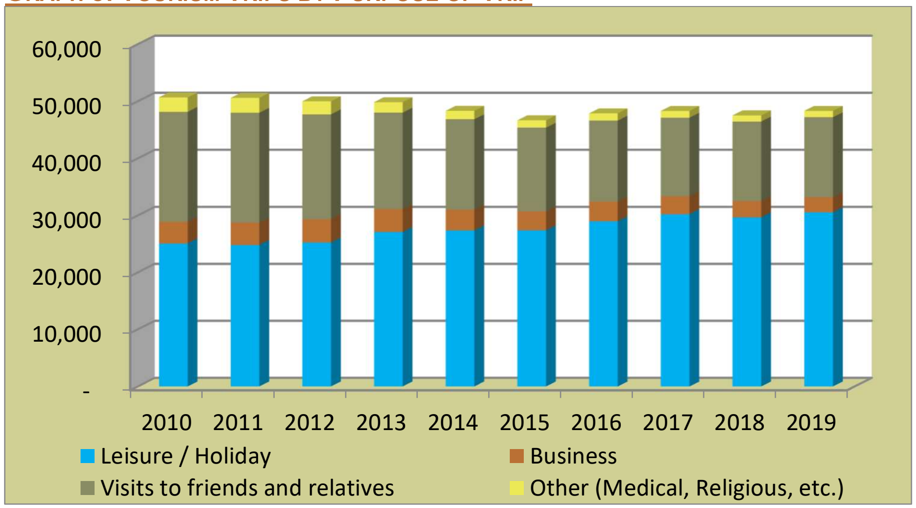
Total employment opportunities grew by 26.6% over the last 10 years, compared to a 15.3% growth in total population and, more importantly, a 23.9% growth in economically active population. This provides some confirmation as to the reduction in unemployment rate.

Graph 7: Tourism Spend (R)



The tourism sector remains an important economic driver with sustained growth over the past 10 years, albeit marginal in 2018.

Graph 8: Tourism Trips by Purpose of Trip

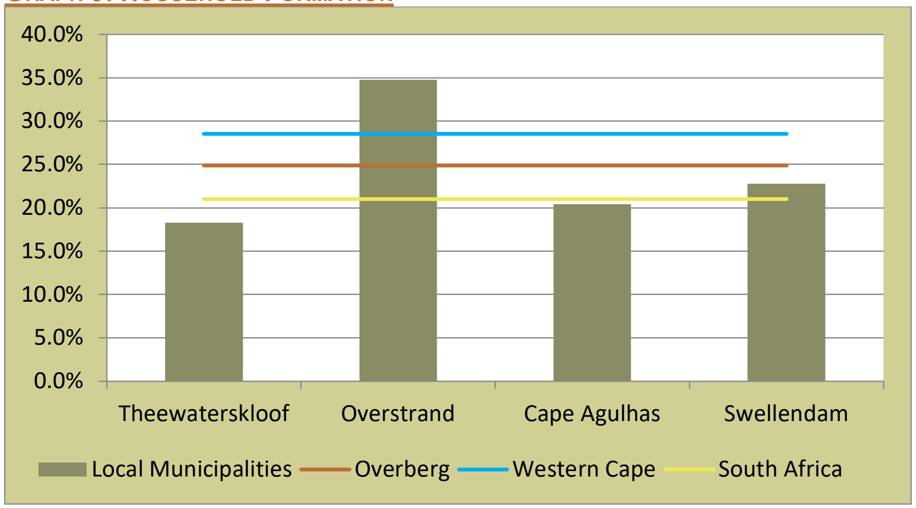


Tourism spend amounted to approx. R 900 million in 2019, which equates to 41.9% of GVA. An analysis of tourism trips reveals that tourism trips has remained relatively stable in recent years, with a marginal decline since 2016. Approximately 63% of trips are for leisure/holidays. Tourism as a key economic sector of the municipality should receive continual attention, especially due to its potential to create jobs and ability to accelerate economic growth in the area.

Household Infrastructure

Between 2010 and 2019 ***household formation*** was 20.4%, this is lower than the district's 24.9%, as well as that of the province with 28.5%. In absolute numbers, the growth of households was 299 year on year and 2,008 in the past 10 years.

Graph 9: Household Formation



Notwithstanding the growth in household formation, Cape Agulhas has always been able to maintain a high ***infrastructure index*** equivalent to the distract and provincial levels and significantly higher than the national level.

An analysis of the minimal backlogs reconfirms the high level of service provided by the municipality, with the exception to refuse removal, compared to other municipalities in the district.

It is important for the municipality to develop a sustainable financing strategy to continue with its capital investment programme to, firstly, maintain its asset base and, secondly, to expand its service delivery even further as the need for services increase.

TABLE 2: HOUSEHOLD INFRASTRUCTURE PROVISION

Infrastructure	Western Cape		Cape Agulhas	
Above RDP Level				
Sanitation	1,834,627	94.3%	11,123	96.2%
Water	1,915,281	98.4%	11,380	98.5%
Electricity	1,890,526	97.2%	11,414	98.8%
Refuse Removal	1,747,688	89.8%	9,952	86.1%
Below RDP or None				
Sanitation	110,918	5.7%	435	3.8%
Water	30,264	1.6%	178	1.5%
Electricity	55,020	2.8%	144	1.2%
Refuse Removal	197,857	10.2%	1,606	13.9%
Total Number of Households	**1,945,545**	**100.0%**	**11,558**	**100.0%**

Updated Historic Financial Assessment

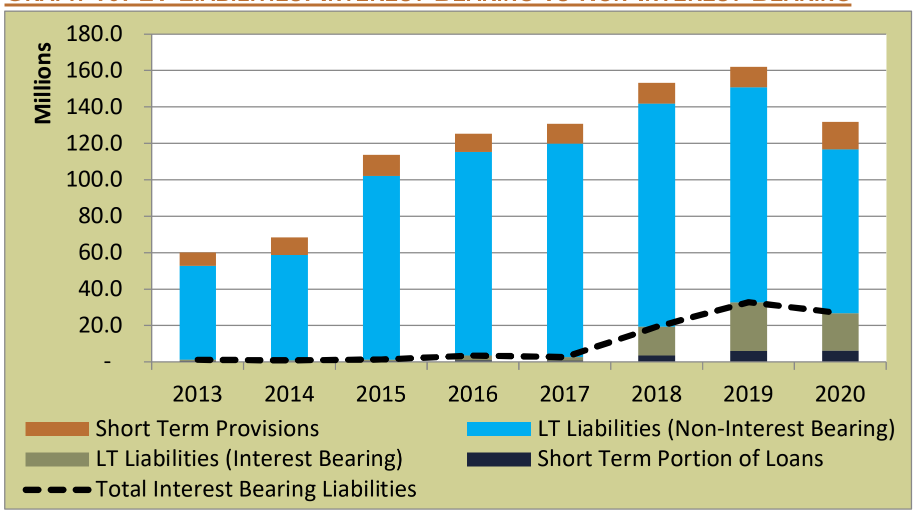
Financial Position

Cape Agulhas LM's financial position remained stable during FY2020. ***Total assets*** increased by R 18.79 million (3.27%) for the year ended 30 June 2020. Current cash increased from R 25.48 million in 2019 to R 49.25 million in 2020. The decline in short-term investments of R 34.47 million was responsible for the over-all decrease in cash and cash equivalents of R 10.7 million.

Current liabilities increased with R 4.19 million of which short-term provisions contributed R 3.86 million. This increase is due to current employee benefits that are provided for, an increase of 21.6% from 2019.

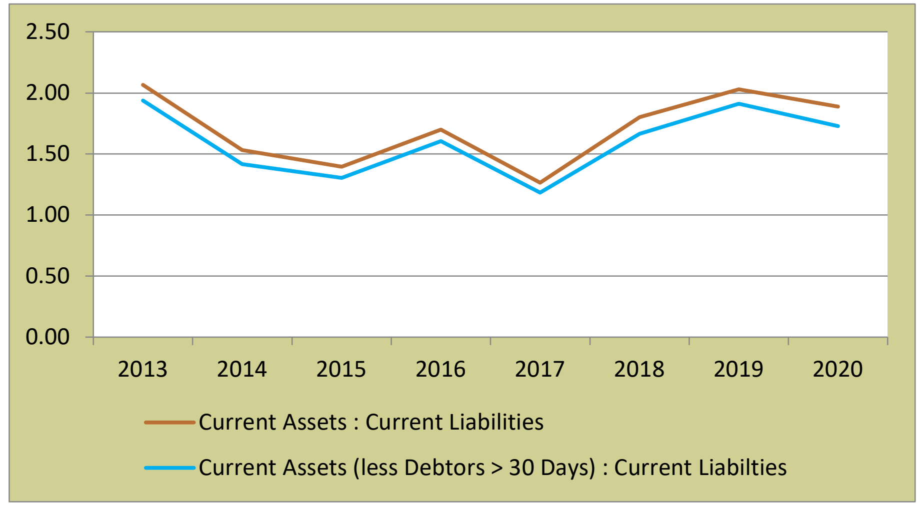
Graph 10 illustrates decrease in ***interest-bearing liabilities*** (R 20.76 million or 22.5%). The decrease was once again attributed to the continuous payment of LT loans totalling R 9.05 million (capital plus interest). As a result, the ***gearing ratio*** decreased to 8% from 10% as at FYE2019. This low gearing ratio is indicative of scope to access external financing, should the servicing of such financing be considered affordable to Cape Agulhas LM.

Graph 10: LT Liabilities: Interest Bearing vs Non-Interest Bearing



Cape Agulhas accessed no additional external long-term borrowing and continued to service the loan taken up during FYE2018. ***Non-interest-bearing liabilities***, which remains the largest pool of liabilities for the municipality, decreased by R 28.23 million (23.9%) to R 89.74 million as at FYE2020.

Graph 11: Liquidity Ratios

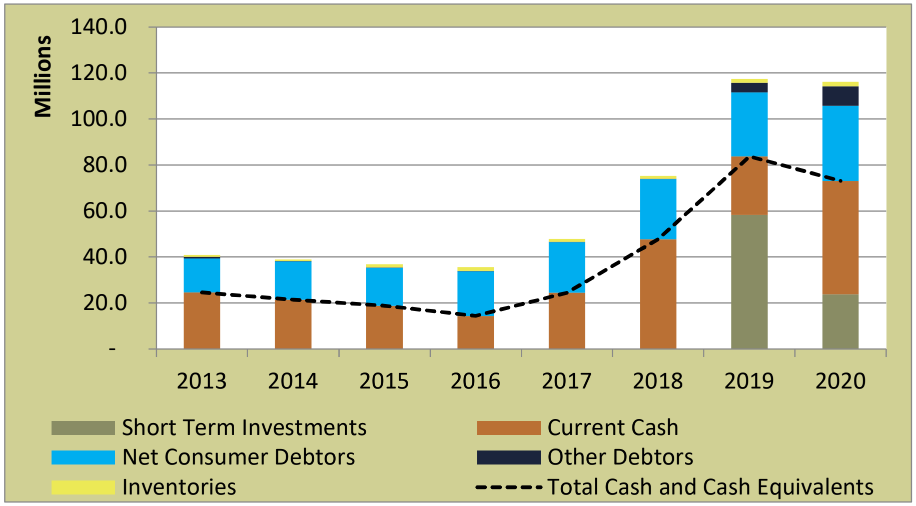


It is positive to note that the municipality continued to provide for the rehabilitation of its landfill sites. The provision increased by R 1.53 million in FY2020. The balance of the provision was R 48.75 million as at FYE2020 and represented a significant 28.13% of the total liabilities of the municipality.

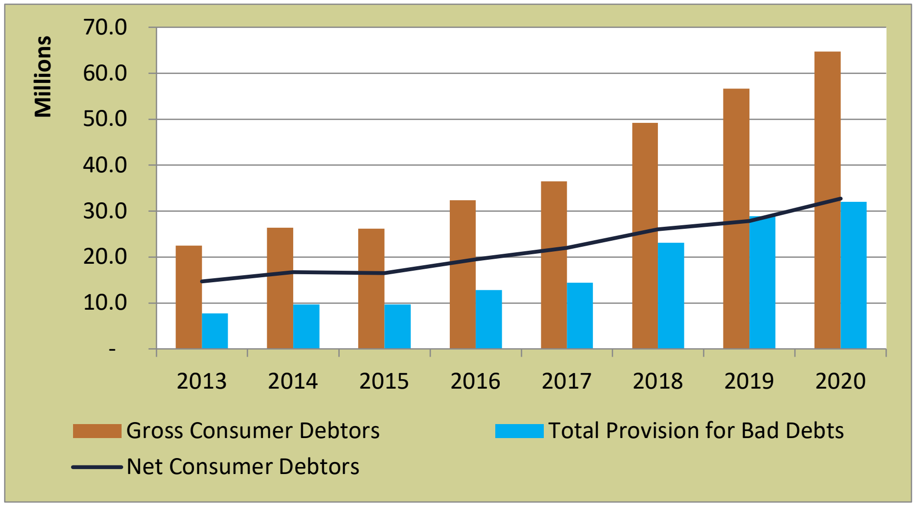
It is therefore recommended that the municipality continue to prudently build liquidity and cash reserves, in anticipation of the cash outflow that will be required to service this provision in future.

The weakening of the liquidity ratio observed during the year, is a result of utilizing own resources to fund capital expenditure and not taking up any available external funding during the past year for capital expenditure purposes.

GRAPH 12: CURRENT ASSETS BY ITEM

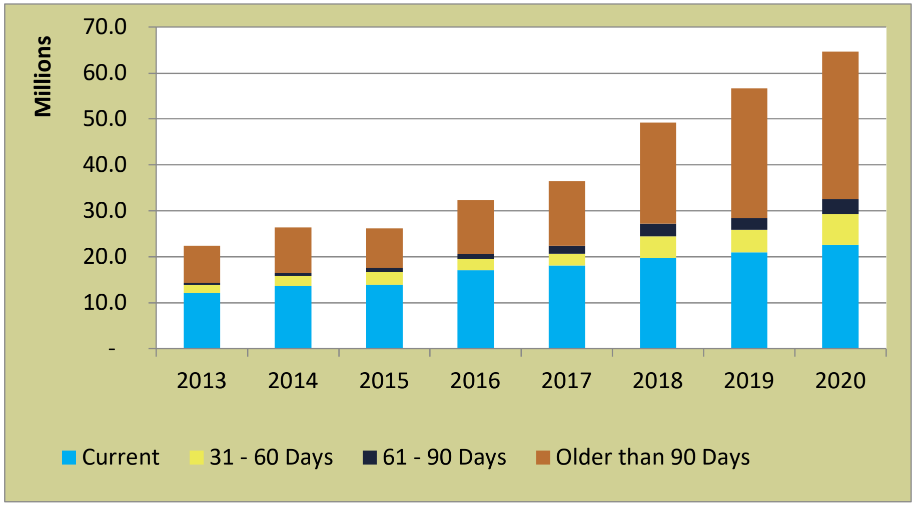


GRAPH 13: GROSS CONSUMER DEBTORS VS NET CONSUMER DEBTORS



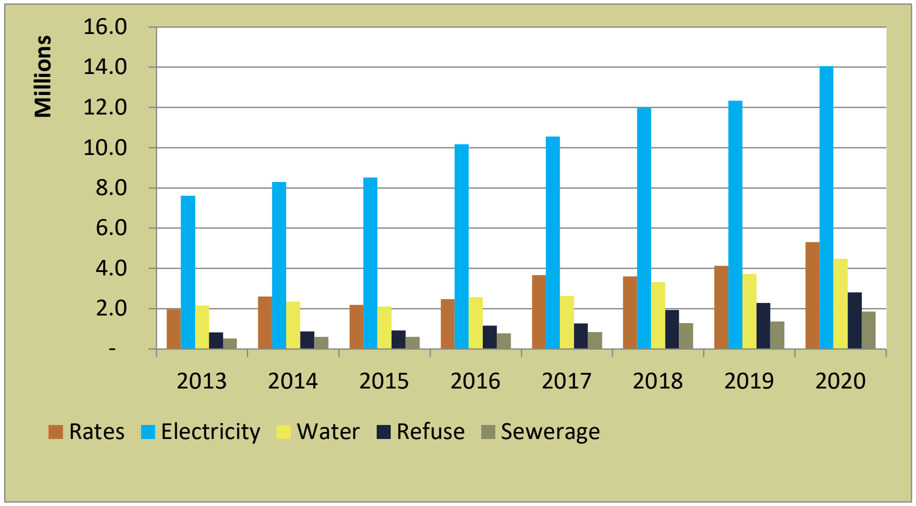
The liquidity ratio decreased from 2.03 in 2019 to 1.89 in 2020. Although this is still above the minimum National Treasury norm of 1.5:1, a target of at least 2:1 should be set to provide a healthy buffer to absorb unforeseen challenges and obstacles, and minimize the effect thereof on the local economy.

GRAPH 14: CONSUMER DEBTORS BY AGE ANALYSIS



At this level, the gearing ratio came to a low 8%, that is well below the maximum recommended norm for Cape Agulhas of 30%.

Graph 15: Consumer Debtor by Type



The debt service cover ratio was at 1.22 times and the debt service as a percentage of total expenditure was only 0.03% (a maximum of 7% is recommended for Cape Agulhas). These indicators reflect the affordability of Cape Agulhas' current debt profile. It has to be noted however that the debtors' days have marginally increased from 41.9 in FYE2019 to 45.4 in FYE 2020.

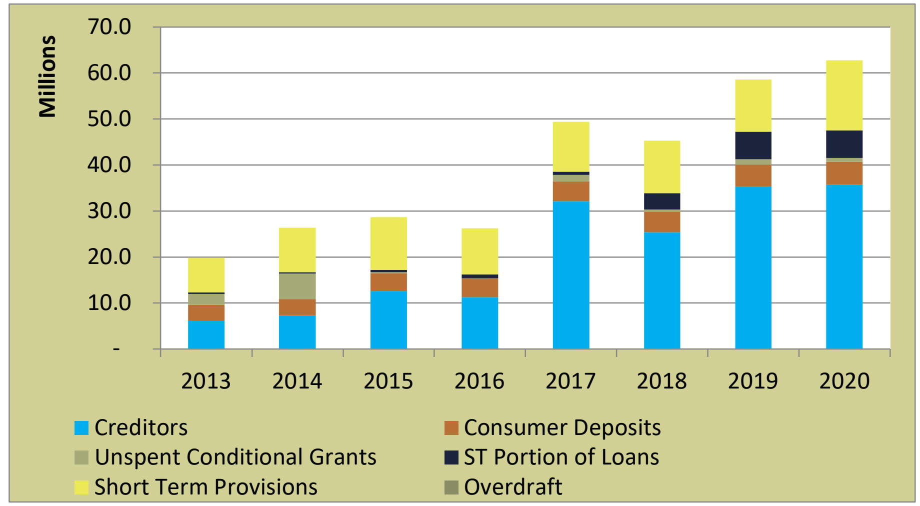
Current assets remained constant for FYE 2020. Notable fluctuations are increased current cash of R 23.77 million and short-term investments declined by R 34.47 million having a nett result on cash and cash equivalents of a decline of R 10.7 million. These results confirm that Cape Agulhas might already feel the effect of the increased debtors' days as indicated above.

The continually growing consumer debtors and the need for increased provisions for doubtful debt are clearly illustrated on **Graph 14** and **Graph 15**. The electricity debtors remain the largest contributor to total gross consumer debtors, while all other debtors have experienced consistent increase from 2012.

With the collection rate dipping below the norm of 95% set by national treasury, the municipality should strive for a collection rate above that , this is considered achievable, especially in light of the 96% achieved on average, over the last seven years.

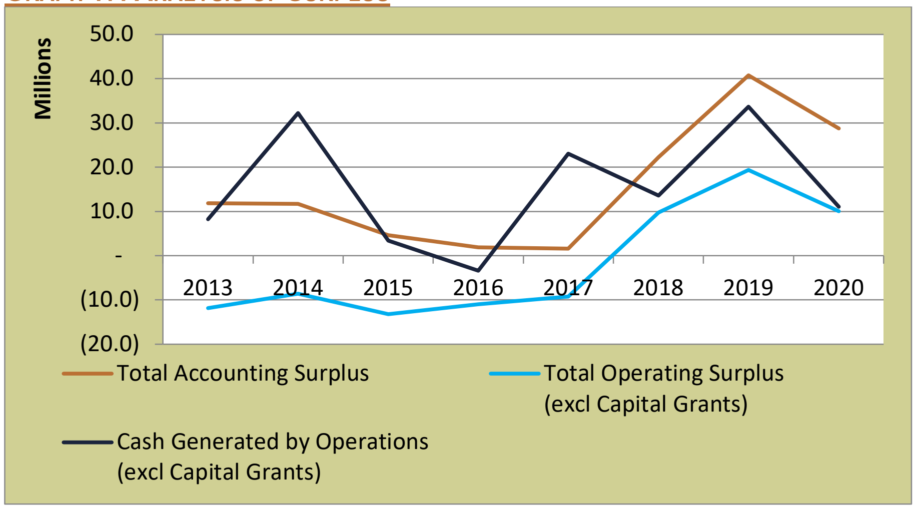
Failure to maintain a high collection rate will only increase the pressure on the cash flow. A solution to retrieve and collect some of the substantial amount of debtors older than 90+ days could alleviate some of the cash flow pressure.

Graph 16: Current Liabilities by Item



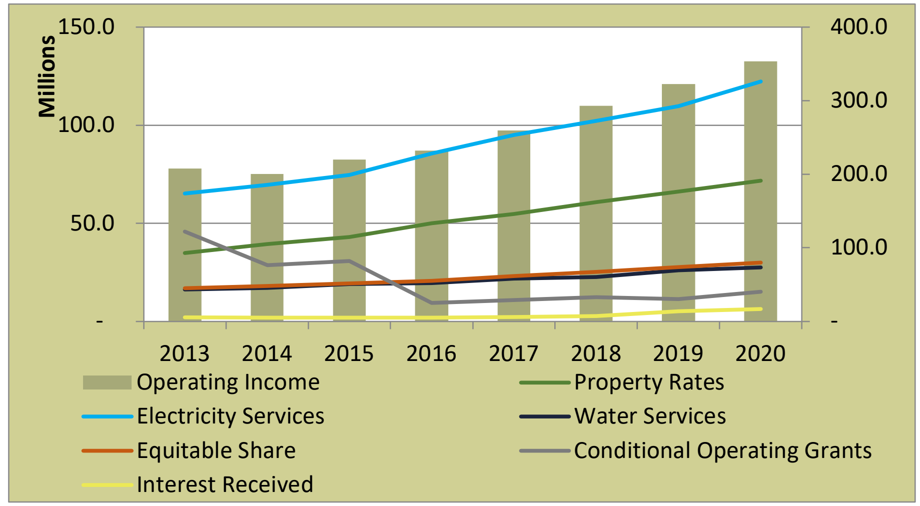
Financial Performance

Graph 17: Analysis of Surplus



Cape Agulhas' profitability declined in FYE2020 from a sustained period of growth since FYE2017. Total income increased by R 30.8 million (9.5%), while operating expenditure increased by R 40.14 million (13.2%). These movements along with a decline in cash generated by operations resulted in the decline in total accounting surplus as well as the total operating surplus. Significant when compared to FYE2019.

Graph 18: Contribution per Income Source

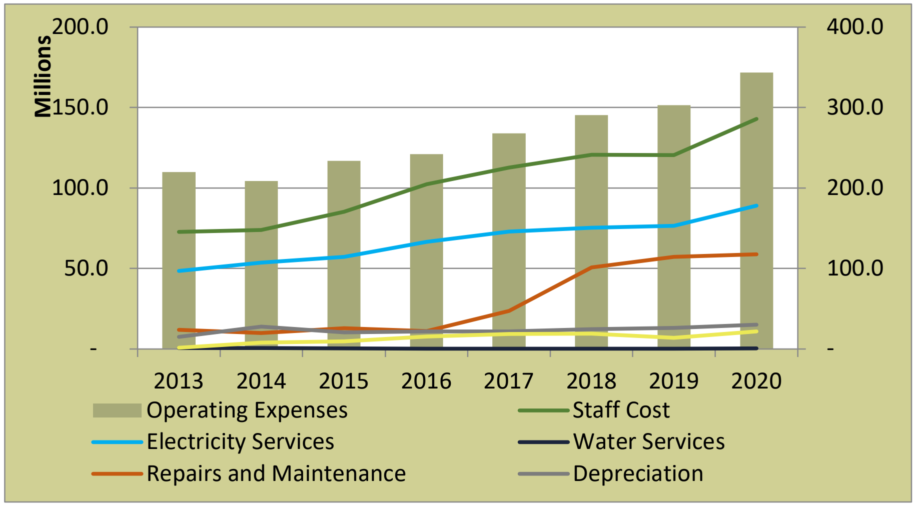


Capital grants represented R18.69 million of total income. Therefore, upon exclusion of capital grants, the municipality realised an operating surplus of R 10.0 million. Compared to FYE2019, major declines were experienced. Cash generated by operations declined by 67.2% which came to R 11.0 million.

Total grants income of R 63.6 million (R 60.3 million during FY2019) represent only 17% of the municipality's Total income, indicating the municipality's relatively low level of reliance on the fiscus and its ability to generate revenue from its own resources.

Billed income increased by R 19.92 million (8.2%). Electricity services and property rates remain the two main income sources of the municipality, generating combined revenue of R 193.8 million or 54.8% of the total operating income of the municipality (R 353.29 million). The annual increases in electricity and property rates income remained above the CPI rate at 11.5% and 8%, respectively.

GRAPH 19: CONTRIBUTION PER EXPENDITURE ITEM



The increase in operating expenditure was mainly driven by an increase in staff costs of R 22.4 million (18.6%). The staff costs contribute 41.6% to the total operating expenditure, which is above the recommended norm of 25%-40%. This is not sustainable for the municipality.

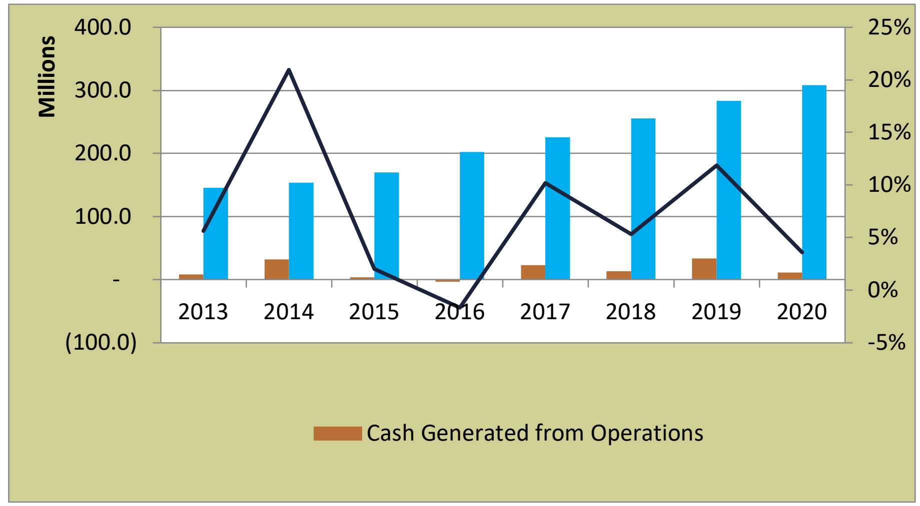
The repairs and maintenance expense to carrying value of PPE was 12.4%, this is above the norm of 8% set by national treasury, though when looked at in relation to capital expenditure, which is quite moderate, this slightly higher percentage is expected due to the fact that adequate resources are allocated to ensure that current assets remain in a properly functioning condition.

There is scope to expand the capital asset base, and due to the very low gearing of the municipality, external funding can be taken up to reduce the strain on cash and reserves and thus ensure that the municipality remains sustainable.

By carefully managing operating expenses, the municipality can continue to improve the overall financial performance.

CASH FLOW

GRAPH 20: CASH GENERATED FROM OPERATIONS/OWN SOURCE REVENUE



Cape Agulhas realised cash generated from operations of R 11.0 million for FY2020. Of the R 40.5 million spent on capital expenditure for FY2020, R 19.2 million was funded through capital grants and R 15.5 million was financed through own cash and the balance was funded with the income received from the sale of fixed assets.

The low gearing ratio combined with the very low debt service as a percentage of operating expenditure of 3% indicate that there is scope for the municipality to take up external financing for capital expenditure purposes and subsequently alleviate the pressure on own cash reserves.

Cash and cash equivalents at year end decreased by R 10.7 million to a balance of R 73.04 million.

As illustrated on TABLE 3, Cape Agulhas is required to maintain sufficient cash reserves to cover unspent conditional grants (R 700 000), short-term provisions (R 15.2 million), and funds, reserves & trust funds (R 35.0 million). Cash must also be available to cover working capital provision (including 1 month's opex) of R 25.6 million.

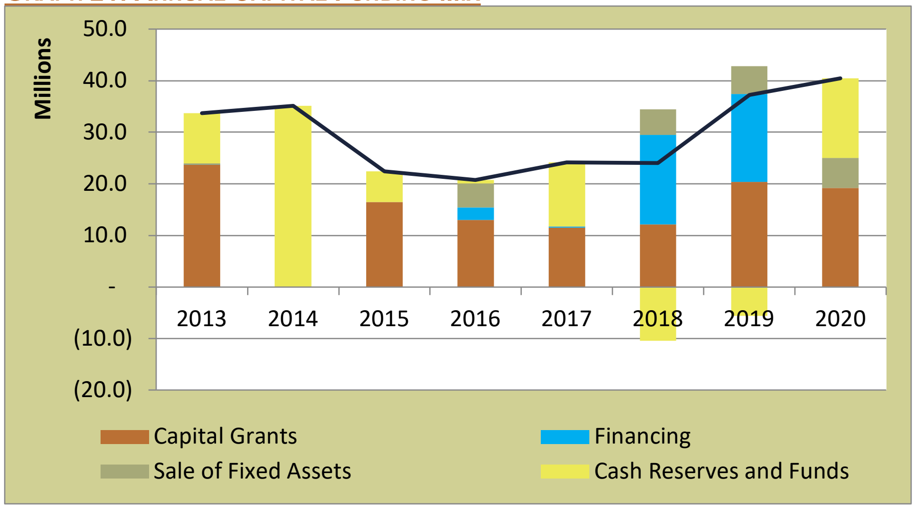
As a result of the decrease in cash and cash equivalents during the past year, the municipality was not able to achieve the minimum liquidity levels required of R 76.6 million and fell short by R 7.4 million. The minimum liquidity requirements do not consider the outstanding creditors, which would have increased the shortfall to R 43.12 million.

Table 3: Minimum Liquidity Levels

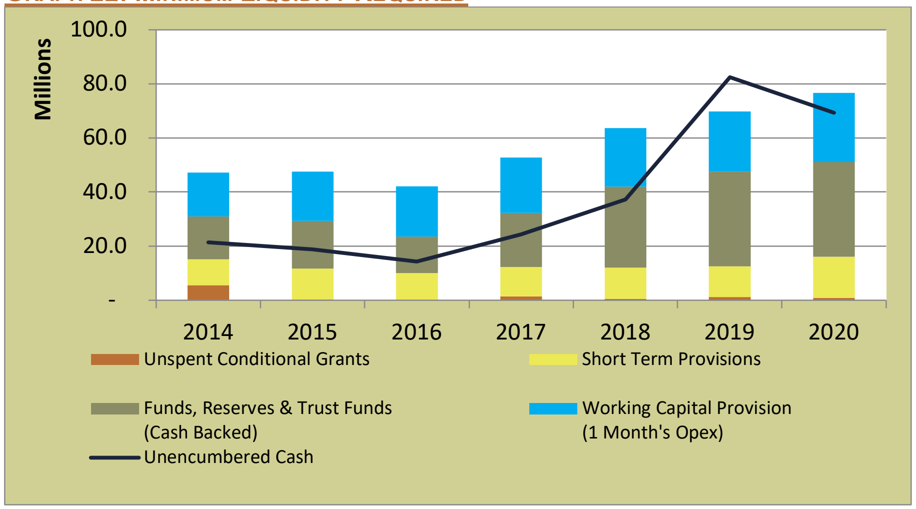
	2013	2014	2015	2016	2017	2018	2019	2020
Unspent Conditional Grants	2.4	5.5	0.2	-	1.4	0.5	1.1	0.7
Short Term Provisions	7.4	9.6	11.5	10.0	10.8	11.5	11.4	15.2
Funds, Reserves & Trust Funds (Cash Backed)	18.5	15.8	17.8	13.5	20.0	30.0	35.0	35.0
Total	**28.3**	**30.9**	**29.4**	**23.5**	**32.2**	**42.0**	**47.5**	**51.0**
Unencumbered Cash	24.5	21.4	18.8	14.3	24.3	37.2	82.4	69.3
Cash Coverage Ratio (excl Working Capital)	0.9	0.7	0.6	0.6	0.8	0.9	1.7	1.4
Working Capital Provision (1 Month's Opex)	17.5	16.3	18.1	18.6	20.5	21.7	22.2	25.6
Cash Coverage Ratio (incl Working Capital)	0.5	0.5	0.4	0.3	0.5	0.6	1.2	0.9
Minimum Liquidity Required	45.8	47.2	47.5	42.1	52.7	63.7	69.7	76.6
Cash Surplus/(Shortfall)	**(21.3)**	**(25.8)**	**(28.7)**	**(27.8)**	**(28.4)**	**(26.5)**	**12.7**	**(7.4)**

It will be prudent to increase the liquidity levels to provide a buffer against any potential future financial shocks, for example the expected future outflow of economic resources to service the rehabilitation of landfill provision.

Graph 21: Annual Capital Funding Mix



Graph 22: Minimum Liquidity Required



IPM Shadow Credit Score

Cape Agulhas LM was assessed for an IPM shadow credit score, to provide information to management and to council as to the current risk rating that Cape Agulhas may receive from external lenders, which will determine their cost of funding. Any improvements to the shadow credit rating over time will result in more affordable lending rates.

The IPM credit model reflects a score of **6.8**, which is comparable to A- on a national ratings scale. This credit score is relatively high, compared to other municipalities, and is at an investment grade level - which means that Cape Agulhas should be successful in accessing external borrowing at relatively affordable rates.

The results obtained from the assessment, per module, are presented below:

Table 4: IPM Credit Model Outcomes

Modules	2019 (5)
Financial	4,0
Institutional	3,4
Socio-Economic	2,4
Infrastructure	3,3
Environmental	3,4

From the assessment it is evident that the socio-economic environment and infrastructure modules continue to be Cape Agulhas' main impediment in achieving higher credit scores. This is mainly linked to the low economic growth in the region, as illustrated by the GVA contractions in 2018 and 2019.

The score achieved on the financial module is driven by the strong liquidity position which needs to be maintained in the future. By implementing the recommendations made in this LTFP update report and maintaining financial discipline and prudent financial management, Cape Agulhas should be able to not only maintain, but even improve this score over time.

1	Planning Process
2	Updated Perspectives (Demographic, Economic, Household Infrastructure)
3	Updated Historic Financial Assessment
4	**Long Term Financial Model Outcomes**
5	Future Revenues
6	Affordable Future Capital Investment
7	Scenario Analysis
8	Ratio Analysis
9	Conclusions

Long Term Financial Model Outcomes

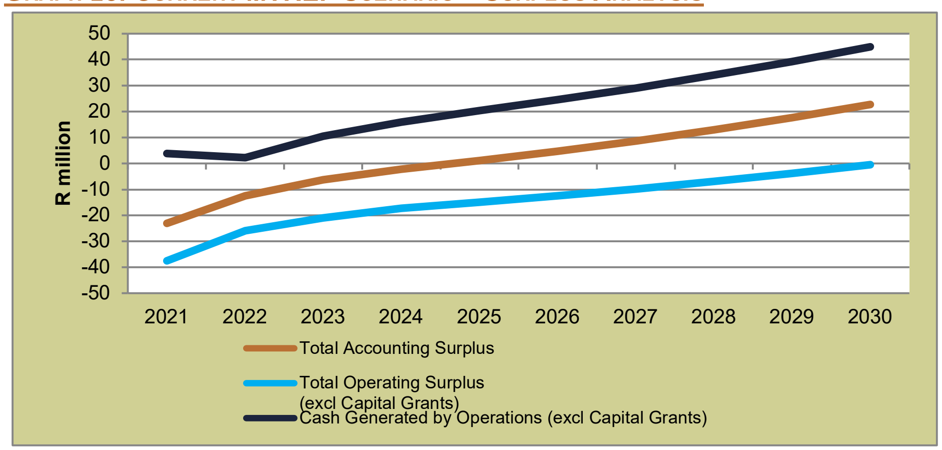
Current MTREF Scenario

The operational and financial challenges, effected by the Covid-19 pandemic in the current financial period, have forced municipalities to adjust their MTREF estimates. Cape Agulhas has consequently budgeted for the non-payment of accounts based on past experience of recovery rates. Comparing the 2020/21 final budget to 2020 AFS results, the following changes were noted:

- The collection rate which is usually at about 95%, was lowered to 90% during the 2020/2021 year,
- The average tariff increase of 7% in property rates, water, sanitation and waste removal services which is in excess of CPI rate,
- Cape Agulhas posts operational deficits mainly a result of sharp increases in certain cost items (i.e. debt impairment, employee related costs and other materials). The 10-year average increase in expenditure of 7.0% is in excess of CPI,
- Repairs and maintenance increases to 16% of PPE consistently from 13.6% in 2020.

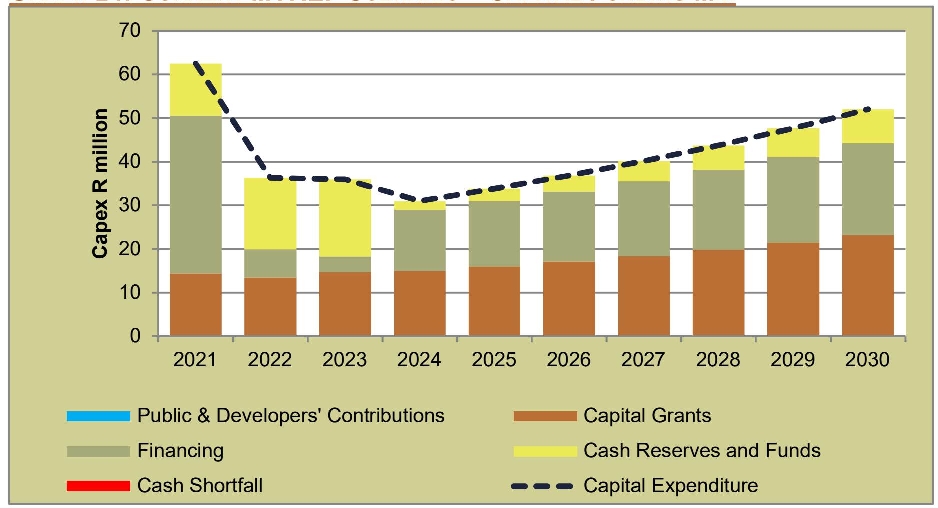
- The outcomes of the MTREF scenario are as follows:

Graph 23: Current MTREF Scenario – Surplus Analysis



Cash generated from operations is at the lowest in 2022 at only R2.2 million while operational deficits are worst at R 37.5 million in 2021.

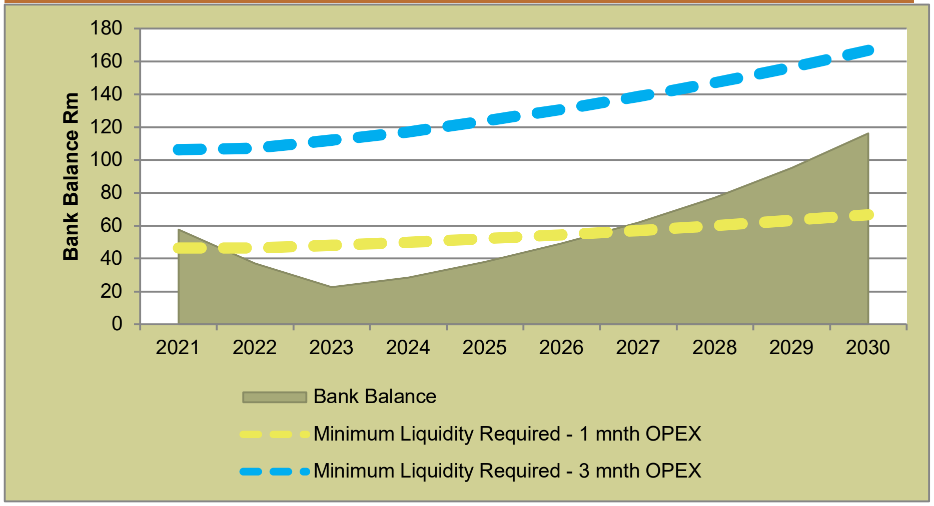
Graph 24: Current MTREF Scenario – Capital Funding Mix



A R22 million (55%) increase in the level of capital programme investment to R60 million in 2021 is noted, followed by a rapid decrease of 67% to R36 million for 2022 and 2023. The funding mix for 2022 and 2023 too reliant on own cash and it will be advisable to have a more consistent borrowing programme.

The result is that cash resources are forecast to deteriorate significantly over the MTREF period and that the liquidity levels will reach levels below the minimum of 1:1 between year 3 and year 6 of the planning period with cash shortfalls of R 6 million to R 26 million. The cash coverage ratio also deteriorates to levels as low as 0.5 in 2023.

GRAPH 25: CURRENT MTREF SCENARIO – BANK BALANCE VS MINIMUM LIQUIDITY



This scenario appears to be more cautious but unlikely, considering the improved financial position that Cape Agulhas established over the past three years and the forecasts made in the previous update of the long-term financial plan. It is our view that the budget is therefore very conservative as a result of the uncertainties previously mentioned.

To address the issues identified in the MTREF scenario, we have modelled the scenarios as follows to arrive at an optimal case for Cape Agulhas:

ADJUSTED MTREF FUNDING MIX SCENARIO

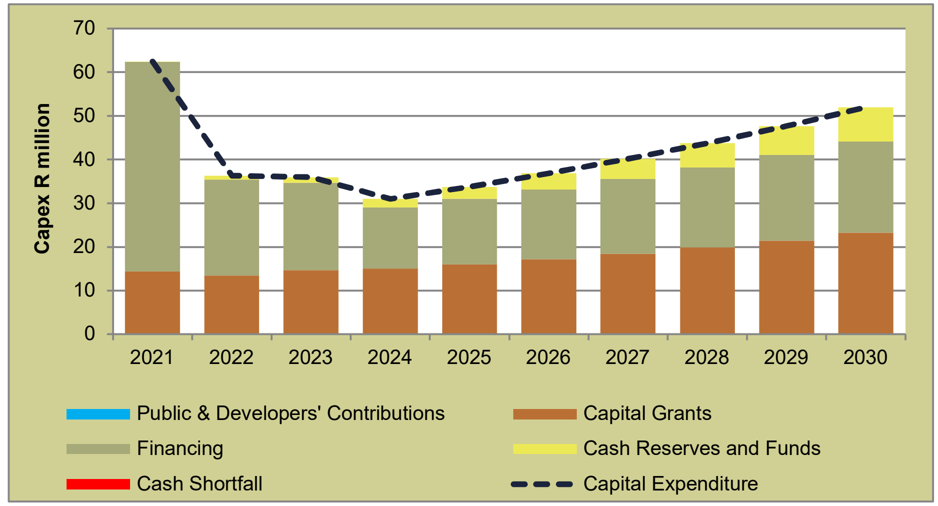
The decline in cash resources over the MTREF period is mainly due to the less than optimal capital funding mix being applied.

The model was adjusted to increase borrowings by R46 million over the MTREF period while maintaining the same level of capex. Stronger liquidity results are obtained - as can be seen in the graphs below.

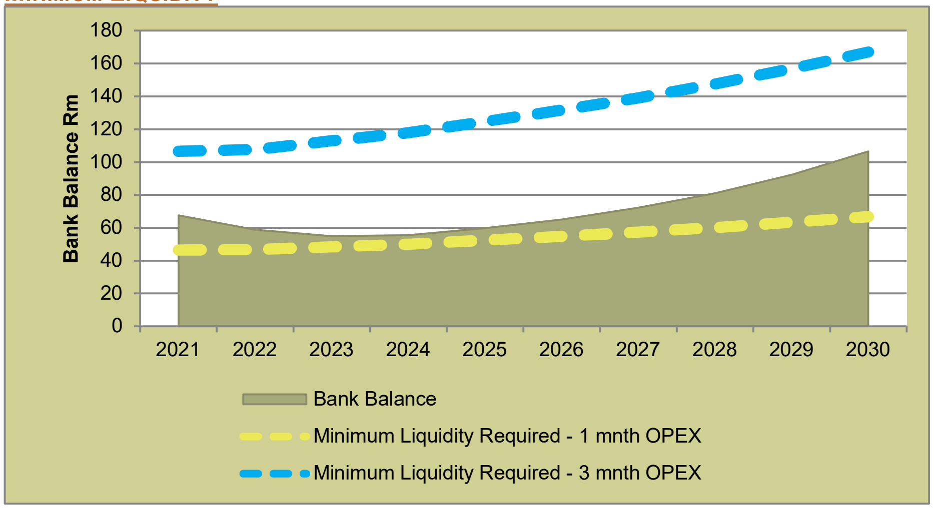
Notwithstanding these increases in borrowing over the MTREF period, debt levels and debt servicing requirements are still within ranges that are considered affordable, and Debt Service to Total Expense ratio remains below the maximum norm set at 7%. The gearing levels remains below 22% against the maximum benchmark of 30%.

The liquidity ratio increases to 1.6:1 in 2030 and the municipality is able to reach the minimum liquidity requirements including 1 month's opex throughout the planning period.

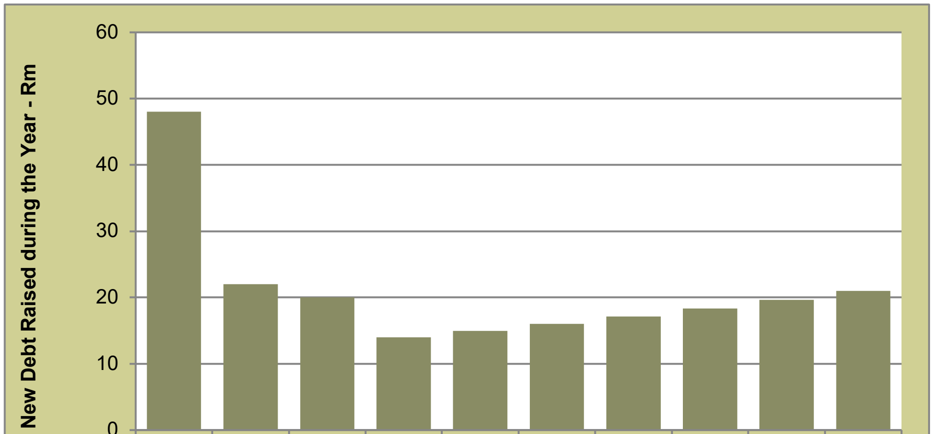
GRAPH 26: ADJUSTED MTREF FUNDING MIX SCENARIO – CAPITAL FUNDING MIX



GRAPH 27: ADJUSTED MTREF FUNDING MIX SCENARIO – BANK BALANCE VS MINIMUM LIQUIDITY

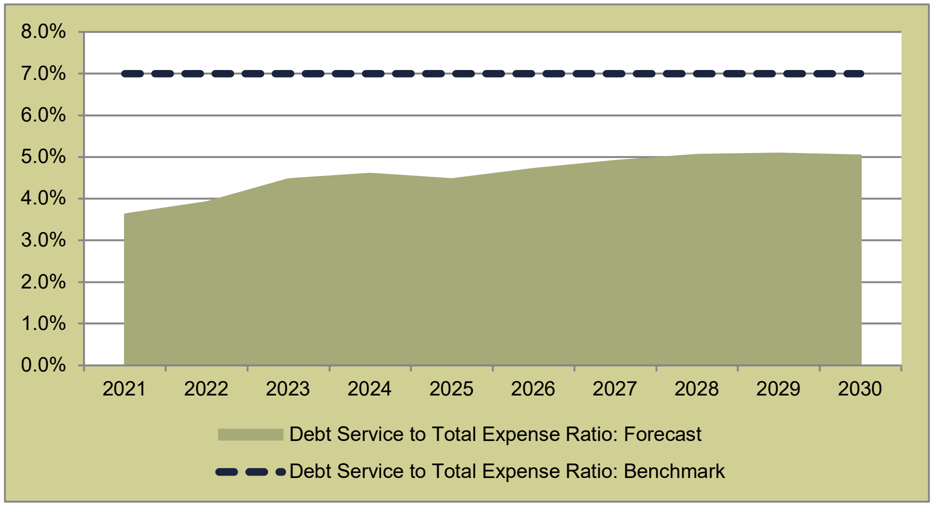


GRAPH 28: ADJUSTED MTREF FUNDING MIX SCENARIO – ANNUAL BORROWING

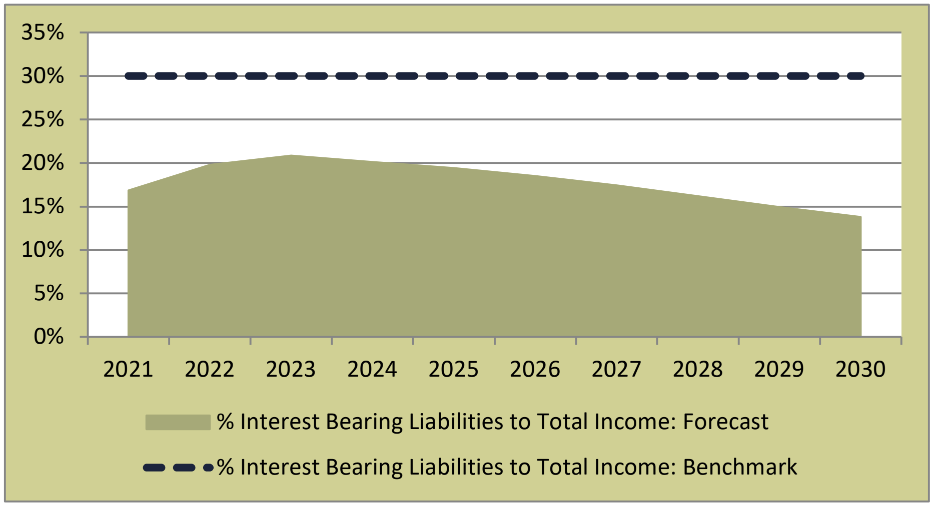


	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
R million	48	22	20	14	15	16	17	18	20	21

GRAPH 29: ADJUSTED MTREF FUNDING MIX SCENARIO – DEBT SERVICE TO TOTAL EXPENSE



GRAPH 30: ADJUSTED MTREF FUNDING MIX SCENARIO – GEARING

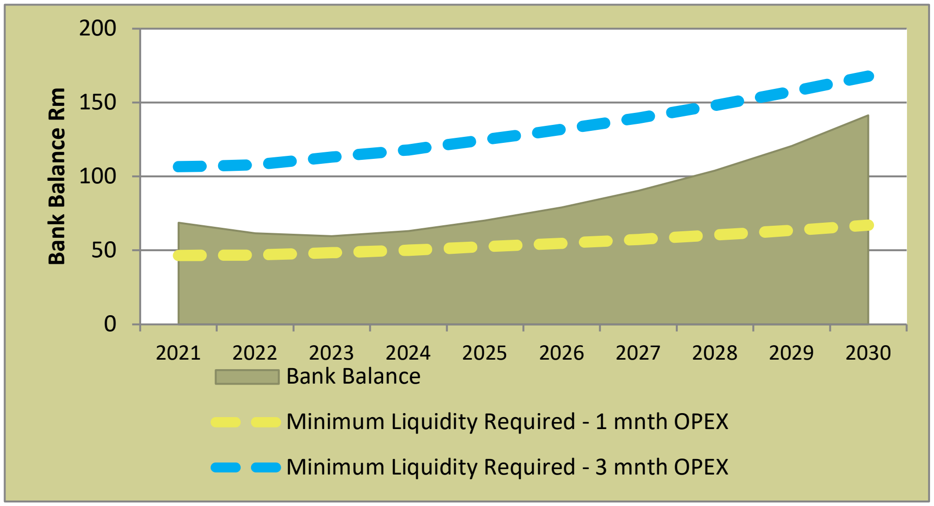


Average Loan Tenor Increase Scenario

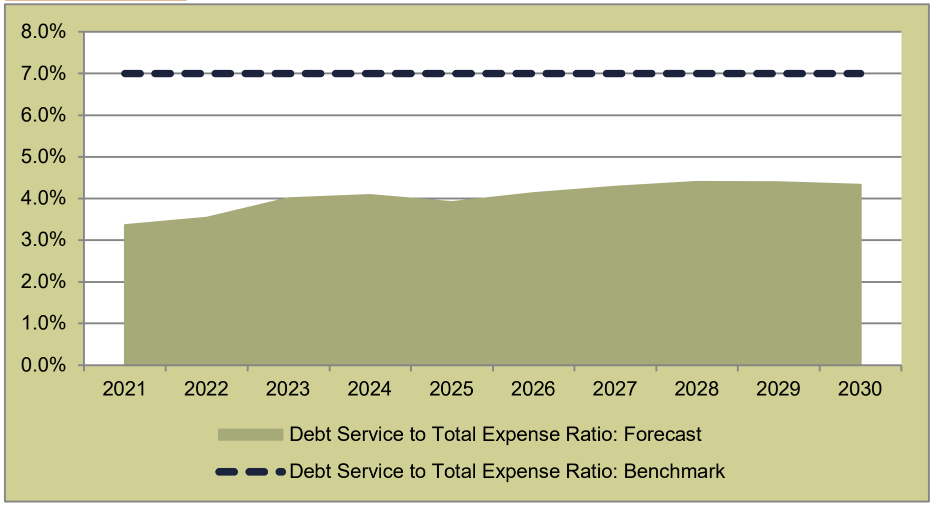
Building on from the MTREF funding mix adjustment scenario, the model demonstrates how Cape Agulhas can benefit from longer loan tenors to further strengthen annual liquidity and avoid excessive debt service requirements.

Should the average loan tenor increase from 10 years to 13 years (by accessing the majority of borrowing for loan tenors of 15 years), keeping all other inputs constant, a significant improvement in liquidity is noted, with the cash balance remaining above the minimum liquidity requirements for the entire planning period. The gearing and debt service indicators also reflect a more positive picture, with both these metrics remaining within affordable levels at or below the maximum recommended norms. These results are reflected in the graphs below.

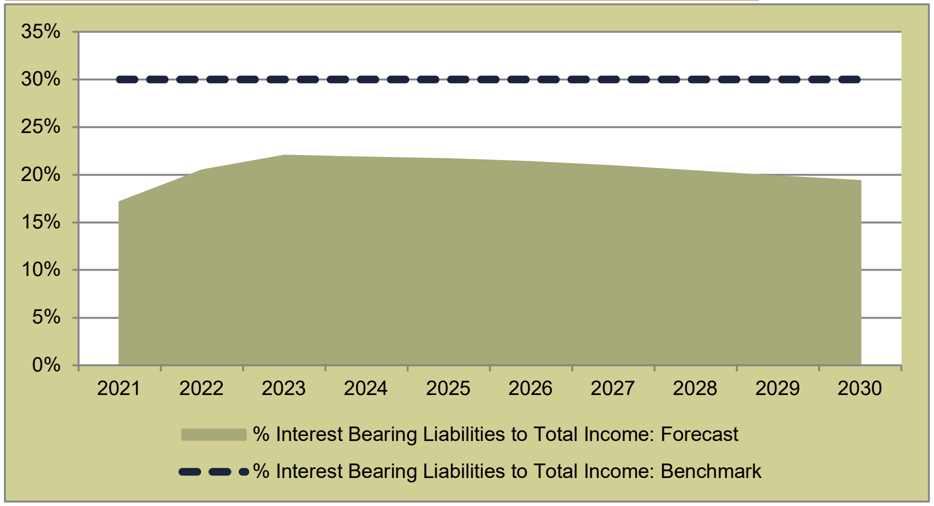
Graph 31: Average Loan Tenor Increase Scenario – Bank Balance vs Minimum Liquidity



Graph 32: Average Loan Tenor Increase Scenario – Debt Service to Total Expense



Graph 33: Average Loan Tenor Increase Scenario – Gearing



Optimal Scenario

Building on from the funding mix adjustment and the increase in average loan tenure scenarios, an optimal scenario was obtained by making reasonable adjustments to reduce the operating expenditure budget by R4 million annually, which translates to a 1% reduction over the longer term. This will allow for an accelerated capital investment programme, maintaining an optimal funding mix and building a liquidity buffer to absorb any unexpected financial shocks that the municipality may experience. The next chapters discuss this optimal scenario in more detail.

Table 5: Optimal Scenario Outcomes

Outcome	10-Year Outcome
Average annual % increase in Revenue	6,5%
Average annual % increase in Expenditure	7,2%
Accounting Surplus accumulated during Planning Period (Rm)	-R 15
Operating Surplus accumulated during Planning Period (Rm)	-R 189
Cash generated by Operations during Planning Period (Rm)	R 193
Average annual increase in Gross Consumer Debtors	9,5%
Capital investment programme during Planning Period (Rm)	R 503
External Loan Financing during Planning Period (Rm)	R 268
Cash and Cash Equivalents at the end of the Planning Period (Rm)	R 94
No of Months Cash Cover at the end of the Planning Period (Rm)	1,8
Liquidity Ratio at the end of the Planning Period	1,1 : 1
Gearing at the end of the Planning Period	26,9%
Debt Service to Total Expense Ratio at the end of the Planning Period	5,3%

1	Planning Process
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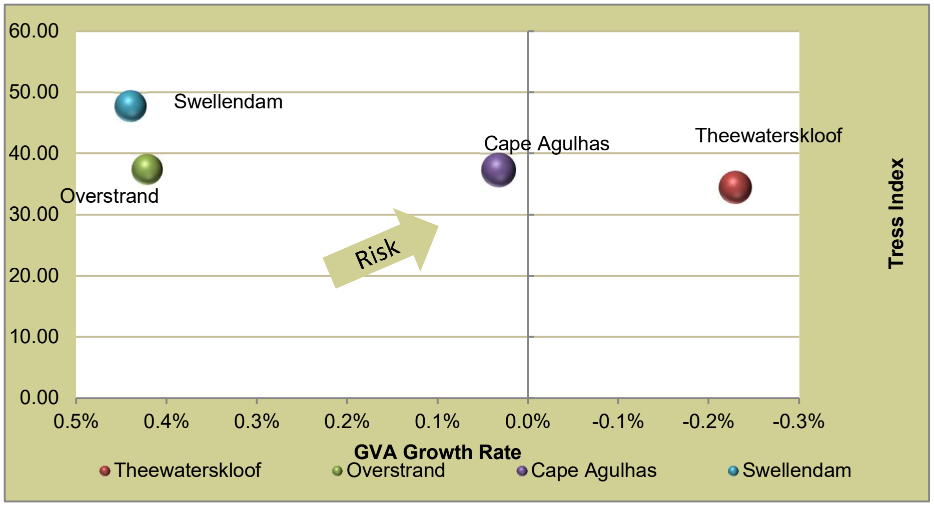
FUTURE REVENUES

MUNICIPAL REVENUE RISK INDICATOR (MRRI) = "HIGH"

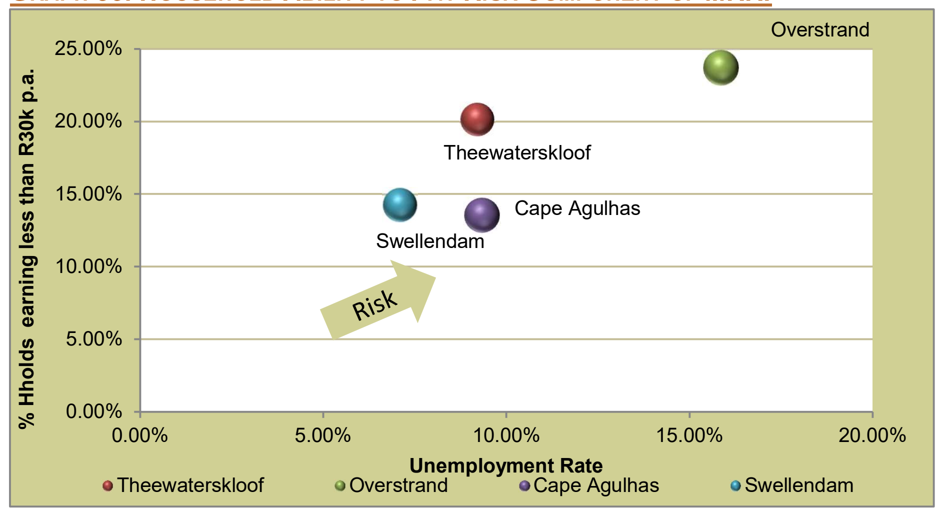
GRAPH 34: ECONOMIC RISK COMPONENT OF MRRI



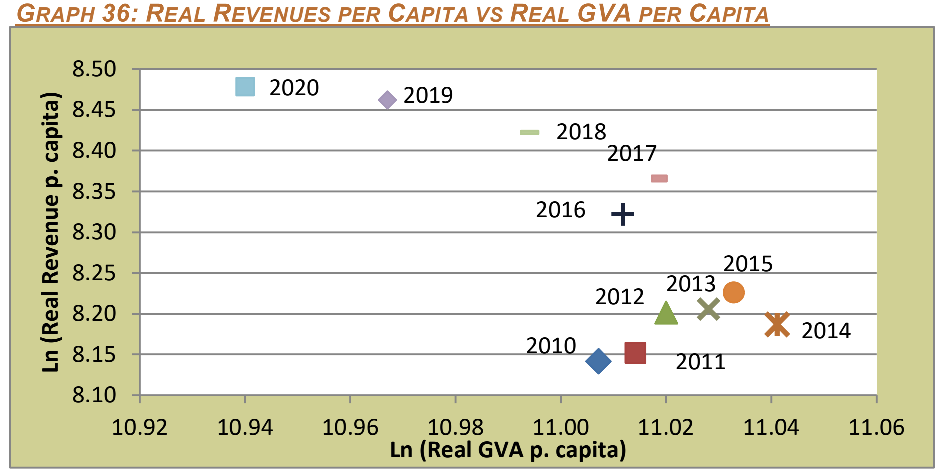
The latest iHS Global Insight update of the Cape Agulhas economy reveals a continuation of sluggish economic growth, similar to most other local municipalities in the country, averaging only 0.03% p.a over the last five years. The small economy with a GVA of R2.16 billion contracted in noted in 2018 and 2019. A Tress Index of 37 suggests that the Cape Agulhas economy is relatively well diversified. The ***economic risk*** component of the MRRI produces a risk assessment for Cape Agulhas of "Medium".

The percentage of households reliant on indigent support combined with the low unemployment rate of 9.3% resulted in a ***household ability to pay risk*** component of the MRRI of "Medium to Low". The overall MRRI risk rating remained "Medium".

GRAPH 35: HOUSEHOLD ABILITY TO PAY RISK COMPONENT OF MRRI



GRAPH 36: REAL REVENUES PER CAPITA VS REAL GVA PER CAPITA

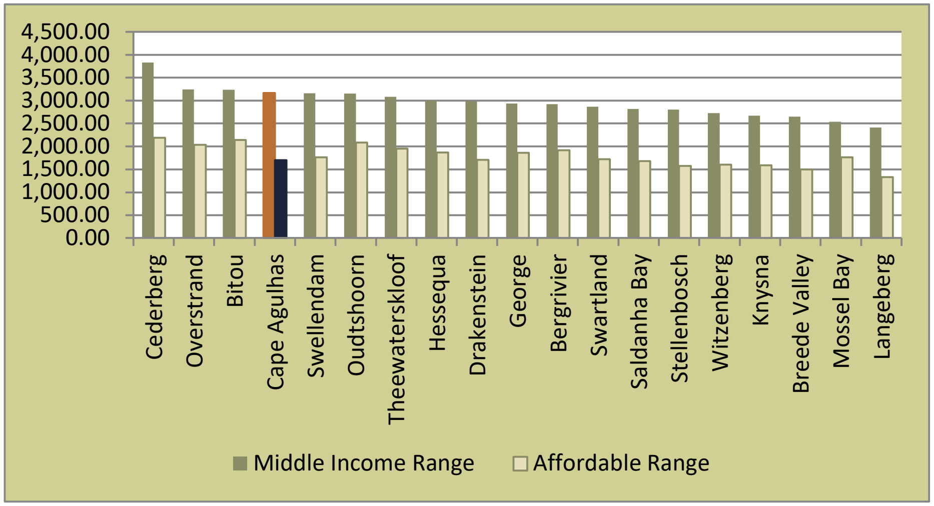


Notwithstanding a further decline in ***real GVA per capita,*** due to a lower GVA growth rate than population growth, the ***real municipal revenue (excluding transfers) per capita*** improved. This indicates increasing pressure on households to service their municipal bill.

The current trend is not sustainable and will significantly limit Cape Agulhas' ability to increase its revenues from increasing tariffs. Economic growth is of utmost importance to support financial sustainability of the municipality over the longer term.

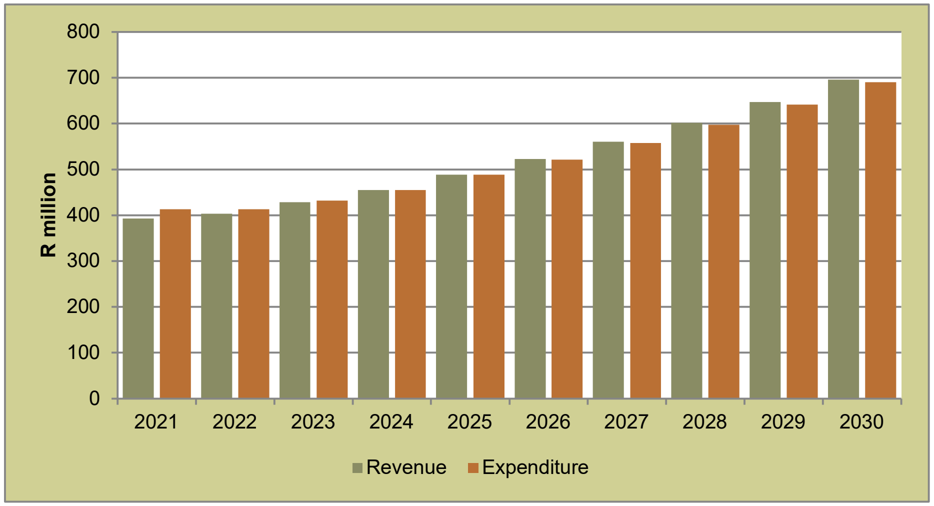
A comparison of the ***average household bill*** for the middle income- and affordable range of a selected number of municipalities in the Western Cape (extracted from Budget Table SA14), based on the 2020/21 tariffs reveals that Cape Agulhas features as the median of the municipalities in the Overberg district are at the higher end compared to the full sample of municipalities in the Western Cape reflected in Graph 37.

Graph 37: Average Monthly Household Bill (R)



Municipal Revenues

Graph 38: Revenue and Expenditure

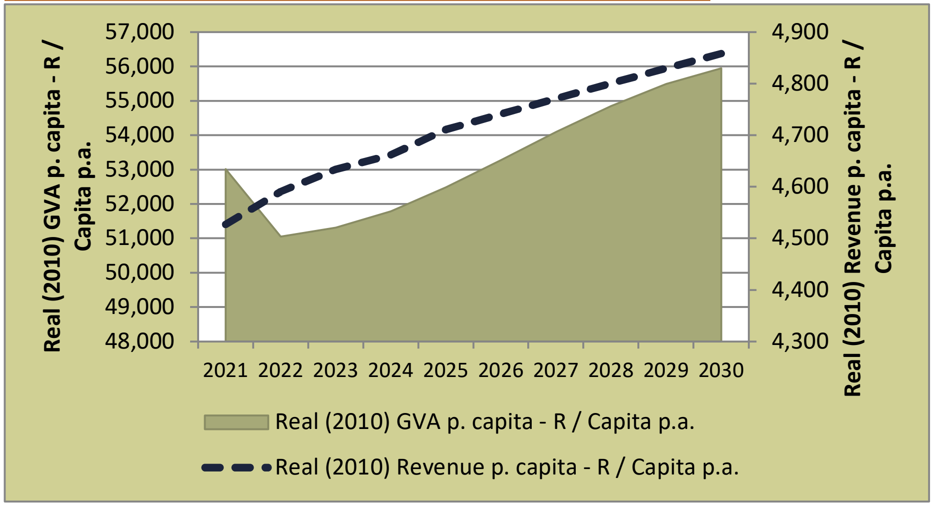


The optimal scenario estimates over the 10-year forecast period indicate that ***future nominal revenue*** (including all grants) is growing at an average rate of 6.5% p.a., while ***future nominal expenditure*** is growing at a higher rate of 7.2%. This is a weaker position than the previous update's forecast. The growth in revenue includes (i) tariff increases (ii) increased sales and (iii) additional revenue sources. Higher growth in expenditure than growth in income is not sustainable over the longer term.

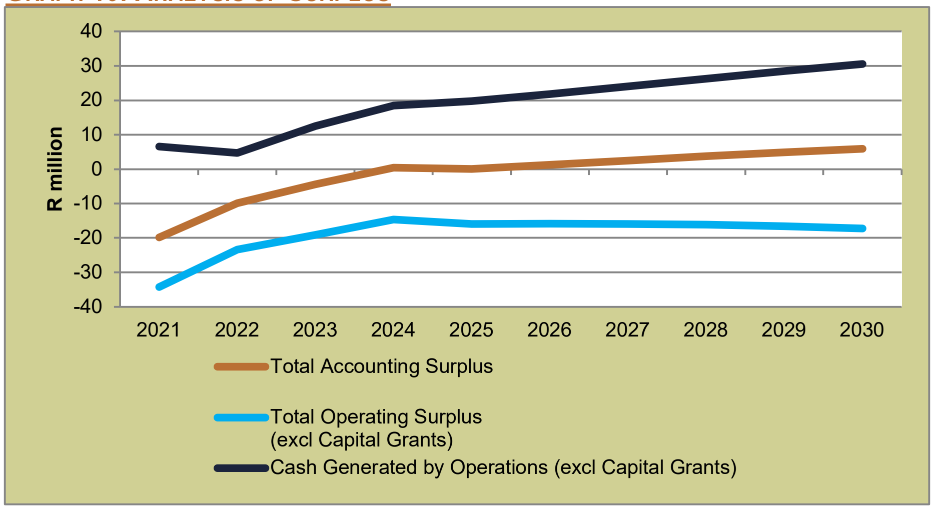
The initial decline in real ***GVA per capita*** is due to a sluggish economic growth rate which is expected to remain lower than the population growth rate over the short term. However, both real ***GVA per capita*** and the ***real revenue per capita*** are expected to improve in the long term. Local GVA growth is critical to expand the municipality's revenue base in order to extract revenue for the municipality and to address the profitability challenges forecast.

Notwithstanding the cash generated from operations, the municipality continues to generate operating deficits over the entire forecast period. This is not financially sustainable over the longer term and should be addressed.

GRAPH 39: PROJECTED REAL GVA AND REVENUES PER CAPITA



GRAPH 40: ANALYSIS OF SURPLUS



CAPEX AFFORDABILITY AND FUNDING

The total capex demand was determined during the preparation of the LTFP in 2014 but is expected to have changed since then. For the purposes of this report, the adjusted estimated capex demand in the previous update was adjusted for inflation.

Total 10-year Capex **Affordability:**	=	R 503 million

The change in the profitability of Cape Agulhas forecasts had a significant negative impact on the capex affordability. In the previous update it was estimated that Cape Agulhas Municipality can afford approximately R 617 million in capital investment over the next 10 years. This has now decreased to R 503 million.

MTREF CAPITAL FUNDING MIX

The MTREF budget 2020/21 to 2022/23, as approved in the original MTREF budget, expects a capital budget amounting to R 134 billion funded as follows:

TABLE 6: 3-YEAR MTREF FUNDING MIX R'M

R'm	*Total*	*2019/20*	*2020/21*	*2021/22*
Loans	**46**	36	6	4
Cash	**46**	12	16	18
Grants	**42**	14	13	15
Contributions	**0**	0	0	0
Total	**134**	62	36	36

Following the adjustments made to reach an optimal forecast scenario, IPM recommends the MTREF capital budget to be adjusted as follows:

TABLE 7: 3-YEAR PROPOSED MTREF FUNDING MIX R'M

R'm	*Total*	*2019/20*	*2020/21*	*2021/22*
Loans	**90**	**48**	**22**	**20**
Cash	**2**	**0**	**1**	**1**
Grants	**42**	14	13	15
Contributions	**0**	0	0	0
Total	**134**	**62**	**36**	**36**

The changes in red reflect changes recommended to improve the funding mix. This funding mix, as proposed, will safeguard liquidity and prevent the depletion of cash resources.

10 YEAR CAPITAL FUNDING MIX

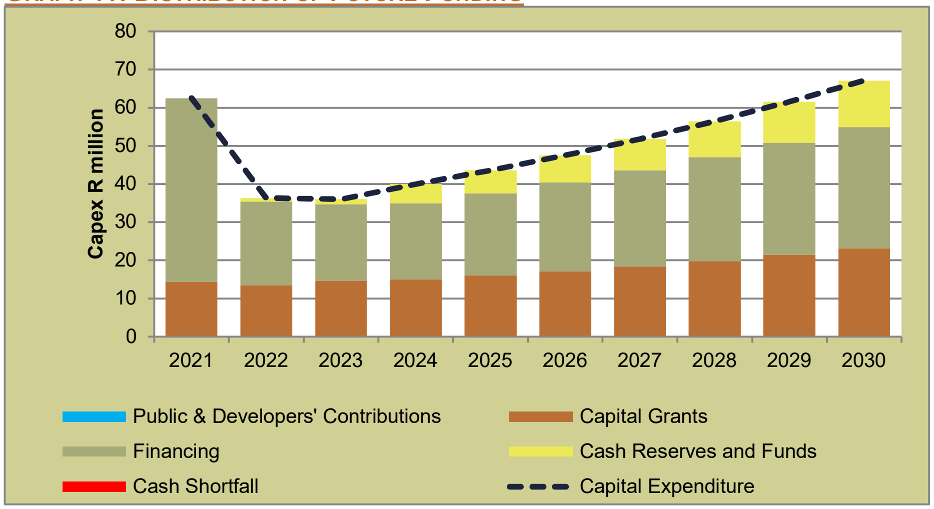
The 10-year capital funding mix is presented in the table below:

TABLE 8: CAPITAL FUNDING MIX

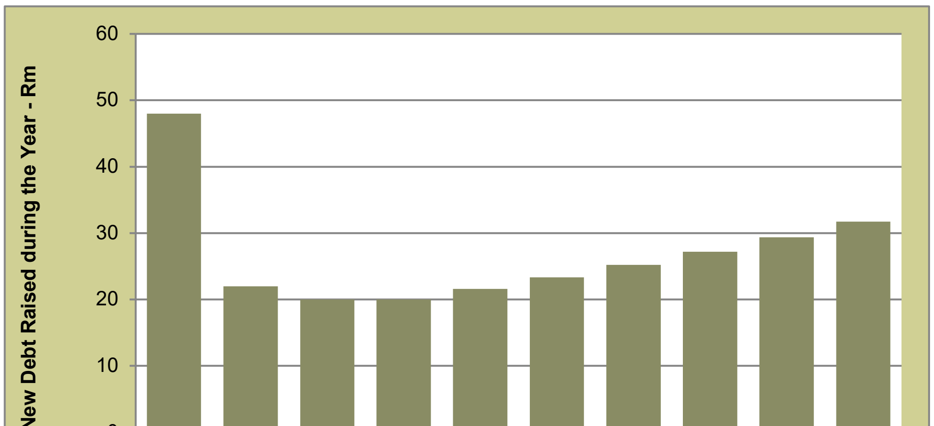
Source	Rm	%
Public & Developers' Contributions	0	0%
Capital Grants	173	34%
Financing	268	53%
Cash Reserves and Funds	62	13%
Capital Expenditure	**503**	**100%**

The distribution of the funding mix and annual borrowing of this base case, based on the current MTREF, are illustrated below:

GRAPH 41: DISTRIBUTION OF FUTURE FUNDING



GRAPH 42: ESTIMATE OF FUTURE EXTERNAL FINANCING



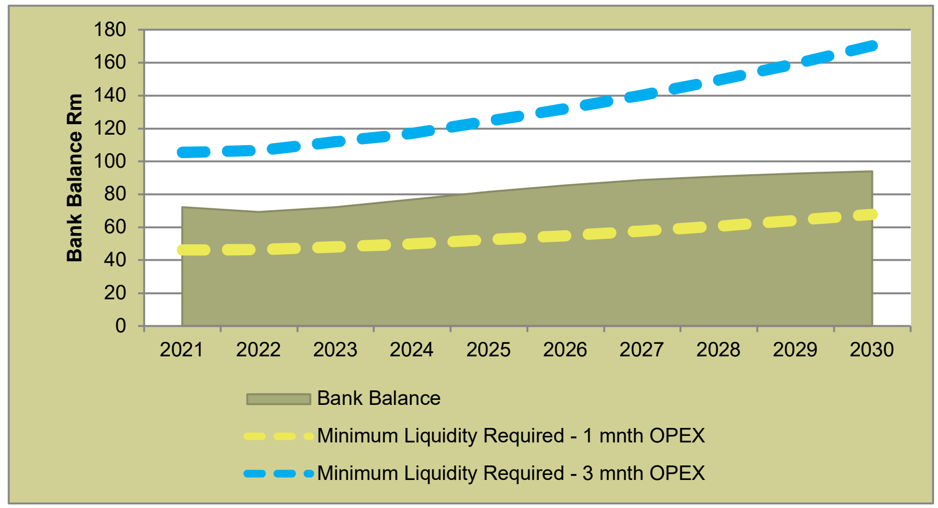
	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
R million	48	22	20	20	22	23	25	27	29	32

LIQUIDITY

For purposes of this report the minimum required liquidity level caters for unspent conditional grants, reserves, short term provisions, and 1 month working capital.

A healthy liquidity position is achievable in this scenario and the municipality's bank balance is sufficient to cover minimum liquidity requirements and up to 1.3 months operating expenditure. The Liquidity Ratio remains above the minimum norm of 1:1, starting at a level of 1.5:1 in FY2021, but then declining to 1.1:1 at the end of the 10-year planning period.

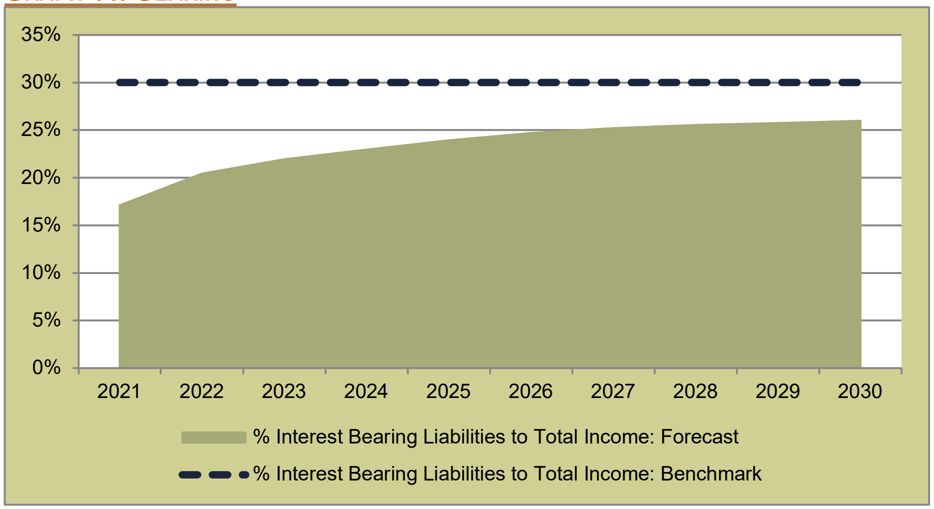
GRAPH 43: BANK BALANCE VS PROPOSED CASH BACKED RESERVES



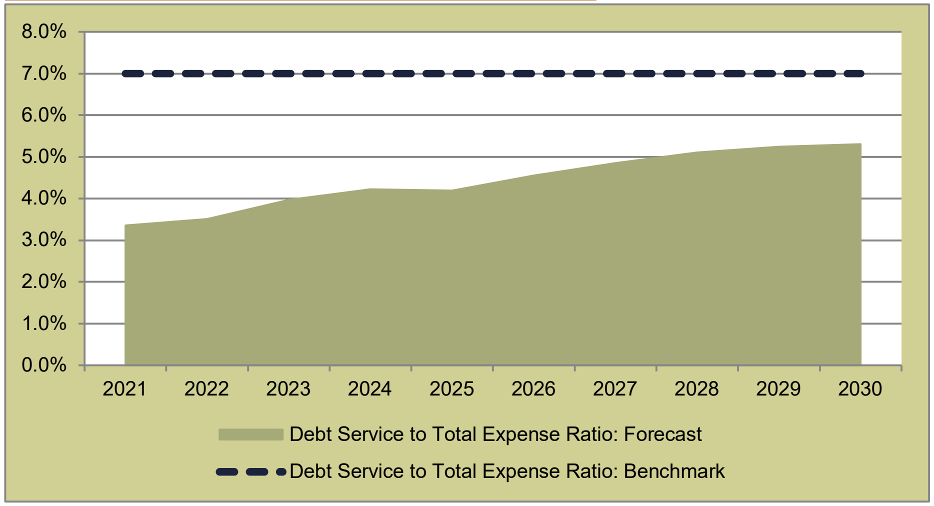
GEARING

The ***gearing ratio*** (long-term interest-bearing liabilities to revenue) and the ***debt service to total expense ratio*** are illustrated in the graphs below. A gearing level of 30% is regarded optimal for Cape Agulhas (although National Treasury provides a benchmark of 45%), while it is recommended that the debt service tot total expense ratio should not exceed 7%. The external financing proposed to be taken up over the MTREF period is considered affordable, with the gearing ratio and debt service ratio forecast to remain within the recommended maximum norms.

GRAPH 44: GEARING



GRAPH 45: DEBT SERVICE TO TOTAL EXPENSE RATIO



1	Planning Process
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Scenario Analysis

Considering our analysis of the proposed MTREF budget and the increased liquidity risk identified as part of this update, the following scenarios were run to indicate the potential outcomes to assist the municipality in its strategic decision-making and to serve as an input to the adjustment budget for FY2021 and potentially the original budget for FY2022:

To indicate the collection rate sensitivity on long-term financial sustainability:

i) A collection rate positive and negative scenario, indicating the impact of an improved collection rate of 1% p.a. higher than the collection rate. assumed in the optimal case or a 2% lower collection rate p.a. than the collection rate assumed in the optimal case, on liquidity levels and cash balances. [Scenario 1: Collection rate sensitivity]

The impact of Covid-19 on Cape Agulhas' long-term financial sustainability:

ii) A best case and worst-case scenario, indicating the potential range of impacts of Covid-19 on the financial health and longer sustainability of Cape Agulhas by reflecting on the growth of key subsectors, formal employment, GVA, and household income. [Scenario 2: Covid-19 worst case and best case]

Scenario 1: Sensitivity Analysis on Collection rate

Building on the optimal case, the graphical representation of the impact of collection rate's increase or decrease on other financial metrics of the municipality by as little as +1% or -2% can be seen on the next page.

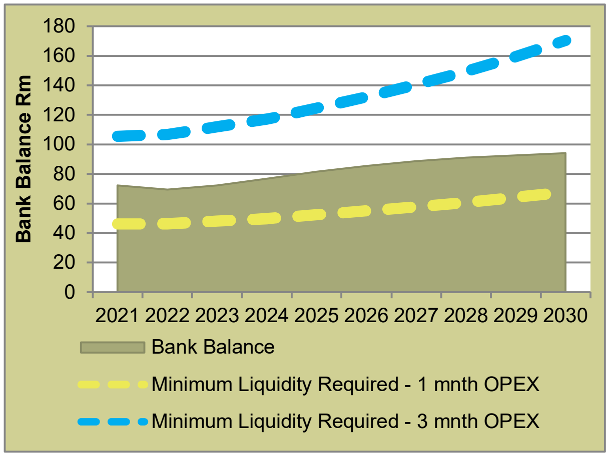
The optimal case is modelled on a collection rate of 90% in 2021 which is lower than the 94% rate achieved in 2020 considering the impact of covid-19 on households' ability to pay for services. Our model has gradually increased collection to 95% from 2024 until the end of the planning period. Should the municipality achieve a collection rate 1% higher than the reference case annually, a marked improvement in liquidity is noted and Cape Agulhas is able to achieve and maintain 2 months working capital requirements from 2026 onwards as compared to a ratio of 1.3 months on optimal case.

Should the projected collection rate for 2021 fall below 89% while other financial variables remain unchanged, the model returns a drastic deterioration in liquidity levels. The liquidity ratio deteriorates to 0.3:1 in 2030 and operational deficits are posted throughout the planning period.

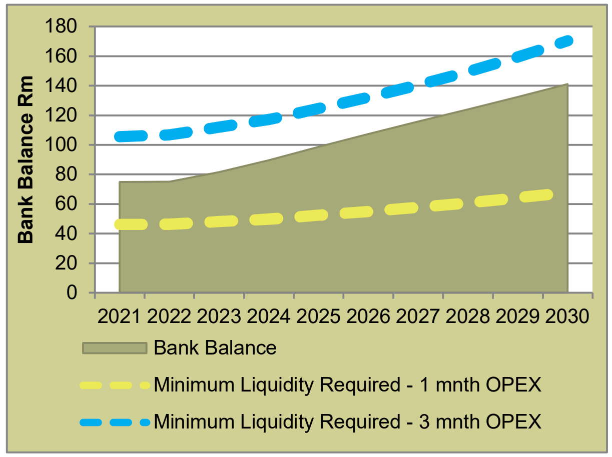
This highlights not only the importance of improving the collection rate, but also increasing operating profits. It is therefore imperative to optimise operational cost and limit annual increases in the main operating expenditure items to improve profitability.

Scenario 1: Sensitivity Analysis on Collection Rate

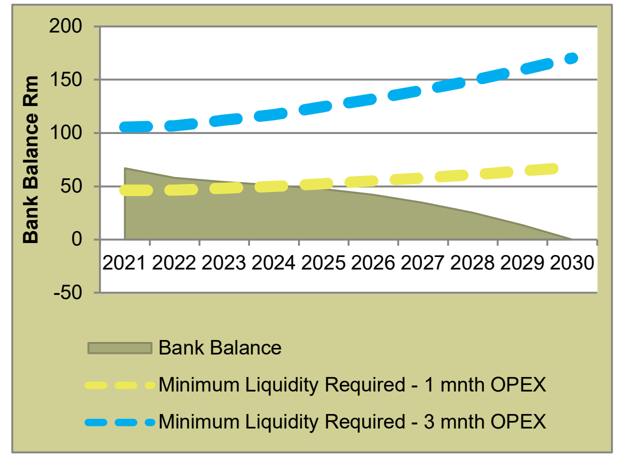
Optimal case

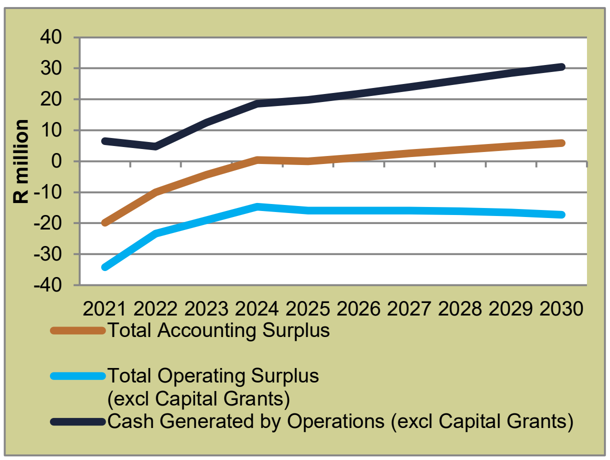


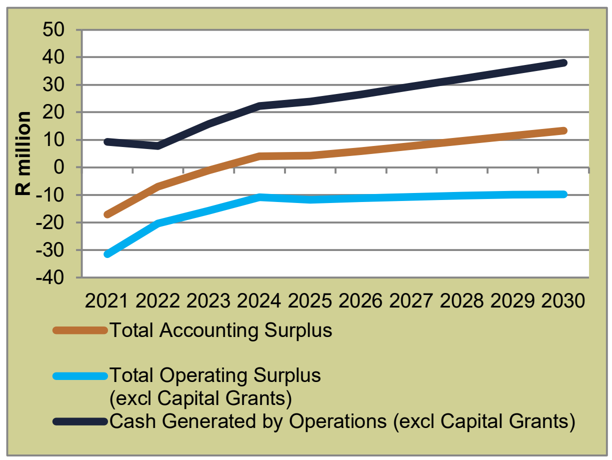
Collection rate +1%

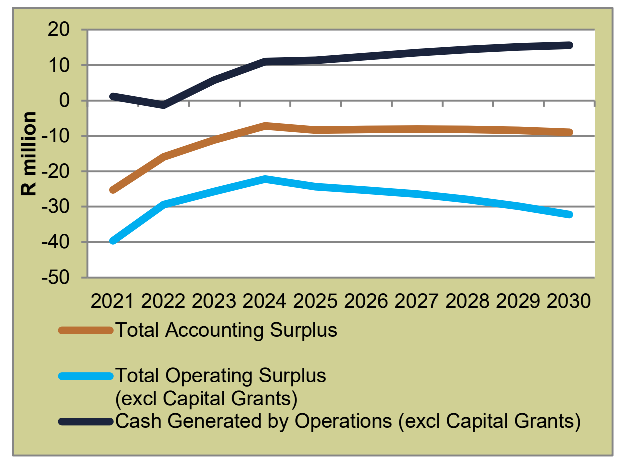


Collection rate -2%



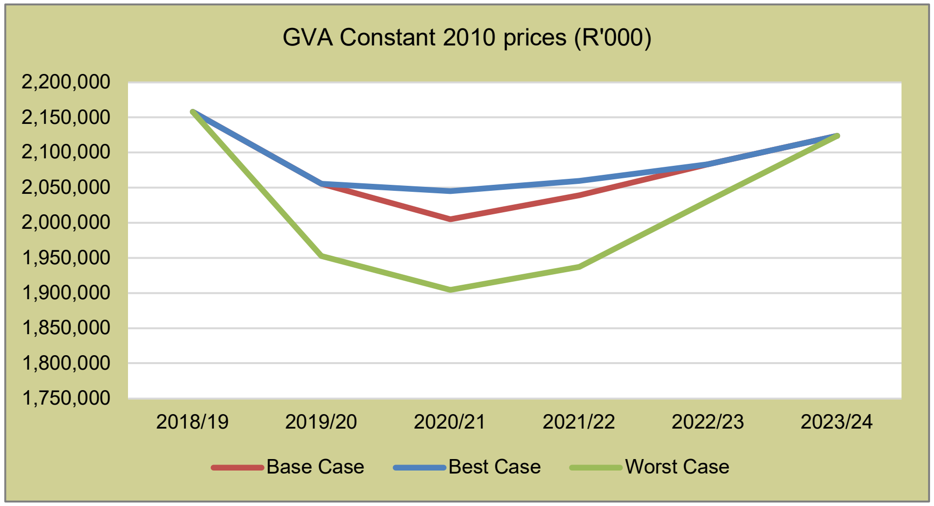






Scenario 2 covid-19 Impact: Best case Vs Worst Case

Graph 46: GVA growth covid-19 impact



It is expected that the finances of municipalities will be severely impacted by Covid-19, with strong pressure on expenditure and reduced revenues, thus increasing operational deficits and the need for increased dependence on fiscal transfers. The negative results will be more visible in the medium term, which solidifies the need for longer term planning to identify risks that may threaten the financial viability of Cape Agulhas.

While the MTREF budget already includes Cape Agulhas' response in mitigation of the associated risks, it is valuable to model different scenarios outlining the worst- and best-case outcomes of Covid-19 on the municipality's financial health in the long term.

The impact of Covid-19 on the financial situation of the municipality was measured against the optimal case scenario and the outcomes are reflected on Table 9 and the graphs below.

Table 9: Outcome of Covid-19 impact scenarios

Outcome	Optimal Case	Covid-19 best	Covid 19 worst
Average annual % increase in Revenue	6,5%	6,5%	6,4%
Average annual % increase in Expenditure	7,2%	7,2%	7,2%
Accounting Surplus accumulated during Planning Period (Rm)	-R 15	R 0	-R 57
Operating Surplus accumulated during Planning Period (Rm)	-R 189	-R 173	-R 230
Cash generated by Operations during Planning Period (Rm)	R 193	R 208	R 151
Average annual increase in Gross Consumer Debtors	9,5%	9,3%	9,9%
Capital investment programme during Planning Period (Rm)	R 503	R 503	R 503
External Loan Financing during Planning Period (Rm)	R 268	R 268	R 268
Cash and Cash Equivalents at the end of the Planning Period (Rm)	R 94	R 109	R 52
No of Months Cash Cover at the end of the Planning Period (Rm)	1,8	2,1	1,0
Liquidity Ratio at the end of the Planning Period	1,1 : 1	1,2 : 1	0,8 : 1
Gearing at the end of the Planning Period	26,9%	26,9%	27,0%
Debt Service to Total Expense Ratio at the end of the Planning Period	5,3%	5,3%	5,3%

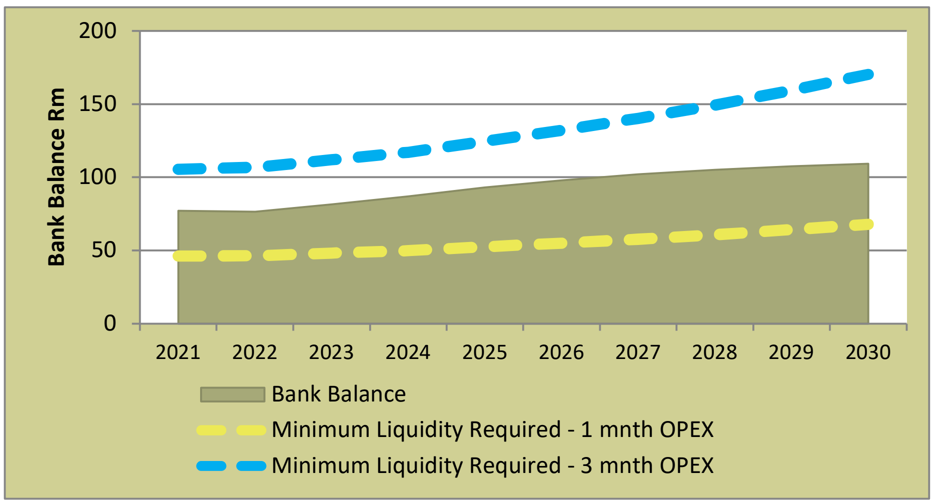
The “***Best Case***” scenario assumes that the Covid-19 impact will result in a GVA contraction of -4.75% and -0.5% in 2020 and 2021 followed by a slow recovery of 0.75% in 2022.

In the “***Worst Case***” scenario the Covid-19 impact is more severe in 2020 as represented by a local GVA contraction of -9.52% and -2.23%, to be followed by a robust growth of 1.55% in 2022.

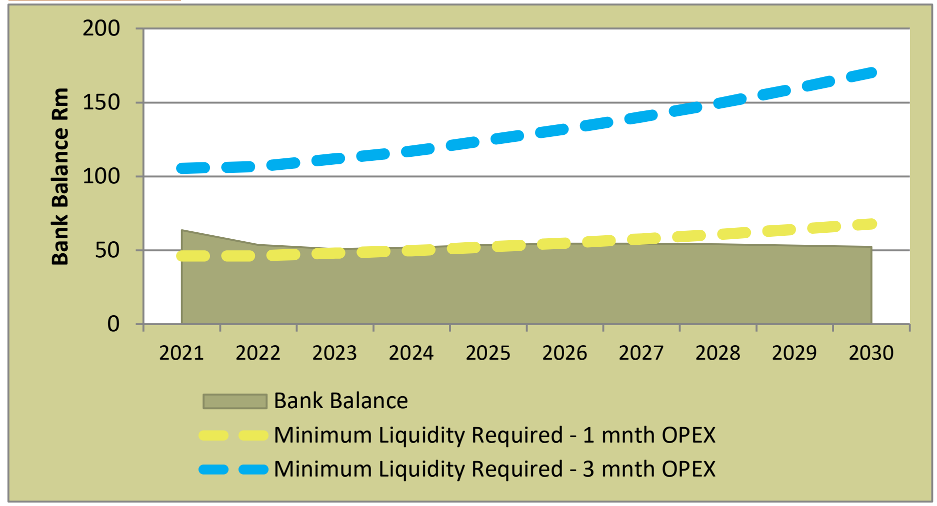
The impact is also illustrated by the graphs below. In the best case the bank balance comes to R109 million in 10-years’ time, which is sufficient to cover the statutory reserves and more than one month’s working capital.

In the worst case scenario, the cash balance deteriorates to an overdraft position of R52 million at the end of the forecast period and is not sufficient to cover statutory reserves and one month’s working capital as represented by a liquidity ratio of 0.8:1 at the end of the planning period.

GRAPH 47: COVID-19 BEST CASE – BANK BALANCE VS MINIMUM LIQUIDITY REQUIREMENTS



GRAPH 48: COVID-19 WORST CASE – BANK BALANCE VS MINIMUM LIQUIDITY REQUIREMENTS



1	Planning Process
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Ratio Analysis

The optimal scenario forecast ratios are presented below. Although the model is not programmed to measure the ratios as required by National Treasury in all instances, it does provide comfort that the municipality is sustainable in future - on condition that it operates within the assumed benchmarks set in the financial plan.

Table 10: Outcome of Future Ratio Analysis

		N.T. NORM	2021	2023	2025	2027	2029	2030	COMMENTS
FINANCIAL POSITION									
ASSET MANAGEMENT									
R29	**Capital Expenditure / Total Expenditure**	10% - 20%	13,1%	7,7%	8,2%	8,5%	8,8%	8,9%	Capex as a % of Total Expenditure continues to decrease over the forecast period to lower levels than the recommended norm. Any improvements in profitability and cash generation ability, which can support increased capital investment should be pursued.
DEBTORS MANAGEMENT									
R4	**Gross Consumer Debtors Growth**		32,0%	6,2%	6,4%	6,7%	7,0%	7,1%	The assumed collection rate of 90% is forecast to increase to 95% and requires the municipality to closely monitor it rate in future.
R5	**Payment Ratio / Collection Rate**	95%	90,0%	95,0%	95,0%	95,0%	95,0%	95,0%	
LIQUIDITY MANAGEMENT									
R49	**Cash Coverage Ratio (excl Working Capital)**		4,4 : 1	4,5 : 1	5 : 1	5,4 : 1	5,6 : 1	5,6 : 1	The liquidity position is healthy, provided the municipality implements the recommendations to mitigate future risks
R50	**Cash Coverage Ratio (incl Working Capital)**		1,6 : 1	1,5 : 1	1,5 : 1	1,5 : 1	1,4 : 1	1,4 : 1	
R51	**Cash Surplus / Shortfall on Minimum Liquidity Requirements**		R 25,7 m	R 23,7 m	R 28,6 m	R 30,3 m	R 27,9 m	R 25,4 m	
R1	**Liquidity Ratio (Current Assets : Current Liabilities)**	1.5 : 1 – 2.0 : 1	1,5 : 1	1,4 : 1	1,4 : 1	1,3 : 1	1,2 : 1	1,1 : 1	
LIABILITY MANAGEMENT									
R45	**Debt Service as % of Total Operating Expenditure**	6% - 8%	3,4%	4,0%	4,2%	4,9%	5,2%	5,3%	Borrowings do not exceed the N.T. Gearing norm of 45% and the Cape Agulhas recommended norm of 30%.The Debt Service Cover Ratio remains within acceptable levels.
R6	**Total Debt (Borrowings) / Operating Revenue**	45%	17,8%	22,7%	24,7%	26,1%	26,7%	26,9%	
R7	**Repayment Capacity Ratio**		4,62	5,11	4,74	4,98	5,12	5,24	
R46	**Debt Service Cover Ratio (Cash Generated by Operations / Debt Service)**		1,5 : 1	1,6 : 1	1,7 : 1	1,6 : 1	1,5 : 1	1,5 : 1	
SUSTAINABILITY									
	Net Financial Liabilities Ratio	< 60%	31,9%	41,4%	45,6%	49,5%	52,8%	54,3%	The negative Operating Surplus Ratios and low profitability needs to be addressed. Asset
	Operating Surplus Ratio	0% - 10%	-9,0%	-4,6%	-3,4%	-2,9%	-2,6%	-2,6%	

		N.T. NORM	2021	2023	2025	2027	2029	2030	COMMENTS
	Asset Sustainability Ratio	> 90%	243,2%	40,2%	43,7%	47,3%	50,6%	52,1%	Sustainability is not calculated but entered as an assumption in the model. a greater proportion of capex is spent on asset replacement in 2021.
FINANCIAL PERFORMANCE									
EFFICIENCY									
R42	Net Operating Surplus / Total Operating Revenue	>= 0%	-9,0%	-4,6%	-3,4%	-2,9%	-2,6%	-2,6%	The Net Operating Surpluses generated are necessary to cross subsidise services. The municipality must ensure that tariffs are set at levels that would maintain the surpluses in future.
R43	Electricity Surplus / Total Electricity Revenue	0% - 15%	27,0%	26,7%	26,0%	25,3%	24,6%	24,3%	
REVENUE MANAGEMENT									
R8	Increase in Billed Income p.a. (R'm)		R 10,4 m	R 19,5 m	R 23,6 m	R 28,3 m	R 34,1 m	R 37,4 m	Operating Revenue growth is above the assumed inflation rate (after the MTREF period) due to tariff increases that exceed the inflation rate along with growth in quantities sold. The national fiscal constraints will necessitate that the municipality strengthens its ability to generate cash from own revenue.
R9	% Increase in Billed Income p.a.	CPI	4,0%	6,7%	7,1%	7,4%	7,7%	7,9%	
R12	Operating Revenue Growth %	CPI	7,2%	6,1%	7,2%	7,2%	7,5%	7,6%	
R47	Cash Generated by Operations / Own Revenue		6,9%	7,8%	9,0%	9,3%	9,4%	9,4%	
R48	Cash Generated by Operations / Total Operating Revenue		5,5%	6,6%	7,6%	7,8%	8,0%	8,0%	
EXPENDITURE MANAGEMENT									
R30	Contribution per Expenditure Item: Staff Cost (Salaries, Wages and Allowances)	25% - 40%	32,7%	36,6%	36,1%	35,6%	35,1%	34,9%	Employee related costs are at the higher end of the proposed norm.
	Contribution per Expenditure Item: Contracted Services	2% - 5%	3,1%	3,3%	3,2%	3,1%	3,1%	3,1%	
GRANT DEPENDENCY									
R10	Total Grants / Total Revenue		22,8%	19,1%	18,4%	18,2%	17,9%	17,8%	The tightening of the national fiscus will enforce a declining dependence on transfers from other spheres of government, specifically as far as it relates to capital grants.
R11	Own Source Revenue to Total Operating Revenue		80,2%	83,8%	84,3%	84,6%	84,9%	85,0%	
	Capital Grants to Total Capital Expenditure		23,0%	40,7%	36,7%	35,5%	34,8%	34,6%	

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OUTCOME OF INDEPENDENT FINANCIAL ASSESSMENT

Cape Agulhas LM managed to realise an accounting surplus of R 28.7 million during FY2020 compared to a surplus of R 40.7 million in FYE2019. Should capital grants be excluded from total income, the operating income for the year reflects a total of R 338.3 million, against operating expenses of R 343.3 million. The result of this was an operating deficit of R 4.99 million for FY2020; a deterioration from a surplus of R 7.98 million at FYE2019.

The declining financial performance by the municipality, in conjunction with a weaker collection rate of 94%, barely enabled the municipality to generate R 11.0 million in cash from its operations (excl. capital grants). This was R 23.7 million (67.2%) less than the cash generated from operations in the previous year.

Actual capital expenditure (R 40.5 million) fell short of budgeted capital expenditure (R 43.3 million), and the funding mix was mostly reliant on the cash generated from operations. The majority of capital expenditure was financed through own cash and reserves, as well as capital grants

The municipality maintained a healthy lower level of gearing of 8% even after above mentioned was taken into account. The debt service cover ratio weakened from 6.28 in FYE2019 to 1.22 in FYE2020, this was due to less grant money received as well as a lower collection rate.

Gross consumer debtors grew by 14% (R 8 million) to R 64.7 million in FYE2020. The provision for doubtful debts of R 31.99 million (an increase of R 3.14 million or 10.8%) is insufficient to cover all consumer debtors older than 90 days (R 32.17 million) by R 180 000. Debtors older than 90 days constituted 49.71% of gross consumer debtors in FYE2020 and current debtors 35.0%. Consumer bad debts written off amounted to R 6.95 million in FYE2020 (R 5.68 – FYE2019).

The increase in current liabilities of R 4.19 million in FYE 2020, which totalled R 62.77 million is largely attributed to an increase of R 3.86 million in short term provisions relating to staff and employee benefit provisions.

The movements in current assets and current liabilities weakened the liquidity ratio of Cape Agulhas LM from 2.03 in FYE2019 to 1.73 in FYE2020.

The liquidity position in which the municipality finds itself, is underlined by the cash coverage ratio of 1.36 as at FYE2020, with a R 7.4 million deficit in cash below the minimum liquidity requirements.

STRENGTHS

- Cape Agulhas has a liquidity ratio of 1.73 (above the norm of 1.5)
- A gearing ratio of 8% indicates affordable level of borrowings along with debt servicing as a percentage of operating expenditure of 3%
- A positive cash coverage ratio including 1 month’s working capital of 1.36
- Although operational expenditure continues to grow Cape Agulhas maintained its relative low reliance on grants.

WEAKNESSES

- Weakening collection ratio of 94%, below the National Treasurry norm of 95%
- Decrease in cash and cash equivalents.
- Staff costs that are more than 40% of total operating expenditure
- Insufficient coverage for debtors older than 90+ days.
- Calculated minimum liquidity shortfall of R 7.4 million (i.e. Cape Agulhas can cover its minimum liquidity requirements nl: Unspent conditional grants, short term provisions, funds, reserves and trust funds (cash backed) however it is the working capital provision of minimum one month’s operating expenditure that causes the shortfall.

LONG TERM FINANCIAL MODEL OUTCOMES

The negative impact of covid-19 on the financial performance of Cape Agulhas results in the continuation of declining profitability, lower levels of cash generated by operations and a deterioration of the cash balances as noted in the FY2020 results. The MTREF projects that the collection rate of 94% achieved in 2020 will decrease to 90% in FY2021 and increase to 93.5% in FY2022. The average tariff increase of 7% in property rates, water, sanitation and waste removal services which is in excess of CPI rate is budgeted to recover the costs of services provided.

The MTREF scenario forecasts a significant increase in the level of capital investment programme in 2021(R62 million), followed by a reduction to a level of R36 million in 2022 and 2023. The funding mix for 2022 and 2023 appears imbalanced and too reliant on internal cash resources. This method is not substantiable in an environment where operating deficits are posted and poses a significant liquidity threat.

In an attempt to preserve liquidity, the model projects that Cape Agulhas will only afford a 10-year capital expenditure of R466 million which is lower that the projection of R617 million from our previous update.

To address these concerns, we modelled an optimal case scenario.

The strategies include:

Adjust capital funding mix

An increase in borrowings of R46 million over the MTREF period while maintaining the same level of capex results in stronger liquidity results. The gearing and debt service cover ratios also remain below the maximum benchmarks.

Increasing the average loan tenor.
An additional measure of applying an average loan tenor of 13 years to all future borrowing instead of 10 years, results in lower costs of servicing future debt and thus further improving liquidity.

Optimal case

A further proposal is to reduce the operational budget by R4 million per year between 2021 and 2024 (which translates to approximately 1% of the opex budget). Cape Agulhas is able to accelerate the 10-year capital programme of R 503 million versus the affordable amount of R466 million on MTREF scenario. There is also scope to obtain external borrowings of R268 million over the next 10 years while maintaining gearing ratios below the maximum benchmark set for Cape Agulhas in the LTFP of 30%.

Collection rate up 1% during MTREF period
Increasing collection by 1% each year results in a marked improvement in liquidity. The surplus liquidity after meeting the minimum requirements can be used to accelerate the municipality's capital investment program within reasonable measures.

Collection rate down 2%.
Payment of rates and service charges by households and businesses will be negatively affected by Covid-19. Should collection rate drop to 90% in 2021, cash generated from operations decline and the municipality holds insufficient funds to cover 1 month's operational expenditure.

In addition to the actions proposed above, the scenarios indicate further the importance of maintaining the collection rate at levels above 95% and the positive impact that a reduction in the expenditure budget of R 4 million per annum can have on the financial performance of Cape Agulhas.

Under the optimal scenario, Cape Agulhas will be able to invest R 503 million in capital over the next 10 years, while maintaining its minimum liquidity levels, borrowing at affordable levels and remaining financially sustainable.

During these uncertain times, it remains vital for Cape Agulhas to prioritise longer term planning so that the municipality can respond, recover, and optimise resources to ensure demands for services are met. The expected sustainable outlook is subject to the condition that the municipality continues to manage its finances with care and discipline.

ANNEXURE 1: PROJECTED FINANCIAL STATEMENTS

Municipal Financial Model - Cape Agulhas
Statement of Financial Performance

Model year	1	2	3	4	5	6	7	8	9	10
Financial year (30 June)	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**
R thousands										
Revenue										
Property rates	74 351	79 072	84 281	90 659	97 976	106 074	115 027	124 909	135 792	147 741
Service Charges	197 695	211 479	225 718	240 975	257 135	274 708	293 925	314 983	338 081	363 408
Rental of facilities and equipment	1 200	1 284	1 374	1 460	1 553	1 655	1 766	1 888	2 021	2 166
Interest earned - external investments	2 410	2 890	3 053	3 617	3 939	4 305	4 653	4 977	5 260	5 504
Interest earned - outstanding debtors	1 839	1 968	2 105	2 237	4 172	4 544	4 964	5 432	5 949	6 514
Dividends received	–	–	–	–	–	–	–	–	–	–
Fines, penalties and forfeits	12 419	13 288	14 218	15 107	16 072	17 124	18 273	19 531	20 908	22 415
Licences and permits	25	27	29	31	33	36	39	42	46	50
Agency services	3 121	3 340	3 573	3 797	4 040	4 304	4 593	4 909	5 255	5 634
Transfers and subsidies (operating)	75 102	65 201	67 102	70 000	74 093	78 540	83 389	88 683	94 465	100 773
Other revenue	10 633	11 235	11 998	12 654	13 463	14 344	15 306	16 360	17 513	18 776
Gain on disposal of PPE	–	–	–	–	–	–	–	–	–	–
Revaluation on investment property gain / (loss)	–	–	–	–	–	–	–	–	–	–
Total revenue before Capital Grants	378 796	389 784	413 451	440 537	472 475	505 634	541 934	581 714	625 289	672 981
Capital Grants	14 389	13 421	14 665	15 000	16 010	17 140	18 406	19 824	21 411	23 187
Public & developers contributions	–	–	–	–	–	–	–	–	–	–
Total Revenue after Capital Grants	393 185	403 206	428 116	455 537	488 486	522 774	560 340	601 538	646 700	696 168
Operating expenditure										
Employee related costs	149 348	156 055	164 985	172 433	184 947	196 317	208 833	222 614	237 782	254 455
Remuneration of councillors	6 034	6 324	6 632	6 927	7 282	7 667	8 084	8 538	9 032	9 568
Debt impairment	36 048	28 346	25 622	27 336	29 197	31 229	33 456	35 898	38 578	41 514
Depreciation and asset impairment	16 051	17 808	18 501	19 150	19 951	20 864	21 894	23 051	24 342	25 776
Finance charges	6 381	7 572	8 736	9 885	11 135	12 586	14 091	15 671	17 341	19 166
Bulk purchases	99 393	106 855	114 074	122 362	131 394	141 277	152 128	164 068	177 221	191 709
Other Materials	56 336	46 958	48 514	50 000	54 499	58 405	62 755	67 598	72 989	78 984
Contracted services	14 955	14 950	15 549	15 745	16 803	17 898	19 095	20 406	21 842	23 412
Transfers and subsidies	4 071	2 605	2 641	2 700	2 873	3 060	3 266	3 491	3 737	4 006
Other expenditure	24 392	25 676	27 249	28 630	30 336	32 196	34 238	36 482	38 946	41 651
Loss on disposal of PPE	–	–	–	–	–	–	–	–	–	–
Total Expenditure	413 009	413 149	432 503	455 168	488 416	521 499	557 841	597 818	641 808	690 242
Suplus/ (Shortfall) for the year	**(19 824)**	**(9 944)**	**(4 387)**	**369**	**69**	**1 275**	**2 500**	**3 720**	**4 892**	**5 926**

Municipal Financial Model - Cape Agulhas
Statement of Financial Position

Model year	0	1	2	3	4	5	6	7	8	9	10
Financial year (30 June)	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**
R thousands											
Non-current assets:	475 472	521 911	540 440	557 930	578 781	602 429	629 089	658 996	692 409	729 612	770 920
Property, plant and equipment	430 862	477 309	495 845	513 343	534 201	557 857	584 525	614 440	647 860	685 071	726 386
Intangible assets	4 120	4 113	4 105	4 097	4 090	4 082	4 074	4 067	4 059	4 051	4 044
Investment properties	40 329	40 329	40 329	40 329	40 329	40 329	40 329	40 329	40 329	40 329	40 329
Investments	–	–	–	–	–	–	–	–	–	–	–
Long-term receivables	161	161	161	161	161	161	161	161	161	161	161
Other non-current assets	–	–	–	–	–	–	–	–	–	–	–
Current assets:	118 578	111 234	107 706	110 908	115 604	120 853	125 238	128 945	131 855	134 269	136 245
Inventories	1 936	6 635	5 970	6 227	6 463	6 973	7 447	7 972	8 554	9 200	9 915
Trade and other receivables	43 600	32 344	32 344	32 344	32 344	32 344	32 344	32 344	32 344	32 344	32 344
Cash & Short term investments	73 041	72 255	69 391	72 337	76 797	81 536	85 447	88 629	90 956	92 725	93 986
TOTAL ASSETS	**594 050**	**633 146**	**648 146**	**668 839**	**694 385**	**723 282**	**754 328**	**787 942**	**824 264**	**863 881**	**907 165**
Municipal Funds:	420 773	400 949	391 005	386 618	386 987	387 056	388 331	390 831	394 551	399 443	405 368
Housing development fund & Other Cash Backed Reserves	–	–	–	–	–	–	–	–	–	–	–
Reserves (Not Cash Backed)	35 000	35 000	35 000	35 000	35 000	35 000	35 000	35 000	35 000	35 000	35 000
Accumulated surplus	385 773	365 949	356 005	351 618	351 987	352 056	353 331	355 831	359 551	364 443	370 368
Non-current liabilities:	110 505	159 031	182 365	203 738	225 974	248 900	272 614	297 198	323 228	351 146	379 358
Long-term liabilities (Interest Bearing)	20 763	60 357	73 911	84 577	95 231	105 688	116 045	126 385	137 282	149 181	160 486
Non-current provisions	89 742	98 674	108 454	119 161	130 743	143 212	156 569	170 813	185 945	201 965	218 872
Current liabilities:	62 772	73 166	74 776	78 482	81 425	87 326	93 383	99 913	106 485	113 292	122 439
Consumer deposits	5 028	5 272	5 533	5 788	6 058	6 346	6 653	6 980	7 330	7 705	8 106
Provisions	15 250	15 250	15 250	15 250	15 250	15 250	15 250	15 250	15 250	15 250	15 250
Trade and other payables	36 468	45 696	45 547	48 111	50 770	54 587	58 509	62 829	67 593	72 850	78 650
Bank overdraft	–	–	–	–	–	–	–	–	–	–	–
Current portion of interest bearing liabilities	6 027	6 948	8 446	9 334	9 346	11 143	12 971	14 854	16 313	17 488	20 433
TOTAL MUNICIPAL FUNDS AND LIABILTIES	**594 050**	**633 146**	**648 146**	**668 839**	**694 385**	**723 282**	**754 328**	**787 942**	**824 264**	**863 881**	**907 165**

Municipal Financial Model - Cape Agulhas
Cash Flow Statement

Model year	1	2	3	4	5	6	7	8	9	10
Financial year (30 June)	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**
R thousands										
Cash flows from Operating Activities										
Suplus/Deficit for the year *including* Capital Grants	(19 824)	(9 944)	(4 387)	369	69	1 275	2 500	3 720	4 892	5 926
Suplus/Deficit for the year *excluding* Capital Grants & Contributions	(34 213)	(23 365)	(19 052)	(14 631)	(15 941)	(15 865)	(15 906)	(16 104)	(16 519)	(17 261)
Capital Grants & Contributions	14 389	13 421	14 665	15 000	16 010	17 140	18 406	19 824	21 411	23 187
Adjustments for non-cash items:										
Depreciation, amortisation and impairment loss	16 051	17 808	18 501	19 150	19 951	20 864	21 894	23 051	24 342	25 776
Revaluation on investment property (gain) / loss	–	–	–	–	–	–	–	–	–	–
Increase / (Release from) current provisions & non-interest bearing liabilities	–	–	–	–	–	–	–	–	–	–
Increase / (Release from) other non-current provisions & non-interest bearing liabilities	8 932	9 780	10 708	11 582	12 469	13 357	14 244	15 132	16 020	16 907
(Increase) / Release from non-current interest bearing assets	–	–	–	–	–	–	–	–	–	–
Capitalised interest	–	–	–	–	–	–	–	–	–	–
Operating surplus before working capital changes:	5 159	17 644	24 822	31 100	32 490	35 496	38 638	41 903	45 253	48 609
Change in W/C Investment	15 785	516	2 307	2 423	3 307	3 449	3 794	4 182	4 612	5 085
(Increase)/decrease in inventories	(4 699)	665	(257)	(236)	(510)	(474)	(525)	(583)	(646)	(715)
(Increase)/decrease accounts receivable	11 256	–	(0)	(0)	0	–	–	–	(0)	(0)
Increase/(decrease) in trade payables	9 228	(149)	2 564	2 659	3 817	3 922	4 320	4 764	5 257	5 800
Net cash flow from Operating activities	20 944	18 160	27 129	33 523	35 797	38 944	42 433	46 084	49 865	53 693
Cash flows from Investing Activities										
Capital expenditure	(62 490)	(36 337)	(35 992)	(40 000)	(43 600)	(47 524)	(51 801)	(56 463)	(61 545)	(67 084)
Decrease/(Increase) in non-current receivables	–	–	–	–	–	–	–	–	–	–
(Additions) / Disposals of investment property	–	–	–	–	–	–	–	–	–	–
Net cash flow from Investing activities	(62 490)	(36 337)	(35 992)	(40 000)	(43 600)	(47 524)	(51 801)	(56 463)	(61 545)	(67 084)
Cash flows from Financing Activities										
New loans raised	48 000	22 000	20 000	20 000	21 600	23 328	25 194	27 210	29 387	31 737
Loans repaid	(7 486)	(6 948)	(8 446)	(9 334)	(9 346)	(11 143)	(12 971)	(14 854)	(16 313)	(17 488)
(Decrease) / Increase in consumer deposits	245	261	255	271	288	307	327	350	375	402
Net cash flow from Financing activities	40 759	15 313	11 809	10 937	12 542	12 492	12 550	12 706	13 449	14 651
Change in Cash	(786)	(2 864)	2 946	4 460	4 738	3 912	3 182	2 327	1 769	1 261
Cash/(Overdraft), Beginning	73 041	72 255	69 391	72 337	76 797	81 536	85 447	88 629	90 956	92 725
Cash/(Overdraft), Ending	**72 255**	**69 391**	**72 337**	**76 797**	**81 536**	**85 447**	**88 629**	**90 956**	**92 725**	**93 986**

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